

Innovative Finance for Social Justice

2016



The Social Dimensions of Development Finance in Asia and the Pacific

Results of a survey among ADFIAP members

Working paper 71

Paula Korth

Patricia Richter

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Foreword

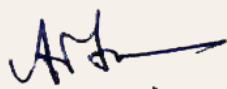
The International Labour Organisation (ILO) and the Association of Development Financing Institutions in Asia and the Pacific (ADFIAP) are pleased to publish this working paper on “The Social Dimensions of Development Finance in Asia and the Pacific”. For almost 100 years, the ILO has worked towards achieving social justice and acknowledged the role that the finance system plays in this endeavour by a multitude of collaborations with financial service providers, support organisations, and relevant policy makers. The ADFIAP is an international organisation, created in 1976, striving to advance sustainable development through its members in Asia and the Pacific. Both organisations are united in a vision of a just world in which the benefits of growth are shared more equitably to create positive social development. Through its unique position, development finance holds a great promise towards advancing the necessary social change.

The analytic work leading to the report was inaugurated at the Joint CEO Forum in Kuala Lumpur, Malaysia, in November 2014, when more than 140 CEOs and senior officials of Development Finance Institutions (DFIs) from Asia and the Pacific as well as from Africa convened to discuss Alternative Models of Development Financing in a Changing World. Participants eagerly engaged with ILO and together developed an agenda for investigating what management systems DFIs employ to identify social risks, impacts, and opportunities. Six DFIs from Asia and the Pacific stepped forward to participate in the study. This report summarises the status of such systems across the industry in Asia and the Pacific, it identifies gaps in the currently available systems, and proposes a way forward.

The main purpose of this report is to share the experience from Asia and the Pacific and open the eyes of the stakeholders as to where the financial industry stands these days. In doing so, this report also proposes an engagement agenda for the industry and calls on the DFIs from Asia and the Pacific and the ILO to continue the collaboration to increase the social capacity of development finance on the continent and beyond.

Arjun Fernando

Craig Churchill



ADFIAP Chairman,
CEO DFCC Bank Sri Lanka

Head Social Finance Programme,
International Labour Organisation



International
Labour Office

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Many thanks to the CEOs and Managing Directors who spearheaded the engagement of these institutions and freed staff to engage with the ILO. Many thanks to the DFI staff members who tirelessly shared relevant documentation and answered to our questions.

This study would not have been possible without the excellent support of the ADFIAP secretariat, especially Octavio B. Peralta (ADFIAP Secretary General) and Enrique I. Florencio (Knowledge and Sustainability Officer), who coordinated the initial sign up of the DFIs to the study and supported the finalisation of the publication.

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Glossary

AADFI	Association of African Development Finance Institutions
ADB	Asian Development Bank
ADFIAP	Association of Development Financing Institutions in Asia and the Pacific
CSR	Corporate Social Responsibility
DB	Development Bank
DFI	Development Financial Institution
EIA	Environmental Impact Assessment
ESG	Environmental, Social and Governance
ESIA	Environmental and Social Impact Assessment
FAO	Food and Agriculture Organisation
FI	Financial Institution
FPIC	Free, Prior, and Informed Consent
GRI	Global Reporting Initiative
GIIN	Global Impact Investing Network
ICESDF	Intergovernmental Committee of Experts on Sustainable Development Financing
IFC	International Finance Corporation
IFI	International Finance Institution
ILO	International Labour Organisation
OSH	Occupational Safety and Health
SEMS	Social and Environmental Management System
S&E	Social and Environmental
SME	Small and Medium-sized Enterprise
WB	World Bank

1 Introduction

UN Member States have repeatedly referred to financial assistance as the “lifeblood” of the Post-2015 Development Agenda (Lebada, 2014). Acknowledging the importance of finance for development, the Intergovernmental Committee of Experts on Sustainable Development Financing (ICESDF) has, however, underlined that the “current financing and investment patterns will not deliver sustainable development” (Lebada, 2014). They committee accentuates the potential contributions of development banks (DBs) to support long-term sustainable investments - in regions and sectors where access to capital is limited and which are in line with national development strategies (United Nations General Assembly, 2014, p. 23).

Through their lending activities, development finance institutions (DFIs) are exposed to a number of social and environmental risks linked to the activities of their clients including occupational safety and health concerns, involuntary resettlement, child labour, or environmental pollution. These risks do not only influence the sustainable development impact of the institutions, but also have a direct link to credit, reputational, and liability risk. A structured management approach is required to effectively assess and manage social and environmental risks and impacts, as well as to seize social and environmental opportunities. Likewise, a rigorous approach to measure social and environmental impacts is of utmost importance to portray and justify the special mission and additionality of DFIs.

New initiatives such as the Sustainable Stock Exchanges Initiative, networks like the Global Impact Investing Network (GIIN), and actors such as NGOs and service providers (like sustainability rating agencies or auditors) are evolving fast to enforce the financial sector’s willingness and capability to deliver on socially just and environmentally friendly development. Cornerstones in the development of sustainable financial standards - globally, and specifically in the Asian context - were the launch of the Equator Principles in 2003, the adoption of Performance Standards on Social and Environmental Sustainability by the International Finance Corporation (IFC) in 2006 and their overall revision in 2012, as well as the approval of the Safeguard Policy Statement by the Asian Development Bank in 2009. Regulators brought forward initiatives such as the Philippine Environmental Impact Statement System, or the Sustainable Banking Network that unites banking regulators and associations from countries like Indonesia, China and Bangladesh. Guided by these international developments, DFIs at national level integrated sustainability considerations in their operations through developing and implementing *Social and Environmental Management Systems (SEMS)*.

Simultaneously, the International Labour Organisation’s (ILO) Social Finance Programme - whose mission it is to support the development and adoption of financial services and policies for social justice through innovation, research, policy dialogue and capacity building¹ - observed a stronger focus on integrating environmental dimensions in the SEMS while social concerns received less attention. This perception was echoed by the Association of Development Financing Institutions in Asia and the Pacific (ADFIAP) whose mission it is to advance sustainable development through its members. ADFIAP does so, among others, through its engagement in the Global Sustainable Finance Network.

It is undisputed that environmental degradation and climate change have socio-economic impacts on poverty, employment and differently affect social groups (in terms of gender, ethnicity, race, etc.). However, the Rana Plaza disaster in Bangladesh, or large resettlements like the displacement of more than 100,000 people in the course of a World Bank funded urban transport project in Mumbai in India in

¹ Recent engagements of the ILO to support the development and adoption of innovative financial services for social justice include research and capacity building for social compliance and impact in agricultural finance; action research on microfinance for decent work, and testing insurance innovations and developing insurance markets.



2003-2005 (World Bank, 2005), illustrate the dramatic social impact of neglecting to adequately address social risks and impacts and manifest the need for compliance with distinctive social safeguards. The collapse of the Rana Plaza building in Dhaka in April 2013, which hosted a number of clothing factories, claimed 1,134 lives, injured many more and affected overall 3,600 workers. The Rana Plaza Coordination Committee calculated that \$40m are needed to compensate the victims (Rana Plaza Arrangement, 2015). People affected by the large-scale resettlement in Mumbai claimed that resettlement sites were among the most polluted areas of Mumbai and therefore put their health at risk. In addition, they were resettled far away, which damaged their well-established businesses without being offered adequate income restoration.

Research of the Food and Agriculture Organisation (FAO) of the United Nations argues that large-scale investments need investor commitment on the individual investment level in order to create benefits in the host countries (Cotula et al., 2009). With such commitment, financial institutions have the potential to realise social opportunities and create long-lasting impact for people and communities. A recent study by GIIN and JP Morgan Social Finance showed that impact investors try to create such impact by selling products and services that positively benefit target populations; by providing employment to target populations; or by integrating target populations into investee supply or distribution chains (JP Morgan and GIIN, 2015). Responsible finance can also make business sense: research from the Global Finance Institute found that portfolios of assets with high environmental, social and governance (ESG) ratings outperform their benchmarks in various contexts (Hoepner, 2013).

The conviction of the need for compliance with distinctive social safeguards brought together the ILO and ADFIAP to investigate the extent to which DFIs in Asia & Pacific have implemented formal Social and Environmental Management Systems with a particular focus on the level of inclusion of the social dimension. A related study was launched at the Joint CEO Forum in Kuala Lumpur, Malaysia in November 2014. This report presents the summary findings of the study to which six ADFIAP members contributed. In parallel, a similar analysis was conducted in Africa in collaboration with the Association of African Development Finance Institutions (AADFI).

The report first outlines the analytical approach (chapter 2) and describes the methodology and the participants (chapter 3). Chapter 4 presents the main findings regarding the level of SEMS implementation, as well as related challenges. Finally, conclusions are drawn and potential ways forward are discussed in chapter 5.

2 Analytical Approach

The study aimed to shed light on the level of implementation of Social and Environmental Management Systems (SEMS) by DFIs in Asia & Pacific with a particular interest in analysing the social dimension of such systems. The analytic approach consisted of identifying and assessing i) the main building blocks that underpin these SEMS and ii) the inclusion/incorporation of social dimensions. The following sub-sections provide more details on the two components of the analytical approach.

2.1 Building Blocks of a Social & Environmental Management System

To be the backbone of a structured management approach, a Social and Environmental Management System needs to be formal and sufficiently resourced. It typically comprises the following six elements:

Figure 1: Building Blocks of a Social and Environmental Management System.



These six building blocks are described in more detail in the next paragraphs.

Building Block 1: A **Social & Environmental Policy** discloses the institution's approach towards sustainability - such as towards risks, impacts and opportunities related to labour conditions, environmental pollution or stakeholder engagement - and should equally address social and environmental elements. It includes at least a general commitment towards sustainable development, as well as some reasoning for this commitment. The policy should be reviewed periodically to allow for adjustments to new developments. Furthermore, the broader legal and regulatory framework (national and international), which is applicable to the institution and clients, could be identified. A further detailed description of this framework should feature in the DFI's institutional S&E standards or safeguards, which form SEMS building block 2.

Building Block 2: The **Social and Environmental safeguards or standards** with which the institution complies should be mentioned and described in detail. They might be oriented towards ADB's social and environmental safeguards or the IFC performance standards but need to be adapted to the local context within which the DFI is operating to render them meaningful guidelines for the institution and staff implementing the SEMS.

Building Block 3: Social & Environmental Procedures describe the institutional practices to identify, assess, mitigate and monitor social and environmental risks and impacts. Hence, the procedures should include all stages of the DFI's credit cycle and match the institution's operational processes. Typically, this process covers:

- Identification,
- Assessment,
- Mitigation / avoidance / management,
- Monitoring / reporting.

The first procedural step is the identification of S&E risks, which includes screening all new applications against an exclusion list, and using a categorisation tool for a preliminary S&E risk classification which may restrict funding going into certain sectors or risk classes. Subsequently, an S&E assessment (including a re-evaluation of the risk category) takes place and risk mitigation / avoidance / management measures are defined in case of non-compliance. These may be fixed in an S&E action plan or S&E monitoring and management plan, which clearly indicates who has which S&E responsibility and which assigns concrete timelines for implementing and reporting on milestones. Moreover, management of S&E risks and impacts includes incorporating the mitigation measures into the loan agreement and monitoring their implementation and effectiveness. The measures should regularly be redefined based on their effectiveness to reach the envisioned impact. Furthermore, in order to help staff to apply the S&E procedures, adequate tools like sectoral guidelines and templates for S&E due diligence or monitoring should be integrated or attached to the S&E procedures. Application of the S&E procedures - in credit appraisal, decision and monitoring - should show that the DFI cannot only describe but also live by its S&E values.

Building Block 4: Social & Environmental Responsibilities describe who in the organisation takes over which SEMS responsibility - from board to senior management, middle management and front and back office staff. In addition, it should be clearly articulated which resources are provided for taking on the respective responsibilities (e.g. human, technical, financial). The board and senior management should guide the institution's overall approach towards sustainability, which includes at least commitment to the S&E policy and critical assessment and approval of suggested S&E covenants. In order to be able to bring forth potential strategic change such as shifting envisaged impact or de-risking, the board and senior management need to be knowledgeable about the S&E risks and impacts on a portfolio level. The middle management should coordinate between the guidance of the board as well as senior management and the actual implementation by staff. This is typically done by an S&E coordinator or manager. Specifically, middle management assists loan and credit officers in evaluation and monitoring of clients, updates the procedures and relevant documents and evaluates S&E risks on the portfolio level. On the implementation level, loan and credit officers (and staff from the monitoring unit, if existent) evaluate and monitor clients on an individual level. Depending on the size of the organisation, further roles might exist in internal audit, legal etc. Furthermore, the human resource function is part of S&E responsibilities for ensuring long-term institutional S&E capacity. These responsibilities should include aligning job descriptions and the performance measurement framework with S&E tasks and targets, recruiting qualified staff for positions that have S&E responsibilities, and ensuring implementation of an S&E capacity building strategy.

Building Block 5: Social & Environmental training shall raise skills and awareness and enable staff to perform their S&E duties. The actual training should be guided by an S&E training strategy, which again should be integrated into the overall institutional capacity building framework and performance management system. Human resources and the S&E coordinator need to work closely to effectively implement the S&E training strategy. This coordinated approach ensures that training can be offered on a sustainable basis and not as a one off or ad hoc activity.

Building Block 6: Internal and external **Social & Environmental reporting** is crucial for controlling S&E performance, sharing relevant S&E information with the right persons and making related decisions, achieving transparency, and positioning the institution as a sustainable finance provider.

2.2 The Approach to Focussing on Social Risks, Impacts, and Opportunities

Building on the assumption that a SEMS is a management tool to promote and ensure a sustainable development impact of a DFI, each building block of a SEMS should balance environmental and social elements and allow the institution to adequately address them. This study analyses each building block of a SEMS to the extent it exists in principle and incorporates social elements. In practical terms, the study looks at specific social safeguards and how they are integrated into S&E due diligence, whether S&E reporting covers positive social development impacts in a systematic way, or whether specialists with experience in social topics are engaged in S&E assessments, either as staff or consultants, when projects involve resettlement, indigenous peoples, or other socially relevant themes.

Although S&E safeguards and standards of large International Finance Institutions (IFIs) and DFIs are typically based on international law there is no consensus which conventions shall be integrated into a safeguard system and how specifically to design the standards. Although the *safeguards on indigenous peoples* of ADB, WB and IFC differ - for instance to what extent they integrate the Free Prior and Informed Consent (FPIC) principle - they are all based on the ILO convention on Indigenous and Tribal Peoples (No. 169; adopted 1989). Generally founded on human rights principles, the *safeguards on involuntary resettlement* of the named institutions tackle in a similar, but not identical manner, physical and economical displacement. Gaps exist, for instance, in the IFC and WB standards which do not cover *temporary* displacement or loss of access to assets or resources. In addition, none cover *voluntary resettlement*, which, despite its voluntary nature, may require safeguard measures against impoverishment and to maximize development benefits (Bugalski and Pred, 2013). *Labour rights and working conditions*, based on the 1989 ILO Declaration on Fundamental Principles and Rights at Work², are differently incorporated by the institutions. Whereas the IFC safeguards refer to all fundamental labour rights, ADB only refers to Occupational, Safety and Health, and the WB does not include standards on labour rights and working conditions. Other social safeguards relate to *community engagement, community health and safety, gender*, as well as to *cultural heritage*.

Hence, there is no clear guidance for a DFI, which international laws are to be translated into safeguards. Based on the comparison (see Table 2), the IFC performance standards are most comprehensive and can therefore serve as a good basis. However, no matter which S&E safeguard guidelines of an IFI a DFI uses as a basis, they *must* be adjusted to the legal requirements of the location where the DFI operates. Ultimately, the stringent implementation of the S&E safeguard guidelines is crucial: A recent Oxfam report (Oxfam, 2015) accuses IFC for not properly investigating the social and environmental systems of the financial intermediaries it invests in and therefore not managing compliance of its sub-investments. Oxfam makes this claim vis-à-vis a total investment value of USD 36 billion in FIs by IFC as of 2013. The fact that also large IFIs are criticised for not adequately applying their safeguards in practice - next to the described inconsistencies among the safeguards - discloses that existing safeguard and operating systems can only serve as a point of comparison rather than as a role model. Sustainable finance is an emerging field, which is open for improvement and innovation.

² Fundamental Principles and Rights at Work cover the ILO conventions on Freedom of Association and Protection of the Right to Organise and Bargain (No. 87, No. 98); Forced Labour (No. 29, No. 105); Child Labour (No. 138, No. 182); and Equal Remuneration and Discrimination (No. 100, No. 111).

Table 1: Consideration of social safeguard dimensions in WB Safeguards, IFC Performance Standards, and ADB Safeguards.

	World Bank Safeguard Policies (2016 review and update not considered)	IFC Performance Standards on S&E Sustainability (2012)	ADB Safeguard Policy Statement (July 2009)
Related social safeguards	<ul style="list-style-type: none"> ✓ Involuntary Resettlement (2001) (4.12) ✓ Indigenous Peoples (2005) (4.10) 	<ul style="list-style-type: none"> ✓ Labour and Working Conditions (PS2) ✓ Community Health, Safety and Security (PS4) ✓ Land Acquisition and Involuntary Resettlement (PS5) ✓ Indigenous Peoples (PS7) ✓ Cultural Heritage (PS8) 	<ul style="list-style-type: none"> ✓ Selected working conditions included in Environmental Safeguards (SR1) ✓ Community Health, Safety and Security; as well as Gender included in Environmental Safeguards (SR1) ✓ Involuntary Resettlement (SR2) ✓ Indigenous Peoples Safeguards (SR3)

3 Methodology

3.1 Participants

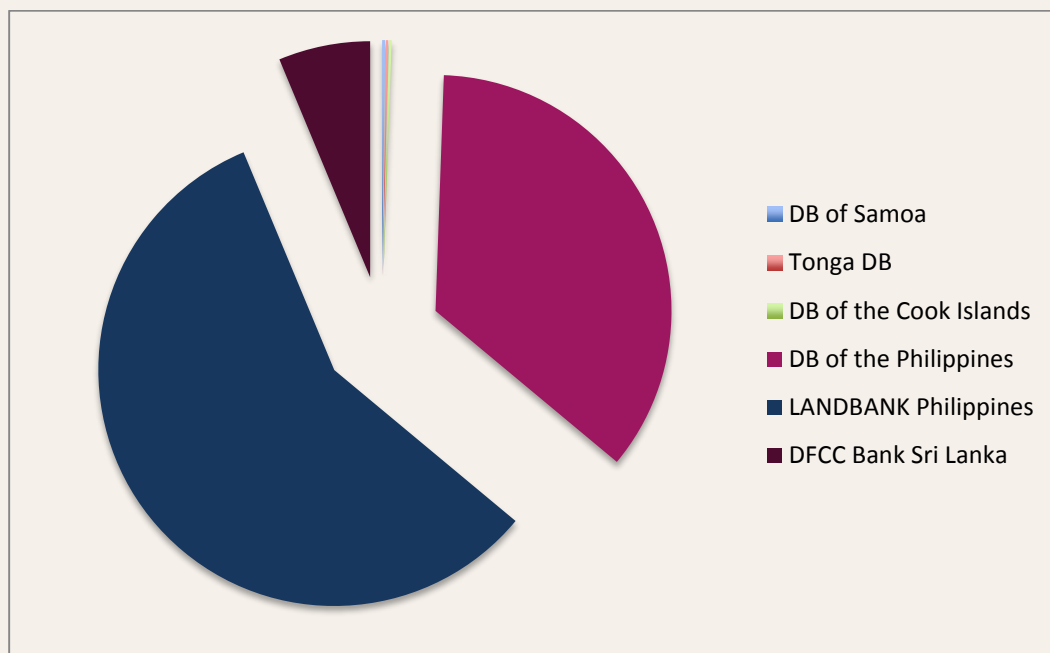
The study was launched by ADFIAP and the ILO at the Joint CEO Forum in Kuala Lumpur, Malaysia in November 2014. After the launch, the ADFIAP secretariat sent out an email invitation to the associations' membership and six DFIs from Asia and the Pacific signed up to participate. The study analysed the S&E policies and practices of these six DFIs. Table 2 lists the participating institutions and presents a brief overview of their ownership structure, assets, and main lending sectors. Apart from one DFI that is a public limited company, all other institutions are government-owned. The main economic sectors receiving funding vary across the institutions and range from tourism to agriculture, manufacturing, infrastructure and logistics, to providing housing and personal loans.

Table 2: Overview of DFIs participating in the study.

Participant	Ownership Structure	Total Assets	Priority Sectors
DB of Samoa	Government	57.5 million USD (as of 2013)	Industry, Agriculture
Tonga DB	Government	42.9 million USD (as of 2014)	Housing & Personal, Industry and Business
DB of the Cook Islands	Government	51.5 million USD (as of 2013)	Housing, Tourism
DB of the Philippines	Government	9.6 billion USD (as of 2013)	Infrastructure and logistics, Environment initiatives, Social services and community development, MSME
LANDBANK Philippines	Government	15.6 billion USD (as of 2012)	Agriculture & Fisheries
DFCC Bank Sri Lanka	Public	1.7 billion USD (DFCC Bank and DFCC Vardhana Bank) (as of 2013)	Manufacturing

As diverse as the priority sectors is the size of the balance sheets of the participating institutions, as shown in Table 2 and Figure 2. Naturally, the assets of DFIs in small island states are lesser such as 52.3 million USD in total assets for Tonga Development Bank. Total assets of the Development of the Philippines stood at 9.6 billion USD in 2013 and at 15.6 billion USD for the LANDBANK Philippines.

Figure 2: Total assets, compared across DFIs participating in the study.



In some countries, the participating DFIs have a substantial market share: The DB of the Cook Islands accounts for 11 % of total assets in the banking system in 2009, the LANDBANK of the Philippines for 9 % in 2009, and the DB of the Philippines for 5.5 % (De Luna-Martínez and Vicente, 2012). The DB of Samoa holds a share of 8.6 % in total assets in the financial system in 2006 (IMF, 2007).

3.2 Method

The analysis is mainly based on a document review. Specifically, the following documents were reviewed: S&E policies, S&E procedures or S&E manuals, descriptions of how S&E responsibilities are embedded in the organisational structure, training materials, tools and documentation of the actual implementation of the SEMS like completed credit appraisals, as well as sustainability sections of annual reports. In addition, outstanding queries were raised in individual written correspondence and telephone interviews during which open survey questions were discussed. The individual inputs substantiate the analysis and allowed to better take into account the specific circumstances of each DFI, perceived challenges and opportunities.

For each institution, the analysis established which building blocks of a SEMS exist and to what extent all relevant elements of each building block, as outlined in chapter 2 of this report, are covered. For this assessment, the following questions lead the analysis:

- How comprehensive, formalised, rigorous, documented, measurable-results orientated, inclusive and easy to implement is the concerned element?
- The analysis paid particular attention to the *social dimension* of the SEMS: how do the management systems consider the assessment and management of social risks and impacts (such as child labour or involuntary resettlement), and to what extent is this ensured by having or involving social experts and by providing training to staff on social risks, impacts, and opportunities?

To analyse each of the six building blocks, we employed a set of indicative questions. Each set of questions was assigned a maximum score, which could be attained. The maximum score was then weighed with a factor between 0.0 and 1.0 (in steps of one tenth) with 0.0 being the lowest and 1.0 being the highest possible value. Table 3 summarises the maximum scores that each SEMS building block could achieve.

Table 3: Building Blocks of a SEMS.

Building Block of a SEMS	Maximum Scores
1) Social & Environmental Policy	15
2) Social & Environmental Standards	5
3) Social & Environmental Procedures	42
4) Social & Environmental Responsibilities	15
5) Social & Environmental Skills and Training	18
6) Social & Environmental Reporting	5
Overall	100

Institutions that did not have any elements of a formal SEMS could reach a maximum of 20 points. In this case, we assessed how comprehensively and rigorously elements of a SEMS are applied *informally* and to what extent the institution commits itself to develop a formal system.

To compare the current state of SEMS implementation across the different institutions, we clustered the DFIs according to similarity in i) scores reached in each building block and ii) qualitative comments. This approach allowed grouping the institutions along similar opportunities for improvement.

At the end of this methodology section we need to mention that the analysis has certain limitations: First of all, we worked with a small and non-representative sample of DFIs. Therefore, no conclusions can be drawn on the state of the art in the whole industry in Asia and the Pacific. Furthermore, some institutions provided more detail than others, e.g. due to confidentiality issues. In addition, we could not look at *all* elements of the SEMS, e.g. at all tools that are being used, neither could we study several examples of how one institution applies its SEMS (e.g. several completed credit appraisals). The examples provided by the institutions were self-selected and hence may represent positive cases and not necessarily the average. Due to the small number of participants, elaborate descriptive statistics would not add value to the analysis and thus results are presented by qualitative description. Lastly, and most importantly, this analysis is based on desk research and has therefore some inevitable limitations in breadth and depth.

4 Survey Results

4.1 Identification of DFI clusters

The analysis identified five clusters that represent different stages of SEMS implementation among DFIs:

- **Cluster “Advanced and balanced SEMS”**
DFIs with formal and comprehensive SEMS that address social and environmental concerns in a balanced manner;
- **Cluster “Advanced SEMS with bias”**
DFIs with formal and comprehensive SEMS that are biased towards either social or environmental themes;
- **Cluster “Early stage SEMS”**
DFIs with formal SEMS with significant room for improvement;
- **Cluster “S&E Policy”**
DFIs that have adopted an S&E Policy without having a system in place for its implementation;
- **Cluster “No SEMS”**
DFIs without formal SEMS.

The following paragraphs describe each cluster and indicate the distribution of the participating DFIs across the clusters.

Cluster “Advanced and balanced SEMS” would include institutions that have a Social and Environmental Management System which is formal, comprehensive, advanced, and balanced towards social and environmental issues. The majority of building blocks as well as the overall scores of this cluster should reach at least 76% of the maximum scores. None of the participating DFIs belongs to this cluster.

Cluster “Advanced SEMS with bias” includes institutions that implemented a formal, comprehensive and advanced Social and Environmental Management System. However, either the environmental or the social dimension is significantly more developed than the assessment and management of the other. The majority of building blocks as well as the overall scores of this cluster obtain between 65% and 75% of the maximum scores. Two institutions were identified in this cluster. On average, they scored 67.45 out of the maximum 100, while being biased towards environmental considerations.

Cluster “Early stage SEMS” consists of institutions that have a formal Social and Environmental Management System in place. However, the SEMS is significantly less comprehensive and fine-tuned than in the previous clusters. In general, this cluster may or may not have a bias towards either social or environmental themes. The majority of building blocks and the overall scores of this cluster receive between 50% and 64%. We found one institution in this cluster that scored 55 out of 100. Similar to the aforementioned cluster, this “Early stage SEMS” institution also shows some strength in terms of environmental management to the detriment of the social dimension - but to a weaker extent than the cluster “Advanced SEMS with bias”.

Cluster “S&E Policy” includes institutions that have an S&E Policy but lack a *formal* system to implement the policy. As in the previous clusters, this cluster may or may not have a bias towards either social or environmental themes. The majority of the building blocks and the overall score of these institutions receive between 21% and 49% of the maximum scores. None of the participating DFIs belongs to this cluster.

Cluster “No SEMS” is comprised of DFIs that have no formal Social and Environmental Management System in place. These DFIs can obtain a maximum score of 20 out of 100. Three of the participating institutions belong to this cluster. On average, the institutions scored 4.67. Despite the low score, the DFIs in this cluster do have a

number of the informal SEMS elements in place and they confirmed their commitment to develop a formal SEMS in the future.

Table 4 summarises the classification of clusters as well as the distribution of participating DFIs across the clusters and indicates the average scores that the DFIs reached.

Table 5: Clusters of DFIs presenting stage of SEMS implementation.

Cluster	Description	Range of Scores	# DFIs	Average Score
Advanced, Balanced SEMS	Social and Environmental Management System which is formal, comprehensive, advanced, and balanced towards social and environmental issues	76 - 100	0	-
Advanced SEMS with bias	Advanced, formal Social and Environmental System with a bias towards social or environmental concerns	65 - 75	2	67.45
Early stage SEMS	Less advanced, though formal Social and Environmental System, significant opportunities for improvement in Social & Environmental Dimension	50 - 64	1	55
S&E Policy	S&E Policy, without having installed a system yet to implement the policy	21 - 49	0	-
No SEMS	No formal Social and Environmental System (neither policy, nor procedures)	0 - 20	3	4.67

The subsequent sections report the analytic results for the three clusters to which DFIs from Asia and the Pacific could be assigned:

- Cluster “Advanced SEMS with bias”,
- Cluster “Early Stage SEMS”, and
- Cluster “No SEMS”.

At first, the level of implementation of each SEMS building block is described and, where applicable, additional noteworthy developments are highlighted. Then, the challenges encountered in SEMS development and implementation are summarised per cluster.

4.2 Cluster “Advanced SEMS with bias”

Two of the participating DFIs fall in this cluster, which is characterised by having an advanced SEMS, which, however, is biased towards either environmental or social themes. On average, the two institutions score between 65% and 75% in five out of the six building blocks and are biased towards environmental considerations. Only one building block, namely S&E standards, scored lower with 50%. Table 5 summarises the scores of the two DFIs in this cluster.

Table 6: Average scores per SEMS building block of DFI cluster “Advanced SEMS with bias”

Building Block	Maximum scores	Average score	Average score in %
Total	100	67.5	67.5
S&E Policy	15	9.9	65.7
S&E Standards	5	2.5	50
S&E Procedures	42	28.1	66.9
S&E Responsibility	15	10.9	72.3
S&E Training	18	12.2	67.5
S&E Reporting	5	4	80

The following paragraphs provide the detailed analytical results per SEMS building block.

Building Block 1: S&E Policy

The institutions in cluster “Advanced SEMS with bias” show a clear commitment to sustainable development and provide the rationale for their commitment. Driven by the respective regulatory environments, sustainability is rather understood in its environmental implications. As a result, social concerns are considered especially in relation to community engagement, which may include community safety, health and security, indigenous peoples, involuntary resettlement, and cultural heritage. However, these are not formally mentioned in the policies. Furthermore, neither commitments on labour and working conditions - specifically occupational safety and health, child labour, forced labour, workers organisations and non-discrimination - nor gender equality feature formally in the institutions’ S&E policies.

The S&E policies of the two DFIs in this cluster have a strong focus on stakeholder inclusion. One institution has an exemplary approach of including stakeholders in the development of products, which is an opportunity to learn about the special needs of minorities and women.

Building Block 2: S&E Standards

Both institutions, rather than drawing up own institutional safeguards, orient their S&E safeguards on international standards like ISO 14001 or national regulations. The safeguards that underpin the SEMS are strong for environmental management. However, they are not comprehensive and lack detail to address social concerns. We also note that not all relevant international conventions and national laws are considered.

An example for inconsistent consideration of social concerns is an institution that does not formally include safeguards on community engagement in its S&E standards. However, the reviewed monitoring reports show that the institution requires borrowers to adhere to Free Prior and Informed Consent (FPIC) with regards to the affected community. In order to ensure that FPIC is applied consistently, the principle should be included formally in the S&E safeguards.

Building Block 3: S&E Procedures

The S&E procedures of the two “Advanced SEMS with bias” institutions are comprehensive, rigorous, detailed and measurable-results orientated for *environmental* management. Environmental assessment and management is consistently aligned with the credit cycle, includes all standard elements as described in chapter 2.1, and due diligence and monitoring formats are standardized and detailed. Selective *social* elements are taken into account, however, inconsistently over the S&E assessment and management cycle. For instance, whereas occupational safety and health topics are considered, the assessment does not inquire or document whether the client’s project

involves any form of involuntary resettlement, has negative impacts on indigenous peoples (such as loss of identity, culture, exposure to impoverishment or disease etc.), pays below minimum wage or prohibits workers' organisations. Furthermore, while occupational safety and health (OSH) is covered in the S&E assessment, the monitoring template did not have a section for reporting OSH issues. Another example is performance measurement: One institution looks at sustainable development impact by including CO2 emissions avoided and replacement of fuel-oil. However, social impact indicators on job creation or job creation for women and minority groups are missing.

Building Block 4: S&E Roles and Responsibilities

The two institutions of the cluster "Advanced SEMs with bias" have different but effective approaches of distributing S&E roles and responsibilities. Whereas one DFI has an environmental department consisting of environmental officers and technical staff that collaborate with account officers, the other DFI announces responsibilities through office orders and has S&E champions and positions in the relevant departments of the organisation. Both approaches are valid as long as, in the first case, sufficient collaboration with account officers is ensured, and appropriate training is available in the latter. Having S&E champions would be an effective tool for both scenarios in order to mainstream S&E responsibilities and anchor a sustainability vision throughout the organisation. As in all other building blocks, however, the main focus is on environmental issues. This is not surprising as it is a consequence of the lack of comprehensive social safeguards which reinforces a weak social assessment.

On the board level, both institutions have some members with a development background. One institution is also strong in having an inclusive board with men and women of different backgrounds which is important for guiding and enforcing a triple bottom line and ensuring a good sustainability leadership.

Whereas one institution mainly hires external environmental experts, the other promotes internal candidates and provides according environmental training. The advantages of internal promotions are the integration of financial and S&E responsibility. Hiring external experts, however, acknowledges a certain status of S&E experts as well as another perspective that can genuinely be brought into the organisation.

Building Block 5: S&E Skills and Training

Both DFIs in the cluster "Advanced SEMs with bias" internally offer *environmental* training to staff which is conducted by the Human Resource or the Environmental Department. Furthermore, access to external trainings by the Ministry of Environment is facilitated for specialists. The training is tailored to the institution and focuses on environmental areas that are deemed to be important, such as renewable energy or updates of environmental regulations.

Exposure to continuous training on developments in environmental and social legislation and regulation is important to ensure having a management system that is up-to-date. Only one of the institutions offers human rights related training (including gender and development, sexual harassment, social conflicts, grievance mechanism).

Building Block 6: S&E Reporting

Both DFIs in the cluster "Advanced SEMs with bias" have published several sustainability reports. The DFIs use the Global Reporting Initiative (GRI) guidelines that allow comparing an institution's sustainability approach with other institutions in a standardized way.

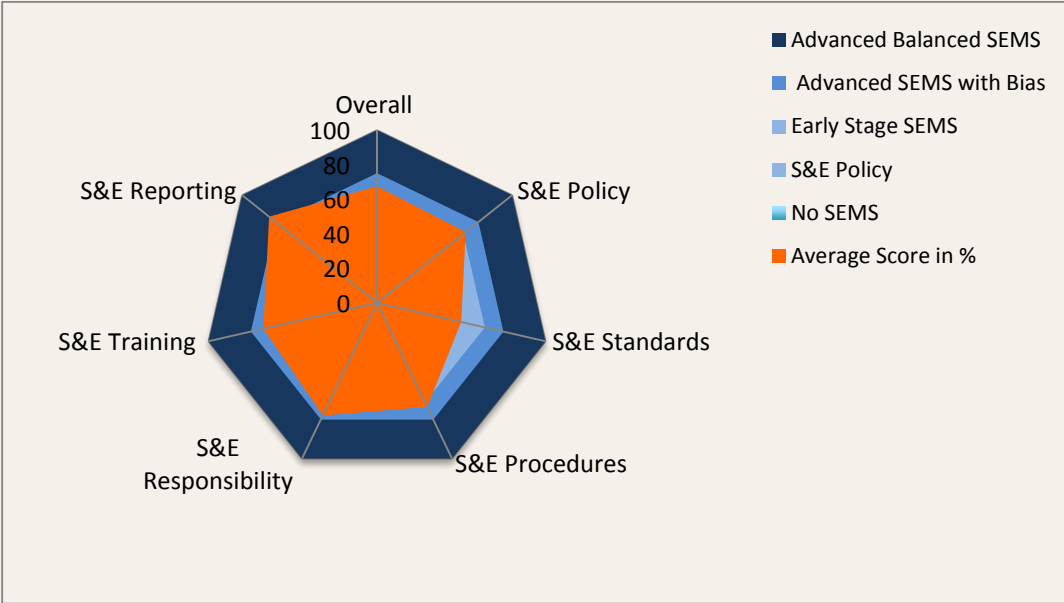
The DFIs report on S&E risks, impacts, and opportunities. Reporting on *risks* relates to environmental protection and management. S&E *impact* reporting related to environmental management monitoring results regarding the banks' resource consumption and greenhouse gas emissions, specific environmental programs, such as a

Forest Programme and its impact, or impacts of social programmes, such as an Education Programme that supported 1,312 scholars as of end-2011, including indigent high school graduates or a Food Supply Chain Programme to increase farmers’ income. Furthermore, the institutions reported on social, environmental, and developmental opportunities, such as lending and investing to priority sectors (e.g. infrastructure and logistics, social services and community development, small farmers and fisher folk, and MSMEs) or collaboration with a public-private partnership on climate change, disaster preparedness and sustainability. Additionally, reports contained information about S&E management systems certification and received S&E awards. Exemplary is the approach of one institution to organise its report systematically along sustainability areas that are key for the institution like enterprise development, community development, environmental protection and management, customer service and employee development.

The DFIs in this cluster provide quarterly internal S&E management reports. These reports are important tools to ensure that senior management and the board is aware of the overall S&E risks in the portfolio and can take strategic action as necessary.

Figure 3 graphically anchors the main findings for DFIs in the cluster “Advanced SEMS with bias”. The blue areas of the spider graphic illustrate the range of scores that define each DFI cluster. The orange area shows how the DFIs in the cluster “Advanced SEMS with bias” actually scored.

Figure 3: Average scores of DFIs reached, in per cent, per SEMS building block in cluster “Advanced SEMS with bias”.



Challenges of DFIs in the cluster “Advanced SEMS with bias”

Both institutions are committed to further develop their SEMS, including the consideration of social issues. However, the DFIs perceive multiple challenges.

Firstly, the institutions experience a lack of awareness of relevant social and environmental laws and regulations on the side of project owners. Secondly, this cluster sees a challenge in the fact that only a few lending institutions acknowledge the importance of social and environmental management systems and implement the same. As a consequence, this lack of awareness in the business community is perceived to lead to disadvantages in a competitive banking sector. Directly related is the lack of

supervision and regulation by the relevant authorities, including the central bank, of the social and environmental performance of financial institutions.

Both institutions were incentivised to develop the social SEMS dimension due to the requirements of overseas development assistance institutions. The cluster does plan and work on rolling out a more balanced consideration of social aspects across the whole portfolio - as far as the challenges just described allow them to do so. Involuntary resettlement, indigenous peoples, child labour, and attention to gender issues were mentioned as the most pressing social issues to be further addressed.

4.3 Cluster “Early Stage SEMS”

DFIs in the cluster “Early Stage SEMS” are characterised by having a formal social and environmental management system. However, the SEMS building blocks have significant room for improvement in terms assessing S&E risks, impacts, and opportunities in more detail and more comprehensively. This cluster is composed of 1 DFI. Typically, the average score defining this cluster would be between 50% and 64%. However, the distribution of individual scores per SEMS building block make it difficult to precisely position the DFI: in two of the SEMS building blocks, namely S&E policy and S&E reporting, the institution scores above 65%. In two other building blocks, namely S&E standards and S&E responsibility, the institution scores below 50%. Scores for S&E procedures and S&E training are within the range of the cluster “Early Stage SEMS”. Table 6 summarises the scores of the one DFI in this cluster. Given the overall score of 55%, we assigned the institution to this cluster.

Table 7: Average scores per SEMS building block of DFI cluster “Early Stage SEMS”.

Building Block	Maximum scores	Average score	Average score in %
Total	100	55	55
S&E Policy	15	10	66.6
S&E Standards	5	1	20
S&E Procedures	42	24.7	58.8
S&E Responsibility	15	4.9	33
S&E Training	18	10.8	60
S&E Reporting	5	3.6	72

The following paragraphs provide the detailed analytical results per SEMS building block.

Building Block 1: S&E Policy

The S&E policy of the one DFI in this cluster covers social and environmental issues - the latter in more detail - and provides a rationale for the commitment to sustainable development. However, this cluster lacks a formal and clear approach towards community engagement, specifically when it comes to indigenous peoples and involuntary resettlement. The policy is also less engaged with the relevant legal framework as will be discussed below.

Building Block 2: S&E Standards

Similar to DFIs in the previous cluster, the institution in the cluster “Early Stage SEMS” has not developed own institutional S&E safeguards that lead the S&E assessment process. The safeguards are only broadly linked to the applicable legal framework. The environmental standards refer to the relevant Environmental Protection Act, whereas the social standards only commits to comply with relevant governmental laws and regulations related to labour and working conditions including child labour and forced

labour, and cultural heritage without mentioning the explicit laws or further specifications. These become, to some extent, more explicit when the related S&E procedures are applied.

Building Block 3: S&E Procedures

The S&E procedures are rather comprehensive as they cover the whole loan cycle from assessment, mitigation, to monitoring. S&E performance is measured at the end of financing a project and includes some social indicators like employment. The DFI also explicitly takes into account S&E risks when defining the interest rate for loans.

However, the S&E procedures could be more elaborate and granular. To a certain extent this results from the lack of explicit safeguards mentioned in building block 2. In addition, the examples provided for credit assessment and monitoring lack comprehensiveness (i.e. few critical areas being tackled) as well as detail. For instance, neither do the S&E standards define what adequate “working conditions” are, nor do the procedures include guidance for the same which makes it difficult for staff - if not arbitrary - to assess actual working conditions. Complementary tools like categorisation tools or checklists for assessment and monitoring activities are not part of the S&E procedures augmenting the challenges in implementing the SEMS.

Building Block 4: S&E Roles and Responsibilities

Overall, S&E-related roles and responsibilities are not clearly documented. However, this is important to mainstream S&E management. Only when roles and responsibilities are clear, necessary work can be accomplished and staff can be held accountable for activities and results and therefore have an incentive to take S&E serious.

While the DFI has an Environmental Officer with comprehensive and relevant tasks, a sole *environmental* position leads to a focus on *environmental* concerns.

The institution in the “Early Stage SEMS” cluster also has a number of board members with a development background which is a constructive basis for effectively anchoring S&E in the organisation’s development.

Building Block 5: S&E Skills and Training

The institution takes training seriously, which is important to enable staff to implement the S&E procedures correctly. The Environmental Officer, as well as other employees, have participated in several externally provided trainings, e.g. on energy conservation, human rights, and environmental issues in project lending. Social issues could be included in the trainings to be in line with the stipulated sustainability approach of the institution.

While the training received is a positive sign, it is not yet guided by a comprehensive S&E training strategy. Neither is it integrated into the overall institutional capacity building framework and performance management system. However, plans exist to build-up an S&E training strategy.

Building Block 6: S&E Reporting

It is worth pointing out that the DFI in this cluster reports along GRI reporting guidelines. As mentioned before, this allows comparing the institution’s sustainability approach with other institutions in a standardized way. Using GRI guidelines for sustainability reporting could improve reporting practice for other DFIs in this cluster.

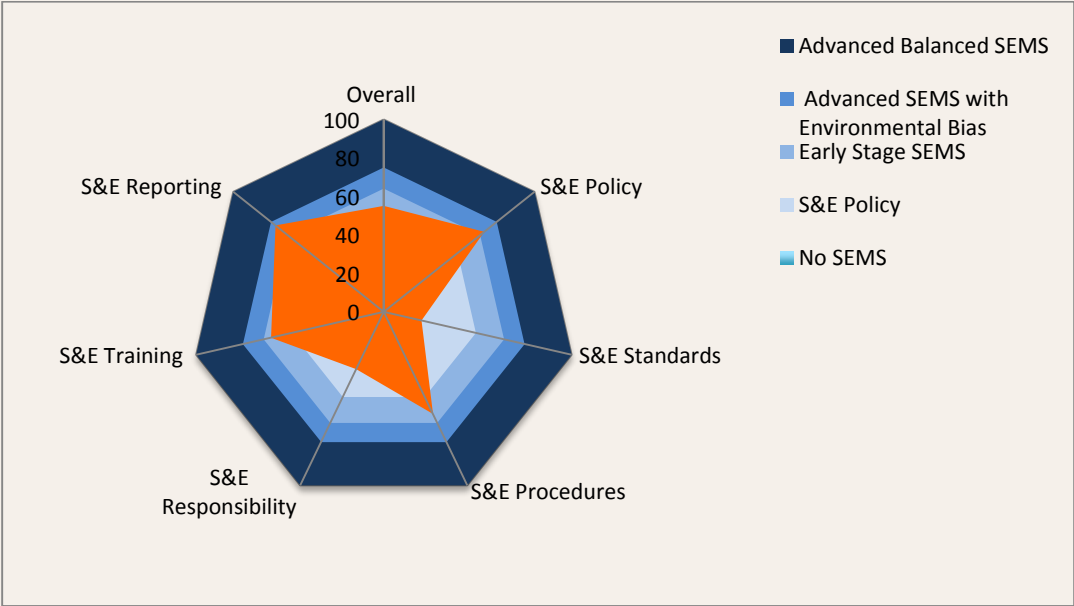
The DFI reported on risks, impacts, as well as on opportunities. In terms of *risks*, the DFI mentioned the projects’ compliance with standards defined by the respective Environment Act and rules and regulations of the Environmental Agency. Compliance with similar social regulations was not mentioned. Reported *impacts* were GHG emissions and the management of resource consumption. *S&E opportunities* were

sought through investments in infrastructure, housing and renewable energy, financing for fragile regions of the country, SMEs, rural entrepreneurs and micro finance institutions for on-lending. Furthermore, the DFI reported to support environmental initiatives and Corporate Social Responsibility (CSR) activities.

Internal reporting to senior management and the board could be strengthened to ensure that the highest decision level knows what S&E risks the institution is exposed to and can include S&E considerations in strategic decisions.

Figure 4 graphically anchors the main findings for the DFI in cluster “Early Stage SEMS”. The blue areas of the spider graphic illustrate the range of scores that define each DFI cluster. The orange area shows how the DFI in the cluster “Early Stage SEMS” actually scored.

Figure 4: Average scores of DFIs reached, in per cent, per SEMS building block in cluster “Early Stage SEMS”.



Challenges of the DFI in the cluster “Early Stage SEMS”

The institution is aware and concerned about the gaps in its approach towards sustainability. Particularly, the need to fine-tune tools and the whole system, to increase knowledge of staff, as well as to keep the Environmental Manager up-to-date with current developments are issues of concern. The institution is committed to develop the system, to build internal capacity, and to benchmark its procedures against industry standards.

Interestingly, the institution emphasised that it did not perceive the challenge of losing clients due to S&E management. Instead, clients themselves saw value in it. This seemed especially true for new and green industries. Nevertheless, it is yet to be seen how clients will react in case of stronger S&E management. It is expected that well-established clients will appreciate the effort, whereas SME clients might not necessarily do so. In terms of industries, the bank might lose clients from well-established industries with easy access to finance, whereas this problem should not arise for companies from less established sectors.

4.4 Cluster “No SEMS”

Institutions in the cluster “No SEMS” do not have a formal SEMS, including formal S&E policies or procedures. In our sample, three out of the six participating DFIs belong to this cluster. While the three institutions do not have a formal system, the analysis identified a number of informal SEMS elements that exist in all three institutions. The informal elements relate mainly to building block 3 and 5 and are described below.

Building Block 3: S&E Procedures

The DFIs in cluster “No SEMS” do address certain social and environmental concerns in their credit appraisals, however, not in a consistent or comprehensive way. The consideration of S&E topics takes place for legal compliance reasons.

The institutions set ad-hoc requirements, like asking for compliance with health and environmental regulations in specific economic sectors, conducting environmental impact assessments (EIAs) in case of the likelihood of hazardous waste and environmental pollution. From time to time, the DFIs require feasibility studies which may include certain S&E elements, or they ask project owners to obtain forms dealing with environmental and social compliance from regulators, such as a development consent form or a disaster recovery plan. However, there are no formal procedures and the informal procedures were applied only in few exceptional cases.

In two of the three DFIs, the related S&E documentation is filed, however, not in detail. The institution requiring the clients to conduct EIAs does include relevant results in the credit appraisal. Once it also included a special condition in the loan agreement that the Ministry of Environment needed to approve the EIA.

In addition, one of the three institutions reported to direct funds particularly towards women’s income generating projects as well as towards projects of NGOs, youth and women groups. Although no formal impact measurements are conducted, the bank qualitatively assesses whether income and living standard of youth and women groups have improved through visits and talking with clients.

Building Block 5: S&E Skills and Training

Two institutions reported that their Ministry of Environment provided technical training on renewable energy, disaster resilience, and selected environmental risks. One institution has sent lending staff to those trainings, the other one plans to send lending staff in the future. Such training is happening on an ad hoc basis when available. It is neither integrated into an S&E training strategy nor into an overall institutional capacity building framework.

Noteworthy addition: Commitment to develop a formal SEMS

All institutions in this cluster expressed their interest to develop a more structured and consistent approach towards social and environmental management. However, no institution has made concrete steps like developing an action plan, including a timeframe and the assignment of clear responsibilities, as of yet. One DFI is considering the possibilities of including S&E aspects across its lending procedures while reviewing the lending manual.

The reasons for thriving for change arise from increasing environmental and climate change awareness, the aim to keep up with a changing legislation and business environment, the aim to address inequalities between income segments, as well as from the awareness of the repercussions of S&E risks on the financial performance of the bank.

Challenges of DFIs in the cluster “No SEMS”

Some DFIs in the cluster “No SEMS” perceive it a challenge to develop social and environmental policies and procedures that are adjusted to the specific circumstances of their respective countries and to the various economic sectors that they are lending to.

All of the DFIs reported that they lack the internal capacity to develop a structured management approach and would require external assistance. Given that some assistance is available for developing capacity for environmental risk and impact assessment, the challenges to build capacity and set up a management system that includes and balances the social dimension became evident. One institution also mentioned the challenges to provide internal or attract external funds for SEMS improvements.

5 Conclusions and Way Forward

5.1 Conclusions

This study was founded on the observation of the ILO and ADFIAP that recent developments in sustainable finance - in particular the implementation of Social and Environmental Management Systems - were characterised by a stronger focus on environmental elements, while social topics received less attention. In addition, the two organisations were convinced that DFIs need to balance both dimensions in order to be able to truly promote sustainable development. Therefore, the ADFIAP and ILO jointly launched a study investigating the extent to which DFIs in Asia and the Pacific have implemented formal Social and Environmental Management Systems with a particular focus on the level of inclusion of the social dimension. Overall, six DFIs based in the Cook Islands, the Philippines, Samoa, Sri Lanka and Tonga participated in the study.

In a first step, the study identified **six building blocks** of a Social and Environmental Management System:

- **Building block 1: S&E Policy**
- **Building block 2: S&E Standards**
- **Building block 3: S&E Procedures**
- **Building block 4: S&E Responsibilities**
- **Building block 5: S&E Skills and Training**
- **Building block 6: S&E Reporting**

In a second step, S&E-related documents received from the participating DFIs were analysed and points for each building block of an institutional SEMS given to the individual DFIs. The results allowed clustering the participating institutions according to similarity in i) scores attained in each building block and ii) qualitative comments. The study identified **five clusters** that showed similar characteristics and opportunities for improvement:

- **Cluster “Advanced and balanced SEMS”**
- **Cluster “Advanced SEMS with Bias”**
- **Cluster “Early Stage SEMS”**
- **Cluster “S&E Policy”**
- **Cluster “No SEMS”**

Two of the participating DFIs were classified as belonging to the cluster “*Advanced SEMS with Bias*”, one to the cluster “*Early Stage SEMS*”, and three to the cluster “*No SEMS*”.

The main findings across all clusters - including the perceived challenges of the DFIs - are summarised below:

Building Block 1: S&E Policy

If S&E policies exist, the DFIs generally reached high scores in comparison to other SEMS building blocks. The main gaps identified are a bias towards addressing environmental elements, which confirmed the validity of engaging in this study. This observation is equally true for those institutions that have not yet implemented a formal SEMS. The comparatively high scores for S&E policies reveal that the main challenges relate to the actual implementation of the policies i.e. S&E procedures, adequate staffing and training.

Building Block 2: S&E Standards

Overall, the participating DFIs received the lowest scores for their S&E standards. None of the participants has developed own institutional safeguards, based on good

international practices *and* adopted to the national or local context. Since, ultimately, the whole SEMS is based on the safeguards, it is of utmost importance to have comprehensive, inclusive, and adjusted safeguards that are described in detail. Otherwise, the gaps will loop back to incomplete S&E procedures, tools and applications of the SEMS, and safeguards will be applied inconsistently on a case-to-case basis. The DFIs with higher scores were in line with national regulatory requirements that originated from the Ministries of Environment. In like manner, the institutions from cluster “No SEMS” reported collaboration with these ministries. A focus on environmental risks and impacts is a natural consequence and could be balanced through further collaboration with the Ministries of Labour.

Building Block 3: S&E Procedures

The three institutions having a formal SEMS did have more or less advanced S&E procedures that were comprehensive, consistent, rigorous and measurable results oriented. Overall, social topics were not systematically integrated in the S&E procedures implying that some social elements were considered when assessing loan applicants and while others when monitoring. Furthermore, applications of the SEMS (e.g. credit appraisals, monitoring reports, final impact measurement of a project) showed less detail in social compared to managing environmental topics. In line with this observation goes a lack of detail in tools (report formats, sectoral guidelines) when social concerns were at stake. For the institution of the cluster “Early Stage SEMS”, the described lack of detail was valid for addressing both social and environmental topics.

On a more specific note, we observed that only one participating DFI considered S&E risks in the overall credit risk rating for pricing purposes. For one other DFI, S&E compliance was a requirement for the renewal of a loan. None of the institutions has arrangements such that interest rates can be adjusted depending on accomplishment of social and environmental milestones (e.g. income increase of smallholder farmers linked to funded project).

Building Block 4: S&E Responsibilities

The study found institutions do hire environmental experts, however, there are no equivalent experts on social topics. Given the different sizes of the DFIs, each institution has to find a balance between individual specialists which may be possible for larger institutions or a combined profile of social and environmental manager.

The boards of directors of the participating institutions were included in sustainability matters through provision of internal management reports and overall responsibility to implement the SEMS. However, in none of the institutions did the board have a specific S&E or sustainability guidance committee or responsible member.

The DFIs with an advanced system did include S&E training in an overall institutional capacity building strategy and aligned compensation with S&E performance for technical S&E staff and S&E management positions. Providing incentives can be an important step to improve S&E performance especially if the organisation has competing goals and limited budget.

Building Block 5: S&E Skills and Training

Overall, the DFIs did take training serious and received relatively high scores for the building block. However, training currently offered by or accessible to the DFIs mainly focused on environmental issues in the lending process like energy efficiency. Social topics were included by some institutions in the form of human rights trainings. However, social and environmental training was not combined. There are also no trainings on specific social risks and impacts, such as involuntary resettlement or child labour as it is the case for environmental topics like pollution, energy efficiency or climate change.

Building Block 6: S&E Reporting

This survey has shown that all three institutions having a SEMS report along GRI guidelines. This is worth pointing out and a good incentive for other institutions to follow suit. The DFIs consistently reported about S&E risks, impacts and opportunities. Whereas especially opportunities were sought to support socially inclusive and environmentally friendly development, reporting on management of S&E risks had a strong focus on *environmental* risks - which is in line with the results of the other building blocks.

Challenges across DFI clusters

Mainly four themes of challenges appeared over and again in the survey.

On the one hand, several, but not all, institutions face a ***lack of awareness regarding social and environmental laws on the side of the project owners*** seeking finance.

Related is the ***lack of social and environmental regulation by the respective central banks***. Whereas central banks in Bangladesh, China and Indonesia - which are part of the Sustainable Finance Network - do attempt to include S&E elements in the regulation of the financial institutions within their reach, this is not the case for the central banks of the DFIs that participated in the study. This fact leads to a lack of S&E management systems by competitors. Due to ***stiff competition*** in the respective banking sectors of the participants, these challenges result in fear of losing clients.

Furthermore, most of the participants where interested in developing their approach towards better managing social risks, impacts and opportunities but mentioned a ***lack of internal capacity*** to do so.

5.2 Suggestions on ways forward

This last section reflects on potential ways forward inspired by the results of the study. In the following, ideas for ways forward are presented along the main stakeholder groups identified by the survey.

The study identified three stakeholder groups that are relevant for improving the social impact of development finance in Asia and the Pacific:

- DFIs
- Central Banks
- Ministries of Environment, and Ministries of Labour

To unlock the positive social impact of development finance, these three stakeholder groups could benefit from capacity building and research:

- Awareness / Sensitisation
 - Training
 - Mentoring
 - Consulting
 - Helpdesk platform
 - Research
- } Capacity building

The next paragraphs describe activities for each stakeholder group and touch on both capacity building and research elements.

1) DFIs

Capacity Building: The analysis revealed several options for capacity building for DFIs, including *sensitisation*, *training*, *mentoring*, *consulting*, and the set-up of a *helpdesk*.

The ILO, ADFIAP and other collaborators could jointly develop and facilitate *sensitisation* and *training* for DFIs on why and how to incorporate a stronger management of social concerns into their current social and environmental management systems or sustainability approaches. The implementation thereof could entail:

- Sensitisation at the board level;
- Management training, targeting senior or middle management of DFIs; or
- Technical training on social risk assessment addressing, for instance, child labour or involuntary resettlement, targeting middle management or operations staff of DFIs.

Such capacity building could be organised through national workshops, institutional training, longer-term distance learning facilities, or *mentoring programs* that could include study visits or temporary staff exchanges through staff development programmes.

In addition, an online platform could be developed to allow DFIs mutual *mentoring*: to share good practices, learn from each other, exchange on recent developments in social and environmental legislation, and develop and share information about a pool of S&E expert consultants. Such an online platform could entail a “*helpdesk*” where the ILO or ADFIAP could provide support to answer specific questions (e.g. related to the development of tools). Another feature of the platform could be the hosting of the “ILO SEMS Assessment Tool” which was developed for this study and has been presented to some extent in chapter 2.1. Access to this tool could allow other DFIs and other sustainable finance providers to self-assess and benchmark their S&E practices. Similar platform concepts are already administered by the International Trade Centre for agricultural value chains³, or by the ILO for multinational companies seeking advice on International Labour Standards⁴. Such a platform would be a sustainable contribution to the suggestion of the report by the Intergovernmental Committee of Experts on Sustainable Development Financing advocating for the establishment of facilitative platforms to encourage coordination among international funds and initiatives, as well as joint platforms for investor groups.

Research: The design and set-up of a new SEMS or the improvement of an existing SEMS by integrating social concerns could be accompanied by vigorous research drawing from the ILO Social Finance Programme’s expertise in researching social impacts of innovative financial services and tools. Research based on robust methodologies could shed light on the impact of improving one SEMS building block on i) other building blocks of the SEMS (“internal trickle down effects”), ii) on the S&E quality of the lending portfolio, and iii) a cost-benefit analysis could be conducted. Potential research questions are:

- To what extent does alignment of social safeguards with national legislation (building block 2) improve the S&E procedures (building block 3) of a DFI and strengthens social topics in the due diligence, credit appraisals, monitoring, and impact measurement? How do supporting tools, such as appraisal and monitoring formats, checklists, or data collection tools, benefit from better alignment?
- What is the impact of aligning social safeguards with national legislation on the S&E quality of the lending portfolio? Baseline, mid-term and endline data over 3-5 years would need to be collected and analysed. Simultaneously, tools for continuous data collection and decision making could be developed, tested, improved, and shared.
- How large are the benefits of technical training on social risks and impacts in comparison to the costs of conducting the training? Benefits could arise, for

³ <http://www.sustainabilityxchange.info/>

⁴ <http://www.ilo.org/empent/units/multinational-enterprises/lang--en/index.htm>

instance, through a decrease of client defaults and delayed payments, as well as a reduction in fines related to liabilities. Results could shed light on whether or not a “business case for S&E for DFIs” exists.

Research results should be discussed at regional conferences or national S&E workshops to share with other relevant stakeholder groups.

2) Central Banks

Capacity Building: The analysis revealed several options for capacity building for central banks, including *awareness raising*, *sensitisation* and *training*. The need for *raising awareness* of central banks to ultimately encourage them to demand financial institutions under regulation to report on sustainability indicators, as well as to make certain sustainable financial practices mandatory, was suggested by the DFIs participating in the study. To this end, the ILO and ADFIAP could encourage and help central banks to learn about experiences of institutions currently implementing regulatory approaches to guide and foster FI’s actions towards sustainability (e.g. Indonesia, Bangladesh, China, Nigeria, and Brazil). As a second step, *training* could be developed and facilitated by the ILO, ADFIAP, and other relevant stakeholders to support central banks in the design and implementation of such an approach.

3) Ministries of the Environment and Ministries of Labour

Capacity Building: The analysis identified several options for the building capacity of relevant ministries, specifically focussing on *awareness raising* and *sensitisation* as a first step, and *training* to follow suit. Collaboration between the Ministries of the Environment and Ministries of Labour and other national and local authorities could facilitate the integration of a social component in national regulatory approaches targeting the environmental impact of FIs - such as the Philippine Environmental Impact Statement System. If there is interest from the named parties, the ILO and ADFIAP could help build capacity to develop and implement balanced regulatory approaches towards a sustainable financial system by providing *training workshops*.

As discussed in the introduction of this report, capacity building for DFIs to assist making measurable progress towards sustainable development is well in line with the recommendations of the UN Intergovernmental Committee of Experts on Sustainable Development Financing. Likewise, the suggestion to extend capacity building to central banks and the ministries of the environment as well as the ministries of labour, would be a valuable contribution to the committee’s proposition to encourage joint reporting not only on financial return but also on environmental and social impacts; to invite regulators to create regulatory frameworks that encourage sustainable practices (e.g. by providing certain portfolio requirements); as well as to invite governments to encourage financial market players to train their employees on social and environmental issues (UN General Assembly, 2014).

The DFIs that participated in this study expected to be able to benchmark their S&E practices against industry standards, to get a better understanding of the current gaps in their systems and approaches, to be in a better position to find access to external technical assistance, and to get support in raising awareness within the national context for the importance of regulating and managing social and environmental risks and impacts. We hope that this report provides some relevant input to these DFIs and we look forward to the results of making the learnings of the study available to other DFIs and stakeholders of development finance who are interested in unlocking further positive social impact of development finance.

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