

# P R A K A R S A *Policy Brief*

November 2023

## Reviewing Bank Sustainability Policies in Indonesia: Are They Serious Enough?



### Key Points:

- Indonesia has made much progress in sustainable financial regulations, but there still needs to be a gap between regulations and practices.
- Several banks have shown progress on sustainability policies. However, it is still slow and needs to be accelerated to strengthen the role of banks in dealing with the climate crisis and improving social welfare.
- OJK needs to encourage a sustainable financing and investment climate through policies and good practices implemented by banks.

### Progress of sustainable finance in Indonesia

Sustainable development is the main agenda for countries in the world. This development agenda does not only focus on economic growth but also pays attention to environmental and social sustainability. The commitment of countries in the world regarding climate change was stated in the ratification of the Paris Agreement in 2015. It was expressed as a Nationally Determined Contribution (NDC) at the country level.

Indonesia is committed to climate change mitigation and adaptation efforts with a target of reducing emissions by 31.89% with its efforts and 43.20% with international support by 2030. To meet this target, Indonesia is estimated to need financing of USD 322.9 billion for implementing actions. Mitigation does not include the costs of adaptation actions and creating a supporting environment (BKF, 2022). Of course, the financing cannot only come from the APBN; multi-party involvement is required, including financial institutions.

On a global scale, financial regulators and central banks are increasingly realizing the importance of implementing sustainable finance, including managing Environmental, Social and Governance (ESG) risks in banking credit distribution policies. Indonesia has also become one of the countries helping to encourage the birth of a more sustainable financial industry and is committed to implementing ESG principles. However, what is the progress of the bank's commitment to supporting handling the climate crisis and improving social welfare in Indonesia?

### Bank policy rating: assessing banking sustainability performance

The Financial Services Authority (OJK) has issued several regulations to encourage the implementation of sustainable finance. These policies include POJK 51/2017 concerning the Implementation of Sustainable Finance, technical guidance POJK 51 where OJK determines 12 categories of sustainable business activities (KUBL), POJK 60/2017 concerning Issuance and Requirements for Environmentally Friendly Debt Securities, Stage I Sustainable Finance Roadmap and II, Reference book for Credit/Financing for Palm Oil Plantations and Industry, First Movers on Sustainable Banking in the Indonesian Sustainable Finance Initiative/IKBI, and the Indonesian Green Taxonomy 1.0.

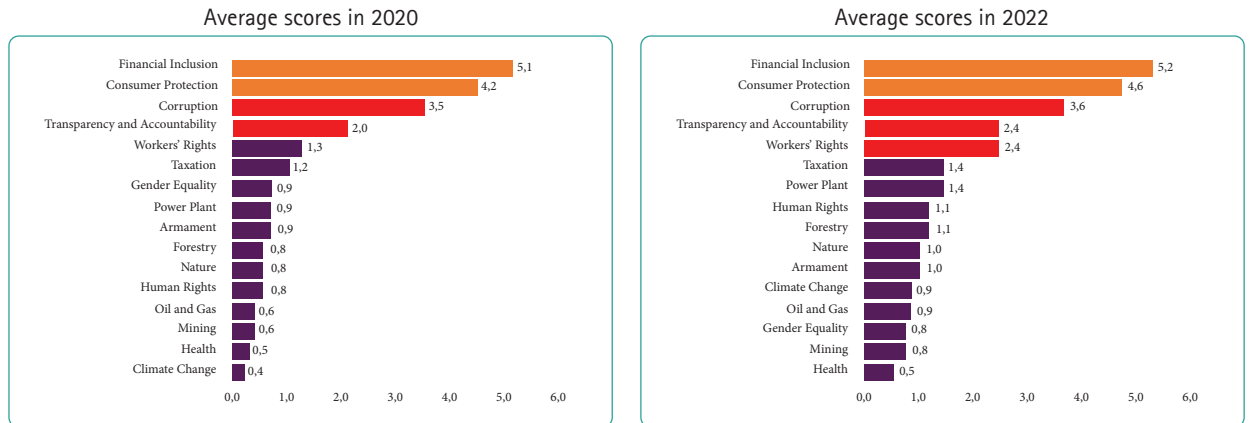
The implementation of sustainable finance is also strengthened by the obligation of banks to develop Sustainable Financial Budget Plans and sustainable reports. However, based on the green taxonomy reporting, of all credit or financing that has been classified by banks, financing to the green economy sector has a relatively low with total debit balance 28% (IDR294.20 trillion) compared to the yellow sector's 37% (IDR392.87 trillion) and red 35% (IDR378.16 trillion) of the total IDR 1,065.23 trillion whose classification has been identified (OJK, 2023).

It is necessary to know the progress of banking policies and commitments in Indonesia in implementing sustainable finance to monitor that products and services labelled as sustainable are being implemented and not greenwashing. ResponsiBank Indonesia in PRAKARSA (2022) assessed of 11 banks in Indonesia on 16 themes. For each theme, the assessment is carried out based on elements related to internal banking operational

policies and financing and investment policies. The score for each bank is based on the proportion of elements contained in the policy with a value range of 0 - 10. The

score is given if a bank policy meets the criteria for the elements being assessed.

Graph 1. Average bank scores based on themes for 2020 and 2022



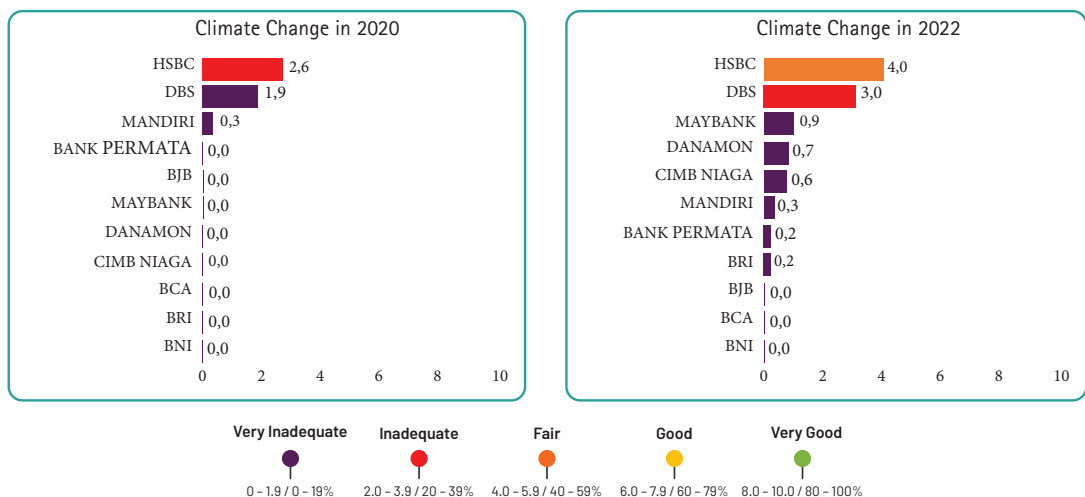
Source: PRAKARSA, 2022

The theme of financial inclusion is the theme that gets the highest average score, followed by the theme of consumer protection. Meanwhile, the themes of health, mining and gender equality are the lowest in 2022. Then, the theme of climate change has experienced changes where banks have begun to commit to reducing climate impacts in their operations and the financing they carry out, although it is still low.

### Several banks are starting to commit to tackling climate change

Banks' commitment to addressing climate change has begun to emerge but is limited to a few banks. Only HSBC and DBS have implemented the IFC Performance Standards and are members of the Equator Principles. Meanwhile, other banks are considered to have yet to ratify this policy, and there are still a few banks that have a list of businesses that still need to be provided with financial support (exclusion list), such as businesses that have a significant impact on climate change.

Graph 2. The average score on the climate change theme in 2020 and 2022



Source: PRAKARSA, 2022

Banks in Indonesia already have policies that support sustainability through their sectoral policies. BRI (2021) has an ESG risk management policy in the palm oil sector, where the company carries out a complete assessment regarding water resource needs and the impact of water releases by considering groundwater needs for plants, hydrological conditions, as well as the application of ESG in the fields of employment, anti-discrimination, and gender equality. Maybank (2021) is committed to implementing ESG by terminating the flow of financing to businesses

that are not in line with ESG principles, one of which is the 'no deforestation' policy, especially in six industries, namely palm oil, forestry and logging, construction and real estate, electricity, oil and gas, as well as mining and quarrying.

Banks are starting to reduce the financial flow to sectors that are vulnerable to the environment. It was found that BRI (2021) does not provide loans to businesses that damage the environment, does not support financing for land acquisition through violence, and does not

finance activities or business sectors that could damage UNESCO World Heritage Sites. HSBC (2021) has a policy of eliminating coal as a power generator but still needs to include a policy for oil and gas power plants. HSBC commits to reduce coal financing gradually by 25% in 2025 and 50% in 2030. HSBC has a sustainable risk policy by not financing companies that violate local communities' rights. A similar commitment was also implemented by DBS (2021), which is actively involved in stopping coal financing for mining or power plants, with the highest threshold of more than 50% since 2019.

A few banks have increased their financing flows in the New Renewable Energy sector. HSBC (2021) is committed to supporting the energy transition mechanism through a public-private partnership led by the Asian Development Bank by accelerating the retirement of coal-fired power plants and increasing investment in renewable energy. DBS is trying to increase its commitment through financing assistance for companies operating in the renewable and clean energy sector, which is close to SGD 1.1 billion. In 2021, DBS has also increased its commitment by financing SGD 50 billion in 2024 towards sustainable finance, including green loans, transition loans, sustainability-related loans and renewable financing (DBS, 2021). Maybank (2021) also provides financing for motorized vehicles with electric and hybrid power and purchasing bonds adapted to sustainable finance principles. Specifically, Maybank has a Sustainable Finance Implementation Action Plan, which provides credit to customers to finance renewable energy projects and their supporters. In addition, Maybank also has a blocklist related to activities producing or trading radioactive materials, including nuclear power plants and related services.

### **Most banks are not yet committed to fulfilling human rights and gender equality**

The bank's commitment to respecting human rights and anti-discrimination has not significantly improved. Only HSBC and BCA have disclosed a commitment to comply with human rights by implementing the United Nations Guiding Principles on Business and Human Rights (UNGPs). In terms of implementing anti-discrimination policies on jobs and positions, only CIMB Niaga and HSBC are considered to commit to implementing this principle. In the 2021 annual report, CIMB Niaga has disclosed its commitment to ensuring equal opportunities for all employees without distinction of ethnicity, religion, race, class, social status, gender, and other discriminatory factors. Meanwhile, HSBC has adopted international standards related to the recognition of human rights, such as the Equator Principles, IFC Performance Standard, UN Global Compact, and UN Principles for Responsible Investment. Apart from these banks, several banks in the 2022 ranking (BNI, Mandiri, Danamon, BJB and Permata Bank) still need policies regarding compliance with human rights principles.

Banks still need to put forward policies related to company financing that are committed to protecting workers' rights, including the protection of occupational health and safety. Regarding workers' rights, 7 out of 11 banks have policies to comply with the ILO Declaration on Fundamental Principles and Rights at Work. However, commitments related to company financing that guarantee freedom of

association for workers and prohibit acts of discrimination are only implemented by BRI, CIMB Niaga, DBS, and HSBC.

Commitments related to prohibiting financing for companies that commit forced labour and child labour have been implemented by more than half of the banks assessed but have not been found at Bank Danamon, Permata Bank and BJB. Regarding worker health and safety, HSBC and DBS have committed to implementing the Equator Principles and IFC Performance Standards. BRI is committed to financing companies with SOPs related to occupational health and safety in the palm oil sector. However, implementing this policy must still be evenly established in all sectors.

Regulations related to gender equality policies in providing investment or corporate credit have not yet been implemented by the majority of banks, even though their internal affairs have regulated policies related to gender equality. For example, HSBC's internal policy is committed to implementing equal salary payments between men and women. HSBC's female board of directors has reached 38% in 2021 and targets to get 40% in 2023. HSBC's commitment to gender equality is also interpreted in training and leadership development policies explicitly aimed at female workers. However, these policies still need to be implemented by other banks.

### **Most banks still need to prioritize strengthening governance, especially related to complaint mechanisms and transparency of financing information**

Only three banks have committed to disclosing their governance information, namely CIMB Niaga, Danamon and HSBC. CIMB Niaga (2021) established policies related to information disclosure by revealing the names of funded companies, the number of companies involved in social and environmental discourse, and the existence of electronic voting and counting mechanisms (e-voting). Apart from that, CIMB Niaga also has a complaint service or Whistle Blowing System (WBS), which is managed independently by a third party while guaranteeing the reporter's anonymity. In its implementation, CIMB Niaga has received 133 reports via WBS with a problem investigation completion percentage of 27% or the equivalent of 36 reports in 2021.

From a governance perspective, Danamon (2021) also has a public complaint mechanism which includes disclosing the number, type and percentage of public complaints. The names of companies or governments funded by Danamon are also disclosed in detail, including economic sectors, geographic areas and syndicated loans. HSBC (2021) is committed to providing increased knowledge and publishing sustainability reports covering ESG topics that are adapted to the Sustainability Accounting Standards Board (SASB) standards.

In terms of governance, banks have not openly provided information regarding credit or company funding on their websites, published portfolio details in cross tables by combining industry and regional data, and published the names of companies listed on the capital market blacklist due to sustainability issues. In this case, for example, although Maybank has explicitly integrated ESG into investment and reporting policies, it still needs

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to implement aspects of transparency and accountability. Maybank still does not provide a complaint mechanism policy, disclosure of financing and investment information, or other information such as a comprehensive financing portfolio.

## Policy recommendations

Based on the results of the bank assessment, several recommendations are:

1. Banks must increase their commitment to several themes and sectors that still have low ratings, such as health, gender equality, mining, climate change, and gas and oil.
2. Banks must have written and explicit policies regarding their financing commitments, such as determining criteria and safeguarding loans for high-risk sectors, such as mining, large-scale energy projects and large-scale plantations.
3. Banks can refer to sustainability criteria developed by various existing international standards as a basis for policy-making and written down explicitly.
4. OJK needs to encourage a sustainable financing and investment climate through policies and good practices by financial service institutions. The development of sustainable financing policies can refer to international standards.
5. OJK can accelerate the implementation of sustainable finance and green financing by implementing a mandatory green taxonomy. OJK also needs to develop incentive and disincentive schemes to attract banks and ensure the green taxonomy's implementation. There is a need for a task force involving multi-stakeholders, including CSOs and the private sector.

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