

Unlocking Islamic Climate Finance





Today we live in a truly interconnected world with ecological limits. We now need to bring the system into balance by putting more emphasis in designing our systems with intrinsic values, such as **relationship, openness and kindness**

(UNEP, Values Based Banking: Bringing the Voice of the Citizen into Finance)

The World is Watching . .

- The demand for financial services that are **responsible** and **provide positive socioeconomic impact** has substantially increased.
- ***For example:***
 - Greenpeace, in a Youtube campaign, exposed Banco Santander's loans of GBP400 million to a logging company expanding its operations in Indonesia.
 - After 3 million views in just 2 days and subsequent public protest, the bank announced within 48 hours that it would no longer lend to the company and that future lending would be based on new sustainability objectives.

<https://www.youtube.com/watch?v=58r1INe1SNM>

<https://www.youtube.com/watch?v=TQQXstNh45g>



Leading Risks

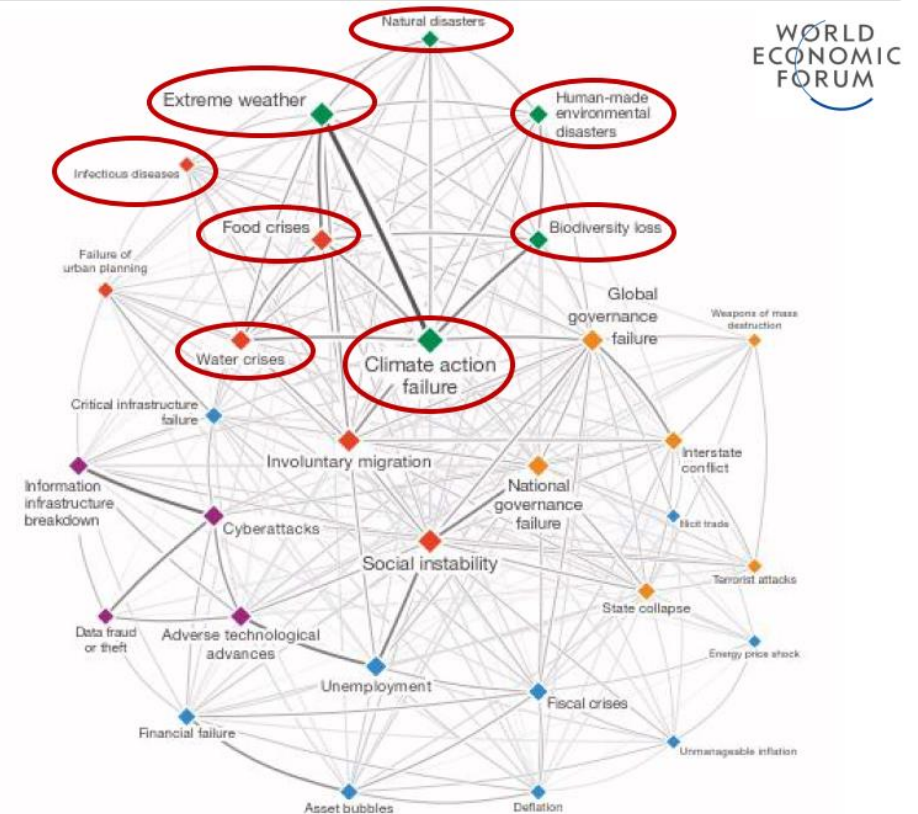
Top 10 risks in terms of Likelihood

- 1 Extreme weather
- 2 Climate action failure
- 3 Natural disasters
- 4 Biodiversity loss
- 5 Human made environmental disasters
- 6 Data fraud or theft
- 7 Cyberattacks
- 8 Water crises
- 9 Global governance failure
- 10 Asset bubbles

Top 10 risks in terms of Impact

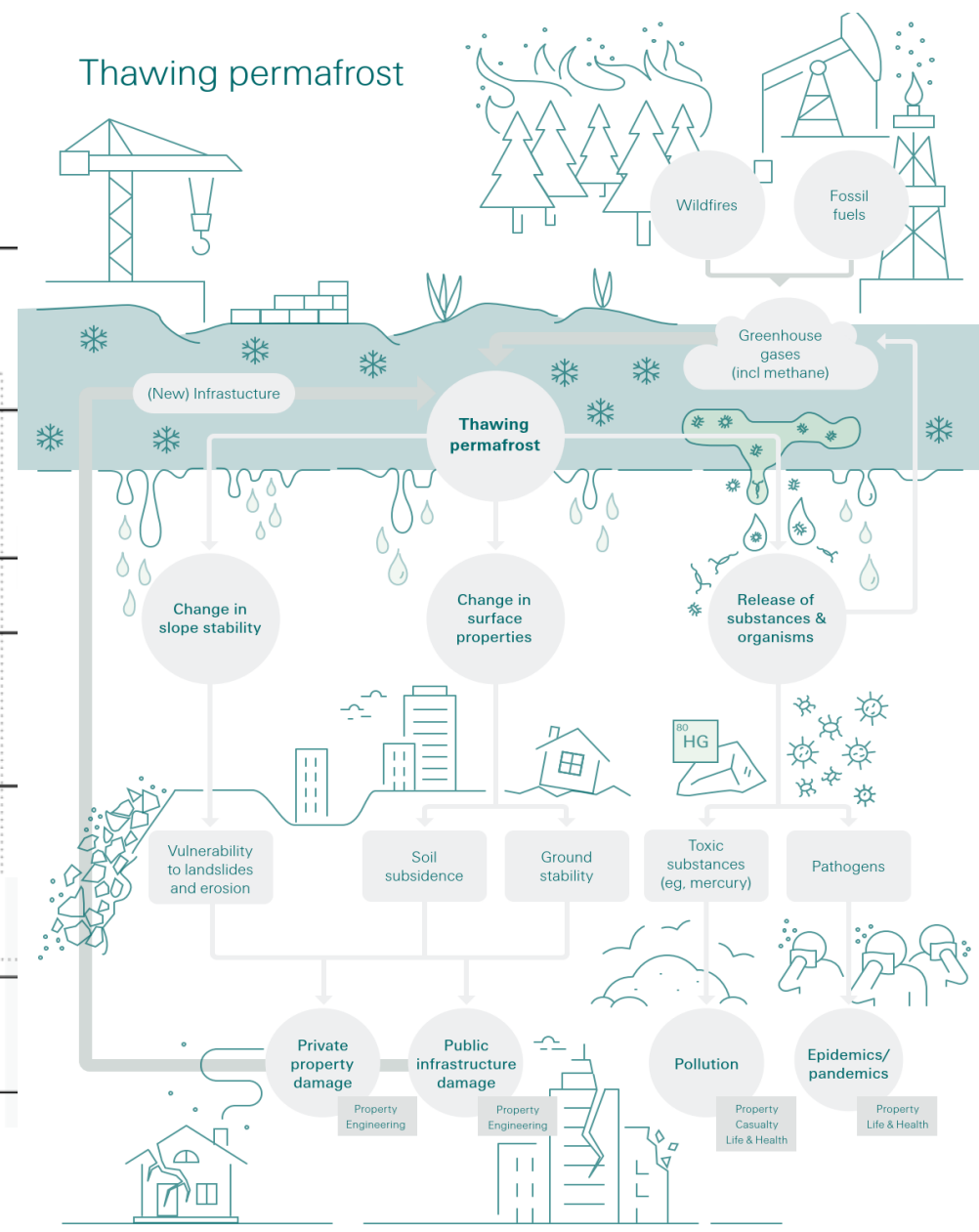
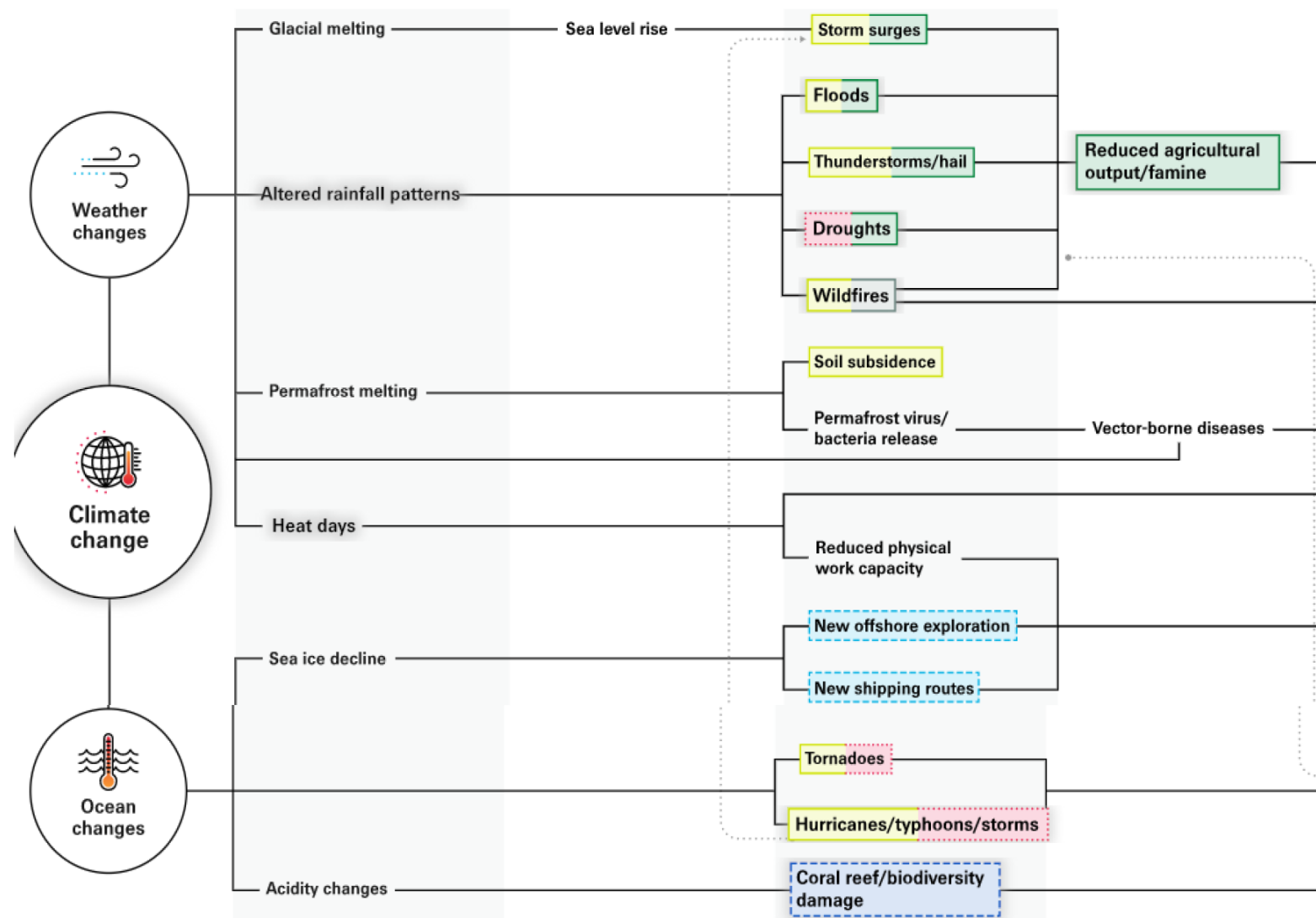
- 1 Climate action failure
- 2 Weapons of mass destruction
- 3 Biodiversity loss
- 4 Extreme weather
- 5 Water crises
- 6 Information infrastructure breakdown
- 7 Natural disasters
- 8 Cyberattacks
- 9 Human made environmental disasters
- 10 Infectious diseases

Environmental risks have most Connections



Source: World Economic Forum

Emerging Risks in Climate Change



Risks in South East Asia



**26%
DECLINE**

Crop yields
could decline
by up to 26%
by 2050



50%

Agricultural land
in the Mekong
Delta could
be affected
by saltwater
intrusion by 2100



10-20MM

Annual sea
level rise in
Greater Mekong,
threatening
major cities



94 MILLION

Increase from
13 million to
94 million
people flooded
annually in
South Asia



1 BILLION

Migrants in
Asia-Pacific
by 2100 due to
climate change

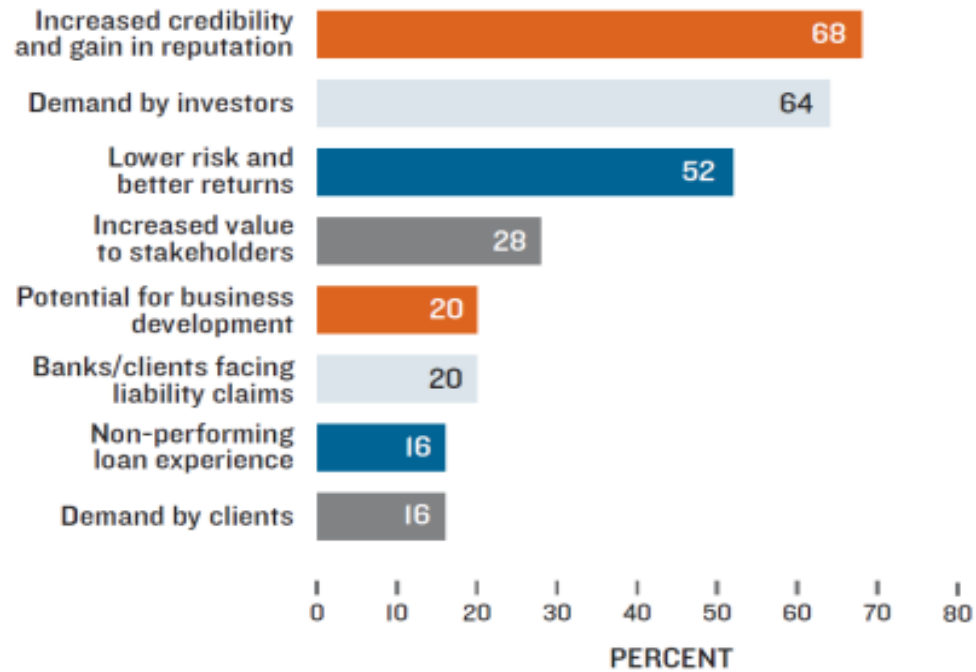


11 %

DECLINE

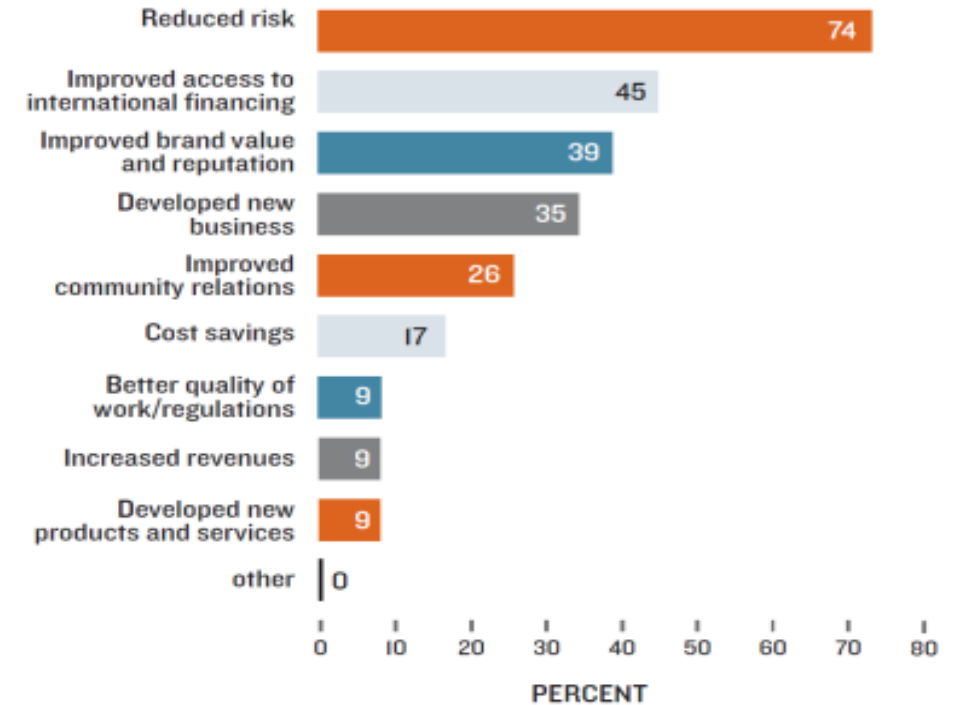
Southeast Asia
GDP could
decline by 11%
by 2100

KEY REASONS WHY BANKS CONSIDER SUSTAINABILITY ISSUES (percent of respondents)



Source: IFC Sustainability Survey of Financial Institutions (2005).

BENEFITS OF CONSIDERING SOCIAL AND ENVIRONMENTAL ISSUES (percent of commercial banks)



Source: IFC Sustainability Survey of Financial Institutions (2005).



- **87% of millennials** believe that business success should be measured by **more than just financial performance**. 63% of British millennials think values-based investing delivers the same or better financial returns (2016 study).

CREATING VALUE THROUGH ISLAMIC GREEN BANKING

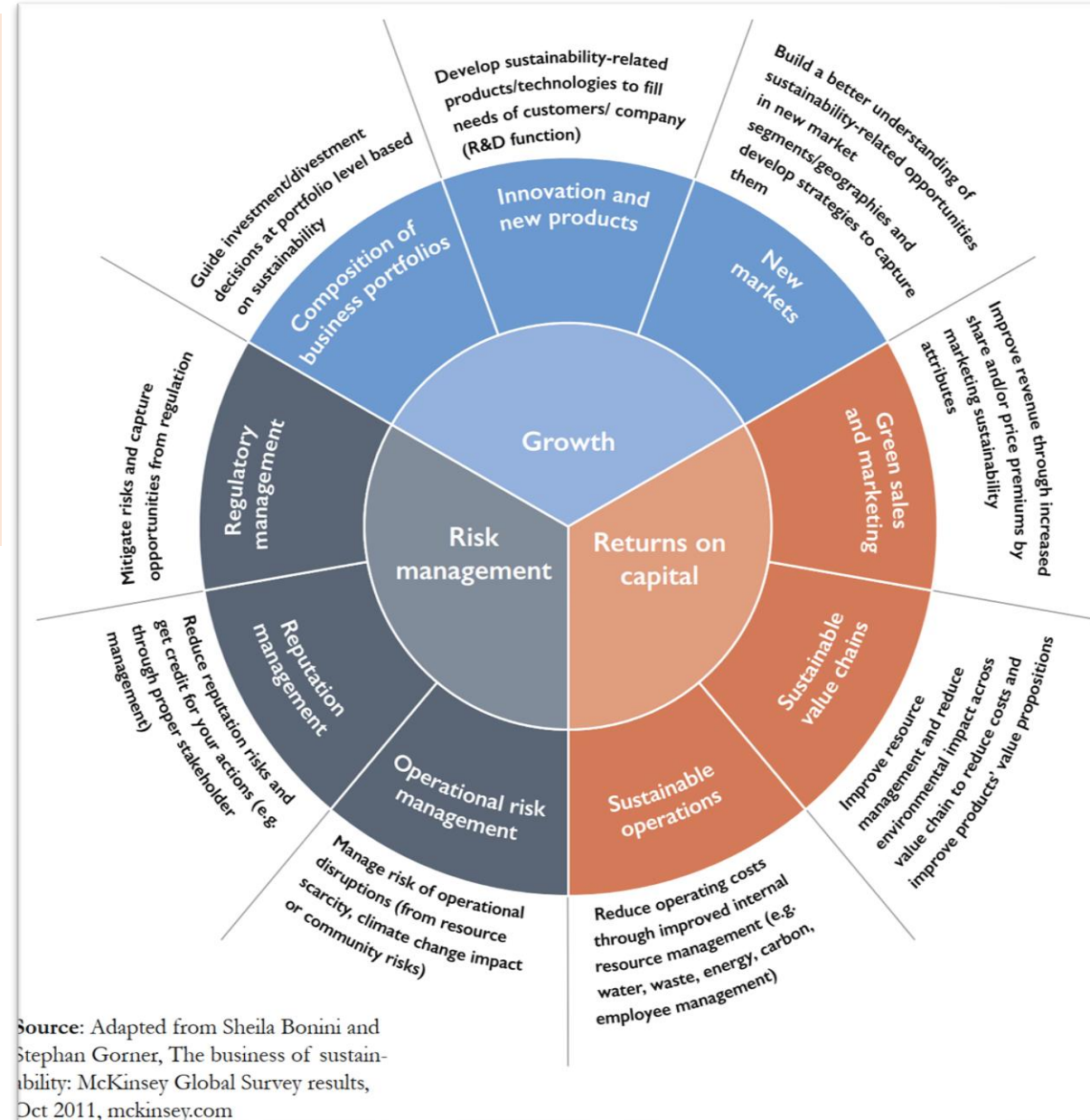
Risks of Inaction

- Loss of business opportunities and financing options through a failure to adapt to changing market realities
- Higher overall risk exposure through a failure to understand the materiality of environmental and social risks
- Potential pressure or disengagement of investors prioritizing sustainable investment choices
- Lack of preparedness for regulatory and policy adjustments
- **Risks to reputation, credibility and image of the Islamic finance ecosystem through failure to respond to stakeholder expectations**

Opportunities

- New business opportunities and diversified Islamic financing options from new market understanding, allowing for competitive advantage
- Stronger, more resilient Islamic banks that are higher rated
- Improved reputation, credibility and recognition of the Islamic brand
- Increased motivation and employee retention due to social impact
- Operational efficiencies and cost reduction through in-house application of sustainability projects (e.g. cost reduction through energy efficient branches)

Source: Adapted from UNEPFI Guide to Banking and Sustainability (2016)

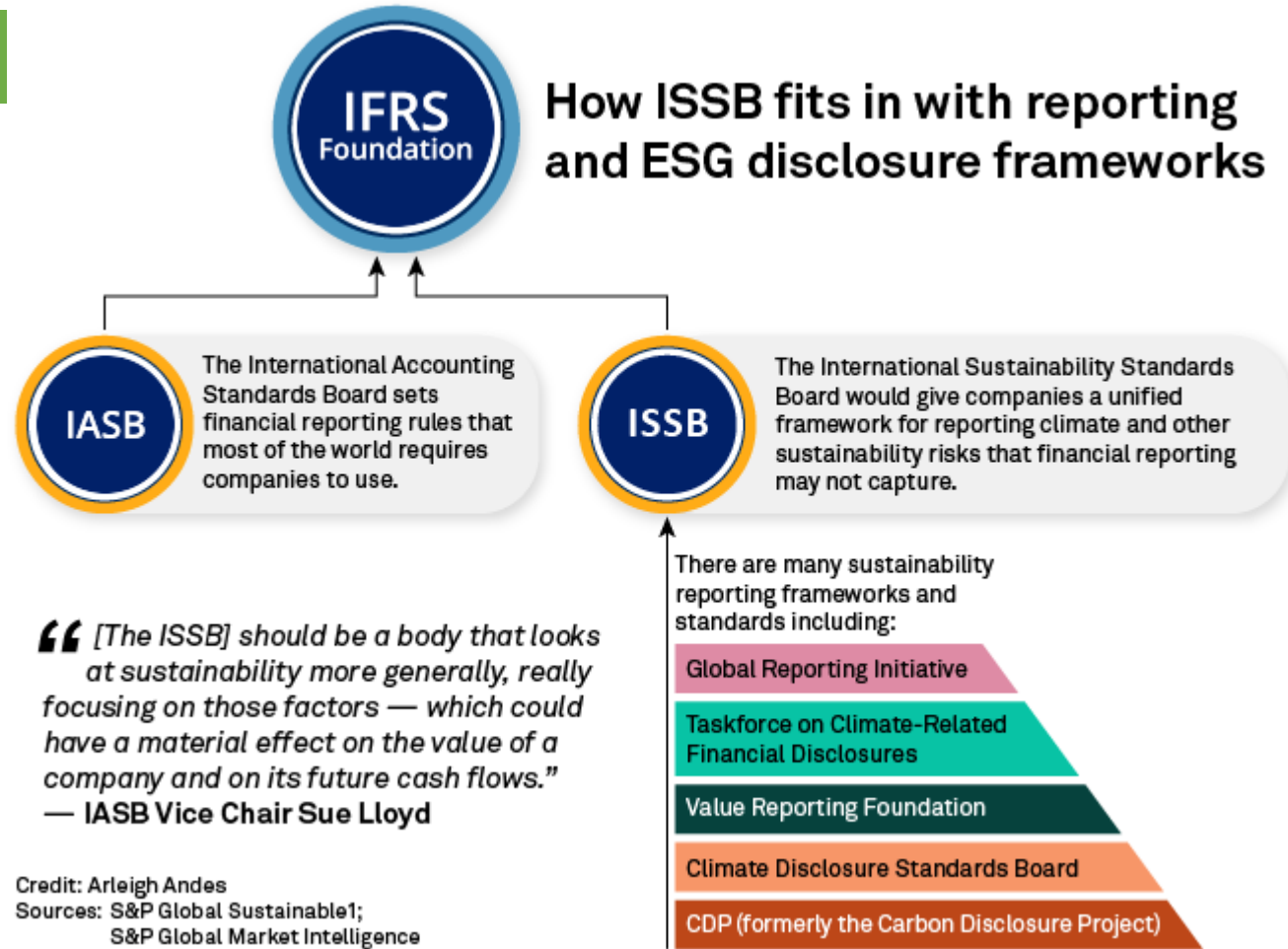


The Response from Financial Institutions

Accounting treatment and disclosure frameworks more effective at tracking ESG activity

Push toward mandatory regulation for banks and climate reporting

ESG-related policies and standards require constant revision with global targets



Entity		Target Sectors and Sub-sectors
California CLEEN Center (California, United States)	 California Infrastructure and Economic Development Bank	<ul style="list-style-type: none"> • Municipal clean energy projects • Clean electricity generation, distribution, transmission and storage • Energy conservation, environmental mitigation and water treatment
Clean Energy Finance Corporation (Australia)	 CLEAN ENERGY FINANCE CORPORATION	<ul style="list-style-type: none"> • Renewable energy (wind, solar PV, thermal and CSP, biomass, geothermal, tidal and other renewable energy [50%]) • "Low emissions" (CEFC 2014a) and energy efficiency [50%]
Connecticut Green Bank (Connecticut, United States)		<ul style="list-style-type: none"> • Energy efficiency • Renewable energy • Other clean technologies, including combined heat and power (CHP), anaerobic digestion, fuel cells, alternative fuel vehicles and infrastructure, storage and others
Green Energy Market Securitization (Hawaii Green Infrastructure Authority) (Hawaii, United States)		<ul style="list-style-type: none"> • Low and moderate-income homeowners, renters and non-profits • Distributed solar PV (initial phase) • Clean energy and energy efficiency (deployed in phases)
The Green Finance Organisation (Japan)		<ul style="list-style-type: none"> • Low-carbon projects (e.g. wind, solar, small-scale hydro, biomass, waste management, geothermal, hot springs, renewals of mid-sized hydro)
Malaysian Green Technology Corporation (GreenTech Malaysia) (Malaysia)		<ul style="list-style-type: none"> • Energy (renewable energy) • Water and waste management • Building (energy and water efficiency, indoor air quality)
Masdar (United Arab Emirates)		<ul style="list-style-type: none"> • Clean energy • Energy efficiency • Carbon capture and storage
New Jersey Energy Resilience Bank (New Jersey, United States)		<ul style="list-style-type: none"> • CHP, fuel cells and solar-tied storage at water and wastewater treatment facilities
NY Green Bank (New York, United States)		<ul style="list-style-type: none"> • Energy efficiency • Renewable energy • Other clean technologies, including CHP, electric vehicle infrastructure, fuel cells and offshore wind
Technology Fund (Switzerland)		<ul style="list-style-type: none"> • GHG reduction technologies • Energy efficiency • Renewable energy • Natural resource conservation technologies
UK Green Investment Bank (United Kingdom)		<p>Priority areas:</p> <ul style="list-style-type: none"> • Offshore wind • Waste recycling & bioenergy • Energy efficiency • Small-scale renewables <p>Other:</p> <ul style="list-style-type: none"> • Biofuels for transport, biomass power, carbon capture and storage, marine energy, renewable heat

Globally, various institutions are financing targeted sectors of green industry (renewable energy, water, waste etc) based on landscape and sustainable direction of the respective countries.

Several models provide Islamic finance opportunity, but has Islamic Finance Innovated in the Net Zero Space?

What about the Positive Climate Space?

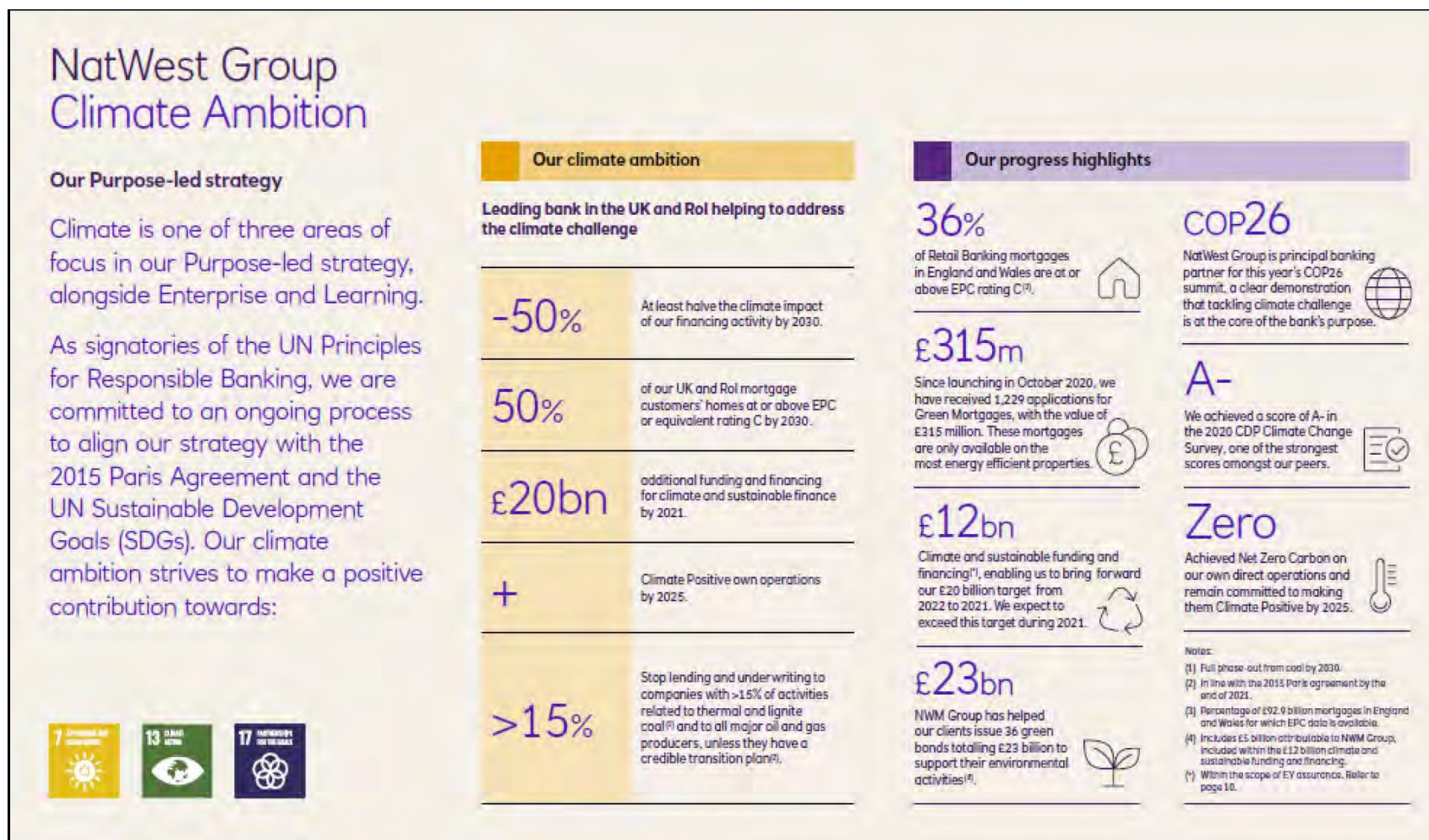
Unfortunately, not yet.

GREEN FINANCING INITIATIVES & INSTRUMENTS



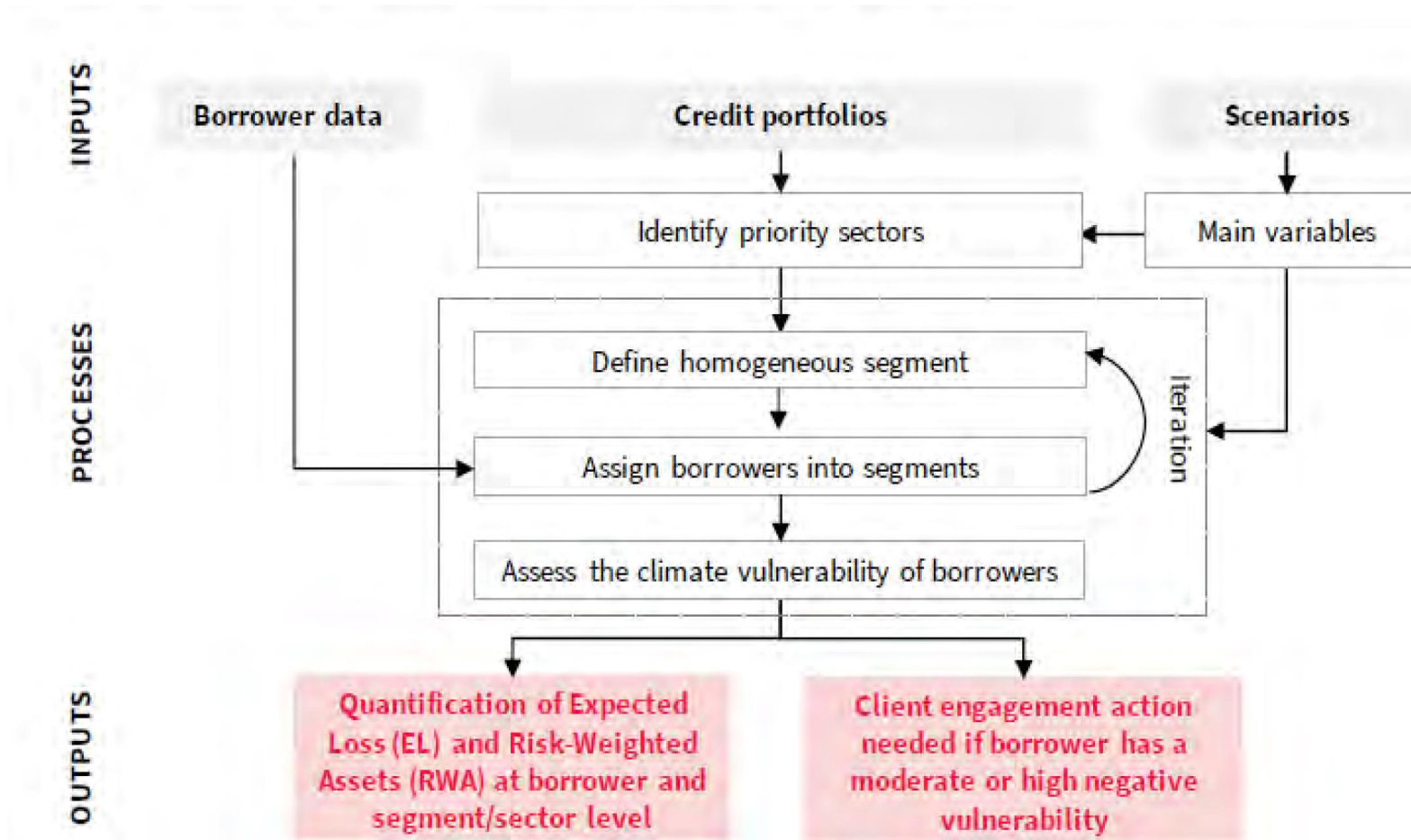
FINANCIAL CENTRE	Frankfurt (Germany)	London (United Kingdom)	Milan (Italy)	New York (United States)	Paris (France)	Tokyo (Japan)	Toronto (Canada)
GREEN FINANCE INITIATIVE	Accelerating sustainable finance	Green finance Initiative	N/A	N/A	Finance for tomorrow	N/A	N/A
Green bond stock exchange listing name	N/A	N/A	N/A	N/A	Euronext green bond franchise	N/A	N/A
Green bond value	€ 26.6 bn	€ 10.1 bn	€ 9.8 bn	€ 4.7 bn	€ 23.4 bn	N/A	N/A
Green bond listed	198	55	83	19	51	N/A	N/A
Certified green bonds	3	2	No	13	4	No	No
Green Lending, Market & Actors	\$ 17.0 bn from 5 major lead arrangers	\$ 8.7 bn from 5 major lead arrangers	\$ 4.5 bn from 3 major lead arrangers	\$ 11.8 bn from 8 major lead arrangers	\$ 17.2 bn from 5 major lead arrangers (RE projects)	\$ 37.20 bn from 5 major lead arrangers	\$ 6.5 bn from 6 major lead arrangers
Green Asset Mgmt. Funds	N/A	N/A	N/A	N/A	7 funds managed by 6 asset managers	N/A	N/A
Green Private Equity Funds	N/A	N/A	N/A	N/A	7 PE funds \$ 700 mn invested in cleantech in 2016 through 85 deals	N/A	N/A
Green crowdfunding	N/A	N/A	N/A	N/A	€ 11.5 mn	N/A	N/A
Green crowdfunding platform	N/A	N/A	N/A	N/A	13	N/A	N/A

Case Study: Conventional Bank Climate Change Approach



Source: NatWest Group Plc's Climate-related disclosures report 2020

Case Study: Societe Generale – Methodology for assessing transition risks on credit portfolios



Source: Société Générale Climate Disclosure Report 2020

BNM Survey on Climate Change Risk Integration

Number of financial institutions invited to participate

35



Number of respondents*

24



Survey questions categorisations

Section A: Strategy and Commitments
Section B: Governance, Risk and Reporting
Section C: Asset and Liabilities
Section D: Products and solutions
Section E: Client Base
Section F: Shareholder and Investor Engagement
Section G: Critical Success Factors and Challenges

Breakdown of respondents*



92%

of respondents have a sustainability **strategy** in place, however only **42%** have made commitments on **net zero**

Strategy



73%

of banking respondents have made some commitments to ban or phase out **financing of coal** related activities

Commitment



83%

of respondents have a sustainability **framework** in their organisation, however only **46%** have reflected **climate risk** in their risk appetite statement

Governance



88%

of respondents offer sustainability **products** to their customers, and **92%** plan to increase the number of sustainability products in the future

Products



21%

of respondents have a **third party verification** process on their sustainability reports

Reporting



95%

of respondents cited **data quality or availability** as one of the key challenges in driving the sustainability agenda

Challenges

What is a **TRANSITION STRATEGY** and how does it relate to Sustainability?

Transition strategies are the plans which are at the core of moving to low emissions and finally, **net zero**

Supports the framework set by the G20 Sustainable Finance Working Group (SFWG), supports efficient allocation of capital across sectors toward net zero

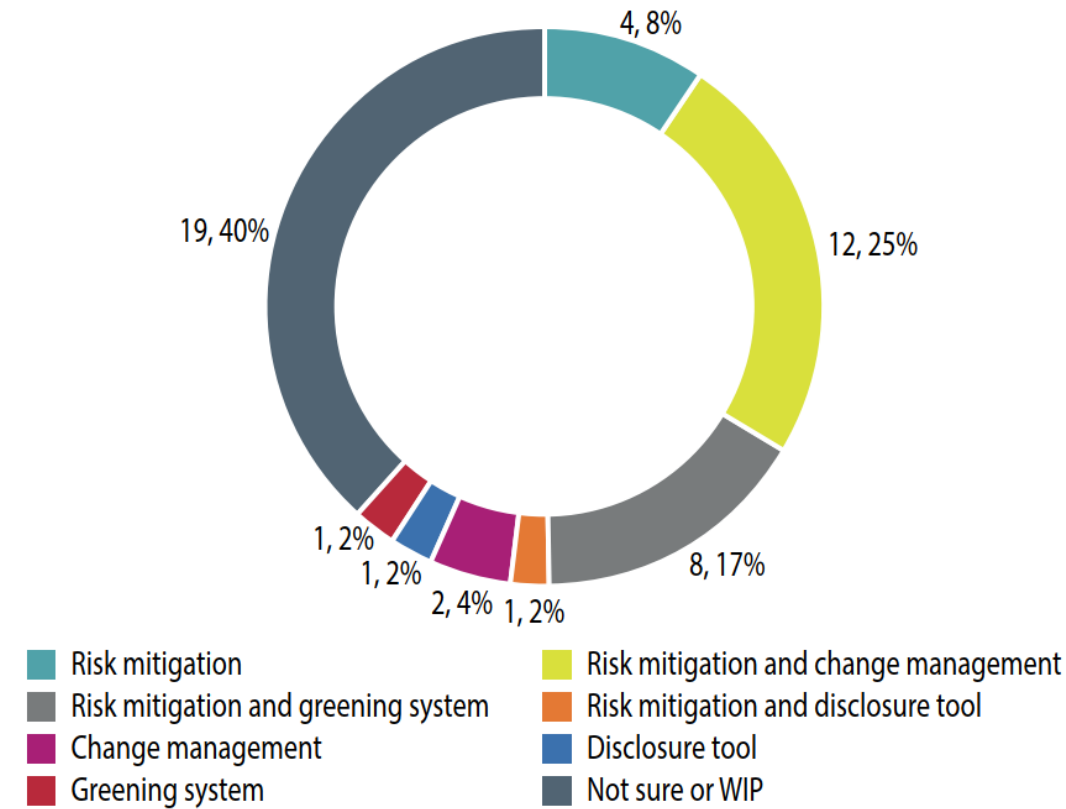
The Taskforce on Climate-Related Financial Disclosures' (TCFD's) 2021 Status Report recommended the introduction of climate transition plans for FIs

There is no standard approach to transitioning

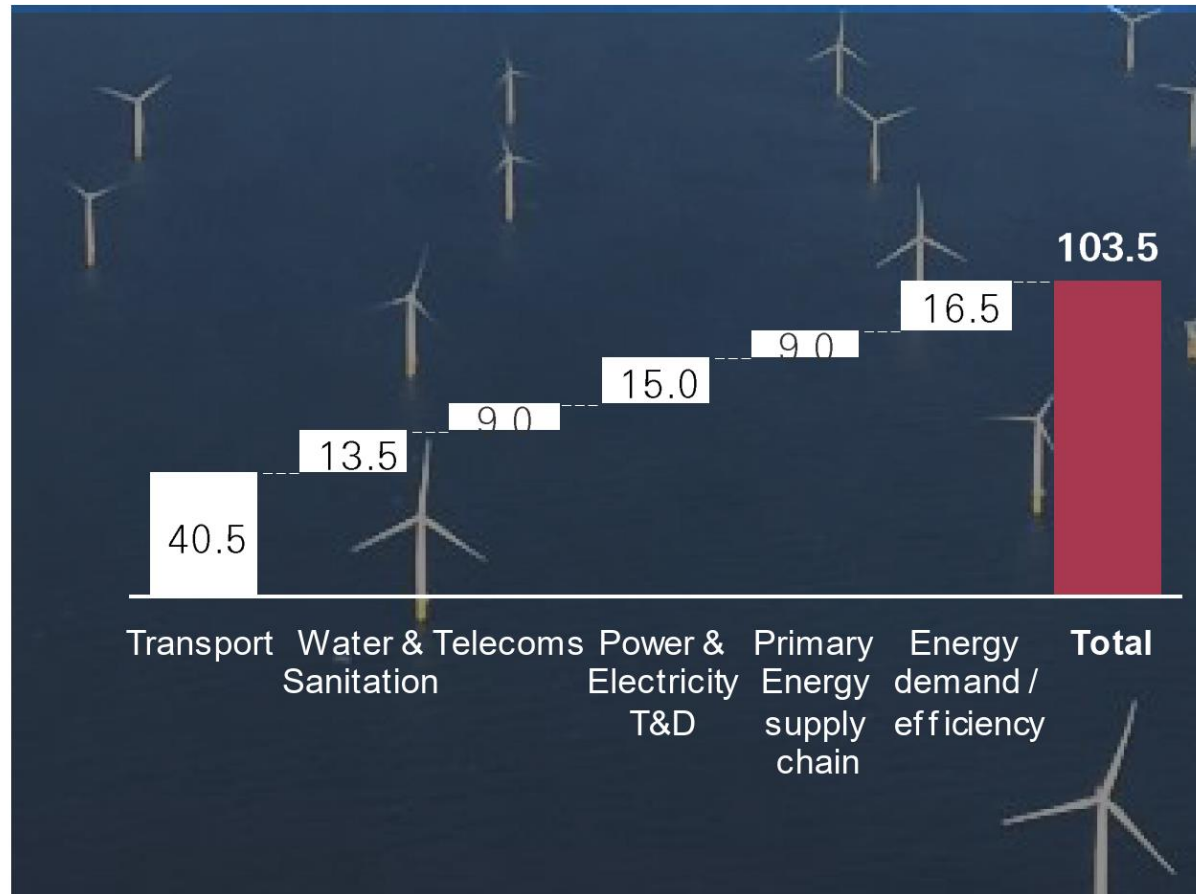
Micro-prudential guidelines are still being adjusted to ensure effective transition plans with practical oversight

Differences exist across jurisdictions

What is the purpose of **TRANSITION STRATEGIES**?



Transition Funding Gaps

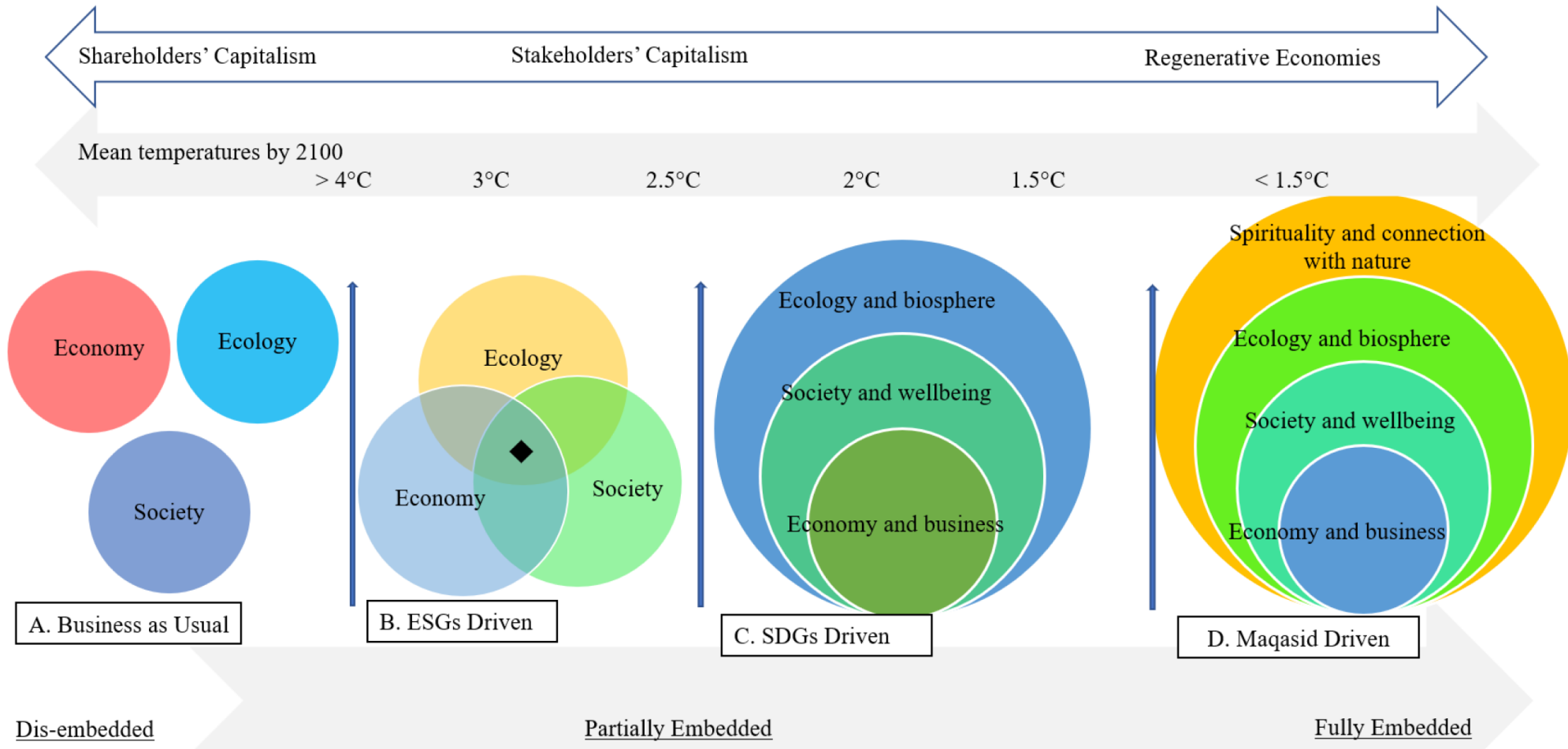


- OECD Research indicates that USD100 trillion is needed to fund sectors in reducing transition funding gaps across 5 sectors
- Islamic transition funding for decarbonisation is broadly unexplored
- Green Sukuk issuances have been limited, and decarbonisation infrastructure even more so
- Offshore jurisdictions like Labuan can support by identifying opportunities in the region, facilitate/manage funding proceeds and even support third party verification for such projects

What does Islamic Finance have to offer?

- ✓ Real Economy Financing and Investment
- ✓ Shared Prosperity = Responsible Intermediation
- ✓ VBI Approach
- ✓ Green Sukuk
- ✓ Shariah Governance – Sukuk
- ✓ Islamic Social Finance Solutions for Climate Refugees
- ✓ Holistic Shariah Objectives

Leveraging on Islamic Objectives to drive to Net Zero



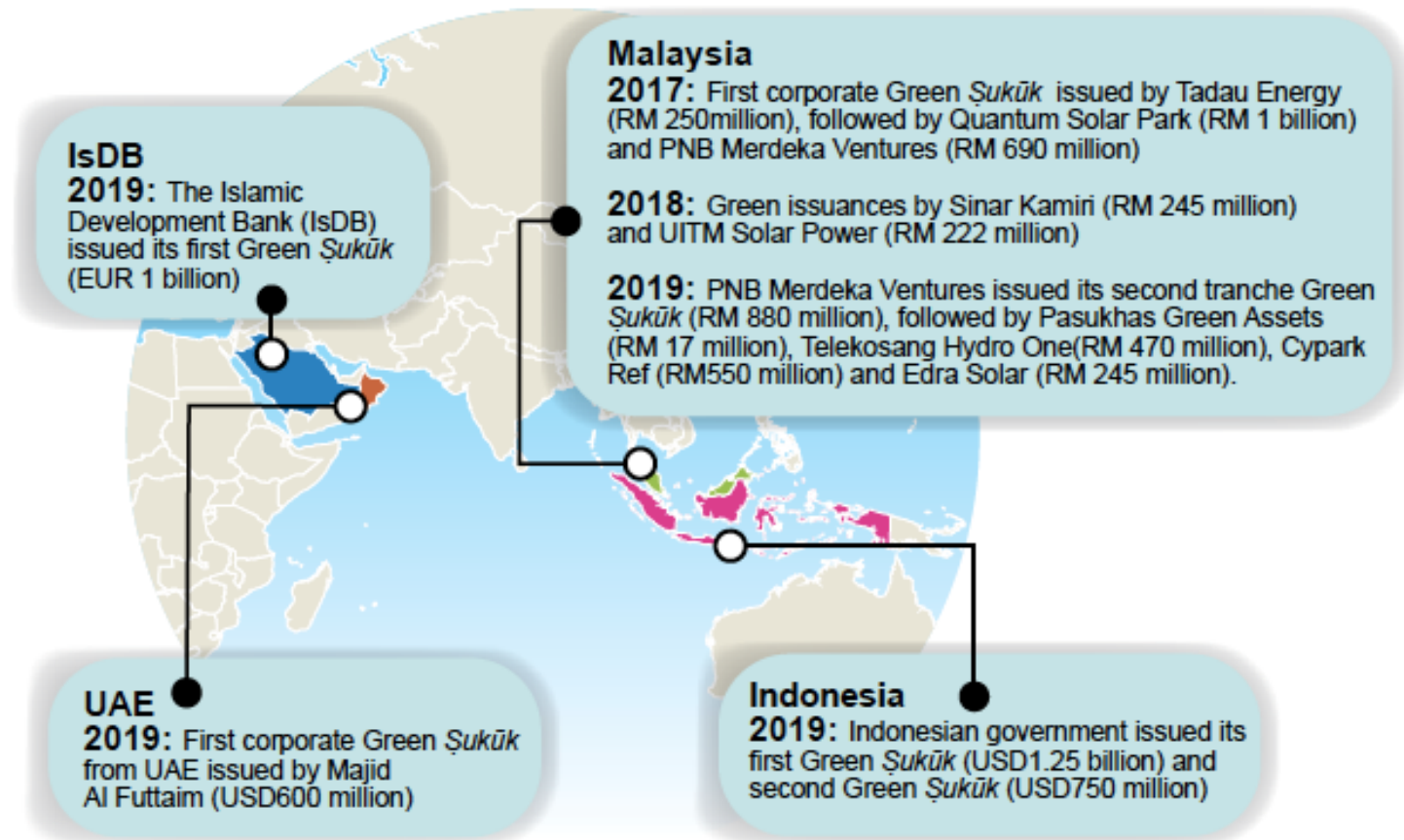
Source: Khan & Thabit (2023)

Green/SRI Sukuk refers to the financing of projects with the objectives to preserve and protect the environment and natural resources; conserve the use of energy; promote the use of renewable energy; reduce greenhouse gas emission; or improve the quality of life of society.

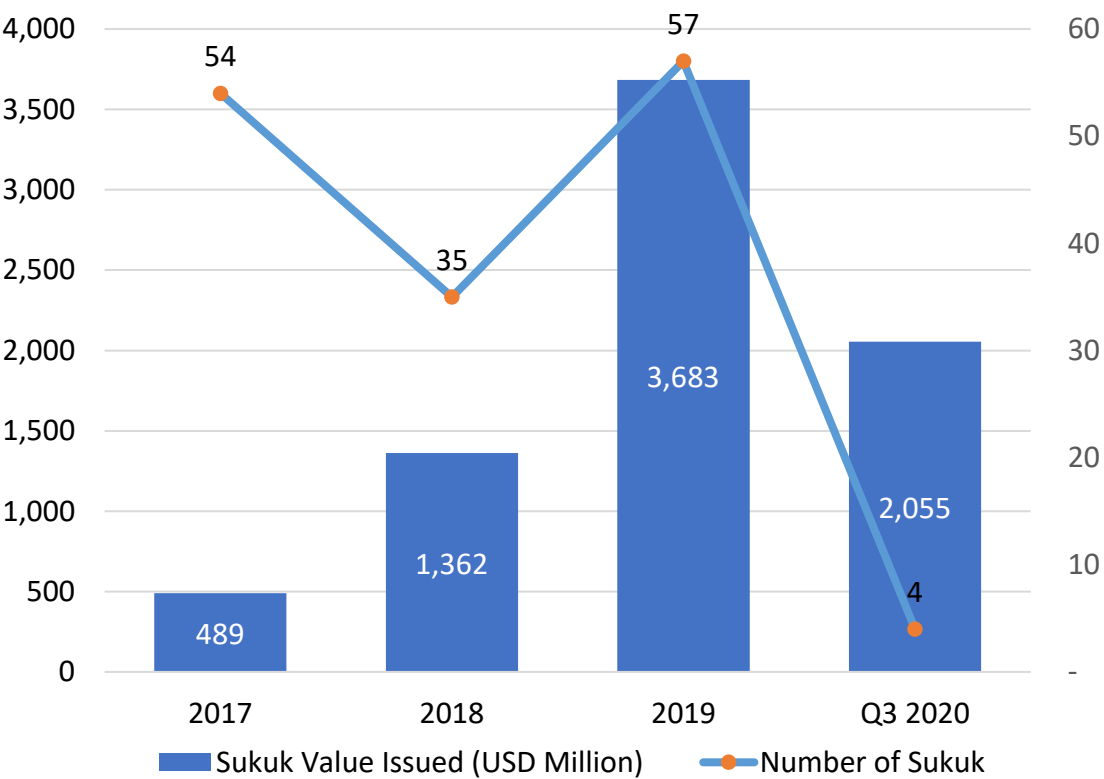


Green sukuk are **Shariah-compliant** investments in sustainable or environmental assets.

GREEN SUKUK

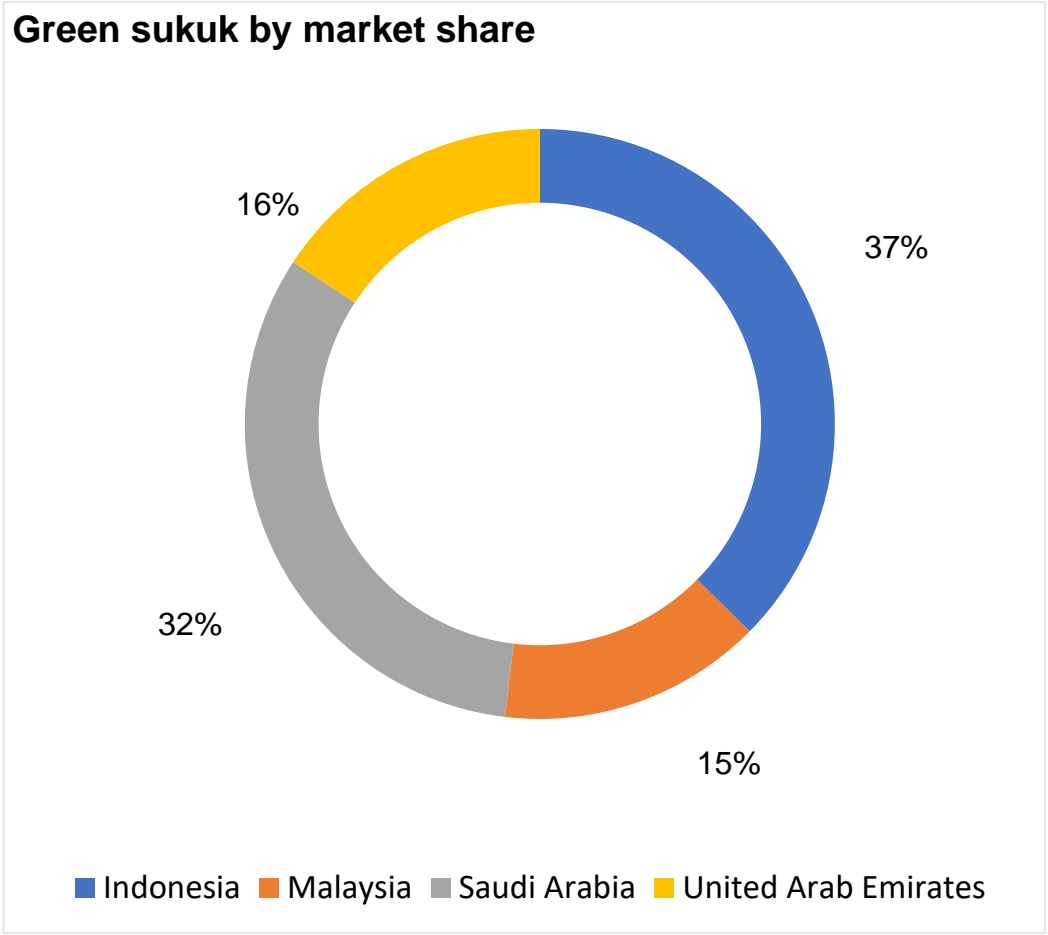


Green Sukuk Historical Issuance 2017 – Q3 2020

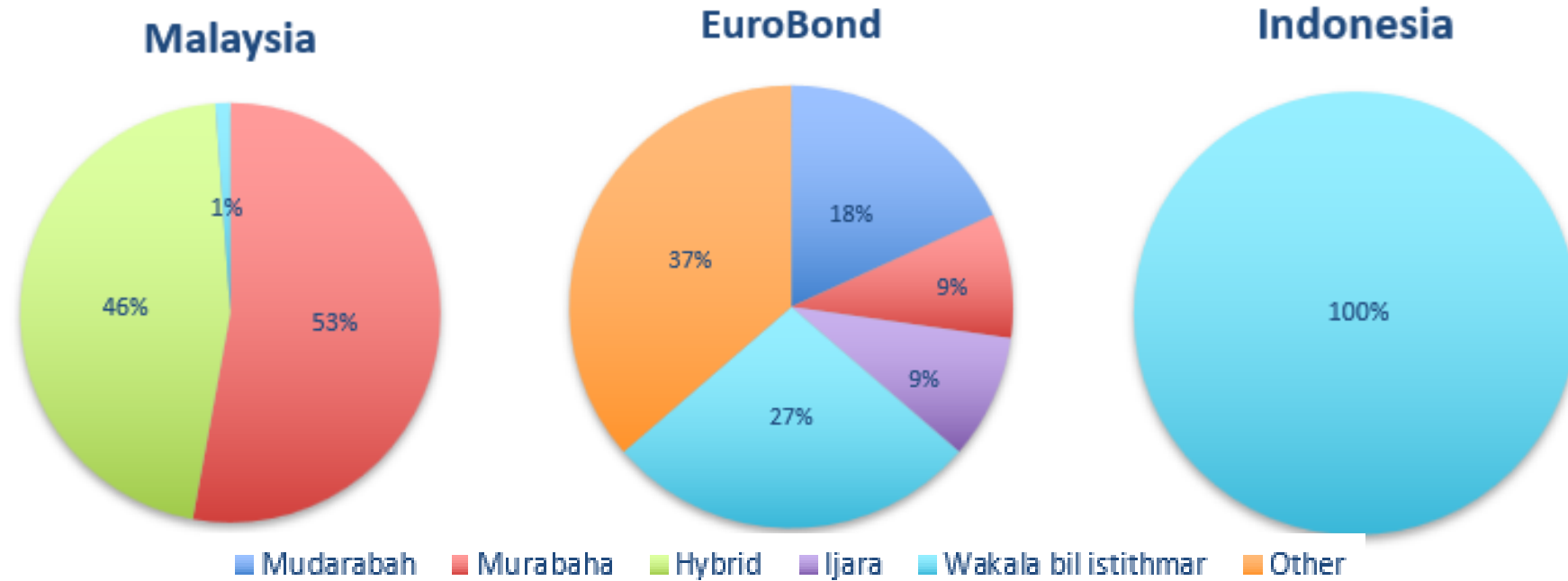


Source: Refinitiv, 2020

Green sukuk by market share



Green Sukuk Types



Country	Issues	Amount Issued (million USD)	Avg. Tenure (years)	%Avg. Coupon
EuroBond	11	\$11,479.400	5	2.7
Indonesia	2	\$725.916	2	5.2
Malaysia	87	\$638.465	6	4.8

Source: Refinitiv Eikon (2022)

Incentivising Green Issuance

Extension of period of tax incentive on issuance of Sustainable and Responsible Investments *Sukuk*

- Effective from years of assessment 2016 to 2020, a tax deduction is given on the issuance cost of Sustainable and Responsible Investments (SRI) *Sukuk** either approved by, authorised by, or lodged with the Securities Commission of Malaysia.
- It is proposed that the above tax incentive be extended for another 3 years.

Effective: Years of assessment 2021 to 2023

SRI Sukuk refers to the financing of projects with the objectives to preserve and protect the environment and natural resources; conserve the use of energy; promote the use of renewable energy; reduce greenhouse gas emission; or improve the quality of life of society.

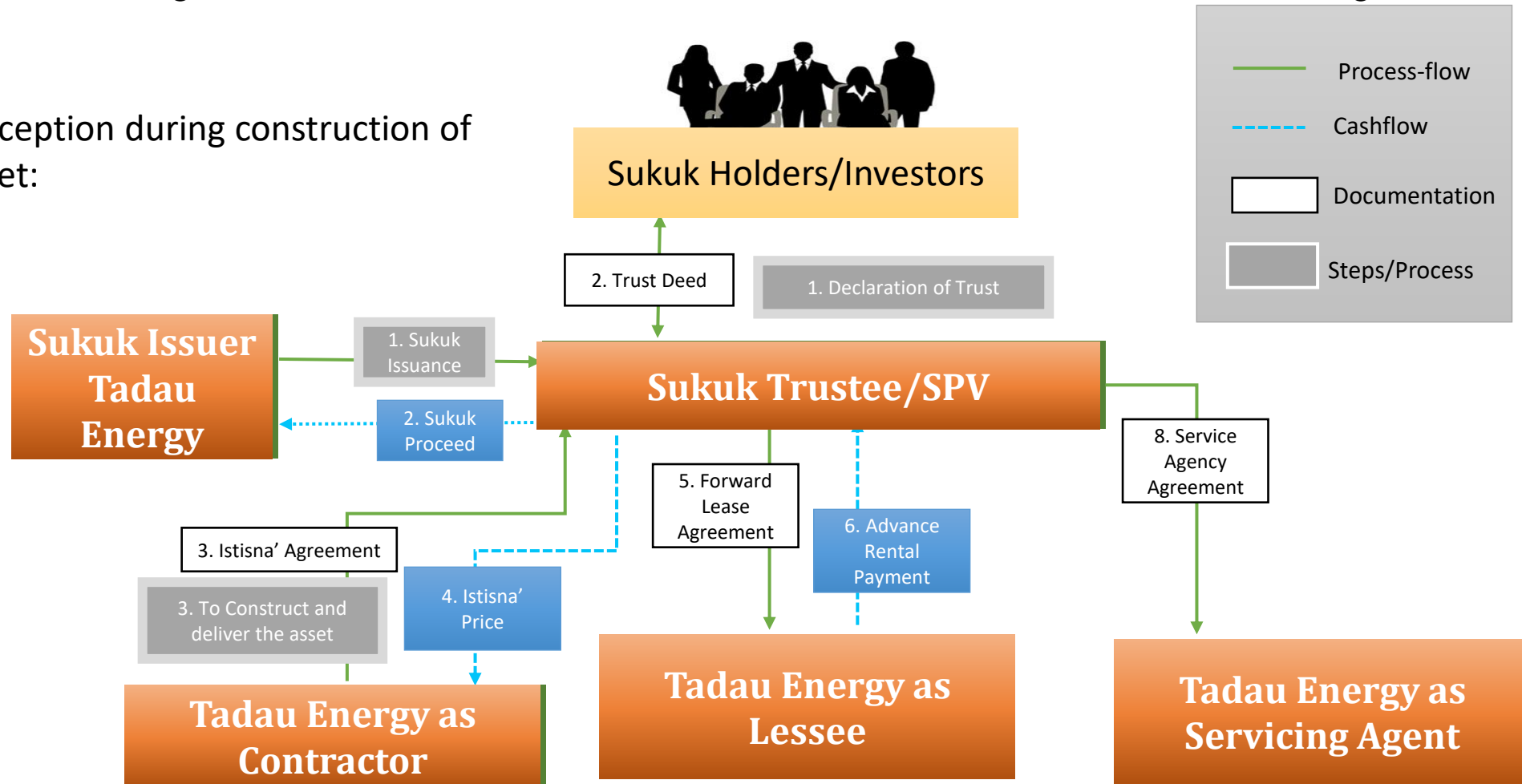
Case Study – Tadau Energy

Case Study: Tadau Energy

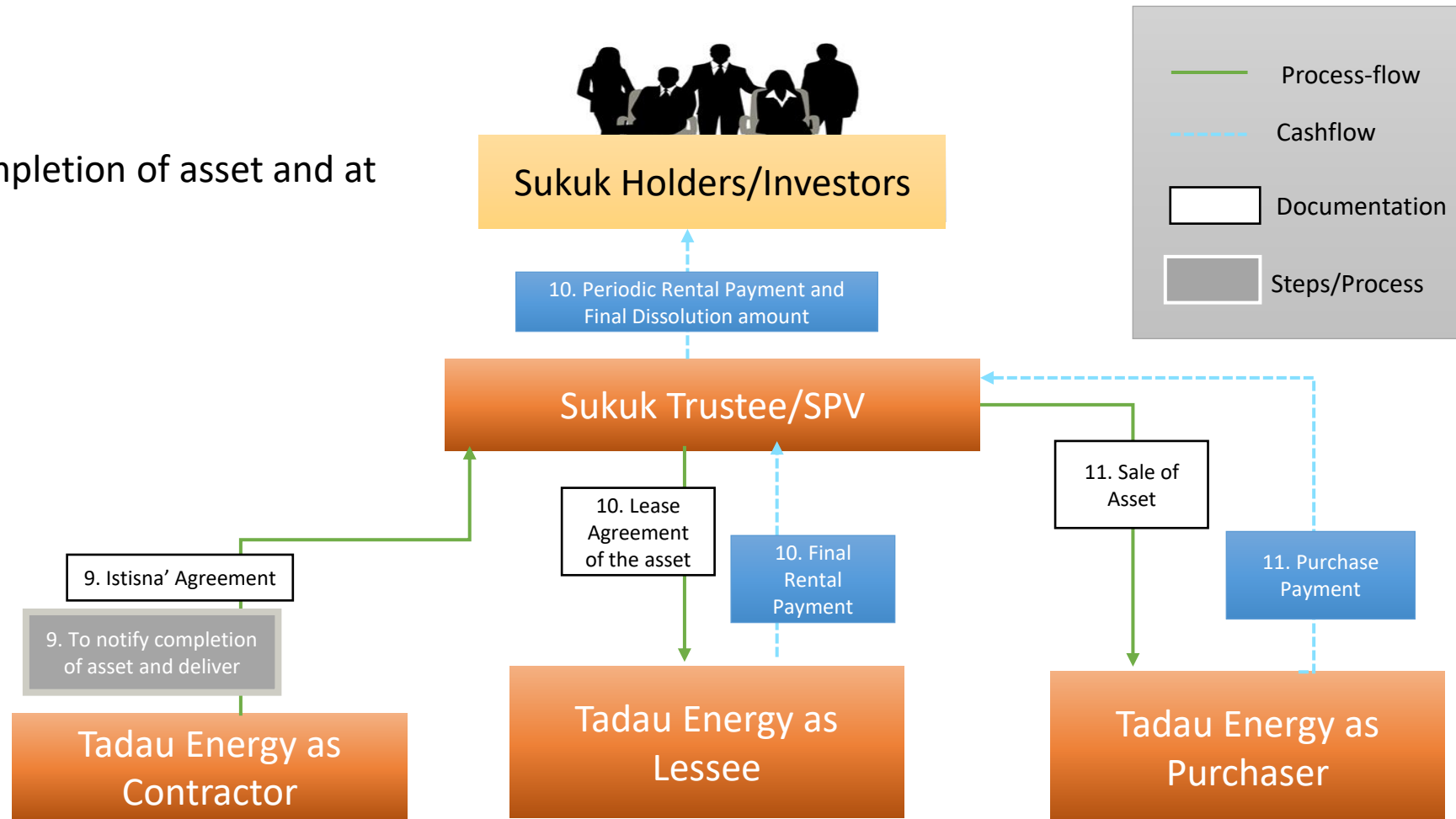
- Solar energy firm Tadau Energy Sdn Bhd had successfully issued RM250 million worth of sustainable responsible investment (SRI) sukuk, making it the first green sukuk issued in Malaysia.
- The proceeds raised will be used to finance a 50MWac solar project in Kudat, Sabah, which was secured under two 21-year power purchase agreements (PPAs) entered into with Sabah Electricity Sdn Bhd (SESB)
- SRI sukuk framework for green projects must ensure that proceeds raised are used to fund eligible SRI projects in natural resources, renewable energy and/or energy efficiency sectors in order to be eligible for tax deductions under SRI sukuk incentives.
- There are three underlying contracts utilised in this sukuk namely *istisna'*, *ijarah* and *ijarah mausufah fi zimmah*.

TADAU ENERGY SDN BHD

a) At inception during construction of the asset:



b) Post completion of asset and at maturity:



Examples of products that have been observed in the global market:



Banks

- **Microfinance** - Financing instrument targeted at low income population
- **Green loans** - Lending to encourage market development in climate aligned sectors
- **Green mortgages** - Encouraging homeowners to purchase new energy efficient homes such as those with solar panel
- **Green vehicle financing** - Incentivise demand for green cars with low greenhouse gas (GHG) intensity and high fuel efficiency ratings
- **Sustainability linked solutions** - Incentivise positive change by offering access to preferential interest rates based on sustainability performance including ESG-linked Revolving Credit Facility (RCF) and ESG-linked Supply Chain



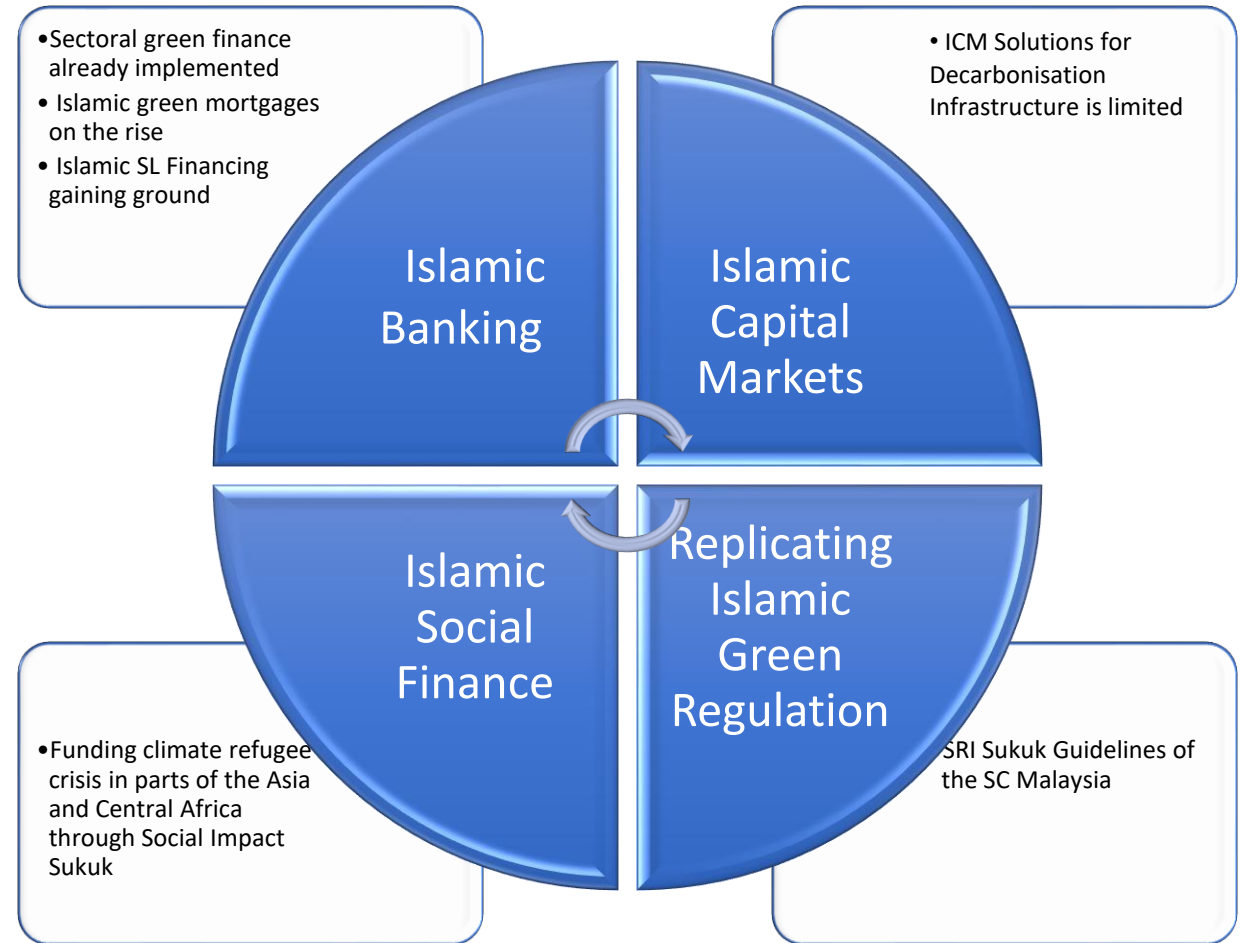
Capital Markets

- **Green bonds** - Funding projects with positive environmental or climate impact
- **Climate bonds** - Financing projects needed to address climate issues
- **Transition bonds** - Funding decarbonisation strategies
- **Low carbon ETFs** - Instruments that invest into companies that meet low carbon emission criteria
- **Private equity infrastructure fund** - Unlisted, closed-end funds investing in renewable infrastructure projects
- **Alternative financing** - Alternative fundraising via equity crowdfunding (ECF) and peer-to-peer (P2P) financing



Insurers

- **Green motor insurance** - Insurance incentives offered on motor vehicles that help reduce greenhouse gases emissions
- **Green housing insurance** - Facilitate use of renewable materials or energies in homes or buildings
- **Green insurance for business** - Insurance incentives for businesses that use alternative materials or energy i.e. Pay as You Drive to track miles driven in your car, installing "green" building systems and materials and coverage for "green" certified rebuilding
- **Green technology** - Insurance to provide risk protection for new green technology such as solar, wind-turbine, energy efficiency technology to help mitigate the risks associated with newly emerging technologies



Embedding climate change criteria in Shari'ah Compliance assessments to encourage Islamic Finance support

Strengthening Shari'ah governance and Shari'ah risk to integrate decarbonisation guidelines

Encouraging innovation in green Islamic products, incentivising, empowering and enlightening

Standardising maqasidic dimensions in the quest for net zero, and encourage disclosure

Benchmarking, adapting and improving traditional offerings

Thank you