Exclusive Interview with Chartered Banker, Rizleen Mokhtar, former Executive Vice President of Credit Risk at AmBank Group
Unfazed by the Future

BANKING INSIGHT

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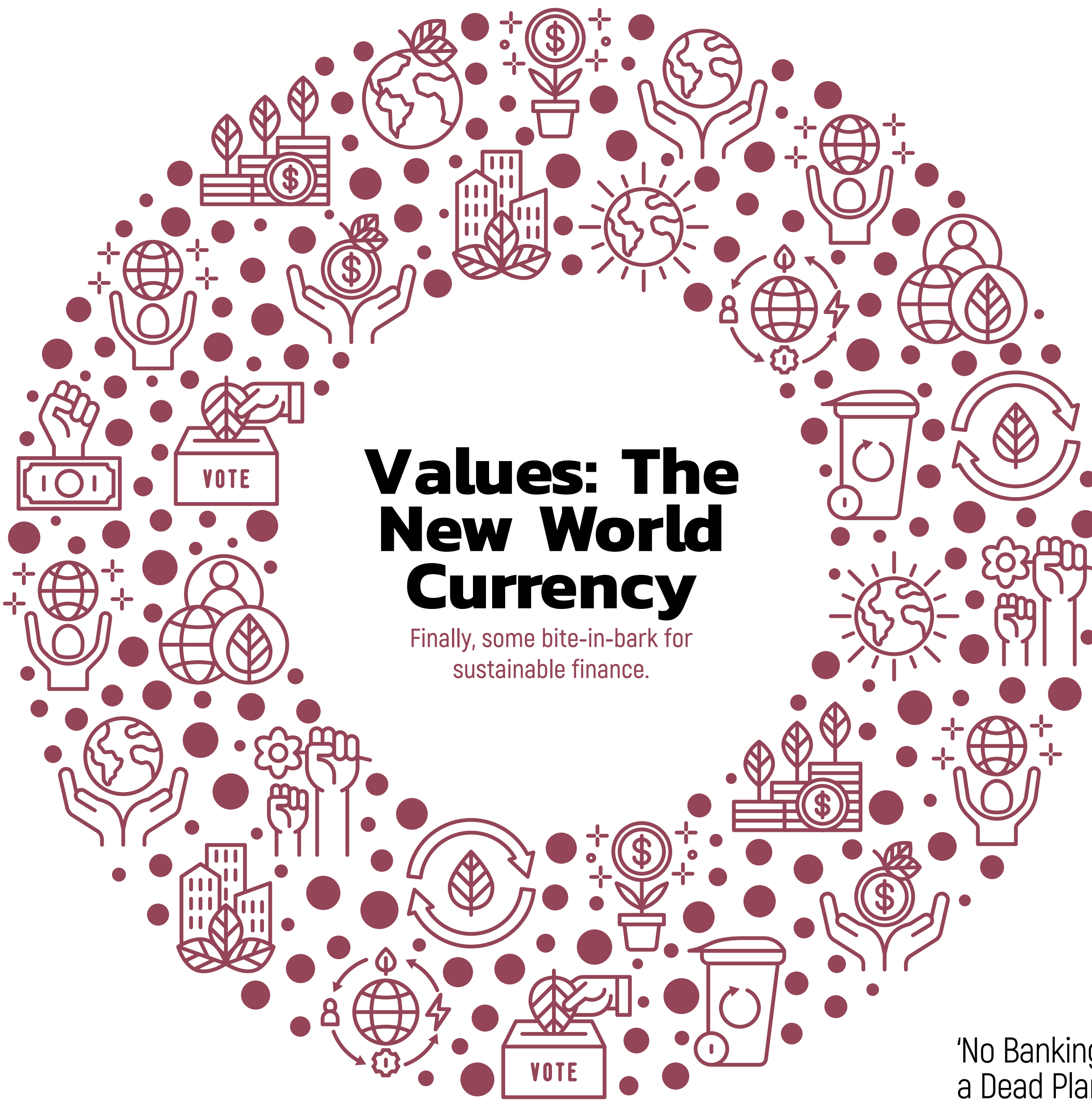

Values: The New World Currency

Finally, some bite-in-bark for sustainable finance.

'No Banking on a Dead Planet'

MANY MARKETS, ONE COMMON LANGUAGE

NOVEL WAYS OF THINKING IN FINANCE

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PRE-EMPT A GREEN SWAN

by Julia Chong

Focus on material sustainability issues to mitigate sustainability risks and achieve alpha.

Whilst alarmist reports make for good headlines, they are an incomplete reflection of the work that has been done to forestall a potential climate-related financial crisis. Reining in sustainability risks has been on the agenda for some time, but garnered little attention from media stalwarts.

Take, for instance, non-profit Ceres' announcement that lending linked to fossil fuels and energy transition could translate into more than USD100 billion in losses for US banks and systemic financial risk. What this soundbite – carried by major newswires throughout the world – fails to reflect is the other side of the story.

COMPLY OR EXPLAIN

In every way, sustainability policies today are the result of years of behind-the-scenes work by supervisory authorities.

The EU's Sustainable Finance Disclosure Regulation (SFDR), which came into effect on 10 March 2021, is a landmark new regulation issued by the European Supervisory Authorities to achieve the goal of a carbon-neutral Union by 2050. The Regulation is a legislative tool designed to reorient capital towards sustainable businesses in order to achieve global climate goals whilst ensuring financial institutions actively combat 'greenwashing' i.e. conveying a false impression or misleading information to investors that the products are environmentally friendly.

An important aspect of the SFDR, specifically Recital 10, is that it is now mandatory for financial institutions to make pre-contractual and ongoing disclosures with regard to sustainability risk to end investors in accordance with regulatory technical standards.

The European Banking Authority (EBA) define sustainability risk as an environmental, social, or governance (ESG) event or condition which could cause an actual or a potential material negative impact on the value of the investment. This provides greater protection for end investors as firms must now disclose sustainability characteristics and risks at both entity and product level in accordance with EU-issued technical standards. Otherwise, firms must explicitly state that the product or entity does not take into account sustainability risks. This is known as a 'comply or explain' regime.

Most European banks have in place policies and/or established frameworks to address this risk and actively inform investors how controls are in place to take into account sustainability impacts. Rothschild & Co Merchant Banking, for instance, discloses to investors how sustainability risk may occur as part of its ESG investments:

"This policy therefore approaches sustainability risk from the perspective of the risk that ESG events might cause a material negative impact on the value of our products' investments. To give an example, if a Merchant Banking fund has significant exposure to digital services businesses which collect and process