Asia-Pacific Economic Cooperation

ABAC
APEC Business Advisory Council

Asia-Pacific Financial Forum Sustainable Finance Development Network Virtual Roundtable

Fostering Financial Sector Climate Leadership

30/31 March 2021

ROUNDTABLE REPORT

As sources of financing for businesses, lenders and investors can significantly impact efforts to promote alignment of business practices with specific goals. The role of socially responsible investing, impact investing and environmental, social and governance (ESG) factors in finance has grown, as more and more shareholders engage to ensure their investments are financing activities reflective of their social values. With the UN Sustainable Development Goals (SDGs) gaining traction in recent years, ESG finance has become an important focus of attention among lenders, investors, financial industry associations, multilateral institutions, governments and regulators.

During their dialogue in 2020, APEC Finance Ministers welcomed ABAC's recommendations on ESG finance. These included a call for a globally consistent and principles-based ESG taxonomy or set of standards that is flexible in approach and open to different speeds of adoption. It should also be dynamic and take into account the impact of evolving technologies and innovation. ABAC called for an inclusive process of developing global standards, frameworks, principles and best practices. Ministers welcomed the proposal to establish a platform, the Sustainable Finance Development Network (SFDN), which has since been formed. It is now undertaking activities and developing a roadmap to promote coherence of approaches to ESG finance among member economies and strengthen the region's role in the development of global standards.

This year, as part of its report to APEC Leaders and Ministers, ABAC aims to develop a set of Climate Leadership Principles that can help guide businesses in addressing climate change and establish a clearer vision about how a low-carbon future in the region could be achieved. Considering the huge role that lenders and investors play in this process, this Roundtable sought to identify principles for fostering financial sector climate leadership that can be incorporated into the ABAC Climate Leadership Principles. Participants also discussed concrete actions that can be taken to facilitate an effective role for lenders and investors in promoting sustainable business practices.

The Role of the Financial Industry in Meeting the Challenge of Climate Change

In recent years, financial industry activities in the field of environmental sustainability have significantly expanded. ESG assets have gone far beyond niche status. Banks are placing restrictions on financing activities such as arctic drilling. The UN Principles for Responsible Investment (UN PRI) now works with more than 3,800 signatories from over 80 economies. As of May 2021, over 2,100 organizations with a combined market capitalization of USD23 trillion and over USD180 trillion in assets under management have become supporters of the Task Force on Climate-related Financial Disclosures (TCFD). Disclosure in line with the TCFD recommendations has increased every year since their release in 2017.

The financial industry's role is critical because the transition to net zero greenhouse gas (GHG) emissions by 2050 will require huge amounts of capital – as much as USD100 trillion over the next three decades

according to some estimates.[1] This presents an opportunity for investing in long-term growth and innovation if lenders and investors are provided a consistent global framework to work with. The opportunity is there especially in emerging markets, where many regulators and banks are now actively seeking to expand their knowledge and understanding of how to integrate ESG criteria into banking guidelines, regulations and practices. The International Finance Corporation's Sustainable Banking Network (SBN), a knowledge, capacity building and best practices sharing platform for financial regulatory agencies and banking associations from emerging markets, has seen its engagement grow to over 40 economies since its launch in 2012.

Partnership between the public and private sectors is critical in developing tangible, actionable and achievable strategic initiatives in this space. It is particularly needed to overcome polarized political discourse and begin to create arenas of emerging profitable opportunities. Within this framework, financial institutions are important enablers, influencing managers on their investment choices. Following are areas that are fertile grounds for financiers to play a meaningful role when they fully engage with policy makers and managers:[2]

- All: Work towards a consensus on climate-enabled frameworks akin to the Equator Principles in project finance. This would guide managers in recognizing the investment virtues of environmental principles, and the benefits of applying them to their investment evaluation.
- Policy makers: In designing incentives, the approaches have to shift from one of emphasizing control and penalizing unsustainable practices to one of rewarding environmentally sustainable practices, transition and innovation. In practical terms, this means providing better borrowing terms to firms demonstrating "virtuous environmental practices," which promises to be a more effective approach compared to exclusion.
- Financial and central bank regulators: Focus on macro-prudential tools, including stress testing, to detect sources of systemic risk in the transition to the 2050 carbon neutral goal ("green swans").
- Financiers: Offer instruments such as resource insurance to de-risk investments such as geothermal exploration, or enable concessionary capital to blend with mainstream finance to transform emerging technologies into acceptable risks to investors and financiers.[3]
- Managers: Work to enable firms to monitor in real time, employing advances in digital technology, the impact of their investments and actions. This would provide evidence of the benefits of virtuous environmental practices, particularly with respect to enhancing their bottom lines instead of enlarging their budgets.

While COVID-19 had no significant direct impact on sustainable finance flows, it highlighted the importance of dealing with unpredictability. Markets are better in dealing with uncertainty, which they always do, compared to governments. Thus, the most effective approach to deal with unpredictability would be for policy makers to provide a clear, holistic and long-term vision and let the market sort out the best way to get there. Partnership between the public and private sectors is once again critical in

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[1] https://www.brookfield.com/powering-transition-net-zero.

[2] These views were shared by the author from a forthcoming book (Barcelona, Ricardo G., Dynamic Decisions: Energy PIVOT, Adaptive Moves, Winning BOUnCE. London and Singapore: World Scientific Publishing 2021), in particular from Chapter 1 (Impasse and PIVOT) and Chapter 2 (Policy and Managerial Actions).

[3] The concept of blended finance is centered on incorporating capital from non-profit entities, concessional funds or governments to assume the non-bankable risks in a project, thus making it commercially attractive. Non-profits like philanthrophies, development financial institutions and governments can, for example, as an alternative to donations, take on the first loss role in a given investment and absorb specific losses (e.g., exploration failure for geothermal power development).

influencing the movement of capital and promoting green finance, including the financing of transition and innovation.[4]

Regulators in the largest Asian emerging markets have taken important steps in providing an enabling framework for transition to net zero GHG emissions, including guidance for banks adopting a granular approach. Collaborating with the banking sector, which covers as much as 90 percent of financing needs in Asia, is important. Being a highly regulated sector in Asia but also where a lot of innovation is taking place, banking is where much attention deserves to be focused in the region. There is a huge need in this space for knowledge and capacity building that must be addressed, such as through the IFC's SBN that provides resources and technical assistance.

Data availability is another critical factor for successful transition to net zero GHG emissions. The TCFD provides a framework for companies to collect and report information that would help them see the risks and opportunities, and manage those risks as well. However, there is still much to be done to improve the quality of disclosure, which in general is not yet sufficiently effective in enabling a view of the scale of systemic risk. Asset owners also need to step up, as they currently underperform companies in terms of providing good quality data on risks to their portfolio. It is expected that the next two years will see a huge drive to improve this state of affairs, particularly after the planned establishment of global sustainability reporting standards and a sustainability standards board at the meeting of the United Nations Climate Change Conference COP26 in November 2021.

Finally, it is important for financial institutions, as well as policy makers and regulators, to start coordinating in order to create opportunities in sustainable finance. Financial institutions, on their part, need to incorporate sustainable finance, including environmental sustainability, in credit assessments, inasmuch as climate-related risks have an impact on business continuity. Policy makers and regulators, on their part, need to shift mind-sets away from a focus on punishment and increasingly toward rewarding sustainable practices.[5]

Challenges Facing Green, Transition and Innovation Financing

Drawing on the past work of ABAC and the APFF's ESG Finance Working Group, the Roundtable discussed institutional investors' approaches, the challenges they face and possible solutions to be considered.[6] Four key challenges have been identified in the APFF's previous discussions, together with possible measures to address them, which are as follows:

- Challenge of ESG rating and evaluation: Possible measures include enhancing the reliability of ESG rating, and distinguishing environmental and social from governance in the rating to better reflect the different nature of these factors.

[4] For example, the basic guidelines issued by Japanese authorities adopt an approach where the transition finance market matures through a dialogue based on sufficient information between issuers or borrowers and financiers. It is the market that will be allowed to evaluate the eligibility of projects for investment and financing based on disclosure elements identified by the International Capital Markets Association (ICMA). Financial Services Agency, Ministry of Economy, Trade and Industry and Ministry of the Environment, Basic Guidelines on Climate Transition Finance, May 2021. [https://www.meti.go.jp/press/2021/05/20210507001/20210507001-3.pdf]

[5] An analogy is how sports arenas knowing that spectators are willing to pay higher prices to get their preferred seats successfully apply tiered pricing to increase their revenues. Similarly, policy makers may offer differentiated support or recognition to firms with a consistent track record of investing in sustainable activities, which would produce better results than relying mainly on punishing non-compliance.

[6] Institutional investors usually follow any or all of five main approaches to sustainable finance, which are as follows:

- Negative screening (exclusion);
- Positive screening (selecting the best in class);
- Thematic investments (green and social bonds);
- Active ownership (stewardship); and
- ESG integration (multi-factor across the firm).

- Challenge of investment selection: Possible measures include ensuring long-term profitability and assessing impact on sustainability, and providing useful information for investors in specific areas for each project and company.
- Challenge of stakeholder education: Possible measures include educating a broader range of stakeholders instead of just investors; and establishing a knowledge system and providing learning opportunities.
- Challenge of investment compliance with capital rules and regulations: Possible measures include working toward a goal of balancing long-term investments, risks and regulation; and promoting regulatory and accounting standards that do not disincentivize long-term investments. [7]

In addition to these specific challenges, ABAC referred in its 2020 Report to the APEC Finance Ministers to the broader challenge of overcoming fragmentation in the development and application of ESG taxonomy.

Three case studies illustrating the growing role of lenders and investors in promoting environmental sustainability, including transition and innovation, were considered in the Roundtable.

Case Study 1: KKR

KKR's responsible investment governance framework enables senior leaders to oversee investments, with global and regional team members collaborating on an integrated approach, supported by subject matter experts. Its global approach to ESG principles, policies, processes, programs and reporting to investors and stakeholders is developed by the company's leadership and global responsible investment management and implemented regionally. Regional implementation draws on regional public affairs team expertise and external subject matter experts. It focuses on diligence of local investments, working with local portfolio companies, application of local laws and exchange of expertise with local investors. Throughout this whole process, the company undertakes cross-functional and integrated diligence and portfolio management.

The company has identified four global imperatives where it aims to be part of the solution and contribute to the realization of the UN Sustainable Development Goals:

- *Mitigating and Adapting to Climate Change: Providing products and services that help companies compete in a resource-constrained world, by promoting energy and resource efficiency, water quantity and quality management, resilient development and renewable energy and storage.*
- *Harnessing the Fourth Industrial Revolution: Investing in companies that are preparing a workforce to help turn big data into smart data that promotes smarter development, mobility, innovative transport, sustainable packaging and more connected supply chains.*
- *Serving Empowered Consumers: Offering solutions that respond to consumers' demand for healthy and safe products, circular economy strategies that mitigate waste, and more transparent supply chains.*
- *Building for the Future: Investing behind solutions-oriented opportunities to address the infrastructure gap in cities with infrastructure needing repair, expansion, and innovation.*

[7] APFF has also identified in its previous reports key regulatory issues and recommendations facing long-term investors. These relate to the application of the following to long-term investors:

- Bank-centric regulations: Standards should reflect the long-term nature of investors, and investors should be allowed to invest in assets with long-term growth opportunities.
- Short-term oriented economic regime: Economic regimes should have a long-term vision, and investors should be encouraged to make decisions based on long-term time horizons rather than on short-term considerations.
- One-size-fits-all models: Standards should be principles-based and aim to achieve comparable outcomes by taking into account diversity across different jurisdictions.

Case Study 2: Citi

Citi has a strong track record of engagement in sustainability for over two decades. It is co-creator of the Equator Principles and the Green Bond Principles and is a founding member of the Principles for Responsible Banking among other leadership activities. The company recently established a 2050 Net Zero commitment builded on the Principles for Responsible Banking, the Task Force on Climate-related Financial Disclosures (TCFD) as well as its own enhanced fossil fuel sector standards. This strategy aims to help the financial institution become the global leader in financing the transition to a more sustainable economy through 3 action lines:

- *Low Carbon Transition. Accelerating the transistion to a Low Carbon Economy through a $250 Billion Environmental Finance Goal[8] based on criteria such as renewable energy, energy efficiency, water quality and conservation, clean technology, green buildings, sustainable transportation, circular economy and sustainable agriculture and land use.*
- *Climate Risk. Measuring, managing and reducing the climate portfolio risk and impact of the client portfolio.*
- *Sustainable Operations. Reducing the environmental footprint of all facilities and strengthening sustainability culture (reducing 45% of greenhouse gas emissions; 40% energy reduction and 100% of renewable electricity sourcing; 30% of water consumption and 25% of water consumer to come from reclaimed/reused sources; 50% reduction in total waste and 50% of waste diverted from landfill; and 40% of floor area to be LEED-, WELL-, or equivalent-certified).*

Citi has also incorporated SDGs into its planning, execution and performance evaluation and is making public reports of the progress (2019 and 2020). As an example, Citibanamex, the Mexican subsidiary , has incorporated SDGs based on four pillars and focusing on 11 action lines. These are as follows:

- *Pillar 1 (Responsible Finance) promotes SDG 16 (Peace, Justice and Strong Institutions) through 2 action lines (anti-corruption and financial inclusion);*
- *Pillar 2 (Economic Development) promotes SDGs 8 (Decent Work and Economic Growth) and 9 (Industry, Innovation and Infrastructure) through 2 action lines (sustainable investment portfolio development and sustainable credit portfolio development);*
- *Pillar 3 (Equal Opportunities) promotes SDGs 5 (Gender Equality) and 8 (Decent Work and Economic Growth) through 3 action lines (decent work, gender equity and people with disabilities); and*
- *Pillar 4 (Environment and Climate Change promotes SDGs 7 (Affordable and Clean Energy); 11 (Sustainable Cities and Communities) and 13 (Climate Action) through 3 action lines (corporate social responsibility and environmental/climate management, environmental footprint, carbon footprint*

Case Study 3: BlackRock

BlackRock's sustainability strategy is focused on long-term value creation, where companies, investors and governments must prepare for a significant reallocation of capital. It is committed to supporting the goal of net zero GHG emissions by 2050 or sooner. It creates solutions designed to help clients meet their financial objectives and other goals by integrating ESG characteristics into financial return analysis. The company views sustainability and climate risks as investment risks, and that integrating sustainability can help investors build more resilient portfolios and achieve better long-term, risk-adjusted returns. This conviction is based on a two-part investment thesis, as follows:

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[8] Update: In 2021, Citi committed $1 trillion to sustainable finance by 2030, aligning with the ambitious agenda of the United Nations' Sustainable Development Goals (SDGs). This $1 trillion commitment includes extending current environmental finance target from $250 billion by 2025 to $500 billion by 2030, further accelerating the transition to a sustainable, low-carbon economy. Citi's commitment also includes an additional $500 billion to invest in other activities that advance the SDGs, such as education, affordable housing, health care, economic inclusion, community finance, international development finance, racial diversity and gender equality.

- *Thesis 1: Asset prices and portfolio risks do not fully reflect sustainability-related factors.*
- *Thesis 2: Market factors will accelerate the reallocation of capital towards issuers and assets with positive sustainability characteristics, in turn impacting valuation.*

BlackRock sees an accelerating tectonic shift toward sustainable investing that is being driven by five major catalysts – the acceleration of the tectonic shift; the influence of sustainability on risk and return; the mounting costs of climate risk; increased reporting as a change driver; and the rising importance of stakeholder capitalism. Based on this analysis, the company has identified key actions for 2021 to help investors prepare their portfolios for a net zero world, including capturing opportunities created by the net zero transition. These key actions are as follows:

- *Measurement and Transparency*
    - *Publishing a temperature alignment metric for the company's public equity and bond funds, for any markets with sufficiently reliable data;*
    - *Publishing the proportion of the company's assets under management that are currently aligned to net zero, and announcing an interim target on the proportion of its assets under management that will be aligned to net zero in 2030, for markets with sufficiently reliable data; and*
    - *Through Aladdin Climate, helping more investors manage and meet their climate objectives by tracking investment portfolios' trajectories toward net zero, and helping to catalyze increasingly robust and standardized climate data and metrics to better serve the industry.*
- *Investment Management*
    - *Incorporating the impacts of climate change into the company's capital market assumptions, the cornerstone for portfolio construction at BlackRock;*
    - *Implementing a "heightened-scrutiny model" in the company's active portfolios as a framework for managing securities that pose significant climate risk;*
    - *Helping clients benefit from opportunities created by the energy transition, from investments in electric cars to clean energy to energy-efficient housing; and*
    - *Launching investment products with explicit temperature alignment goals, including products aligned to a net zero pathway.*
- *Stewardship*
    - *Using investment stewardship to communicate the company's expectation that the companies its clients invest in are mitigating climate risk and considering the opportunities presented by the net zero transition;*
    - *Asking companies to disclose a business plan aligned with the goal of limiting global warming to well below 2°C, consistent with achieving net zero global greenhouse gas emissions by 2050; and*
    - *Increasing the role of votes on shareholder proposals in the company's stewardship efforts around sustainability.*

These moves by lenders and investors to actively play a role in integrating ESG factors in financing economic activities are being undertaken in the context of market and policy developments supporting these directions. With issuance growing rapidly over the past few years, green bonds have become the fastest-growing asset class globally. In major Latin American economies, governments issuing sovereign bonds have been important drivers. Many regulators around the world have in recent years undertaken measures to support disclosures consistent with the TCFD recommendations, both domestically in terms of creating institutional frameworks for inter-agency coordination, and internationally in terms of participation in the Network for Greening the Financial System (NGFS).

However, much remains to be done by policy makers and regulators to support financial sector efforts and to provide an enabling environment, particularly through the following measures:

- Taxonomy: Developing a common global ESG taxonomy that is practical, globally applicable and readily adapted to the needs of users across diverse jurisdictions at different levels of economic, social and political development (as recommended in the 2020 ABAC Report to APEC Finance Ministers);[9]
- Disclosure and reporting: Facilitating the adoption of a common sustainability and climate reporting standard that can allow investors to make meaningful comparisons across jurisdictions;[10]
- Scaling and catalyzing green activities: Increasing the use of mechanisms such as carbon pricing and in particular, through fiscal and macro-prudential incentives to help accelerate transition, catalytic capital and green bonds, plus climate policies that are globally connected; and
- Fair and just transition: Providing for a fair and just transition to build durable support for transition through long-term policies.[11]

Financial Sector Leadership to Take the Climate Change Agenda Forward

Progress in addressing these challenges faced by lenders and investors requires close international collaboration between public and private sectors. International efforts are currently being led by the European Union and global regulators' organizations and standard setters like the International Organization of Securities Commissions (IOSCO), the Network for Greening the Financial System (NGFS) of central banks, and the Sustainability Accounting Standards Board (SASB), among several others. However, the role of the financial sector in shaping the global policy and regulatory landscape around responses to climate change has also been growing through actions being undertaken by industry organizations and individual firms.

Following are some examples:

- The Asia Securities Industry & Financial Markets Association (ASIFMA) is an independent regional trade association with over 140 member firms comprising a diverse range of leading financial institutions from both the buy and sell side. It has played an active role in developing consensus positions for the industry and in providing a bridge to regulators and policy makers. As a member of the Global Financial Markets Association (GFMA), it also provides a bridge from the Asian region to global efforts to harmonize the global sustainable finance landscape. ASIFMA's activities focus on integrating perspectives from Asian jurisdictions, including economies in transition, into global harmonization of standards and approaches and in the development of a global taxonomy, as well as in capacity building to scale up sustainable finance in the region.

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[9] Such a taxonomy should have the following characteristics:

- Principles-based rather than prescriptive;
- Globally consistent;
- Flexible in approach and acknowledging, e.g., different shades of green and brown instead of a binary choice between green and brown, and that is open to different speeds of adoption;
- Dynamic, taking into account future changes in the level of sustainability of assets and activities due to technological developments;
- Adaptable and easily implementable;
- Broad coverage of activities and financial products; and
- Inclusive and adhering to the global pledge that no one should be left behind.

[10] Standardized reporting ensures that disclosures of companies can be more consistent and comparable and that third party ESG ratings can potentially converge with better data. Domestic regulation and international cooperation are important to facilitate the adoption of greater disclosure as well as reporting by companies in alignment with the recommendations of TCFD and SASB until a global standard is adopted. Companies and regions that are on the forefront of that transition could benefit disproportionately from global capital flows.

[11] This is particularly important for emerging economies where certain consumers may have lower purchasing power or may be located in regions disproportionately impacted by the transition. The physical impacts of climate change, from flooding and droughts to extreme weather and loss of arable land are most likely to disproportionately impact the most vulnerable parts of society, and thus will entail a huge societal cost from lack of action.

- The London Stock Exchange Group (LSEG) is Europe's leading equities business, with 48 percent of the FTSEurofirst 100 by market capitalization. LSEG is composed of the London Stock Exchange, Refinitiv, LSEG Technology and FTSE Russell, and has majority stakes in LCH Clearing House and Tradeweb. It plays an active role in convening the market to drive action, focusing on promoting consistent and comparable data and disclosures, the green economy and climate transition. It is co-chairing the UN Sustainable Stock Exchanges (SSE) initiative, a peer-to-peer learning platform for exploring how exchanges, in collaboration with investors, regulators, and companies, can enhance corporate transparency and performance on ESG issues and encourage sustainable investment.
- The Task Force on Climate Related Financial Disclosures (TCFD) is a private sector-driven organization established by the Financial Stability Board, which plays a very important role in markets. In 2017, it released climate-related financial disclosure recommendations to help companies provide information needed to support informed capital allocation. These recommendations are structured around four themes: governance, strategy, risk management, and metrics and targets. As mentioned earlier in this report, the main challenge for TCFD has been the insufficient quality of disclosure by companies.
- The Institute of International Finance (IIF) is the global association of major players in the financial industry, with close to 450 members from 70 jurisdictions. It harnesses expertise from within and outside member organizations to develop staff and position papers and holds consultations on behalf of its members with regulators and policy makers. It is currently focusing on two key themes for 2021 – risk (promoting global alignment and engagement; better disclosure and seeking a common approach to scenario analysis and stress testing) and opportunity (highlighting industry climate commitments, key role for insurers, support for transition in emerging markets, and natural capital including such objectives as promoting biodiversity). It provides recommendations to individual economies, prudential authorities, standard setters and other relevant international groups.

In a recent (January 2021) report,[12] the IIF sought to contribute financial industry perspectives to policymakers' and regulators' efforts to address climate-related risks. The report set out a framework to discuss objectives that prudential authorities could consider pursuing.

- It proposed pursuing the microprudential objective of promoting resilience of financial institutions through the materiality lens of climate and environmental risks as they impact their business. This could involve financial supervisors: (a) engaging with firms to assess strategies for responding to risks and opportunities as a foundation for the development and use of other microprudential tools and instruments; (b) promoting risk monitoring and market discipline, which would generate data that informs other microprudential tools and instruments; (c) promoting sound risk management within individual institutions; (d) undertaking supervisory scenario analysis exercises to complement firms' own scenario analysis and stress testing activities with sectoral views on exposures and alignment; and (e) possibly implementing risk-based adjustments to capital requirements if sufficient evidence exists to measure and calibrate balance-sheet risks.
- The report proposed pursuing the macroprudential objective of promoting system-wide alignment within the financial system and the real economy through the materiality lens of climate and environmental risks as they impact the financial system, as well as the impact of the financial system on climate and environmental outcomes. This could involve supervisors: (a) gathering perpectives from across the industry and providing feedback based on peer review to inform judgments

[12] Prudential Pathways: Industry Perspectives on Supervisory and Regulatory Approaches to Climate-Related and Environmental Risks (https://www.iif.com/Publications/ID/4224/Prudential-Pathways-Industry-Perspectives-on-Supervisory-and-Regulatory-Approaches-to-Climate-Related-and-Environmental-Risks).

regarding performance of firms vis-à-vis system-wide trends; (b) providing disclosure guidelines to enable economic decisions that reduce systemic risks through greater transparency and better information; (c) contributing to mitigation or management of system-wide financial risks; (d) focusing scenario analysis exercises on assessing potential system-wide vulnerabilities and transmission channels for risks between the financial system and the real economy; and (e) possibly implementing risk-based capital requirements to effectively mitigate systemic risks not addressed by microprudential measures.
- The report reflected the views of IIF member institutions that the use by authorities of prudential tools to directly incentivize capital allocation to achieve climate policy goals may not be advisable. Examples of such actions that are not recommended would include supervisory engagement to directly promote greener activities by firms; introducing disclosure requirements on the real economy climate outcomes of financing activities; introducing differential risk standards and tolerances based on climate impact or exposure; linking scenario exercise results directly to prudential requirements; or implementing a green supporting or brown penalizing factor to actively incentivize lending to certain sectors that are seen as leading to the low-carbon transition.

The report recommended that prudential authorities and standard-setters consider the adoption of the following prudential tools:

- Supervisory engagement and monitoring with climate-related risks as a key focus and the identification of global sound practices;
- Leveraging market-led efforts on disclosure such as the TCFD framework and encouraging comparability and appropriate harmonization;
- Developing meaningful global principles and best practices on the management of climate-related risks in collaboration with the financial industry to clarify risk management expectations;
- Undertaking supervisory scenario analysis exercises to help inform views of financial system-wide risks and macro-financial feedback effects due to climate-related risks, but not for the purposes of capital requirements; and
- Consideration of using Pillar 2 (supervisory review process) or macroprudential tools in the future if risks build up, instead of using regulatory capital requirements.

Finally, the report suggested a short-term roadmap for collaboration among international standard-setting bodies, prudential authorities and supervisors and industry, with the following elements:

- International standard-setting bodies to clarify the building blocks of common approaches, define expectations for future work, and agree on a common work roadmap;
- Prudential authorities to develop platforms for joint scenario analysis exercises across jurisdictions, explore options to develop centralized analytical utilities including for data pooling and model development;
- Prudential authorities to explore the establishment of jurisdictional regulatory and ministerial climate coordination bodies to structure engagement with other authorities on climate risk and system-wide alignment; and
- Firms and supervisors to engage in ongoing and structured dialogue on climate risk and system-wide alignment at jurisdictional and global levels.

The Roundtable also discussed how to develop better indicators that can be effectively used by investors for developing economies and MSMEs. There are metrics that have been developed through a bottom-up approach to work effectively in economies with limited resources. One particular standard is the Harmonized Indicators for Private Sector Operations (HIPSO) that has been developed to reduce the administrative reporting burden of private sector entities receiving financing from multiple DFIs. HIPSO

metrics have recently been aligned with the SDG framework to help DFIs, impact investors, and other users to better monitor, manage, and communicate their SDG contributions to their stakeholders.

Another example is the Global Impact Investing Network's IRIS, which has become the generally accepted accounting system that leading impact investors use to measure, manage, and optimize their impact. Proper use of the IRIS+ system ensures a minimum level of consistency in a users' impact claims and performance, which makes it easier for investors to analyze and extract useful information for decision making and facilitates the comparison of impact information. These two examples highlight the advantages of using a bottom-up approach to developing harmonized metrics that can be used across economies to help lenders and investors better incentivize companies in developing economies to align their practices with SDGs.

Discussions also touched on the issue of decoupling from fossil fuels, which is easier said than done, especially for economies that have limited energy self-sufficiency and limited access to renewable energy due to geographical factors, and thus continue to be heavily dependent on fossil fuels. There are challenges in the use of renewable energy, including fluctuations that require continued reliance on fossil fuels in the power grid to maintain stable energy supply. Who bears the higher cost of renewable energy compared to fossil fuels will also need to be addressed, particularly at a time when governments' fiscal positions have deteriorated in the wake of COVID. In this context, dialogue and collaboration among all the major stakeholders will be critical in identifying the best pathway to zero GHG emissions.

Finally, the Roundtable discussions focused on the role that APEC can play in providing a platform for financial sector leadership to help APEC member economies develop effective responses to climate change and strengthen the voice of the region in the global standard setting process. The establishment of the Sustainable Finance Development Network (SFDN) within the APFF following the ABAC dialogue with APEC Finance Ministers in 2020 provides a platform under the Finance Ministers' Process that can be harnessed to reduce duplication, promote sharing of resources, enhance coordination and enable synergy among the various ongoing initiatives by the public and private sectors and multilateral institutions to benefit APEC member economies.

The SFDN has received the support of key international actors and major institutions engaged in the ESG space that have agreed to play active roles, including leadership of working groups. With regard to the Climate Leadership assumptions and principles that ABAC is developing in 2021, the SFDN can help promote alignment of the strategies and activities of participating financial industry firms and organizations to assume financial sector climate leadership, as follows:

- ***Alignment with Climate Leadership Assumptions:***
    - Collaboration: Advocacy for efficiencies, alignment and inclusion, and promotion and support of effective stakeholders' approaches.
    - Natural ecosystems: Promoting financial sector transitioning to effectively play its role in supporting business transitioning in the region.
    - Iterative process: Adoption of a dynamic and flexible approach in sustainable finance development and promotion of capacity building to support implementation of policies and practices.
- ***Alignment with Climate Leadership Principles:***
    - Reduction: Advocacy and financial incentives and support to the transition journey of companies and innovation, such as through development of financing products as incentives for transitioning, supporting the development of inclusive taxonomies to allow green finance to support transitioning and innovation, and investor advocacy in climate disclosure and climate risk policies.

- Adaptation: Capacity building and implementation of TCFD recommendations.
- Just transition: Advocating for an inclusive approach in international fora to address APEC economies' contexts and addressing MSMEs' transition and reporting challenges and incentives (this could include expanding sources of financial support for MSMEs in transition and innovation; addressing challenges faced by MSMEs in managing climate risk; supporting large companies' work with their supply chain partners; developing comparable key performance indicators to support the flow of financing through financial products; and supporting stakeholders such as the International Chamber of Commerce's SME Climate Hub).

Conclusions

The Roundtable highlighted the central role that the financial sector needs to play in attaining the goal of zero GHG emissions by 2050, from mobilizing the huge amount of capital required for transition and innovation, to their role as enablers influencing managers on their investment choices, and to their role in helping the public sector obtain a deeper understanding of the needs and realities in the market. It also underscored the importance of cooperation between the financial sector on one side, and standard-setters, governments and regulatory and supervisory authorities on the other, both at the jurisdictional and international levels. Such cooperation can be critical in developing globally consistent policies and regulations that would provide effective incentives for companies to identify and seize opportunities in sustainable development and accelerate the transition to net zero emissions across the region.

Lenders and investors are making significant progress in incorporating sustainability in their lending and investment decisions, and this is a process that is expected to accelerate in the next few years. The financial sector is active in helping shape policies and regulations through efforts to develop consensus within the industry, to generate knowledge, undertake advocacy and hold dialogues with policy makers and regulators. There are many areas where such collaboration is needed in order to create an enabling environment for financing transition and innovation, including the development of a globally consistent and effective taxonomy, improvements in data and disclosure, scaling and catalyzing sustainable activities and facilitating a just and fair transition.

The Sustainable Finance Development Network (SFDN) can play a constructive role in providing a platform for coordination and collaboration among the many ongoing initiatives. It can help reduce duplication of efforts, create synergy, and link the public and private sectors together to focus on helping APEC member economies to achieve the goal of net zero emissions. It can also help align strategies and activities of the financial sector with the Climate Leadership Assumptions and Principles that ABAC is developing in 2021, to foster financial sector climate leadership in the Asia-Pacific region.

ANNEX: ROUNDTABLE AGENDA (*Times displayed are Japan Standard Time*)

1000-1010	**OPENING SESSION** **Welcome and Opening Remarks** Mr. Hiroshi Nakaso, Chair, Advisory Group on APEC Financial System Capacity Building; and Chairman, Daiwa Institute of Research
1010-1050	**SESSION 1 (Panel Discussion)** **The Role of the Financial Industry in Meeting the Challenge of Climate Change** Moderator: Ms. Vicky Cheng, Head of Government and Regulatory Affairs, Asia-Pacific, Bloomberg LP
1010-1015	**Introduction** by Moderator
1015-1020	**Introductory statement** Mr. Mathew Nelson, Global Climate Change and Sustainability Services Leader, EY
1020-1025	**Introductory statement** Ms. Wei Yuan, Asia Coordinator, Sustainable Banking Network; and ESG Advisory, International Finance Corporation
1025-1030	**Introductory statement** Dr. Ricardo Barcelona, Managing Director and Board Director, Barcino Capitas Limited; Adjunct Professor, Asian Institute of Management; and Author, Energy Investments: An Adaptive Approach to Profiting from Uncertainties
1030-1045	**Panel Discussion**
1045-1050	**Concluding summary** by Moderator
1050-1130	**SESSION 2 (Panel Discussion)** **Challenges Facing Green Finance** Moderator: Mr. Makoto Okubo, Co-Sherpa, APFF Sustainable Finance Development Network; and General Manager, International Affairs, Nippon Life
1050-1055	**Introduction** by Moderator
1055-1100	**Introductory statement** Mr. David Katz, Director and Head of Public Affairs for Asia Pacific, KKR Asia Ltd.
1100-1105	**Introductory statement** Mr. Alan X. Gomez Hernandez, Head of Sustainability, Citibanamex
1105-1110	**Introductory statement** Mr. Venn Saltirov, Portfolio Manager, Asia Fixed Income and Credit, BlackRock
1110-1125	**Panel Discussion**
1125-1130	**Concluding summary** by Moderator
1130-1220	**SESSION 3 (Panel Discussion)** **Financial Sector Leadership to Take the Climate Change Agenda Forward** Moderator: Mr. Pablo Casaux, Sherpa, APFF Sustainable Finance Development Network; and Market Structure Strategist, Bloomberg

1130-1135 **Introduction** by Moderator

1135-1140 **Introductory statement**
Ms. Helena Fung, Head of Sustainable Investment, APAC, FTSE Russell; and Co-Chair, Sustainable Finance Working Group, Asia Securities Industry & Financial Markets Association (ASIFMA)

1140-1145 **Introductory statement**
Dr. Matthew Gamser, CEO, SME Finance Forum; and Chief Operations Officer, International Finance Corporation

1145-1150 **Introductory statement**
Mr. Jeremy McDaniels, Senior Advisor – Sustainable Finance, Institute of International Finance

1150-1155 **Introductory statement**
Mr. Masaaki Nagamura, Sherpa, APFF Disaster Risk Financing and Insurance Network; Fellow and General Manager International Initiatives, Corporate Planning Dept., Tokio Marine & Nichido Fire Insurance Co., Ltd.; and Member, Task Force on Climate-Related Financial Disclosures

1155-1215 **Panel Discussion**

1215-1220 **Concluding summary** by Moderator

1220-1230 **CLOSING SESSION**

Concluding Remarks
Mr. Hiroshi Nakaso, Chair, Advisory Group on APEC Financial System Capacity Building; and Chairman, Daiwa Institute of Research