



WWF

SUSTAINABLE  
FINANCE  
REPORT

2017



NUS  
National University  
of Singapore

Centre for Governance, Institutions  
and Organisations (CGIO)  
NUS Business School



# SUSTAINABLE BANKING IN ASEAN:

ADDRESSING ASEAN'S FORESTS, LANDSCAPES, CLIMATE, WATER, SOCIETIES

# ACKNOWLEDGEMENTS

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WWF is one of the world's largest and most experienced independent conservation organizations, with over 5 million supporters and a global network active in more than 100 countries. WWF's mission is to stop the degradation of the planet's natural environment and to build a future in which people live in harmony with nature. Environmental and social risks and opportunities are becoming increasingly important to financial decision-making. Some actors in the finance sector have made tremendous strides in their approach to incorporating environmental and social principles in their business models, and many are awakening to the investment opportunity they represent. WWF's International Finance Programme seeks to support this vision by engaging directly with banks, asset managers, regulators, stock exchanges and other financial institutions. It helps strengthen lending and investment criteria for key industry sectors, provides insights and data on environmental and social risks, fulfils critical research gaps, helps unlock innovation breakthroughs in sustainable financial products and convenes key stakeholders to progress the sustainable finance agenda.

The Centre for Governance, Institutions and Organisations (CGIO) was established by the National University of Singapore (NUS) Business School in 2010. It aims to spearhead relevant and high-impact research on governance and sustainability issues that are pertinent to Asia, including corporate governance, governance of family firms, state-linked companies, business groups, and institutions. CGIO also organizes events such as public lectures, industry roundtables, and academic conferences on topics related to governance and sustainability.

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# FOREWORD

**We live in a world which worships money. Individuals and families need to earn money in order to survive. Governments accumulate reserves in order to defend themselves against any future crisis. Businesses need to borrow money from banks and other financial institutions to fund their activities and expansion. In this world, the financier wields enormous power.**



**Tommy Koh**

*Ambassador-At-Large*  
Ministry of Foreign Affairs,  
Singapore

UNEP Champion of the Earth

*“Those who fund the growth of our world have the power – and responsibility – to ensure that their money is promoting development that is economically, environmentally and socially sustainable.”*

We have grown more prosperous but not more secure. In our quest for development and economic progress, we have done enormous damage to our natural environment. For example, with climate change, 1 billion people in the Asia Pacific may face food and water shortages. They will also face physical risks from extreme weather events. The annual economic losses in ASEAN due to climate change are estimated to be 2.5 times greater than the global average.

It is time for us to re-examine our current thinking on wealth and progress. Those who fund the growth of our world have the power – and responsibility – to ensure that their money is promoting development that is economically, environmentally and socially sustainable.

I warmly welcome WWF’s initiative to envision a resilient future for ASEAN by involving our financial sector. Singapore, as one of the world’s largest financial centres, has a critical role to play. I am gratified that the Ministry of Finance, the Monetary Authority of Singapore, the Singapore Exchange and the Association of Banks in Singapore are all committed to sustainable development.

I urge all my friends in the banking industry in this region to be part of this ASEAN sustainable growth story and ensure that the activities of their clients fully support the Paris Agreement on climate change and the UN’s Sustainable Development Goals. Together, I believe we can create great businesses and prosperous economies that do good for people – and the planet.

**Tommy Koh**

*Ambassador-At-Large*, Ministry of Foreign Affairs, Singapore  
UNEP Champion of the Earth



# FOREWORD

**As a global insurer and investor, we are acutely aware that the investments we make today will influence the world we live in tomorrow.**



**Steve Waygood**

Chief Responsible Investment Officer, Aviva Investors

*“There has never been a more exciting time to work on sustainable finance: across the world individuals, companies, investors, governments and global institutions are joining forces and creating a financial system that works better for everyone.”*

For generations, policymakers have sought to align the interests of the financial markets and society. Nowhere is this tension more keenly and persistently reflected than in the relentless pressure on the capital markets, including the banking sector, to allocate capital to short-term, unsustainable uses, and policymakers’ need to plan for the long term. This includes tackling a range of environmental and social issues, such as the nexus of issues surrounding poverty, climate change, water, sustainable resource use and human rights.

That being said, there has never been a more exciting time to work on sustainable finance: across the world individuals, companies, investors, governments and global institutions are joining forces and creating a financial system that works better for everyone.

In 2015, the ground-breaking Sustainable Development Goals and Paris Agreement on climate change represented global turning points. And we are now seeing further progress via initiatives such as the EU Sustainable Finance High Level Expert Group, this year’s Forum on Financing for Development and the recommendations of the Financial Stability Board’s Task Force on Climate-related Financial Disclosures, all of which Aviva Investors has been heavily involved in.

In fact, more global policy measures related to green finance have been introduced since June 2016 than in any other one-year period this century. The Southeast Asian region is home to a number of leading and emerging economies and will be critical in the global effort to tackle climate change. This insightful report provides a useful snapshot of the policy framework to support sustainable development on a country-by-country basis and highlights the potential for ASEAN banks to play a critical role in delivering these national goals

It is abundantly clear that financial institutions are constrained in what they can achieve on an individual basis. Before capital markets can be genuinely sustainable, investors need capital market policymakers to have greater regard for future generations when setting policy.

I encourage ASEAN financial institutions to engage with regulators and banking associations to demonstrate support for their sustainable finance regulations and take urgently needed steps to create a robust sustainable banking framework. I further encourage policymakers, regulators and individuals in the region and beyond to engage with the ideas presented here and work with civil society to create a multi-stakeholder based solution. We must now expand and amplify this discussion in order to build the financial system that the world demands and needs.

**Steve Waygood**

Chief Responsible Investment Officer, Aviva Investors

# FOREWORD

**This year marks ASEAN's 50th anniversary. Within a span of five decades, it has become the world's seventh-largest market and third-largest labour force.**

**The rapid development of this region has generated economic growth and lifted millions out of poverty, but at the same time led to increasing environmental and social degradation that could have been avoided.**

The socio-economic livelihoods of all 650 million people in ASEAN have never been at greater risk than they are today. Climate change, for instance, will result in projected economic losses of approximately 6.7 per cent of regional GDP by 2100. The precious biodiversity and natural capital of this region are equally at risk. Our lives are intertwined with nature, our very survival depends on nature.

*"Banks are key enablers for ASEAN countries to achieve both their Sustainable Development Goals and commitments under the Paris Agreement."*

Through the direction and conditions of their financing flows, banks are key enablers for ASEAN countries to achieve both their Sustainable Development Goals and commitments under the Paris Agreement. Regulators can provide crucial guidance to both create a level playing field and ensure impactful adoption of environmental, social and governance (ESG) practices. Investors play a role too in using their voice as shareholders to align portfolio banks with their own commitments on climate and other ESG matters. International consensus is that sound corporate governance must include the consideration of environmental and social risks and opportunities. As such, the foundation for sustainable finance should exist to support ASEAN banks to take on their role and responsibility for sustainable development.

This inaugural report is therefore a timely collaboration between WWF, with its deep environmental and sustainable finance expertise, and the National University of Singapore Business School's Centre for Governance, Institutions and Organisations, which has research excellence in corporate governance and sustainability reporting. The report presents a comprehensive overview of the level of disclosure against the key pillars of corporate governance and ESG integration across the ASEAN banking sector, against the backdrop of existing regulatory frameworks and national sustainable development agendas. This collaboration aims to spur awareness and prompt action toward financing sustainable development that has positive economic, environmental and social outcomes.

The message is clear: banks, their regulators and shareholders need to act now to galvanize the entire ASEAN banking sector to integrate ESG and create positive economic, environmental and social impacts on the ground in order for the region to survive and thrive in the next 50 years.

**Jeanne Stampe** *Head, Asia Finance & Commodities, WWF*

**Lawrence Loh** *Director of Centre for Governance, Institutions and Organisations, NUS*

# EXECUTIVE SUMMARY

**Unsustainable consumption and production practices in Southeast Asia have led to severe environmental and social damage, driving major threats such as climate change, deforestation, biodiversity loss and water scarcity. Natural capital stocks have been depleted, putting humanity at risk.**

**The region is extremely vulnerable to food and water crises due to climate change and ecosystem destruction.<sup>1</sup>**

Urgent changes are needed to the unsustainable development patterns of the past to prevent severe negative impacts on socio-economic development and human well-being. ASEAN countries recognize that the transition to more sustainable economic growth is crucial, and have all committed to the Paris Agreement on climate change and to deliver the Sustainable Development Goals (SDGs).

A key enabler to fulfil these commitments is the financial sector. Banks and financial institutions have the means to influence change in the real economy by directing the flow of capital away from environmental and social degradation and toward sustainable, climate-friendly alternatives. On top of that, global international frameworks such as the Task Force on Climate-related Financial Disclosures (TCFD) and United Nations Guiding Principles on Business and Human Rights (UNGP) have underscored the importance for the financial sector to be transparent and accountable for climate change and human rights risks arising from the activities of the clients they finance. Adverse weather patterns, resource scarcity and regulatory changes also pose increased credit risks in financial institutions' investment and lending portfolios and, more importantly, the financial system at large. Conversely, achieving sustainable development requires trillions in capital, generating vast opportunities for banks. There is therefore an urgent need to mobilize and empower the ASEAN banking sector to make a powerful contribution to sustainable development and to enhance its own long-term resilience and growth prospects.

This report highlights the vast potential of and nascent steps already taken by the ASEAN banking sector in driving sustainable development in the region. It is targeted at banks, financial regulators and investors; specifically those who are in the position to drive change in the banking sector to promote robust ESG integration for positive outcomes.

## OVERVIEW OF REPORT

The report considers the banking sectors of six ASEAN countries, namely Indonesia, Malaysia, the Philippines, Singapore, Thailand and Vietnam. It explores the sustainable finance regulatory landscape as well as the supporting corporate governance codes and sustainability reporting guidelines that pertain to the banking sector in these countries. It assesses disclosure by 34 listed banks against a set of indicators that represent the fundamental pillars of (i) sound corporate governance practices (board, shareholders and stakeholders, disclosure and transparency, audit and risk) and (ii) robust ESG integration practice (purpose, policies, processes, people, products, portfolio). These indicators are aligned to key international frameworks such as GRI and Sustainability Accounting Standards Board (SASB). The report uses public disclosure in the English language as of 30 August 2017 to consider information typically accessible to all stakeholders.



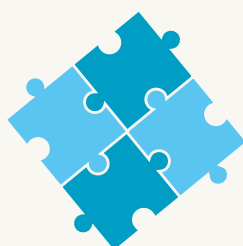


## KEY FINDINGS

**1. Sustainable development is strongly on the national agenda of policymakers in ASEAN countries, with common themes and a distinct role highlighted for the financial sector.** All six countries have included climate change mitigation and SDGs into their national policy agenda and formulated green growth strategies. Financial institutions are identified as key players to finance green technologies, promote green sectors and develop sustainable products that are aligned with sustainable development aims. In Malaysia and Thailand, the role of the finance sector in achieving sustainability targets has been formally recognized in national development plans.



**2. Existing sustainable finance regulations and guidelines are not fully aligned with the national development policy agendas, so there is untapped potential for the ASEAN finance sector to drive sustainable, resilient growth in the real economy.** Unlike national sustainable development strategies, the sustainable finance guidelines only provide suggested environmental and social (E&S) topics for banks to consider, and allow significant leeway for banks to decide which risks are material. As such, while 21 banks acknowledge ESG risks apply to their portfolios, only 14 disclose specific E&S risks that could impact their clients. It is therefore not clear what these banks' positions are when it comes to material sustainability issues, and whether they are aligned to national goals. However, 12 banks have taken steps to align their financial flows toward more sustainable activities on the ground through the use of exclusion lists and/or industry sector policies.



**3. There is significant potential for greater harmonization of sustainable finance regulations across ASEAN, given the common elements across corporate governance guidelines, listing rules and sustainability reporting guidelines.** Corporate governance guidelines in ASEAN countries are well structured and cover the key pillars of good corporate governance. The corporate governance guidelines, listing rules and sustainability reporting guidelines, when considered together, have common elements regarding ESG disclosure requirements. However, the sustainable finance regulations and guidelines are less harmonized. Three countries have no existing regulations or industry guidelines at all (Malaysia, Philippines and Thailand) while others have taken different approaches, with the Vietnam regulator issuing a mandatory directive, Singapore's banking association producing voluntary guidelines and Indonesian authorities providing sector-level guidelines and issuing regulations on sustainable finance.



**4. Supporting regulatory frameworks (corporate governance guidelines, listing rules and/or sustainability reporting guidelines) are already present in all six countries to support six pillars of ESG integration.** Corporate governance guidelines in all six countries are moving beyond traditional corporate governance aspects to consider E&S issues and also include the responsibility of the boards. Listing rules and/or sustainability reporting guidelines in all countries except Indonesia require stakeholder engagement and recognize local communities as stakeholders. Four of the six countries' frameworks also require or recommend companies to develop E&S policies and to establish E&S risk management.



**5. ASEAN banks are undergoing a paradigm shift in embracing sustainability as a core business strategy; they are coming to understand that their ESG risks and opportunities lie mainly within their portfolios rather than in their own operations.** Of the 34 ASEAN banks, 13 still consider the concept of sustainability to apply only to their own direct footprint via their buildings and employees, and have interpreted the corporate governance codes and sustainability reporting guidelines from that perspective. This is slowly changing, with six banks out of the 21 that recognize the E&S impacts of the activities they finance taking a step further to include responsible lending in their leadership statements.



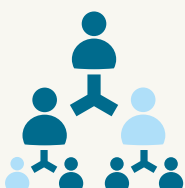
**6. ASEAN banks have a good corporate governance foundation on which to build up their ESG integration and fully incorporate both ESG risks and opportunities into strategy and operations.** With in-depth guidance from regulators, results show that banks are providing relatively robust disclosure on traditional corporate governance performance indicators such as board responsibilities and information disclosure. This foundation, primarily for risk management practices, can be used to enhance ESG integration and disclosure on E&S indicators, especially in light of the inclusion of E&S risk management into corporate governance codes.



**7. Existing sustainable finance regulations and guidelines are high level and impose neither incentives nor penalties to drive ESG integration, resulting in slower implementation and less stringent or inconsistent standards.** Existing sustainable finance regulations do not provide sector-specific guidelines, with the exception of Indonesia's palm oil and Singapore's anti-haze guidelines. Nor do they include requirements for internationally accepted credible sustainability standards. As such, only four banks disclose specific E&S requirements for their clients. There is no prescriptive guidance on how ESG integration should be implemented, resulting in inconsistent and incomplete disclosure on key pillars of ESG integration.



**8. Sustainability is not formally included in the mandate of board committees and senior management, with limited disclosure on board and senior level oversight of material ESG issues such as climate change.** Sustainability has not been disclosed as a consideration in the drafting of terms of reference for nominating committees, remuneration committees or audit committees for any of the countries studied. In addition, 24 out of 34 banks did not disclose whether senior management has oversight of the implementation of ESG integration; this suggests that ESG integration is not on the agenda of the senior leadership.



**9. Capacity gaps and lack of training are hindering banks from implementing ESG integration in a robust manner and from grasping opportunities to develop new sustainable finance products and deepen client relationships.** With only one bank disclosing a dedicated ESG team and 11 banks disclosing ESG training for staff, the capacity gap manifests itself in the lack of disclosure against key ESG integration indicators and in the slow uptake of ESG opportunities. While 17 banks mention sustainable banking products, none disclose the use of client outreach activities to share E&S insights and stimulate demand for sustainable banking products.



**10. There is no disclosure at all on portfolio-level management of ESG risks and opportunities, which suggests that a more strategic approach to sustainable banking is needed.** None of the ASEAN banks are disclosing the accumulated E&S risks or carbon intensity across their portfolios, nor their risk exposure reduction or green financing targets to align their portfolios to a resource- and carbon-constrained environment. This suggests there could be hidden and unknown E&S risks embedded in their portfolios and that there should be a more strategic approach to both risk management and the seizing of E&S opportunities.

## RECOMMENDATIONS

### WE RECOMMEND ASEAN BANKS:

- Create and implement a sustainable finance strategy underpinned by six fundamental pillars and with measurable time-bound targets to drive resilient economies. This strategy should be at least in line with, or more ambitious than, national agendas on climate change and sustainable development.
- Elevate sustainability to a core part of corporate strategy that has full board level oversight and focus from senior management, by including it in remuneration criteria and other corporate governance practices.
- Disclose sustainable finance practices and risk exposures using the recommended indicators and in alignment with TCFD for climate-related issues, to be accountable to stakeholders and enable shareholders to benchmark relative sustainability performance.
- Collaborate with stakeholders, such as regulators, banking associations and NGOs, to enhance capacity on sustainable finance, jointly develop sustainable banking guidelines and impact measurement/frameworks/methodologies, and create industry-wide change and a level playing field.
- Participate in relevant multi-stakeholder initiatives for the banking sector to demonstrate commitment by setting ambitious targets for ultimate alignment with the SDGs and the Paris Agreement, stay abreast of sustainable finance developments and benefit from peer-to-peer learning.

### WE RECOMMEND ASEAN CENTRAL BANKS AND BANKING ASSOCIATIONS:

- Facilitate ESG integration in the banking sector by establishing prescriptive, time-bound, enforceable national sustainable finance regulations or guidelines.
- Acknowledge that climate change and other material ESG risks could pose a systemic risk to the financial sector, providing guidelines for and mandating disclosure on these risks in line with TCFD recommendations. These guidelines should require banking clients to undertake climate risk materiality assessments and provide transition plans for relevant cases, and banks to perform environmental stress tests and assess alignment with the Paris Agreement when methodologies for climate scenario analysis are available.
- Design sustainable finance regulations in dialogue with policymakers in charge of climate change and sustainable development agendas to harness the power of the finance sector to contribute to these goals.
- Collaborate with regulators and banking associations from other ASEAN countries to harmonize ESG regulations. This will create a level playing field, ensure consistency for banks and prevent a race to the bottom in terms of sustainable finance standards.
- Support capacity-building for the banking industry by partnering with NGOs who can provide deep insights into E&S issues and create useful tools and guides.

### WE RECOMMEND SHAREHOLDERS OF ASEAN BANKS:

- Engage with ASEAN banks in investment portfolios to support the five recommendations for banks listed above and use their voting power to assert influence.
- Require portfolio banks to perform and disclose results of environmental stress tests and participate in initiatives to develop methodologies for climate scenario analysis of bank loan portfolios. This will enable investors to assess the level of alignment with their own climate/ESG commitments and policies and with the SDGs and the Paris Agreement, especially in light of TCFD disclosure recommendations.
- Engage with banks to require them to make public commitments using quantifiable targets to reduce their exposure to high carbon and high ESG footprint activities if the clients do not have adequate time-bound transition plans in place.
- Engage with stock exchanges in the region to require sector-specific disclosure guidelines for banks that reflect the recommended standards and align with TCFD recommendations.
- Engage with regulators and banking associations to demonstrate support for their sustainable finance regulations and affirm the business case for sustainable finance.

### WWF CAN SUPPORT THE FINANCE SECTOR BY:

- Building capacity in banks on ESG integration and sharing expert insights into key ESG issues such as climate, water and deforestation to enable banks to meet sustainable finance regulations and contribute to sustainable development.
- Developing useful tools and guides for the banking sector that facilitate ESG integration and reflect the latest science-based positions on sustainability.
- Advocating for change and providing expert insights on E&S issues to banking sector regulators and banking associations to support their formulation of sustainable finance regulations.
- Monitoring ESG integration progress in the ASEAN banking sector by issuing annual reports on banks' disclosure and level of harmonization of ESG regulatory frameworks.
- Collaborating with investors to increase their focus on the role of their portfolio banks in the transition to a carbon- and resource-constrained world and facilitate engagement with banks in ASEAN on these topics.

### CGIO CAN SUPPORT THE FINANCE SECTOR BY:

- Performing analysis on listed companies and highlighting overall trends in corporate governance disclosures via comprehensive frameworks.
- Assessing the strengths and weaknesses in corporate governance in ASEAN countries through various studies on their listed companies.
- Shedding light on outstanding progress and stagnation among banks in their practices and disclosures, which is useful to regulators and policymakers.
- Raising awareness of the importance of sustainability reporting and providing thought leadership on ESG issues by organizing events, conferences and seminars.





# INTRODUCTION

ADDRESSING ASEAN'S FORESTS,  
LANDSCAPES, CLIMATE, WATER,  
SOCIETIES



# INTRODUCTION

**Human activity in the form of unsustainable consumption and production has placed unbearable pressure on nature through habitat destruction, deforestation, climate change, overexploitation of species and pollution.**

The Earth's ecosystems provide a flow of natural resources and services to humanity, but over the last decades we have been consuming more than the planet can regenerate. In 2016, our consumption of natural resources and services required the capacity of 1.6 Earths.<sup>2</sup> The depletion of our natural capital stocks has led to unprecedented losses in biodiversity – the WWF Living Planet Index shows a 58 per cent drop in species populations between 1970 and 2012.

While many living organisms face extinction, the very survival of humanity is at risk. We depend on nature for vital ecosystem services such as food, water, fuel and a stable climate. The depletion of natural capital results in climate change, acidification of oceans and the disappearance of biomes, intensifying food and water insecurity. Lives are lost and property is damaged due to extreme weather events, which are increasing in frequency and intensity as a result of climate change. In addition, it is typically the poor who suffer more, as already experienced in developing countries.

All this creates downward pressure on social and economic development. The strong interdependence between economic, environmental and social well-being is recognized in the SDGs<sup>3</sup> which came into effect in January 2016. This set of 17 global goals includes multiple environment-related targets covering areas such as climate action, clean water, life in the oceans, life on land, and responsible consumption and production.

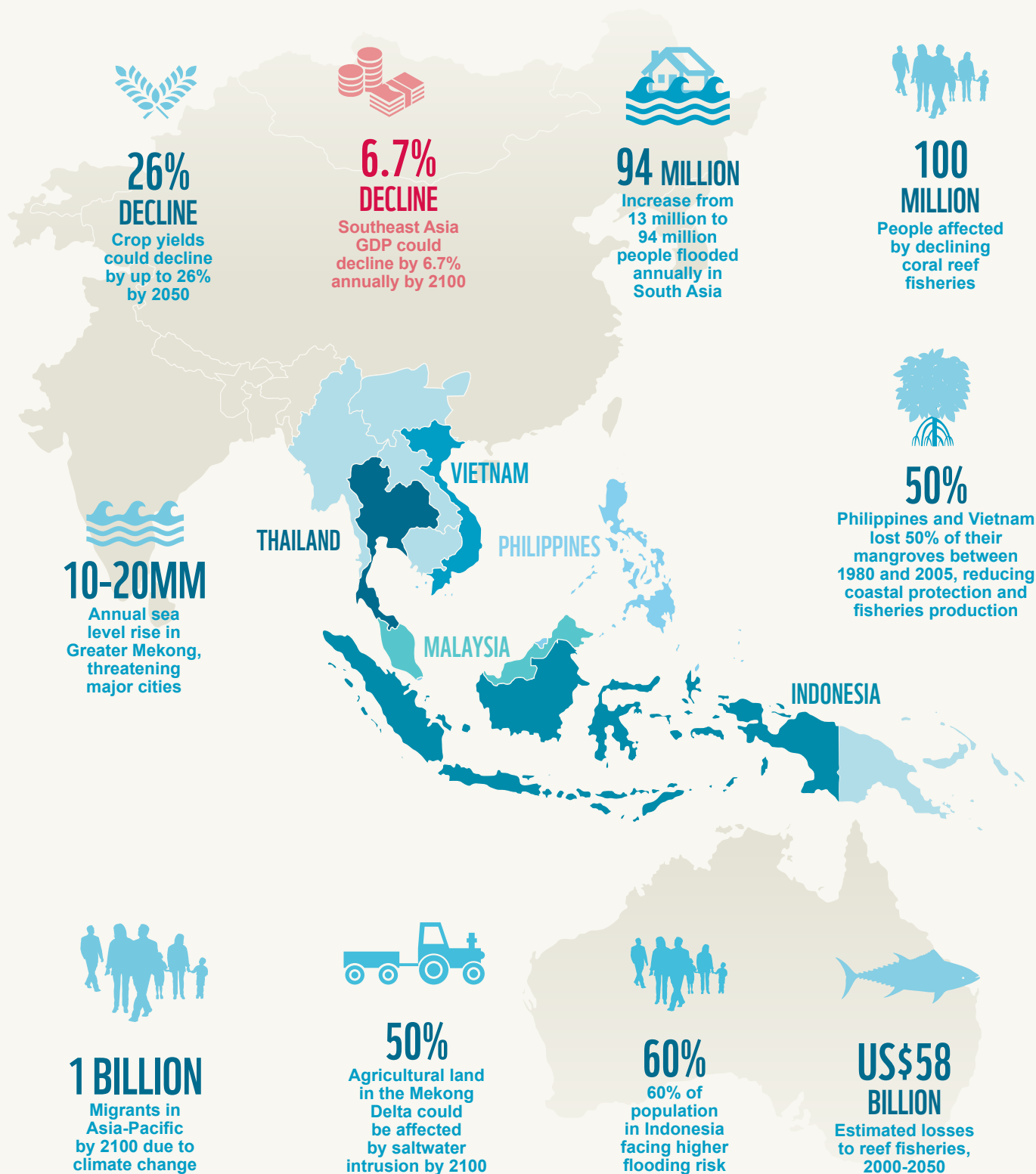
Global action is critical as the impacts of climate change and ecosystem degradation are felt globally. Food and water crises will have knock-on impacts beyond the countries in which they occur due to global food supply chains and geopolitical instability from mass migration or wars. This is a global problem affecting each and every one of us.

## AT THE ASEAN REGIONAL LEVEL

### FOSSIL FUEL-BASED ENERGY PRODUCTION IS EXACERBATING CLIMATE CHANGE AND AIR POLLUTION

Southeast Asia produces 12 per cent of the world's greenhouse gas (GHG) emissions with fossil fuels accounting for 74 per cent of the region's energy mix.<sup>4</sup> Energy generation is the main cause of air pollution in Southeast Asia with a severe toll on human lives, with 200,000 premature deaths a year in Indonesia alone.<sup>5</sup> While Southeast Asia has the potential to significantly mitigate emissions by increasing the proportion of energy derived from renewable sources, it is one of the few regions where demand for coal – the most heavily polluting energy source – is projected to increase. According to the International Energy Agency (IEA)<sup>6</sup>, by 2040 coal will represent the largest fuel in the energy mix and account for 29 per cent of Southeast Asia's energy demand, with the overall share of renewable energy expected to decline from 26 per cent to 21 per cent.

FIGURE 1: ENVIRONMENTAL AND SOCIAL THREATS IN ASEAN<sup>7,8,9,10</sup>



### FRESHWATER SYSTEMS HAVE BEEN DEGRADED BY UNSUSTAINABLE DAM CONSTRUCTION AND AGRICULTURE AS WELL AS POOR WATER AND RIVER BASIN GOVERNANCE



Water resources in Southeast Asia are under growing stress from pollution, agriculture and population growth.<sup>11</sup> Rapid economic and demographic growth have resulted in sudden industrialization and urbanization, which have not been followed by the development of appropriate wastewater treatment infrastructure. At present, only between 2 to 20 per cent of households in Indonesia, Vietnam and the Philippines are connected to sewerage systems.<sup>12</sup> The problem affects all Southeast Asian countries with 90 per cent of wastewater in the region being discharged into water streams without treatment.<sup>13</sup>

The problem is further exacerbated by the water intensity of agricultural activities in the region. Regional water withdrawal for agriculture accounts for more than 80 per cent of the total withdrawal, with peaks of 92 per cent in mainland Southeast Asian countries, much higher than the world average of 70 per cent.<sup>14</sup>

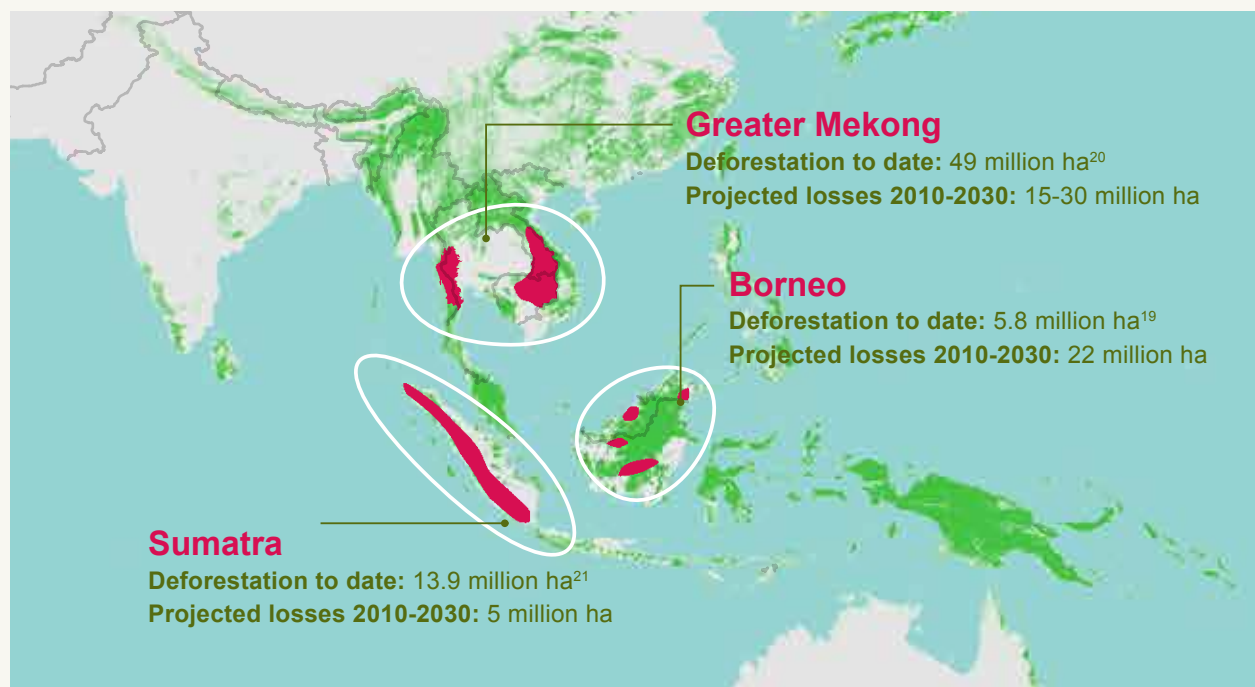
Growing energy demand driven by population and economic growth has led to an unprecedented rate of hydroelectric dam building with significant impacts on freshwater ecosystems and the people that rely on these. Up to 11 new dams are planned for the Lower Mekong River alone, degrading the fisheries and ecological services that support at least 60 million people.<sup>15</sup>

### DEFORESTATION FROM UNSUSTAINABLE BUSINESS ACTIVITIES HAS RESULTED IN SEVERE BIODIVERSITY LOSS, ECOSYSTEM DESTRUCTION, DISPLACEMENT OF LOCAL COMMUNITIES AND GHG EMISSIONS



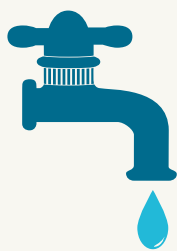
Southeast Asia contains some of the world's most biodiverse tropical forests, but suffers from rapid rates of forest loss due to a heavy dependence on natural resources and soft commodities for economic development. Some tropical areas such as Indonesian and Malaysian Borneo have already lost over half of their original forest cover.<sup>16</sup> Mainly due to the production of palm oil, pulp and paper, and rubber, as well as infrastructure projects, Southeast Asian countries will lose most of their native forests and biodiversity within 20 years if irresponsible business practices do not change. Deforestation has resulted in the displacement of local communities who depend on forests for their livelihoods and in the destruction of key ecosystems, including marine and freshwater ecosystems.

Deforestation is also a key driver of GHG emissions from ASEAN with the recurring haze from Indonesia providing a jarring reminder of natural capital depletion by human activities. The related peat fires from irresponsible land clearing result in skyrocketing GHG emissions related to the agriculture sector. Indonesia's peat fires in 2015 caused daily emissions levels exceeding the average daily emissions from all US economic activity.<sup>17</sup>

FIGURE 2: SOUTHEAST ASIA DEFORESTATION MAP<sup>18</sup>

Source: WWF Living Forests Report: Chapter 5<sup>22</sup>

## CLIMATE CHANGE, DEFORESTATION AND DESTRUCTION OF FRESHWATER ECOSYSTEMS WILL CAUSE ECONOMIC AND HUMAN LOSSES AS WELL AS SEVERE WATER AND FOOD INSECURITY RISK IN ASEAN



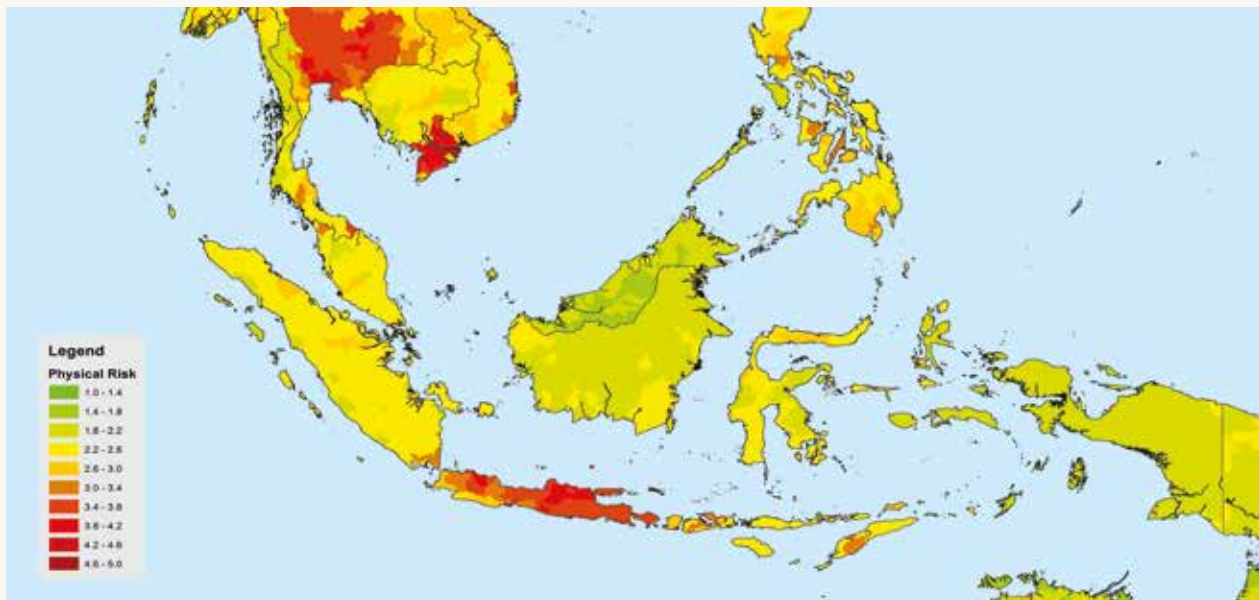
The Intergovernmental Panel on Climate Change (IPCC) has identified forestry, agriculture and water resources as the sectors most vulnerable to climate change impact in Asia.<sup>23</sup> For ASEAN in particular, the Asian Development Bank (ADB) has projected that climate-related disasters including the impact of climate change on the agricultural sector, coastal zones, health and ecosystems will result in annual economic losses in the magnitude of 6.7 per cent of the region's GDP by 2100, far higher than the global average of 2.6 per cent.<sup>24</sup>



Rising temperatures will leave ASEAN countries exposed to more frequent extreme weather events including floods and droughts. These events will cause loss of lives and destruction of infrastructure and property, as well as interrupting the operations of local businesses and global supply chains. Nineteen of the 25 cities most exposed to sea level rise are in Asia.<sup>25</sup> Southeast Asian countries are the most vulnerable with seven of these cities located in the Philippines and 5.9 million Indonesians projected to be affected by coastal flooding every year to 2100. With many of ASEAN's largest cities located in coastal zones, the combination of rising sea levels and pumping water from coastal aquifers means urban water supplies will face growing threats of saltwater intrusion, impacting food production and the availability of drinking water. Saltwater intrusion and rising temperatures are projected to decrease crop yields in the region with cereal production projected to decline by up to 10 per cent and rice yields by 6-12 per cent by 2050.

The extent of this vulnerability is already evident when looking at the Greater Mekong Sub-region (GMS) where severe droughts have led to the lowest water levels in the last century, emptying urban water reserves and causing saltwater intrusion to impact half of the delta’s agricultural lands.<sup>26</sup> Empty underground aquifers and reservoirs and rising sea levels are causing major urban centres in the GMS to sink, exposing 20 million people to the risk of displacement by the end of the century.<sup>27</sup> Detailed modelling from Massachusetts Institute of Technology researchers predicts serious water shortages will hit Asia Pacific by 2050 with as many as 1 billion people becoming water-stressed.<sup>28</sup> Without increased action to mitigate climate change, by 2100 a projected 1 billion people in Asia Pacific will be forced to migrate to escape its negative consequences,<sup>29</sup> with a significant proportion of them from Southeast Asia.

**FIGURE 3: SOUTHEAST ASIA WATER RISK MAP**



Source: WWF Water Risk Filter ([waterriskfilter.panda.org](http://waterriskfilter.panda.org)), which banks can use to assess their clients’ water risk exposure and mitigation efforts.



**GOVERNMENTS AND THE PRIVATE SECTOR HAVE PLEDGED BILLIONS OF DOLLARS TO ADDRESS CLIMATE CHANGE**

**CAN THESE PROBLEMS BE SOLVED, HOW AND BY WHOM?**

We need to change the global economic system to decouple human development from environmental degradation and social exclusion, resulting in a resilient planet for both people and nature. WWF believes that this transition will require: (1) preservation of natural capital, (2) equitable resource governance, (3) sustainable and resilient consumption and production markets, (4) transformation of food and energy systems and (5) redirection of financial flows. Everyone has a part to play and partnerships are needed between governments, the private sector and civil society.

We witnessed such a collaboration in the 2015 Paris Agreement within the United Nations Framework Convention on Climate Change (UNFCCC).<sup>30</sup> This came out of concerted global efforts from many stakeholders resulting in nearly all countries committing to combat climate change. Governments and the private sector have pledged billions of dollars to address climate change via commitments to decrease GHG emissions, adopt renewable energy and engage in sustainable resource management.<sup>31</sup> The SDGs provide further evidence of the international commitment to addressing unsustainable development and environmental degradation: 193 governments have signed up<sup>32</sup> and many businesses have also adopted the SDG agenda.<sup>33</sup>





ALL 10 ASEAN COUNTRIES HAVE SIGNED UP TO THE SDGs AND TO THE PARIS AGREEMENT

## RECOGNITION AND COMMITMENT AT THE ASEAN REGIONAL LEVEL

At the regional level, the 10 ASEAN countries recognize the importance of addressing E&S issues. All of these countries have signed up to the SDGs and to the Paris Agreement. One of the targets of the ASEAN Economic Community Blueprint 2025 is “to create a more dynamic and resilient ASEAN, capable of responding and adjusting to emerging challenges through robust national and regional mechanisms that address food and energy security issues, natural disasters, economic shocks, and other emerging trade-related issues as well as global mega trends”.<sup>34</sup> The incorporation of a sustainable growth agenda and support for green technology and energy are also included as part of the vision.

## WHAT IS THE ROLE OF THE FINANCE SECTOR AND WHAT DOES IT NEED TO DO TO CONTRIBUTE TO SUSTAINABLE DEVELOPMENT?

The finance sector has a unique enabling role to play in the transition by redirecting financial flows toward sustainable operations and away from environmentally and socially destructive business activities. This will help preserve natural capital and promote resilient and sustainable markets. The impending acute resource scarcity, water stress and disruptive weather events, coupled with increasingly stringent environmental regulations, will impact businesses and increase risks in financial institutions’ lending and investment portfolios. On the flip side, the transition to a resource-constrained economy will create significant financing needs in renewable energy, energy efficiency, sustainable agriculture, sustainable infrastructure and financial inclusion for the bottom of the pyramid. Failure to act is not an option for the finance sector as these E&S issues are increasingly material to financing decisions.



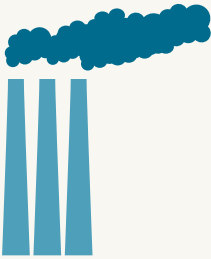
THE FINANCE SECTOR MUST BE PART OF THE SOLUTION RATHER THAN THE PROBLEM

The Paris Agreement highlighted the crucial role of financial flows in achieving the goals of keeping global temperature rise this century well below 2°C above pre-industrial levels and strengthening the ability of countries to adapt to climate change. The Marrakech Partnership for Global Climate Action, which aims to accelerate the implementation of the Paris Agreement in the period 2017-2020, marks the finance sector among key actors.<sup>35</sup>

While the Paris Agreement deals with climate change, the same principle regarding the role and responsibility of the finance sector applies to other environmental and social issues: the finance sector must be part of the solution rather than the problem. The World Bank’s *Billions to trillions* report<sup>36</sup> identified that “the private sector will play a pivotal role in financing the post-2015 development agenda.”<sup>37</sup> In 2017, the Office of the United Nations High Commissioner for Human Rights clarified that the UN Guiding Principles on Business and Human Rights (UNGPs) apply to banks, meaning they must account for adverse human rights impacts caused by their clients’ activities.<sup>38</sup> This underpins the role and responsibility of the finance sector in driving sustainable development.

At the same time, the finance sector must protect its own financial viability and competitiveness; a 2017 report by Bank Of America Merrill Lynch pinpoints ESG integration as a good indicator of stocks’ earning potential, offering investors substantial mitigation of price and earning risks.<sup>39</sup> For example, financial institutions that are attuned to water risks can ensure that investments and assets are not stranded as water resources come under further pressure. Conversely, as risks grow, so too do opportunities to invest in or lend to companies with robust water stewardship strategies that are likely to perform better. ESG integration can enhance risk management and maximize opportunities for the finance sector.

To drive sustainable development and to make their own business models viable in a resource-constrained world, banks in particular need to fully integrate ESG into the core of their business – into their purpose, policies, processes, people, products and services and their entire portfolio. Banks need a paradigm shift in how they view their impact on the real economy, on the environment and society. For a start, they need to acknowledge that climate and other material ESG risks and opportunities exist within their portfolios (i.e. their indirect footprint) due to the enabling role they play as a finance provider, rather than demarcate their ESG impact as only the direct footprint of their workforce and offices.



THE MOST RECENT GAME-CHANGING SUSTAINABILITY INITIATIVE TAKEN BY THE FINANCE SECTOR IS THE TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES

### WHAT KEY STEPS HAVE THE FINANCE SECTOR, AND BANKS IN PARTICULAR, ALREADY TAKEN TOWARDS A RESILIENT PLANET FOR NATURE AND PEOPLE?

The most recent game-changing sustainability initiative taken by the finance sector is the Task Force on Climate-related Financial Disclosures (TCFD)<sup>40</sup> created by the Financial Stability Board (FSB) at the initiative of the G20. The task force has worked with the private sector and public members to develop recommendations for a standardized climate-related financial disclosure framework. It aims to make it mainstream for financial reporting to cover climate change-related risks so that investors, lenders, insurers and other stakeholders can appropriately assess and price such risks and opportunities. Banks are hence core to the discussion as they are both users and disclosers of climate-related information. Banks are instructed by a Supplemental Guidance for the Financial Sector<sup>41</sup> which covers disclosure of risks and opportunities in the banks' lending portfolios and other financial intermediary business activities.

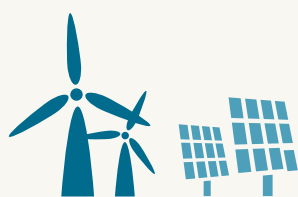
The recommended climate-related disclosure by asset owners and fund managers themselves will also trigger these investors to request banks to adequately disclose and manage climate change risks in their investment portfolios. Boston Common's 2017 investor-backed report emphasizes that investors are increasingly looking at how banks institutionalize the management of climate risk or opportunities, having revealed that top global banks are still not fully aligned with the 2°C scenario.<sup>42</sup> Boston Common subsequently led a coalition of institutional investors managing more than \$1tn in assets to demand that the 60 largest banks in the world disclose their exposures to climate-related risks and their plans to ensure compliance with the Paris Agreement and support the transition to a low-carbon economy.<sup>43</sup>

Evidence also demonstrates as well that banks can become subject to litigation due to inadequate disclosure on climate risk relating to their financing activities. Commonwealth Bank of Australia most recently came under scrutiny after it was taken to court by its shareholders for not being transparent enough on the risks that climate change poses to its businesses.<sup>44</sup> Understanding the urgency to address climate risk, 11 global banks have already committed to work on developing tools to implement TCFD recommendations.<sup>45</sup>



13 GLOBAL BANKS PLEDGED TO ACHIEVE ZERO NET DEFORESTATION WITHIN THEIR COMMODITIES PORTFOLIOS BY 2020

Actions by banks have not been limited to dealing with climate change risks. Banks are increasingly recognizing other major ESG risks such as deforestation, water scarcity and human rights abuses in the activities they finance. The New York Declaration on Forests, which endorses a global timeline to halve natural forest loss by 2020 and strive to end it by 2030, has banks among its signatories.<sup>46</sup> In addition, 13 global banks pledged to achieve zero net deforestation within their commodities portfolios by 2020 as part of a 'Soft Commodities Compact'.<sup>47</sup> Financial institutions have collaborated with a number of organizations including the Natural Capital Finance Alliance to develop a tool to stress-test bank loan portfolios under drought scenarios.<sup>48</sup> In 2016 the Dutch banking sector signed an agreement on international responsible business conduct<sup>49</sup> to integrate protection and respect of human rights into banks' policy commitments, client engagement strategies, corporate loans and project finance activities. The signatories of



FINANCING PROJECTS SUCH AS RENEWABLE ENERGY, RURAL ELECTRIFICATION AND SUSTAINABLE AGRICULTURE LIFTS MILLIONS OUT OF POVERTY AND HELPS ASEAN COUNTRIES ACHIEVE SDGs

the agreement committed to collaborate with counterparts including the UN and other international networks to inspire other banks, governments, trade unions and non-governmental organizations (NGOs) to join their efforts. Within the European Union, the European Commission established a High-Level Expert Group (HLEG) on Sustainable Finance in September 2016, whose task is to develop a strategy in creating a sustainable finance system.<sup>50</sup> The HLEG consists of experts from civil society (including WWF), the financial sector and academia.

The pressure on banks and their own initiatives to be accountable for their indirect ESG impacts have therefore gained tremendous traction in recent years. The banking sector's commitment to contribute to society and development, linked to the banks' purpose in life, has extended beyond traditional corporate social responsibility (CSR) and evolved into ESG integration, albeit not always on a comprehensive basis nor adhering to adequate ESG risk mitigation standards.

### WHAT DOES THIS IMPLY FOR ASEAN BANKS?

Banks in ASEAN countries can play a significant role in driving sustainable development. They can use access to and the cost of their loan capital to require their clients to take ambitious steps to transform food, energy, transport and infrastructure systems in the region. This will ensure that the regional finance sector, upon which many SMEs and local businesses (rather than multinational corporations) rely, acts as a key enabler for ASEAN to achieve both its SDGs and its commitments under the Paris Agreement. Banks could finance activities which are aligned with fulfilling the SDGs. For instance, financing of climate change adaptation and mitigation projects such as renewable energy, rural electrification, sustainable agriculture, green cities, green transport and water conservation can help ensure access to sustainable and affordable food, water, energy, education and healthcare to all ASEAN citizens, lifting millions out of poverty and helping ASEAN countries achieve SDGs.



ASEAN BANKS AND INVESTORS HAVE BEEN TARGETED FOR FINANCING UNSUSTAINABLE PALM OIL PRODUCTION

### ARE ASEAN BANKS READY TO STEP UP?

The ASEAN banking sector has improved its corporate governance practices due to stronger regulations in this area over the years. However, banks have yet to shift their current main focus on corporate governance to a wider integration of E&S indicators. Sound corporate governance, as reflected by the most recent corporate governance codes in Malaysia and Thailand, requires corporations to fully manage their material risks, which should include E&S risks.<sup>51</sup> Beyond ASEAN and within the Asia Pacific community, the Japanese corporate governance code<sup>52</sup> goes one step further and requires companies to take appropriate measures to address sustainability issues, including social and environmental matters, in order to create value for all stakeholders while increasing corporate value over the medium to long term.

The delay in integrating ESG by ASEAN banks has resulted in increased scrutiny from NGOs for their role in financing unsustainable operations. The 2015 WWF report *Sustainable Finance in Singapore, Indonesia and Malaysia: A review of financiers' ESG practices, disclosure standards and regulations*<sup>53</sup> highlighted the business case for ESG integration by these three countries' banks. Between 2015 and 2016, on-the-ground assessment by Responsibank<sup>54</sup>, Rainforest Action Network<sup>55</sup> and the Global Canopy Programme<sup>56</sup> found many ASEAN banks were not adopting sustainable lending practices for the palm oil sector. Investors themselves are also being probed, as is evident in the Aidenvironment report which exposed how Nordic investors are indirectly financing unsustainable palm oil in Indonesia through their investment portfolio in Southeast Asian banks.<sup>57</sup> There are hence severe implications for investors too if they are found to be investing irresponsibly.

On a positive note, a number of ASEAN banks have come up with improved ESG frameworks over the past two years. This is driven partly by regulators and banking associations stepping up to issue green finance-related guidance, and partly by constructive support and advocacy from intergovernmental organizations and development agencies such as the International Finance Corporation (IFC), the United Nations Environment Programme Finance Initiative (UNEPFI) and the German international development corporation GIZ, and NGOs such as WWF. At the regional level, the ASEAN Bankers Association convened ASEAN banks, associations and regulators in September 2017 to share learning experiences and know-how and stimulate collaboration, in a Sustainable and Responsible Financing Workshop organized in partnership with WWF and IFC. In short, progress has been made but there is still vast potential to harness the power of the ASEAN banking sector to drive sustainable development.

## PURPOSE OF THIS REPORT

**This report investigates the sustainable finance landscape in the ASEAN region to shed light on recent developments in the ESG integration progress of banks.**

**Our main objectives are to:**

- Highlight the potential of the finance sector in driving sustainable development in ASEAN with positive environmental, social and economic outcomes.
- Highlight common threads of national sustainable finance/ESG regulations and guidelines across ASEAN to promote harmonization.
- Assess the level of alignment between national banking regulations/banking association guidelines and national commitments on key sustainability outcomes such as the Paris Agreement and SDGs.
- Demonstrate how existing regulatory frameworks (corporate governance codes and listing rules) support ESG integration by banks.
- Ascertain if there is a good foundation of disclosure on corporate governance indicators on which banks can build to include management of E&S risks and opportunities.
- Assess the disclosure on indicators of ESG integration to identify gaps in implementation that can be addressed by banks and/or policymakers in cooperation with other stakeholders such as NGOs.
- Provide a useful framework and key indicators of ESG integration against which banks can assess and monitor progress and provide meaningful disclosure to stakeholders.

### WHO THIS REPORT IS AIMED AT:

- **Banking regulators and associations** can use the report to formulate and refine national ESG regulations and guidelines and seek to harmonize them across ASEAN. The bank-level assessments can help regulators monitor the level of ESG integration and hence the success of policy implementation on the ground.
- **Banks** (board members, CEOs, CFOs, CROs, credit, risk and sustainability teams) can use the report to understand and improve their level of ESG integration and disclosure against objective indicators. They can identify more progressive peers which have worked with stakeholders such as NGOs to advance their internal capacity and create peer-to-peer learning and sharing opportunities.
- **Investors** (CIOs, risk officers, portfolio managers, banking sector analysts, ESG analysts) can use the report to gain insights into the ESG performance of ASEAN banks already in their portfolios or under consideration for investment. They can understand if these banks have ESG policies aligned to their own ESG commitments. They can use the results to engage with portfolio banks to support and drive faster progress.



# CHAPTER 1

METHODOLOGY



# BANKS INCLUDED IN THE REPORT

This report covers 34 banks across six ASEAN countries, namely Indonesia, Malaysia, the Philippines, Singapore, Thailand and Vietnam.

The major publicly listed banks headquartered in each country were included to represent the regional banking industry upon which most local businesses rely. Banks from Myanmar are not included in this year's assessment, as most of the banks have not yet disclosed their 2016 annual report by the time of the publication. Banks from Cambodia, Laos and Brunei were also not considered as these countries do not have publicly listed banks on their stock exchanges. *The list of banks reviewed can be found in the table opposite:*



TABLE 1: ASSESSED BANKS

1 INDONESIA	2 MALAYSIA	3 PHILIPPINES	4 SINGAPORE	5 THAILAND	6 VIETNAM
<ul style="list-style-type: none"> <li>■ Bank Central Asia Tbk (BCA)</li> <li>■ Bank Mandiri (Persero) Tbk (Mandiri)</li> <li>■ Bank Negara Indonesia Tbk (BNI)</li> <li>■ Bank Panin Tbk (Panin)</li> <li>■ Bank Permata Tbk (Permata)</li> <li>■ Bank Rakyat Indonesia Tbk (BRI)</li> <li>■ Bank Victoria International Tbk (Victoria)</li> </ul>	<ul style="list-style-type: none"> <li>■ AMMB Holdings Berhad (Ambank)</li> <li>■ CIMB Group Holdings Berhad (CIMB)</li> <li>■ Hong Leong Bank Berhad (Hong Leong)</li> <li>■ Malayan Banking Berhad (Maybank)</li> <li>■ Public Bank Berhad (Public Bank)</li> <li>■ RHB Bank Berhad (RHB)</li> </ul>	<ul style="list-style-type: none"> <li>■ BDO Unibank, Inc (BDO)</li> <li>■ Bank of the Philippine Islands (BPI)</li> <li>■ China Banking Corporation (CBC)</li> <li>■ Metropolitan Bank &amp; Trust Company (Metrobank)</li> <li>■ Philippine National Bank (PNB)</li> <li>■ Security Bank Corporation</li> </ul>	<ul style="list-style-type: none"> <li>■ DBS Group Holdings Limited (DBS)</li> <li>■ Oversea-Chinese Banking Corporation Limited (OCBC)</li> <li>■ United Overseas Bank Limited (UOB)</li> </ul>	<ul style="list-style-type: none"> <li>■ Bangkok Bank</li> <li>■ Bank of Ayudhya (Krungsri)</li> <li>■ Kasikorn Bank (KBank)</li> <li>■ Krung Thai Bank (KTB)</li> <li>■ Siam Commercial Bank (SCB)</li> <li>■ Thanachart Bank (TBANK)</li> <li>■ TMB Bank (TMB)</li> </ul>	<ul style="list-style-type: none"> <li>■ Bank for Investment and Development of Vietnam (BIDV)</li> <li>■ Joint Stock Commercial Bank for Foreign Trade of Vietnam (Vietcombank)</li> <li>■ Vietnam Export-Import Commercial Joint Stock Bank (Eximbank)</li> <li>■ Vietnam Joint Stock Commercial Bank for Industry and Trade (VietinBank)</li> <li>■ Vietnam Prosperity Bank (VPBank)</li> </ul>

### SCOPE OF BANKING ACTIVITIES INCLUDED IN THE REVIEW

The corporate governance review covers the entire corporation. The ESG integration review focused only on the banks' external or indirect ESG footprint in terms of the client activities they finance rather than the corporation's own direct footprint, as the former is overwhelmingly larger in magnitude and impact.

The review focused mainly on the corporate/wholesale lending divisions of the regional banks. Retail banking, private banking, investment banking and asset management divisions were excluded. The reason for this is twofold: (i) the client operations financed by the wholesale lending versus retail and private banking have the largest ESG footprint and hence the largest potential contribution toward sustainable development in ASEAN; and (ii) the regional banks have a larger proportion of their businesses in wholesale lending versus investment banking or asset management compared to international banks. Nonetheless, certain ESG integration indicators such as commitments to international initiatives and client approval processes typically apply to clients across all divisions of banks.

### INFORMATION USED TO UNDERTAKE THE RESEARCH

We reviewed only publicly available disclosure in the English language in the form of 2016 annual reports, 2016 sustainability or CSR reports that were released before 30 June, and information posted on corporate websites such as company policies, statements, investor presentations and press releases (last accessed on 30 August 2017). This public disclosure represents what is accessible to international investors and stakeholders to develop an understanding of how the banks are managing climate and ESG risks and opportunities so as to contribute to sustainable development. The financial reports of all 34 banks had full English language disclosure and we believe that the same level of transparency and accessibility should apply to ESG/sustainability-related information which is material to stakeholders including investors, as highlighted in the introduction. Information reported in other languages was not considered for this reason. The banks were not interviewed and have not verified the information contained in this report.

### DISCLOSURE ASSESSMENT FRAMEWORK

The review was undertaken using an assessment framework based on four key aspects of good corporate governance and six fundamental pillars of robust ESG integration.













**FIGURE 4: THE FOUNDATIONS AND PILLARS OF SUSTAINABLE BANKING**

**Corporate governance:** In order to achieve their long-term goals and strategy, banks should have an independent, diversified and competent **board** to guide senior management and monitor the implementation of strategic plans. **Shareholders** and other **stakeholders** should also be valued: banks need to clearly set out policies to ensure the rights of their shareholders and communication channels to engage stakeholders. Once the policies are in place, banks should provide **transparency** and **disclosure** via their reports and corporate websites in a timely and reliable manner. To increase credibility and effectiveness, banks need to make ongoing efforts on **audit** and **risk management**.

**ESG integration:** Banks need to recognize that sustainability is a necessary condition for long-term growth and they have a crucial role to play in financing sustainable development. This is their **purpose** and link to the real economy. They need to set **policies** to guide the integration of E&S principles into internal **processes** and engagement with clients. To do so, they need to have well-trained **people** in place with clear roles and responsibilities and senior-level oversight. ESG integration is not just about management of E&S risks: it is also about translating the banks' knowledge and purpose into sustainable banking **products** to capitalize on opportunities. In order to manage enterprise-level risks and opportunities and ensure that the bank's business model properly embraces sustainability, a strategic overview at **portfolio** level is crucial.

**THERE ARE 11 CORPORATE GOVERNANCE INDICATORS AND 11 ESG INTEGRATION INDICATORS BEHIND THE FOUNDATIONS OF CORPORATE GOVERNANCE AND ESG INTEGRATION.**

TABLE 2: CORPORATE GOVERNANCE ASPECTS AND ESG INTEGRATION PILLARS

ASPECTS (CG)	No.	INDICATORS	PILLARS (ESG)	No.	INDICATORS
<b>1) BOARD</b> 	1	Independence and qualifications of the board	<b>1) PURPOSE</b> 	1	Relevance of sustainability to the organization and its strategy for addressing sustainability
	2	Clearly stated roles and monitoring the implementation of corporate strategy		2	Participation in commitment-based sustainable finance initiatives (BEI, Equator Principles, UNEPFI, etc.)
	3	Appointment, selection, training and re-election	<b>2) POLICIES</b> 	3	Public statements on principles and risk appetite and aspects of ESG
	4	Remuneration and appraisal		4	Sector-specific policies
<b>2) SHAREHOLDERS AND STAKEHOLDERS</b> 	5	Rights of shareholders	<b>3) PROCESSES</b> 	5	Processes for assessing ESG risks in client and transactional approvals
	6	Policies on stakeholder engagement and list of stakeholder groups engaged		6	Procedures for client monitoring and engagement
	7	Stakeholder reporting and communicating mechanisms	<b>4) PEOPLE</b> 	7	Responsibilities for ESG
<b>3) DISCLOSURE AND TRANSPARENCY</b> 	8	Release of reports and disclosure on ESG issues		8	E&S staff competency and performance evaluation
	9	Corporate website	<b>5) PRODUCTS</b> 	9	ESG integration in products and services
<b>4) AUDIT AND RISKS</b> 	10	General audit function and audit on sustainability	<b>6) PORTFOLIO</b> 	10	ESG risk assessment and mitigation at portfolio level
	11	Risk management frameworks and ESG-related risks		11	Disclosure of ESG risk exposure and targets

The indicators are created with reference to international frameworks, standards and initiatives such as G20/OECD Principles of Corporate Governance,<sup>58</sup> GRI Sustainability Reporting Guidelines,<sup>59</sup> the International Integrated Reporting Council (IIRC)'s International Integrated Reporting Framework,<sup>60</sup> TCFD and the Sustainability Accounting Standards Board (SASB),<sup>61</sup> as well as national principles and guidelines on corporate governance and sustainability reporting.

The indicators are used to highlight common areas of progress as well as identify areas where action needs to be undertaken across the banking industry. Disclosure against each indicator is assessed using 2-13 sub-indicators in the form of yes or no questions where we gave 1 for Yes answers or 0 for No answers. The results were aggregated and presented at the indicator level. The list of 108 sub-indicators is presented in Appendix 1. The overview of individual banks reviewed in each country is included in the respective country chapters at the indicator level.

On the ESG integration side, our assessment focused only on the governance of E&S issues; we did not look at how the banks assessed the corporate governance practices of their clients, as this is already a well-established practice via existing anti-money laundering and know your client (KYC) processes. We considered E&S topics that are most relevant to countries in Southeast Asia as well as the global agenda on SDGs.

The report does not consider the quality and strength of specific sector policies disclosed or the financial instruments designed. The former aspect will be included in future updates of this report as new tools to benchmark sector policies are under development.





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# CHAPTER 2

## REGIONAL RESEARCH FINDINGS

## REGULATORY SUMMARY

**We undertook research to identify commonalities in available regulatory frameworks that are relevant to ESG integration in the banking sector in six ASEAN countries.**

**This ESG regulatory framework includes:**

- Sustainable finance regulations, guidelines, roadmaps of central banks and banking associations
- Corporate governance codes, principles or manuals
- Sustainability reporting guidelines of stock exchanges/stock exchange commissions
- Listing rules of stock exchanges.

The table opposite provides an overview of the common elements found in ESG regulatory frameworks across all countries, organized around our six pillars of ESG integration. An overview of each individual country's regulatory framework can be found in the relevant country chapters.



**TABLE 3: COMMON ELEMENTS ACROSS REGIONAL SUSTAINABLE FINANCE REGULATIONS AND GUIDELINES - ALIGNMENT WITH SIX PILLARS OF ESG INTEGRATION**

CENTRAL BANK/BANKING ASSOCIATION REGULATIONS, GUIDELINES, ROADMAPS		ID	MY	PH	SG	TH	VN
<b>ELEMENTS PERTAINING TO BANKS</b>		OJK/ Perbanas	BNM/ ABM	BSP/ BAP	MAS/ ABS	BOT/ TBA	SBV/ VNBA
PURPOSE	Recommendations to consider indirect footprint of activities financed	●			●		●
POLICIES	Recommendations to develop E&S policies or sector-specific requirements	●			●		
POLICIES	Guidance on E&S requirements and/or sensitive sectors guidelines	●			●		
PROCESSES	Recommendations to establish E&S risk management process	●			●		●
PEOPLE	Recommendations for board responsibilities to include the oversight of E&S policies and strategy	●			●		
PEOPLE	Recommendations for capacity-building on E&S issues	●			●		
PEOPLE	CB / BA commitment / involvement to help build capacity	●			●		●
PRODUCTS	Recommendations to develop green products	●	●				●
PRODUCTS	CB is active in developing / facilitating green products	●	●		●		
PORTFOLIO	Recommendations to establish time-bound targets related to E&S risks	●					
PORTFOLIO	Banks required to disclose or report portfolio-level exposure to E&S risks						●
CORPORATE GOVERNANCE CODES/SUSTAINABILITY REPORTING GUIDELINES/ LISTING RULES		ID	MY	PH	SG	TH	VN
<b>ELEMENTS PERTAINING TO BANKS</b>		OJK/ NCG	BURSA MALAYSIA/ SC	PSE/ SEC	SGX/ MAS	SET/ SEC	HOSE/ SSC
PURPOSE	Rules / code clearly distinguish between indirect and direct E&S footprint		●		●		●
PURPOSE	Companies recommended to consider E&S issues	●	●	●	●	●	●
PURPOSE	Rules / code include sector-specific guidance for banks		●				
PURPOSE	Companies recommended to do stakeholder engagement on E&S issues		●	●	●	●	●
PURPOSE	Companies recommended to recognize communities among key stakeholders		●	●	●	●	●
POLICIES	Companies recommended to develop E&S policies		●	●	●	●	
PROCESSES	Companies recommended to establish E&S risk management		●	●	●		●
PEOPLE	Recommendations for board to consider E&S issues	●	●	●	●	●	●
PORTFOLIO	Companies recommended to set E&S risk exposure using targets		●	●	●		

# BANKS' CORPORATE GOVERNANCE AND ESG INTEGRATION PERFORMANCE

## CORPORATE GOVERNANCE

TABLE 4: CORPORATE GOVERNANCE RESULTS (AVERAGE PER INDICATOR FOR EACH COUNTRY)

CORPORATE GOVERNANCE ASPECTS AND INDICATORS		ID	MY	PH	SG	TH	VN	AVG
1) BOARD	1. Independence and qualification of the board							
	2. Clearly stated board's role and monitoring the implementation of corporate strategy							
	3. Appointment and selection, training and re-election							
	4. Remuneration and appraisal							
2) SHAREHOLDERS AND STAKEHOLDERS	5. Rights of shareholders							
	6. Policies on stakeholder engagement and list of stakeholder groups engaged							
	7. Stakeholder reporting and communicating mechanisms							
3) DISCLOSURE AND TRANSPARENCY	8. Release of reports and disclosure on ESG issues							
	9. Corporate website							
4) AUDIT AND RISKS	10. General audit function and audit on sustainability							
	11. Risk management frameworks and ESG-related risks							

## DISCUSSION: CORPORATE GOVERNANCE RESULTS

The following contains a brief discussion of the corporate governance results for 34 banks across four aspects and 11 indicators. The results are presented in relation to the differing regulatory frameworks and landscapes of countries.

### BOARD



Banks disclosed well on the board responsibilities indicator, which reflects the respective codes' emphasis on clearly delineating the board's roles and responsibilities in leading the company and supervising the corporate strategy, vision and mission. For instance, Singapore's Code of Corporate Governance outlines the board's role and responsibilities, which include providing "entrepreneurial leadership" and setting strategic objectives.

Disclosure on the board structure and appointment and selection was mixed across countries. For example, while the majority of the board of all three Singaporean banks is independent, only two banks each in Indonesia and Thailand disclosed the same, and none of the banks in Vietnam and the Philippines disclosed anything to this effect. Gender and ethnic diversity in the composition of boards was disclosed by all ASEAN banks with the exception of one bank in Vietnam and one in the Philippines.

Outside Vietnam, all ASEAN banks reviewed have remuneration committees. However, none of the terms of reference of these committees consider sustainability. Also, while the majority of the remuneration committee of all three Singaporean banks are independent, the same cannot be said for the other countries. Five banks each in Malaysia and Thailand and four in the Philippines disclosed that most of their committee members are independent, compared to only two banks in Indonesia and none in Vietnam.

### SHAREHOLDERS AND STAKEHOLDERS



All of the banks in all countries, except one in Vietnam, disclosed policies that ensure shareholders' rights to participate in and vote at general meetings. With the exception of Vietnam, all of the countries also disclosed well on stakeholder engagement and stakeholder communication.

The role and rights of stakeholders is held as a basic tenet in corporate governance. For example, 'The Rights of Shareholders and Key Ownership Functions', 'The Equitable Treatment of Shareholders' and 'The Role of Stakeholders' form half of the G20/OECD Principles of Corporate Governance. Consequently, most countries' corporate governance codes emphasize the management of relations and rights of shareholders; the lack of a governing code in Vietnam could explain why Vietnamese banks have disclosed the least on their stakeholder rights, engagement and communication strategies and measures. With the publication of a code for Vietnamese corporations scheduled in the near future, this is expected to improve.



## DISCLOSURE AND TRANSPARENCY



In general, banks reviewed disclosed the most on disclosure and transparency aspects. This relative strength may be due to the extensive regulations countries have covering these issues in their respective corporate governance codes. For instance, transparency is one of five general principles of Indonesia’s Code of Good Corporate Governance, while the Philippines’ Code of Corporate Governance for Publicly Listed Companies encourages companies to ensure that “*material and reportable non-financial and sustainability issues are disclosed*”.

Specifically, 33 banks make good disclosure of their corporate website and investor relations. However, seven banks – five of them from Vietnam – do not have a CSR/ ESG section on their website. All 34 ASEAN banks have disclosed their related party transactions and interested person transactions, with the exception of four banks in Malaysia; this could be because the Malaysian Code on Corporate Governance does not stipulate that corporations disclose such transactions.

Notably, all of the Singaporean, Malaysian, Thai and Indonesian banks assessed publish sustainability reports, along with five out of six in the Philippines and four out of five in Vietnam. This reflects a growing commitment to sustainability. However, only six banks mentioned responsible lending in their leadership statements, signifying that more progress can be made in the area of sustainable banking.

## AUDIT AND RISKS



All of the ASEAN banks studied, with the exception of one Philippine bank, disclosed their key risks as well as how these risks are assessed and managed. All 34 banks have also disclosed the existence of internal audit functions. This indicates that banks have generally adopted good audit and risk disclosure practices for financial-related risks.

However, while banks often disclose that they perform diligent audits and risk management, they did not disclose as much on E&S risks. Only 12 out of all 34 ASEAN banks have identified E&S risks in their risk management frameworks; the rest do not disclose review or assessment of E&S risks. Corporate governance regulations often do not adequately include and address E&S risks. ASEAN banks need to make progress here, particularly in light of the global consensus on the need for climate-related financial disclosures.

Overall, ASEAN banks generally performed well in their disclosure on corporate governance indicators. This corresponds to the presence of regulations and guidelines in the respective countries. However, banks do not adequately go beyond traditional corporate governance practices to incorporate and disclose E&S issues into their frameworks. This is particularly evident in how sustainability has not been considered in the drafting of terms of reference of nominating, remuneration and auditing committees in any of the six countries.

Specifically, the relative performance of banks across aspects tends to correlate with the emphasis or lack thereof in the respective countries’ corporate governance codes. Banks generally perform better on aspects where there are clear guidelines. As regulatory bodies in ASEAN begin to emphasize sustainability reporting and E&S assessment, ASEAN banks can be expected to boost their efforts in the disclosure of E&S-related matters, in addition to existing corporate governance practices.



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Access to clean water and sanitation is one of the Sustainable Development Goals. Water scarcity and pollution present as material risks for ASEAN banks.

## ESG INTEGRATION

TABLE 5: ESG INTEGRATION RESULTS (AVERAGE PER INDICATOR FOR EACH COUNTRY)

ESG INTEGRATION PILLARS AND INDICATORS		ID	MY	PH	SG	TH	VN	AVG
1) PURPOSE	1. Relevance of sustainability to the organization and its strategy for addressing sustainability							
	2. Participation in commitment-based sustainable finance initiatives (BEI, Equator Principles, UNEPFI, etc.)							
2) POLICIES	3. Public statements on principles and risk appetite and aspects of ESG and ESRM							
	4. Sector-specific policies							
3) PROCESSES	5. Process for assessing ESG risks in client and transactional approvals							
	6. Procedures for client monitoring and engagement							
4) PEOPLE	7. Responsibilities for ESG							
	8. E&S staff competency and performance evaluation							
5) PRODUCTS	9. ESG integration in products and services							
6) PORTFOLIO	10. ESG risk assessment and mitigation at portfolio level							
	11. Disclosure of ESG risk exposure and targets							

## DISCUSSION: ESG INTEGRATION RESULTS

**The discussion below looks at disclosure by banks against the 11 indicators behind the six pillars of ESG integration. It presents the disclosure by banks with reference to existing ESG regulatory frameworks.**

### PURPOSE



Sustainability needs to be recognized as one of the key factors influencing long-term growth and factored into business strategy. While 26 out of 34 banks refer to sustainability in their core business strategies, only six mentioned responsible lending in their leadership statement, suggesting a lack of strategic focus and leadership on sustainability. While 21 banks disclosed that they differentiate between direct and indirect footprints, only 14 banks disclosed material E&S issues that impact their businesses and stakeholders. These gaps can be explained by the fact that although corporate governance codes require or recommend banks to consider E&S issues, they do not provide guidance to banks on how to deal with indirect E&S risks in their portfolios. Banking associations and/or regulators need to step in with sustainable banking guidelines.

Although 23 banks listed local communities among key stakeholders, only eight disclosed stakeholder engagement on E&S impacts of financial services. It was not clear if banks consider local communities to mean the neighbourhoods to which they provide banking services rather than the local communities impacted by the client operations they finance. Corporate governance frameworks, listing rules and sustainability reporting guidelines in most countries identify local communities as key stakeholders and stipulate that stakeholder engagement must include sustainability issues. Some banks interpret this to be about CSR activities or financial inclusion. The inclusion of civil society as a key stakeholder is notably lacking, which means that banks have limited insights into how the activities that they finance impact local communities and the environment.

With all countries committed to mitigating climate change and achieving SDGs on the national level, just 12 banks disclosed that they acknowledge climate change risk and nine referenced SDGs. None of the analysed ASEAN regulatory frameworks specifically require banks to assess and disclose climate change risks.

Furthermore, only one bank disclosed participation in a commitment-based initiative to deal with sustainable finance issues. Seven banks (four from Indonesia) reported on discussions with regulators to build capacity in sustainable finance topics.



## POLICIES



Banks which distinguish between direct and indirect footprints have not yet translated this understanding into policies to indicate their position on key E&S issues. Banks are not yet transparent about what risks they deem most pertinent to their business, including the client businesses they finance. All banks from Singapore disclosed that they recognize biodiversity loss and/or deforestation risks in their clients' activities. Five banks (three from Thailand) recognized human rights risks, while one Malaysian bank considered water shortage in its risk management approach and one Singapore bank recognized water pollution as a risk in its clients' activities. Only four banks disclosed specific E&S requirements for their clients, with two using exclusion lists. Eleven other banks with exclusion lists do not state specific activities they will not finance, making general statements that they would not finance activities that are environmentally unsustainable, without stating the criteria or standard for sustainability. None of the banks disclosed an exclusion of new coal-fired plants and coal mines, nor any requirement for high-risk clients to do water risk assessment and commit to water stewardship. Only one bank stated that it will not finance clients with operations in World Heritage Sites.

Existing sustainable finance regulations do not require banks to lay out minimum E&S requirements which clients must meet within an agreed timeframe. Furthermore, even though corporate governance codes require or recommend companies to set E&S policies, banks interpret this to be about their own footprint. By contrast, international frameworks, such as TCFD and UNGP, stress the importance of the financial sector recognizing and managing specific indirect E&S risks.

Although some sectors have higher E&S risks and require separate policies to manage them, only three banks disclosed that they have specific policies or requirements for sensitive sectors. None of the banks reviewed disclosed all their sector policies, resulting in limited visibility with reference to internationally accepted standards in E&S risk mitigation. In Singapore and Indonesia, financial regulators/banking associations recommended that banks develop sector-specific requirements or published guidelines for certain sectors. There is thus greater disclosure by banks in those countries which either have or have committed to create sector-specific requirements or policies.

## PROCESSES



Across the 21 banks which recognize their indirect footprint, 15 disclosed that they incorporate E&S factors when evaluating clients and transactions, while 11 disclosed that credit decisions are impacted by such E&S assessments. However, in the absence of disclosure of the actual E&S policies, it is not clear against which criteria clients are assessed. Only one bank disclosed that it considers the track record of clients in relation to sustainability. Banks did not elaborate on their client and transaction approval processes, with only four banks disclosing escalation procedures for controversial cases and five banks disclosing they classify clients based on E&S assessments.

Banks are not disclosing any engagement with their clients to influence their E&S performance, with only one saying it develops E&S risk management action plans with high- and medium-risk clients. Seven banks (four from Indonesia) disclosed the use of periodic E&S reviews as part of their processes to ensure that they have updates on clients' E&S risk levels throughout the lifetime of the loan. Only two banks disclosed how they deal with non-compliance cases, so it is not clear if banks are ready to exit the relationship with the client if their performance does not improve.

The sustainable finance regulations analysed require or recommend banks to have E&S risk management processes but they do not elaborate on what constitutes a sound E&S risk management framework. It is noteworthy that E&S risk management is highlighted by corporate regulatory frameworks in four analysed countries.



## PEOPLE



Although corporate regulatory frameworks in all countries highlight (though do not necessarily mandate) the responsibility of the boards to consider E&S issues, only 10 banks have senior management oversight of E&S issues in their financing activities. Only one bank stated that the board oversees climate change risk. Insufficient board and senior management oversight can explain why ESG integration has not been fully implemented. In addition, banks are not transparent on whether ESG responsibilities are distributed across the organization to relevant functions. For example, no banks stated that ESG responsibilities are assigned to the bank's three lines of defence.

Not all the banks that have partially embodied E&S factors into policies and processes disclosed that they train staff on E&S issues and/or have dedicated staff for ESG integration. Only one bank said it links ESG performance to staff appraisal processes. On the senior management level, only two banks disclosed capacity-building of senior managers to drive ESG integration from the top.

In three countries, banking regulators or banking associations have committed to help build capacity in ESG integration via workshops and guidance. In addition, some NGOs are able to offer deep insights into E&S issues and best management practices. Banks should make full use of these supporting initiatives.

## PRODUCTS



Banks in ASEAN are starting to grasp opportunities created by the transition to sustainable economies, with 17 banks disclosing that they have specific products and services, albeit mainly for renewable energy and energy efficiency. Some of these banks have responded to regulatory support to develop sustainable products. However, only five banks disclosed that they integrate E&S factors into capital allocation decisions, indicating that E&S issues are not yet mainstreamed into strategic portfolio management. For these banks, the loan volumes to targeted sustainable activities amount to a single digit percentage based on the total loan portfolio. Only 11 banks disclosed that they have training on ESG and one bank disclosed that it has dedicated staff or expertise on ESG matters, suggesting a lack of capacity to develop sustainable products on a greater scale. Furthermore, among the 17 banks which have sustainable products, five do not have E&S risk assessment processes in place. This suggests that banks are missing the balance between risks and opportunities and may be fuelling the problem even while offering some solutions – for example lending to dirty coal mines while offering renewable energy financing products. Banks also do not yet tap into opportunities to develop deeper relationships with clients, as none use E&S as a topic for client outreach events.

## PORTFOLIO



Among ASEAN banks, portfolio management of E&S risks is at the nascent stage with banks rarely going beyond disclosing sector-based loan exposures. Only two banks provided information on the composition of their energy loan portfolio; as such there is very limited visibility into climate change risk across the ASEAN banking sector, particularly when we consider that other sectors such as transport, real estate and agriculture are also highly vulnerable to climate change risks. Only two banks disclosed their aggregated client/transaction E&S assessment results, but this was limited to a specific sector or project finance.

There was no disclosure at all regarding the proportion of relevant sector clients or loans in the portfolio covered by E&S commitments, such as no deforestation and no exploitation, or working toward sustainability certification. Furthermore, banks did not disclose time-bound targets to reduce overall exposure in certain E&S risky sectors or with high-carbon-emitting clients.

So far there is limited emphasis on managing indirect E&S risks at the portfolio level in ASEAN sustainable finance regulations. The State Bank of Vietnam does mandate banks to report (to itself, not publicly) on selected portfolio-level E&S risk metrics such as the number of transactions screened for E&S risks, but does not require banks to commit to time-bound targets to reduce E&S risks in their lending portfolio.

JUST  
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**Results indicate** that there is some progress on disclosure against ESG integration indicators in ASEAN banks with the support of existing ESG regulatory frameworks. Banks are increasingly demonstrating understanding that their E&S footprint lies also with their clients' E&S performance and that sustainability is essential for their business. Equally, there is increasing pressure from stakeholders such as civil society and investors demanding more transparency and accountability from banks. Analysis shows that financial regulators in ASEAN are also following suit by providing guidelines to spur ESG integration.

Given the urgency of solving pressing E&S issues, ASEAN banks need to act upon their commitments to sustainability and translate this into the fundamentals of their businesses: purpose, policies, processes, people, products and portfolio. Those banks which do not yet fully appreciate the importance of sustainability need to catch up fast with their local and regional peers to ensure they have a viable business model that contributes to sustainable development.





# CHAPTER 3

INDONESIA

## NATIONAL CLIMATE CHANGE AND SUSTAINABLE DEVELOPMENT GOALS

**As a G20 member, Indonesia has announced commitments to unconditional GHG emissions reduction targets of 26 per cent by 2020 and 29 per cent by 2030 through its own efforts, and 41 per cent by 2030 with international help.<sup>62</sup> Indonesia bases 60 per cent of its emissions reduction on agriculture, forestry and other land use.<sup>63</sup>**

Its climate change pledge, or Intended Nationally Determined Contribution (INDC), builds upon the government's commitment to achieve SDGs to ensure aspects such as food security, sustainable management of forests, oceans and water, biodiversity loss and other problematic areas are addressed.<sup>64</sup> The INDC lays out priority actions to achieve such outcomes and integrate them in the National Medium Term Development Plan 2020. This vision has already been reflected in the National Medium Term Development Plan 2015-2019 (RPJMN 2015-2019)<sup>65</sup> which sets national targets for water security, GHG emissions reduction, and forest and marine conservation. Indonesia also aspires to increase renewable energy to 23 per cent of primary energy supply by 2025, as dictated by the 2014 National Energy Policy.<sup>66</sup>





# SUPPORTING REGULATORY FRAMEWORK PERTAINING TO SUSTAINABLE BANKING

## BANKING REGULATIONS AND BANKING ASSOCIATION GUIDELINES

**Starting in 1998, Bank Indonesia encouraged banks to assign greater importance to analysing the environmental impact assessment of large or high-risk clients.<sup>67</sup>**

This was followed up in 2012 with the introduction of Asset Quality Ratings for commercial banks, requiring them to include the “*efforts undertaken by the debtor in the framework of environment conservation*”<sup>68</sup> in their assessment of the debtor’s business prospects. Moreover, Bank Indonesia has encouraged banks to consider the results from the Program for Pollution Control, Evaluation and Rating (PROPER) environmental reporting initiative by the Ministry of Environment, which assesses companies on their compliance with environmental regulations.<sup>69</sup> In 2015 The Ministry of Finance established the Indonesian Oil Palm Estate Fund pledging Rp 4.5 trillion (US\$336 million) to revitalize aging smallholders’ oil palm plantations. The Fund cooperates with the Ministry of Agriculture and local banks (including Bank Mandiri and Bank Negara Indonesia) to supervise recipients’ utilization of government funds.<sup>70</sup>

In a significant further step to find sustainable solutions for economic development as well as to solve climate-change-related problems, the Indonesian Financial Services Authority (OJK) working with the Ministry of Environment and the support of IFC and the Sustainable Banking Network<sup>71</sup> launched the *Roadmap for Sustainable Finance* in Indonesia.<sup>72</sup> The roadmap introduces a comprehensive rollout of the sustainable finance programme for the mid-term (2015-2019) and long-term period (2015-2024). It serves as a “*reference for OJK and the financial services industry as well as other parties who have an interest in supporting sustainable development*”. The roadmap specifies four principles of sustainable finance which are integral to stimulating a transition toward a competitive low-carbon economy and promoting green investments in various business sectors.<sup>73</sup>

### **The principles comprise:**

- i) Integration of E&S factors in financial service institutions’ (FSIs) risk management to avoid negative impacts of their business activities;
- ii) Creating financial inclusivity by increasing financial activities in the priority economic sectors (industry, energy, agriculture, infrastructure, and micro, small and medium enterprises) and allocating financial services to those with limited or no access to the formal financial sector;
- iii) Promoting transparency and alignment of ESG practices by FSIs through periodic reporting of the progress of applying sustainable finance principles; and
- iv) Enhancing the capacity of FSIs to implement sustainable finance principles as well as facilitating multi-stakeholder cooperation between key stakeholders like FSIs, regulators, government and international partners to promote sustainable finance.<sup>74</sup>

The roadmap lays out targets for OJK to come up with requirements and incentives for the Indonesian financial sector in relation to all of these principles, such as mandatory sustainability reporting, regulations in risk management, and increased supply of sustainable finance products.



OJK is keen to see an increase in the volume of sustainable finance products such as green bonds and green indices, and it is expected to launch a framework and regulation for green bonds in 2017.<sup>75</sup> Other future plans include developing a green lending model for all priority sectors.<sup>76</sup> OJK released a handbook on clean energy in 2014 to increase FSIs' understanding of clean energy and their willingness to invest in clean energy projects.<sup>77</sup> It also developed the Guidelines for Sustainable Palm Oil Financing in collaboration with WWF in early 2017 to facilitate FSIs in incorporating relevant E&S aspects into their palm oil sector policies.<sup>78</sup> In August 2017 OJK issued a new regulation on sustainable finance mandating financial institutions to develop short- and medium-term Sustainable Finance Action Plans with time-bound targets between one and five years.<sup>79</sup> The action plans will cover three areas of focus, namely i) the development of sustainable finance products and services, ii) internal capacity building on E&S integration, and iii) updated E&S risk management procedures. Financial institutions are required to disclose their targets and progress in yearly sustainability reports to be submitted to OJK together with the bank's annual report. The regulation will take effect starting from January 2019.

In 2016, with the support of WWF-Indonesia and eight Indonesian banks representing 46 percent of total national banking assets, OJK launched a pilot project named *'First steps to be a sustainable bank'* to support banks in meeting their targets on building internal capacity for better E&S risk management and governance as laid out in the roadmap.

## CORPORATE GOVERNANCE FRAMEWORK, LISTING RULES AND SUSTAINABILITY REPORTING GUIDELINES

In 2006 the National Committee on Governance of Indonesia published the Code of Good Corporate Governance, providing guidelines for companies on a voluntary basis.<sup>80</sup> One of its purposes is to *"stimulate the company's awareness of social responsibilities in particular the environmental and societal interests of the communities in which a company operates"*. Additionally, it recommends companies engage in *"appropriate planning and implementation to address E&S issues"*. In particular, it illustrates the social responsibility that the board should take and policies that a company should consider in terms of community and users of products and services.

In the Indonesian Law on Limited Liability Company No. 40 of 2007, all listed companies should disclose how they implement the commitment to participate in sustainable economic development (Social and Environmental Responsibility) in their annual report.<sup>81</sup> But only companies having operations that involve natural resources are obliged to responsibly manage the E&S impact of their economic activities; companies failing to do so will be subject to administrative sanctions including written warnings and restrictions or suspension of business activities.<sup>82</sup> In 2012, OJK regulation KEP-431/BL/2012 further specified the obligation for all public companies to conduct and disclose CSR initiatives.<sup>83</sup> The regulation refers to a comprehensive definition of CSR as *"the commitment of businesses to behave ethically and to contribute to sustainable economic development by working with all relevant stakeholders"*.<sup>84</sup> OJK regulations KEP-431/BL/2012 and No. 8/POJK.04/2015 mandate full disclosure of these activities in both the company's annual reports and website.<sup>85</sup>

In a cooperation between IDX and the Indonesian Biodiversity Foundation, the KEHATI-SRX Index was formed. This sustainability-related index is expected to provide additional information to investors who wish to invest in listed companies that are well aware of environmental issues and score high on corporate governance.<sup>86</sup>

# CORPORATE GOVERNANCE DISCLOSURE RESULTS

**TABLE 6: INDONESIA CORPORATE GOVERNANCE DISCLOSURE RESULTS**

CORPORATE GOVERNANCE ASPECTS AND INDICATORS		BCA	MANDIRI	BNI	PANIN	PERMATA	BRI	VICTORIA	AVG
1) BOARD	1. Independence and qualification of the board								
	2. Clearly stated board's role and monitoring the implementation of corporate strategy								
	3. Appointment and selection, training and re-election								
	4. Remuneration and appraisal								
2) SHAREHOLDERS AND STAKEHOLDERS	5. Rights of shareholders								
	6. Policies on stakeholders engagement and list of stakeholders groups engaged								
	7. Stakeholder reporting and communicating mechanisms								
3) DISCLOSURE AND TRANSPARENCY	8. Release of reports and disclosure on ESG issues								
	9. Corporate website								
4) AUDIT AND RISKS	10. General audit function and audit on sustainability								
	11. Risk management frameworks and ESG-related risks								

### BOARD



All the banks have disclosed their board's roles and responsibilities, with four of the banks' boards monitoring the implementation of the corporate strategies. However, only one Indonesian bank stipulated a maximum term limit for independent directors and only two banks disclosed the periodic re-election of directors. The Corporate Governance Task Force of OJK has recognized these gaps in its 2014 Corporate Governance Roadmap<sup>87</sup> and has recommended regulators set provisions and require companies' adherence on a 'comply or explain' basis.

### SHAREHOLDERS AND STAKEHOLDERS



All banks disclosed policies to ensure rights of minority shareholders and five banks disclosed policies to engage with their stakeholders. In addition, Indonesian banks have demonstrated strong shareholder communication, where all of the banks allow shareholders to raise concerns on the resolutions for discussion and voting. Three banks disclosed measures to understand the views of various stakeholders. The emphasis on shareholders' rights and long-term shareholder value in Indonesia's 2014 Code of Corporate Governance Manual<sup>88</sup> may have encouraged the banks to facilitate these good practices.

### DISCLOSURE AND TRANSPARENCY



Transparency is one of the five main principles in Indonesia's Code of Good Corporate Governance, which emphasizes providing material and relevant information that is accessible to stakeholders for decision-making. All banks have disclosed information such as their corporate and ownership structures, as well as their related party transactions. Moreover, all banks have sustainability reporting. However, only one bank has disclosed responsible lending in its leadership statement. Reporting of CSR activities for businesses related to natural resources has been compulsory since 2007, and required for all public companies since 2012. Disclosure should include both the company's website and annual report.<sup>89</sup>

### AUDIT AND RISKS



All of the banks have disclosed on separate internal audit functions, key risks and how they are assessed and managed, and frameworks to evaluate and improve their risk management. But still two banks did not have an audit committee where the majority of its directors are independent. In terms of E&S-related auditing and risks, three of the banks have identified ESG-related risks and only one conducted periodic reviews of its E&S policies and procedures. This is reflective of the current lack of guidance and regulation on disclosing sustainability performance, which has resulted in the banks' lack of incorporation of E&S factors into their audit and risk frameworks.





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Collecting palm fruit at an RSPO-certified plantation in Sumatra, Indonesia. Credible certification can help banks manage E&S issues in high-risk sectors.

# ESG INTEGRATION DISCLOSURE RESULTS

TABLE 7 : INDONESIA ESG INTEGRATION DISCLOSURE RESULTS

ESG INTEGRATION PILLARS AND INDICATORS		BCA	MANDIRI	BNI	PANIN	PERMATA	BRI	VICTORIA	AVG
1) PURPOSE	1. Relevance of sustainability to the organization and its strategy for addressing sustainability								
	2. Participation in commitment-based sustainable finance initiatives (BEI, Equator Principles, UNEPFI, etc.)								
2) POLICIES	3. Public statements on principles and risk appetite and aspects of ESG and ESRM								
	4. Sector-specific policies								
3) PROCESSES	5. Process for assessing ESG risks in client and transactional approvals								
	6. Procedures for client monitoring and engagement								
4) PEOPLE	7. Responsibilities for ESG								
	8. E&S staff competency and performance evaluation								
5) PRODUCTS	9. ESG integration in products and services								
6) PORTFOLIO	10. ESG risk assessment and mitigation at portfolio level								
	11. Disclosure of ESG risk exposure and targets								



## PURPOSE



Five Indonesian banks made reference to sustainability in their strategy and vision. However, only four banks clearly distinguish between direct and indirect footprint concepts. These four banks subscribed to the OJK roadmap's efforts to improve transparency by providing information on their E&S aspirations and commitments toward playing a role in sustainable development and becoming 'sustainable banks'. They disclosed engagement efforts with OJK to lead the financial sector's transition to greater sustainability; however, only one bank disclosed participation in UNEP Finance Initiative. Two banks disclosed an alignment of their vision of sustainability with the SDGs and three recognized climate change risk. Although five banks listed local communities among stakeholders, only two disclosed E&S engagement efforts.

## POLICIES



Consideration of ESG risks is aligned with the Indonesia Corporate Governance Manual from 2014 (CGM 2014), which states that companies should consider environmental risk within "*material foreseeable risk factors*".<sup>90</sup> So far only two banks have specified that they commit to avoid financing of activities causing negative E&S impact; however, they did not disclose the impact threshold nor list the activities. In terms of embedding E&S commitments into sector policies, only two banks disclosed they have palm oil policies. Although the actual policies were not disclosed, the two banks referenced international E&S standards such as RSPO to enhance the sustainability of client operations. Disclosing E&S policies will further align Indonesian banks toward CGM 2014, which calls for banks to "*consider disclosing [...] environmental policies, and the internal regulations for the Board of Commissioners and its committees amongst others*".<sup>91</sup>

## PROCESSES



Four banks disclosed the use of results of national environmental management performance ratings, such as AMDAL and PROPER, and commitments to only work with clients above certain E&S risk thresholds set by the banks. Currently banks apply this requirement only for clients where such national ratings are available and did not disclose any internal risk classification frameworks that apply to all clients. Banks did not disclose if they factor in assessment of capacity, commitment and track record and if there are escalation mechanisms to deal with controversial transactions. Four banks mentioned that they perform periodic reviews of their client's profile on E&S, but further insights into client monitoring and engagement processes were not provided. In the long term (2019-2024) OJK expects banks to achieve "*strengthening of risk management and corporate governance in environmental and social aspects*", as well as provide reports on their progress. Therefore, banks should consider developing comprehensive E&S risk management frameworks which go beyond minimum national environmental ratings and extend into engagement activities for clients to close E&S performance gaps.

## PEOPLE



Indonesian banks can further benefit from increasing transparency over the governance structures to support E&S processes. Two banks disclosed that oversight of E&S policies is included in senior management responsibilities. Four banks disclosed information on E&S training for their staff which aligns with OJK's emphasis on the importance of capacity-building. As the four largest banks are all participating in the OJK-led pilot programme with WWF, the foundation has been laid for more widespread internal training.

### PRODUCTS

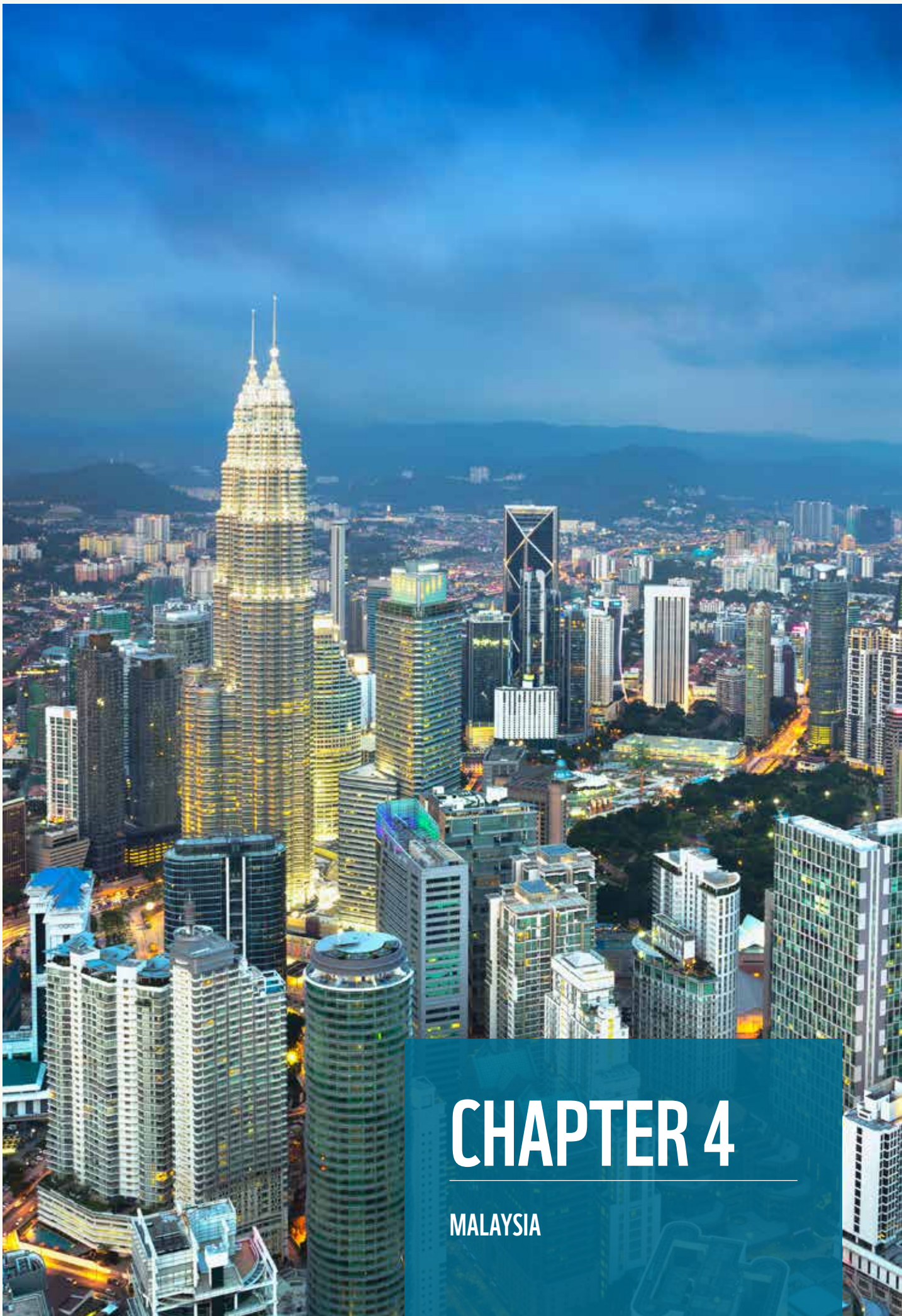


Banks are responding to OJK's call to action to *"increase the volume of sustainable financing in the priority economic sectors [agriculture in the broadest sense, manufacturing, infrastructure, SMEs and energy]"*. Four banks have developed a range of products or services to facilitate renewable energy and energy efficiency, and two of these four banks mentioned products for sustainable agriculture. Three banks also quantified the amount of capital allocated toward green products. More substantiated disclosure will enable stakeholders to understand which priority sectors receive access to green products. Banks did not disclose the use of E&S as a topic of client outreach activities.

### PORTFOLIO



All banks disclosed their loan exposures by sector. One bank disclosed the percentage of palm oil clients that have sustainability certifications as well as the composition of loans disbursed according to the PROPER ratings based on the assessment results. However, since PROPER rating is not available for all companies in Indonesia such rated clients comprise single-digit percentages of the loans portfolio. Two banks disclosed the number of clients that are RSPO or ISPO<sup>92</sup> certified, however, since banks did not disclose their sector policies, it is not clear if certification is a mandatory policy requirement. In general, the banks have not provided more detailed disclosures on overall exposure to E&S risks such as sub-sectoral breakdown of energy portfolio, carbon intensity, or percentage of portfolio aligning with E&S commitments; nor did they disclose commitments to portfolio-level E&S related targets.



# CHAPTER 4

MALAYSIA



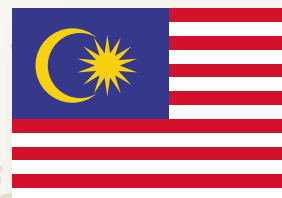
## NATIONAL CLIMATE CHANGE AND SUSTAINABLE DEVELOPMENT GOALS

**To be equipped for future economic challenges and climate-related risks, Malaysia has adopted a green growth strategy and rolled out key initiatives to create a stable and resilient economy. The government aims for the country to become an advanced economy through “a resilient, low-carbon, resource-efficient and socially-inclusive” route under the 11th Malaysian Plan (11MP) slated for 2016-2020.<sup>93</sup>**

Malaysia has committed to support and implement the SDGs, integrating them into its planning framework.<sup>94</sup> The green growth strategy encapsulated in the 11MP marks a paradigm shift in how Malaysia regards the role of natural resources and the environment in its pursuit of socio-economic development. It pinpoints the establishment of sustainable financial mechanisms as an enabling factor,<sup>95</sup> next to others such as creating green markets and ensuring natural resource security. The 11MP is also used as a roadmap to achieve the country’s target of reducing the GHG emissions intensity of GDP by 45 per cent by 2030.<sup>96</sup> This consists of a 35 per cent reduction on an unconditional basis and a further 10 per cent reduction conditional upon receipt of climate finance, technology transfer and capacity-building from developed countries.

This national focus on sustainability began in 2010, when the Malaysian government introduced its New Economic Model (NEM), which is an important constituent of the government’s 2020 vision to transform the country into a high-income economy.<sup>97</sup> Sustainability forms one of the core goals of the NEM, which serves to ensure that all proposed measures defined in the NEM must be economically and environmentally sustainable. The NEM comprises eight Strategic Reform Initiatives, the last of which is sustainable growth. This last initiative includes sub-policy goals to boost green investments by facilitating bank lending and financing. The following measures are recommended: (i) developing banking capacity to assess credit approvals for green investment, (ii) liberalizing entry of foreign experts who specialize in financial analysis of the viability of green technology projects, and (iii) supporting green technology investment.<sup>98</sup>

### MALAYSIA



# SUPPORTING REGULATORY FRAMEWORK PERTAINING TO SUSTAINABLE BANKING

## BANKING REGULATIONS AND BANKING ASSOCIATION GUIDELINES

**The Green Technology Financing Scheme (GTFS) previously established by the central bank Bank Negara Malaysia (BNM) in cooperation with the Ministry of Finance and the Ministry of Energy, Green Technology and Water has been extended to 2022 after the government approved a RM5 billion (US\$1.16 billion) allocation for the next phase.<sup>99</sup> The fund aims to help viable and innovative green technology companies meet the E&S criteria set by the fund to access financing.<sup>100</sup> As of August 2016, 26 financial institutions have participated in the scheme,<sup>101</sup> which reduces the risks they bear through a government guarantee covering 60 per cent of the loan amount.<sup>102</sup> Close to RM3 billion has been granted for GTFS projects as of March 2017.<sup>103</sup>**

Previously, BNM issued a policy for 2015-2016 on financing priority sectors, which aimed to promote growth in SMEs as well as other new SME sub-sectors.<sup>104</sup> These include areas such as green technology. Banks were required to submit their financing targets for priority sectors, followed by quarterly submission of the amount of loans provided and rejected.

Furthermore, the Securities Commission Malaysia launched a Sustainable and Responsible Investment (SRI) Sukuk framework in August 2014 in response to growing concerns over the E&S impacts of businesses.<sup>105</sup> The framework provides guidelines for issuers to ensure SRI Sukuk are utilized to fund eligible SRI projects that fulfil these conditions: a) Preserve and protect the environment and natural resources; (b) Conserve the use of energy; (c) Promote the use of renewable energy; (d) Reduce greenhouse gas emissions; or (e) Improve the quality of life for the society.<sup>106</sup> Issuers need to disclose how they will fulfil at least one of these conditions and state that they comply with relevant ESG standards or recognized best practices.

At present, there is no regulation or mandate on sustainable or green finance. For instance, the guidelines for “responsible financing” issued in 2011 by BNM do not include ESG factors<sup>107</sup> as the interpretation of “responsible” was limited to preventing excessive lending to borrowers rather than requiring mitigation of negative E&S impacts of client activities. There are regulations based on Sharia law to govern Islamic finance, which has elements of environmentally and socially responsible financing. However Islamic finance is not equivalent to ESG integration, which has a more comprehensive scope and applies across the entire banking portfolio.



## CORPORATE GOVERNANCE FRAMEWORK, LISTING RULES AND SUSTAINABILITY REPORTING GUIDELINES

In 2017, the Securities Commission released the new Malaysian Code on Corporate Governance (MCCG) which emphasizes internalizing good corporate governance culture amongst listed firms.<sup>108</sup> With a view to reducing the problem of companies being mechanical about their corporate governance practices, MCCG 2017 requires companies to disclose on an ‘apply or explain an alternative’ basis.<sup>109</sup> Moreover, the Code broadened the board’s responsibility by clearly specifying how the board should include strategies on ESG issues supporting sustainability.<sup>110</sup> As part of the new MCCG, 100 Malaysian companies are called upon to move towards integrated reporting by 2019.

Under the 2015 Sustainability Amendments by Malaysia stock exchange Bursa Malaysia,<sup>111</sup> it is mandatory for issuers to disclose a narrative statement of their management of material economic, environmental and social risks. This replaces a simpler statement on their CSR practices in their annual report, which was the previous requirement.<sup>112</sup> The Sustainability Amendments will take effect on a staggered basis over the period 31 Dec 2016 to 31 Dec 2018.<sup>113</sup> To support listed issuers in integrating sustainability into their organizations, Bursa Malaysia issued a Sustainability Reporting Guide<sup>114</sup> and Sustainability Reporting Toolkit.<sup>115</sup> Compliance is on a voluntary basis, even though companies are strongly encouraged to follow the Guide as best practice. The guidelines recommend that companies promptly assess E&S risks that could affect their business by incorporating these factors into their risk framework.<sup>116</sup> In particular, they warn that financial institutions “*could be exposed to credit risks as a result of economic, environmental and social issues such as a long term impact like climate change effects [...] faced by their clients*”. The Guide refers financial institutions to *GRI Sector Disclosures: Financial services*<sup>117</sup> for more guidance on product and services responsibility, emphasizing the importance of considering indirect E&S impacts. In order to ease the transition of listed companies into adopting the new sustainability framework, Bursa Malaysia is offering ESG-related training for company directors and senior management.<sup>118</sup>

In 2014, Bursa Malaysia launched an ESG index in cooperation with the FTSE known as FTSE4Good Bursa Malaysia Index for Malaysian companies.<sup>119</sup> The Index recognizes listed companies and banks from the top 200 Malaysian stocks that meet a variety of ESG inclusion criteria. The criteria are in line with international disclosure frameworks such as the GRI and CDP. In December 2016, the Index had 42 constituents, of which eight belonged to the finance sector. However, it is important to note that the criteria only assess the companies and banks on how they manage their direct ESG impact.

## CORPORATE GOVERNANCE DISCLOSURE RESULTS

TABLE 8: MALAYSIA CORPORATE GOVERNANCE DISCLOSURE RESULTS

CORPORATE GOVERNANCE ASPECTS AND INDICATORS		AMBANK	CIMB	HONG LEONG	MAYBANK	PUBLIC BANK	RHB	AVG
1) BOARD	1. Independence and qualification of the board							
	2. Clearly stated board's role and monitoring the implementation of corporate strategy							
	3. Appointment and selection, training and re-election							
	4. Remuneration and appraisal							
2) SHAREHOLDERS AND STAKEHOLDERS	5. Rights of shareholders							
	6. Policies on stakeholders engagement and list of stakeholders groups engaged							
	7. Stakeholder reporting and communicating mechanisms							
3) DISCLOSURE AND TRANSPARENCY	8. Release of reports and disclosure on ESG issues							
	9. Corporate website							
4) AUDIT AND RISKS	10. General audit function and audit on sustainability							
	11. Risk management frameworks and ESG-related risks							

## BOARD



While all six Malaysian banks have disclosed gender and/or ethnic diversity as well as provision of training for board members, three banks also disclosed that the board monitors the implementation of corporate strategy, vision and mission. Nonetheless, the Code recommends that boards review and monitor the implementation of management’s proposals as well as considering E&S issues supporting sustainability in their strategy formulation.<sup>120</sup> This underlines the emphasis that the Code has on the board aspect and on sustainability.

## SHAREHOLDERS AND STAKEHOLDERS



All banks acknowledged and disclosed safeguards for their shareholders’ right to participate in and vote at general meetings. Five of the banks disclosed policies to ensure the rights of minority shareholders and that voting is carried out by poll. This is in line with the Code, which encourages the board to take action in facilitating greater shareholder participation during general meetings and to consider electronic voting in place of traditional means so as to make voting more accessible.<sup>121</sup> Four of the banks disclosed the list of stakeholders engaged, and five disclosed policies to engage with stakeholders and measures to understand their views. The apparent strength in communication with stakeholders is reflected in the Code, which includes the intended outcome of constant communication with stakeholders to facilitate understanding of each other’s aims and expectations, including “*policies on governance, the environment and social responsibility*”.<sup>122</sup>

## DISCLOSURE AND TRANSPARENCY



In general, the varying levels of disclosure mirror the relative significance given to these various indicators in the MCCG. For example, ownership structure is mentioned in the MCCG but related party transactions (RPTs) and interested person transactions (IPTs) are not. Our results show that all six banks made disclosure on the ownership structure, but only two out of six banks disclosed on RPTs and IPTs. Similarly only one bank mentioned responsible lending in the leadership statements even though all banks have published sustainability reports. While Bursa Malaysia’s Sustainability Reporting Guide includes recommendations to consider product and services responsibility for financial institutions, Malaysian banks may still be in the process of complying with the guidelines.

## AUDIT AND RISKS



For all the E&S-related auditing questions, such as identification of ESG-related risks and auditing of E&S policies, no more than one bank disclosed relevant information. However, all six banks disclosed relating to traditional corporate governance auditing and risk matters, such as how the majority of their audit committee directors are independent and having policies to evaluate and improve risk management. In this instance, while guidelines relating to audit committees are clearly outlined in the Code, guidelines relating to sustainability, especially the auditing of ESG risks, are absent.

## ESG INTEGRATION DISCLOSURE RESULTS

TABLE 9: MALAYSIA ESG INTEGRATION DISCLOSURE RESULTS

ESG INTEGRATION PILLARS AND INDICATORS		AMBANK	CIMB	HONG LEONG	MAYBANK	PUBLIC BANK	RHB	AVG
1) PURPOSE	1. Relevance of sustainability to the organization and its strategy for addressing sustainability							
	2. Participation in commitment-based sustainable finance initiatives (BEI, Equator Principles, UNEPFI, etc.)							
2) POLICIES	3. Public statements on principles and risk appetite and aspects of ESG and ESRM							
	4. Sector-specific policies							
3) PROCESSES	5. Process for assessing ESG risks in client and transactional approvals							
	6. Procedures for client monitoring and engagement							
4) PEOPLE	7. Responsibilities for ESG							
	8. E&S staff competency and performance evaluation							
5) PRODUCTS	9. ESG integration in products and services							
6) PORTFOLIO	10. ESG risk assessment and mitigation at portfolio level							
	11. Disclosure of ESG risk exposure and targets							

PURPOSE



Five banks have included clear references to sustainability in their strategy; four banks also acknowledged a difference between direct and indirect E&S footprint. Aligned with the MCCG 2017 view that corporate governance “requires balancing the needs of other stakeholders such as [...] society and communities”, five banks listed communities among stakeholders, although only one bank engages with stakeholders to understand the impacts of its financing activities on stakeholders. Only two banks disclosed E&S issues in their materiality analysis. Banks can refer to Bursa Malaysia’s Sustainability Reporting Toolkit,<sup>123</sup> which offers comprehensive guidance on materiality assessment and examples of sustainability risks including but not limited to climate change, ecosystem decline, and water supply. Three banks referred to SDGs and one bank recognized the impact of climate change on society and business. Banks did not disclose participation in sustainable finance initiatives. Only one bank mentioned engagement with regulators on the topic of E&S issues in lending practices, but it did not disclose details of this engagement.

POLICIES



Five banks did not disclose any position statements or commitments in relation to key E&S issues such as climate risk, water and human rights. Currently, only one bank recognizes water shortage and human rights risks, although this does not translate into policy requirements for clients to manage these risks as conditions of financing. Banks did not disclose sector policies or sector-specific E&S performance requirements for clients.

PROCESSES



Banks did not disclose details of their E&S risk management processes. Only one bank mentioned that it has a responsible lending policy to identify, evaluate and mitigate E&S risks. However, the policy is not disclosed so details of E&S standards against which clients are assessed and requirements for mitigating action plans are not provided. Disclosure of E&S risk management processes will enable banks to align with the MCCG 2017 guidance that disclosure needs to include discussion on how “key risk areas [which include sustainability risk] were evaluated and the controls in place to mitigate or manage those risks”.<sup>124</sup>

PEOPLE



Two banks mentioned senior management oversight of their E&S processes, which aligns with the MCCG 2017 requirement for the board to “ensure that the strategic plan of the company supports long-term value creation and includes strategies on economic, environmental and social considerations”. None of the banks disclosed any information on the presence of ESG specialists, E&S-related staff training or the distribution of E&S roles and responsibilities across their organization.

PRODUCTS



Three banks disclosed participation in the GTFS. Two banks disclosed involvement in the rollout of SRI Sukuk bonds in line with the framework issued by the Securities Commission. This shows that policy initiatives can boost adoption of sustainability measures by the financial sector.

PORTFOLIO



All banks disclosed their loan exposures by sector. However, they did not provide more detailed disclosures on overall exposure to E&S risks such as sub-sectoral breakdown of energy portfolio, carbon intensity or percentage of portfolio aligning with E&S commitments, nor did they disclose commitments to portfolio-level E&S targets. The Sustainability Reporting Guide highlights the importance of “reducing exposures to sustainability-related risks”.





# CHAPTER 5

THE PHILIPPINES

## NATIONAL CLIMATE CHANGE AND SUSTAINABLE DEVELOPMENT GOALS

**The Philippines' 2015 INDC frames the country's commitment to shift toward cleaner energy sources to reduce fossil fuel dependency. According to the submitted pledge, the country is expected to reduce its GHG emissions by 70 per cent by 2030 in comparison to a business-as-usual scenario.<sup>125</sup>**

The emission reduction target is to be achieved via increasing national carbon sinks and economy-wide measures; however, details are yet to be disclosed. The INDC states that the target is conditional on “*the extent of financial resources, including technology development & transfer, and capacity building, that will be made available to the Philippines*”.<sup>126</sup> The National Economic and Development Authority (NEDA) is expected to provide further guidance for the country's development pathway as it plans to formulate a sustainable development roadmap to streamline national and regional plans, achieve SDGs and ensure a smooth transition to a sustainable economy.<sup>127</sup> The roadmap is expected to be published by the end of 2017.

The 2011 Philippine National Climate Change Action Plan (PNCCAP) prioritizes the mitigation of key E&S risks such as food and water stress, ecosystem and environmental degradation, fossil fuel dependency and lack of capacity development as the strategic direction for 2011 to 2028.<sup>128</sup> According to the PNCCAP, public financing will focus on adaptation efforts to reduce the vulnerability of marginalized communities. At the same time, private sector participation will be encouraged to leverage mitigation opportunities and achieve sustainable development.



**PHILIPPINES**

# SUPPORTING REGULATORY FRAMEWORK PERTAINING TO SUSTAINABLE BANKING

## BANKING REGULATIONS AND BANKING ASSOCIATION GUIDELINES

At present, the Philippines' banking regulators do not provide an overarching regulatory framework pertaining to sustainable banking. The Sustainable Energy Finance (SEF) programme represents the first national initiative aimed at supporting private banks through capacity-building, technical evaluation and product development to help them finance energy efficiency and renewable energy projects.<sup>129</sup> The SEF was allocated US\$10 million from the Clean Technology Fund governed by Climate Investment Funds<sup>130</sup> and is being implemented by the IFC in cooperation with the two largest banks in the Philippines, namely the Bank of the Philippine Islands and BDO. As of December 2016, the SEF supported the disbursement of US\$120 million in loans and US\$200 million in total project investments.<sup>131</sup> The programme has catalysed investments in 66 sustainable energy projects, which will cut CO<sub>2</sub> emissions by more than 740,000 tonnes a year.<sup>132</sup>

## CORPORATE GOVERNANCE FRAMEWORK, LISTING RULES AND SUSTAINABILITY REPORTING GUIDELINES

According to the 2017 Code of Corporate Governance, publicly listed companies are required to disclose their corporate governance measures on a 'comply or explain' basis.<sup>133</sup> Last reviewed in 2016 by Securities and Exchange Commission (SEC) Philippines and IFC, the updated Code includes a list of recommendations on ESG disclosure, transparency and shareholder protection.<sup>134</sup> Based on the Code, the board is responsible for establishing a clear disclosure policy for non-financial information, with emphasis on the management of economic, environmental, social and governance issues. Companies are encouraged to adopt standardized reporting frameworks such as GRI and SASB. Furthermore, in order to ensure transparency and proper governance, companies are recommended to identify and analyse key risk exposures relating to ESG factors and assess them against targets. The Code also encourages sustainability and social responsibility in all companies' dealings with communities to foster comprehensive and balanced development.

There are no specific sustainability reporting guidelines requiring disclosure of E&S performance.<sup>135</sup> Nonetheless, in recognizing the gap regarding disclosure, the regulators, namely Philippine Stock Exchange (PSE) and SEC, are pursuing efforts to extend PSE listing requirements to include the production and disclosure of sustainability reports on a 'comply or explain' basis.<sup>136</sup> In the meantime, listed companies are encouraged to improve their sustainability reporting efforts to meet the expectations of foreign institutional investors on reporting processes.<sup>137</sup>

It is worth noting that according to the Philippines' Corporate Social Responsibility Act of 2011, companies should take responsibility for their operations through CSR-related initiatives.<sup>138</sup> Companies are encouraged to contribute on a voluntary basis to sustainable economic development by working with relevant stakeholders for a sustainable development agenda.



# CORPORATE GOVERNANCE DISCLOSURE RESULTS

TABLE 10: PHILIPPINES CORPORATE GOVERNANCE DISCLOSURE RESULTS

CORPORATE GOVERNANCE ASPECTS AND INDICATORS		BDO	BPI	CBC	METROBANK	PNB	SBC	AVG
1) BOARD	1. Independence and qualification of the board							
	2. Clearly stated board's role and monitoring the implementation of corporate strategy							
	3. Appointment and selection, training and re-election							
	4. Remuneration and appraisal							
2) SHAREHOLDERS AND STAKEHOLDERS	5. Rights of shareholders							
	6. Policies on stakeholders engagement and list of stakeholders groups engaged							
	7. Stakeholder reporting and communicating mechanisms							
3) DISCLOSURE AND TRANSPARENCY	8. Release of reports and disclosure on ESG issues							
	9. Corporate website							
4) AUDIT AND RISKS	10. General audit function and audit on sustainability							
	11. Risk management frameworks and ESG-related risks							



## BOARD



It is noteworthy that all Philippine banks have disclosed fully against the board responsibilities indicator, giving a clear statement of the board's roles and responsibilities and supervision of the implementation of the corporate strategy, vision and mission by the directors. This could be attributed to the Philippine Corporate Governance Blueprint 2015<sup>139</sup> drawn up by the SEC, which promotes the need to highlight the importance of the roles and responsibilities of the Board in order to ensure the development and growth of the local capital markets. However, for all banks surveyed, the majority of the directors on the board are not independent, despite the fact that the Code of Corporate Governance specifies that they should be.

## SHAREHOLDERS AND STAKEHOLDERS



The banks provided high levels of disclosure on stakeholder engagement. Specifically, all banks disclosed the list of stakeholder groups engaged, and five out of the six banks disclosed policies and procedures to engage them as well as the reporting mechanisms when their rights are violated. In this area, the Blueprint has also played an instrumental role in encouraging banks to go beyond the interests of shareholders to engage with other stakeholders, which includes implementing various engagement mechanisms to address their interests.

## DISCLOSURE AND TRANSPARENCY



None of the banks mentioned responsible lending in their leadership statement, indicating a lack of emphasis from the top on this matter. This could be because the banks foster social responsibility by adopting a CSR approach rather than ESG integration, making responsible lending less of a priority.<sup>140</sup> Nonetheless, the revised Code, which will take effect later this year, encourages companies to integrate sustainability and social responsibility into their business. It is hence possible that Philippine banks will practise responsible lending and disclose details on ESG integration in the near future. Besides this, all Philippine banks have responded to the Blueprint's call to disclose their corporate and ownership structures, as well as related party transactions.

## AUDIT AND RISKS



Only one bank made disclosure regarding external audit on sustainability reports and ESG-related risks, which could be linked to the absence of existing reporting guidelines for sustainability.

The Blueprint is promulgating more comprehensive and balanced development of social responsibility in companies, which means that Philippine banks can be expected to improve in the disclosure of their sustainability-related considerations.

# ESG INTEGRATION DISCLOSURE RESULTS

TABLE 11: PHILIPPINES ESG INTEGRATION DISCLOSURE RESULTS

ESG INTEGRATION PILLARS AND INDICATORS		BDO	BPI	CBC	METROBANK	PNB	SBC	AVG
1) PURPOSE	1. Relevance of sustainability to the organization and its strategy for addressing sustainability							
	2. Participation in commitment-based sustainable finance initiatives (BEI, Equator Principles, UNEPFI, etc.)							
2) POLICIES	3. Public statements on principles and risk appetite and aspects of ESG and ESRM							
	4. Sector-specific policies							
3) PROCESSES	5. Process for assessing ESG risks in client and transactional approvals							
	6. Procedures for client monitoring and engagement							
4) PEOPLE	7. Responsibilities for ESG							
	8. E&S staff competency and performance evaluation							
5) PRODUCTS	9. ESG integration in products and services							
6) PORTFOLIO	10. ESG risk assessment and mitigation at portfolio level							
	11. Disclosure of ESG risk exposure and targets							

## PURPOSE



Four banks included sustainability references in their vision and mission statements, with three of these banks recognizing the E&S impact of client operations financed by the banks. Sustainability reports did not make any direct references to the key sustainability topics of climate change and SDGs. Two of the banks acknowledged the materiality of E&S issues for businesses and stakeholders, while four banks listed local communities or NGOs as stakeholders, which is also prescribed by the 2017 Code of Corporate Governance. None of the banks disclosed participation in international sustainable finance initiatives or engagement with national regulators on ESG-related matters.

## POLICIES



Philippine banks did not disclose information pertaining to E&S policies and principles, with the sole exception of one bank publicly committing to stop financing projects deemed to have harmful effects on the environment and local communities. This is despite the Code recommending the identification and analysis of key risk exposure relating to E&S factors. As such, banks should create and disclose a policy framework to ensure that they have a clear position on how they manage these risks that is transparent to both clients and stakeholders.

## PROCESSES



Only one bank disclosed information on the ESG assessment of its clients and transactions. As part of its credit approval process, the bank classifies debtors according to the E&S risks of their operations. None of the banks disclosed any monitoring of clients' compliance on E&S issues, or procedures for dealing with non-compliance.

## PEOPLE



Sustainability reports of Philippine banks did not include information on the responsibilities of staff for ESG matters. Only one bank disclosed the presence of senior management oversight on the development and implementation of E&S policies, despite the Code recommending board supervision on the disclosure of ESG policies. None of the banks disclosed the existence of any internal dedicated ESG teams nor the responsibilities of other departments in ESG implementation. Three of the assessed banks have joined international initiatives such as the Sustainable Energy Finance (SEF) programme to benefit from training on green financing and boost green lending in the country.<sup>141</sup>

### PRODUCTS



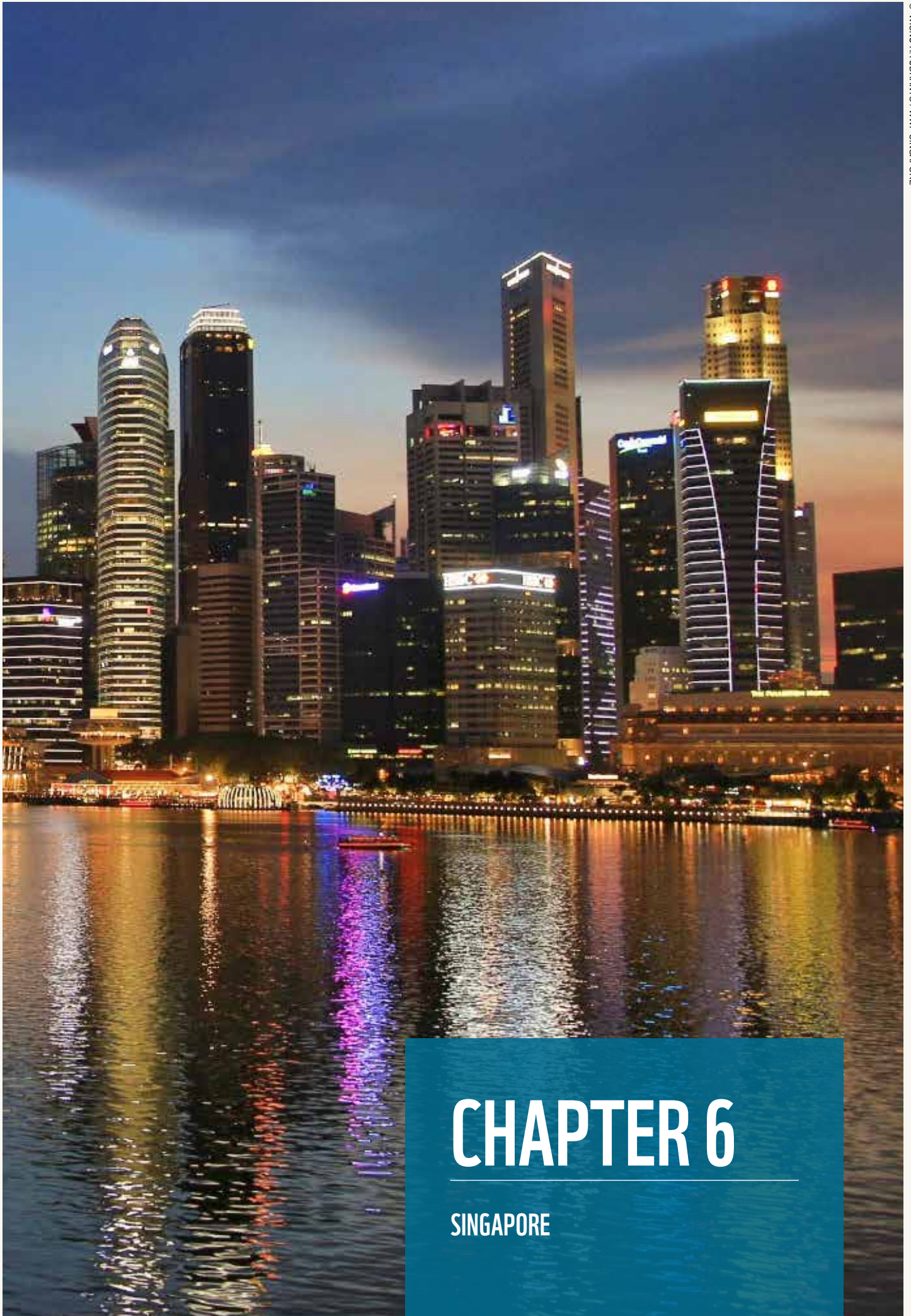
Three banks disclosed the development of sustainable finance products catering to the needs of clients investing in energy efficiency and renewable energy projects. One of these banks developed products covering a wider environmental scope beyond renewable energy. Another bank developed a unit investment trust fund incorporating ESG criteria in portfolio selection to favour investments in listed companies that exhibit good ESG practices. No bank provided disclosure on the integration of E&S factors into existing products nor on client outreach efforts.

### PORTFOLIO



All banks disclosed their loan exposures by sector. However, they did not provide more detailed disclosures on overall exposure to E&S risks such as sub-sectoral breakdown of their energy portfolio, carbon intensity or the percentage of their portfolio aligning with E&S commitments, nor did they disclose commitments to portfolio-level E&S targets. The Code includes the identification and analysis of key risk exposure relating to E&S factors, reinforcing the need for banks to disclose their exposure to ESG and climate-related risks and related risk management targets.





# CHAPTER 6

SINGAPORE



## NATIONAL CLIMATE CHANGE AND SUSTAINABLE DEVELOPMENT GOALS

**Singapore has pledged to reduce its emissions intensity by 36 per cent from 2005 levels by 2030.<sup>142</sup> A Climate Action Plan was published in 2016 by the National Climate Change Secretariat (NCCS), demonstrating how Singapore will reduce GHG emissions and increase energy efficiency targets.<sup>143</sup>**

Some of the key strategies include developing low-carbon technologies and stimulating the collaboration between government agencies, individuals, businesses and the community. In the 2017 Singapore budget, the Ministry of Finance introduced two measures to accomplish its goals in curbing emissions as well as conserving natural resources.<sup>144</sup> One measure was to raise the water price to increase water conservation and strengthen water security, and the other was to impose a carbon tax from 2019 onwards on large direct emitters of GHGs.<sup>145</sup>

In support of the national climate change strategy, the Ministry of Environment and Water Resources (MEWR) acknowledged the role of all stakeholders, including investors, in combating climate change in its speech at the UNFCCC conference in 2016.<sup>146</sup> The ministry singled out the protection of forests and prevention of peatland fires as key to the global climate change plan, and also envisions a haze-free ASEAN by 2020 through strong regional cooperation. Furthermore, the Singapore government is committed to the 2030 Agenda, which comprises the SDGs and associated targets<sup>147</sup>. This is evident in the Sustainable Singapore Blueprint 2015 developed by MEWR and the Ministry of National Development, which outlines the government's vision and plans to create a more liveable and sustainable city.<sup>148</sup> Developing a leading green economy is one of the aspirations of the blueprint.



**SINGAPORE**

# SUPPORTING REGULATORY FRAMEWORK PERTAINING TO SUSTAINABLE BANKING

## BANKING REGULATIONS AND BANKING ASSOCIATION GUIDELINES

**The Association of Banks in Singapore (ABS) recognizes that the Singapore banking sector can contribute to sustainable development by embedding responsible financing into its core strategy.<sup>149</sup>**

This vision is congruent with the statement of the central bank (the Monetary Authority of Singapore, MAS) that “*lenders, investors, consumers, NGOs and the media all have roles to play in sustainability matters*”.<sup>150</sup> To ensure minimum standards on responsible financing are adopted across the board, ABS launched the Guidelines on Responsible Financing in consultation with banks in October 2015.<sup>151</sup> The guidelines state that “*financiers have an important role to play in shaping and expecting the responsible actions from their employees and clients.*”

**The guidelines list three principles on responsible financing in banks’ business models:**

- i) Disclosure of senior management’s commitment to implement responsible financing;
  - ii) Establishing internal controls through policies and procedures and defining specific roles dedicated to responsible financing; and
  - iii) Capacity-building to raise staff awareness, so as to integrate E&S into daily operations.
- In order to drive greater transparency and accountability, banks must disclose policy frameworks and their senior management commitment to responsible financing in their annual reports.<sup>152</sup>

On top of the main principles, ABS also defines a number of high-risk industries which banks should take into consideration when developing their financing policies. These include agriculture, chemicals, defence, energy (especially oil, gas and coal), forestry, infrastructure, mining and metals, and waste management. Regarding haze risk management, ABS released a “*Haze Prevention and Fire Risk Assessment*”, developed together with WWF, as an additional toolkit in early 2017 to assist banks in assessing and monitoring their clients.<sup>153</sup> Banks are expected to fulfil these requirements by ensuring that clients comply with practices such as no open burning, adherence to local regulations regarding new planting on peat, best practice management of existing peat plantations as well as working with local communities on responsible land clearing.<sup>154</sup>

In support of the green finance agenda, in June 2017 MAS launched a green bonds scheme. This assures investors that funds will be funnelled into projects that create environmental benefits.<sup>155</sup> MAS will offset up to S\$100,000 (US\$73,000) of the cost of issuing green bonds, which have a minimum size of S\$200 million (US\$147 million) and a tenure of at least three years.<sup>156</sup> This scheme will run from June 2017 to end of May 2020.<sup>157</sup>

The sustainable banking regulatory framework is voluntary with no penalties for non-compliance.<sup>158</sup> No assessment framework or indicators have been established in order to monitor financial institutions’ performance on ESG integration. The guidelines do not specify step-by-step actions that banks should take to achieve the recommended targets and overarching goals. Nevertheless, ABS facilitates the implementation of the guidelines by allocating resources for capacity-building and skills development in cooperation with relevant stakeholders such as WWF to support banks in this transition to sustainable financing. It expects banks to meet these guidelines by 2017.

## CORPORATE GOVERNANCE FRAMEWORK, LISTING RULES AND SUSTAINABILITY REPORTING GUIDELINES













































In Singapore, listed companies must disclose their corporate governance practices with reference to the Code of Corporate Governance,<sup>159</sup> under the purview of MAS and Singapore Exchange (SGX). The Code specifies the board's duty to consider sustainability issues such as E&S factors as part of its strategic formulation. Last reviewed in 2012, the Code is under review in 2017 by a Corporate Governance Council set up by MAS to ensure sustained corporate performance and help maintain investor confidence.<sup>160</sup>

In 2011, SGX launched the Guide to Sustainability Reporting for Listed Companies.<sup>161</sup> Although sustainability reporting was voluntary at the time, the Guide's objective was to raise awareness by explaining the purpose, process, structure and content for reporting. In further promotion of sustainability issues amongst listed companies, SGX announced the launch of the SGX Sustainability Indices in May 2016.<sup>162</sup> In partnership with Sustainalytics to produce the indices, SGX aims to improve the level of sustainability disclosures, as well as to provide guidance for investors who look at sustainability factors before investment.<sup>163</sup> None of the Singapore banks are included in the ESG Index.

The launch was also in tandem with SGX's introduction of sustainability reporting for listed companies in June 2016 on a 'comply or explain' basis from the financial year ending on or after 31 December 2017.<sup>164</sup> The revised listing rules not only require the issuers to release a sustainability report within five months after the financial year end, but also to incorporate the new Sustainability Reporting Guide and elaborate on the additional components such as material ESG factors, policies and targets.<sup>165</sup> In particular, to reinforce the Code, the company's sustainability report is required to contain a statement from the board specifying they have determined the material ESG factors as well as overseen the monitoring process. The Guide suggests a phased approach whereby over three years a company moves toward incorporation of quantitative and qualitative targets for each material ESG factor and disclosure of performance against those targets. In addition, the Guide proposes linking targets to management performance incentives. Another noteworthy improvement is that stakeholder engagement requirements have been strengthened in the new Guide. It encourages companies to consider views of all stakeholders including local communities when identifying the material ESG factors and to take into account ESG factors in their engagement with stakeholders.

## CORPORATE GOVERNANCE DISCLOSURE RESULTS

TABLE 12: SINGAPORE CORPORATE GOVERNANCE DISCLOSURE RESULTS

CORPORATE GOVERNANCE ASPECTS AND INDICATORS		DBS	OCBC	UOB	AVG
1) BOARD	1. Independence and qualification of the board				
	2. Clearly stated board's role and monitoring the implementation of corporate strategy				
	3. Appointment and selection, training and re-election				
	4. Remuneration and appraisal				
2) SHAREHOLDERS AND STAKEHOLDERS	5. Rights of shareholders				
	6. Policies on stakeholders engagement and list of stakeholders groups engaged				
	7. Stakeholder reporting and communicating mechanisms				
3) DISCLOSURE AND TRANSPARENCY	8. Release of reports and disclosure on ESG issues				
	9. Corporate website				
4) AUDIT AND RISKS	10. General audit function and audit on sustainability				
	11. Risk management frameworks and ESG-related risks				

## BOARD



Of the three banks reviewed, only one disclosed a limit on the number of boards that independent and executive directors can serve on at once. Despite extensive elaboration on the need for independent directors on boards, and stipulating that they should make up at least one-third of boards, the Code only recommends that companies set their own limits for the number of boards executive and independent directors can serve on at once. This could perhaps explain the lack of disclosure in this regard by Singaporean banks.

## SHAREHOLDERS AND STAKEHOLDERS



All of the banks disclosed measures to uphold their shareholders' rights, which is in alignment with the Code's principle in treating all shareholders "fairly and equitably" while facilitating the use of their rights. Although this should prevent the violation of rights, the Code does not address what should happen if rights are violated; as such, none of the Singaporean banks disclosed the detailed reporting and resolving mechanisms that could be utilized when the rights of stakeholders are violated. Moreover, in terms of stakeholder engagement, one bank did not disclose any policies or procedures to engage stakeholders.

## DISCLOSURE AND TRANSPARENCY



All three banks disclosed important corporate information in both their websites and reports; pertinent information such as their corporate structures, ownership structures and related party transactions are well disclosed for the relevant parties' perusal. In addition, two out of three banks' leadership statements mentioned responsible lending, and all the banks' websites have a sustainability section.

## AUDIT AND RISKS



All the banks have disclosed auditing measures for corporate governance, but they did not disclose as much against sustainability criteria for audit and risks. While they disclosed the identification of ESG-related risks, they did not disclose any periodic audits on their sustainability policies or E&S risk assessment procedures. This could be a result of limited regulations governing sustainability in the Code, which necessitates only that the board "*considers sustainability issues, e.g. E&S factors, as part of its strategic formulation*". Furthermore, as SGX mandates that companies are to report on sustainability issues beginning FY2017 on a 'comply or explain' basis, there is more incentive for banks to improve their auditing in this area.

With the impending enforcement of the SGX Sustainability Reporting Guide as well as an ongoing review of the Code aimed at enhancing the quality of disclosure of corporate governance,<sup>166</sup> it is expected that corporate governance in Singapore will further improve along all fronts, and especially in sustainability reporting.





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Transport and infrastructure sectors can have a large ESG and carbon footprint. Banks need to manage these risks.

# ESG INTEGRATION DISCLOSURE RESULTS

TABLE 13: SINGAPORE ESG INTEGRATION DISCLOSURE RESULTS

ESG INTEGRATION PILLARS AND INDICATORS		DBS	OCBC	UOB	AVG
1) PURPOSE	1. Relevance of sustainability to the organization and its strategy for addressing sustainability				
	2. Participation in commitment-based sustainable finance initiatives (BEI, Equator Principles, UNEPFI, etc.)				
2) POLICIES	3. Public statements on principles and risk appetite and aspects of ESG and ESRM				
	4. Sector-specific policies				
3) PROCESSES	5. Process for assessing ESG risks in client and transactional approvals				
	6. Procedures for client monitoring and engagement				
4) PEOPLE	7. Responsibilities for ESG				
	8. E&S staff competency and performance evaluation				
5) PRODUCTS	9. ESG integration in products and services				
6) PORTFOLIO	10. ESG risk assessment and mitigation at portfolio level				
	11. Disclosure of ESG risk exposure and targets				

## PURPOSE



All Singaporean banks disclosed efforts to integrate sustainability concepts in their core business strategy and clearly distinguished between indirect and direct ESG footprint of their business activities. Two banks disclosed their material ESG issues, but only one bank recognized climate change as a risk for society and businesses. However, only one bank has disclosed a commitment to contribute to the SDGs, specifying four goals. Moreover, just two banks listed local communities within the list of key stakeholders and disclosed engagement with key stakeholders to understand ESG factors important to them and relevant to the bank's business. Disclosure on engagement efforts on these topics will enable banks to align with SGX Sustainability Guidelines, which recommend issuers of reports to "consider ESG factors in their engagement with stakeholders".<sup>167</sup> No banks disclosed participation in commitment-based sustainable finance initiatives, except for one bank stating its role in working together with the banking association to develop sustainable finance guidelines.

## POLICIES



Banks have made progress in recognizing some key E&S issues such as deforestation, biodiversity loss and human rights. They all have exclusion lists, with one bank including World Heritage Sites as a no-go area. One bank recognized the risk of water pollution stemming from its clients' activities, which reflects water being stated as one of the potential material ESG factors in the SGX Sustainability Reporting Guidelines.<sup>168</sup> However, none of the banks disclosed requirements for all clients across sensitive ESG sectors to take actions such as committing to no deforestation or conducting water risk assessments. Two banks' E&S requirements apply to financial services beyond lending, for example to capital markets activities or in some cases across the group. Apart from two banks making reference to sensitive sectors identified in ABS guidelines, such as agriculture, forestry and defence, banks did not disclose corresponding sector policies, with the exception of one bank disclosing only its palm oil policy. The three banks did not disclose position statements covering cross-cutting E&S issues mentioned above.

## PROCESSES



Although all banks disclosed standardized E&S risk assessment and credit approval frameworks to evaluate clients and transactions, only two elaborated on escalation mechanisms and how assessment results affect client acceptance decisions. One bank disclosed the consideration of clients' track records, while another disclosed the assignment of ESG risk ratings to its borrowers. Even though banks do assess clients, they did not disclose sufficient information about engagement and monitoring procedures. Only one bank disclosed the requirement for medium- and high-risk clients to comply with agreed ESG milestones as part of loan approval as well as disclosing the monitoring of clients' compliance with agreed action plans. Another bank disclosed that it periodically reviews its clients' ESG profiles and stated that non-compliance with agreed E&S action plans can lead to reassessment of the transaction.

## PEOPLE



Reports indicate that all banks' senior management are responsible for implementing E&S policies and procedures. One bank disclosed climate risks as one of the material ESG risks, for which the board is responsible. However, responsibilities and roles within banks on E&S issues are often not disclosed, for example distribution of E&S responsibilities to the three lines of defence. Two banks disclosed they train staff on E&S issues. Only one bank disclosed sustainability-related KPIs, although it would be in accordance with the SGX Sustainability Guidelines requirement to link ESG targets with management performance incentives.

### PRODUCTS



Two banks disclosed sustainable banking products within their portfolio. One bank recently issued its own green bonds, which aim to finance green projects or assets such as climate change adaptation and sustainable transportation using the net proceeds.<sup>169</sup> Another bank offers a socially responsible impact investment product aimed at improving the living standards of communities in Southeast Asia and China. While these are nascent signs of sustainability-oriented market solutions, there is still no indication that banks are integrating E&S factors into mainstream capital allocation decisions. Banks do not disclose any client outreach activities to increase clients' understanding of E&S issues.

### PORTFOLIO



All banks disclosed their loan exposures by sector. However, they did not provide more detailed disclosures on overall exposure to E&S risks such as sub-sectoral breakdown of energy portfolio, carbon intensity or percentage of portfolio aligning with E&S commitments, nor did they disclose commitments to portfolio-level E&S targets.

In general, banks provided better disclosure on issues that were covered in the ABS guidelines such as creating E&S policies and staff capacity, but still have room to improve on their disclosure on ESG product development and portfolio management.





# CHAPTER 7

THAILAND



## NATIONAL CLIMATE CHANGE AND SUSTAINABLE DEVELOPMENT GOALS

To facilitate the achievement of the SDG commitments, the Thai government has been guided by the Sufficiency Economy Philosophy (SEP) of the late King Bhumibol Adulyadej to create the “SEP for SDGs Partnership” as a guide for decision-making processes.<sup>170</sup>

The SEP espouses “*moderation, appropriate technology, careful risk management, and flexibility*” in making decisions that are inclusive, cost-effective and environmentally friendly.<sup>171</sup> Green financing is mentioned as a tool to support both SEP and SDGs through provision of green loans for entities engaging in eco-friendly projects such as renewable energy.

The government also acknowledges the country’s vulnerability to climate change. To mitigate climate change risks, Thailand’s submitted INDC commits to implement economy-wide measures to cut GHG emissions by 20 per cent by 2030, compared to the 2010 projected business-as-usual level.<sup>172</sup> Thailand’s contribution to reducing GHGs could increase to 25 per cent if appropriate access to technology, financial resources and capacity-building is made available under the UNFCCC framework.



The National Economic and Social Development Board (NESDB) released its 12th National Plan in 2017 to map out the nation's key strategies for 2017-2021. The 12th plan is in accordance with the 20-year national strategy 2017-2036, in which green growth has been identified as one of the six key targets of development.<sup>173</sup> The plan envisions an environmentally friendly economy and society created by increasing green economic activities and reducing risks of natural disasters linked to global climate change. This is also illustrated in the fourth strategy of the NESDB, which pursues “*green growth for sustainable development*”, through the balance of conservation and the sustainable use of natural resources, building water security, improving environmental quality as well as enhancing capacity for climate adaptation and mitigation.<sup>174</sup> In the plan, the NESDB emphasized the need to establish public-private financial mechanisms to support climate change mitigation actions, such as developing carbon credits, carbon markets and carbon taxes.<sup>175</sup>

## SUPPORTING REGULATORY FRAMEWORK PERTAINING TO SUSTAINABLE BANKING

### BANKING REGULATIONS AND BANKING ASSOCIATION GUIDELINES

**It is notable that the Thai Bankers' Association (TBA) established a link between its five-year plan and the 12th National Plan, highlighting the integral role of the banking sector in helping to meet some of the goals stated in the government plan.<sup>176</sup> For instance, the TBA seeks to create a more inclusive financial system to support the real economy by singling out the priority of enhancing credit access for SMEs with a goal of providing bank loans for up to 70-80 per cent of SMEs.<sup>177</sup>**

The Bank of Thailand (BOT), in cooperation with the Ministry of Finance, has set the goals and strategic directions for financial sector development through the implementation of the Financial Sector Master Plan (FSMP).<sup>178</sup> The third phase will be executed from 2016 to 2020. The overarching goal is to promote a Thai financial sector that is “*competitive, inclusive, connected and sustainable*”.<sup>179</sup> Promoting financial access to encourage inclusive growth is hence one of the key initiatives of the FSMP.<sup>180</sup> The BOT has acknowledged its role in driving Thailand's sustainable growth, and actively supports the goal of sustainable well-being, for which strong economic fundamentals are a prerequisite.<sup>181</sup> However, it does not elaborate on what is envisaged by the term “*sustainable finance sector*”.

The current finance regulations in Thailand do not yet specify how commercial banks should take ESG criteria into consideration. As a result, commercial banks are not obligated to integrate E&S criteria when issuing loans or introducing new financial products apart from requiring clients to comply with existing laws. BOT is currently engaging with civil society and other stakeholders on sustainable finance topics to create a suitable framework for the Thai banking sector.

## CORPORATE GOVERNANCE FRAMEWORK, LISTING RULES AND SUSTAINABILITY REPORTING GUIDELINES

In Thailand, listed companies are required to disclose their corporate governance policies on a ‘comply or explain’ basis with reference to the Principles of Good Corporate Governance for Listed Companies 2012 released by the Stock Exchange of Thailand (SET). The Principles recommend that the board should consider E&S issues from both direct and indirect operations and set clear policies on E&S issues to ensure that the company contributes to sustainable development. Furthermore, they recommend that the board should encourage the company to create a separate sustainability report, or at least integrate the information into the firm’s annual report.<sup>182</sup> In 2017, the Securities and Exchange Commission of Thailand (SEC) released the Corporate Governance Code for Listed Companies, shifting from the ‘comply or explain’ requirement to an ‘apply or explain’ basis to encourage the board to “*comprehensively apply the CG Code to the company’s business in the interest of long-term sustainable value creation*”.<sup>183</sup>

Effective from 2014, the SET mandated all listed companies to disclose their CSR and ESG<sup>184</sup> practices regarding stakeholders, the economy, society and environment in their annual report or a standalone report.<sup>185</sup> SET underlines the importance of an ESG approach as opposed to “*CSR as a philanthropic or charitable activity*”. To provide further guidance on ESG reporting, SET has published the Guidelines for Sustainability Reporting (in Thai) and regularly organizes training on social responsibility and sustainable development for listed companies.<sup>186</sup> The Guidelines were developed based on international reporting framework ISO 26000 and GRI; however, being only available in the Thai language, they are inaccessible to global investors.

Furthermore, as the first stock exchange in ASEAN joining the UN Sustainable Stock Exchange (SSE) initiative, SET continues to promote and develop Thai listed companies’ performance and disclosure on sustainability matters. In 2015, SET released the Thailand Sustainability Investment, which lists Thai companies with the best (in country) performances on ESG aspects, to further encourage sustainable practices amongst listed firms and respond to investor demand for responsible investment options.<sup>187</sup> The evaluation of ESG performance is done in line with the guidelines of the Dow Jones Sustainability Index and is reviewed annually.<sup>188</sup>

## CORPORATE GOVERNANCE DISCLOSURE RESULTS

TABLE 14: THAILAND CORPORATE GOVERNANCE DISCLOSURE RESULTS

CORPORATE GOVERNANCE ASPECTS AND INDICATORS		BANGKOK BANK	KBANK	KRUNGSRI	KTB	SCB	TBANK	TMB	AVG
1) BOARD	1. Independence and qualification of the board								
	2. Clearly stated board's role and monitoring the implementation of corporate strategy								
	3. Appointment and selection, training and re-election								
	4. Remuneration and appraisal								
2) SHAREHOLDERS AND STAKEHOLDERS	5. Rights of shareholders								
	6. Policies on stakeholders engagement and list of stakeholders groups engaged								
	7. Stakeholder reporting and communicating mechanisms								
3) DISCLOSURE AND TRANSPARENCY	8. Release of reports and disclosure on ESG issues								
	9. Corporate website								
4) AUDIT AND RISKS	10. General audit function and audit on sustainability								
	11. Risk management frameworks and ESG-related risks								



## BOARD



For the board aspect, some gaps included how none of the banks subject their directors to re-election at least once every three years, and only one bank has an independent chairman. This is despite the Code recommending that the board chairman should be an independent director. The Code suggests that if the chairman is not an independent director, more than half of the board should be independent directors. Likewise, five out of seven banks did not heed this recommendation.

## SHAREHOLDERS AND STAKEHOLDERS



Responsibilities to stakeholders form the core of sustainable value creation that is emphasized within the Principles.<sup>189</sup> As such, reporting and resolving mechanisms dealing with the violation of stakeholders' rights are disclosed by five out of seven Thai banks. However, it is noteworthy that only one bank disclosed policies to provide information on major changes that are likely to affect its market value to its shareholders, even though the Code requires such practice.

## DISCLOSURE AND TRANSPARENCY



None of the banks has disclosed the number of days taken to release the financial results and annual reports. Responsible lending was mentioned in two banks' leadership statements. Thai banks are mandated by SEC and CSR Club (from the Stock Exchange of Thailand) to report their CSR operations and practices. As such, all of the banks have sustainability reporting.

## AUDIT AND RISKS



The emphasis on sustainability reporting resulted in four Thai banks identifying sustainability-related risks. However, it should be recognized that Thailand did not score as well in other sustainability-related audit and risk areas. Specifically, only three of the banks have external audit on their sustainability reporting and five do not periodically review their E&S policies and procedures.



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Clean energy generation at the Sankampaeng solar power station, Chiang Mai, Thailand. Renewable energy or energy-efficient products are part of the solution to mitigate climate change.

# ESG INTEGRATION DISCLOSURE RESULTS

TABLE 15: THAILAND ESG INTEGRATION DISCLOSURE RESULTS

ESG INTEGRATION PILLARS AND INDICATORS		BANGKOK BANK	KBANK	KRUNGSRI	KTB	SCB	TBANK	TMB	AVG
1) PURPOSE	1. Relevance of sustainability to the organization and its strategy for addressing sustainability								
	2. Participation in commitment-based sustainable finance initiatives (BEI, Equator Principles, UNEPFI, etc.)								
2) POLICIES	3. Public statements on principles and risk appetite and aspects of ESG and ESRM								
	4. Sector-specific policies								
3) PROCESSES	5. Process for assessing ESG risks in client and transactional approvals								
	6. Procedures for client monitoring and engagement								
4) PEOPLE	7. Responsibilities for ESG								
	8. E&S staff competency and performance evaluation								
5) PRODUCTS	9. ESG integration in products and services								
6) PORTFOLIO	10. ESG risk assessment and mitigation at portfolio level								
	11. Disclosure of ESG risk exposure and targets								

## PURPOSE



Six out of seven banks made reference to sustainability in their corporate strategy, out of which five distinguished between their own direct footprint and the indirect footprint of the client activities they finance. Five banks acknowledge climate-related risks and three of them are taking SDGs into account in their corporate vision. Five banks also listed local communities and/or NGOs as stakeholders. Engagement with stakeholders is however seldom about the impacts of banks' lending activities, with only two banks stating that they engage regularly with regulators on issues such as responsible lending. Five of the banks identified E&S issues that are material for their business and for their stakeholders. These issues include, among others, climate change and human rights risks.

## POLICIES



Four of the banks disclosed exclusion lists, stating they will not finance activities that may violate environmental laws or other issues like human rights. However, further elaboration on the types of activities was not provided. Three banks have made additional statements on recognizing human rights impacts caused indirectly by clients' activities, with one bank disclosing that it conducts human rights risk assessment for its project financing activities. With regards to risks such as deforestation and water shortage, all banks interpret these risks to apply only to their own operations rather than the client operations that they finance. None of the banks disclosed any ESG or sector policies.

## PROCESSES



Four out of seven banks disclosed the consideration of ESG issues during credit analysis of loans, with two banks using E&S impact assessments to evaluate activities being financed. All four banks disclosed that credit risk assessment outcomes influence client and transaction acceptance decisions. However, just two banks disclosed escalation mechanisms for high-risk transactions. In addition, one bank disclosed a standardized E&S credit assessment framework for project finance, although it is not aligned with the Equator Principles. None of the banks disclosed requirements for medium- and high-risk clients to implement specific E&S action plans or disclosed if they review ESG performance of clients post loan disbursement. Only one bank disclosed a periodic review of its clients' ESG profile and one other bank disclosed that it will take necessary action when dealing with non-compliance.

## PEOPLE



Only two banks disclosed that senior management has oversight of the implementation of ESG policies and procedures. This is despite SET's 2012 Principles of Good Corporate Governance encouraging company boards to set clear policies on E&S issues including those pertaining to indirect operations, which for banks would equate to the E&S impact of client activities that they finance.<sup>190</sup> Although three banks have disclosed the existence of dedicated CSR teams or committees which are responsible for all sustainability matters, it is not clear whether these matters include ESG integration as banks do not specify the roles of these committees. Moreover, there is no disclosure on capacity-building programmes to train staff on ESG implementation, nor on whether staff are evaluated for their performance on such matters.

### PRODUCTS



Thai banks have made some headway in product development compared to other aspects of ESG integration. Four banks have created credit loans for renewable energy or energy-efficiency projects, with some also addressing microfinance, such as by supporting entrepreneurs to gain access to funds to develop environmentally friendly technologies. However, just two banks have disclosed that they devoted capital to projects related to alternative energy or investments in organizations that comply with ESG standards.

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### PORTFOLIO



There is no indication that banks are conducting portfolio-level risk assessment and mitigation for E&S issues. Disclosure at the portfolio level reflects the emphasis placed on renewable energy projects, as two banks provided information on the composition of their energy loan portfolios. One of these two banks further elaborated on its transaction and client assessment results by providing concrete figures for the number of approved project finance activities which passed E&S assessment. However, none of the banks disclosed their portfolio-wide loan exposure pertaining to E&S issues. All banks disclosed their overall loan exposure by sector.





# CHAPTER 8

VIETNAM

## NATIONAL CLIMATE CHANGE AND SUSTAINABLE DEVELOPMENT GOALS

**Sustainable growth has been on the Vietnamese policy agenda since 1992 when the National Plan for Environment and Sustainable Development<sup>191</sup> introduced sustainable development as one of the key principles in the country's growth strategy for the period 1991-2000.<sup>192</sup>**

In 2012 the government approved the 2011-2020 Sustainable Development Strategy<sup>193</sup> listing objectives and targets that guide the nation's path towards sustainable development. Furthermore, to achieve SDGs by 2030, the government incorporated the 2030 Agenda into its National Action Plan<sup>194</sup> in 2017, which aims to mobilize support from all stakeholders to achieve SDGs and *"sustain economic growth in parallel with ensuring social progress and justice and ecological environment protection, effective management and utilization of natural resources and proactively respond to climate change"*.<sup>195</sup>

The country is a signatory of the Paris Agreement, having submitted its unconditional commitment to cut GHG emissions by 8 per cent by 2030 compared to business as usual,<sup>196</sup> with contributions from energy, agriculture, waste and land use, land-use change and forestry sectors. In addition, the government has devised several strategies to address the growing threat of climate change, such as the 2014-2020 Green Growth Action Plan which prescribes the actions to be taken to guide the country toward green growth.<sup>197</sup> These actions require active collaboration with the financial sector to revise credit policies in alignment with green growth goals and to build financial organizations' capacity to develop green financial products and services.<sup>198</sup>



# SUPPORTING REGULATORY FRAMEWORK PERTAINING TO SUSTAINABLE BANKING

## BANKING REGULATIONS AND BANKING ASSOCIATION GUIDELINES

**In 2015 the State Bank of Vietnam (SBV) issued a Directive on Promoting Green Credit Growth and Environmental and Social Risks Management in Credit Granting Activities.<sup>199</sup> Its objective is to ensure that credit granting activities of financial institutions are complementary to the green growth strategy and the achievement of SDGs. Financial institutions are required to:**

- i) Develop strategies to enhance green lending, for instance by developing green products or prioritizing funding to projects in green economic sectors.
- ii) Manage E&S risks in their lending activities by conducting E&S risks credit appraisal as well as monitor their own E&S risk management frameworks.
- iii) Communicate to external stakeholders on their E&S risk management frameworks and green lending policies.
- iv) Prepare reports disclosing the statistics of transactions screened based on E&S risks and the value of green loans granted, which must be submitted quarterly to SBV.<sup>200</sup>

The directive also states that the central bank will “*guide financial institutions in developing and implementing an E&S risk management system*” by building their capacity on this topic. The credit department of SBV monitors the implementation of the directive. Although the directive is a requirement that all credit institutions have to comply with, there are currently no enforcement mechanisms nor penalties in place to deal with non-compliance.

The Vietnamese government has also shown commitment to develop a “sustainable microfinance system”, as stated in the Vietnam Microfinance Development Strategy 2011-2020.<sup>201</sup> The objective of the strategy is to cater to those under-served by conventional banking, such as the poor, low-income clients and micro-enterprises.<sup>202</sup>

## CORPORATE GOVERNANCE FRAMEWORK, LISTING RULES AND SUSTAINABILITY REPORTING GUIDELINES

In 2007, the State Securities Commission of Vietnam (SSC) and the IFC published a Corporate Governance Manual offering a comprehensive summary of frameworks and international best practices to help listed companies implement good governance standards.<sup>203</sup> In the same year, the Ministry of Finance issued circular No. 155-2015-TT-BTC<sup>204</sup> to govern the disclosure of information on the securities market, which requires the companies to disclose E&S issues and identify E&S-related risks in their annual report. To help Vietnamese companies become more competitive, SSC has been working with IFC since August 2016 to develop a countrywide Code of Corporate Governance, which is expected to be launched later in 2017.<sup>205</sup>

In response to the rise in public demand for companies to disclose their ESG performance, SSC and IFC have developed a Sustainability Reporting Handbook<sup>206</sup> to promote sustainability reporting among listed companies. The Handbook covers general recommendations on how to report according to international reporting frameworks, as well as details on what topics to cover such as E&S risks, materiality analysis and stakeholder engagement. It includes a ‘report or explain’ framework designed to encourage Vietnamese companies to start reporting, or explain why they have chosen not to.<sup>207</sup>

# CORPORATE GOVERNANCE DISCLOSURE RESULTS

TABLE 16: VIETNAM CORPORATE GOVERNANCE DISCLOSURE RESULTS

CORPORATE GOVERNANCE ASPECTS AND INDICATORS		BIDV	EXIM BANK	VIETCOM BANK	VIETIN BANK	VPBANK	AVG
1) BOARD	1. Independence and qualification of the board						
	2. Clearly stated board's role and monitoring the implementation of corporate strategy						
	3. Appointment and selection, training and re-election						
	4. Remuneration and appraisal						
2) SHAREHOLDERS AND STAKEHOLDERS	5. Rights of shareholders						
	6. Policies on stakeholders engagement and list of stakeholders groups engaged						
	7. Stakeholder reporting and communicating mechanisms						
3) DISCLOSURE AND TRANSPARENCY	8. Release of reports and disclosure on ESG issues						
	9. Corporate website						
4) AUDIT AND RISKS	10. General audit function and audit on sustainability						
	11. Risk management frameworks and ESG-related risks						



## BOARD



Although the indicator on board responsibilities has the highest average disclosure in this category, with four out of five banks disclosing the roles and responsibilities of the board, only two banks shared details on the supervision of corporate strategy implementation. This could be because there is no countrywide code of corporate governance for the banks to seek guidance on such matters. They can only rely on the Manual, which only provides recommendations on best practices and is non-binding. This also applies to other indicators such as board structure and board appointment.

## SHAREHOLDERS AND STAKEHOLDERS



All five banks disclosed that shareholders are informed of policies and procedures related to voting and general meetings, which is a recommended practice under the 2007 Corporate Governance Manual. In addition, four banks asserted the right of shareholders to participate in and vote at general meetings, which is also recommended in the Manual. None of the banks disclosed the whistleblowing policies and reporting mechanisms when the rights of stakeholders are violated.

## DISCLOSURE AND TRANSPARENCY



Despite the lack of a code of corporate governance, Vietnamese banks have provided some information on disclosure and transparency. Notably, only one bank did not have sustainability reporting. This is due to the fact that sustainability reporting is encouraged under a 'report or explain' framework contained in the Sustainability Reporting Handbook.<sup>208</sup> All five banks have made disclosure on related party and interested party transactions. This is in accordance with the disclosure requirements set out in Vietnamese Accounting Standards No. 26 on RPTs.<sup>209</sup> None of the banks have a sustainability section on their websites.

## AUDIT AND RISKS



All banks disclosed key risks, and four of the banks disclosed policies to improve their risk management. The SBV's introduction of a Basel II-type risk-based supervisory approach in 2012 could explain the high disclosure of risk-related issues.<sup>210</sup> Basel II requires banks to consider their capital and financial risks, making it necessary for Vietnamese banks to have adequate risk management policies for such risks. However, Vietnamese banks disclosed very little on audit and risk areas pertaining to sustainability such as external audit on sustainability and identification of ESG-related risks.



# ESG INTEGRATION DISCLOSURE RESULTS

TABLE 17: VIETNAM ESG INTEGRATION DISCLOSURE RESULTS

ESG INTEGRATION PILLARS AND INDICATORS		BIDV	EXIM BANK	VIETCOM BANK	VIETIN BANK	VPBANK	AVG
1) PURPOSE	1. Relevance of sustainability to the organization and its strategy for addressing sustainability						
	2. Participation in commitment-based sustainable finance initiatives (BEI, Equator Principles, UNEPFI, etc.)						
2) POLICIES	3. Public statements on principles and risk appetite and aspects of ESG and ESRM						
	4. Sector-specific policies						
3) PROCESSES	5. Process for assessing ESG risks in client and transactional approvals						
	6. Procedures for client monitoring and engagement						
4) PEOPLE	7. Responsibilities for ESG						
	8. E&S staff competency and performance evaluation						
5) PRODUCTS	9. ESG integration in products and services						
6) PORTFOLIO	10. ESG risk assessment and mitigation at portfolio level						
	11. Disclosure of ESG risk exposure and targets						

## PURPOSE



Three banks referred to sustainability in their business strategy. Two banks acknowledged and recognized the ESG footprint of their client operations and the importance of climate change for society. Only one bank disclosed information on its engagement policy with key stakeholders, including local communities and NGOs, regarding the economic, social and environmental impact of the bank's activities. Banks did not disclose clear references to SDG targets or list material E&S issues affecting the bank and stakeholders. This is despite the Sustainability Reporting Handbook recommending companies list material E&S aspects.<sup>211</sup> None of the banks disclosed any participation in international sustainable finance initiatives or engagement with national regulators on ESG-related matters.

## POLICIES



Only one bank disclosed its commitment not to finance projects that have negative environmental effects in accordance with the country's laws on environmental protection. None of the banks disclosed information on their ESG risk appetite and sector policies.

## PROCESSES



The SBV Directive requires banks to consider E&S risks in their lending activities. However, only two banks disclosed that they conduct E&S risk assessment of clients and transactions. Furthermore, banks did not disclose whether this assessment influences the outcome of the loan application or whether the E&S track record of clients is taken into account. Banks did not provide details on whether there are escalation mechanisms for controversial cases, nor if they categorize clients and transactions according to assessment results. Only one bank disclosed that it conducts periodic review of clients' E&S risk profiles. Banks did not disclose how they deal with non-compliance by clients with the bank's policies and with agreed E&S action plans.

## PEOPLE



Vietnamese banks did not disclose information on their staff ESG responsibilities nor on the presence of senior management oversight on the implementation of E&S policies. Two banks provided details concerning their in-house training programmes for credit officers to enable the integration of E&S principles in the credit approval process.

### PRODUCTS



The SBV Directive emphasizes the importance of boosting green credit and prioritizing financing for green projects in the country. Despite this, only one bank disclosed information on the integration of E&S principles into its financial products with the issuing of preferential loans to support renewable energy and sustainable agriculture projects in collaboration with international partners. There was no other disclosure on how E&S factors are used for either capital allocation decisions or new product development. Banks did not disclose any engagement with clients on ESG issues as part of their client outreach efforts.

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### PORTFOLIO



All banks disclosed their loan exposures by sectors. However, they did not provide more detailed disclosures on overall exposure to E&S risks such as sub-sectoral breakdown of energy portfolio, carbon intensity or percentage of portfolio aligning with E&S commitments, nor did they disclose commitments to portfolio-level E&S-related targets.





# CHAPTER 9

CONCLUSION AND NEXT STEPS

## CONCLUSION

**Our research shows that ASEAN governments are recognizing the role of the financial sector in driving sustainable development and combating climate change. They are also recognizing that it is important for the sector to manage ESG risks, with some regulators taking steps to issue guidelines. We identified emerging common threads of national sustainable finance and ESG regulations across the region; however, few of these explicitly address climate change and the SDGs, with no prescriptive guidelines to align financial sector objectives to national climate change and sustainable development agendas.**

This indicates that there is potential for greater harmonization at the regulatory level. Existing corporate governance codes and sustainability reporting guidelines provide a supporting base for the six pillars of ESG integration, and ASEAN banks are disclosing well against corporate governance indicators. This demonstrates that there is a good starting point from which ASEAN banks can tackle ESG integration. The existing disclosure gaps in banks' corporate governance and ESG integration performance can be addressed with more comprehensive regulatory support and capacity-building, in partnership with NGOs (and academia). This would enable immediate progress to be made while regulators work with various other policymakers to refine their sustainable banking guidelines.

With this in mind, this report provides a number of recommendations for ASEAN banks, central banks and banking associations, as well as shareholders of banks. Civil society representatives and academic institutions can also support all stakeholders to drive greater ESG integration and harmonization across the ASEAN banking sector.

## NEXT STEPS

### WE RECOMMEND ASEAN BANKS:

- Create and implement a sustainable finance strategy underpinned by six fundamental pillars and with measurable time-bound targets to drive resilient economies. This strategy should be at least in line with, or more ambitious than, national agendas on climate change and sustainable development.
- Elevate sustainability to a core part of corporate strategy that has full board-level oversight and focus from senior management, by including it in remuneration criteria and other corporate governance practices.
- Disclose sustainable finance practices and risk exposures using the recommended indicators and in alignment with TCFD for climate-related issues, to be accountable to stakeholders and enable shareholders to benchmark relative sustainability performance.
- Collaborate with stakeholders, such as regulators, banking associations and NGOs, to enhance capacity on sustainable finance, jointly develop sustainable banking guidelines and impact measurement/frameworks/methodologies, and create industry-wide change and a level playing field.



- Participate in relevant multi-stakeholder initiatives for the banking sector to demonstrate commitment by setting ambitious targets for ultimate alignment with SDGs and the Paris Agreement, stay abreast of sustainable finance developments and benefit from peer-to-peer learning.

#### **WE RECOMMEND ASEAN CENTRAL BANKS AND BANKING ASSOCIATIONS:**

- Facilitate ESG integration in the banking sector by establishing prescriptive, time-bound, enforceable national sustainable finance regulations or guidelines.
- Acknowledge that climate change and other material ESG risks could pose a systemic risk to the financial sector, providing guidelines for and mandating disclosure on these risks in line with TCFD recommendations. These guidelines should require banking clients to undertake climate risk materiality assessments and provide transition plans for relevant cases, and banks to perform environmental stress tests and assess alignment with the Paris Agreement when methodologies for climate scenario analysis are available.
- Design sustainable finance regulations in dialogue with policymakers in charge of climate change and sustainable development agendas to harness the power of the finance sector to contribute to these goals.
- Collaborate with regulators and banking associations from other ASEAN countries to harmonize ESG regulations. This will create a level playing field, ensure consistency for banks and prevent a race to the bottom in terms of sustainable finance standards.
- Support capacity-building for the banking industry by partnering with NGOs who can provide deep insights into E&S issues and create useful tools and guides.

#### **WE RECOMMEND SHAREHOLDERS OF ASEAN BANKS:**

- Engage with ASEAN banks in investment portfolios to support the five recommendations for banks listed above and use their voting power to assert influence.
- Require portfolio banks to perform and disclose results of environmental stress tests and participate in initiatives to develop methodologies for climate scenario analysis of bank loan portfolios. This will enable investors to assess the level of alignment with their own climate/ESG commitments and policies and with SDGs and the Paris Agreement, especially in light of TCFD disclosure recommendations.
- Engage with banks to require them to make public commitments using quantifiable targets to reduce their exposure to high-carbon and high-ESG-footprint activities if the clients do not have adequate time-bound transition plans in place.
- Engage with stock exchanges in the region to require sector-specific disclosure guidelines for banks that reflect the recommended standards and align with TCFD recommendations.
- Engage with regulators and banking associations to demonstrate support for their sustainable finance regulations and affirm the business case for sustainable finance.

### **WWF CAN SUPPORT THE FINANCE SECTOR BY:**

- Building capacity in banks on ESG integration and sharing expert insights into key ESG issues such as climate, water and deforestation to enable banks to meet sustainable finance regulations and contribute to sustainable development.
- Developing useful tools and guides for the banking sector that facilitate ESG integration and reflect the latest science-based positions on sustainability.
- Advocating for change and providing expert insights on E&S issues to banking sector regulators and banking associations to support their formulation of sustainable finance regulations.
- Monitoring ESG integration progress in the ASEAN banking sector by issuing annual reports on banks' disclosure and level of harmonization with ESG regulatory frameworks.
- Collaborating with investors to increase their focus on the role of their portfolio banks in the transition to a carbon- and resource-constrained world and facilitate engagement with banks in ASEAN on these topics.

### **CGIO CAN SUPPORT THE FINANCE SECTOR BY:**

- Performing analysis on listed companies and highlighting overall trends in corporate governance disclosures via comprehensive frameworks.
- Assessing the strengths and weaknesses in corporate governance in ASEAN countries through various studies on their listed companies.
- Shedding light on outstanding progress and stagnation among banks in their practices and disclosures, which is useful to regulators and policymakers.
- Raising awareness of the importance of sustainability reporting and providing thought leadership on ESG issues by organizing events, conferences and seminars.

## APPENDIX: CORPORATE GOVERNANCE ASPECTS AND ESG INTEGRATION PILLARS

ASPECTS AND INDICATORS					
CORPORATE GOVERNANCE ASPECTS	NO.	INDICATORS	ESG INTEGRATION PILLARS	NO.	INDICATORS
1) BOARD	1	Independence and qualifications of the board	1) PURPOSE	1	Relevance of sustainability to the organization and its strategy for addressing sustainability
	2	Clearly stated roles and monitoring the implementation of corporate strategy		2	Participation in commitment-based sustainable finance initiatives (BEI, Equator Principles, UNEPFI, etc.)
	3	Appointment, selection, training and re-election	2) POLICIES	3	Public statements on principles and risk appetite and aspects of ESG
	4	Remuneration and appraisal		4	Sector-specific policies
2) SHAREHOLDERS AND STAKEHOLDERS	5	Rights of shareholders	3) PROCESSES	5	Processes for assessing ESG risks in client and transactional approvals
	6	Policies on stakeholder engagement and list of stakeholder groups engaged		6	Procedures for client monitoring and engagement
	7	Stakeholder reporting and communicating mechanisms	4) PEOPLE	7	Responsibilities for ESG
3) DISCLOSURE AND TRANSPARENCY	8	Release of reports and disclosure on ESG issues		8	E&S staff competency and performance evaluation
	9	Corporate website	5) PRODUCTS	9	ESG integration in products and services
4) AUDIT AND RISKS	10	General audit function and audit on sustainability	6) PORTFOLIO	10	ESG risk assessment and mitigation at portfolio level
	11	Risk management frameworks and ESG-related risks		11	Disclosure of ESG risk exposure and targets

## CORPORATE GOVERNANCE

ASPECT 1: BOARD			
NO.	INDICATORS	NO.	SUB-INDICATORS
1	INDEPENDENCE AND QUALIFICATIONS OF THE BOARD	1	Are a majority of the directors on the board independent?
		2	Is the chairman independent?
		3	Does the bank have a term limit of nine years or less for its independent directors?
		4	Has the bank set a limit of five board seats or fewer that an individual independent director can hold at the same time?
		5	Are all executive directors of the bank serving on no more than two boards of listed companies outside of the group?
		6	Do the board members have varied qualifications and backgrounds?
		7	Is there gender and/or ethnic diversity on the board?
		8	Is there disclosure of all the directorships and chairmanships held by the directors at present and over the past three years?
2	CLEARLY STATED ROLES AND MONITORING THE IMPLEMENTATION OF CORPORATE STRATEGY	9	Are the roles and responsibilities of the board of directors clearly stated?
		10	Does the board monitor the implementation of the corporate strategy, vision and/or mission?
3	APPOINTMENT, SELECTION, TRAINING AND RE-ELECTION	11	Does the bank have a nominating committee?
		12	Are the majority of nominating committee directors independent?
		13	Do the terms of reference of the nominating committee or the criteria used in appointing new directors cover a requirement to consider sustainability?
		14	Does the bank provide training for new directors?
		15	Are all the directors subject to re-election at least once every three years?
4	REMUNERATION AND APPRAISAL	16	Does the bank have a remuneration committee?
		17	Are the majority of remuneration committee directors independent?
		18	Do the terms of reference of the remuneration committee or the criteria used in the remuneration policies cover a requirement to consider sustainability?
		19	Do the shareholders have the opportunity to approve remuneration for the directors and/or senior management?

## CORPORATE GOVERNANCE

ASPECT 2: SHAREHOLDERS AND STAKEHOLDERS			
NO.	INDICATORS	NO.	SUB-INDICATORS
5	RIGHTS OF SHAREHOLDERS	20	Do the shareholders have the right to participate in and vote at the general meetings?
		21	Are the shareholders informed of major changes that may affect the bank's market value?
		22	Are the shareholders informed of the policies and procedures related to the voting and general meetings?
		23	Does the bank vote by poll for all resolutions at the most recent AGM?
		24	Does the bank have policies to ensure the rights of minority shareholders?
6	POLICIES ON STAKEHOLDER ENGAGEMENT AND LIST OF STAKEHOLDER GROUPS ENGAGED	25	Does the bank disclose a list of stakeholder groups engaged?
		26	Are there any policies and procedures to engage stakeholders?
7	STAKEHOLDER REPORTING AND COMMUNICATING MECHANISMS	27	Does the bank have a whistleblowing policy?
		28	Does the bank allow the shareholders to raise any concerns/issues for the resolutions to discuss and vote in the general meetings?
		29	Are there reporting and resolving mechanisms when the rights of stakeholders are violated?
		30	Has the bank taken any measures to understand the views of other stakeholders (excluding shareholders)?
ASPECT 3: DISCLOSURE AND TRANSPARENCY			
8	RELEASE OF REPORTS AND DISCLOSURE ON ESG ISSUES	31	Does the bank disclose the number of days taken to release the financial results and annual reports?
		32	Does the bank have sustainability reporting?
		33	Is responsible lending mentioned in the leadership statement?
		34	Does the bank have an anti-corruption policy?
		35	Does the bank disclose the corporate structure such as the parent company, subsidiaries, and joint ventures?
		36	Does the bank disclose the ownership structure that shows the identity and shareholdings of major shareholders that hold 5% shares or more?
		37	Is there disclosure of any related party transactions (RPTs) and/or interested person transactions (IPTs)?



## CORPORATE GOVERNANCE

ASPECT 3: DISCLOSURE AND TRANSPARENCY			
NO.	INDICATORS	NO.	SUB-INDICATORS
9	CORPORATE WEBSITE	38	Is the address of the bank's website provided in the annual report?
		39	Does the website have an investor relations section?
		40	Is the investor relations contact given on the website and in the annual report?
		41	Does the website have an ESG/sustainability/CSR section?
ASPECT 4: AUDIT AND RISKS			
10	GENERAL AUDIT FUNCTION AND AUDIT ON SUSTAINABILITY	42	Does the bank have a separate internal audit function?
		43	Does the bank have an audit committee?
		44	Are the majority of audit committee directors independent?
		45	Do the terms of reference of the audit committee or the criteria used cover a requirement to consider sustainability?
		46	Does the bank implement periodic audit to assess implementation of E&S policies and E&S risk assessment procedures?
		47	Is there external audit on sustainability?
11	RISK MANAGEMENT FRAMEWORKS AND ESG-RELATED RISKS	48	Does the bank disclose key risks and how these risks are assessed and managed?
		49	Does the bank identify ESG-related risks?
		50	Are there policies or frameworks to evaluate and improve risk management?
		51	Does the bank periodically review the E&S policies and procedures?

## ESG INTEGRATION

PILLAR 1: PURPOSE			
NO.	INDICATORS	NO.	SUB-INDICATORS
1	RELEVANCE OF SUSTAINABILITY TO THE ORGANIZATION AND ITS STRATEGY FOR ADDRESSING SUSTAINABILITY	1	Is there a clear reference to sustainability in the bank's strategy and vision?
		2	Does the bank clearly recognize that its ESG footprint extends to its business activities and portfolio?
		3	Is there a clear reference to the Sustainable Development Goals in the bank's strategy or vision?
		4	Does the bank acknowledge the importance of climate risk for society and businesses?
		5	Does the bank list local communities and/or NGOs as key stakeholders?
		6	Does the bank engage with key stakeholders to ensure that the sustainability impacts of the bank's financing activities are properly understood?
		7	Does the bank list material E&S issues that impact both the business and stakeholders?
2	PARTICIPATION IN COMMITMENT-BASED SUSTAINABLE FINANCE INITIATIVES (BEI, EQUATOR PRINCIPLES, UNEPFI, ETC.)	8	Does the bank participate in relevant commitment-based sustainable finance initiatives such as BEI, RSPO, NY Declaration on Forests, EP, UNEPFI?
		9	Does the bank engage with regulators and policymakers to support transition to a sustainable financial system or sustainable global system (energy, low carbon etc.)?
PILLAR 2: POLICIES			
3	PUBLIC STATEMENTS ON PRINCIPLES AND RISK APPETITE AND ASPECTS OF ESG	10	Does the bank have an exclusion list which includes E&S-sensitive sectors or activities?
		11	Does the bank require clients in carbon-intensive sectors to undertake climate-related risk assessment and mitigation/transition plans to ultimately align with the Paris Agreement?
		12	Does the bank exclude financing new coal-fired power plants and coal mines?
		13	Does the bank acknowledge biodiversity loss and/or deforestation risks in clients' activities?
		14	Does the bank require its clients across the board to commit to "no deforestation"?
		15	Does the bank refrain from providing products and services to clients engaged in industrial activities that have a negative impact on World Heritage Sites?

## ESG INTEGRATION

PILLAR 2: POLICIES			
NO.	INDICATORS	NO.	SUB-INDICATORS
3	PUBLIC STATEMENTS ON PRINCIPLES AND RISK APPETITE AND ASPECTS OF ESG	16	Does the bank recognize water scarcity and water pollution as risks for its clients' activities?
		17	Does the bank require its clients in high-risk sectors and geographies to do water risk assessment and commit to water stewardship?
		18	Does the bank recognize human rights risks including those related to local communities, in the activities which it finances?
		19	Does the bank require all its clients to commit to protecting human rights (e.g. supporting the UNGP)?
		20	Does the bank recognize labour rights and occupation health and safety as risks across all sectors?
		21	Does the bank require all its clients to adhere to ILO standards or an equivalent?
		22	Are the bank's E&S requirements applicable to businesses/divisions beyond lending (e.g. capital markets, asset management)?
4	SECTOR-SPECIFIC POLICIES	23	Does the bank have sector policies or sector-specific requirements for ESG-sensitive industries e.g. agri commodities, energy and mining, seafood, infrastructure?
		24	Does the bank disclose all its sector policies?
		25	Do all the bank's sector policies state E&S requirements or recommendations based on international standards for good E&S practices (e.g. IFC Performance Standards, RSPO, FSC etc.)?
PILLAR 3: PROCESSES			
5	PROCESSES FOR ASSESSING ESG RISKS IN CLIENT AND TRANSACTIONAL APPROVALS	26	Does the bank use some standardized frameworks for client/transaction E&S risk assessment e.g. due diligence lists, questionnaires, scoring tools or use of third-party assessment?
		27	Does the bank assess capacity, commitment and track record of clients in relation to sustainability as part of its E&S risk assessment process?
		28	Is there an escalation mechanism for more complex or controversial cases?
		29	As part of the approval process does the bank classify its clients and transactions based on E&S risk assessment?
		30	Do the E&S risk assessment outcomes influence transaction and client acceptance decisions?

## ESG INTEGRATION

PILLAR 3: PROCESSES			
NO.	INDICATORS	NO.	SUB-INDICATORS
6	PROCEDURES FOR CLIENT MONITORING AND ENGAGEMENT	31	Does the bank require all medium- and high-risk clients to implement time-bound E&S action plans?
		32	Does the bank monitor clients' compliance with the agreed E&S action plans?
		33	Does the bank perform periodic reviews of its clients' profiles on E&S?
		34	Does the bank disclose how it deals with non-compliance by existing clients with the bank's policies and with the agreed E&S action plans?
PILLAR 4: PEOPLE			
7	RESPONSIBILITIES FOR ESG	35	Is there senior-management-level oversight of ESG integration?
		36	Do senior management's responsibilities include overview of climate change risks and opportunities impacting the bank's financing activities?
		37	Does the bank disclose the responsibilities of various departments or committees involved in ESG implementation?
		38	Does the bank assign E&S issues to three lines of defence?
8	E&S STAFF COMPETENCY AND PERFORMANCE EVALUATION	39	Does the bank have a dedicated ESG team to implement E&S policies and procedures?
		40	Does the bank train its staff about E&S policies and risk management processes?
		41	Does the bank have special training for its senior management to ensure sustainability flows into the bank's strategy and leadership?
		42	Is advancing the sustainability agenda part of the staff's KPIs/appraisal process?
PILLAR 5: PRODUCTS			
9	ESG INTEGRATION IN PRODUCTS AND SERVICES	43	Does the bank have specific products and services that support the mitigation of E&S issues e.g. climate change mitigation and adaptation, water scarcity and pollution, deforestation etc. (e.g. green bonds, clean energy, energy efficiency, impact financing)?
		44	Does the bank integrate E&S factors into capital allocation for existing mainstream products and for client selection (e.g. specified pools of loan capital for low carbon or green sectors or sustainability leaders)?
		45	Does the bank hold client outreach to share E&S knowledge and impact sustainability performance of clients (e.g. joint workshops on E&S topics)?

## ESG INTEGRATION

PILLAR 6: PORTFOLIO			
NO.	INDICATORS	NO.	SUB-INDICATORS
10	ESG RISK ASSESSMENT AND MITIGATION AT PORTFOLIO LEVEL	46	Does the bank periodically review its portfolio exposure to E&S issues (e.g. deforestation or human rights risk across the portfolio)?
		47	Does the bank specifically review its portfolio exposure to climate-related risks and disclose methods used?
		48	Does the bank have a strategy to identify, assess and mitigate climate-related risks of its portfolio (e.g. energy sector)?
11	DISCLOSURE OF ESG RISK EXPOSURE AND TARGETS	49	Does the bank disclose its loan exposure by industry sector?
		50	Does the bank disclose the alignment of its portfolio with scientific scenarios (e.g. 2°C climate scenario) and international agreements for sustainability?
		51	Does the bank disclose the composition of its energy loan portfolio (i.e. fossil fuel versus wind, hydro, solar etc.)?
		52	Does the bank disclose 2°C alignment or carbon intensity of its portfolio by sector?
		53	Does the bank disclose its client/transaction E&S assessment results e.g. no. of assessed transactions, no. escalated, no. approved, no. approved with qualifications?
		54	Does the bank disclose the percentage of its soft commodities clients that have time-bound plans to achieve 100% certification using multi-stakeholder sustainability standards?
		55	Does the bank disclose what percentage of its portfolio is covered by cross-cutting commitments e.g. “no deforestation”, “no exploitation”, water risk assessments?
		56	Does the bank disclose the percentage of its clients that are not meeting their time-bound E&S action plans?
57	Does the bank set goals to ultimately align with SDGs and the Paris Agreement, and measurable annual targets to reduce high risk E&S exposure (e.g. reduction in exposure to certain sectors such as fossil fuels or certain issues such as high-carbon-emitting companies)?		



# ABBREVIATIONS

<b>ABM</b>	Association of Banks in Malaysia	<b>NCG</b>	National Committee for Governance
<b>ABS</b>	Association of Banks in Singapore	<b>NEM</b>	New Economic Model (Malaysia)
<b>ADB</b>	Asian Development Bank	<b>NESDB</b>	National Economic and Social Development Board (Thailand)
<b>ASEAN</b>	Association of Southeast Asian Nations	<b>OECD</b>	Organisation for Economic Co-operation and Development
<b>BAP</b>	Bankers Association of the Philippines	<b>OJK</b>	Indonesian Financial Services Authority
<b>BEI</b>	Banking and Environment Initiative	<b>PROPER</b>	Program for Pollution Control, Evaluation and Rating
<b>BNM</b>	Bank Negara Malaysia	<b>PSE</b>	Philippine Stock Exchange
<b>BOT</b>	Bank of Thailand	<b>RPT</b>	Related party transaction
<b>BSP</b>	Bangko Sentral ng Pilipinas	<b>RSPO</b>	Roundtable on Sustainable Palm Oil
<b>CSR</b>	Corporate social responsibility	<b>SASB</b>	Sustainability Accounting Standards Board
<b>E&amp;S</b>	Environmental and social	<b>SBV</b>	State Bank of Vietnam
<b>EP</b>	Equator Principles	<b>SC</b>	Securities Commission Malaysia
<b>ESG</b>	Environmental, social and governance	<b>SDGs</b>	Sustainable Development Goals
<b>FSB</b>	Financial Stability Board	<b>SEC</b>	Securities and Exchange Commission
<b>FSI</b>	Financial services institution	<b>SEF</b>	Sustainable Energy Finance (Philippines national initiative)
<b>FSMP</b>	Financial Sector Master Plan	<b>SEP</b>	Sufficiency Economy Philosophy (Thailand)
<b>FTSE</b>	Financial Times Stock Exchange, part of the London Stock Exchange	<b>SET</b>	Stock Exchange of Thailand
<b>GHG</b>	Greenhouse gas	<b>SGX</b>	Singapore Exchange
<b>HLEG</b>	European Commission High-Level Expert Group on Sustainable Finance	<b>SMEs</b>	Small and medium-sized enterprises
<b>HOSE</b>	Ho Chi Minh City Stock Exchange	<b>SRI</b>	Sustainable and Responsible Investment (Malaysia)
<b>IEA</b>	International Energy Agency	<b>SSC</b>	State Securities Commission
<b>IFC</b>	International Finance Corporation	<b>SSE</b>	UN Sustainable Stock Exchange
<b>IIRC</b>	International Integrated Reporting Council	<b>TBA</b>	Thai Bankers' Association
<b>INDC</b>	Intended Nationally Determined Contribution – a country's pledged climate actions toward meeting the Paris Agreement	<b>TCFD</b>	Task Force on Climate-related Financial Disclosures
<b>ILO</b>	International Labour Organisation	<b>UNEP FI</b>	United Nations Environment Programme Finance Initiative
<b>IPCC</b>	Intergovernmental Panel on Climate Change	<b>UNFCCC</b>	United Nations Framework Convention on Climate Change (UNFCCC)
<b>IPT</b>	Interested person transaction	<b>UNGP</b>	United Nations Guiding Principles on Business and Human Rights
<b>ISPO</b>	Indonesian Sustainable Palm Oil	<b>VNBA</b>	Vietnam Banks Association
<b>MAS</b>	Monetary Authority of Singapore		
<b>MCCG</b>	Malaysian Code on Corporate Governance		

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