

July 14, 2014

Mr. Osvaldo Gratacos
Compliance Advisor Ombudsman
International Finance Corporation
2121 Pennsylvania Avenue, N.W.
Washington DC 20433

cc. Ms. Meg Taylor
Senior Adviser

Dear Mr. Gratacos:

IFC Management's Response to the CAO Compliance Investigation Report on Banco
Financiera Comercial Hondureña S.A. (Ficohsa)

Thank you for the CAO's compliance investigation report regarding IFC's investments in Banco Financiera Comercial Hondureña S.A. (hereafter Ficohsa).

Overall, the report correctly identifies shortcomings in previous practice, particularly as regards gaps in IFC's appraisal, prior to the IFC Capitalization Fund¹ equity investment in Ficohsa in 2011 and a lack of due consideration of the potential environmental and social (E&S) risks in the bank's portfolio. Our practices and procedures at that time did not require us to cross check our FI client's key exposures against our own direct investment portfolio projects. Since then we have taken steps to close these gaps and facilitate better information sharing among staff working in different parts of the institution. The report findings will further inform our efforts in this area. We also welcome the finding confirming that IFC did not invest in Ficohsa with the intention of providing additional financing to Corporacion Dinant.

IFC has been taking a number of steps that address many of the report findings, including through the 2012 Sustainability Framework updates and the Action Plan developed as a result of CAO's audit of IFC investments in financial intermediaries (FIs). IFC is on schedule with the implementation of this Action Plan, which was approved by our Board's Committee on Development Effectiveness in September 2013. As per the Action Plan, IFC has expanded annual field supervision requirements from FI-1 clients to include FI-2 clients applying the Performance Standards. This means that IFC is increasing the number of clients we visit on a regular basis to cover more medium risk clients. IFC has also implemented a protocol for validating the implementation of an FI client's Environmental and Social Management System through a review of a sample of sub-clients.

¹ The IFC Capitalization Fund, established by the IFC asset management company in 2009, makes equity and equity related investments in, and subordinated loans to, systemically important commercial banks in emerging markets.

In addition to the Action Plan, IFC has identified other structural and process improvements to address the gaps identified in the report. For example, IFC has formalized measures to assess the risks to new FI clients, arising from their exposure to sub-clients with high E&S risks. IFC is also formalizing processes to promote greater information flow between investment, regional and E&S specialist teams working across sectors.

IFC is also currently undergoing an internal reorganization which will result in a new Risk and Sustainability Vice-Presidency as of Oct. 1, 2014. One of the key reasons for this reorganization is to leverage the expertise of staff in different parts of the institution and reduce the information silos that are referenced in the investigation report. This new organizational structure will bring together staff working on different aspects of risk into one Vice Presidency, to ensure greater information sharing and communication. Under this new structure, E&S risk will receive the same weight and attention as financial and reputational risk.

IFC's E&S risk management practice is constantly evolving and we seek to continually improve in this regard. When there are gaps in our approach, as was the case with our investments in Ficohsa, we remain committed to acting quickly, learning from our mistakes, and making the necessary course corrections for our future endeavors.

We are also seeing positive progress in our work with Ficohsa to strengthen its E&S risk management systems and practices. As part of the action plan that Ficohsa has committed to with IFC, an enhanced E&S risk management policy was approved by Ficohsa's Board of Directors in May 2014. Ficohsa has also expanded its team dedicated to E&S risk management from one part time person to three full time specialists, forming a dedicated unit for E&S risk management under its Corporate Risk department, and its E&S procedures have been updated to incorporate the Performance Standards. In addition, to ensure the effectiveness of its E&S risk management system across its operations, the new E&S team will roll out training to the entire organization by the end of the calendar year.

In 2008, IFC launched an active engagement in Honduras, one of the poorest countries in the region. The objective was to identify projects that would expand access to finance for small and medium enterprises, promote job creation, and introduce environmental and social standards in private sector operations. Our engagement with Ficohsa was part of this effort.

Small and medium enterprises make significant contributions to Honduran economy. They account for approximately 45 percent of all employment and generate up to 45 percent of GDP. Yet nearly 60 percent of those entrepreneurs report unmet credit needs and the country has an estimated US\$7.3 billion loan financing gap. Since 2008, IFC has maintained a strategic relationship with Ficohsa, specifically to support its lending to

small and medium-sized enterprises and for low to middle-income mortgages. During this time Ficohsa has disbursed more than US\$360 million through 7,000 new loans to small and medium-sized enterprises and another US\$250 million to 5,500 individuals for new housing loans.

We firmly believe that improving access to finance through financial sector development in countries such as Honduras, has a direct impact on job creation, poverty reduction, and the promotion of shared prosperity.

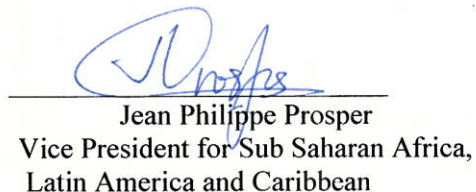
We remain committed to working with partners like Ficohsa and will continue to support them to expand their reach and impact and improve their E&S risk management. In this context, the Capitalization Fund subscribed to the Ficohsa rights issue in June 2014 alongside other international development finance partners.

Even as these steps are underway, we assure you of our commitment to strengthening our approach to E&S risk management with our FI clients and to continued dialogue with the CAO and civil society organizations.

Sincerely,



Ethiopis Tafara
Vice President and General Counsel



Jean Philippe Prosper
Vice President for Sub Saharan Africa,
Latin America and Caribbean

cc: Messrs./Mmes. James Scriven;
Morgan Landy;
Irene Arias;
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Carlos Mayorga.