

GLOBAL PROGRESS REPORT of the Sustainable Banking Network

Innovations in Policy and Industry Actions in
Emerging Markets

October 2019

Executive Summary



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Executive Summary

The Sustainable Banking Network, or SBN, is a unique, voluntary community of financial sector regulatory agencies and banking associations from emerging markets that have committed to advancing sustainable finance in line with international best practices. This community is a significant force for sustainable finance, as SBN's 38 member countries represent \$43 trillion—or 85 percent—of emerging market banking assets.

SBN members are committed to moving their financial sectors toward sustainability, with the twin goals of improved environmental, social and governance (ESG) risk management and increased capital flows to activities with positive climate impact. SBN provides a platform for knowledge sharing and capacity building that helps members design and implement national sustainable finance initiatives.

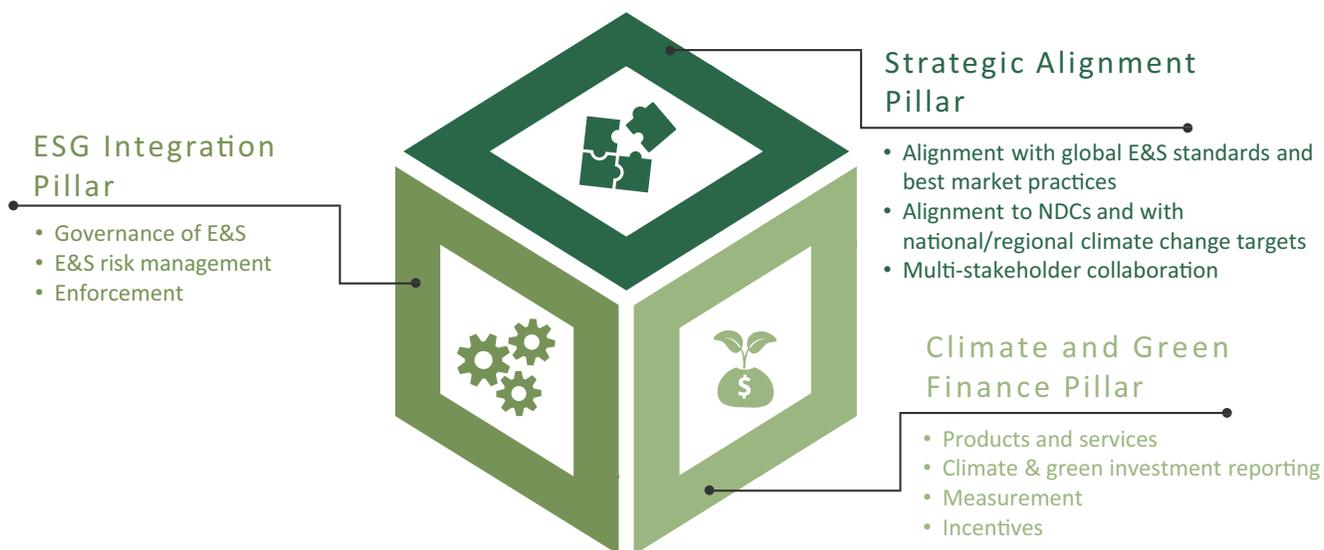
Notable SBN achievements so far include the creation of a progress measurement framework and the inaugural publication of a Global Progress Report (www.ifc.org/sbnreport) in 2018 that detailed member progress and was supported by individual country progress reports. This second Global Progress Report provides further updates on member progress from June 2017 to June 2019, and includes 42 case studies from member countries. It is supported by 30 individual country progress reports.

SBN members have identified three essential components to implementing a sustainable finance framework (Figure ES1). Each contributes in practical ways to financial stability and improved competitiveness of local financial sectors:

- i) **Strategic Alignment:** members find that national policies that are aligned with global good practices and international frameworks are more likely to be effective and to attract international investment.*
- ii) **Climate & Green Finance:** new financial products that address climate, environmental, and social objectives are becoming increasingly popular as a way to achieve national sustainability goals while unlocking financial sector innovation.*
- iii) **ESG Integration:** better management of ESG risks by banks is also leading to reduced credit risk, while contributing to financial stability.*

These three components are detailed in Chapter 1.

Figure ES1: SBN Measurement Framework



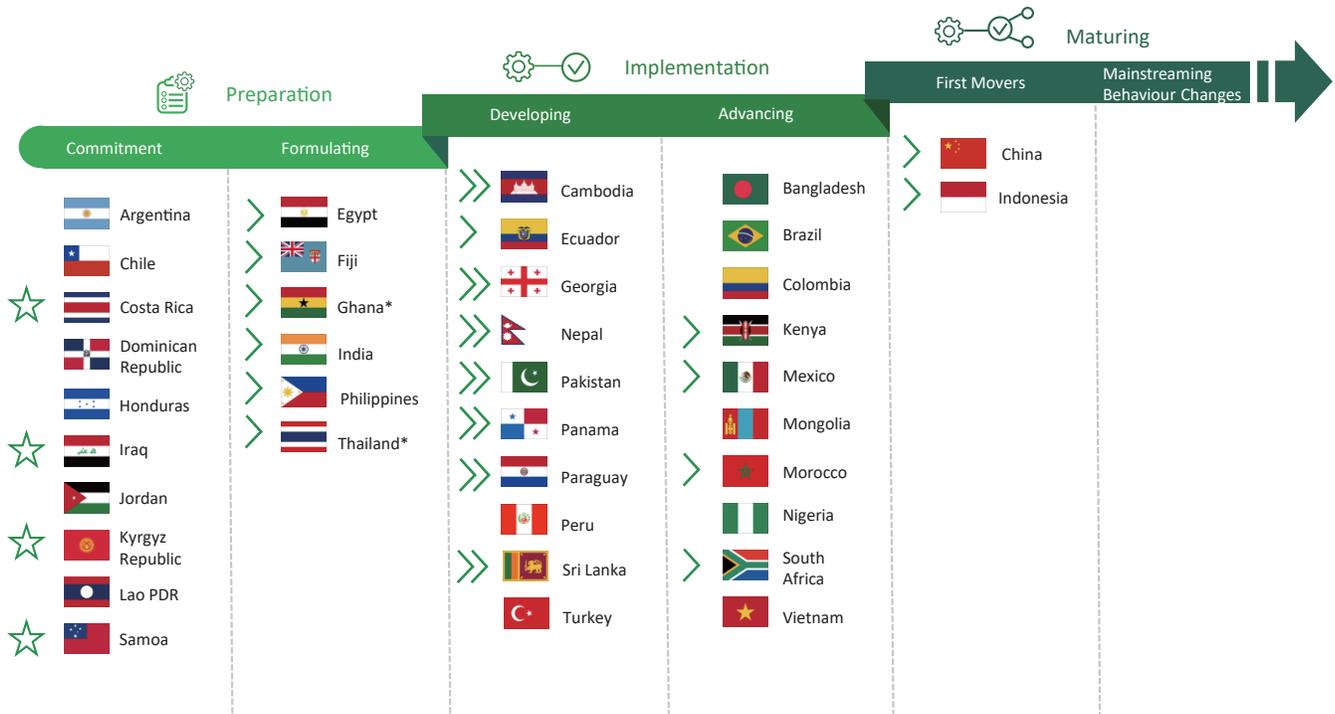
SBN was created in 2012 with 10 member countries, of which only two—Bangladesh and China—had officially launched national sustainable finance policies. **With 38 member-country today, SBN now includes 22 countries that have such policies in place.**

This report provides an assessment of these 22 countries’ national sustainable finance policies and principles, based on 19 indicators for

comprehensiveness of coverage, depth, and clarity. Results of these assessments feed into the **SBN Progression Matrix** (Figure ES2, with a detailed assessment in Chapter 1) that maps countries to the different stages of development that SBN members typically follow. The framework allows each member to review its own progress and identify the strengths and weaknesses of its approach. The framework is applied annually and is updated to reflect the collective advancement of SBN members in defining new frontiers of good practices.

Figure ES2: SBN Progression Matrix with assessment results

Assessment based on progress up to the end of June 2019



Progress since the 2018 Report

- ★ 4 new SBN member countries made progress in the Commitment Stage
- 14 countries made progress within the same stage
- > 13 countries moved up one sub-stage
- >> 7 countries moved up two sub-stages

The SBN Progression Matrix shows the overall progress of SBN’s 38 member countries toward developing and implementing sustainable financing frameworks across three development stages, each of which is made up of two sub-stages. These stages are underpinned by specific key milestones.

Note: Ghana and Thailand launched their policies and principles in August 2019, after the cut-off date of June 2019 for this report.

Overall progress based on the SBN Progression Matrix assessment results

Over the past two years, 24 out of 38 SBN member countries progressed to the next stage in the SBN Progression Matrix. Other countries also progressed within the same stage. These advancements showed tangible and widespread progress on policy and market development across the spectrum of SBN member countries.

For the first time, two countries entered the Maturing Stage.

China and Indonesia have become First Movers in this stage and have demonstrated pioneering policy actions, including the measurement of bank adoption of new practices and the impacts of green finance.

Indonesia's financial regulator (OJK) was the first to introduce a 10-year strategic roadmap for sustainable finance market development in 2014. This was followed by an umbrella policy to green the entire financial system, a set of sustainability reporting requirements, green loan definitions, and a green bond framework. With OJK's guidance and supervision, eight major Indonesian banks have been pioneering policy implementations to systematically green their investment portfolios.

China's banking regulator and central bank have issued guidelines to improve Chinese banks' ESG practices and accelerate green lending since 2012. Green loans made by Chinese banks reached \$1.37 trillion by the first quarter of 2019, up 4.3 percent from the beginning of the year and accounting for 9.9 percent of total loans.

Eight countries moved from the Preparation Stage to the Implementation Stage, shifting from vision to practice in sustainable finance policy action. Cambodia, Ecuador, Georgia, Nepal, Pakistan, Panama, Paraguay, and Sri Lanka have launched sustainable finance policies or principles since the last report and moved into the Implementation Stage. Within that stage, four countries moved from Developing to Advancing. These countries—Kenya, Mexico, Morocco, and South Africa—have launched additional guidance and implementation tools and have seen evidence of adoption of these tools by local financial institutions.

Sixteen countries have not yet launched a policy framework. However, six of these are in the process of formulating policies or principles: Egypt, Fiji, Ghana, India, Philippines, and Thailand moved from Commitment to Formulating within the Preparation Stage and initiated multi-stakeholder consultations on draft policy frameworks. Four countries joined SBN recently and made commitments to develop sustainable finance policy frameworks. These are Costa Rica, Iraq, Kyrgyz Republic, and Samoa, all of which entered the Commitment Stage.

Eleven low-income SBN countries face more acute challenges to achieve sustainable finance, but they continue to demonstrate ingenuity and determination toward that goal. A recent analysis of SBN country initiatives confirms that member countries of all income

levels, as defined by the World Bank, are advancing in sustainable finance, with lower-income countries quickly joining the ranks of those further up the income ladder. Seven low-income countries are in the Implementation Stage. The types of challenges low-income countries face are similar to those faced by other SBN members, though they are often more acute. Their experiences demonstrate that sustainable finance can be addressed alongside other development goals, including promoting financial inclusion and supporting priority sectors. However, competing priorities and a lack of resources mean there is greater need for country-level capacity building—for both the public and private sectors.

SBN members can make rapid progress, leapfrogging ahead by learning from others.

Peer-to-peer knowledge sharing is a hallmark of SBN and often results in some countries rapidly applying successful approaches of other countries to their own landscape. For example, Mongolia, Georgia, and Sri Lanka released sustainable finance roadmaps in 2018/2019. All of them benefited from examples of pioneering roadmaps developed by Indonesia, China, and Morocco, with active member exchanges and cooperation an effective part of the effort. Mongolia's central bank and banking association organized a study tour to China in 2017; Indonesia's OJK shared its experience with the central bank of Sri Lanka during the country's first sustainable finance workshop in 2017; and the Moroccan capital market regulator brought its experience to Georgia's first sustainable finance forum in 2017, organized by the National Bank of Georgia.

Findings based on SBN Measurement Framework

The United Nations Sustainable Development Goals and the Paris Agreement are informing strategies for national sustainable finance initiatives, while public-private partnerships and interagency collaboration are ensuring compatibility with national priorities. SBN countries continue to align their sustainable finance policies and principles with international standards and global goals when developing national frameworks. Partnerships between financial regulators, industry, and environmental and climate change agencies, as well as private sector engagement and capacity building, are consistently adopted across almost all countries embarking on the development of sustainable finance policies and principles.

Development of regulatory or voluntary guidelines that set an expectation for how financial institutions should manage ESG risks has shifted from being niche to widely adopted, which has helped to level the playing field among banks. Twenty-two countries have issued guidelines on ESG integration in alignment with good international industry practices that include IFC Performance Standards and the Equator Principles on environmental and social risk management. These guidelines direct banks to manage potential risks to the environment and communities that arise from projects they finance. In a notable trend, financial regulators are integrating such

requirements into banking supervisory activities and supporting them with implementation tools and mandatory reporting requirements. Concerns over environmental degradation, national green growth strategies, and social development priorities are driving financial regulators' actions.

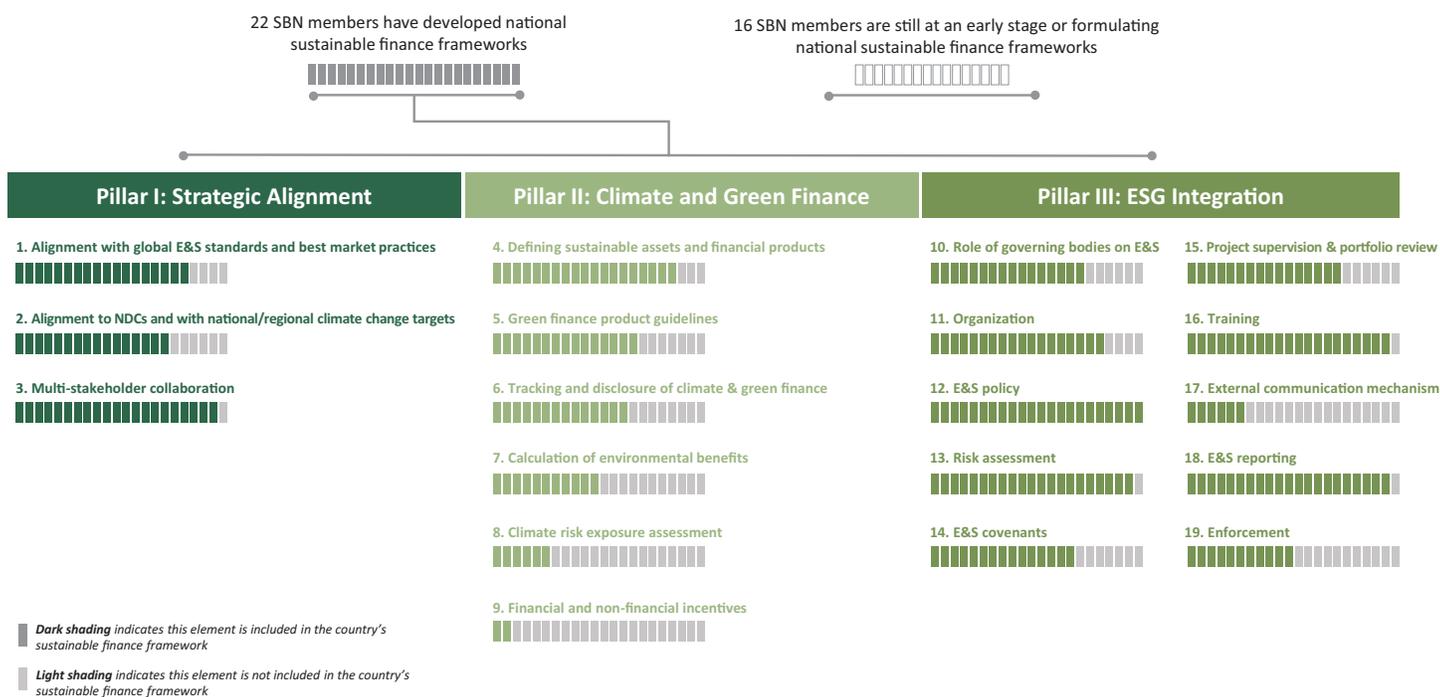
More countries have developed definitions and guidelines for green financial assets, especially for green bonds. Despite this trend, there is still significant potential to green the emerging market banking industry. Fourteen SBN countries have developed green bond guidelines that substantially align with or directly reference international standards such as the Green Bond Principles and the Climate Bonds Initiative. Six countries now provide definitions and/or examples of sustainable financial products and services beyond green bonds. From 2012 to 2018, emerging markets issued a total of US\$140 billion in green bonds; US\$43 billion of that was issued in 2018 alone. Considering that SBN members influence some 85 percent of the total banking assets across emerging market countries, there is enormous potential to redirect financial flows to climate and green sectors.

Robust efforts to understand and assess financial market risks and opportunities related to climate change have not yet begun in any significant way in most SBN member countries. Financial sector assessments by the World Bank underscore the need for banking supervisors to further integrate climate and sustainability risks into supervision. Only a few countries—Brazil and China among them—are collecting data on the exposure and impact of climate risks, and a few are setting precedents for regulator-led and industry-led approaches.

For example, Brazilian banking association Febraban recently developed a Climate Risk Sensitivity Assessment Tool to analyze the sensitivity of banks' credit portfolios to climate risks. This could assist banks with implementation of the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD).

While private sector financial institutions have not yet shown comprehensive behavior change toward sustainable finance, progress is well underway, and leaders are demonstrating high levels of interest in doing so. Regulatory data from China and Indonesia, as well as Felaban (the Latin American Federation of Banks) confirms that regulatory and voluntary initiatives are resulting in changing practices by financial institutions. However, comprehensive behavior change is still lacking in most cases. There are positive indications that banks are moving in the right direction, however. And case studies from pioneering banks show market innovation in green finance and best practices to manage ESG and climate risks.

Figure ES3: Elements included in SBN member countries' sustainable financing frameworks



Next steps

Policy is only a means to an end. What ultimately matters is the measurable change in practices by banks and the impacts of the businesses and projects they finance. After initial progress on setting a collective vision and creating an enabling framework for sustainable finance, SBN members are now moving into the phase of **Driving Measurable Change**, with a focus on four areas:

- 1. Sustainable finance needs to be central to financial supervision.** Financial sector regulators need to embed ESG and climate risk management, as well as green and climate-finance targets, into their day-to-day supervision activities.
- 2. Robust reporting and monitoring frameworks need to be established.** Commitments to disclosure and transparency on sustainable finance increase the ability of financial institutions to manage these issues. The data and insights from reporting and monitoring also empower regulators and supervisors to exercise effective checks and balances at both the institutional and the market level.
- 3. More work is urgently needed to enable financial market players to understand and manage both physical and transitional climate-related risks.** The World Bank is piloting an assessment module of climate change and environmental risks as part of the Financial Sector Assessment Program (FSAP). Global initiatives, including the Task Force on Climate-related Financial Disclosures (TCFD) and the Network for Greening the Financial System (NGFS), could provide much-needed technical resources for emerging markets.
- 4. Industry-wide capacity building remains critical to supporting broad behavior change among emerging market financial institutions.** Most countries are still working to embed sustainable finance in the practices of local financial institutions. For less developed markets, where there are competing priorities to develop basic financial market infrastructure, the challenge is even greater. Concerted efforts by international development agencies and other stakeholders could help address these challenges.



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www.ifc.org/SBN2019Report



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