Compendium of Key Takeaways
2021 Virtual Dialogue Series

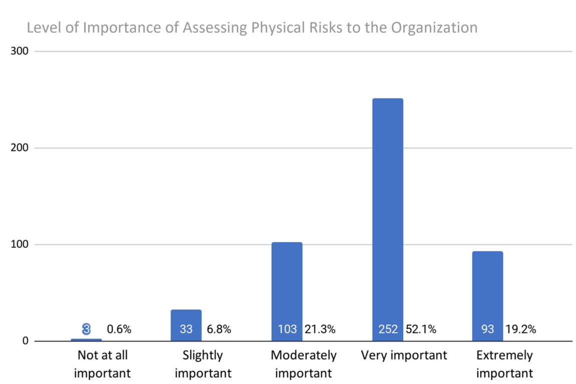
The Greening the Banks (GTB) initiative, led by Allotrope Partners, has collaborated with the Bangko Sentral ng Pilipinas or BSP (Philippine Central Bank) throughout 2021 to design and host a four-part dialogue series covering relevant topics requested by Philippine stakeholders, including **climate-related physical and transition risks**, **green finance challenges and opportunities**, as well as a **self-assessment and capacity building for BSP Working Groups**.

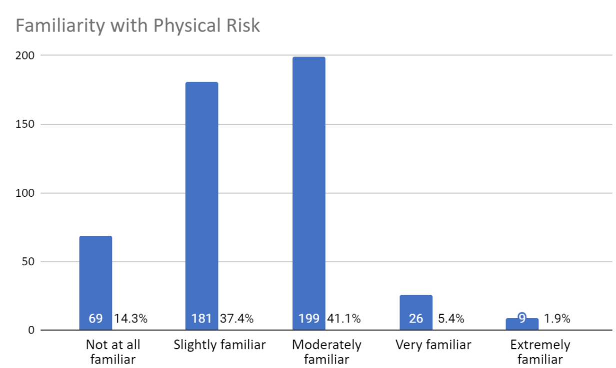
Through this webinar series, Greening the Banks engaged over **650 participants** representing more than 160 commercial, rural, cooperative, and local banks across the Philippines, together with BSP personnel and management, and other energy and finance market stakeholders. Throughout these virtual dialogues, the GTB team received extremely positive feedback from banks and developers, and participants requested further GTB support to move these discussions forward in 2021 and beyond.

This document summarizes the key takeaways from these four GTB convenings.

<u>Physical Risks for Rural and Community Banks:</u>

GTB's virtual dialogue on **physical risk assessment** for rural and community banks was aimed at strengthening the capacity of banks to identify and assess physical risks through bank-to-bank exchange. More than 400 financial leaders representing 130 rural banks, savings and loan associations, and cooperative banks from across the Philippines attended the session. A poll of participants indicated that while over two-thirds of rural and community bankers expressed it is *very important* to assess physical risks, more than half of Philippine bankers were *slightly familiar* or *not at all familiar* with how to proceed.

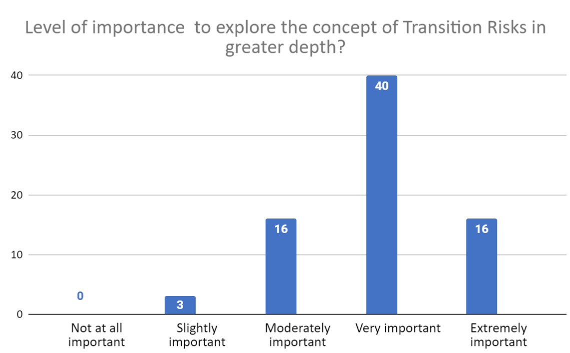


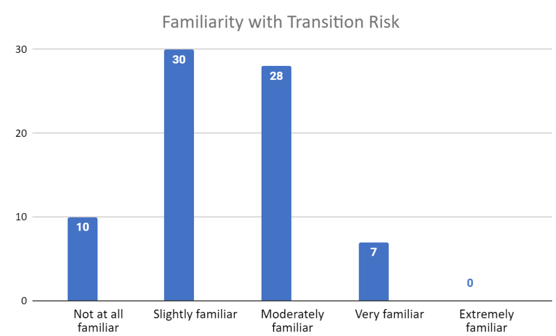


Key takeaways from the physical risk dialogue include:

- The Philippines is highly vulnerable to extreme weather events and local banks are not impervious to the effects of these natural disasters. Extreme weather events negatively affect banks' loan growth and deposit growth, especially for rural and cooperative banks. **There is an urgent need to increase banks' familiarity with climate-related physical risks, build capacity on how to assess these risks, and integrate physical risks into risk management frameworks.**
- Effectively managing physical risks **can create opportunities for banks** to gain important business and reputational benefits, access better financing and international markets, and improve relationships with regulators, clients, and other stakeholders.
- **Free online tools** are available to assess the vulnerability of a bank and its clients' assets to natural disasters and climate change. Examples currently being used by leading Philippine banks include:
    - **Adverse effects of drought, flooding, landslides, or storm surge:** http://noah.up.edu.ph/#/; https://hazardhunter.georisk.gov.ph/
    - **Adverse effects of sea level rise:** https://coastal.climatecentral.org/map
    - **Adverse effects of typhoons or heavy rains:** https://hazardhunter.georisk.gov.ph/

<u>Transition Risks for Commercial Banks</u>:
Continuing to dive into climate-related risks, GTB led a focused discussion on **transition risks** with Philippine commercial and universal banks. Session participants indicated that exploring transition risks is *very important* to their bank. However, more than half of participating bankers from commercial banks were only *slightly familiar* or *not at all familiar* with transition risks, with another 37% being only *moderately familiar*.





Key takeaways from the transition risk dialogue include:

- As countries shift towards greener economic solutions, transitions can result in carbon-intensive sectors having decreased assets (including stranded assets) and increased costs of doing business. **Exposure to assets with high transition risks can increase a bank's exposure to potential defaults.**
- Certain sectors that Philippine banks lend to face greater transition risks from the shift to a low-carbon economy than others. In addition to exposure to the **power sector**, of which the Philippine banks have a 9.6% direct loan exposure, other sectors with high transition risks include: **Mining, Oil & Gas, Steel & Metal Manufacturing, Automotive, Agriculture, Chemicals, Logistics, Real Estate, Shipping, and Aviation.** The Logistics sector, including trucking businesses, was specifically identified to be affected in the medium term, due to advances in technology.
- Even if a bank has no direct exposure to the fossil fuel industry, **the energy transition is systemic in nature and is likely to trigger chain reactions** that can positively or negatively impact the performance and viability of various loan and investment portfolios.
- The low-carbon transition also presents **opportunities for banks** to offer guidance to clients exposed to carbon-intensive sectors; structure innovative financial products, like transition bonds; provide finance restructuring, risk sharing facilities, and guarantee facilities; and support the overall greening of their clients' assets.
- **Banks can take steps to implement transition risk mitigation strategies now.** Key steps include:
    1. Fact Finding: Identifying the bank's exposure to climate risk
    2. Internal capacity building on climate awareness
    3. Dialogue with key clients on sustainability as early as possible
- **The international community can also take steps to support the Philippines banking sector in mitigating transition risks.** Key steps include:
    1. Increase international collaboration through partnerships and financial instruments that address transition risks.
    2. Leverage Official Development Assistance (ODA) capital to support the shift of assets that are vulnerable to transition risks toward low-carbon assets.
    3. Enhance cooperation between multilateral development banks, government, and financial market stakeholders to promote climate finance and introduce financial products, such as guaranties or risk sharing facilities, to mobilize finance in support of the clean energy transition.
- As with physical risks, **properly managing transition risks can provide brand and reputational advantages, as well as economic benefits, for banks of all sizes.**

<u>Assessing Opportunities for Financing RE in the Philippines</u>:
GTB also led a virtual dialogue on assessing **opportunities for financing the renewable energy (RE)** ambition of the Philippines, together with the Philippines' National Renewable Energy Board (NREB), RE developers, and financiers. This webinar served as an avenue for banks to offer their insights on supportive policy and financing mechanisms in pursuit of the country's goal of reaching 35% RE in the power mix by 2030. This dialogue facilitated greater alignment among energy regulators, financial institutions, and other market stakeholders by presenting financing opportunities in the energy sector and discussing challenges that developers face in accessing project financing.

Key takeaways from the RE Financing dialogue include:

- NREB emphasized that the Philippines' pursuit of achieving 35% RE in the power mix by 2030 presents **a trillion peso (USD $20.5 billion) investment opportunity**. **46.9 terawatt-hours of <u>new</u> RE generation (equivalent to 20GW)** is needed to meet this goal.
- In addition to the Renewable Portfolio Standard (RPS), additional **policies and programs to meet this goal are on the horizon, but full implementation needs to occur rapidly.** Emerging efforts include the Green Energy Option Program (GEOP), Green Energy Auction Program (GEAP), and enhanced net-metering.
- Coal currently dominates the power mix in the Philippines, making up 55% of electricity generated, while RE only comprised 21% in 2019. **The Philippines could face USD $20 billion in stranded assets if new coal power plants continue to expand in the future**. This further underscores the need to shift investment toward RE development.
- Unlike conglomerate-backed RE developers, **smaller independent developers face difficulties securing financing**. Nevertheless, they can still **play an important role in markets,** as they are close to the ground, can originate projects quickly, and can create positive competition by giving consumers options and ultimately decreasing costs for end-users.
- Currently, **banks have limited knowledge and experience investing in RE merchant plants** (projects without long-term, bankable offtake agreements). **Identifying ways to advance these projects could serve as an entry point for the emergence and scale up of small, independent RE developers.**
- Another challenge is the interplay between insurance and financing, which creates a chicken-and-egg situation, where without insurance, projects cannot attract financing, but projects without financing will not be insured.

Self-Assessment and Capacity Building for BSP Working Groups:

GTB deepened collaboration with BSP through a closed-door virtual workshop on **self-assessment and capacity building**, which brought together 106 BSP officers across different working groups and departments. This dialogue complemented the second phase of BSP's Sustainable Central Banking (SCB) program and efforts to assess the impacts of climate and environmental risks on BSPs offices and branches and determine the areas of BSP operations where green practices can be most effectively integrated. The event showcased sustainability initiatives being undertaken by other Asian central banks and strategic activities that BSP can begin to implement in the near-term.

Key takeaways from the BSP self-assessment dialogue include:

- **Central banks are credible and powerful actors in developing countries, and can play a key role in addressing financial and macroeconomic risks and market failures to improve overall sustainability.** Central banks can effectively guide and influence private investment decisions. Moreover, central banks' financial market expertise and transnational networks can help them to **promote best practice reforms across the financial sector.**
- **Central banks can use a range of tools to scale up green finance and enhance the financial sector's understanding and awareness of risks**, including micro-prudential assessment tools, detailed guidance or requirements on ESG risk analysis and disclosure, green finance incentive mechanisms, and other supportive initiatives like recognizing exemplary sustainability performance of local banks or adjusting the risk weights for green assets and high-carbon assets.
- **Strategic actions BSP could consider taking in the near-term include:**
    - Performing analysis to inform BSPs focus areas, including analysis of **sectors most impacted by climate change (both physical and transition impacts) as well as sectors that play an outsized role in supporting the economy and influencing market behavior**.
        - An initial step could include conducting an emissions inventory to calculate a baseline of BSP's scope 1, 2, and 3 emissions and their sources using the GHG Protocol Corporate Standard This could help BSP determine high-emission, priority areas as well as ensure it can track progress over time.
            - It is important for BSP to focus on analysis at the asset class or portfolio level (beyond its own physical operations), as reducing financed emissions from its portfolios can have a significant impact on its overall GHG footprint.
    - Sharing BSP's data and models used for scenario analysis to help inform other financial institutions and small-to-medium enterprises (SMEs).

- Establishing common thresholds and clear timelines for decarbonization targets for BSP's portfolio to enable banks to implement Environmental and Social Risk Management Systems in a level playing field.
- Reducing the burden of requiring ESG assessments by identifying or designing a central ESG assessment and certification system and database or by subsidizing the cost of clients' capacity building through incentives such as tax deductions.
- Leading the way by committing to net-zero emissions and sending a strong signal to other banks to do the same.
- Working with other government agencies to develop enabling systems that facilitate the growth of low-carbon technologies and businesses in energy, transport, and other sectors, so finance and technology can work in harmony to decarbonize the country.

For more information on the Greening the Banks initiative, please visit https://www.allotropepartners.com/greenfinance or contact Gabriel Silan, Program Manager, at jgs@allotropepartners.com.