The intention-action gap

BANKING ON PALM OIL IN SOUTHEAST ASIA

Hope and renewal, or more of the old greenwashing?

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Author:
Gulzhan Musaeva
www.linkedin.com/in/gulzhan-musaeva/

Contact:
contact@gulzhanmusaeva.com
info@aidenvironment.org

Designer
Athur Sinai
www.helliumworkstudio.com

Burnt peat forest for oil palm in Indragiri Hulu, Riau
Image by **Aidenvironment**

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Summary

These days pronouncements about climate change and other impending environmental cataclysms are made so often that they seem trite. One hears about energy and transport and their impacts, but land — the broad theme of this report — features less. **The focus is on the exploitation of land resources by the palm oil sector and the facilitation of this process by banking institutions.**

Why palm oil? For a highly efficient crop that it is, it has always been controversial by reason of its association with hefty environmental and social offenses. **Geographically, it is the two leading producing nations of Southeast Asia, Indonesia and Malaysia, that are being examined, while the bank network includes the biggest local financiers from the same nations, plus neighbouring Singapore.**

Because Southeast Asia is home to the tropics, the effects of climate change are more exaggerated here. Heat, storms, flooding, sea level rise, water scarcity are among the immediate concerns. While industries have been affecting the air, agriculture has been stripping the land of its natural resources and leaving a deeply negative imprint on biodiversity. **In recognition of these twin threats to the region's economic, social and political stability, the policymakers and the private sector alike have been stepping up their game to minimise losses and leverage opportunities,** although not without exception (see Indonesia's omnibus bill).

Local financial regulators have been pulling their weight. As members of the Network for Greening the Financial System (NGFS) and other similar initiatives, they have acknowledged the systemic nature of environmental, social and governance (ESG) issues in finance and busied themselves with drafting guidelines for the industry to use in their risk management. Sensitivity to outside criticism and nationalism, though, are potent.

Real change, of course, requires an ecosystem of stakeholders who are willing to listen, commit and collaborate. **Banks generally seem to be more open to learning about ESG and implementing the relevant guidelines where they exist, but that is easier said than done.** As creditors, they are notoriously stingy with data about their clients, and commitments to greater transparency have not so far translated into greater disclosure.

This report sets out to map out palm oil sector specific policies of Southeast Asian banks, a sample of 15 institutions, to evaluate their progress in the area of sustainable finance, especially when it comes to execution.

Summary

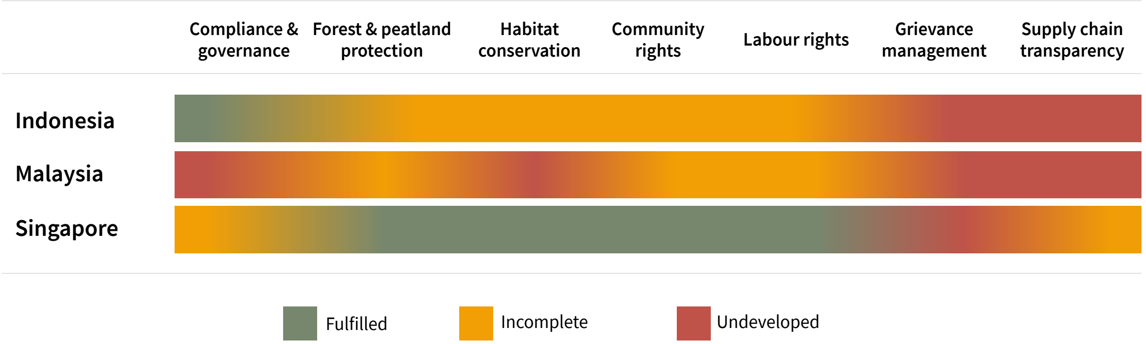
Bank policies on palm oil

Bank financing of palm oil

Bank policies on palm oil

Regulatory developments are gaining ground all around. Indonesian banks have had to come up with sustainable finance plans this year and start reporting accordingly. The Singaporean banks are advancing on the ESG front voluntarily while simultaneously trying to distance themselves from palm oil. The picture looks muddled in Malaysia where the leaders and the laggards are separated by a deep divide.

Scores of all sample banks on forest relevant sustainability policies



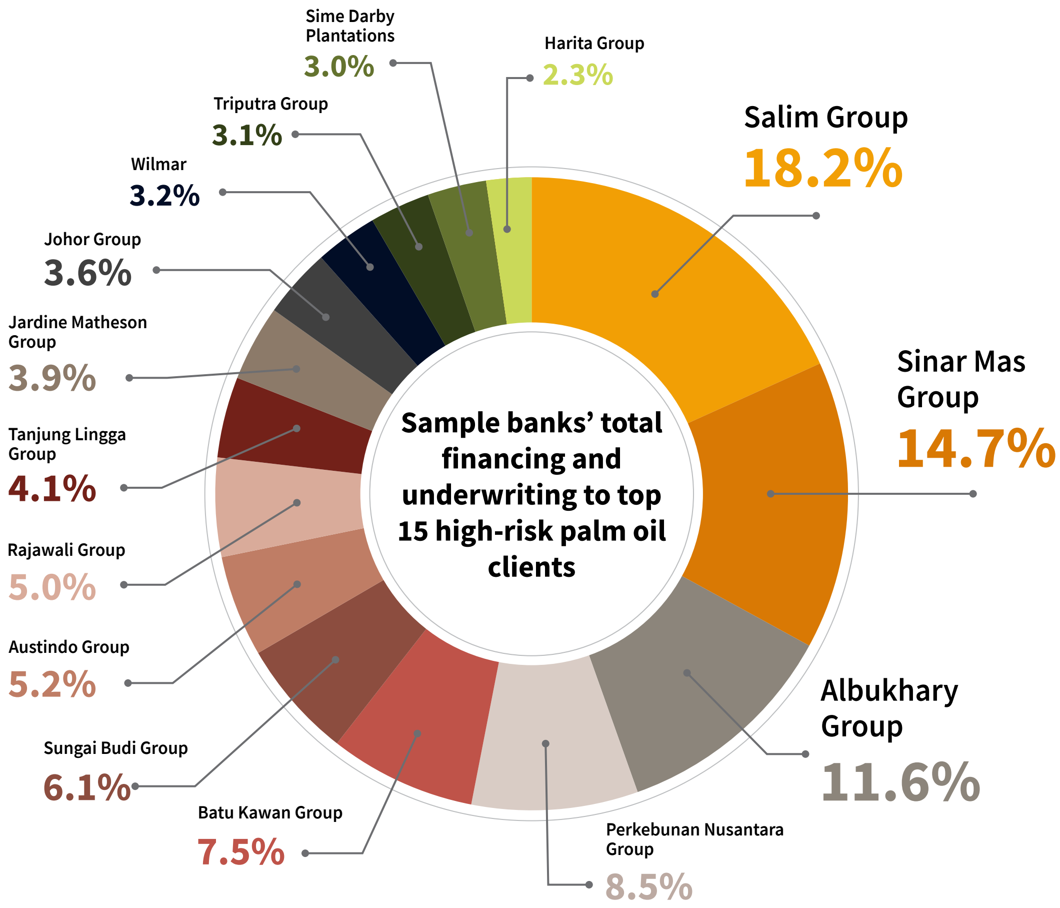
While policies are being crafted more actively than before, their quality is a mixed bag. Not all banks mention even the foundational tenets that disallow deforestation, peat development or ill treatment of communities and workers. Some other topics — smallholders, third-party supply chain, grievances, among other things — are hardly covered at all. No bank measures or publishes its forest footprint.

So improving policies is imperative. But the more complicated exercise is ensuring they are all properly and fully implemented, which banks have struggled with. This calls for a rethink of strategies and a shift of efforts from reaction to prevention. For one, compliance with forest policies must become a requirement, not an option, for all clients. Better enforcement could mean going against the grain, bypassing certain traditional practices such as client confidentiality.

Summary

Bank financing of palm oil

The 15 banks from Indonesia, Malaysia and Singapore were selected based on their activity in the palm oil sector as both lenders and securities underwriters. According to Forests & Finance, an independent data platform, they supplied on aggregate $13.6 billion in new credit to palm oil clients based in Southeast Asia between 2016 and April 2020 — equivalent to 47% of $29 billion provided to the sector by all financial institutions globally. Another $2.1 billion was issued by the same banks in investment monies through underwriting for debt and equity capital.



Tellingly, close to 85% of combined financing and underwriting went to forest-risk clients who possess a confirmed record of either environmental or social transgressions, or both, over the past five years. This, in effect, means that the banks conducting business with such clients are operating at variance with their own ESG policies. And there is no way to know if the financiers have taken any action against these or other high-risk clients anytime in the past since company names or their specific violations are never revealed.

For the palm oil sector in Southeast Asia (and elsewhere), banking acts as a prime enabler (that has proven to be more important than investment). It is a financial lifeline, but also a source of social validation that can drive more business. Therefore, it is critical that banks are careful about whom they are assisting. **By and large, regional financial institutions are no longer in denial about their role in creating environmental and social crises. But wary of radical reform in the absence of strict binding regulation, many seem unsure of what to do about their new responsibilities.**

The State of Palm Oil

Time has not been unkind to palm oil. Since it was brought to British Malaya from its far home in West Africa over a century ago and its economically advantageous qualities came to light, the markets for this commodity have thrived. This meant that tremendous swaths of forested land were converted to oil palm plantations — invariably leaving a trail of destruction and conflict.

Not surprisingly, palm oil has developed quite a controversial reputation. On the one hand, it is almost a miracle crop with high yields and numerous uses that has purportedly lifted millions of rural folk out of poverty. On the other hand, it is also one commodity that has driven deforestation of devastating proportions and is alleged to have enriched legions of corrupt conglomerates.

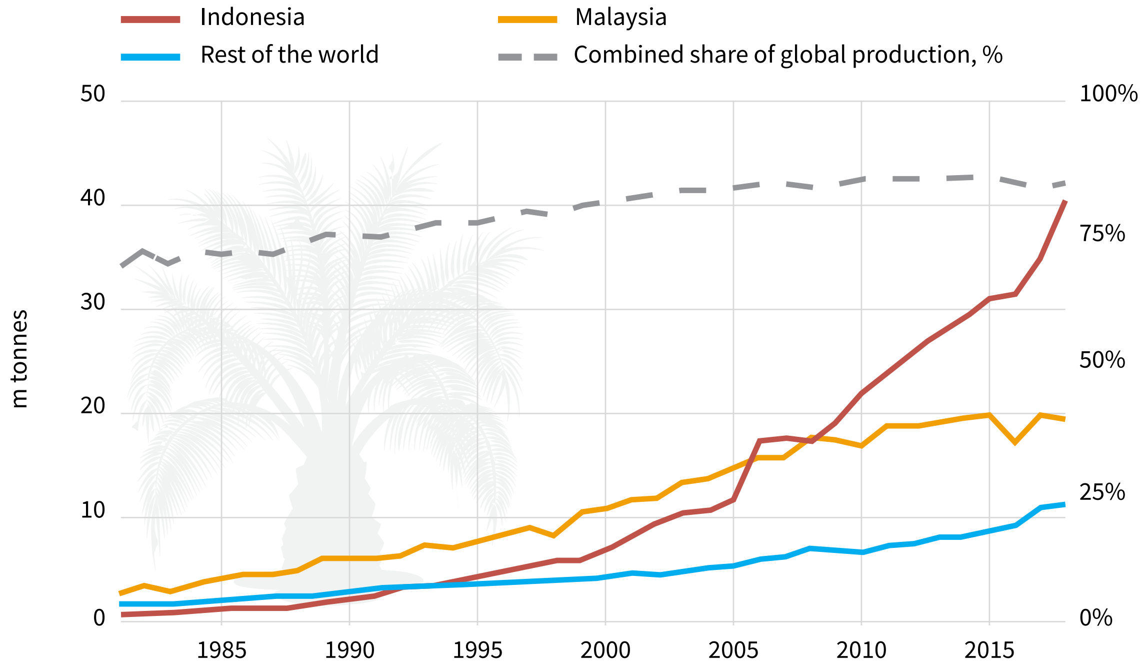
Whether palm oil is a boon or a bane continues to be a topic of much heated discussion on various levels. Local populations in Indonesia and Malaysia have been at the receiving end of numerous **campaigns** in defense of palm oil, so their attitudes towards the sector are **mixed**. While both sides present some valid arguments, many argue for the middle road that does not propagate shunning the commodity, but advocates for its cultivation within limits and conditions that are environmentally and socially fair.

The State of Palm Oil

1.1 The proof is in the numbers

Despite activist criticism through the years and excepting short-term gyrations, palm oil markets today are as strong as ever. The global production has increased ten times from 7m tonnes in the mid-1980s to 75m tonnes in 2020, spurred by ever-growing demand for the versatile vegetable oil in food, chemicals and fuel. More than 80% is produced by only two countries in Southeast Asia, Indonesia (the bigger chunk, or about half of the total) and Malaysia.

Palm oil production volumes



Source: FAO

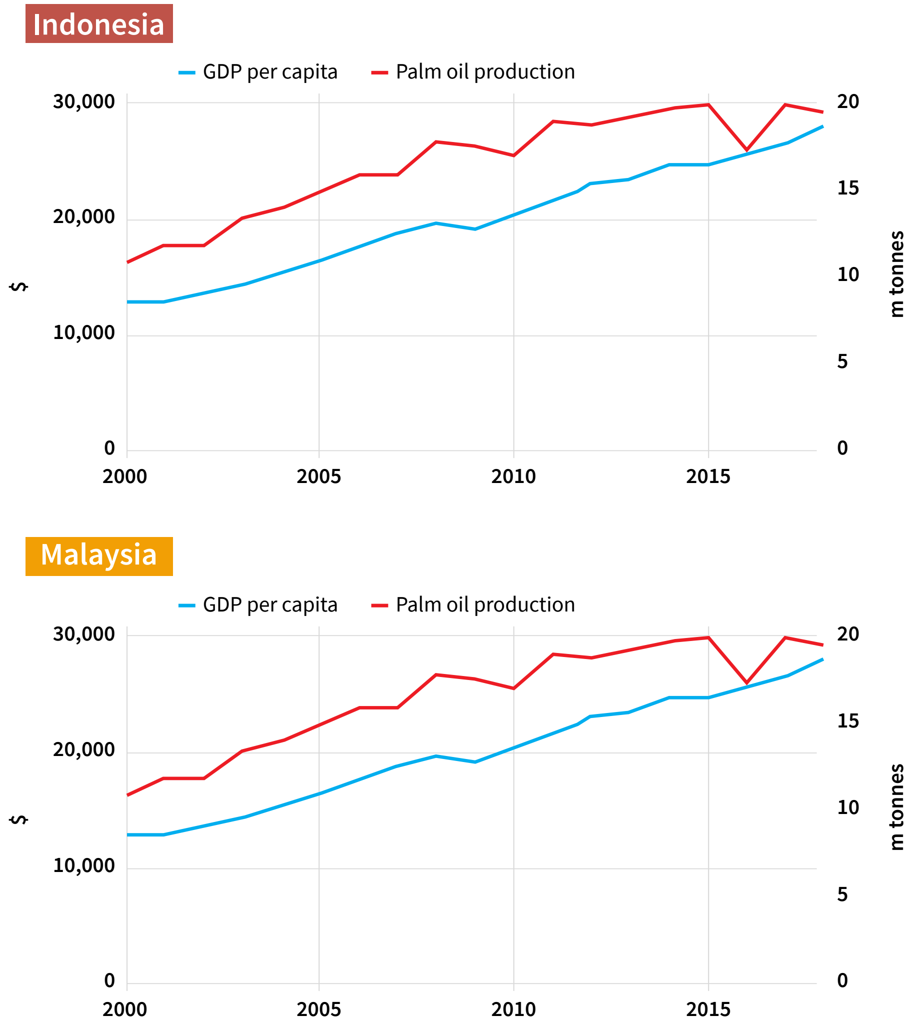
Indonesia, the largest economy in the region, has taken to palm oil especially fondly, having expanded the area dedicated to oil palm harvests by 2,000% over the last three decades to almost 13m ha (equal to 13% of forested land). The commodity is the archipelagic state's biggest agricultural export, contributing about 15% to total. However, alongside consequent economic gain, what it has lost as a result is irrecoverable: from 9m ha of primary forests lost since the beginning of this century, close to one-fourth have been razed to make way for new oil palm plantations.

Palm oil's contribution to national output in **Malaysia** — where the sector assumed national importance in the early 1980s — is roughly similar: it made up 38% of total agricultural production last year and about 3% of GDP. Malaysia too has paid a dear price for its pursuit of economic self-interest. Since the 2000s, Malaysia has lost more than 29% of its tree cover and 17% of primary forests. Both countries, along with neighbouring Singapore, suffer from annual bouts of haze that follow fires set deliberately to clear land for plantations.

Prices have reflected the commodity's positive performance, with Malaysian palm oil futures quadrupling to MYR4,000 per tonne between 2000 and the end of 2020. Relative affordability has made palm oil the preferred choice in populous developing countries such as China, India and Pakistan. The consumption of cooking fats and oils in these and other importing nations (to a lesser degree in Europe and the Americas) is expected to grow exponentially and thus guarantee the future of palm oil.

It is almost certain that the sector will continue to prosper in the future due to a confluence of attractive propositions of palm oil as a crop. And this might not help encourage the transformation of production processes along environmental and social lines for the sake of sustainability. Nonetheless, the sector has been making some patent strides in forest protection, particularly in Southeast Asia.

Positive correlation between GDP growth and palm oil production volumes



Source: World Bank

The State of Palm Oil

1.2 On the bright side

There has been some good news in recent years. The Roundtable on Sustainable Palm Oil (RSPO), a leading certification body for sustainability, has improved by leaps and bounds under incessant pressure from non-profits and now scores highly for biodiversity protection and assurance. More and more major players along the palm oil supply chain, from growers to refiners to traders, are committing to No Deforestation, No Peat, and No Exploitation (NDPE).

Tropical growers Malaysia and Indonesia have made promises to manage their remaining forests sustainably, in line with the Sustainable Development Goal 15. **Malaysia** is to maintain at least 50% of its territory under forest cover; by 2025, half of all production forests and agricultural areas are to be certified and sustainably managed. Sabah, one of the two Malaysian states on Borneo which supplies about one-third of the total palm oil production, aims for full RSPO compliance by 2025. Nationwide, the mandatory Malaysian Sustainable Palm Oil (MSPO) certification scheme covers 87% of the total area planted with oil palm. There is a national cap on land dedicated to oil palm plantations of 6.5m ha to 2024 and a permanent ban on converting forest reserves and peatlands.

Indonesia too is paying more attention to the sector through improved environmental regulations. There exists a similar ban on converting primary forests and peatlands (although the 2018 moratorium on new oil palm permits has just expired). In 2019, President Joko Widodo ratified the five-year National Action Plan for Sustainable Palm Oil, followed by a revision of the Indonesian Sustainable Palm Oil (ISPO) programme. The largest local companies have turned NDPE compliant over the past decade; the adoption rate is notably high in the midstream market.

These efforts combined are at least partly responsible for lower rates of deforestation that Southeast Asia has been witnessing in the last few years. Primary forest loss in both Indonesia and Malaysia has slowed for the fourth straight year, in stark contrast to some other deforestation hotspots worldwide. Indonesia released on average 200 Mt of CO_2 annually from deforestation between 2016 and 2020, three times less than table leaders Brazil and the Democratic Republic of the Congo each.

In recognition of Indonesia's advances in forest preservation, the government of Norway had decided to disburse the long-awaited first payment of $56 million under the Reducing Emissions from Deforestation and Forest Degradation (REDD+), a results-based fund initiated a decade earlier. The transfer, however, is off the cards now due to Indonesia abruptly terminating the agreement in September, citing the lack of implementation progress.

A new initiative, the Lowering Emissions by Accelerating Forest finance (LEAF) Coalition, will be picking up the baton, hopefully making conservation more financially attractive to jurisdictions with forest-based natural resources.

Land clearing in PT Prima Bahagia Permai's concession
Image by **Aidenvironment**

The State of Palm Oil

1.3 Sticking issues

It is a peculiar thing about palm oil that almost every argument on one side of the debate can be countered by a seemingly equally sound argument from the opposing side. In Southeast Asia, the momentum and the leadership buy-in for sustainability in the sector are evident. But critics say the reforms do not go far enough.

To start, RSPO still misses the mark and apparently does little to protect endangered species and habitats; one study goes as far as to call it outright 'meaningless'. RSPO currently only covers 19% of the global production, which could be attributable to its voluntary nature. There is overall progress on NDPE policies but implementation has been patchy, especially among upstream companies.

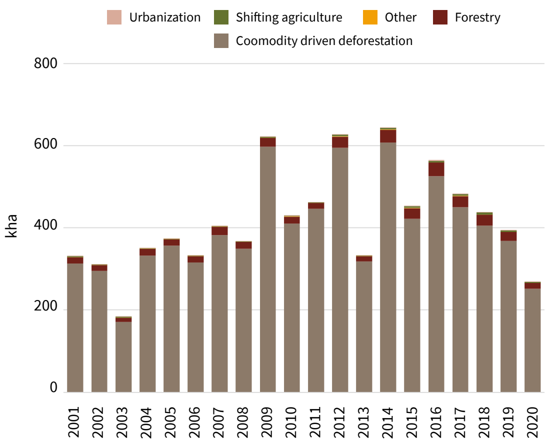
There is a public governance problem too: the moratoriums are deemed to be deficient, and the regional governments have not cracked down on burning practices — not in Indonesia where most fires take place, not in Malaysia or Singapore either which suffer from haze. Neither are fines on deforesting companies being duly administered.

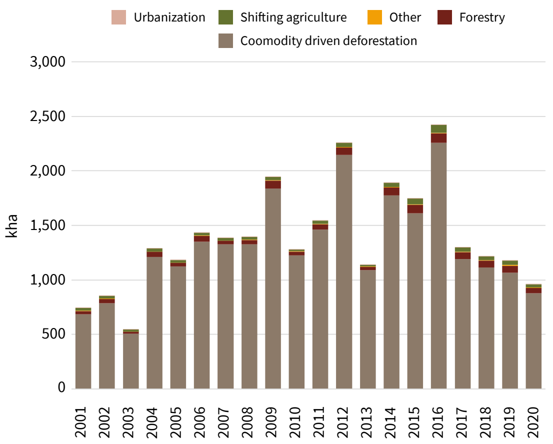
ISPO, a localised version of RSPO that companies and smallholders are being pushed into, has been revised but is still far from perfection; fellow MSPO is also undergoing changes following past criticism. More data is being collected on plantations but monitoring on a granular level is practically absent.

Deforestation may have decelerated regionally, but country figures do not flatter. Indonesia accounts for two-thirds of all forests replaced by oil palm; close to 50% of deforestation in Malaysia has been driven by palm oil. This helps explain why Southeast Asian forests have become a net source of carbon emissions in the last 20 years, even as forest land overall remains an important net carbon sink globally.

Emissions stemming from agriculture are particularly problematic in Indonesia given its size and population. It rivals Brazil and China in that sense, emitting nearly 1b tonnes of CO_2 equivalent a year. Oil palm is the biggest culprit as clearing just one hectare of rainforest for oil palm produces about 638 tonnes of CO_2 equivalent. Combined emissions from conversion to oil palm in Indonesia and Malaysia account for more than 20% of total regional greenhouse gases.

Tree cover loss driven by deforestation





Source: Global Forest Watch

While both the countries have made pledges under the Paris Agreement — Indonesia to reduce emissions by 29% and Malaysia by 45% by the year 2030 — it has been suggested that their targets fall short of what may be achievable. In the case of Indonesia, national projections surreptitiously allow for the tripling of emissions across sectors other than forestry.

Yet another reason why palm oil invites controversy is a host of social issues in producer nations it is associated with. At the bottom of it is the infringement of customary rights of local communities who many a time lost their land to plantations, without compensation or access to effective recourse or remedy. Land conflicts aside, the sector is plagued with abuses of labour involving wage dicrimination, trafficking, forced and child labour.

Although these concerns are getting highlighted by some importers as of late, the amount of pressure on incriminated corporations is not nearly enough to inspire a systemic change. It could not possibly be, seeing that more than half of global demand for palm oil comes from developing countries which do not place sustainability at the forefront of trade relations. Data from 2019 confirms: only 3-4% of total volume consumed in China, India, Indonesia, Malaysia and Singapore was certified.

A recent omnibus bill and possible implications for the palm oil sector

To the casual observer, Indonesia's recent progress in curbing deforestation is undeniable. Yet it is tempting to doubt the sincerity of these efforts, given the complicated reality on the ground. President Joko, presently in his second term, has been vocal about his single-minded focus on business interests, which he hopes to stimulate by means of the Job Creation law, or the so-called omnibus bill which amends 79 laws in one go, swiftly drafted and passed in 2020.

The new law is purported to be cutting through the bureaucratic quagmire faced by industrialists. But in doing so, it is rather ruthlessly getting rid of existing environmental and social safeguards, much to the chagrin of non-governmental organisations and labour unions. One example of a process being butchered is the environmental impact assessment (known as Amdal) which will no longer include public participation or allow for legal challenges. Another that can embolden deforestation is the removal of a 30% minimum requirement for islands to be kept under forest cover. Also, applications for new plantation permits or their approval will not be restricted anymore.

Although the legal status of the bill (or its final version for that matter) is not yet finalised given the ongoing hearings in the Constitutional Court, the government has already started rolling out regulations and decrees to execute it. The Indonesian Palm Oil Association (GAPKI), for its part, lists the application of the omnibus law among its focus areas in 2021. And while responsible investors may wisely try to stay clear of Indonesian climate- and forest-risk sectors in view of questionable novel legislation, less scrupulous financiers may be encouraged — with grave consequences for sustainable development.

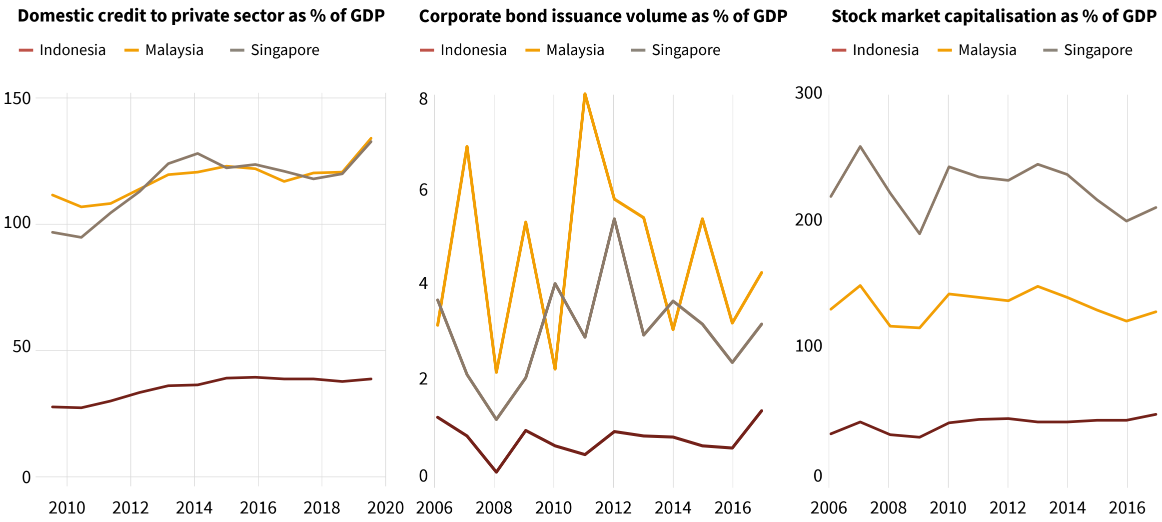
Banking for Palm Oil

Banking for Palm Oil

2.1 Industry dynamics

The financial system in Southeast Asia has developed in tandem with its burgeoning economy. Regional nations grew at an average rate of about 5% over the past decade, on the back of rising exports, real wages and infrastructure investments. (Following a downgrade in 2021 in view of pandemic restrictions, the average growth rate is expected to return to 5.2%.) Banks across Indonesia, Malaysia and Singapore have all grown assets and profits, albeit from different starting points. Inclusion of large swaths of the underbanked population and digitalisation of services, against or alongside fintech challengers, are ongoing tasks that support the outlook for institutions even as the pace of economic growth inevitably slows.

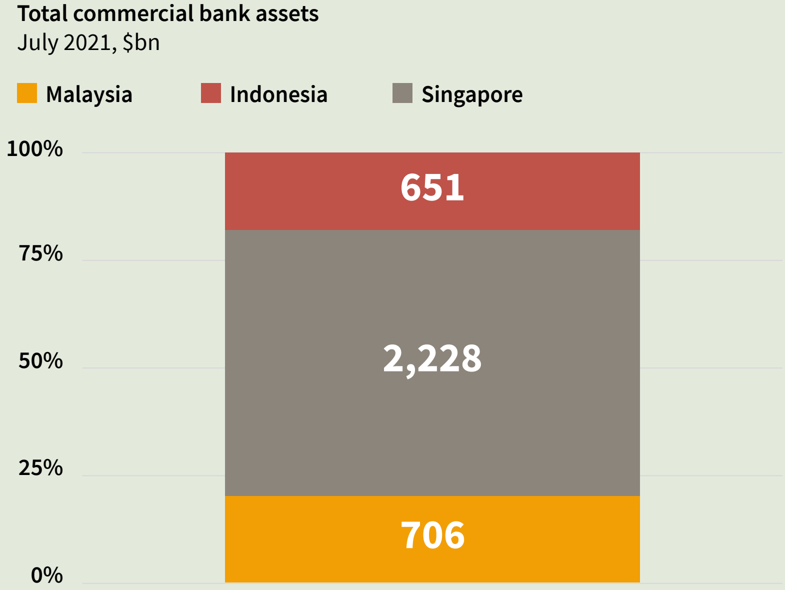
Financial development measured by financial capital to GDP



Source: World Bank

Banks have the lowest penetration in Indonesia at about 40% of GDP which is an indication of the financial system's relative immaturity but also of an untapped opportunity to raise the volume of credit. In contrast, Malaysia's credit-to-GDP stands at 137% and Singapore's at 175% — which shows how engaged banking institutions are in the real economy. Bond markets are active in both Malaysia and Singapore, whereas Indonesia is characterised by an excess of equity and a low debt level in finance.

Relative sizes of banking sectors in Indonesia, Malaysia and Singapore



Source: Central banks

Retail, wholesale and investment banking activity from Southeast Asia has picked up considerably, lifting incumbents higher on global and Asian lists of banks. Indonesia features heavily, not least due to a sheer multitude of banks — 110 of commercial type. Malaysia maintains a closely integrated pool of eight locally owned banks, dominated by few which have branched out far and wide across national borders. Singapore is a key financial hub that accounts for the lion's share of banking revenues in the region; the industry is the second largest contributor to GDP.

Not only have leading banks been catching up in size but also product innovation and technological sophistication. As they enter the next stage of development, calls are mounting for them to adopt new business models that will facilitate sustainable growth. The spectrum of material topics includes culture change, opportunities and threats of new technologies, and emerging economic, market and operational risks. Conventional financial performance will have to be appropriately supported by a reformed vision and long-term value proposition. To thus help financial institutions stay relevant in the new age, guidance from public agencies will be essential.

Singapore
Image by **Aditya Chinchure, Unsplash**

Banking for Palm Oil

2.2 Regulatory background

Historically, Southeast Asia has seen much experimentation in regulatory management given the diversity of financial markets and economies. The bank based system in Indonesia — where banks own 80% of total financial assets — went through multiple stages of liberalisation and deregulation. Malaysian banks walked the path of consolidation and rationalisation following the Asian financial crisis of 1998 in a bid to raise their competitiveness. Meanwhile, Singapore has always been a well-oiled machine whose financial institutions gained prominence by participating in the country's trade-driven growth story. Overall, prudential regulations have resulted in shored up capital and liquidity and hence banks that are more resilient to systemic shocks.

Today, the world of financial services regulation is at the crossroads. After a protracted period of accommodating monetary policies and globally coordinated initiatives at establishing a more stable financial system, a tendency toward regulatory fragmentation has become pronounced. At the same time, supervisory expectations are at an all-time high, with regulators emphasising principles based approaches. In this context, responsible finance has emerged as a major transformation trend.

The need for action on environmental change and the urgency of it has not escaped regulators, for many of whom ESG initiatives have come to form part of efforts to ensure financial sector stability and broader economic sustainability. Southeast Asia too has followed these developments. The need for enhanced disclosure is the most commonly addressed aspect; however, direct instructions to banks for ESG to be integrated into risk management remain the exception rather than the rule.

Banking for Palm Oil

2.3 Responsible finance regulation

Southeast Asian states are participants in international initiatives on sustainability of the financial sector, but only slightly uneager. For example, the much publicised Task Force on Climate-related Financial Disclosures (TCFD) has been endorsed by just a few Indonesian and Malaysian companies. The United Nations Environment Programme Finance Initiative's (UNEP FI) Principles for Responsible Banking (PRB) count only two Malaysian banks as members; the newer Net-Zero Banking Alliance has none from Southeast Asia. Even the more specific Tropical Forest Alliance organised by the World Economic Forum involves no regional public sector partners.

Indeed, much of the action has been demand-side driven, started by multilaterals, civil society actors and public entities in developed jurisdictions where clean supply chains appear to matter more. Much of the impetus comes from the EU which has imposed restrictions on the import of palm oil as part of the larger climate and energy overhaul (though the bloc's tone has become more reconciliatory since the initial talk of restrictions). Its action plan on sustainable finance has been set in motion with the publishing of a taxonomy of economic activities for climate change mitigation and adaptation, which will be followed by several others, including one for the protection and restoration of biodiversity and ecosystems. EU-based financial institutions must start reporting on the alignment of their portfolios with the taxonomy from the end of 2021.

Global action to further the momentum

The much-awaited 26th UN Climate Change Conference of the Parties (COP26) held in Glasgow in November ended with a flurry of renewed pledges and commitments. Discussions taking place ahead of the event had placed hope in strengthening policymaking for sustainable land use in tropical regions, but the actual outcomes were disappointing. Indonesia, along with a hundred other countries (not including Malaysia), has declared its intention to halt and reverse deforestation by 2030. However, there are valid reasons to suspect that this declaration, much as the one made previously in New York, was made in bad faith. In Indonesia's case, its green rhetoric on the international stage is being contradicted at home, not least by its own the Ministry of Environment and Forestry.

Overall, COP26 saw a very low level of finance committed to forests by rich countries. The rights of indigenous peoples and local communities were not adequately highlighted by the governments concerned, nor were many agricultural companies willing to speak up. Finance industry representatives have made a bigger splash, though they count only two member banks from Southeast Asia.

Another UN event took place in Kunming in October, COP15 to the Convention on Biological Diversity (CBD). It has produced the world's newest agreement, a pledge to reverse biodiversity loss — that, according to the Intergovernmental Panel on Climate Change (IPCC), is inextricably linked with climate change — by 2030. The framework for delivering on that goal is going to be developed in spring 2022 during the second phase of the conference. The finance sector has shown some interest with its biodiversity pledge which has 55 signatories to date who have committed to align financial flows to nature positive outcomes, including restoration. Asian financial institutions, excepting a smallish Japanese asset manager, are conspicuously absent.

Also on the finance front, extending the prevalent climate change focus of environmental action is the Taskforce on Nature-related Financial Disclosures (TNFD) which is expected to be established by the end of the year. This development should help financial institutions adapt their financing and investment strategies based on biodiversity impact and begin reporting publicly on their overall contributions to biodiversity on the basis of a standardised framework.

Informally, financial institutions across Southeast Asia do refer to sustainability frameworks developed by organisations — such as the Sustainability Accounting Standards Board (SASB), the Global Reporting Initiative (GRI) and the CDP — for reporting purposes. Mostly, the ESG impact is measured and disclosed for internal operations but rarely for lending and investment portfolios where it is of much greater consequence. Regulatory encouragement on this front has been picking up slowly.

Indonesia: The movement towards sustainable finance in Indonesia began with the Financial Services Authority (OJK) joining the Sustainable Banking Network (SBN) that is hosted by the International Finance Corporation (IFC). By SBN's generous assessment, OJK has reached the 'established' stage of impact reporting post-implementation. It is true that the regulator has shown commitment to sustainable finance by developing instructions for the financial sector to increase the understanding of sustainability issues and include the same in funding processes. In fact, it is the only country in the region that has legally enforced the implementation of sustainable finance principles and its reporting (even though at this point violators may get away with little more than a wordy slap on the wrist). Financial institutions have started officially reporting on their sustainability performance only this year, so it is very early in the day yet. But implementation is likely to be deficient. Still, OJK is ploughing on: next on the agenda is a guideline for land-based sectors containing specific recommendations for protection of forests and peats.

Jakarta
Image by **Afif Kusuma, Unsplash**

2014	Sustainable Finance Roadmap I by OJK	Part of the National Long Term Development Plan (RPJPN 2005-2025) which includes "Realising a greener and sustainable Indonesia" as one of the eight development missions; medium-term focus to 2019 was on establishing a basic regulatory framework, initiating reporting, training staff and providing incentives.
2017	Sustainable Finance Umbrella Policy by OJK	Defines sustainable finance, stipulates sustainable finance principles and makes the development and implementation of short- (one-year) and long-term (five-year) Sustainable Finance Action Plans (RAKB) and annual reporting on sustainability performance mandatory for banking, capital markets and non-banking players from 2019 onwards.
2018	Indonesia Sustainable Finance Initiative	A joint initiative of OJK and eight local banks initially (now 14 representing more than half of total banking assets) to promote responsible banking practices.
2020	Sustainable Finance Roadmap II by OJK	Long-term focus to 2025 is on integrating sustainability into risk management, corporate governance and information systems.

Against the conceptual framework of sustainable finance regulations suggested by the WWF, the **Sustainable Finance Umbrella** Policy (referred to locally as POJK51) is found to be deficient in several ways. The regulation only covers lending practices and does not mention human rights or labour issues among ESG considerations. Neither does it ask the banks to develop sector specific policies or perform an assessment of portfolio level exposure to environmental and social risks. But it fulfils other thresholds relating to the incorporation of sustainability into strategy, governance, risk management and capacity building.

Malaysia: Progress on sustainable finance is probably the least tangible in Malaysia. Value-based Intermediation (VBI) financing and investment guidelines released by the central bank, Bank Negara Malaysia (BNM), bear the closest resemblance to sustainable finance principles. But VBI technically applies only to Islamic financial institutions (which account for just 37% of total financing activity in the country) and is entirely voluntary in nature. Conventional banks are having to refer to VBI's sectoral guides in the absence of marketwide alternatives. There are tentative signs, however, that BNM, as a member of the NGFS, may be getting more serious. It has most recently developed a climate change focused taxonomy of economic activities for financial institutions; its implementation remains optional all the same.

Sunset view from Trader's Hotel towards KLCC
Image by **Esmonde Yong, Unsplash**

2019	VBI Financing and Investment Impact Assessment Framework (VBIAF)	Aims to facilitate the implementation of an impact-based risk management system for assessing financing and investment activities of Islamic financial institutions.
2021	VBIAF Sectoral Guides on Palm Oil, Renewable Energy and Energy Efficiency	Complementary guidance for financial institutions to incorporate environmental, social and governance risk considerations in financing and investment processes.
2021	Climate Change and Principle-based Taxonomy (CCPT) Guidance Document	Sets out five guiding principles to help financial institutions assess and categorise economic activities based on climate change impact and support for a low-carbon economy.

VBIAF is best characterised by the laxity of its guidelines, seeing that banks (primarily, Islamic but also conventional by extension) are given absolute freedom to choose which parts of the framework to adopt and to which extent to integrate the same. By contrast, the recently released taxonomy is indeed an upgrade. For the first time, the guidance formally applies to all financial institutions and brings much needed clarity in the way of a system classifying client activities based on their climate, overall environmental and social impacts. However, the point of these categorisation efforts is not entirely clear when the regulator openly discourages exclusions of activities based on perceived unsustainability. The new document also does not make reporting on any environmental or social risks obligatory.

Singapore: Sustainable finance in Singapore is an agenda under the Green Plan 2030 which has motivated the Monetary Authority of Singapore (MAS) to formalise the inclusion of climate change and other environmental issues into banks' risk management frameworks. Previously, initiatives were spearheaded by self-organised industry participants that form the Association of Banks in Singapore (ABS). The latter's loose set of guidelines on responsible financing has been newly replaced by environmental risk management guidelines whose implementation is supposed to be tracked.

2015	Guidelines on Responsible Financing by ABS	Define the minimum standards on responsible financing practices to be integrated into member financial institutions' business models.
2019	Green Finance Action Plan by MAS	Aims to support sustainable Singapore and facilitate Asia's transition to a sustainable future, with a key thrust to strengthen the financial sector's resilience to environmental risk.
2020	Guidelines on Environmental Risk Management for Banks by MAS	Sets out supervisory expectations for financial institutions to assess, monitor, mitigate and disclose environmental risk, with a transition period of 18 months before these expectations turn into legally binding requirements.

Early ABS Guidelines on Responsible Financing were brief and undemanding. In fact, the leading banks in the city-state have come to routinely outdo the suggestions. Now, MAS' new environmental risk management guidelines are a definite step-up. They outline regulatory expectations for the board and senior management and ask for processes to identify and assess environmental risks, on both customer and portfolio levels. Also mentioned is the need for policies for specific sectors with heightened vulnerability; disclosure is recommended to be TCFD aligned. Importantly, MAS is to follow up on the implementation of these rules this year.

ASEAN: There has been talk of sustainable development within the Association of Southeast Asian Nations (ASEAN) as well, the main unifying politico-economic body in the region. Its green, social and sustainable bond standards have seen good adoption by corporates and public issuers alike. Plans of a common taxonomy of sustainable finance have just been announced. It is meant to complement national guidelines, including Malaysia's climate change and principle-based taxonomy and soon Singapore's green finance taxonomy. It will be interesting to see how the regulators reconcile their different notions of sustainability given the wide disparity in economic maturity across ASEAN, which may be one reason why the development of sustainable banking principles under the ASEAN Central Banks' Agenda on Sustainable Banking is being delayed.

A key point in the discourse on regulation of responsible finance is whether disclosures on ESG risks should be made mandatory. The financial imperative for requiring detailed corporate reporting of material environmental or social exposures is becoming increasingly clear. And the regulators are responding. The US Securities and Exchange Commission (SEC), whose climate guidance is presently under public consultation, and the UK are moving in that direction. Their Southeast Asian counterparts would do well to catch up, considering that a principles-based approach without consistent implementation and monitoring mechanisms may not be appropriate as far as ESG issues are concerned.

Singapore
Image by **Jason Rost, Unsplash**

Banking for Palm Oil

2.4 Forest sector standards

It is a hoary truism that finance is the oil that keeps the economic machine running. But the weighty leverage of financial actors over business comes with added fiduciary duties and moral responsibilities, which by now have been acceded to by most. In the transformation of financial institutions from pure service providers to ecosystem influencers, the need for unifying industry standards has never been greater.

In the space of sustainable agricultural production, NDPE has become the golden standard referred to by growers, refiners, traders and downstream companies alike across a range of forest-risk commodities, most commonly palm oil. NDPE commitments mean:

- ***No deforestation*** — protecting High Conservation Value (HCV) and High Carbon Stock (HCS) areas, zero burning and reducing greenhouse gas emissions from operations;
- ***No development on peat*** — no new developments on peat, best management practices on existing plantations on peat and peat restoration;
- ***No exploitation*** — respecting the rights of indigenous peoples, local communities, workers and smallholders.

Hence, any forest sector specific policies should be assessed against NDPE as best practice. How exactly NDPE can be implemented to classify good and bad actors has been neatly organised by the Accountability Framework, established by conservation organisations, through a set of 12 principles.

When developing a sustainability strategy, financial institutions invariably make references to generic as well as specific frameworks that have come to define best-in-class ESG practices. Climate change impact of operations and supply chains, for instance, is normally assessed and disclosed in accordance with the Task Force on Climate-Related Financial Disclosures (TFCD), which also covers land use emissions. Social considerations tend to be covered by such broad documents as the Universal Declaration of Human Rights, the UN Guiding Principles on Business and Human Rights and the International Labour Organization (ILO) Labour Rights. Public reporting is often done based on the Global Reporting Initiative's (GRI) Financial Services Sector Disclosure Framework.

In palm oil, RSPO is the strongest benchmark, bolstered by a 2018 update which aligned it with NDPE. While RSPO's Manual on Best Management Practices is referred to by some banks for clients with cross-border operations, less rigorous MSPO and ISPO are still relied on in the assessment of smaller businesses. But whichever scheme is selected, it is imperative that separate due diligence is conducted by banks to ensure the certification credits are valid and independently verified. Any ongoing grievances against the prospective debtor or investee should be examined and followed up.

Financial institutions today have access to several ESG methodologies relevant to portfolio companies in forest-risk sectors. **The sample of Southeast Asian banks chosen for this report has been reviewed against essential requirements adapted from the Accountability Framework, Forests & Finance and Forest 500.** A responsible financial institution must apply the following non-exhaustive list of forest-risk policies to all products and deals:

Compliance & governance	Companies and their suppliers must ensure compliance with all relevant national laws and regulations.
Forest & peatland protection	Companies and their suppliers must commit to remove deforestation and conversion of all natural ecosystems.
Habitat conservation	Companies and their suppliers must not affect protected areas including primary, HCV and HCS forests.
Community rights	Companies and their suppliers must ensure the Free, Prior and Informed Consent (FPIC) of indigenous and local communities.
Labour rights	Companies and their suppliers must respect internationally recognised human rights and ensure compliance with key labour standards and all laws.
Grievance management	Companies and their suppliers must have a transparent and effective mechanism for grievances to be reported and remedied.
Supply chain transparency	Companies and their suppliers must disclose subsidiaries operating in forest-risk commodity sectors and ensure supply chain traceability.

Importantly, these policies ought to be effectively implemented through regular monitoring of clients for compliance and a timebound process invoked in cases of non-compliance, with suspension or cancellation of loans and divestment as the last option if engagement is unsuccessful. The implementation progress should be transparently recorded and publicly reported.

Palm oil fruit
Image by **tristantan, Pixabay**

Bank Assessment

The subject of this study is a sample of Southeast Asian banks across three countries, ordered by asset size:

- **6 Indonesian banks** — Bank Mandiri, Bank Rakyat Indonesia (BRI), Bank Central Asia (BCA), Bank Negara Indonesia (BNI), Bank Tabungan Negara (BTN), Bank Pan Indonesia (Bank Panin);
- **6 Malaysian banks** — Malayan Banking (Maybank), CIMB Group Holdings (CIMB), RHB Bank, Public Bank, AMMB Holdings (AmBank), Affin Bank;
- **3 Singaporean banks** — DBS Group Holdings (DBS), Oversea-Chinese Banking Corporation (OCBC), United Overseas Bank (UOB).

Under review is their progress on sustainability commitments and correlated financial performance over the last five years following the adoption of the Paris Climate Accords, between 2016 and 2020. Of specific interest are sustainability policies, or their absence, relevant to forest-risk sectors including palm oil.

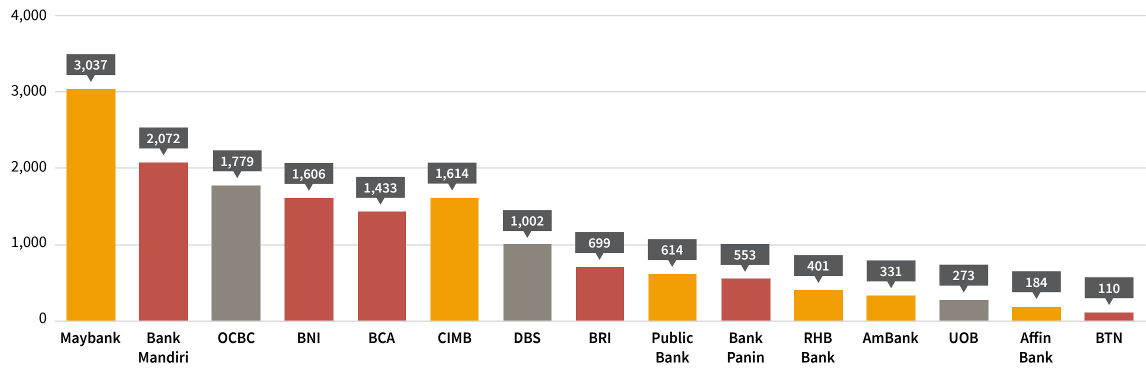
Banking for Palm Oil

3.1 Involvement in palm oil

The 15 banks have been selected based on their activity in the palm oil sector as both lenders and securities underwriters. Aggregate numbers are hard to come by, and in their most comprehensive form are presented on [Forests & Finance], a data platform run by civil society organisations. **Between 2016 and April 2020, the banks in Indonesia, Malaysia and Singapore supplied on aggregate $13.6 billion in new credit to palm oil clients based in Southeast Asia — equivalent to 47% of $29 billion provided to the sector by all financial institutions globally.** Another $2.1 billion was issued by the same banks in investment monies through underwriting for debt and equity capital.

Total credit disbursed & capital raised for the palm oil sector by the sample banks

2016-Apr 2020, $mn



Source: Forests & Finance

It is apparent that the financial flows from the Southeast Asian troika of nations are the energising force behind forest-risk commodities, particularly palm oil. **Indonesia is the top jurisdiction for palm oil financiers with a 41.2% share, followed closely by Malaysia where banks contributed 39.3%; last, but not least, is Singapore with 19.4%.**

Regional banks, therefore, bear the greatest responsibility for the conduct of forest clients whom they support. In order to succeed in discharging this responsibility effectively, the banks have to take all the necessary precautions when dealing with these high-risk businesses, which entails, first and foremost, the development of appropriate policies and their subsequent implementation.

Banking for Palm Oil

3.2 Financial standing

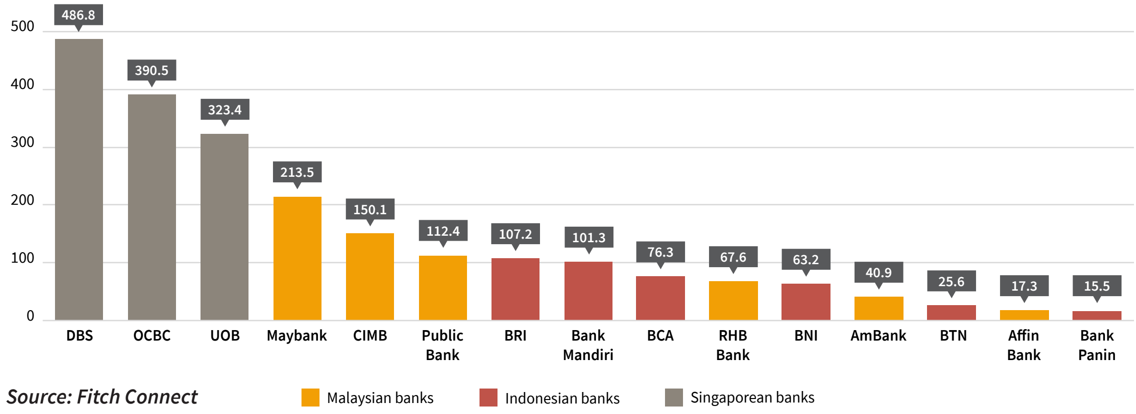
Nowhere is stakeholder capitalism — which promotes long-term value creation for all versus profit maximisation for shareholders — making more progress than in finance. New regulatory requirements and incentives in favour of sustainable assets are pushing banks to adjust their lending policies by preparing and integrating ESG scoring methodologies. This process produces two kinds of outcomes for the participating banks: one is mitigation of ESG risks associated with non-green assets; the other is a potential for additional income generation.

And while the emerging markets have not exactly led the movement on ESG initiatives, economies which rely on commodities under heightened scrutiny for environmental or social reasons — be it fossil fuels or palm oil — are exceptions where market players, banks included, cannot afford to ignore growing calls for sustainability. Material risks aside, the business case for sustainability is strong: there is evidence that companies operating sustainable models can increase their profitability and market value, which is good news for banks that fund them. The palm oil sector in Indonesia, for example, could lift its value by $9 billion through innovations motivated by climate transitions.

Palm oil fruit
Image by **tristantan, Pixabay**

Sample banks ranked by size

Total assets, end-2020, $bn

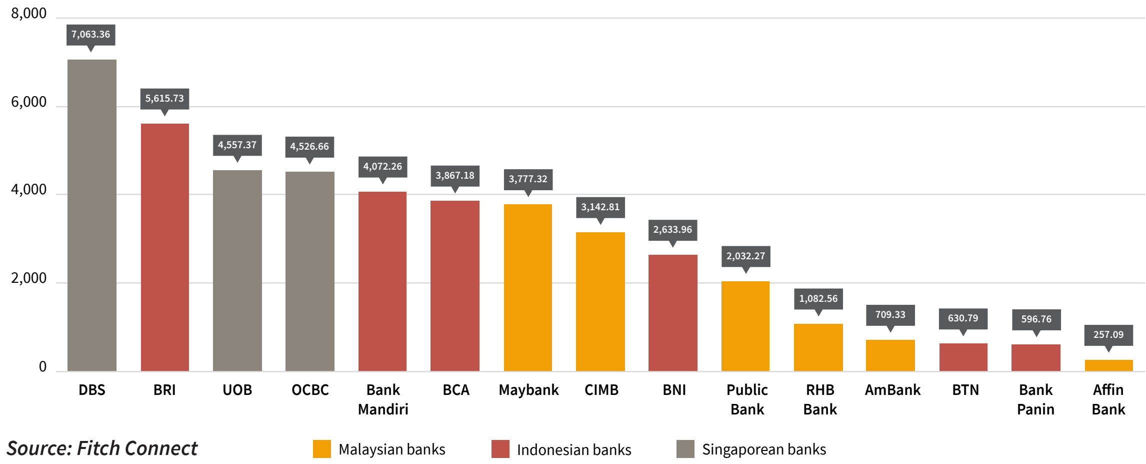


Source: Fitch Connect

The three Singaporean banks dominate size wise and account for more than one-fifth of the combined value of assets, according to the latest published fiscal figures. They are followed neatly by the top three banks in Malaysia and then Indonesia. For perspective, sample banks cumulatively hold about 58% of total banking assets in the three countries. The yields on earning assets are high, which allows for relatively high returns.

Sample banks ranked by profitability

Net interest income, 2020, $mn



Source: Fitch Connect

The profitability picture is more diverse. (Needless to say, 2020 was an exceptional year due to pandemic induced credit losses.) Large Indonesian banks with access to affordable funding have the highest net interest margins — a reflection of their dexterity in executing a market rate dependent business model. Banks in Singapore and Malaysia, in contrast, make more income through fees and service charges of various kinds. At the same time, margin compression due to steep operating costs is a major challenge across the region.

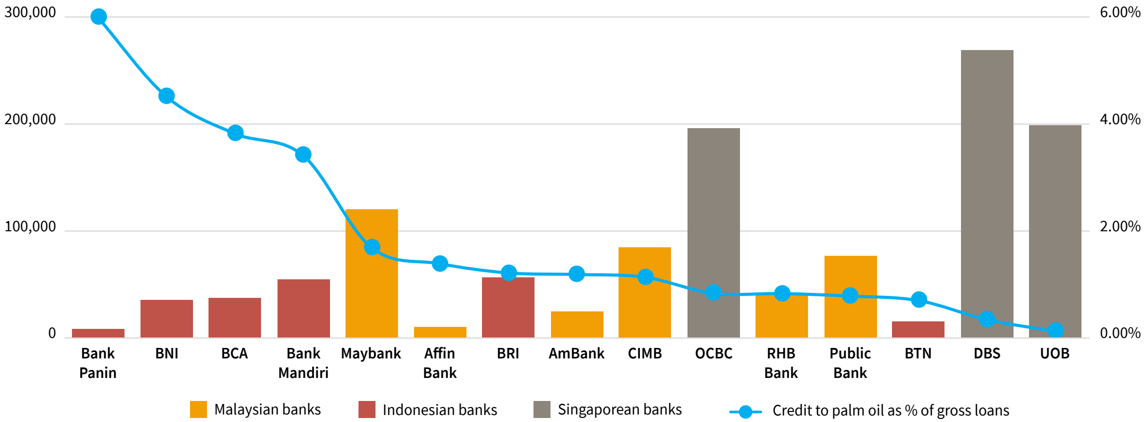
Performance statistics for the sample banks as of end-2020

Combined total assets	**$2.2 trillion**
Combined gross loans	**$1.3 trillion**
Combined operating profit	**$20.9 billion**
Combined net interest income	**$44.6 billion**
Average net interest margin	**3.1% (2019: 3.3%)**
Average return on assets	**0.7% (2019: 1.4%)**
Average return on equity	**5.9% (2019: 10.8%)**

Source: Fitch Connect

Orangutan visiting the feeding platform in the dry season (Tanjung Puting National Park, Kalimantan, Indonesia)
Image by **Dimitry B, Unsplash**

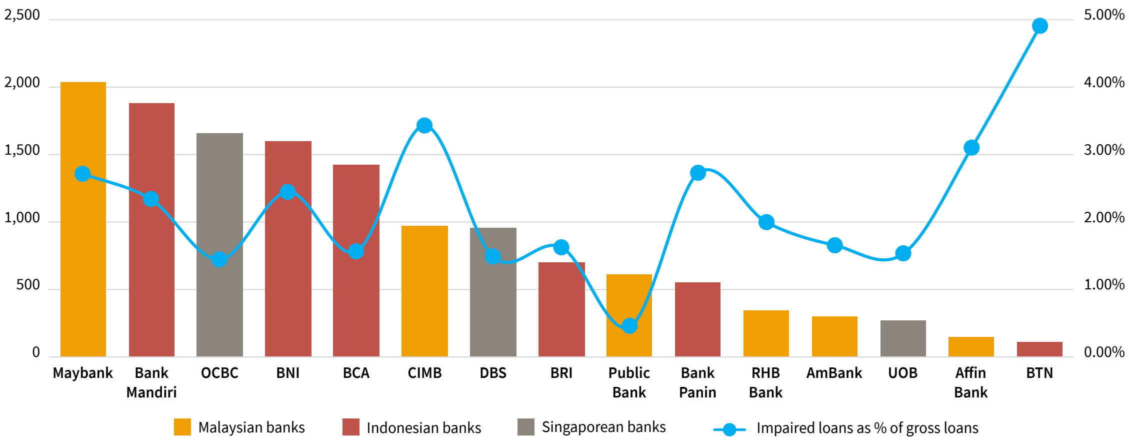
Sample banks' gross loans as of 1Q'20 vs. palm oil credit between 2016 and April 2020



Source: Fitch Connect, Forests & Finance

The juxtaposition of credit disbursements to regional palm oil companies against total loan balances could be taken as an indication of some financial institutions' growing reluctance to deal with palm oil business. Singaporean banks with larger portfolios are a case in point. There are exceptions, of course: at 1.7%, Maybank's financing of the palm oil sector as a percentage of gross loans was the highest among non-Indonesian banks in the sample group. Indonesian banks on the whole show a greater commitment to palm oil clients.

Sample banks' impaired loans ratio as of 1Q'20 vs. palm oil credit between 2016 and April 2020



Source: Fitch Connect, Forests & Finance

Finally, there appears to be little correspondence between the banks' financing of palm oil projects and asset quality represented by non-performing loans. Their averages do not diverge far from global medians. Overall, Singaporean and Malaysian banks had entered the pandemic from a position of strength thanks to good earnings buffers. The credit outlook remains negative for Indonesia — the sovereign, state-owned enterprises and the entire banking sector. With systematic risks heightened in 2021, the region is expected to get back to normalcy unevenly and over a longer period of time.

Banking for Palm Oil

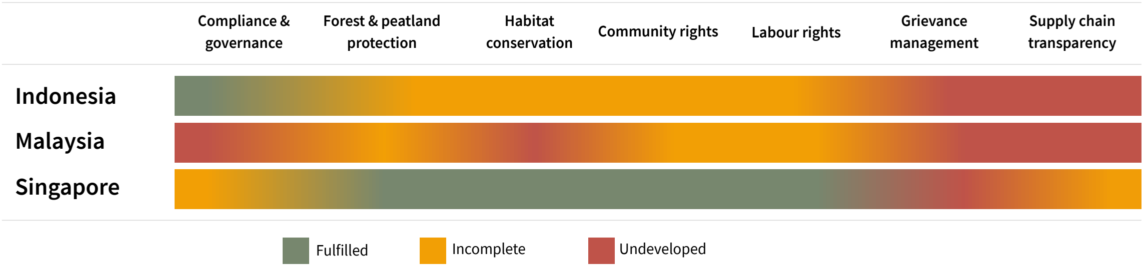
3.3 Sustainability policies

The risks of dealing with palm oil clients are established and consequential. This is because the risks they face are passed on to financiers as potential liabilities. There is a much higher likelihood that forest-risk companies turn out to be bad payers due to ESG issues. The bank in such a case would incur a direct financial loss and possibly additional costs through legal fines or regulatory penalties. Reputational damage that ensues is intangible but no less serious. Therefore, an accurate cost-benefit analysis of clients from high-risk sectors works to the benefit of financial institutions, above all. It is also what makes banks primed to address ESG risks in their portfolios.

A 2019 Sustainable Banking Assessment (SUSBA) study found that while most banks ASEAN banks formally recognised ESG risks that exist within their portfolios, their general sustainability as well as specific sector policies needed further polishing. Nor were the policies, where they existed, being put to practice across the board, with banks withholding important information on client assessment and monitoring in accordance with enhanced due diligence standards. Portfolio-level exposure to climate and other ESG risks was barely explored. Also, sustainability-linked financing was noticeably skewed towards renewable energy and green buildings, with opportunities in other sectors such as green agriculture less favoured.

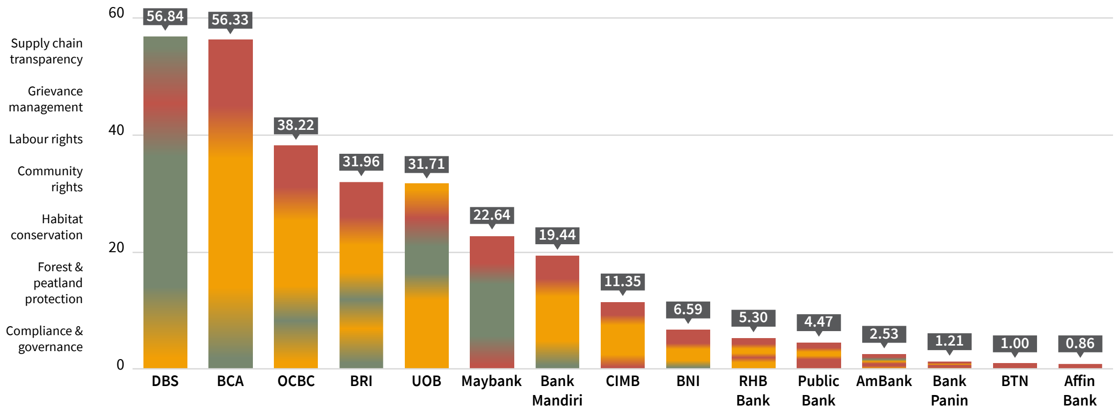
Two years on, this review of sustainability performance has not produced a starkly different result. Only that regulatory developments are gaining ground. The Indonesian banks have had to come up with sustainable finance plans and started reporting accordingly. Singaporean banks are advancing on the ESG front voluntarily while simultaneously trying to distance themselves from palm oil. The picture looks muddled in Malaysia where the leaders and the laggards are separated by a deep divide.

Combined scores of the sample banks on sustainability policies



Sample banks ranked by size

Market capitalisation, 28 Sept 2021, $bn

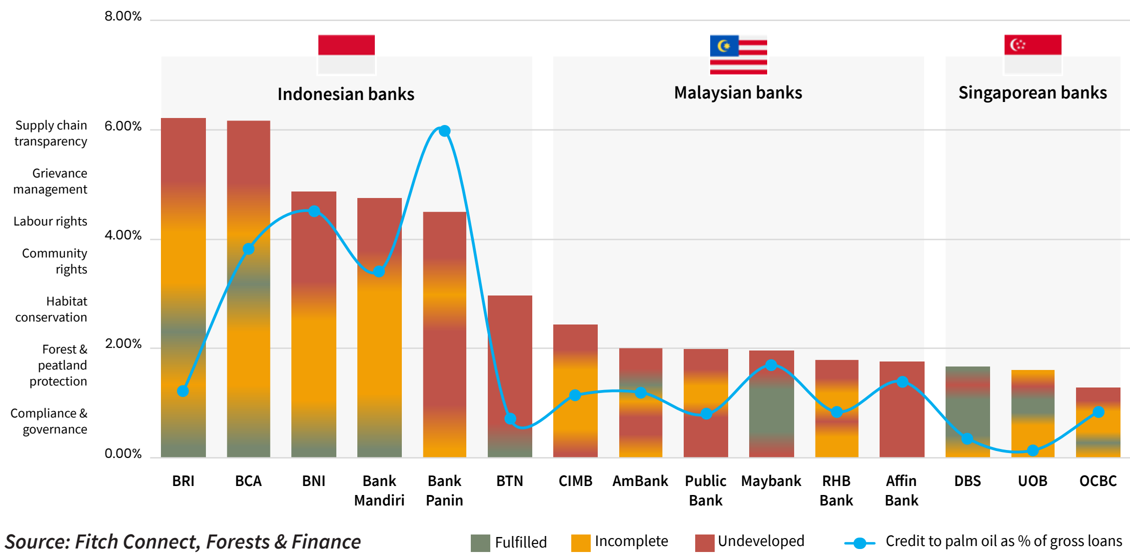


Source: Fitch Connect

Not to conflate correlation with causation, but generally banks with a weightier public standing as measured by market capitalisation seem to have more stringent ESG policies and take the risks that come with financing and underwriting palm oil deals more seriously. The maturity level of financial markets is a principal concomitant factor at play. Thus, the top-tier financial entities in Singapore and, to some extent, Malaysia appear to be held to a slightly higher standard of sustainability performance than the listed entities in Indonesia.

Sample banks ranked by profitability

Net interest margins, 2020 vs. palm oil credit, 2016-Apr 2020



Source: Fitch Connect, Forests & Finance

At the same time, the absence or presence of effective ESG policies and their implementation cannot yet be clearly linked to financial performance. The profitability of banks under review seems to have little to do with their servicing of palm oil. The Indonesian banks which lend the most to the sector on a relative basis feature the highest net interest margins on average, but this warrants no conclusion about sustainability and its possible association with financial accomplishments, as this is an area in need of exacting scientific research.

3.3.1 Indonesia

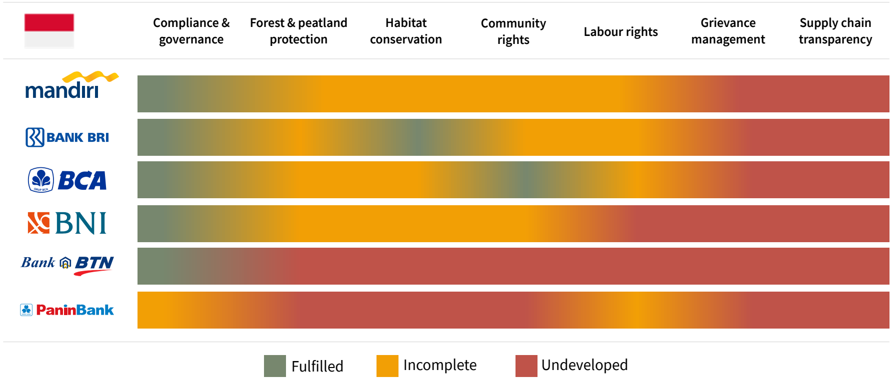
Because of palm oil's economic standing in Indonesia, it has emerged as a priority sector for the implementation of sustainable finance. The regulatory approach and action have helped promote ESG considerations in risk management. And since disclosure is mandatory now, sustainability reports are more or less standardised and therefore easier to read. But 2020 was just the first year in which (large commercial) banks reported on their sustainable finance activities in accordance with OJK's requirements and guidelines. Not all banks have specific palm oil policies yet; many still defer to the certifying bodies of ISPO or RSPO or the International Sustainability and Carbon Certification (ISCC) but do not verify client statuses by conducting their own ESG compliance checks and monitoring.

On average, Indonesian banks receive low-to-medium scores from external sustainability appraisers such as Forests & Finance and Forest 500 that look specifically at how forest sectors are being handled. Their newly developed sustainable finance action plans (RAKB in the local language) are still rudimentary, featuring minimum legal requirements — such as Amdal accompanied by environmental management and environmental monitoring reports (UKL-UPL) — and references to certifications as extra safeguards. One of them is the Ministry of Environment and Forestry's Program for Pollution Control, Evaluation and Rating (PROPER) which ranks companies based on their compliance with environmental regulations.

Some banks, like the eight comprising the OJK initiated project 'First Movers on Sustainable Banking', had started their sustainability journeys earlier and by now have successfully moved from capacity and policy development into execution. Even for them, however, transparency is still unsatisfactory. Under the pretext of client confidentiality, even the most forward banks do not reveal real issues they encounter during credit assessment and monitoring nor the names of their wayward clients.

One other issue plaguing Indonesian banks is a pervasive endorsement for gradual conversion to sustainability through education in place of enforcement through harsher measures. With ISPO, for instance, some banks accept a mere document of registration as proof of good intentions, when only full certification should be acceptable. Admittedly, such leniency is valid as far as smallholders are concerned, but this argument can be hardly applied across the board to all clients regardless of size and ability. It is expedient, no doubt, but not helpful in effecting meaningful change in companies who can do better than that.

Indonesian sample of banks: progress matrix on policies



mandiri

Financier profile in numbers

Credit to palm oil as % of gross loans	4.41%	Percentage of total for Indonesian banks
Gross loans	$55.2bn	26.3%
Credit extended to palm oil sector	$1.9bn	30%
Capital raised for palm oil sector	$0.19bn	94%
Total funding provided to palm oil sector	$2.1bn	32%
Funding of 'bad actors' as percentage of total	94.3%	*Of top 5 high-risk* palm oil clients:* *-Salim Group* *-Perkebunan Nusantara Group* *-Sungai Budi Group* *-Jardine Matheson Group* *-Sampoerna Group*

Gross loans as of 1Q'20; palm oil figures between 2016 and April 2020.
**Defined as companies that do not have NDPE policies or fall short on their implementation.*

Majority state-owned Bank Mandiri is the largest bank in the country by assets. Like all other large commercial banks, it has newly developed a sustainable finance action plan as mandated by the regulator. In addition, 13 strategic initiatives were formulated in 2019, one of them for palm oil, whose criteria lists compliance with local environmental and social regulations. In 2019, the bank started piloting an engagement programme for selected palm oil debtors to 'educate' them on sustainable production practices with the ultimate goal of helping them comply with ISPO. Initiatives like this, according to Bank Mandiri, bring to light the low level of ESG awareness among customers and their difficulties in satisfying certification requirements. By end-2020, 83% of all its corporate clients were certified.

Policy status	Policy details	Implementation
Sustainable finance action plan and sector specific policies	Details minimum general and palm oil specific ESG criteria and mitigation plans	Discloses some monitoring results and indexes reporting against SUSBA

Compliance & governance	Requires a plantation permit, Amdal, PROPER	
Forest & peatland protection	Denies financing for plantations on peatlands and those cleared by burning	Does not clearly mention deforestation as a prohibited activity
Habitat conservation	Stipulates protection for HCV and HCS peatlands	Does not mention other natural landscapes (e.g. forests)
Community rights	Demands clear land ownership and protection rights of ethinic minorities	Does not mention the concept of FPIC
Labour rights	Outlaws employing underage workers and discrimination	Does not mention other possible forms of labour abuse (e.g., forced labour)
Grievance management	No such requirement for the palm oil sector	
Supply chain transparency	No such requirement for the palm oil sector	

**None of these apply to the clients' suppliers or smallholders.*

- Sustainable finance portfolio: IDR77.2tn ($5.4tn) as of end-2020

BANK BRI

Financier profile in numbers

Credit to palm oil as % of gross loans	1.22%	Percentage of total for Indonesian banks
Gross loans	$57.1bn	27.2%
Credit extended to palm oil sector	$0.699bn	11%
Capital raised for palm oil sector	-	-
Total funding provided to palm oil sector	$0.699bn	11%
Funding of 'bad actors' as percentage of total	93.8%	*Of top 4 high-risk* palm oil clients:* *-Rajawali Group* *-Sungai Budi Group* *-Perkebunan Nusantara Group* *-Sampoerna Group*

Gross loans as of 1Q'20; palm oil figures between 2016 and April 2020.
**Defined as companies that do not have NDPE policies or fall short on their implementation.*

The oldest bank in Indonesia, also state-owned, BRI held the top position for the longest time. Yet, it only incorporated ESG analysis in credit assessment last year, although its palm oil sector policy dates back to 2017. In the latter, outright stipulations are avoided, replaced with gentler encouragements towards good sustainability and certification. This might be due to BRI's extensive experience of working with smallholders who are the hardest to convert. On a positive note, the bank appears to take monitoring seriously, with a third-party assurance mechanism in place. Reporting is supposed to be benchmarked to GRI, TCFD and SASB but leaves out salient policy implementation details.

Policy status	Policy details	Implementation
Sustainable finance action plan and sector specific policies	Details risk mitigation criteria including licensing, environmental permits and certifications	Explains the monitoring process, follows up but does not disclose full results

Compliance & governance	Requires Amdal, PROPER, UKL-UPL, social impact assessment	
Forest & peatland protection	Denies financing for plantations on peatlands and those cleared by burning	Does not clearly mention deforestation as a prohibited activity
Habitat conservation	Stipulates protection for primary, HCV and HCS forests and peatlands	
Community rights	Demands respect for the rights of local communities and their resources	Does not mention the concept of FPIC
Labour rights	Expects employers to follow local labour laws	Does not reference international labour standards
Grievance management	No such requirement for clients	
Supply chain transparency	No such requirement for clients	

**None of these apply to the clients' suppliers or smallholders.*

- Sustainable financing portfolio: IDR88.3tn ($6.2tn) as of end-2020

BCA

Financier profile in numbers

Credit to palm oil as % of gross loans	3.82%	Percentage of total for Indonesian banks
Gross loans	$37.4bn	17.8%
Credit extended to palm oil sector	$1.4bn	23%
Capital raised for palm oil sector	$0.004bn	2%
Total funding provided to palm oil sector	$1.4bn	22%
Funding of 'bad actors' as percentage of total	96.2%	*Of top 3 high-risk* palm oil clients:* *-Salim Group* *-Sinar Mas Group* *-DSN Group*

Gross loans as of 1Q'20; palm oil figures between 2016 and April 2020.
**Defined as companies that do not have NDPE policies or fall short on their implementation.*

As the largest privately-owned bank in Indonesia, BCA is held to higher standards of efficiency. It is probably the most customer-oriented banking institution, just not one with the best environmental and social credentials. Although it mentions land use and natural resources as the biggest financed category of businesses, it does not give prominence to palm oil. (Interestingly, BCA used to be owned by conglomerate Salim Group whose food business has been mired in multiple controversies.) General requirements such as obtaining environmental assessment documents and certifications are mentioned in passing. High-risk clients are requested to periodically submit a mitigation plan. Only 36% of palm oil debtors were certified by either ISPO or RSPO in 2020.

Policy status	Policy details	Implementation
Sustainable finance action plan	Sustainable land use is mentioned as a key category for financing without specific sector policies	Outlines non-compliance procedures but does not disclose engagement results

Compliance & governance	Requires Amdal, PROPER, UKL-UPL	
Forest & peatland protection	Does not support clients involved in 'irresponsible land clearing' and deforestation	Does not clearly mention development on peatlands
Habitat conservation	Urges environmental protection and preservation of biodiversity	Does not mention explicitly mention HCV or HCS areas
Community rights	Denies financing for clients involved in violating the rights of local communities	
Labour rights	Demands protection for human and worker rights in line with the ILO	Does not require compliance with applicable labour laws
Grievance management	No such requirement for clients	
Supply chain transparency	No such requirement for clients	

**None of these apply to the clients' suppliers or smallholders.*

- Sustainable finance portfolio: IDR49.8tn ($3.5bn) as of end-2020

BNI

Financier profile in numbers

Credit to palm oil as % of gross loans	4.51%	Percentage of total for Indonesian banks
Gross loans	$35.4bn	16.9%
Credit extended to palm oil sector	$1.6bn	25%
Capital raised for palm oil sector	$0.008bn	4%
Total funding provided to palm oil sector	$1.6bn	25%
Funding of 'bad actors' as percentage of total	61.3%	*Of top 4 high-risk* palm oil clients:* *-Sinar Mas Group* *-Tanjung Lingga Group* *-Rajawali Group* *-Gozco Group*

Gross loans as of 1Q'20; palm oil figures between 2016 and April 2020.
**Defined as companies that do not have NDPE policies or fall short on their implementation.*

BNI is another important state-owned player that advocates the carrot rather than the stick approach in tackling ESG issues in forest-linked sectors. While it positions itself against deforestation and for biodiversity and conservation, it wraps such declarations in soft language pleading with clients to pay heed to their sustainability record. Nor is BNI ready to cut ties with persistent violators, turning instead to warnings to 'minimise credit'. Governance and processes for ESG risk management have been established and outlined, but compliance audit results are insufficient, as per usual.

Policy status	Policy details	Implementation
Sustainable finance action plan and sector specific policies	Limits credit to companies achieving at least a PROPER Blue status; requires ISPO or RSPO certification	Discloses credit distributed to compliant palm oil clients but not issues encountered with others

Compliance & governance	Requires plantation permits and licenses, Amdal, PROPER, ISPO/RSPO	
Forest & peatland protection	'Policies indirectly aims to avoid' deforestation	Does not clearly mention deforestation as a prohibited activity
Habitat conservation	'Pays attention' to conservation areas	Does not clearly reference HCV and HCS areas
Community rights	'Pays attention' to surrounding communities	Does not mention the rights of communities or FPIC
Labour rights	No such requirement for clients	
Grievance management	No such requirement for clients	
Supply chain transparency	No such requirement for clients	

**None of these apply to the clients' suppliers or smallholders.*

- Sustainable sector financing: IDR26.8tn ($1.9tn) as of September 2020

Bank BTN

Financier profile in numbers

Credit to palm oil as % of gross loans	0.71%	Percentage of total for Indonesian banks
Gross loans	$15.5bn	7.4%
Credit extended to palm oil sector	$0.109bn	2%
Capital raised for palm oil sector	-	-
Total funding provided to palm oil sector	$0.109bn	2%
Funding of 'bad actors' as percentage of total	100.0%	*Of the top high-risk* palm oil client: -Salim Group*

Gross loans as of 1Q'20; palm oil figures between 2016 and April 2020.
**Defined as companies that do not have NDPE policies or fall short on their implementation.*

Long-established state-owned BTN has a general sustainable finance framework but does not touch on forest sectors at all. Barring a requirement for Amdal, ESG risk management is not existent at this point. Few specific assessment factors such as 'reforestation' and 'development on degraded lands' are mentioned as favourable. The bank plans to begin integrating ESG issues into risk management and corporate governance from next year.

Policy status	Policy details	Implementation
Sustainable finance action plan	Environmental permits if required by local governments	Not relevant to land use activities

Compliance & governance	Requires Amdal, UKL-UPL and agricultural land permits
Forest & peatland protection	No such requirement for own operations and vendors or clients
Habitat conservation	No such requirement for own operations and vendors or clients
Community rights	No such requirement for clients
Labour rights	No such requirement for clients
Grievance management	No such requirement for clients
Supply chain transparency	No such requirement for clients

**None of these apply to the clients' suppliers or smallholders.*

PaninBank

Financier profile in numbers

Credit to palm oil as % of gross loans	5.98%	Percentage of total for Indonesian banks
Gross loans	$9.2bn	4.4%
Credit extended to palm oil sector	$0.553bn	9%
Capital raised for palm oil sector	-	-
Total funding provided to palm oil sector	$0.553bn	9%
Funding of 'bad actors' as percentage of total	100.0%	*Of top 2 high-risk* palm oil clients:* *-Sinar Mas* *-Jardine Matheson Group*

Gross loans as of 1Q'20; palm oil figures between 2016 and April 2020.
**Defined as companies that do not have NDPE policies or fall short on their implementation.*

Bank Panin, one of the two private banks in the Indonesian sample and one which was the first to start trading on the Jakarta Stock Exchange, has an ESG risk management system applied for credit approval, devised by an executive task force. Specific guidelines for palm oil — which accounts for just 1.2% of total financing, reassures the bank — apparently exist but there are very few details, except that ISPO or RSPO certified customers are given priority.

Policy status	Policy details	Implementation
Sustainable finance action plan and sector specific policies	Incentivises certification	Discloses financing amounts extended to high risk sectors but no other details

Compliance & governance	Requires Amdal	Does not list complete requirements for E&S assessment
Forest & peatland protection	No such requirement for own operations and vendors or clients	
Habitat conservation	No such requirement for own operations and vendors or clients	
Community rights	No such requirement for clients	
Labour rights	No such requirement for clients	
Grievance management	Includes forced and child labour in the exclusion list	Does not refer to labour laws and standards
Supply chain transparency	No such requirement for clients	

**None of these apply to the clients' suppliers or smallholders.*

- Sustainable lending portfolio: IDR21.75tn ($1.5tn) as of end-2020

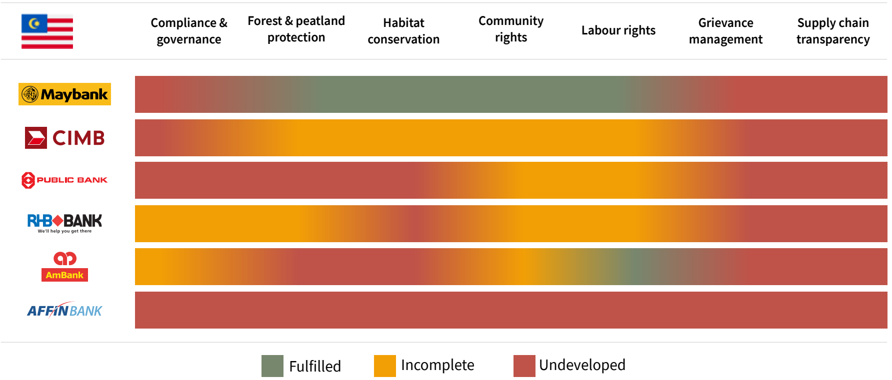
3.3.2 Malaysia

As already mentioned, the regulatory stance in Malaysia on sustainable finance is not yet forward enough since there are no specific or binding principles to follow. BNM's deferences to VBI, an industry effort meant originally only for Islamic financial institutions, have left banks with little choice but to use VBI's palm oil specific guidelines to create their own sector policies. Although the guidelines recommend full compliance with MSPO (and RSPO or other local certification schemes for clients operating outside of Malaysia), the document only covers upstream activities and does not provide a sufficient base for setting minimum sustainability standards. The newly released taxonomy promises to add clarity but may fall short of potential, once again, given its unenforceability.

Out of six local banks under review, four have developed palm oil specific policies in different stages of development. However, none discloses these policies in full. The rest make do with very few and very basic requirements that are only generally or partly relevant to palm oil and other forest-risk clients. Nobody measures or reports the forest footprint of their portfolio companies. Most have green financing schemes but those are focused around 'low carbon'/'climate resilience' themes and largely fail to account for the role of forest-linked sectors.

Because the guidelines are all optional in implementation, there are considerable variations between individual Malaysian banks on the breadth and scope of sustainability policies and their disclosure. Maybank and CIMB are the forerunners, while Public Bank — the third largest institution — trails far behind. Reporting though is a weak spot for all since at this time, as publicly traded companies, they have to comply only with the stock exchange requirements, and Bursa Malaysia asks for a fairly simple Sustainability Statement whose parts were adapted from the GRI.

Malaysian sample of banks: progress matrix on policies



Maybank

Financier profile in numbers

Credit to palm oil as % of gross loans	1.7%	Percentage of total for Malaysian banks
Gross loans	$120.3bn	33.5%
Credit extended to palm oil sector	$2.0bn	46%
Capital raised for palm oil sector	$0.997bn	56%
Total funding provided to palm oil sector	$3.0bn	49%
Funding of 'bad actors' as percentage of total	74.7%	*Of top 5 high-risk* palm oil clients:* *-Albukhary Group* *-Batu Kawan Group* *-Sinar Mas Group* *-Sime Darby Plantations* *-Triputra Group*

Gross loans as of 1Q'20; palm oil figures between 2016 and April 2020.
**Defined as companies that do not have NDPE policies or fall short on their implementation.*

The largest bank by assets in the country, Maybank took its time warming up to sustainability as an agenda. It drafted its first responsible lending guidelines in 2015 but incorporated them into risk management, with TCFD as the baseline, only three years later. It was also when initial risk acceptance criteria for palm oil were established, which last year were updated to cover the entire value supply chain including downstream activities, thus going beyond existing MSPO requirements. Not coincidentally, Maybank led the development of VBI's palm oil sector guide and is positively engaged with the sector players. But it is only now in the process of developing a comprehensive group-wide ESG risk framework.

Policy status	Policy details	Implementation
Sustainability strategy and sector specific policies	Enhanced lending criteria for palm oil (2018/updated 2020) and adoption of NDPE (2020)	No disclosure of policies or reporting on the assurance process

Maybank Group's newest five-year M25 strategy features sustainability as a strategic priority and is a major upgrade from its previous plan to 2020. The board and senior management have been accorded greater oversight duties over sustainability issues. The bank has committed to a long-term goal of reaching net zero carbon emissions — which includes portfolio companies — by 2050. And it has already made some early steps in that direction by adopting NDPE and no longer funding new coal projects. Still, among all high ESG risk sectors, its loan exposure to palm oil is the greatest.

Compliance & governance	Does not disclose details
Forest & peatland protection	Requires fulfillment of NDPE requirements
Habitat conservation	Requires fulfillment of NDPE requirements
Community rights	Requires fulfillment of NDPE requirements
Labour rights	Requires fulfillment of NDPE requirements
Grievance management	No such requirement for clients
Supply chain transparency	No such requirement for clients

**None of these seem to apply to the clients' suppliers.*

- Green financing facilities: over MYR7bn ($1.68mn) in 2020
- Sustainable finance commitment: MYR50bn ($12bn) by 2025

CIMB

Financier profile in numbers

Credit to palm oil as % of gross loans	1.14%	Percentage of total for Malaysian banks
Gross loans	$84.6bn	23.6%
Credit extended to palm oil sector	$0.968bn	22%
Capital raised for palm oil sector	$0.645bn	37%
Total funding provided to palm oil sector	$1.6bn	26%
Funding of 'bad actors' as percentage of total	80.4%	*Of top 5 high-risk* palm oil clients:* *-Batu Kawan Group* *-Sinar Mas Group* *-Johor Group* *-Sungai Budi Group* *-Sarawak Oil Palms*

Gross loans as of 1Q'20; palm oil figures between 2016 and April 2020.
**Defined as companies that do not have NDPE policies or fall short on their implementation.*

Another systemically important bank in the region, CIMB has been a recent frontrunner on sustainability among Malaysian candidates. It was the only ASEAN bank among the 28 founding members of PRB. It also signed on to PRB's Collective Commitment to Climate Action (CCCA). Climate action, in fact, has been the cornerstone of CIMB's sustainability initiatives, with other ESG facets appended almost as an afterthought. The Group has announced a phaseout of coal financing, the first by a Southeast Asian bank, by 2040.

Policy status	Policy details	Implementation
Sustainability strategy and sector specific policies	Sector guide for palm oil (2019) as part of the Group Sustainable Financing Policy	Does not disclose policies but provides summaries of enhanced due diligence cases

A sustainability roadmap of 2019 led to the formulation of the group-wide sustainable financing policy and sector guides, palm oil among them. The texts of the guides have not been made publicly available but, based on what can be gleaned from other transcripts, the palm oil standards appear to apply only to upstream companies, paralleling VBI's sector guide. According to its Forward23+ strategy, the bank plans to set sector-specific portfolio targets by 2023. Although CIMB is a participant in TCFD's pilot for banks and subscribes to the GRI, it does not fully disclose the results of its engagement with high-risk clients.

Compliance & governance	Does not disclose details	
Forest & peatland protection	Supports NDPE commitments	Does not require compliance with NDPE
Habitat conservation	Supports NDPE commitments	Does not require compliance with NDPE
Community rights	Supports NDPE commitments	Does not require compliance with NDPE
Labour rights	Supports NDPE commitments	Does not require compliance with NDPE
Grievance management	No such requirement for clients	Does not refer to labour laws and standards
Supply chain transparency	No such requirement for clients	

**None of these seem to apply to the clients' suppliers or smallholders.*

- Sustainability-linked loans disbursed: MYR1bn ($240mn) as of end-2020
- Sustainability-linked loans earmarked: MYR3bn ($720mn) to 2024

PUBLIC BANK

Financier profile in numbers

Credit to palm oil as % of gross loans	0.79%	Percentage of total for Malaysian banks
Gross loans	$77.4bn	21.6%
Credit extended to palm oil sector	$0.614bn	14%
Capital raised for palm oil sector	$0.001bn	0.035%
Total funding provided to palm oil sector	$0.615bn	10%
Funding of 'bad actors' as percentage of total	99.5%	*Of top 3 high-risk* palm oil clients:* *-Albukhary Group* *-NPC Resources Group* *-United Malacca Group*
Shares held in 'bad actors'	$223.1bn	*Split between 2 high-risk palm oil companies:* *-IOI Group* *-Sime Darby*

Gross loans as of 1Q'20; palm oil figures between 2016 and April 2020; shareholding as of April 2021.
**Defined as companies that do not have NDPE policies or fall short on their implementation.*

Although Public Bank is the third largest banking group in Malaysia by assets, it does not act in accordance with its position. It follows mostly outdated sustainability precepts that remind of the good old days of corporate social responsibility. Reporting on sustainability is limited to a brief statement in the annual report where topics like customer satisfaction and digital security outshine the theme of responsible lending. The bank is making early strides in the latter by having initiated the adoption of BNM's Climate Change and Principle-based Taxonomy guidelines. In addition, it has introduced an ESG based exclusion list: forest-risk relevant prohibitions include illegal logging, forced or child labour and violations of the rights of local communities. VBI principles are applied only to the group's Islamic subsidiary.

Policy status	Policy details	Implementation
Sustainability strategy	Basic ESG policies and standard ESG lending exclusion list	No reporting on the assurance process
Compliance & governance	Does not disclose details	Does not list complete requirements for E&S assessment
Forest & peatland protection	No such requirement for own operations and vendors or clients	
Habitat conservation	No such requirement for own operations and vendors or clients	
Community rights	Does not finance activities that violate the rights of local communities	Does not refer to FPIC or international standards
Labour rights	Lists forced and child labour in the exclusion list	Does not mention any other issues or applicable standards
Grievance management	No such requirement for clients	
Supply chain transparency	No such requirement for clients	

**None of these seem to apply to the clients' suppliers or smallholders.*

- Green lending approved: MYR17.2mn ($4.3mn) as of end-2020

RHB BANK
We'll help you get there

Financier profile in numbers

Credit to palm oil as % of gross loans	0.84%	Percentage of total for Malaysian banks
Gross loans	$41.0bn	11.4%
Credit extended to palm oil sector	$0.344bn	8%
Capital raised for palm oil sector	$0.057bn	3%
Total funding provided to palm oil sector	$0.401bn	6%
Funding of 'bad actors' as percentage of total	72.6%	*Of top 4 high-risk* palm oil clients:* *-Johor Group* *-TH Group* *-Wilmar* *-TSH Resources*

Gross loans as of 1Q'20; palm oil figures between 2016 and April 2020.
**Defined as companies that do not have NDPE policies or fall short on their implementation.*

RHB Bank is a relative newcomer to responsible banking whose sustainability framework was set up in 2019 as part of its medium-term FIT22 strategy. Along with an enhanced sustainability governance structure, the bank developed additional risk assessment criteria for palm oil and few ESG sensitive sectors. These criteria — which implicitly, although incompletely, conform to NDPE — have not yet been rolled out group-wide; for example, the Indonesian subsidiary which focuses on investment banking has not committed. Plantation owners are required to obtain a certification either from MSPO or RSPO/ISPO if operations are regional. Smallholders are assessed based on their adherence to the Malaysian Palm Oil Board's (MPOB) Codes of Good Practice, as are palm oil refiners. As far as smallholders are concerned, this may be a sensible decision given MSPO's low coverage of them; millers, on the other hand, should rightly be made to comply with proper certification schemes. Although ESG issues have been recognised and integrated into the conventional risk management system, the group is yet to start reporting on the practice — which makes it impossible to gauge the sustainability strategy's success rate.

Policy status	Policy details	Implementation
Sustainability strategy and sector specific requirements	Requires national and/or international certification for plantations	No reporting on the assurance process

Compliance & governance	Requires MSPO/RSPO/ISPO for plantations and implementation of MPOB for smallholders and refiners	
Forest & peatland protection	Expects clients to avoid virgin forest and peatlands	Does not explicitly mention deforestation or burning
Habitat conservation	No such requirement for own operations and vendors or clients	
Community rights	Asks clients to avoid aboriginal or heritage land	Does not refer to FPIC or international standards
Labour rights	Lists forced and child labour in the exclusion list	Does not mention any other issues or applicable standards
Grievance management	No such requirement for clients	
Supply chain transparency	No such requirement for clients	

**None of these seem to apply to the clients' suppliers or smallholders.*

- Green lending and fundraising issued: MYR3.1bn ($775mn) as of end-2020
- Green lending and fundraising commitment: MYR5bn ($1.3bn) by 2025

AmBank

Financier profile in numbers

Credit to palm oil as % of gross loans	1.2%	Percentage of total for Malaysian banks
Gross loans	$25.1bn	7.0%
Credit extended to palm oil sector	$0.3bn	7%
Capital raised for palm oil sector	$0.031bn	2%
Total funding provided to palm oil sector	$0.331bn	5%
Funding of 'bad actors' as percentage of total	59.0%	*Of top 3 high-risk* palm oil clients:* *-MP Evans* *-Sarawak Oil Palms* *-Ta Ann Holdings*

Gross loans as of 1Q'20; palm oil figures between 2016 and April 2020.
**Defined as companies that do not have NDPE policies or fall short on their implementation.*

AmBank is a rather undistinguished local banking institution but has made some progress on sustainability. Its Focus 8 Strategy 2021-2024 has integration of ESG considerations, including VBI principles, into business as one of the strategic tasks. Like other major banks in Malaysia, AmBank is an active participant in BNM-SC's Joint Climate Change Committee and has just started classifying new loans based on the Climate Change and Principle-based Taxonomy. It has developed its own green financing taxonomy for several sectors; one of them is palm oil. The trouble with these policies is that no particulars have been disclosed whatsoever.

Policy status	Policy details	Implementation
Sustainability strategy and sector specific requirements	Defines basic ES requirements but provides no policy details for specific sectors	No reporting on the assurance process

Compliance & governance	Requires essential environmental, health and safety permits	Does not mention relevant certifications
Forest & peatland protection	No such requirement for own operations and vendors or clients	
Habitat conservation	No such requirement for own operations and vendors or clients	
Community rights	Stipulates that operations must not affect local and indigenous communities	Does not refer to FPIC or international standards
Labour rights	Demands compliance with local and international labour laws	
Grievance management	No such requirement for clients	
Supply chain transparency	No such requirement for clients	

**None of these seem to apply to the clients' suppliers or smallholders.*

AFFIN BANK

Financier profile in numbers

Credit to palm oil as % of gross loans	1.4%	Percentage of total for Malaysian banks
Gross loans	$10.6bn	2.9%
Credit extended to palm oil sector	$0.148bn	3%
Capital raised for palm oil sector	$0.036bn	2%
Total funding provided to palm oil sector	$0.184bn	3%
Funding of 'bad actors' as percentage of total	99.9%	*Of top 4 high-risk* palm oil clients:* *-Puncak Niaga Holdings* *-Kwantas Group* *-Boustead Group* *-Rimbunan Hijau Group*

Gross loans as of 1Q'20; palm oil figures between 2016 and April 2020.
**Defined as companies that do not have NDPE policies or fall short on their implementation.*

Affin Bank, which sits just outside the Malaysian top ten size wise, has been lagging even behind the laggards of the sample group. Its sustainability statement is diluted with non-ESG matters, while responsible financial services do not rank highly on the materiality index. The bank claims to be developing ESG lending criteria but provides no timeline as to their release. At present, it is only the group's insurance and investment banking subsidiaries that appear to apply at least basic ESG principles.

Policy status	Policy details	Implementation
Sustainability roadmap	No ESG policies developed	Not applicable

Compliance & governance	Does not disclose details
Forest & peatland protection	No such requirement for own operations and vendors or clients
Habitat conservation	No such requirement for own operations and vendors or clients
Community rights	No such requirement for clients
Labour rights	No such requirement for clients
Grievance management	No such requirement for clients
Supply chain transparency	No such requirement for clients

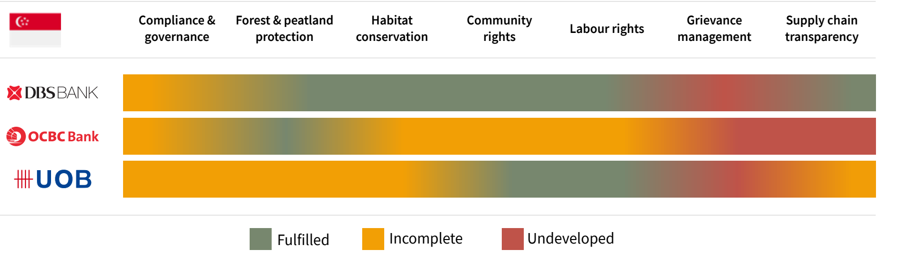
3.3.3 Singapore

For such a small place, Singapore is home to Southeast Asia's largest banks and exercises an outsized influence on regional banking dynamics. The island's well-managed banks have developed rather progressive ESG risk management policies, and financial policymaking is making headway. The initial guidance on responsible financing developed by the industry has now been supplemented by the regulator's formal instruction on environmental risk management. Most financial institutions will not need to make much effort to comply seeing their competence, at least their comparative competence over regional peers, in sustainable performance.

The three banks in this review all have overall and forest-sector specific financing and investment policies in place. DBS is in the lead, and UOB together with OCBC are following in its footsteps. In addition to ESG risk management guidelines, the banks also follow green and sustainability-linked loan principles. With no protectionist sentiments over forest sectors to worry about, these Singaporean banks seem to be allocating their sustainable finance commitments more evenly between energy and agriculture.

Sustainability as a strategy is overseen by a robust governance structure involving simultaneously the board and the executives at various levels. ESG training is established and common. However, reporting — as mandated by the Singapore Exchange's basic listing rules on sustainability disclosure — misses a lot of essential information, despite adaptations from GRI, TFCD and others.

Singaporean sample of banks: progress matrix on policies



DBS BANK

Financier profile in numbers

Credit to palm oil as % of gross loans	0.36%	Percentage of total for Singaporean banks
Gross loans	$268.5bn	40.5%
Credit extended to palm oil sector	$0.956bn	33%
Capital raised for palm oil sector	$0.046bn	27%
Total funding provided to palm oil sector	$1.0bn	33%
Funding of 'bad actors' as percentage of total	59.1%	*Of top 3 high-risk palm oil clients:* *-Salim Group* *-Wilmar* *-Harita Group*

Gross loans as of 1Q'20; palm oil figures between 2016 and April 2020.
**Defined as companies that do not have NDPE policies or fall short on their implementation.*

The largest bank in the region, originally government established, DBS practices the Basel committee's three lines of defence in risk management, which includes ESG. Routine assessments for credit applicants are followed by additional evaluation for sensitive cases as well as periodic audit of the entire due diligence process. At its most basic level, ESG issues have been incorporated into the group's credit risk policy. The more granular responsible financing standard is reviewed annually and contains nine sector guides. The bank even introduced its own categorisation framework for sustainable finance activities in 2020, thus preceding the proposed taxonomy by MAS.

Policy status	Policy details	Implementation
Sustainability strategy and sector specific requirements	Requires NDPE and RSPO compliance for all clients and their suppliers	Regular or event-triggered monitoring but limited reporting

The palm oil guide, whose full text is not publicly available, is said to be aligned with both NDPE and RSPO for all players along the supply chain excluding smallholders. Monitoring purports to be diligent but reporting is inadequate (which DBS admits and explains by its adherence to financial privacy laws) because the issues prompting engagement and their resolution are not disclosed.

Compliance & governance	Requires fulfillment of local or national laws	Does not name licences or permits required
Forest & peatland protection	Requires compliance with NDPE and RSPO	
Habitat conservation	Requires compliance with NDPE and RSPO	
Community rights	Requires compliance with NDPE and RSPO	
Labour rights	Excludes companies involved in forced or child labour and other abuses	
Grievance management	No such requirement for clients	
Supply chain transparency	Encourages product traceability and full applicability of NDPE	

**Requirements to comply with NDPE and RSPO do not apply to smallholders.*

- Sustainable financing transactions: S$9.6bn ($7.3bn) in 2020
- Sustainable bonds raised: S$9.7bn ($7.4bn) in 2020
- Sustainable finance commitment: S$50bn ($38bn) by 2024

OCBC Bank

Financier profile in numbers

Credit to palm oil as % of gross loans	0.84%	Percentage of total for Singaporean banks
Gross loans	$196.2bn	29.6%
Credit extended to palm oil sector	$1.7bn	57%
Capital raised for palm oil sector	$0.123bn	71%
Total funding provided to palm oil sector	$1.8bn	58%
Funding of 'bad actors' as percentage of total	70.8%	*To top 5 high-risk palm oil clients:* *-Austindo Group* *-Sime Darby Plantations* *-Triputra Group* *-Jardine Matheson Group* *-Wilmar*
Shares held in 'bad actors'	$219.8bn	*Of top 3 high-risk palm oil clients:* *-Salim Group* *-Wilmar* *-Harita Group*

Gross loans as of 1Q'20; palm oil figures between 2016 and April 2020; shareholding as of April 2021.
**Defined as companies that do not have NDPE policies or fall short on their implementation.*

The oldest bank in Singapore and second by asset size, OCBC finds itself considerably behind DBS on sustainability. Although ESG considerations have been instilled in the risk management process following the three lines of defence model, the bank reveals very little of its overall or sector specific financing policies. (Palm oil falls under its agriculture and forestry policies.) The same applies to its illusive responsible investing policy. The sustainability report provides scanty information but some details have been divulged elsewhere.

Policy status	Policy details	Implementation
Sustainability framework and sector specific requirements	Few details of adopted ESG policies	Limited reporting on monitoring results

In the guide for agriculture and forestry, OCBC references some elements of NDPE, RSPO, the ABS Haze Diagnostics Kit and the Equator Principles. Green financing products are heavily geared towards small and medium enterprises for sustainable activities in several categories including natural resources and land use.

Compliance & governance	Requires clients to fulfil local pollution prevention laws	Does not refer to any other law or regulations
Forest & peatland protection	Prohibits deforestation, open burning and peat development	
Habitat conservation	Requires borrowers to preserve HCV areas	Does mention HCS areas
Community rights	Considers 'resettlement of affected communities'	Does not discuss the rights of local or indigenous communities
Labour rights	Excludes companies involved in forced or child labour	Does not seemingly outlaw forced or child labour unless deemed 'harmful'
Grievance management	No such requirement for clients	
Supply chain transparency	No such requirement for clients	

**None of these seem to apply to the clients' suppliers or smallholders.*

- Sustainable finance portfolio: S$10b ($7.6bn) as of end-2020
- Green lending commitment: S$25b ($19bn) by 2025

UOB

Financier profile in numbers

Credit to palm oil as % of gross loans	0.14%	Percentage of total for Singaporean banks
Gross loans	$199.0bn	30.0%
Credit extended to palm oil sector	$0.269bn	9%
Capital raised for palm oil sector	$0.004bn	2%
Total funding provided to palm oil sector	$0.273bn	9%
Funding of 'bad actors' as percentage of total	82.3%	*To top 4 high-risk palm oil clients:* *-Wilmar* *-Harita Group* *-Sungai Budi Group* *-Jardine Matheson Group*

Gross loans as of 1Q'20; palm oil figures between 2016 and April 2020.
**Defined as companies that do not have NDPE policies or fall short on their implementation.*

UOB is another local stalwart of a bank. Its sustainable finance frameworks cover trade finance, smart city, real estate and circular economy. A sector guidance for palm oil was released in August. Few relevant issues such as deforestation and burning are mentioned in the prohibition list, while the guiding principles for financing have been borrowed from the ABS. UOB, however, takes a soft stance on proper certification by 'recommending', but not requiring, RSPO and NDPE. As with other banks, ESG risk considerations, monitoring and non-compliance procedures have been outlined but the disclosure of assurance results is partial.

Policy status	Policy details	Implementation
Sustainability frameworks for specific sectors	Requires local compliance, encourages international certification	Discloses the number of borrowers with ESG issues but no further details

Unlike its regional peers though, UOB has uniquely stopped funding 'greenfield' plantation projects. It does not mean, however, that the bank is pulling out of palm oil altogether. Sustainable land use is mentioned among priority sectors for responsible financing opportunities, and one of its major sustainability-linked loans in 2020 was disbursed to Wilmar International, an Asian agribusiness group.

Compliance & governance	Requires compliance with local regulations	Does not insist on compliance with RSPO and/or NDPE
Forest & peatland protection	Prohibits open burning	Does not compel borrowers to commit to zero deforestation or development on peatland
Habitat conservation	Requires protection of HCV forests	Does not mention HCS areas
Community rights	Prohibits companies involved in violation of the rights of local peoples	
Labour rights	Excludes companies involved in exploitation of labour as per ILO rules	
Grievance management	No such requirement for clients	
Supply chain transparency	Advises borrowers to improve traceability in their supply chains	

**None of these seem to apply to smallholders except in the case of open burning.*

- Sustainable financing extended: S$11bn ($8.4bn) as of end-2020
- Sustainable financing commitment: S$15bn ($11.4bn) by 2023

Banking for Palm Oil

3.4 Links to bad actors

Although there is absolutely a large population of palm oil companies that are implicated in negative social and environmental issues, we must resist the temptation to paint all businesses with the same brush for fear of doing a disservice to the sector by ignoring its genuine efforts at reform. But having ascertained the banks' level of exposure to palm oil, the next logical step would be to identify their explicit links to bad actors.

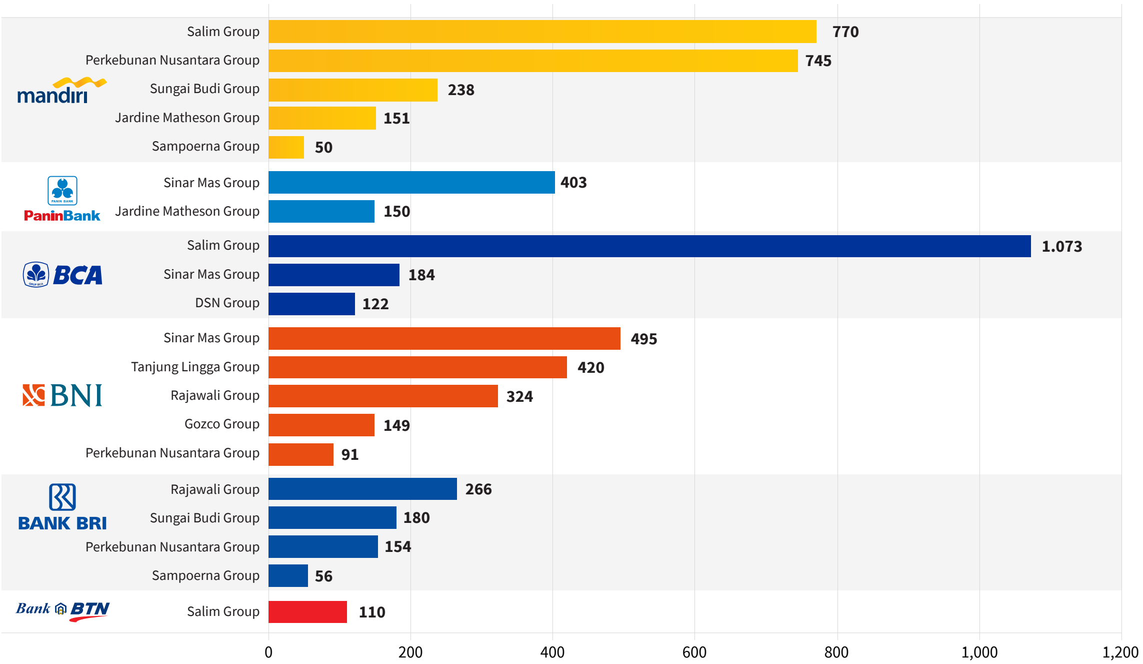
This task, once again, is far from straightforward and requires assembling bits and pieces of information from a number of sources, most of which specialise in forest research. Forests & Finance — that has been used above to extract palm oil financing and underwriting data — also provides a useful snapshot of forest-risk companies which banks have done business with. These are the businesses who have either appeared in the media for the wrong reasons or received grievances through RSPO.

Bad actors in forest sectors often come along with offenses on the entire ESG spectrum. Biodiversity loss, climate change, diminished access to clean water and pollution are some of the direct consequences of tropical deforestation and degradation. Social risks include displacement and violation of the rights of local communities, land conflicts, labour exploitation and health hazards of transboundary haze. Bribery, illegal operations, tax evasion and reputational damage are among common governance issues.

Company profiles below and details of their ESG issues have been extracted from dedicated palm oil sections of databases BankTrack and SPOTT which compile projects deemed damaging to the environment or society. For consistency, the scope of the search is limited to palm oil groups headquartered and/or primarily operating in Indonesia and Malaysia. **By continuing to deal with these offenders, banks undermine their public sustainability commitments and contravene their own responsible financing policies.**

Indonesian sample banks' funding of top 'bad actors' in palm oil

2016-Apr 2020, $mn



Source: Forests & Finance

As the most active group of palm oil financiers in the region (and beyond), Indonesian banks carry the most exposure — averaging over 80% of their sector-specific credit facilities and underwriting services — to high-risk clients in absolute terms. The largest funding amounts have been extended to a pair of Indonesian conglomerates, Salim Group and Sinar Mas Group, which each feature a long record of environmental and social transgressions.

They are also typical specimens of a distinctively Southeast Asian breed of family-run enterprises. While often recognised as powerful drivers of economic growth, these companies possess a unique ability to evade government regulation and supervision. At the same time, they are strong lobbyists whose efforts in Indonesia have culminated in the omnibus bill that loosens ESG restrictions around food, agriculture and land use.

Steep slope clearing
Image by **Aidenvironment**

Salim Group, Indonesia

Profile

Indonesia's biggest conglomerate, Salim Group holds a majority stake in Jakarta listed Indofood Sukses Makmur (Indofood) which, in turn, owns the second largest oil palm land bank in the country through subsidiary Indofood Agri Resources.

Issues

Despite their size and prominence, neither Indofood nor its parent have committed to NDPE or addressed persistent labour rights violations and deforestation offences — most notably at London Sumatra, a related entity whose RSPO membership was terminated in 2019.

Financial links

Sample financiers materially exposed to Salim Group include Indonesia's BCA ($1.07bn), Bank Mandiri ($770mn) and BTN ($110mn), as well as Singapore's DBS ($413mn).

Sinar Mas, Indonesia

Profile

Sinar Mas is a large Indonesian conglomerate that operates oil palm — through Golden Agri Resources (GAR), among others — and pulpwood plantations.

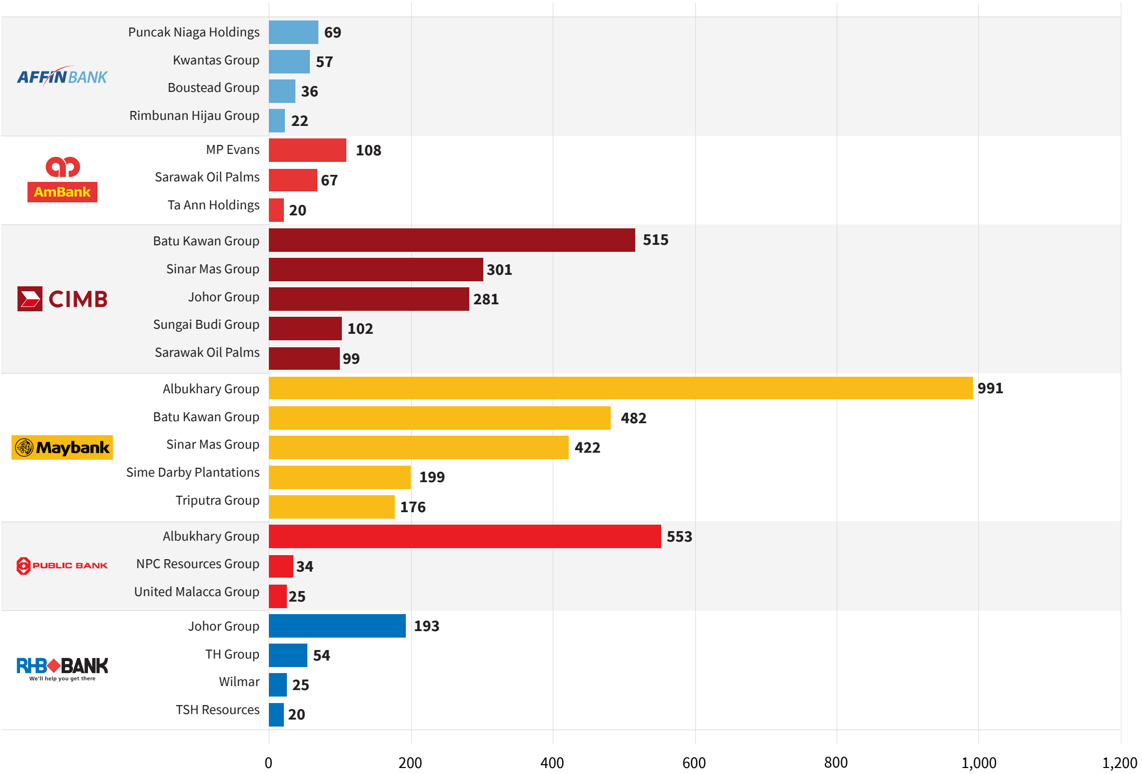
Issues

The group's obscure governance structure has allowed it to get away with scores of community conflicts, rights violations and land clearing events. GAR, along with other subsidiaries, has been implicated in deforestation, biodiversity loss and peatland destruction. The newest complaint against it to RSPO is currently under investigation.

Financial links

Sample financiers materially exposed to Sinar Mas include Indonesia's BNI ($495mn), Bank Panin ($403mn) and BCA ($184mn), Malaysia's Maybank ($422mn) and CIMB ($301mn), as well as Singaporean OCBC ($109mn).

Malaysian sample banks' funding of top 'bad actors' in palm oil
2016-Apr 2020, $mn



Source: Forests & Finance

Malaysia has its own fair share of tycoon capitalists who have been running legacy conglomerates with profitable plantation businesses. A prime example is the Albukhary Group whose Tradewinds Corporation has a subsidiary producing palm oil and rubber with one of the largest operations in the country. Previously a public company and an RSPO member, Tradewinds Plantation ceased being either in 2013 and 2015 respectively, which has resulted, not unintentionally, in much less oversight over its sustainability performance. Multiple reports of illegal appropriation of indigenous lands have been brushed away and ignored by law enforcers and financiers alike.

On the other end of the spectrum are government-linked corporations owned by various state agencies. Their status, peculiarly, also makes it easier for them to skirt the rules. State governments and monarchs maintain an impervious hold over forests and lands in their respective territories and feature heavily as owners of palm growers, most of whom do not subscribe to NDPE policies. For instance, Johor Corporation's oil palm plantation operator Kulim has been an RSPO member since 2004 but formally acceded to NDPE only in 2018, possibly following accusations of unsustainable production practices and a divestment by Norway's sovereign wealth fund.

SARAWAK OIL PALMS BERHAD
GROUP OF COMPANIES

Sarawak Oil Palms, Indonesia

Profile

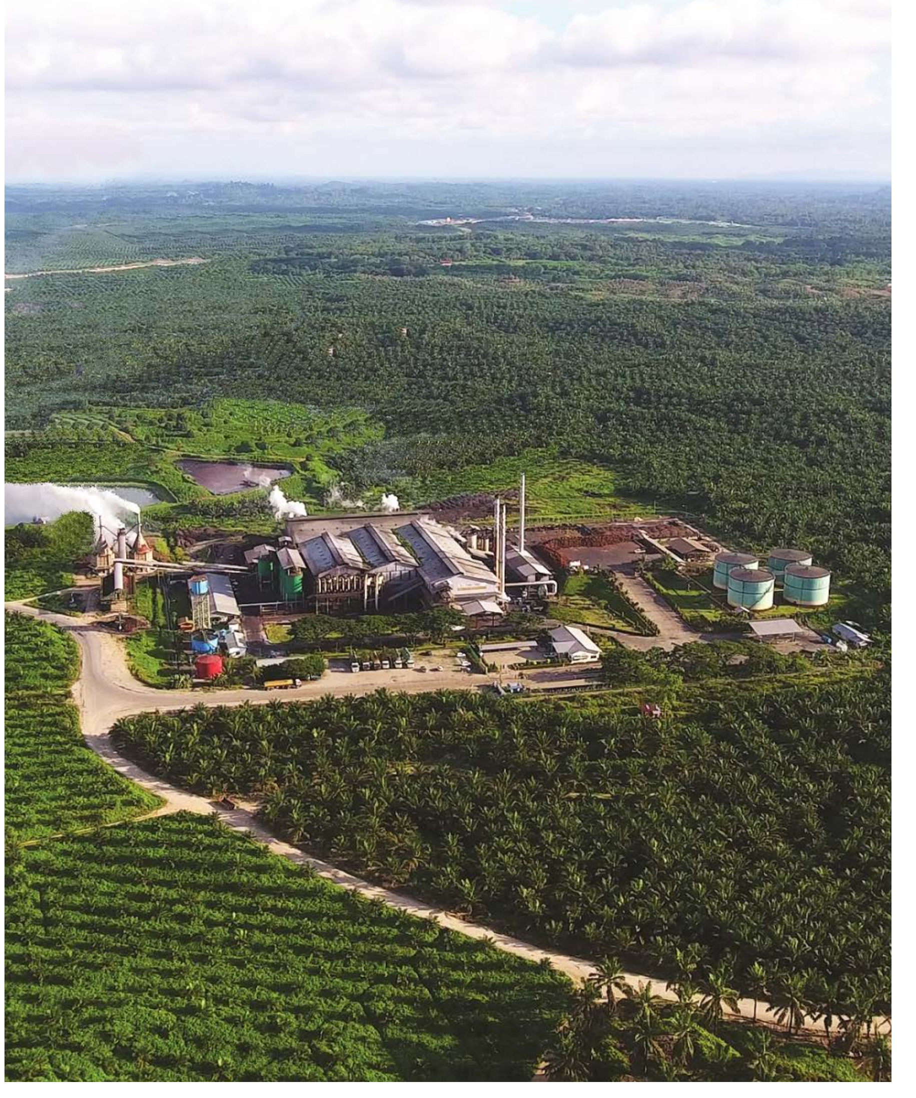
Sarawak Oil Palms is jointly owned by a family-run conglomerate Shin Yang Plantations (35%) and the Sarawak State Government (28%).

Issues

Non-RSPO member Sarawak Oil Palms has been repeatedly flagged by environmental groups for its association with deforesting suppliers in violation of its NDPE policies. The key shareholder Shin Yang Group, in turn, has been implicated in a number of land conflicts with indigenous groups in its home state of Sarawak on Borneo.

Financial links

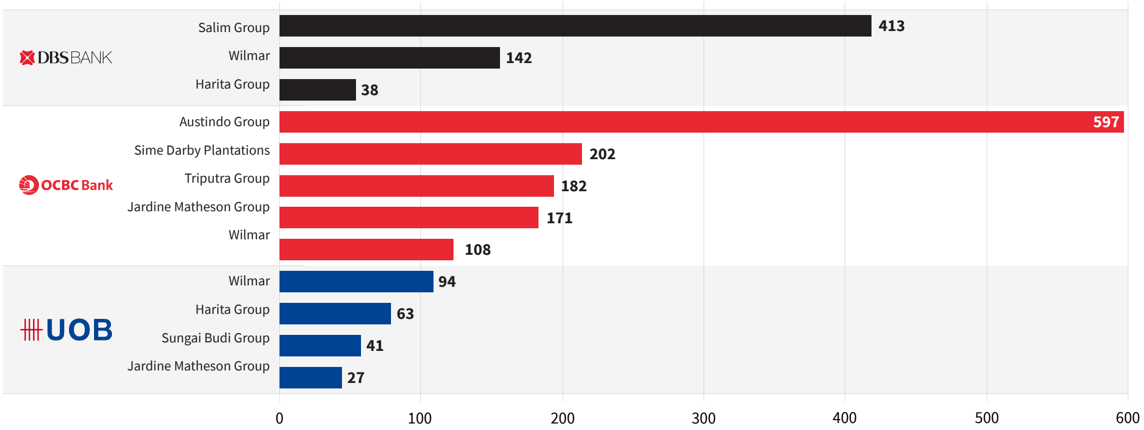
Sample financiers materially exposed to Sinar Mas include Malaysia's CIMB ($99mn) and AmBank ($67mn).



Milling buildings
Image by **Sarawak Oil Palms, www.sop.com.my/business-divisions/milling/milling-overview/**

Soil erosion as an impact of monoculture plantation
Image by **Aidenvironment**

Singaporean sample banks' funding of top 'bad actors' in palm oil
2016-Apr 2020, $mn



Source: Forests & Finance

Attempts at dissociating from palm oil notwithstanding, Singaporean banks are still exposed to the bad seeds of the sector. There is a degree of commonality among these palm oil companies: they are mostly large publicly traded entities. Sime Darby of Malaysia and Hong Kong based Jardine Matheson — whose Indonesian palm oil growing subsidiary Astra Agro Lestari is also listed — are examples. This speaks of Singaporean financiers' predilection for clients with open and acceptable public faces, from whom investors tend to expect more in terms of governance and sustainability as compared to their private counterparts.

In the case of palm oil, however, it is fairly hard to avoid controversy. Sime Darby Plantation, the largest listed company of its kind, has been embroiled in a number of land disputes with local communities and labour law violations in both Southeast Asia and West Africa. The same goes for Astra Agro Lestari whose record is tainted with land grabbing and other contraventions of NDPE. Partly it is a question of who holds the shares. For Sime Darby Plantation, it is Malaysian government entities who are naturally tolerant to malefactions in the palm oil sector. For nominally listed (with only 10% of shares floated) Austindo Nusantara Jaya, another palm oil business with financial ties to Singapore, it is domestic (family-related) companies and individuals who too put up comfortably with low standards.

Wilmar, Singapore

Profile

Wilmar International, listed on Singapore Stock Exchange, is the world's largest palm oil trader.

Issues

Although a subscriber to NDPE since 2014, Wilmar has been involved in deforestation, land disputes and poor labour practices through its subsidiaries. A 2018 Greenpeace report uncovered the group's evident connection to KPN Plantation (previously GAMA), a notorious deforester in Indonesia.

Financial links

Sample financiers materially exposed to Wilmar include Singapore's DBS ($145mn), OCBC ($108mn) and UOB ($94mn); smaller positions are held by Malaysian RHB Bank and Indonesia's BRI and Bank Mandiri.

Palm oil fruit
Image by tristantan, Pixabay

Conclusion

On balance, under growing pressure to do more, the finance industry is turning noticeably more committed to sustainable financing. Southeast Asian banks, whose exposure to forest-risk sectors is among the highest in the world, are progressing too — on paper, at least. But their attitudes are shaped significantly by local political sensibilities and specific governance structures, which do not intrinsically advance social and environmental causes.

Given the importance of palm oil for the regional economy, most banks have acknowledged the heightened risks the commodity carries and are trying to manage these risks. Financiers should be assessing palm oil (and other forest) clients against a range of defined criteria. To summarise, the existing policies of Southeast Asian banks address ESG issues, as organised by SPOTT, to varying degrees:

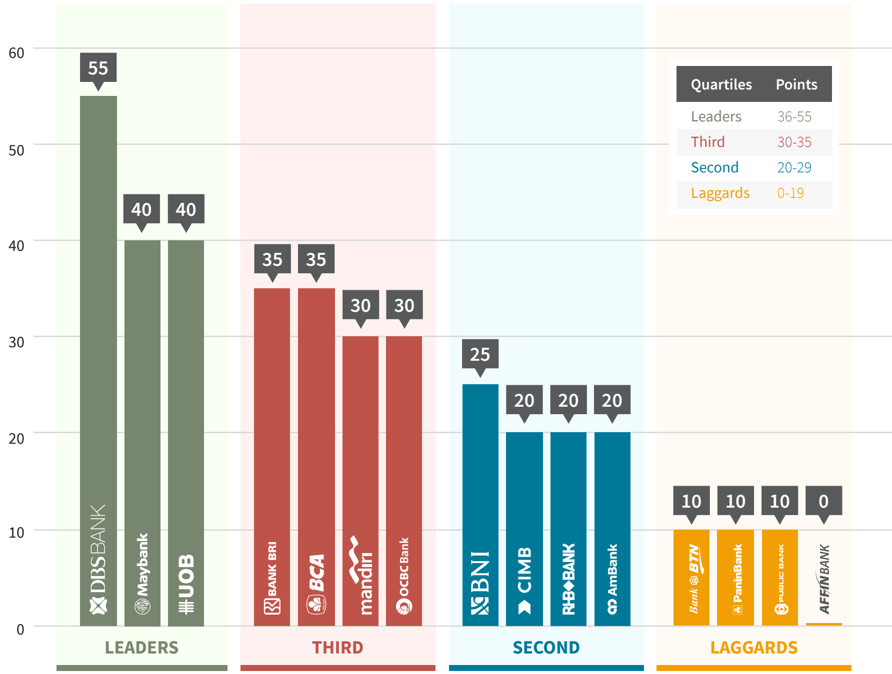
Palm oil fruit
Image by **Orientierungslust, Pixabay**

ESG risk acceptance criterion	Overall level of undertaking by sample banks
Sustainability policy & leadership	High
Landbank, maps & traceability	Low/Nil
Certification standards	High
Deforestation & biodiversity	Medium
HCV, HCS & impact assessments	Medium/Low
Peat, fire & GHG emissions	Medium/Low
Water, chemicals & pest management	Low
Community, land & labour rights	Medium/Low
Smallholders & suppliers	Low/Nil
Governance & grievances	Nil

While policies are being crafted more actively than before, sector specific documents are not usually made publicly available, at least not for forestry and land use. What can be picked up from limited disclosure suggests a work-in-progress. Probably the most complete coverage is seen in certification standards as banks tend to depend on them to do the hard work of verifying and tracking the companies' conformity with ESG requirements.

In contrast, not all banks explicitly mention even the foundational tenets which make up NDPE. Unqualified calls for the protection of tropical forests and peatlands and the rights of local communities (especially using formal terms such as HCV, HCS and FPIC) are still few and far between. Some other topics — like smallholders, third-party supply chain, grievances — are hardly covered at all. No bank measures or publishes its forest footprint.

Banks ranked by progress on forest-sector policies



So improving policies is imperative. But that will be the easy, conceptual, part of the task. **The more complicated exercise is ensuring they are all properly and fully implemented, which banks have struggled with.** This calls for a rethink of strategies and a shift of efforts from reaction to prevention. For one, NDPE must become a requirement, not an option, for all clients. It ought to be recognised that engagement as the principal pathway is not working and does not forward the sustainable financing agenda for the sector.

Policies, once established, have to be converted into internal procedures. This is another area at an early stage of development. Risk management incorporating ESG may be present but putting it into effect at branch level is problematic.

Is there hope that implementation will improve materially? **There is a modest case for optimism, with some fine-tuning to experiments that are afoot.** To start with, it is essential that forests and biodiversity start being treated on par with climate issues which currently dominate. Conditional finance in the form of sustainability-linked products should be extended to projects averting forest clearance as well as restoring ecosystems. By thus incentivising companies to meet anti-deforestation criteria, banks will be attracting flows from the growing pool of natural capital investors.

Better enforcement could mean going against the grain, bypassing certain practices of traditional customer relations. Client confidentiality, notably, is a major hurdle to transparent reporting. However, it turns out that revealing lending relationships when necessary is both technically and legally plausible. HSBC's practice of securing client consent for disclosure prior to initiating a transaction could be adopted as a model for high risk businesses.

Crucially, it is economically sensible that banks should collaborate and align their forest-risk policies to a **shared standard** in order to split the costs and due diligence expertise. It could contribute to scaling sustainable finance for soft commodities and eventually even galvanise global systemic support for NDPE compliance across commodities. Indeed, there are plenty of sensible recommendations to follow; the will to act on them is a rarer asset to come by.