



PROPOSAL

ASEAN SUSTAINABLE BANKING PRINCIPLES

*Prepared by the State Bank of Vietnam
Technical guidance from the International Finance Corporation-
supported Sustainable Banking Network*

Contributions by ASEAN Central Banks

Hanoi, September 2020

Table of contents

Introduction	1
1. The concept of Sustainability	3
2. Rationale for the ASEAN Sustainable Banking Principles	4
3. The ASEAN Sustainable Banking Principles	6
4. The expected outcome at ACGM	11
Reference	12

Introduction

Within the context of financial sector regional partnerships, ASEAN member countries have actively developed and implemented various sustainable finance initiatives to enhance the region's reputation and position in the global economy while also turning regional initiatives into national programs with specific tangible benefits. As such, a number of ASEAN financial sector initiatives have delivered important impacts to enable member countries to leverage and maximize regional collaboration in the attraction and utilization of external resources to drive economic and administrative reforms as well as enhance institutional structures to realize a business and investment-enabling environment at national level.

“A *Cohesive and Responsive ASEAN*” is proposed by Vietnam as the key theme of ASEAN 2020, comprised of five main elements: (i) advance ASEAN's active role and contribution to the maintenance of regional peace, security and stability, (ii) promote regional connectivity and integration, heighten ASEAN's responsiveness and harness opportunities arising from the 4th Industrial Revolution, (iii) foster ASEAN's sense of community and identity, (iv) advance partnerships for peace and sustainable development with countries around the world and (v) improve the responsiveness and operational effectiveness of ASEAN. The key ASEAN 2020 theme for the finance and banking sector is Cohesiveness - Inclusiveness - Responsiveness. Thus, sustainable finance is one of the key deliverables of the ASEAN 2020 partnership within the finance and banking sector.

To help realize this objective, “**The ASEAN Sustainable Banking Principles**” initiative is supported by Vietnam's Prime Minister to be one of the crucial areas of finance and banking cooperation and partnership among ASEAN 2020. These principles have been developed to guide future related policies and commitments among ASEAN central banks to promote sustainable banking across ASEAN members. This initiative is an exciting new milestone for the ASEAN banking sector's advancement towards sustainable financial sector development.

“**The ASEAN Sustainable Banking Principles**”, initiated by the State Bank of Vietnam - with technical guidance from the International Finance Corporation (IFC)-supported Sustainable Banking Network, are developed in line with global emerging sustainable finance standards and industry practices as well as recent findings from the research on “The Roles of ASEAN Central Banks in Managing Climate and Environment-related Risks”.

This proposal is comprised of four main parts:

- Part 1: The concept of Sustainability
- Part 2: Rationale for the ASEAN Sustainable Banking Principles
- Part 3: Proposed ASEAN Sustainable Banking Principles. Each principle will be structured by its rationale and main implementation commitments
- Part 4: The expected outcome for Endorsement of the Proposal at the upcoming ASEAN Central Bank Governors' Meeting (ACGM) (on 2nd October 2020).

The proposal was first presented at the ASEAN Senior Level Committee (SLC) on Financial Integration on Feb 22, 2020 in Hanoi. SLC endorsed the initiative towards the ASEAN Sustainable Banking Principles and requested SBV to circulate the proposal to SCL members for further review and detailed feedbacks on a non-objection basis. SBV received comments from BNM and BI and this revised proposal incorporated BNM and BI comments.

The SLC seek for ASEAN Central Bank Governors to endorse the initiative of ASEAN Sustainable Banking Principles and task the SLC to finalize and launch the Principles, which will serve as reference for individual ASEAN Central Banks in their sustainable banking agenda.

The State Bank of Vietnam wishes to warmly acknowledge the valuable inputs from all members in developing this Proposal.

1. The concept of Sustainability

In 1987, in the "Our Common Future" report by the United Nations World Commission on Environment and Development (WCED) (known as the "Brundtland Report"), "sustainable development" was defined as: "Sustainable development is development that meets the needs of the present without compromising the ability of future generations to meet their own needs". The goal of sustainable development is economic and environmental stability. This can only be achieved through integrating economic, environmental and social issues through the decision-making process at all levels.

The United Nations Environmental Programme Finance Initiative (UNEP FI) defines "sustainable finance" as involving considerations of environmental, social, governance and economic issues in the decision-making process, as illustrated in Figure 1:

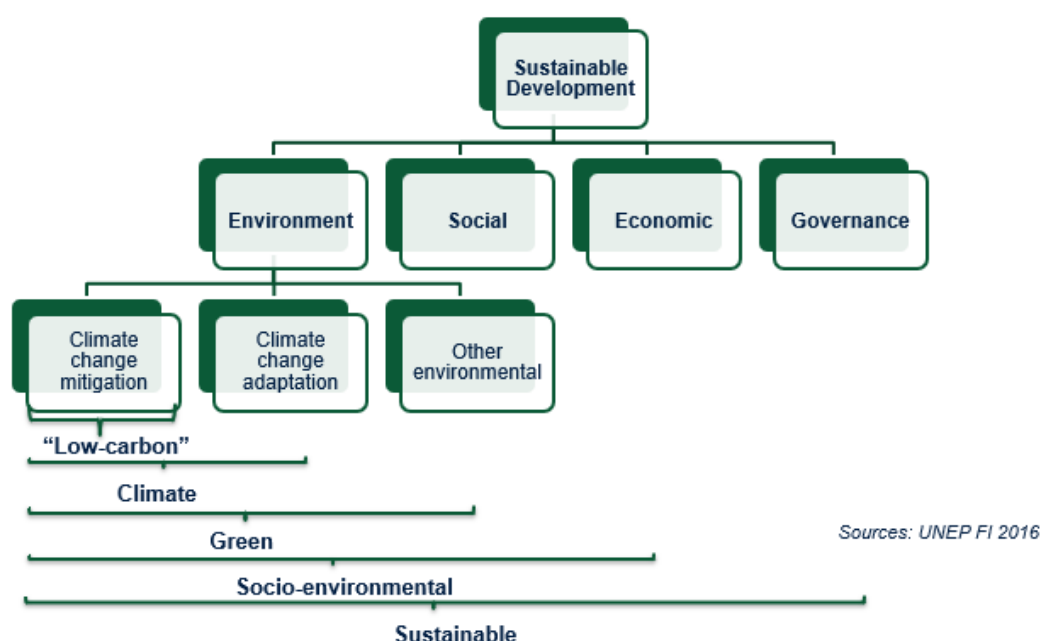


Figure 1: Definitions of Sustainable Development - Source: UNEP FI

The European Union Sustainable Finance Action Plan defines "sustainable finance" as generally referring to the process of taking due account of environmental and social considerations in investment decision-making, leading to increased investments in longer-term and sustainable activities. More specifically, environmental considerations refer to climate change mitigation and adaptation, as well as the environment more broadly and related risks (e.g. natural disasters). Social considerations may refer to issues of inequality, inclusiveness, labor relations, investment in human capital and communities. Environmental and social considerations are often intertwined, as especially climate change can exacerbate existing systems of inequality. The governance of public and private institutions, including management structures, employee relations and executive remuneration plays a fundamental role in ensuring the inclusion of social and environmental considerations in the decision-making process.

In the "Guide to Banking and Sustainability" issued by UNEP FI in 2016, it refers to three aspects of sustainable banking:

- (i) Addressing sustainability issues requires responsibilities and actions to be taken at all levels and across all the key functions of banks.
- (ii) A sustainable bank is one that not only understands and manages the risks that arise because of sustainability issues, but also perceives the strategic dimension of these issues. This means thinking ahead about business implications and opportunities brought by the increasingly pervasive environmental, social and developmental challenges of our time.
- (iii) Communicating and engaging - within the bank, with peers and with stakeholders - is critical to embracing something as complex and as vital as sustainability issues.

At ASEAN, the Indonesia Financial Services Authority (OJK), defines sustainable finance as “comprehensive support from the financial service industry to achieve sustainable development resulted from a harmonious relationship between economic, social and environmental interests”¹

Upon reviewing the various international definitions and initiatives on sustainable development and sustainable finance, the State Bank of Vietnam is proposing that sustainable banking, as enshrined by the proposed Sustainable Banking Principles, in ASEAN should cover two important aspects of business operations:

- (i) **Risk management:** Integrate environmental, **climate-related, social and governance** risks into lending considerations to avoid or mitigate financial losses, reputational risk or harm to the environment and people. Increasingly, a growing number of markets also recognize climate risk as a standalone factor impacting performance of lenders and borrowers.
- (ii) **Business opportunities:** Support lending to **investment in** businesses that are **sustainable**, environmentally friendly and socially responsible, a rapidly growing trend in line with a global commitment to increase funding for **sustainability solutions**.

2. Rationale for the ASEAN Sustainable Banking Principles

The ASEAN region faces numerous and intensifying environmental and social challenges, ranging from climate change to transboundary haze pollution. Impacts are being witnessed across the region, such as Vietnam’s Mekong Delta facing saline intrusion and prolonged flooding impacting on agricultural production, while 2015’s forest fires in Indonesia led to widespread environmental damage, health costs and economic losses. In its 2018 progress report, the Network for Greening the Financial System (NGFS) pointed out that “climate-related risks are a source of financial risk. It is, therefore, within the mandates of central banks and supervisors to ensure the financial system is resilient to these risks”. As a manager of the banking system, ASEAN central banks play an important role in encouraging banks to manage risks related to climate, environment and society, as well as to innovate and invest in new sectors and technologies, as part of their sustainable finance journey.

At a global level, UNEP FI issued the "Guide to Banking and Sustainability" in 2016 as a tool to help banks, banking associations and banking regulators to understand and promote sustainability, champion banks’ roles in preserving the banking system’s safety and soundness vis-a-vis environmental and social risk drivers.

¹ <https://ojk.go.id/sustainable-finance/id/Default.aspx>

In its comprehensive report of 2019, the Network for Greening the Financial System (NGFS) made recommendations to the central banks to implement measures to cope with climate risks, one of the drivers of financial risks. Some recommendations related to: (i) integrating climate-related risks (including physical and transition risks) into prudential supervision, including engaging with banks to ensure that climate-related risks are understood and discussed at board level, considered in risk management and investment decisions and embedded into banks' strategies, (ii) incorporating elements of sustainability into banks' portfolio management, (iii) supporting the development of a taxonomy of green or sustainable economic activities and (iv) encouraging banks to implement recommendations of the Task Force on Climate-related Financial Disclosures (TCFD). These are also core principles of sustainable banking.

The 2019 Global Progress report and 30 country reports of the Sustainable Banking Network (SBN) found that 22 SBN member countries have market-wide guidelines in place for banks to manage risks to the environment and communities that arise from projects they finance. A number of countries have developed definitions and guidelines for green loans in addition to green bonds. SBN recommendations included: (i) embed environmental, social and governance (ESG) and climate risk management, green and climate-finance targets into financial operations, (ii) establish robust reporting and monitoring frameworks, (iii) understand and manage climate risks and (iv) support behavior change of financial institutions through capacity building.

In the joint statement of the 5th ASEAN Finance Ministers and Central Bank Governors' Meeting in Chiang Rai, Thailand (April 2019), the Ministers of Finance and Governors of the ASEAN Central Banks agreed on "the important role that banks play in the allocation of resources. Banks' intermediation has helped promote growth and stability for ASEAN economies." They also encouraged "the banking community of ASEAN to gradually adopt the principles of sustainable finance into business practices."

In the ASEAN Vision to 2025, ASEAN countries recognized the importance of sustainable development as an integral part of the regional growth strategy. Protecting the environment and natural resources will support economic growth and vice versa, hence the banking industry has a pivotal role to play in promoting environmental and natural resources protection. Therefore, a set of Sustainable Banking Principles for the ASEAN region that incorporate the management of environmental, social and climate impacts will help achieve this goal, towards sustainable development of the region.

In addition, ASEAN nations Cambodia, Indonesia, Laos PDR, the Philippines, Thailand and Vietnam are now members of the IFC-supported SBN, while Malaysia, Singapore, Thailand, Cambodia and Indonesia are members of the NGFS. These countries have been, or are, developing national sustainable finance roadmaps, principles and guidelines.

In a recent research report on the Roles of ASEAN Central Banks in Managing Climate and Environment-related Risks,² the ASEAN Task Force indicated that central banks play an important role in managing and responding to climate and environmental-related risks. ASEAN central banks are aware that climate-related risks represent a key source of risks. Moreover, it is stated that key challenges ASEAN financial industry faced in coping with climate change are lack of common taxonomy, standards or principles; lack of data and technical expertise and existing structural barriers in obtaining capital for green projects. The Task Force also suggests seven strategic themes

² Conducted by the ASEAN Task Force comprising nine ASEAN Central Banks

to manage climate and environment-related risks, including: (1) Capacity building and awareness, (2) Central bank leadership; (3) Regulatory and Supervisory Framework, (4) ASEAN Green Map; (5) ASEAN Voice, (6) Surveillance and Assessment framework and (7) Communication strategy. More specifically, it is recommended that ASEAN central banks should integrate climate and environment-related risks in the monitoring and supervision. More important, the Task Force suggests to "undertake a study to consider the development of a roadmap or an "ASEAN Green Map" to ensure a comprehensive development and unified efforts across banking and insurance, the capital market and ancillary services". Those recommendations lead to the need of a set of sustainable banking principles standardizing the related practices across ASEAN members. In response, a common guidance is essential to put these critical issues into practice at financial institution level and will raise ASEAN voice at international platforms of sustainable finance.

Therefore, the development of the ASEAN Sustainable Banking Principles will create a common policy framework for the whole region and act as guiding principles to help ASEAN central banks develop further sustainable banking guidelines and tools aligned with each country context.

3. The ASEAN Sustainable Banking Principles

3.1. Objectives of the ASEAN Sustainable Banking Principles

The ASEAN Sustainable Banking Principles are developed to:

- (i) Provide general principles of sustainable banking for banking systems in member countries.
- (ii) Guide members' banking systems to formulate sustainable banking guidelines and implementation roadmaps.
- (iii) Contribute to implementation of the sustainable economic development goal of the ASEAN Economic Community (AEC) Blueprint 2025.

3.2 Applicability of the ASEAN Sustainable Banking Principles

The ASEAN Sustainable Banking Principles are voluntarily applicable to the banking system of each ASEAN member country. As the banking industry is part of financial sector, implementation of these principles, therefore, should align with the related ASEAN principles and commitments for financial sector (e.g. capital market, insurance). Implementation of the Principles at each ASEAN member country can be further guided by its banking regulator to align with its related legal framework, international and national commitments and context of development.

3.3. ASEAN Sustainable Banking Principles

3.3.1. Principle 1: Business strategy should align with and contribute to individuals' needs and society's goals, as expressed in the Sustainable Development Goals (SDGs), the Paris Climate Agreement and relevant national and regional frameworks.

a. Rationale

Business strategy plays an important role in the survival and development of a bank. To become a sustainable bank, its business strategy should be aligned with the SDGs and climate change targets, especially Nationally Determined Contributions (NDCs), while lending policies should have a positive effect on the environment, climate and society.

Moreover, financial inclusion is an important factor in achieving sustainable banking goals. The bank should develop plans to promote financial inclusion to ensure customers of different backgrounds and levels have access to banking products and services.

b. Key elements of the Principle

- The bank develops and implements a business strategy embedding sustainability as core business practices; hence business vision, mission, goals, plans, processes and product/service development are targeted to meet the needs of society, environment and climate;
- A sustainable banking mandate, built on knowledge pertaining to the needs of respective stakeholders that the Bank serves, is integrated into the bank's vision, mission, business plan, processes and product development programs;
- In the development of products and services, the Bank refers to available sustainability indicators or develops sustainability indicators to assess impact of its portfolio/products/services;
- The bank builds innovative banking products and services to support business activities with positive environmental, climate and social impacts;
- The bank endeavours to build a sustainable portfolio, which include green/climate-related/social impact portfolio and to set quantitative targets for increasing portfolio share for sustainable lending and investment;
- The bank develops a plan to implement its financial inclusion strategy to ensure customers have access to banking products and services, especially those disadvantaged in society.

c. Relevant international standards/guides

- Principles for Mainstreaming Climate Change³
- ICMA Green Bond Principles
- Green Loan Principles
- Climate Bond Initiative
- ASEAN Green Bond/Social Bond/Sustainability Bond Standards⁴
- Global Partnership for Financial Inclusion, G20 Financial Inclusion Indicators
- Alliance for Financial Inclusion
- Maya Declaration on Financial Inclusion
- ASEAN related targets and frameworks such as ASEAN Socio-Cultural Community Blueprint 2025 and ASEAN Community Vision 2025.

3.3.2. Principle 2: Implement robust risk management framework to manage environmental climate-related, social and governance risks

a. Rationale

As environmental, climate, social and governance issues are inherent in client/investee operations, almost all bank transactions are exposed to some degree of environmental, climate, social and governance risk. Considering those risks as part of the risk management process for transactions helps a bank to decrease its exposure to overall risk and contributes to its long-term financial viability. There is a clear business case for banks to establish a management system that incorporates environmental, climate, social and governance risks into their overall approach to risk management.

b. Key elements of the Principle

³ A large coalition of the world's leading financial institutions have signed the five voluntary Principles, which support and guide financial institutions in the process of adapting to and promoting climate smart development. They were launched in 2015 under the umbrella of the World Bank.

⁴ <https://www.theacmf.org/initiatives/sustainable-finance/list-of-issued-asean-green-social-and-sustainability-bonds>

- The bank has in place appropriate governance framework to ensure effective oversight of sustainable business strategies and objectives and management of environmental, climate-related, social and governance risks.
- The bank has in place adequate internal policies, procedures and tools to identify, measure, manage, monitor and report on environmental, climate-related, social and governance risks throughout lending/financing/investment activities at transaction and portfolio levels.
- The bank has in place appropriate information system and data collection solutions to track, manage, monitor and report on environmental, climate, social and governance risks.

c. Relevant international standards/guides

- IFC Performance Standards⁵
- United Nations Guiding Principles for Business and Human Rights⁶
- OECD Guidelines for Multinational Enterprises⁷
- World Bank Group Environmental, Health and Safety Guidelines
- Equator Principles
- ISO 14001 - Environmental Management
- Guiding Principles for Business and Human Rights: Implementing the United Nations “Protect, Respect and Remedy” Framework.⁸

3.3.3. Principle 3: Assess and manage impact of internal banking operations on environmental and climate-related, social and governance risks

a. Rationale

The bank itself is also a business unit, so its operational activities will impact the environment, society and be impacted upon by climate change. Therefore, to achieve sustainable banking, it is essential to manage and minimize the effects of banking operation footprints on the environment, climate and the society. This will ensure the goals and core values of sustainable banking are integrated and reflected in a consistent and transparent manner within products and services provided to customers as part of bank internal operations.

b. Key elements of the Principle

The bank should effectively and efficiently manage its assets and physical resources through:

- Developing and implements a sustainable operating strategy to manage and minimise the impact of its banking operation footprints on the environment, climate and the society e.g. improving energy and water consumption, minimising waste, switching to clean energy sources and recycling materials where feasible.
- Endeavoring to contribute towards environmental protection and community development activities and supports similar initiatives by other stakeholders.

c. Relevant international standards/guides

- Knowledge Hub of the Task Force on Climate-related Financial Disclosures (TCFD)⁹
- CDP, formerly the Carbon Disclosure Project¹⁰
- Water Footprint Network, the Water Footprint Assessment Manual¹¹

⁵ www.ifc.org/performancestandards

⁶ www.unglobalcompact.org/library/2

⁷ <http://mneguidelines.oecd.org/themes/human-rights.htm>

⁸ www.unglobalcompact.org/library/2

⁹ <https://www.tcfhub.org/>

¹⁰ <https://www.cdp.net/en/guidance/guidance-for-companies>

¹¹ https://waterfootprint.org/media/downloads/TheWaterFootprintAssessmentManual_2.pdf

- Forest Stewardship Council (FSC) rules and methods guiding the certification of sustainable paper and paper products¹²
- Universal Standards for Social Performance Management (manual of best practices for microfinance)¹³

3.3.4. Principle 4: Strengthen governance and human resource capacity towards sustainable banking

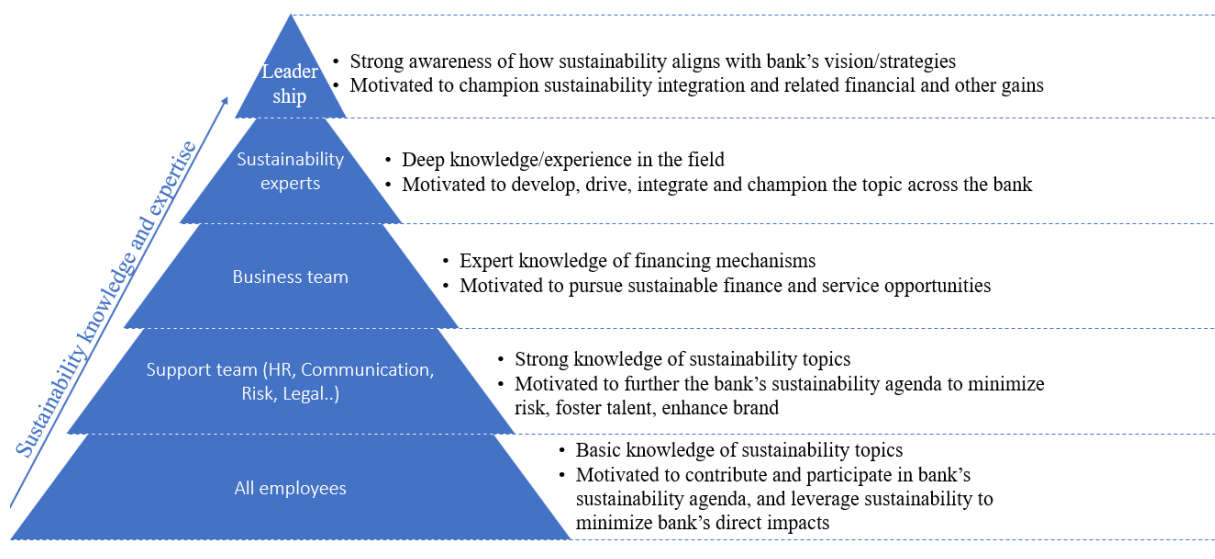
a. Rationale

Governance framework and human resources are important factors to ensure the success of the bank's sustainable development strategy, which should include not only those at operational level that directly conduct bank business activities, but also senior management and leadership who should play the driving role in sustainable banking implementation. This will ensure the bank has sufficiently qualified human resources to develop and implement sustainable banking strategies throughout its system.

b. Key elements of the Principle

To ensure resources for sustainable banking implementation, the bank must:

- Establish a clear governance structure for sustainability, including clear and specific roles and responsibilities at the Board level, senior management and across all functions to ensure adequate resource allocation and accountabilities to achieve the sustainable banking goals and targets.
- Develop and implement a competency framework encompassing technical knowledge, specific expertise and necessary skills will be required at each position/role to support the implementation of the sustainable banking strategy.
- Effectively integrate the competency framework in its training and capacity-building programs to strengthen the technical expertise/skills of existing staff and in its recruitment policy to employ professional and experienced staff with relevant sustainable banking backgrounds.
- Consider the level of knowledge and expertise required since it is varying depending on the location of each department as shown in Figure 2.



¹² <https://fsc.org/en>

¹³ <https://sptf.info/universal-standards-for-spm/start-here>

Figure 2: Sustainable Banking Knowledge required - Source: UNEP FI

- Improve the quality of human resources for sustainable banking

A bank's determination to embrace sustainable banking will be reflected by the level of enhancement to its human resources. This should be integrated not only in training and capacity-building programs to strengthen bank staff sustainable banking knowledge, but also in the recruitment of professional and experienced staff with sustainable banking backgrounds.

Sustainable banking training can be conducted periodically targeting senior leaders and down the staffing ladder.

c. Relevant international standards/guides

- IFC First for Sustainability¹⁴
- IFC Sustainability Training and E-Learning Program (STEP)
- IFC E-Learning Course on Managing Environmental and Social Performance
- UNEP FI Sustainable Finance training program (including e-learning)¹⁵

3.3.5. Principle 5: Enhance disclosure, transparency and stakeholder communication

a. Rationale

Banks today operate in an environment where their business is affected by numerous stakeholders, not just shareholders. Building a high degree of loyalty, cooperation, and mutual trust with key stakeholders through disclosure and transparency as well as dynamic stakeholder engagement can have a significant impact on its future performance¹⁶.

b. Key elements of the Principle

- The bank establishes an appropriate disclosure and transparency framework to provide key and meaningful information to its stakeholders on its sustainable banking strategy encompassing environmental, climate-related, social and governance risks.
- The bank establishes an effective stakeholder engagement and communication policy for the purpose of obtaining/ responding to feedback from relevant stakeholders to better inform and implement its sustainable banking strategy.

c. Relevant international standards/guides

- Global Reporting Initiative (GRI) standards¹⁷
- Recommendations of the Task Force on Climate-related Financial Disclosure¹⁸
- Integrated Reporting Framework of the International Reporting Council
- Sustainability Accounting Standards Board.¹⁹
- IPCC's Principles for Effective Communication and Public Engagement on Climate Change²⁰
- Beyond the Balance Sheet, IFC Toolkit for Disclosure and Transparency

¹⁴ <https://firstforsustainability.org/>

¹⁵ <https://www.unepfi.org/training/training/>

¹⁶ Beyond the Balance Sheet, IFC Toolkit for Disclosure and Transparency

¹⁷ Global standards for sustainability reporting. They feature a modular, interrelated structure and represent global best practice for reporting on a range of economic, environmental and social impacts.

<https://www.globalreporting.org/Pages/default.aspx>

¹⁸ <https://www.fsb-tcfd.org/>

¹⁹ <https://www.sasb.org/>

²⁰ <https://www.ipcc.ch/>

4. Expected outcome at ACGM

The SLC expects to achieve the following outcomes at the upcoming ACGM (on 2nd October 2020) for endorsement:

ASEAN Central Bank Governors to endorse the initiative of ASEAN Sustainable Banking Principles and task the SLC to finalize, which will serve as reference for individual ASEAN Central Banks in their sustainable banking agenda.

REFERENCES

ASEAN Community Vision 2025

Sustainable Banking Network., (2019). *Global Progress Report*.

Task Force on Climate-related Financial Disclosures, (2017). *Final Report*.

The Network for Greening the Financial System., (2018). *Progress report of 2018*.

The Network for Greening the Financial System., (2019). *Comprehensive report of 2019*.

United Nations Environment Programme Finance Initiative., (2016). *Guide to banking and sustainability*.

United Nations Environment Programme Finance Initiative., (2016). *Definitions and concepts, Background note*.

United Nations World Commission on Environment and Development., (1987). *Our Common Future Report (Brundtland Report)*.