

Sustainable Banking- International Best Practices from the Perspective of International Development Financial Institutions

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What is the EBRD?

- AAA-rated international financial institution
- The largest lender and private equity investor in Central & Eastern Europe, CIS and SEMED
- 35 local offices thru' region
- 65 countries as member states
- 29 countries of operations
- 1877 employees
- 30 billion in capital
- Since '91 financed: 3500+ projects, Euro 75 billion
- 2012 financed: over 300 projects, Euro 8.9 billion



Recent Years Expansion



- Mongolia became a country of operation - 2006
- 2008 Turkey became a country of operation
- After the Arab Spring, EBRD was asked to expand to SEMED region – Egypt, Morocco, Tunisia & Jordan



EBRD in Turkey

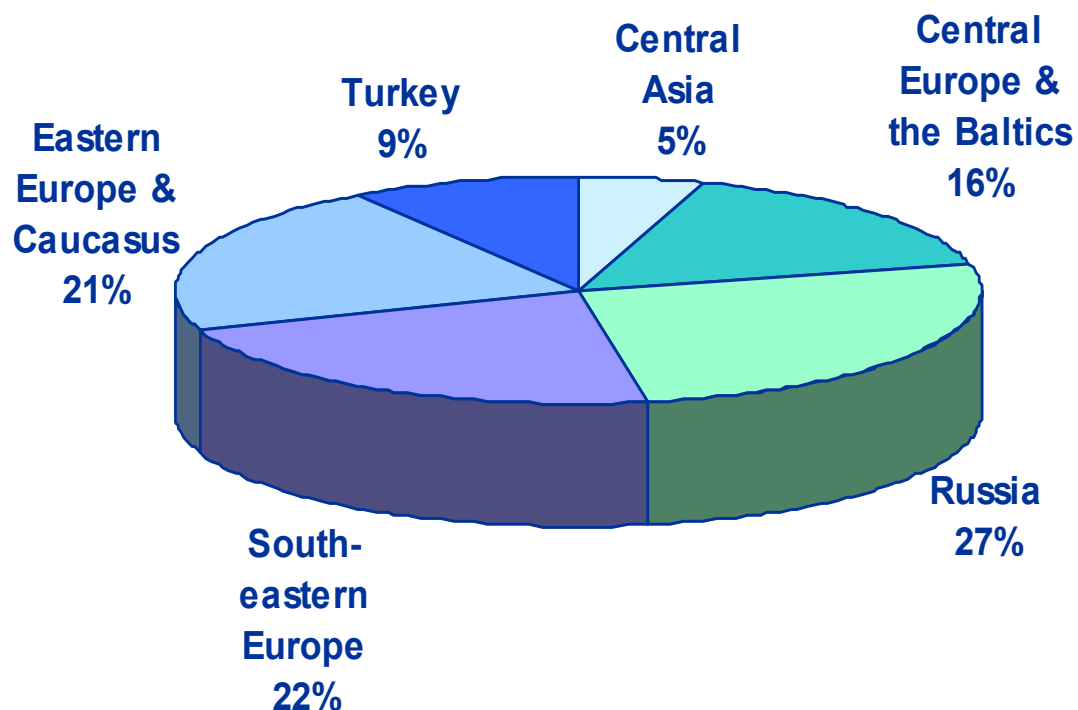
- By the end of Q3 2012 EBRD had delivered over €2.1 billion of investment to banks, enterprises and municipalities in Turkey.
- Main areas of focus for the EBRD are:
 - Sustainable energy
 - Support for micro, small and medium-sized enterprises (MSMEs)
 - Agribusiness
 - Improving utilities to residents outside of the main urban centres
 - Support for privatisation



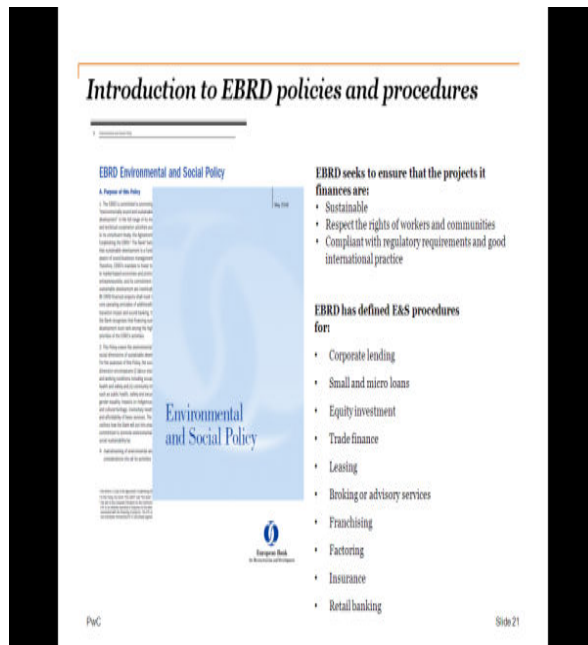
EBRD Financial Institutions Portfolio

Geographic Distribution:

Broad
coverage
across 33
countries of
operations
(including SEMED)



EBRD's Environmental and Social Policy



- Finance development which is environmentally sound, socially responsible, and sustainable in the long term
- Minimise environmentally and socially derived risks to both EBRD and its financial partners:
 - Financial - Legal -Reputational
- Ensure EBRD's investment criteria for FIs is consistent with Environmental and Social policy requirements

Performance Requirements and FIs

10 Performance Requirements

PR1: E&S Appraisal & Management

PR2: Labour & working conditions

PR3: Pollution prevention & abatement

PR4: Community Health & Safety

PR5: Land Acquisition, Involuntary Resettlement and Economic Displacement

PR6: Biodiversity Conservation and Sustainable Natural Resource Management

PR7: Indigenous Peoples

PR8: Cultural Heritage

PR9: Financial Intermediaries

PR10: Information disclosure and stakeholder engagement

Requirements for FIs are in:

PR2: Labour and working conditions



PR9: Financial Intermediaries



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Environmental and social commitments made by EBRD's financial partners

To:

- Apply relevant **FI Environmental and Social Procedures (ESMS)**
 - Compliance with the Environmental and Social Exclusion and Referral List
 - **Nominate** member of management **responsible** for environmental and social matters, including implementation of the procedures
- Conduct activities with due regard to environmental and social factors and the principle of sustainable development
- Ensure that customers comply with National Environment, Health and Safety and Labour Regulations
- Report to EBRD on the Environmental and Social Performance of FI's business
- Manage staff in accordance with national labour laws and international core labour standards

Best Practice recommendations for all FIs

- Apply PR 9 across the whole portfolio, not just EBRD-funded transactions.
- Report periodically to their external stakeholders on environmental and social issues (eg. FI Annual report, website)
- Work towards in-house environmental management (eg. Energy & resource efficiency, waste reduction and recycling).
- Adopt and implement human resources policies and practices in accordance with PR2 – Labour and Working Conditions.



Key sustainable development challenges pursued by the EBRD

- Support market transition and provide access to capital.
- More efficient use of energy and other resources.
- Replacing obsolete with modern technologies and processes.
- Introducing best industrial and resource extraction practices.
- Improving public participation in decision making.
- Supporting development of economic instruments for reform.



Environmental and Social Risks – Consequences and Opportunities

What risks do environmental issues create for financial institutions?

Financial



- Inability to make payments due to environmental costs
- Loss of value of security due to environmental impairment
- Effect on value of assets owned by bank due to environmental costs or loss of market share



- Direct liability of bank, through managerial control, for environmental damage (including taking possession of environmentally damaging assets)

Reputation



- Damage to reputation through association with polluting entities/activities of customers

- Environmental risk should also be considered at a portfolio level
- A bank should avoid overexposure to particular industries sensitive to environmental pressures



Impact of E&S issues on business

Consequences of failing to manage E&S issues

Financial costs

- Plant upgrades
- Clean up costs
- Compensation payments
- Production delays and operational disruptions
- Loss of share price and company value
- Inability to pay creditors
- In extreme cases, business failure

Legal action:

- Regulatory fines, penalties, lawsuits
- Civil action by stakeholders or other businesses
- Loss of permits and regulatory licences

Reputational damage:

- Negative media coverage and stakeholder campaigns
- Loss of customers and market share
- Loss of social licence to operate from stakeholders
- Inability to attract talented employees



Reputational Risks for banks

Reputational risks



Source: Telegraph

Protests at Royal Bank of Scotland in London
against its financing of oil sands



- A bank may suffer serious damage to its reputation as a result of association with a client who creates serious environmental and social damage.

PwC

December 2011
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Social Consequences - Example

Social consequences of Belo Monte

Indigenous groups oppose Belo Monte dam construction

Indigenous groups were among hundreds of campaigners who occupied the construction site of the Belo Monte dam in the Brazilian Amazon to demonstrate against the project.



Natives and peasants occupy Belo Monte hydroelectric project. Photo: EPA

Source: The Telegraph, 28 October 2011

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IN BRAZIL

Context

- Hydroelectric dam under construction in Brazil
- World's third largest hydroelectric dam

Consequences:

- Involuntary displacement of 16,000 people (some estimate up to 40,000)
- Impact lives of 800 indigenous people from various groups
- Expected in-migration of over 100,000 people, straining infrastructure and natural resources
- Loss of biodiversity

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Likely involuntary displacement of 16,000 - 40,00 people

Social

Change lifestyle and livelihoods of indigenous people around Xingu River

Social

Inward migration

Social

Deforestation, flooding, reduction in fish stocks

Environmental

Loss of Biodiversity

Environmental



E&S Risk Management

- Banks need to have E&S policies:
 - Capacity building and training (human and financial resources)
 - Key performance indicators/evaluation standards
 - Effective reporting to bank's shareholders, stakeholders, IFIs, etc..
- Process should be tailored to fit the bank's own business goals and organisational structure.
- Banks need to integrate a systematic approach - Environmental and Social Risk Management Systems (ESMS) - into their credit appraisal process and operations.



E&S Risk Management Benefits

- ESMS risk management improves the quality of a bank's portfolio and lowers liabilities.
- Pursuing innovative financial products generates profits in new markets with new clients.
- Contributes to improving a bank's brand value/reputation and improve community relations.
- Better access to capital from international financial institutions
- Benefits of implementation outweigh the costs.



E&S Risk Management

- IFC survey (2002): 86% reported positive changes of integrating ESMS system into their business; 19% saw changes as significant; 0% reported negative change.
- UNEPFI survey (2007): 26 financial institutions in CEE to assess the state of sustainability awareness in the finance sector. Over 90% of institutions that had implemented sustainable business practices experienced clear benefits such as reputation enhancement and cost savings. Key sustainability issues were:
 - Environmental credit risk, asset management
 - Socially responsible investment and
 - Corporate social responsibility.



Case Study: Banca Comerciala Romania

- BCR – Romania's largest bank – Government of Romania stake = 69.88%
- 2003 – Government of Romania invited EBRD and IFC to participate in a pre-privatisation strategy.
- Institutional Building Plan enhancing the bank's operational efficiency, improving processes and strengthening corporate governance.
 - Key component : building capacity in E&S management.
- IFC & EBRD provided E&S training and “A training of trainers program”.
- 2004 – BCR established an EHS unit.
- 2005 BCR provided its own training workshop on E&S risk management to BCR's loan officers.
- BCR positively influenced the environmental performance of its customers.
- 2006 - Erste Bank bought 61.8825% of the BCR shares from the Romanian Government, EBRD and IFC, paying EUR 3.75 billion.



E&S Opportunities for Growth

- There are many initiatives by the finance industry that focus on E&S issues in lending and investing and many development banks that focus on E&S issues.
- Effectively managing E&S opportunities alongside risks banks create long-term value for their business.
- Banks should be aware of the opportunities that E&S issues offer their clients, for example to improve their operational efficiencies by reducing costs
 - waste minimisation
 - energy efficiency/eco-efficiency
 - reduction in emissions and water use
- Access new markets by developing 'responsible products' such as organic or Fair Trade labelled goods.
- Enhance reputation and brand



Turkey Mid-size Sustainable Energy Financing Facility (MidSEFF)

- Financing facility, developed by EBRD.
- EUR 1,050 million in loans through Turkish banks (Akbank, Denizbank, Garanti, Vakifbank, Yapikredi and Finansbank) for on-lending to private sector borrowers, for financing mid-size investments in renewable energy, waste-to-energy and industrial energy efficiency: EUR 700 million from EBRD and EUR 350 million from the European Investment Bank (EIB).
- The project aims at boosting mid-size investments for the following type of projects:
 - mid-size (5 - 50 MW; up to 40 MW for hydropower plants - HPP) renewable energy Sub-projects;
 - energy efficiency improvements in the industrial sector;
 - private sector investments in municipal and/or industrial waste-to-energy projects;



EBRD: Turkish Sustainable Energy Financing Facility (TurSEFF)

- US\$ 285 million facility, TurSEFF, aims at supporting small-scale investments in energy efficiency and renewable energy. Under TurSEFF, which is supported by the Clean Technology Fund and the EU, long-term credit lines are provided to local financial institutions for on-lending to the private sector. The maximum loan amount is US\$ 5 million. Technical assistance is provided to both local financial institutions in the form of training and capacity building and end-user clients in the form of energy audits.
- TurSEFF results up to Q3 2012:
 - more than US\$ 230 million of sub-loans disbursed
 - 343 projects implemented, of which
 - 304 energy efficiency projects
 - 39 renewable energy projects
 - almost 800,000 tonnes of CO2 emissions avoided
 - energy savings are estimated at 275,900 toe.



EBRD Sustainable Energy Initiative (SEI)

EBRD Sustainable Energy Initiative (SEI): Scaling up finance to address climate change

- Objectives

- Scale up the EBRD's sustainable energy investments.
- Improve the business environment for sustainable investments.
- Work closely with donors to develop effective measures to address key barriers with technical cooperation and investment grants.

- Targets (2012-14)

- EBRD SEI financing target of €4.5 billion to €6.5 billion with a target total project value range of €15 to €25 billion; and
- a target CO2 emission reduction range of 26 to 32 million tonnes CO2/year

- The EBRD is the first International Financial Institution to set an emission reduction target.

More information on EBRD web-site:



Sustainability and Finance

- Financial Institutions as providers of finance have a pivotal role to play in sustainability by:
 - promoting sustainability across sectors, industries, communities.
 - improve FIs own products and services
- Managing social and environmental risks in the loan or investment appraisal process.
- Identifying opportunities for innovative products (renewable energy, energy efficiency, cleaner production, biodiversity, access to finance for women, low-income housing).



Sustainability Requirements of IFIs



Sustainability Requirements of IFIs

- Both EBRD & IFC's cooperation with banks and other financial intermediaries includes a strong emphasis on the adoption of policies and systems for environmental and social risk management.
 - Projects financed by EBRD are expected to be in line with good international practice related to sustainable development. EBRD has defined 10 Performance Requirements that cover key areas of E&S issues and impacts.
 - The IFC applies Performance Standards and Environmental, Health and Safety Guidelines to its investment projects to minimise their E&S impacts.
- The Inter-American Development Bank takes the view that *“ecosystems are critical to economic growth and poverty reduction and that the inclusion of traditionally excluded groups such as indigenous peoples, women, or those with disabilities is fundamental to meaningful development.”* It evaluates, approves and monitors each project with respect to E&S aspects.



Sustainability Requirements of IFIs

- The African Development Bank's overarching objective is to "spur sustainable economic development and social progress in its regional member countries, thus contributing to poverty reduction." To support this goal, it has policies and guidelines around E&S issues, such as an Involuntary Resettlement Policy and an Environmental Safeguards Policy.
- The Asian Development Bank aims for an Asia and Pacific region that is free from poverty. As part of this objective, it has identified the Environment as one of its five core operational areas. The ADB also uses a policy framework to address E&S risks in its projects.



Harmonisation amongst IFIs

- Improved coordination
- From projects to programs and greater institutional sustainability
- Equator Principles and promotion of Performance Standards in emerging markets
- Coordination, consistency and harmonization among development finance institutions
- Capacity building



IFI Collaboration

- FMO, IFC, EBRD, UNEPFI and other DFI partners collaborating to implement a strategy to catalyse sector-wide engagement for sustainable finance and to build local capacity.
- In selected countries, FIs and relevant government authorities come together at the highest management level to drive a locally owned sustainability agenda.
- UNEPFI/EBRD – Collaborated on several Sustainable Finance outreach events in CEE and Turkey



Environmental and Social Practices in Banks Worldwide



E&S Practices in Banks Worldwide

- There are many initiatives by the finance industry that focus on E&S issues in lending and investing.
 - The 1992 UNEP Statement of Commitment by Financial Institutions on Sustainable Development represents its signatories' recognition that economic development needs to be compatible with human welfare and a healthy environment and that to ignore this is to risk increasing social, environmental and financial costs.
 - The Equator Principles, commonly called EP, are a set of principles that act as a framework for evaluating and managing E&S risks in project finance transactions. The principles are adopted voluntarily by financial institutions and are typically applied to projects where total capital costs exceed US\$10 million.
- EBRD encourages FIs to consider joining appropriate existing international initiatives that promote best practice in the financial sector such as Equator Principles, UNEP FI and Principles for Responsible Investment



European Principles for the Environment

- EBRD and four leading Europe-based multilateral financing institutions (MFIs) signed the European Principles for the Environment declaration in May 2006.
 - EBRD, the Council of Europe Development Bank, European Investment Bank, Nordic Environment Finance Corporation, Nordic Investment Bank (NIB).
- Support environmental protection and promote sustainable development globally and across all sectors of their activities
- Joint initiative aims to harmonise environmental benchmarks used for the financing of projects.
- Promotes the EU approach to environmental sustainability and the application of EU benchmarks to projects financed by them.



Implementation support



Implementation support



- Since 1994 - over 300 + FIs trained (including Turkey: Garanti bank, Isbank, Denizbank, Vakifbank)
- 2012 – over 480 Trade Finance officers from 180 FIs
- Target audience = credit risk departments and CEOs
- Delivered by:
 - Consultants (mainly)
 - EBRD own Environment Staff
 - Training provided free of charge to FIs who need priority assistance to implement the EBRD's E&S requirements
- On-going guidance/hand-holding





EBRD ESDD Training Workshops For FIs

- Provide support to FIs wishing to address E&S issues (including Policy development)
- Training on EBRD Environmental and Social Policy and relevant Procedures/Requirements for FIs
- Potential environmental impacts of high-risk sub-projects
- Good practices for managing environmental and social risks
- Overview of relevant national regulations
- Demonstration of the EBRD tools to help manage the E&S risks : eg the EBRD Environmental and Social Risk Management Manual (E-manual) download from EBRD website.
 - Key areas:
 - Education: background information on sources of risk & key environmental risk management activities
 - Supporting Tools: reference materials including checklists, contacts, sectoral guidelines, reporting formats



EBRD'S E&S E-learning courses



Further information

- EBRD Sustainability Report 2011 – available on the Bank’s web-site
<http://www.ebrd.com/pages/research/publications/flagships/sustainability.shtml>
- Environmental and Social Risk Management Manual for Financial Institutions (E-manual)– download from EBRD website –
 - <http://www.ebrd.com/pages/about/principles/sustainability/intermediaries.shtml>
 - Key areas:
 - Education: background information on sources of risk & key environmental risk management activities
 - Supporting Tools: reference materials including checklists, contacts, sectoral guidelines, reporting formats
- EBRD Trade Finance E-Learning Programme
<http://dev.ebrd.coastlinesolutions.com/>
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