ESG on the agenda in emerging markets

Financial institutions and the sustainable transformation

The bank at your side

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Foreword

This year marks half a century since the very first global conference focusing on the impact of humanity's activities on the environment. The 1972 United Nations Conference in Stockholm sparked debate and dialogue on an international level, setting in motion what has become a worldwide effort to unite behind a common cause. Today, 50 years on, sustainable development is a primary focus across all areas of society and the economy.

To date, Europe has played a leading role in driving the ESG agenda, pioneering wide-reaching regulatory and fiscal initiatives that serve to make sustainable investment a core focus for investors, financial institutions (FIs) and businesses with a view to making the transition to a sustainable economy faster (through incentivisation) and more transparent and implementing comparable standards worldwide.

However, Europe is by no means alone in taking action, and ESG developments are not limited to the world's advanced markets – emerging markets are taking action too. Across the globe, efforts to establish effective reporting methodologies for businesses, investors and FIs are underway. Yet the sheer volume of different ESG reporting frameworks means that understanding what is required by whom, when and where, and whether disclosures are mandatory or voluntary, can be challenging.

For businesses to adapt to and succeed in an ESG-driven future, they need to be positioned with the right suite of tools to navigate the changes, overcome obstacles and capture the opportunities on offer. FIs therefore have a pivotal role in influencing and driving global sustainable development – and facilitating it by creating and delivering effective, innovative sustainable finance solutions, suited to the differing needs of stakeholders across the world.

Communication, transparency and close collaboration between banks and their clients are paramount in tailoring the solutions and support clients need to progress towards meeting their sustainability goals over time.

With our core business, at Commerzbank we want to exert influence on the sustainable development of the economy and society as a whole, give our customers fair and competent advice and steadily reduce our ecological footprint. By making sustainable investment decisions today, Commerzbank is making its commitment to the society of tomorrow.

On that note, we hope you enjoy reading our whitepaper on sustainability.

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Introduction

The global economy is in the midst of a profound shift – a transformation rooted in the concept of sustainable development. Stakeholders across the world have recognised that in order to achieve the goals of the Paris Agreement, and avoid the most severe impacts of climate change, fundamental change is needed across borders and economic sectors.

The transformation underway has gained particular urgency in recent years as the risks and costs of climate change become amply clear, and governments, corporates and financial markets are affording ever more importance to environmental, social and governance (ESG) issues. But while action is already being taken, with sustainability regulation now implemented across several key markets, strategies and pace of change will differ immensely across countries, sectors and businesses.

The increasing prominence of ESG concerns among all stakeholders is having cascading effects across supply chains and permeating beyond national borders. Government regulation and industry-wide ESG commitments made in one part of the world can have a global impact, as companies wanting to partake in international trade are required to meet the sustainability standards of their trading partners.

Reconciling sustainability goals with economic development

To differing degrees, advanced and emerging markets are being confronted with a momentous challenge: How to implement **sustainability standards**, while also achieving **social and economic progress** and **safeguarding the wellbeing** of their population.

While all countries face this dilemma, for many emerging markets, this challenge necessitates difficult decisions. These countries are rightfully looking to advance their economic development, expand their supply chains and support their growing middle-income societies. Deciding on a course of action that will maximise their potential, while managing ESG requirements, including the standards and expectations of their trading partners, is therefore exceedingly complex.

This whitepaper addresses and explores the following topics:

- What international ESG regulations have already been implemented, what is in the pipeline, and is there a difference in the approach adopted by different regions and markets?
- Why are emerging markets particularly affected by issues of sustainability, and how are they adapting to the new economic reality?
- What investments are needed to foster economic development in emerging markets while ensuring compliance with sustainability standards?
- What role can financial institutions play in financing sustainable development in emerging markets, and promoting the green transformation?

As governments and corporates alike seek ways to address issues of sustainability and work to shape their role in the rapidly changing landscape, one thing is clear: **financial institutions will be instrumental** in supporting the transition, and helping to drive an optimised future for all.

Section 1

ESG regulation: what's currently on the agenda

The ESG strategies and developments underway are being implemented in accordance with the goals of the Paris Agreement, which has been signed by almost every nation on Earth.

The Agreement sets out a framework for limiting global temperature increases to "well below" 2°C – ideally no more than 1.5°C – above pre-industrial levels by the end of the century. Countries are also encouraged to become carbon neutral by 2050. With regard to the financial sector, Section 2.1 c of the Paris Agreement specifically outlines the following:

"Making finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development".

To date, Europe has played a leading role in driving the ESG agenda, pioneering wide-reaching regulatory and fiscal initiatives that serve to make sustainable investment a core focus for investors, financial institutions (FIs) and businesses with a view to making **the transition to a sustainable economy faster** (through incentivisation) and more transparent – and implementing comparable standards worldwide.

Key examples of regulatory initiatives include the EU Green Deal, the European Climate Law, the EU Taxonomy and nation-specific projects, such as the German Climate Action Programme.

The EU is also in the process of writing up a due diligence directive, focused on improving ESG performance across the breadth of the supply chain, and is also considering extending the scope of the Capital Requirements Regulation (CRR) to include disclosures of ESG risks. Germany has already launched the German Supply Chain Law (Lieferkettensorgfaltsgesetz), coming into effect in 2023 for businesses employing more than 3000 personnel.

Europe is by no means alone in taking action, however, and ESG developments are not limited to the world's advanced markets – emerging markets are taking action too. Figure 1 gives a snapshot of some important initiatives and directives impacting the industry.

Where adopted/applicable	Policy/initiative	Details/commitments
Global (exceptions =include Iran, Eritrea, Libya, Yemen)	Paris Agreement	International climate treaty, focused on limiting global warming to 1.5°C or "well below 2 degrees" above pre-industrial levels.
Global (adopted by UN member states)	Sustainable Development Goals (SDGs)	The UN's roadmap for achieving sustainable development by 2030. The SDG Index is an assessment of all member states' overall performance on the 17 SDGs, with equal weight given to each goal.
European Union	• EU Green Deal • European Climate Law • EU Taxonomy	The European Commission's set of policy initiatives designed to make Europe climate-neutral by 2050.
United Kingdom	Climate Change Act	The UK's legally binding system commits to achieving net zero emissions by 2050 through mandatory disclosures, a UK Taxonomy based on EU regulation and the issuance of Green Gilts.
United States	Inflation Reduction Act	Among broader economic measures, the bill outlines significant investment to reduce emissions and incentivise and develop clean energy solutions.
Australia	Australia's Sustainable Finance Roadmap	Includes 37 recommendations to embed ESG into business practice, while building sustainable financial markets, with a view to enabling resilience across the nation.
Canada	Final Report by the Expert Panel on Sustainable Finance	Includes 15 recommendations falling under three pillars of Defining the Opportunity Foundations for Market Scale, and Financial Products and Markets for Sustainable Growth.
Hong Kong	Cross-Agency Steering Group on Green and Sustainable Finance	Outlines strategic focus areas to strengthen climate-related financial risk and management, promoting information flow across levels, encouraging innovation and strengthening regional and international collaboration.
China	• Belt and Road Initiative • International Green Development Coalition • Opinions on financial support for reaching peak carbon emissions and carbon neutrality	These guidelines integrate ESG principles into the policies and priorities of China's monumental infrastructure development strategy – in line with international best practices. The "Opinions" propose fiscal policy tools to support the green transition: China will reach peak emissions before 2030 and achieve carbon neutrality by 2060.
Brazil	Social, Environmental and Climate Responsibility Policy	The current government has expressed its opposition to many of Brazil's existing climate policies, and recent legislation has weakened legal frameworks that limit environmental destruction, including deforestation.
India	National Action Plan on Climate Change (NAPCC)	Outlines eight "National Missions" on climate change, renewable energy and environmental issues. India's most recent stimulus package is dedicating two-thirds of its resources to a "green recovery". However, it will also provide finance for coal projects.
Mexico	General Climate Change Law	Under the current government, ESG policies have been rolled back, with the elimination of Mexico's Climate Change Fund and the dissolution of the National Institute for Climate Change.
Turkey	• National Climate Change Strategy • National Climate Change Action Plan	Turkey is yet to pass a climate change law, and national strategy and plans only partially cover short-term climate change mitigation.
South Africa	Integrated Resource Plan	This plan marks a major shift in national electricity policy away from coal and towards renewable sources. However, the full implementation of this strategy is unclear following the disruption of the pandemic .

Figure 1: Some of the important ESG initiatives/policies of select countries or areas

ESG data and disclosure at a glance

Developments in the global spectrum of ESG regulation are being announced on a frequent basis, and many regulatory updates are focused on introducing measures for disclosure – i.e. accurate, effective collection and reporting of ESG data. Information on areas such as carbon emissions, composition of the types of energy being used, labour standards and diversity all shed light on different aspects of a company's sustainability profile. This data is naturally of interest to investors and regulators, much in the same way regular financial information is. Indeed, some disclosures are also made publicly available.

- **Reporting channels and data:** Since ESG is an umbrella term covering an array of issues, a wide spectrum of frameworks has emerged in recent years covering several reporting channels.
- **Type of disclosure obligation:** The obligation on the reporter might be voluntary, mandatory or even operate with a "comply or explain" principle to allow some flexibility. Some ESG data is self-reported by corporates, while other information is collected and reported by external organisations, such as NGOs. In general, companies with the greatest public interest are likely to have legislative or regulatory requirements and disclose the most ESG data[1]. That is not to say voluntary ESG disclosure is unpopular. Many corporates, FIs and investors – especially in the UK and EU – have participated in ESG disclosures before they were made compulsory, a transition in progress with some proposed frameworks[2].
- **Role of FIs:** FIs form a key part of reporting channels by taking on the responsibility to review corporates' ESG data, while also having their own obligations towards regulators.
- **Metrics:** Depending on the framework, a variety of metrics are used to measure businesses' ESG performance.

Reporting methodologies: Regional initiatives

Across the globe, efforts to establish effective reporting methodologies for businesses, investors and FIs are underway (see Figure 2). In April 2021, the **EU** released its Corporate Sustainability Reporting Directive (CSRD), mandating comprehensive disclosure standards to improve consistency and reliability of reporting by **corporates.** These are due to come into effect in 2023. The

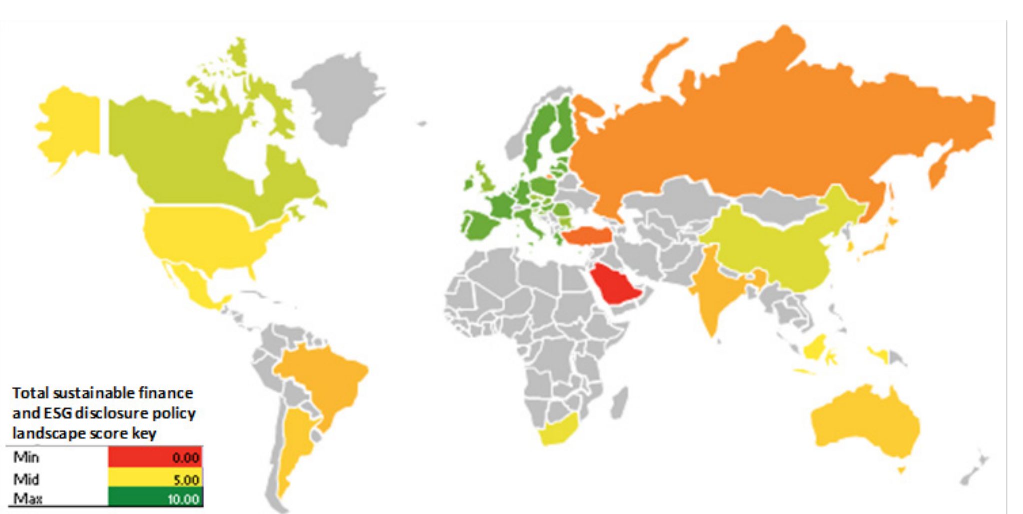


Figure 2: G20 country scores for sustainable finances and ESG disclosure policies

Source: Bloomberg NEF, 2021
The figure maps the mandatory disclosure policies of each country in the G20, scoring the regulatory landscape from zero to ten and mapped in red, amber and green. The rating was determined by looking at the scope (how much they cover) and robustness (how ambitious and guided they are) of the countries' policies, and the alliance (the level of international collaboration influencing them).

European Central Bank also published a guide on climate-related and environmental risks in 2020, explaining how banks are expected to manage and transparently disclose such risks.

Meanwhile, in March 2022, the **US** announced climate-related disclosures to provide greater transparency for **investors**, with a new set of rules proposed by the Securities and Exchange Commission (SEC). The SEC's disclosure guidelines draw heavily on the standards drawn up by the Task Force on Climate-related Financial Disclosures (TCFD), an industry body composed of both preparers and users of financial disclosures from across the G20[3].

In some developing countries, too, regulators have begun outlining sustainability disclosure requirements. Many **emerging markets** are rapidly embracing sustainable financing practices, establishing their own ESG priorities, as well as developing strategies to comply with directives imposed by advanced economies.

In the **Asia-Pacific** region, for example, ESG reporting is already well established. **Corporates** are dedicating specialist units for ESG reporting, driving high levels of ESG data disclosure[4]. In fact, research has shown that Asia-Pacific businesses are more likely than those from other regions to have in-house ESG teams, and investors here have

the highest confidence when it comes to reporting on the social side of ESG.

Standardisation initiatives

The sheer volume of different ESG reporting frameworks means that **understanding what is required by whom, when and where, and whether disclosures are mandatory or voluntary**, can be challenging. The lack of standardisation has given rise to “ESG data gaps” where information is incomplete or insufficient, in both quality and quantity[5]. Indeed, as countries implement their own methodologies and frameworks, inconsistencies across jurisdictions are complicating an already fractured sustainable finance landscape. With approximately 600 ESG reporting standards in existence across the globe, there is limited uniformity, and the need for consistency to enable reliable comparability is clear[6].

To tackle the disparity, several international initiatives have been proposed:

- The soon-to-be-introduced EU Taxonomy aims to provide a classification system that can help FIs, investors and supply chain participants understand whether certain economic activity is environmentally sustainable.
- The SFDR, ISSB and TCFD reporting standards, among other global and regional initiatives, are also playing an important role. Of course, while establishing a degree of global standardisation is important, flexibility will also be needed to account for different regional and sector requirements.

Section 2

ESG regulation: where are we heading and what is the role of emerging markets?

Why are emerging markets concerned about ESG?

Emerging markets are by no means strangers to the importance of ESG. Indeed, they are often located in geographical areas that are particularly exposed to the speed and destructive impact of climate change. They also have a vested interest in improving social and working standards. And while climate change is global, less economically developed countries can be more vulnerable to its effects due to having fewer resources to afford the goods and services they need to recover quickly and effectively from the increased and more frequently materialising physical risks of climate change.

The threats facing these markets are clear, and they require solutions – solutions that need to

ESG issues extend beyond environmental and social impacts, with financial and economic implications also clear to see. For instance, the US non-profit RAND estimates that air pollution-related health costs reduced China's labour productivity by **6.5% of GDP each year** between 2000 and 2010, thereby having significant financial implications.

In addition, climate change has led to an increased frequency of extreme weather events, which take a high humanitarian and economic toll, especially in developing countries. South America's second longest river, the Paraná, is at its lowest levels in 77 years. Running from south-east Brazil through Paraguay and Argentina, the drought has crippled trading routes and hydroelectric energy production, limiting crucial sources of income in the afflicted countries.

This first-hand exposure is leading many emerging markets more favourably towards sustainability in general. Indeed, research conducted by the Economist Intelligence Unit found a substantial shift in public sentiment towards nature in markets such as India, Pakistan and Indonesia. The study combined opinion surveys with social media, search and news analytics, finding that between 2016 and 2020 the most dramatic growth in awareness about climate change has occurred in Asia, most notably India (190%), Pakistan (88%) and Indonesia (53%)[7]. In Latin America, the volume of tweets related to nature and biodiversity soared by 136% from 2016 to 2019. The surge is explained, in part, by Twitter users in Brazil urging their government to take action on forest fires in the Amazon rainforest.

be devised, built and financed, representing a clear business opportunity that dovetails with sustainability goals.

Of course, there is no "one size fits all" approach. The diversity of the circumstances of different emerging markets demands individual, customised strategies. Two economies with similar resources may pursue different aspects of ESG. For example, one country may levy its natural river system as a conduit for international trade, creating new jobs and reinforcing social development. Another country with a strong economic reliance on tourism may invest in another form of infrastructure to manage and preserve its natural river ecosystem while promoting sustainable travel.

For middle-income economies in particular, such as Mexico, Turkey, India and China, whose industrialisation journey is already well underway, **the conundrum is especially great**. Such countries have invested in numerous non-sustainable developments to secure future economic growth prior to the sustainability agenda. If they were to abandon these to pursue only sustainable projects, a host of "white elephants" would be left in limbo – either incomplete or unable to be used. This is especially applicable to energy projects. In India alone, for example, 281 coal plants are in operation, while 28 are in the process of being built and 23 are in the pre-construction phase[8]. In addition they would eventually neglect the UN SDG 8 "Decent Work and Economic Growth".

With emerging markets' exposure to the effects of climate change, the impetus to act is all too evident. What's more, **reputational risk** is a growing concern for many businesses in relation to ESG, with awareness that negative brand publicity can have significant consequences regarding sales and investment.

Many businesses in these regions – close to the realities of the situation – are therefore building this more sustainable future; and they are already working on developing effective solutions. But importantly, **making this future a reality needs financing and support**.

It also requires coordination. With different countries on their own trajectories and with differing priorities, making sure the scope of needs is addressed is crucial to facilitating progress towards sustainability goals across the globe.

The **Sustainable Banking and Finance Network (SBFN)** was established in 2012 by the World Bank-backed International Finance Corporation (IFC), alongside 10 member countries. It brings together regulators, banking and environmental associations from emerging markets in pursuit of a common goal: advancing sustainable finance opportunities for emerging economies.

SBFN helps to facilitate the sharing of knowledge and access to support regarding the implementation of local sustainable finance initiatives. It is working to consolidate various approaches and definitions to help progress ESG reporting standardisation.

As of March 2022, the network has grown to 72 member institutions – representing 62 countries and accounting for around 86% of total bank assets in emerging markets. In early 2022 it announced plans to advance the growth of the green bond market among its members. The aim is to help emerging economies tap into the thriving climate-focused investment market, with opportunities worth an estimated US$23 trillion by 2030, according to the IFC. It has rapidly become a serious player on the global stage, setting a standard for sustainable investment initiatives.

Supply chains extend the reach of sustainable regulation

For emerging markets, membership of networks such as SBFN is becoming a growing necessity, as the pressure to implement their own ESG and climate-related regulation and adapt to the requirements of the developing economies which they rely on for trade mounts.

This is particularly important, as government regulation and industry-wide ESG commitments made in advanced economies are increasingly having ripple effects across the globe. While the regulatory focus in advanced markets has generally been on a business's own ESG performance, **in a globalised economy the effects of standards imposed in one market reverberate through the wider supply chain**. Indeed, with up to 90% of a business's environmental impact lying in its global value chain, supply chains are of particular relevance in the ESG transition[9]. As a result, businesses are increasingly evaluating their suppliers' sustainability credentials, and suppliers worldwide will therefore need to demonstrate their ESG score if they are to ensure their continued participation in global supply chains.

The global impact of the EU's Sustainable Products Initiative

The EU's 2020 Sustainable Products Initiative (SPI) is a prime example of a regional initiative with global impact. The regulation means that companies wanting to sell their products in Europe must meet tougher sustainability standards. The initiative targets high-impact product categories such as textiles, electronics, chemicals and wooden furniture. Companies involved in these supply chains will therefore need to comply with more stringent rules to continue trading with counterparties in the region.

Nonetheless, making the jump to sustainable production will require coordination across the supply chain, going beyond regulatory measures. The **EU's Strategy for Sustainable and Circular Textiles** was published in the same circular economy package as the SPI – and its ambition to make all textiles on the EU market recyclable and durable by 2030 reflects the urgent need to tackle textiles manufacturing as one of the world's most polluting industries[10]. However, many of the EU's textile imports are manufactured in emerging markets, some of which are still recovering from the pandemic. To incentivise improved sustainability standards, some European corporates are working closely with FIs to make ESG-linked supply chain financing options accessible to their suppliers[11].

Social and governance not to be overlooked

For many emerging markets, navigating the complexities of ESG reporting is only part of the challenge. When it comes to ESG regulations drawn up in advanced markets, they are often regarded by emerging markets as being too focused on environmental aspects, and not enough on the **social and governance – "S" and "G" – elements**, which are in fact the more pressing priorities in many geographies. In fact, the EU's sustainable textiles strategy has received criticism from civil society groups for failing to address key human rights issues in the supply chain[12]. Moreover, Africa is responsible for less than 4% of the world's greenhouse gas emissions[13].

It is expected that, in the near future, regulators will begin urging businesses to take a closer look at social and governance factors within their value chains. For example, complementary to the EU Taxonomy, a "Social Taxonomy" is conceivable and already being discussed – although, with social factors often more difficult to define and measure, it recently was announced that plans have been put on hold indefinitely.

The widespread disruption caused by the COVID-19 pandemic has pushed **regulation of social practices** further up government and industry agendas. In Latin America, several countries have published and indeed updated national action plans on business and human rights and associated human rights programmes, including Chile, Colombia, Mexico and Peru. However, the region does not yet have an overreaching legal framework, and individual countries are at different stages of implementing their own. Given recent regulatory engagement on this issue, companies in the region and non-governmental bodies have created voluntary initiatives along these lines, and forthcoming regulation will start to close the gaps – increasing the consequences for non-compliance[14].

Both social and environmental regulations are achieving progress on important issues, however **governance structures** represent an important foundation in emerging economies. In markets that sometimes carry associations of economic and political instability, good governance structures are crucial for participation in all aspects of the global economy. Governance measures, for example, improve the transparency of public institutions and combat corruption. They also influence the perception of risks associated with investing in certain markets and impact the expected quality of corporate governance.

Corporate governance codes and regulations have been effective in improving emerging markets' governance practices and affirming confidence in capital markets. Not only have emerging markets adopted regulations, but many have advanced their standards in recent years: China, India, Brazil and South Africa have all updated their corporate governance codes since 2016[15].

Sustainable development strategies in a nutshell

Many economies sit at a fork in the road. While global targets have been set by the Paris Agreement, specific strategies have not been enforced, meaning that individual countries can determine their own route to achieving them. The direction they choose to take, their degree of focus on ESG and the timescales adopted will have consequences for all.

Up until recently, the trajectory for many emerging markets experiencing high growth was clear: the well-trodden path to prosperity taken by advanced markets. Now, another route has emerged: a green one. And although this path is largely unexplored, strategies have emerged to achieve a more sustainable kind of development:

- **Leveraging legacy production techniques/ practices.** For instance, the traditional approach to textiles still used in Bangladesh, in which materials are all natural, could position such economies with the goods that meet evolving sustainable requirements and consumer demand.

- **Leveraging natural resources.** Emerging economies can leverage their natural resources in new ways that are less carbon-intensive – harnessing solar, wind, hydro and geothermal power and promoting sustainable tourism.

- **New sectors and solutions.** The shift to an ESG-focused global economy means demand across the world will evolve. Emerging markets can develop new solutions focused on meeting these needs rather than "the needs of old" – this positions businesses for the future. For example, as a biodiversity hotspot playing host to 20% of the world's plant and animal species, South Asia is a prime candidate for developing natural carbon capture systems – supported and protected by targeted investment programmes.

- **Circular economy.** Circular economic practices are centred around ensuring resources and products maintain their value for as long as possible while delivering a positive social impact. Emerging markets could build new business models around this concept – for example, waste often ends up at emerging market locations. It should be possible to truly recycle this and channel it back into the supply chain.

- **Leapfrogging.** For emerging markets positioned to invest in new capabilities, there is the option of doing so with ESG in mind. Instead of investing in a coal plant, for example, funds could be focused on developing renewable forms of energy such as wind farms or solar power. This approach also applies to technology. To do this, they will require support from international FIs, as well as technical know-how from major industry players to help them build up their own capacity.

- **Manufacturing relocation.** The strategic position of some emerging markets could play a role in more advanced markets relocating their manufacturing capabilities there, shortening their supply chains. For instance, the geographic location of Africa, Latin America and the Middle East – closer to advanced post-industrial economies in Europe and North America – gives countries in these regions an opportunity to benefit from shifts in globalisation and supply chain management. The disruption created by the pandemic has led many businesses to consider relocating manufacturing capabilities from further afield – China and South Asia, for example – leaving closer markets in a good position to build their manufacturing industries instead.

Section 3

The sustainability transformation: the role of financial institutions

For businesses to adapt to and succeed in an ESG-driven future, they need to be positioned with the right suite of tools to navigate the changes, overcome obstacles and capture the opportunities on offer. FIs therefore have a pivotal role in influencing and driving global sustainable development – and facilitating it by creating and delivering effective, innovative sustainable finance solutions, suited to the differing needs of stakeholders across the world.

The influence of FIs is of particular importance in emerging markets, where banks control assets worth an estimated US$50 trillion, meaning they can make a critical impact on sustainable development in these regions.

> *"A sustainable financial system is [...] one that creates, values and transacts financial assets in ways that shape real wealth to serve the long-term needs of an inclusive, environmentally sustainable economy."*
>
> United Nations Environment Programme, Inquiry into the Design of a Sustainable Financial System, 2016

A UN-backed "Call to Action", announced in late 2021, said that action by FIs was "critical", and urged for the creation of a net-zero global financial system to meet the goals of the Paris Agreement. Among its recommendations was the unlocking of trillions of climate finance, required to support developing economies in meeting the transition to net zero, and provide these markets with viable alternatives to fossil fuels through investment in infrastructure.

Green finance: falling under the umbrella of sustainable finance, the G20 Green Finance Study Group defines green finance as "focused investment that provides environmental benefits in the broader context of environmentally sustainable development". This can include reduction in pollution or greenhouse gas emissions, improved energy efficiency, or mitigation of climate-related risks.

Climate finance: refers specifically to initiatives in-line with the UN's climate change provisions. The UN's Sustainable Development Goals (SDGs) represent a roadmap for achieving sustainable development by 2030. And they remain the only common language and vision across all UN member states on a three-pronged approach to sustainable development: economic, social and environmental.

FIs' commitment to support the sustainability transition

Many FIs are embracing their role of leading by example, with ambitious goals to reduce carbon emissions from their managed assets to net zero, while directing capital into more sustainable business. Almost 115 banks, collectively controlling 38% of the financial industry's global assets, have joined the Net-Zero Banking Alliance[16], committing to net-zero emissions by 2050, for example.

As part of their strategies, they are increasingly moving away from industries and companies that aren't actively looking to forge a more sustainable path, with policy frameworks for handling environmental and social risks within their core business.

Yet, it is important to note that FIs are not seeking or expecting transformation overnight. Different industries and businesses in different geographies have their own strategies and priorities, and some will have longer, more complex transition periods than others. Various other factors also need to be considered, including the way the various components of ESG interact. A project might appear unfavourable from an "E" perspective, but have positive impacts with respect to the "S" perspective. The hydrocarbon sector, for instance, can be a valuable source of employment for a number of emerging markets[17]. Mining and manufacturing represent similar opportunities for rapid economic growth, with environmental downsides. Were FIs to completely withdraw, there would be negative social consequences for many.

That is why communication, transparency and close collaboration between banks and their clients are paramount in tailoring the solutions and support clients need to progress towards meeting their sustainability goals over time. As part of this, FIs need to use their networks, frequently collaborating with each other, to promote emission-reducing technologies through suitable financing solutions, for example. In addition, FIs can team up with governments enabling the financing of sustainable and publicly

Commerzbank ESG Framework

With its **ESG Framework**, Commerzbank strives to provide its stakeholders with the greatest possible transparency on its approach to sustainability. All of the key building blocks of the bank's sustainability strategy are outlined within the framework.

As stated in its ESG Framework, Commerzbank will not undertake the financing of:

- New coal mines
- New coal power stations
- New coal infrastructure projects
- Uranium mines
- New nuclear power stations
- Projects related to Arctic drilling, fracking, mountaintop removal, tar sands and ultra-deep-water drilling

Furthermore, it performs intensive assessments of all finance transactions and business relationships with connections to areas viewed as particularly susceptible to social and ecological risks. The findings of such analysis can result in shorter terms, higher pricing or even rejection of loan applications. Such sectors include:

- Textiles
- Forestry and agricultural commodities (e.g. wood, cotton, palm oil)
- Mining
- Energy/fossil fuels
- Ship breaking
- Armaments

subsidised projects. International commercial banks can provide access to global financial markets, and by working together with their regional counterparts, gain local expertise and insights. Meanwhile, supranational banks may play an overarching role by defining international frameworks and using their significant resources to mobilise change on a global scale.

Channelling sustainable finance to emerging markets

Bridging the funding gap. The global ESG transition undoubtedly requires significant capital. It will be down to FIs to direct funding and facilitate investment, particularly when it comes to the distribution of capital to meet the needs of emerging markets. This is especially true given that there currently remains a significant financing gap. Systemic barriers persist in many developing economies that often hinder access to finance, including substantial upfront capital and transaction costs, longer timescales, and considerable project or country risk.

The African Development Bank (AfDB), for example, estimates that the continent will require US$170 billion a year by 2025 to finance its infrastructure development needs, with a projected gap of around US$100 billion annually. For all emerging markets, the UN has estimated a gap of up to US$40 trillion. In efforts to bridge this gap, the G7 announced in August 2022 that it would pledge US$600 billion in public and private funds over the next five years. The EU's Global Gateway initiative, launched in December 2021, aims to mobilise €300 billion by 2027 in an effort to promote good governance and clean infrastructure across the globe[18]. Furthermore, UN Secretary-General, António Guterres recently called on FIs – namely multilateral development banks (MDBs) – to take more risks to adequately support the energy transition for emerging markets.

Certainly, private sector financiers and MDBs are invested in overcoming these barriers and facilitating green business with emerging markets. By adopting innovative approaches to traditional finance FIs can help to remove barriers to climate-related finance and sustainable development for emerging markets. What's more, sustainable business can benefit from greater access to financing, and green "stamps of approval" for transactions that meet strict ESG requirements.

Negotiating long-term debt. Complexities also exist in the form of extreme global headwinds, which are raising the stakes in emerging markets and influencing what are already tough decisions facing governments on ESG. With many developing countries experiencing mounting debt-stress in the wake of COVID-19, for example, some – as a means of ameliorating economic hardship – may deprioritise their climate change commitment goals; instead focusing on raising short-term debt by drawing on their natural resources. Here, FIs can play a crucial role to ensure that economic progress remains closely tied to ESG ambitions.

It is possible for emerging markets to negotiate with holders of their long-term debt. Chinese government-sponsored banks are the largest bilateral creditors throughout emerging markets[19]. In the case of Ecuador, for instance, which owes nearly US$5 billion to China, one opportunity for the country is to restructure its debt swaps linked to sustainability goals. "Debt-for-nature" deals allow some loans to be "forgiven" in return for investment in environmental conservation. As China seeks to take on a global role in biodiversity finance, announcing its Kunming Biodiversity Fund in October 2021, such financial tools present an important method for emerging markets to remain on course to achieve ESG objectives[20].

The UN's Development Programme has also urged Sri Lanka to pursue debt-for-nature swaps as it renegotiates its US$45 billion of long-term debt as the country tackles an economic crisis[21]. Indeed, it is important to note that restructuring debt does not solely benefit the recipient. These negotiations are essential to helping developing countries recover from the pandemic and wider economic headwinds, increasing the likelihood that the remainder of the debt will be repaid.

Section 3.1 Sustainable finance solutions: the bond market

In response to investor demand, and to incentivise and fund projects that specifically deliver environmental benefits, the bond market has evolved to include green – and more recently, blue – bonds. ESG investments – i.e. financial assets that fulfil certain minimum social and environmental criteria – are experiencing rapid growth. According to recent estimates, ESG-related debt issuance more than tripled in 2021 to US$190 billion, while green equity fund flows rose to US$25 billion, bringing total assets under management to nearly US$150 billion globally.

Green bonds in emerging markets

For individual countries, investment in sustainable and environmental projects can place significant strain on public finances. As such, sovereign bond issuance presents a useful alternative source of funding. Sovereign green bonds issued by developing countries also flag a national commitment to decarbonisation and can help to kickstart private sector green bond issuance.

Governments play an essential role in regulating and directing green finance. For example, in 2020, 38% of China's green bonds were issued by government-backed entities. Despite the economic slowdown associated

Green, blue, climate and social bonds:
Most green bonds, and their subsets, are earmarked for specific sustainability-focused projects or assets.

- **Green bonds:** financial instruments that finance green projects
- **Blue bonds:** raise capital for marine and ocean-based projects
- **Climate bonds:** linked to climate change solutions
- **Social bonds:** for projects with a positive social outcome
- **Sustainable bonds:** can address a combination of green and social issues
- **Sovereign green bond:** a green bond issued by a sovereign government

Sustainability-linked bonds:
An alternative arm of the green bond market that is increasing in popularity. Unlike sustainable bonds, their proceeds are not earmarked for a specific project. Instead, the financing conditions of the bond are structurally linked to the issuer's achievement of agreed-upon climate or sustainable development goals. These incentivise borrowers to increase spending on sustainable projects by setting specific sustainability targets for the issuer. Therefore, some investors believe they encourage a more holistic view of a business's ESG agenda.

Greeniums:
Bond issuers frequently benefit from lower borrowing costs because the bonds command a higher price (and therefore offer a lower yield) than conventional bonds issued by the same entity.

with COVID-19, domestic and overseas issuance reached US$44 billion, ranking China as the largest emerging market issuer of green bonds[22].

Corporate issuers played a larger role than in previous years – Beijing Jingneng Clean Energy was the largest non-financial corporate issuer, with one bond amounting to US$2.1 billion. Its net proceeds were exclusively directed to financing and refinancing wind and solar projects, and to supplement working capital for these businesses. Figure 3 demonstrates the growth in green bonds across emerging and developed markets, and Figures 4 and 5 provide a breakdown according to largest issuing markets.

But there remains huge potential for growth, and long-term regulatory considerations will be important. Nearly half of the green bonds issued in China in 2020 are not aligned with other global criteria for green bonds, and key "gatekeepers" of the labelled bond market, such as external review providers and underwriters, should insist on high standards. It will be essential that the Chinese government provides consistent and credible policy signals to meet these criteria.

Beyond engaging emerging economies, new solutions have also emerged to include high-emitting issuers in green finance. While some

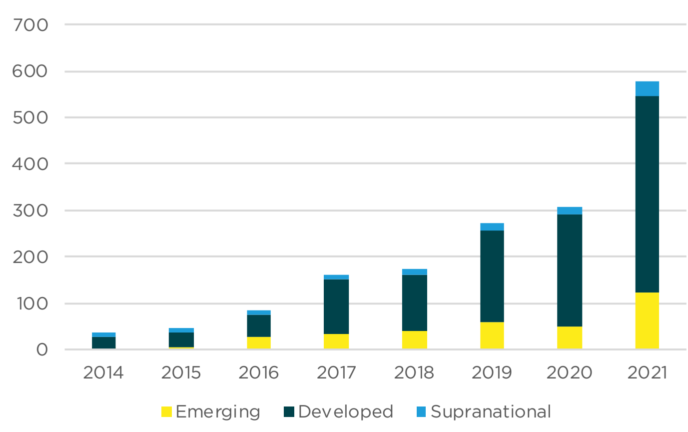
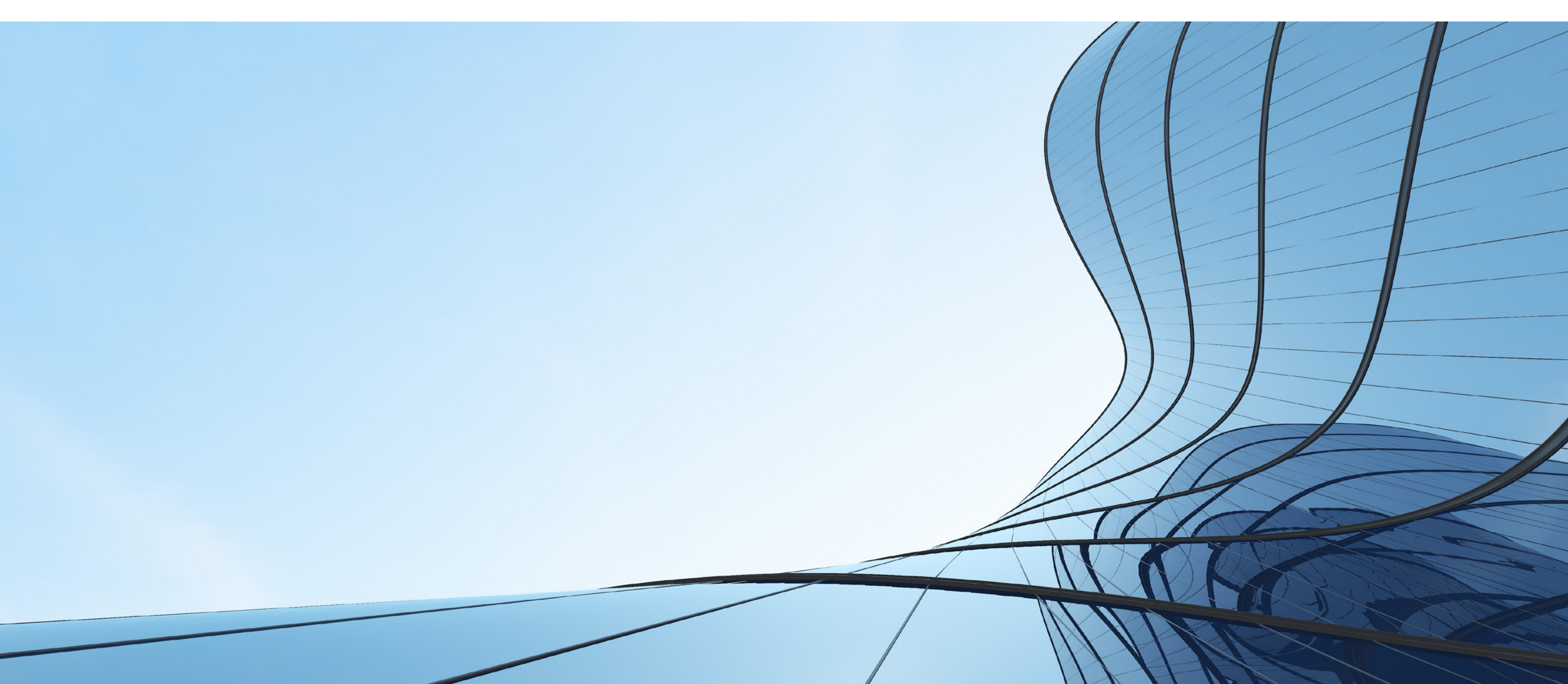


Figure 3: Climate bond growth[24]

Source: Climate Bond Intiative
Emerging markets' share of global bond issuance increased during 2021, most notably for sustainability-linked bond and loan instruments. It was also the first year that developing economies gained market share at the expense of their more advanced counterparts. Investments in ESG now total 18% of foreign financing for emerging markets and that figure is set to grow. The IFC predicts green bond issuance in emerging markets will reach more than US$100 billion by 2023[23].

European oil companies have already opted to sell green bonds, there is concern among investors that claims of "greenwashing" might devalue the wider market. In one innovative response to this concern, the Japanese government branched out into a relatively new form of climate debt: encouraging the issue of transition bonds, which target the shift to cleaner technologies. The Japanese utilities sector is set to lead this market



globally, but to be successful, high-emitters must demonstrate that proposed technology transition is realistic and science-based[27]. Indeed, to substantiate its climate friendly credentials, Japan's largest oil refiner, Eneos Holdings Inc., has proposed transition-linked bonds pinned to its long-term carbon dioxide reduction targets.

The value of sustainable finance in the bond market

The purpose of measuring and reporting on ESG is to demonstrate sustainability efforts and credentials, and in this rapidly evolving market, FIs need to take into consideration differences in standardisation and labelling in the bond market.

While the World Bank and the IFC have established eligibility criteria for green projects, it is ultimately up to the issuer to interpret the "green" credentials of their proposal. The Green Bond Principles (GBPs) – of which Commerzbank became a member soon after their establishment in 2014 – lay out voluntary best practice guidelines on the information that issuers should disclose to their stakeholders.

From an investor perspective this data is, of course, needed for designing portfolios, with the aim of generating returns. Transparent, accurate communication is therefore crucial: from the fundraising stages to a project's completion. These practices can incur some additional costs compared to other traditional debt instruments. But issuers do enjoy some beneficial borrowing conditions, including "greeniums". Indeed, pricing in the bond market will be crucial, with some green transactions pricing below standard assets. The relatively low cost of green debt could demonstrate that, at least in part, investors wish to incentivise spending on sustainable projects, and so may be willing to accept a lower yield. Future standard pricing is likely to evolve that penalises non-ESG compliant issuers, with green transactions being less expensive.

Country	Total green bond issuance (US$ billion)[25]
USA	303.9
China	199.1
France	167.2
Germany	157.1
Netherlands	78.8
Sweden	58.3

Figure 4: Main issuers of green bonds

Country	Total green bond issuance (US$ billion)[26]
India	22.1
Chile	11.9
Brazil	11.2
Indonesia	8.1
Poland	6.5
Mexico	3.6

Figure 5: Main emerging market issuers of green bonds

Section 3.2
Sustainable finance solutions: MDBs and ECAs

Multilateral development banks (MDBs) and export credit agencies (ECAs) have important roles to play in directing green finance in emerging markets. They can encourage sustainable development by transforming existing infrastructure – for instance, by prioritising energy efficiency in the projects they finance. MDBs invest directly or indirectly – in partnership with local and international FIs alike – to support local businesses/projects.

MDBs mobilising private finance: AfDB case study

MDBs are significant financing partners in countries' efforts to catalyse capital toward the SDGs, including from the private sector. MDBs help mobilise private financing by structuring sound investment projects,

Multilateral development banks

Multilateral development banks (MDBs) are international FIs created by two or more countries for the purpose of encouraging economic and social development. They are non-profit organisations and, rather than obtain a return for shareholders, their goal is to issue grants and low-cost loans to fund projects that improve the economic conditions of developing countries – such as the building of new roads or providing clean water to communities.

MDBs can use innovative finance mechanisms to mobilise private finance for sustainable infrastructure and initiate bankable projects. They may do this through blended finance, guarantees and green bond markets. Indeed, guarantees are well suited to finance sustainable infrastructure because they can be precisely targeted to policy risks, although there is a limit to which FIs with such guarantees can be made responsible for the fulfilment of certain ESG goals. They can also leverage their technical expertise to help build the capacity of staff and clients on the ground, expanding local knowledge of the latest trends and technologies while helping to build resilience and independence into the system. From an advisory standpoint, MDBs can play a role in assisting governments with creating an effective enabling environment for sustainable investing, through technical assistance and project preparation.

Crucially, multilateral organisations work hand in hand with private financiers to ensure that sustainable principles are embedded in the projects financed by the private sector. They can act as mobilisers of private finance for sustainable infrastructure, have convening power and assist client governments with project preparation and technical assistance on infrastructure.

coinvesting alongside commercial investors, and developing new financial products to unlock additional flows.

The AfDB, for example, has raised funds for projects across Africa under its Green Bond Framework, promoting “green growth” by building resilience to climate shocks, providing sustainable infrastructure, creating ecosystem services and making efficient and sustainable use of natural resources, especially water – a resource central to growth but most affected by climate change.

One project funded by an AfDB bond is Egypt’s Gabal El-Asfar Wastewater Treatment Plant (GAWWTP). The plant will improve public health and environmental protection – ultimately improving sanitation for the eight million people living in Cairo East[28]. Large-scale infrastructure projects such as the GAWWTP also represent how AfDB’s environmental goals are balanced with its aims to protect livelihoods and spur innovation, job creation and economic development.

Export credit agencies (ECAs)

Operating under the mandate of their local government, export credit agencies (ECAs) provide insurance options and (in some instances) financing for the benefit of exporters. Their goal is to support the domestic economy while fostering financial inclusivity.

Traditionally limited to standard export finance transactions, in recent years their scope has expanded to new products, with sustainability-focused ECA products on the rise. ECAs have unique benefits when compared to capital market instruments: customisable to the specific needs of a given project, ECAs have emerged as an effective long-term financing tool in emerging markets for banks to aid sovereign investment plans and local businesses seeking support to grow.

Certainly, the AfDB has been active in driving sustainable initiatives. Under the Paris Agreement, each signatory country has delineated Nationally Determined Contributions (NDCs) – specific climate action goals that need to be met. In 2018, the AfDB established the Africa NDC Hub with 18 international partners, including other partner MDBs such as the Islamic Development Bank, to provide resources to help countries in the region achieve these NDCs. For example, the AfDB has supported Cote d’Ivoire in developing an NDC investment plan.

Key developments introduced by the Africa NDC Hub include creating a digital tool for policymakers to help embed the NDCs, SDGs – as well as the African Union’s Africa Agenda 2063 sustainability strategy – into national development plans. The AfDB has also rolled out tools to support private sector investment in opportunities related to NDCs.

ECAs: plugging the investment gap

The climate goals of a country are frequently reflected within its ECA policy, representing a significant opportunity to translate this agenda into action. In time, such ECAs may altogether move away from projects without a positive environmental outcome. While ECA strategies to incentivise sustainable projects are still very much under development, in the future, ECA backing could become a form of green or social guarantee. Certainly, as businesses face growing scrutiny on their ESG credentials, an ECA “stamp of approval” could be incredibly valuable, demonstrating that a given project is green or socially beneficial.

The structure of ECA finance lends itself to concrete projects, like infrastructure, as opposed to general investment. With respect to the “social” aspect of ESG, infrastructure is crucial as emerging markets develop, and ECAs have a key role to play here as governments and agencies adapt to the changing needs of the market. In fact, emerging markets’ infrastructure projects typically have no other funding options

for long tenors. ECAs – together with international FIs – are therefore paramount in driving financial inclusion.

Partnerships between FIs and ECAs are increasing, with ECAs providing high-quality collateral to the covering bank against bad debt losses through export credit guarantees. This creates cost-effective long-term financing – with benefits all round. In Africa in particular, we at Commerzbank are seeing a steady growth in ECAs as a percentage of trade finance transactions. A recent example from our own books is the expansion of an African fishing port by an international marine technology conglomerate. The extensive infrastructure measures required around €100 million in the first phase of construction. Based on our extensive experience in this specialist market, we identified an ECA loan as the most appropriate financing solution. Commerzbank provided half the buyer credit alongside a fellow European bank to the respective African Ministry on the basis of viable ECA cover from a European agency.

ECAs and FIs are collaborating to plug the investment gap in emerging markets. They provide essential options to bolster development where the private sector simply cannot.

Section 3.3 Sustainable finance solutions: the loan market

2021 was a record year globally for the green and sustainability-linked lending market, having reached an all-time high of US$681 billion, up 275% on the previous year. Of that volume, loans alone accounted for over US$600 billion, up 350% on 2020 figures[29].

Sustainable loans are now mainstream products and there are several types of loans on the market aimed at promoting sustainable business. The original format of sustainable loans issued was the "green loan" – derived from the already existing green bonds – which allows borrowers to access capital to fund a specific project with a sustainable or environmental objective. These "use of proceeds" loans can deliver preferential terms and rates, as long as the borrower conforms to certain sustainability objectives, or that the project is focused on environmentally friendly processes and products. As seen with green bonds, assessment and reporting requirements are placed on the borrower. These core principles were defined by the LMA in 2018 and adopted by loan issuers worldwide, including the World Bank's International Finance Corporation (IFC).

Much the same as in the bond market, sustainable loans have also expanded in their definitions and scope. Social loans were introduced to finance socially focused projects, such as affordable housing, food security and socioeconomic advancement. Like a green loan, the already preferential terms of a social loan can be improved further by a commitment to sustainability indicators.

Carbon offsetting

Many environmentally orientated targets seek to reduce carbon emissions, but ultimately some are unavoidable. Therefore, to achieve neutrality, carbon offsetting is a mechanism to compensate for residual emissions by supporting projects that absorb or reduce emissions. For example, Commerzbank has been climate neutral since 2015, compensating for residual emissions through the purchase of high-quality CO_2 certificates, carefully selecting the offsetting projects we commit to. One such project, offsetting 20,000 tonnes of CO_2 in 2021, supports the development of the Jepirachi wind-based generation facility in Colombia, helping to increase renewables capacity.

Sustainability-Linked Loans

Following the growth of the sustainable debt market, Sustainability-Linked Loans (SLLs) have emerged as the most popular form of sustainable loans. These are structured to incentivise a borrower to reach certain pre-defined Sustainability Performance Targets (SPTs) – based either on ESG-KPIs or an ESG rating. Usually, this is achieved in the form of a margin reduction, in case the SPTs have been met, or a margin increase in case SPTs have been missed, offering a greater degree of flexibility in how borrowers can use funds to improve their sustainability performance. The Sustainability-Linked Loan Principles (SLLP) were originally published in 2019 by the Loan Market Association (LMA) and provide a framework and guidelines how to structure an SLL.

Sustainable loans and emerging markets

In emerging markets, sustainable loans are utilised in the development of waste management, renewable energy, clean transport or research into future tools for sustainability.

Of the estimated $33 billion in outstanding green loans worldwide, the World Bank calculates that developing countries account for just $1.6 billion. However, the green loan market is set to outpace the bond market in the near term due to the comparatively low transaction costs, as green loans contribute to the ESG objectives of emerging markets.

One example of a green loan in action is the IFC's participation in Mexico's Infraestructura Energetic Nova (IEnova) solar project in 2020. The IFC structured a 15-year green loan facility totalling US$541 million, to finance the construction of five solar plant projects with a total installed capacity of 536 megawatts. The loan supported IEnova, one of Mexico's largest private power suppliers, to transition towards a more sustainable business model by displacing carbon-intensive energy generation. Once fully operational, the solar plants will eliminate 793,000 tonnes of CO_2 equivalent annually.

Section 3.4
Sustainable finance solutions: trade finance

Trade finance is currently less developed than the loans and bonds market in terms of sustainable finance activity[30]. This is for a multitude of reasons, but the complexity of global trade and the number of different parties involved (over 20 are typically involved in a single transaction[31]) can make

implementing change – with respect to both processes and mindsets – particularly challenging. Certainly, applying incentives to entire supply chains, involving participants from across the globe, presents logistical challenges. Interest in such schemes has also been limited until relatively recently, meaning that many developments are at a nascent stage.

Progress has been made, however, with the introduction of a number of initiatives to encourage environmentally conscious supply chains. For example, sustainable shipment letters of credit (SSLCs) have been launched by the International Finance Corporation (IFC) and Banking Environment Initiative (BEI). Like a normal letter of credit (LC), an SSLC guarantees payment by a buyer, but offers discounted financing provided that a shipment meets pre-agreed sustainability criteria. These criteria are not universally standardised, but are determined by factors such as the sector, size and geography of the relevant shipment. Similarly, green guarantees function in a similar way to a trade guarantee, with preferential terms agreed should parties conform to sustainability goals.

For FIs, such tools provide opportunities to incentivise businesses to undertake sustainable development through their trade activity. What's more, with emerging markets disproportionately affected by a lack of funding for renewable energy, green guarantees can offer a solution. By blending governmental and philanthropic funding in developing nations, such guarantees can help to drive further private investment into emerging markets due to the reduced risk provided by the guarantees.

The **International Chamber of Commerce (ICC)** in September 2021 established a programme to begin **defining and setting the standards for sustainable trade** in a manner that is practical, comprehensive and provides sufficient transparency into the sustainability of a transaction.

- Define sustainable trade and trade finance
- Establish a framework to measure and assess the sustainability of a given trade transaction/trade finance portfolio meeting the standards for sustainable trade
- Engage with the broader trade community to iterate and refine these over time

As a first result, the ICC has developed the following definitions for sustainable trade and sustainable trade finance:

"Sustainable trade represents the import, export, or trade of goods and services which actively support the achievement of one or more UN Sustainable Development Goals (SDGs) without infringing on the achievement of any other SDGs."

"Sustainable trade finance involves the financing or facilitation of sustainable trade, using recognised trade finance instruments."

Digitalisation and access to finance

The benefits of the digitalisation of trade finance extend far beyond the “E” of ESG. By improving the efficiency, transparency and risk mitigation of trade finance, digital solutions can help to drive supply chain inclusivity, with countries and businesses viewed as “riskier”, or having an unattractive “risk-reward” ratio due to due diligence costs, able to access trade finance more easily. As such, this could transform emerging markets’ ability to participate in global trade and support the growth potential of businesses across these regions.

Supply chain finance (SCF) programmes and digital marketplaces are helping FIs to mitigate risk. Trade asset distribution networks, for example, are creating opportunities for banks to “offload” risk from their balance sheets to a range of investors. Meanwhile, SCF enables a bank to pay its corporate clients’ suppliers directly, with the risk sitting with the corporate buyer instead of the “riskier” suppliers.

New and emerging technologies such as Blockchain/Distributed Ledger Technology will also play a key role in making supply chains more inclusive and sustainable. Such technology can address many of the information gaps existing today. In addition, open standards and harmonised communication channels can solve some of the integration issues that the fragmented trade landscape with its numerous stakeholders is facing. Many digital platforms have formed around this value proposition such as Contour and Komgo.

“There are clear economic and political imperatives to accelerating digital trade facilitation [and legal reform for digitalisation], with potential total benefits of nearly US$1.2 trillion to Commonwealth trade by 2026[32].”

Section 4

Emerging market initiatives: sustainable finance in action

An examination of ESG initiatives currently underway in emerging markets reveals solutions that are both innovative, but also wholly pragmatic. In lieu of effective cross-market standards and with growing pressure from more advanced trading partners, regulatory bodies within emerging markets are taking matters into their own hands. Through the creation of targeted frameworks for reporting and guidelines for sustainable investment, some emerging markets are becoming frontrunners in their own right. Meanwhile, local FIs are recognising the limitations of domestic investment, attracting international partners through incentivised programmes and state-backed development projects.

Below are just a few standout examples of homegrown ESG initiatives from emerging markets:

India proposes new blue bond standard

- Indian regulator proposed a list of activities to be funded by blue bonds, including offshore wind farms and sustainable fishing
- Fisheries, coastal tourism and aquaculture seen as key growth sectors for the country

At present, there is no global standard on blue bond issuances. An ongoing project by the International Capital Markets Association (ICMA) is set to finalise cohesive guidelines by the end of 2022. Until then, India's financial regulator, the Securities and Exchange Board of India (SEBI), has proposed its own blue bond standards.

The South Asian nation has been at the forefront of sustainability regulation within emerging markets. In January 2022, SEBI was the first to propose legislation targeting ESG ratings providers. With its proposed framework, the regulator has also listed various potential activities that could be funded by its blue bonds, including offshore wind farms, sustainable fishing, restoration of coral reefs and eco-tourism initiatives.

Developing India's blue economy has been flagged as a key growth catalyst, taking advantage of its 7,500km coastline and 14,500km of navigable inland waterways. Almost a third of India's 1.4 billion population lives in coastal areas, making fisheries, tourism, aquaculture and other so-called "blue trade" major economic factors. It could also encourage further investment into new sources of income, such as India's budding oceanic mining activity. At present, the industry is constrained by biodiversity and environmental damage concerns, but standardised blue bonds could facilitate a carbon credit-style system that would offset the impact of deep-sea mining, allowing India to meet the global demand for rare minerals. As well as a new blue bond standard, SEBI has also proposed the strengthening of its green bond framework, solidifying the definition of green bond securities and enhancing

disclosures, while expanding to include prevention and control of pollution, and circular economy initiatives. The proposals are largely in line with ICMA's 2021 Green Bond Principles.

Microfinance in Mexico

- In a country where 98% of businesses are SMEs, microfinance is an important way of achieving social development goals
- A 2021 project to expand access to finance in rural areas is expected to reach 135,000 small businesses, the majority female owned

Access to adequate financing options to address ESG challenges is undoubtedly a major barrier for developing economies, and impacting "social" aspects of ESG in particular. It is an issue affecting businesses both large and small, with independent businesses in less-connected, rural communities particularly underserved. However, traditional financial products are unsuitable here. Instead, the microfinancing model can more appropriately meet the needs of those who would otherwise lack access to conventional finance.

As an example, in Mexico – one of the fastest growing emerging markets – SMEs account for 50% of the country's GDP and represent 98% of all businesses, the vast majority of which rely on non-traditional finance. The World Bank estimates a formal financing gap for Mexican SMEs of around US$64 billion, or 14% of Mexico's GDP.

In 2021, Mexico's largest microfinance institution Banco Compartamos expanded its group lending operations in Mexico and Peru to improve access to finance in rural areas. In partnership with Citi, the US International Development Finance Corporation and the Japan International Cooperation Agency, it secured US$70 million in loans to provide finance for small businesses in less developed regions. The loans are expected to reach more than 135,000 small businesses, the majority of which are female owned[33].

Egyptian banks setting new climate standards

- The Egyptian banking sector looks to lead the way for Africa in adopting ESG risk analysis and disclosures
- The country is targeting investment in green hydrogen as it seeks to capitalise on its strategic position

As host of 2022's COP27 climate summit, the eyes of the world will be on Egypt and its sustainability credentials. The transcontinental nation – straddling North Africa and the Middle East – is a gateway between two developing regions, and is also strategically close to Europe's advanced markets. Egypt's economy has boomed in the past decade and is forecast to grow steadily in the coming years. Yet the famously arid nation is especially vulnerable to the effects of climate change.

Driven by its policymakers, Egypt's banking sector sits at the heart of its sustainable development. Its top banks are actively decarbonising their portfolios and are now integrating ESG risk analysis into all credit rating decisions. Categorising lending opportunities into high-, medium- or low-risk, lenders are measuring the environmental and social impact of each transaction. Collectively, Egyptian banks are also lobbying for the creation of an EU-style taxonomy to cover African markets.

In 2021, Egypt's central bank and the Financial Regulatory Authority issued joint guidelines on sustainable finance, making climate-related disclosures mandatory for companies listed on the Egyptian Exchange. Meanwhile, the Federation of Egyptian Banks has devised a strategic action plan to address the systemic transformation of the country's FIs, from a governance, risk and sustainability perspective, in a bid to level the playing field.

The Egyptian government is looking to ramp up foreign investment, having already signed several agreements with international

companies to begin producing green hydrogen in the Suez Canal Economic Zone. The efforts of its banking sector have created a particularly favourable environment for its flourishing green energy industry, turning it into a regional renewables hub, and facilitating much-needed diversification away from fossil fuels. It is hoped by many that Egypt's increasingly sustainable economy will set a new standard for its hydrocarbon-reliant neighbours.

Nigeria's solar power projects

- Renewables may be the solution to Nigeria's enduring electricity reliability problem
- Government programmes have connected many communities to the grid, but large-scale projects will require international investment

The World Bank ranks Nigeria 171 out of 190 nations for access to electricity with 43% of the population having no access to the grid. The lack of consistent power is a significant constraint for Nigerian businesses, resulting in a projected annual loss of more than US$26 billion, equivalent to around 2% of its GDP. Access to reliable electricity is therefore a major focus for the steadily growing nation.

Solar power has been touted as a potential solution to Nigeria's energy woes, but the biggest hurdle is finance. The Renewable Energy Association of Nigeria estimates that an investment of US$2 billion into its solar energy sector could meet the needs of Nigerian businesses.

In December 2020, the government of Nigeria launched an ambitious project aimed at connecting 25 million citizens to a solar-powered grid. Called the Solar Power Naija Programme, it will also create around 250,000 more jobs in the energy sector. By April 2021, the project had already deployed 100,000 solar connections.

Yet, the programme targets predominantly underserved communities, and greater investment is needed to tackle the real problem: Nigeria's inadequate and outdated infrastructure.

Securing the necessary capital to switch its grid to more reliable solar power and shift away from fossil fuels has been high on the agenda for Nigeria's federal government in recent years. Nigeria's Ministry of Finance has been seeking suitable foreign partners to back such a project.

As a result, in August 2022, the state-owned Niger Delta Power Holding Company managed to secure US$1.5 billion in ECA finance from the US Export-Import Bank. This 20-year loan will support the construction of new solar facilities and ultimately create a more reliable national power supply for Nigeria's growing businesses. Further ECA-backed power projects for Nigeria will follow.

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