Executive Summary of Evaluation

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Author of Final Report of Evaluation	*Elaine Wee-Ling Ooi*
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Author of this Executive Summary	*Elaine Wee-Ling Ooi, Nurudeen Ogunsanya*
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Background

The Environment and Social Risk Management (ESRM) program is an IFC initiative funded by the State Secretariat for Economic Affairs (SECO) of the Government of Switzerland. The program's goal is to catalyze behavior change for Financial Institutions (FI) in the East Asia and Pacific region (EAP) to finance projects in an environmentally and socially sustainable manner that reflect best practices and international standards. Private sector FI in EAP lag behind counterparts in other regions in terms of awareness, capacity and incentives when it comes to considering the environmental and social impacts of projects they finance. As an example, of 83 FIs adopting the Equator Principle banks, only one is from EAP emerging markets. Six countries (China, Indonesia, Mongolia, the Philippines, Thailand and Vietnam) are covered by the EAP program, of which Indonesia is home to the second largest biologically diverse rainforest and China has the largest banking assets in emerging market at $30 trillion as of February 2016, with growing overseas financing in high-risk infrastructure projects.

The program has been operational for three years. The program started at different times in each country. While China and Vietnam started in 2011, with the other EAP countries following in February, 2013 and Mongolia and Indonesia signing their respective Cooperation Agreements with IFC in March and May of 2014, respectively. So far, China and Vietnam have made significant strides for their banking industries to adopt environmental and social risk management (ESRM) practices. Domestic banks in Mongolia have shown particularly strong support for the program with an active role of the Mongolian Bankers Association (MBA).

Objectives

The program has adopted a three-pronged approach, starting with strengthening regulatory drivers at the top, developing FI capacity in the middle and market capacity at the bottom:

1. **Regulatory-level engagement: Create demand/induce responses from FIs.** Engaging regulatory bodies to develop policies, guidelines and incentives (regulatory drivers) for FIs, as few banks

would adopt ESRM practices and sustainable banking without mandatory requirements. The thrust of the ESRM program is aimed at this component.

2. **Financial Institution Engagement: Service demand from FIs and as a demonstration effect.** Engaging selected FIs to raise awareness, train and develop their capacities to implement E&S risk assessments and management frameworks. This also serves to have a demonstration effect on other banks.
3. **Consulting market development: Create sustainable technical service providers to address future demand.** Developing the capacity of a community of consultants and training partners to train and build the capacity of FIs around sustainability risks and business opportunities on a demand basis.

This evaluation was commissioned to determine if:

1. ESRM is a cost effective vehicle for delivering advisory services to maximize impacts. What is the likelihood of achieving impacts?
2. What are the lessons learned to improve its design and delivery?

Analysis

Relevance: Overall relevance of the ESRM is high.

Central bank regulators engaged IFC and its ESRM program to help them support the national priorities in green financing. Demand for ESRM and green financing is seen in all program countries and appears highest in China, Indonesia, Vietnam and Mongolia. In China, Indonesia and Vietnam, the program has been appropriately designed at three levels – encompassing regulators, individual banks and building of a market for FI consulting/training, of which the regulatory development component is to provide important momentum to engage banks and the FI consulting community in program's interventions. The exception is Mongolia, where the highly energetic Banking Association has led the way in launching voluntary standards and principles for E&S Risk Management for Mongolian banks.

Effectiveness: Based on a weighted review of the program towards the regulatory driver component, the report found the program to be effective.

So far, China has been the most progressive regulator adopting international E&S standards and practices to develop regulatory tools needed for bank oversight. Since the launch of the regulatory guidance, more than 20 first-tier Chinese FIs have installed or upgraded E&S risk management frameworks. Indonesia and Vietnam have issued regulatory guidelines (in Indonesia a Roadmap to Sustainable Finance has been issued, to be followed by an umbrella policy in 2016; the State Bank of Vietnam issued the Directive on Green Credit and ESRM in March 2015), while Mongolia has adopted voluntary Sustainable Finance Principles.

Efficiency: There are no comparable programs against which to assess cost effectiveness.

At the time of the MTR, there was no data to complete a cost benefit analysis and returns on investment. There is an expectation that the Chinese Green Credit Statistical system will have valuable data once Chinese banks have scaled-up implementation of the program.

IFC has effectively used the Sustainable Banking Network (SBN) as a mechanism to respond to demands from new countries. New ideas and tools continue to be generated and shared through the SBN members and learning events, an efficient and self-sustaining way of maintaining member country interest.

Impact: The level and scope of impact is rated too early to tell.

It is too early to forecast impacts of the overall regional program. In China, the program's target is to support China Banking Regulatory Commission (CBRC) to have top 19 banks screening 85% of corporate loans in line with Green Credit Policy. The 19 banks together account for an 85% market share. The Impact target could be evaluated at the end of the program.

In Vietnam, the program has made extensive headway, but it is still too early to confirm whether its actual impact targets will be met. The ESRM target for Vietnam is to screen $208 billion worth of credit by 2017. The evaluator is cautiously optimistic that leading Vietnamese banks will have significantly shifted their practices by the program's end.

Sustainability: Sustainability is likely.

Program gains in the regulatory sphere (directives, guidelines) for China, Indonesia and Vietnam seem permanent. All regulators are devoted to deepening and expanding their engagement with IFC and the SBN to fulfill their own organizational sustainable financing goals.

Chinese banks are compelled to follow the ESRM framework as it has been adopted by the Chinese Government. Therefore, ESRM gains at the F1 level will be sustainable. In Mongolia, the evaluator expects gains made are unlikely to be reversed in the short term. However, long term sustainability might be jeopardize if the government does not enact regulations that bolster voluntary guidelines created by FIs.

Conclusions and Recommendations

1. The ESRM program has proven beneficial and its SBN component enjoys strong support from member nations. The SBN is essential as it wields substantial influence and has a multiplier effect on promoting E&S standards on regulators and the banking community. The network allows interested parties to keep abreast of new trends and global practices.
2. The ESRM program is a complicated policy initiative that requires time for benefits to fully emerge. A strong understanding of the political economy of countries is necessary. Therefore, the evaluator recommends IFC provide sufficient staff support with necessary rankings, skills, and experience to navigate through the process. Also, senior country staff or a country representative should be on standby to address any policy issue if required.
3. Staff should tailor the ESRM's agenda to each country and ensure the plan is flexible enough to adapt to changing circumstances. While this is already a program approach, greater attention should be given for proper execution.
4. ESRM staff should be familiar with the FI landscape in each country, especially with banks with the riskiest portfolios and potential to have the highest E&S impacts.
5. Staff should improve program flexibility to create more options to satisfy new clients demanding sustainable finance not within the program's current scope.

6. The adoption and implementation of the E&S framework entails major changes to FIs' credit approval and supervision practices. The program should document methods adopted by different ESRM countries.
