



Accelerating Labuan IBFC's Sustainability Maturity

Conceptualising Sustainability

The disruption brought about by the pandemic recently is an urgent call for countries across the globe to transition into a sustainable economy. As this global move gathers momentum and response to climate change risks becomes more dire; regulators have started to introduce requirements which focused on long-term sustainability. This is to preserve and enhance market efficiency and economic prosperity; both for the immediate and longer-term horizon.

The financial sector, in general, and financial institutions (FIs), specifically, are key movers and shakers of an economy which can create and push for sustainability impetus within a particular market. In fact, the international commitments from the Paris Agreement have exerted mounting pressures for FIs to integrate sustainability principles into their decision-making processes and practices in the international business landscape. As a result of the enactment of the Paris Agreement, countries undertook serious efforts to

address climate change to better manage its effects. These initiatives include rendering of enhanced technical support to developing countries which are initiating sustainability efforts. In addition, the establishment of The Network for Greening the Financial System (NGFS) was a similar effort aimed at fostering cross-border collaborations amongst member central banks and supervisory authorities. The NGFS enables sharing of best practices and methodologies on sustainability policy which would promote the integration of climate-related considerations into FIs' decision-making.

In other ways, FIs can improve their risk management, increase competitiveness, and achieve long-term financial success, by embracing sustainable practices and business models. As depicted in Diagram I, these practices are built upon three-pronged sustainability foundations - the environmental, social, and economic pillars which are intended to:

- Benefit and preserve the current circumstances; and
- Ensure a meaningful and resilient legacy for generations to come.



Diagram I: Sustainability Pillars

Regulations are integral to building up the transparency and integrity of a sustainable finance market. This would not only boost investor confidence but also provide greater transparency on fundamental standards to be adhered by the market. It enables better tracking and measurement of sustainable finance flows to avoid and prevent greenwashing malpractices. The role of sustainable finance is crucial to drive a more sustainable and equitable economy by mobilising capital towards investments that generate both financial returns and positive environmental and social impact. On this note, the Environmental, Social and Governance (ESG) perspective is a typical framework in developing a sustainable financial ecosystem. It serves as a cornerstone of ethical conduct by instilling transparency, accountability, and resilience within a financial market.

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The Asian Sustainability Agenda

With the growing sustainability drive across the globe, the same wave has also swept across Asia, particularly with ASEAN countries beginning to effect comprehensive sustainability initiatives within their respective markets. Diagram II provides an insight into the ASEAN initiatives on sustainable practices which are progressing at varying speeds and momentum:

ESG Policy Framework

- The Philippines shows the highest value in adopting the Policy Framework despite its vulnerability to climate risks due to its geographical location.
- Malaysia, Indonesia and Singapore have also solidified their position by committing towards achieving a low-carbon and climate-resilient economy.

ESG Investment Framework

- The Philippines, Singapore and Malaysia are the top three in performing the ESG Investment Framework.
- In December 2023, the Monetary Authority of Singapore launched the Singapore-Asia Taxonomy for Sustainable Finance, the first taxonomy to pioneer the concept of a 'transition' category tailored to the needs of the Asian region.

The Report is conducted between October 2022 and June 2023 and was measured using a checklist approach which consists of the following:

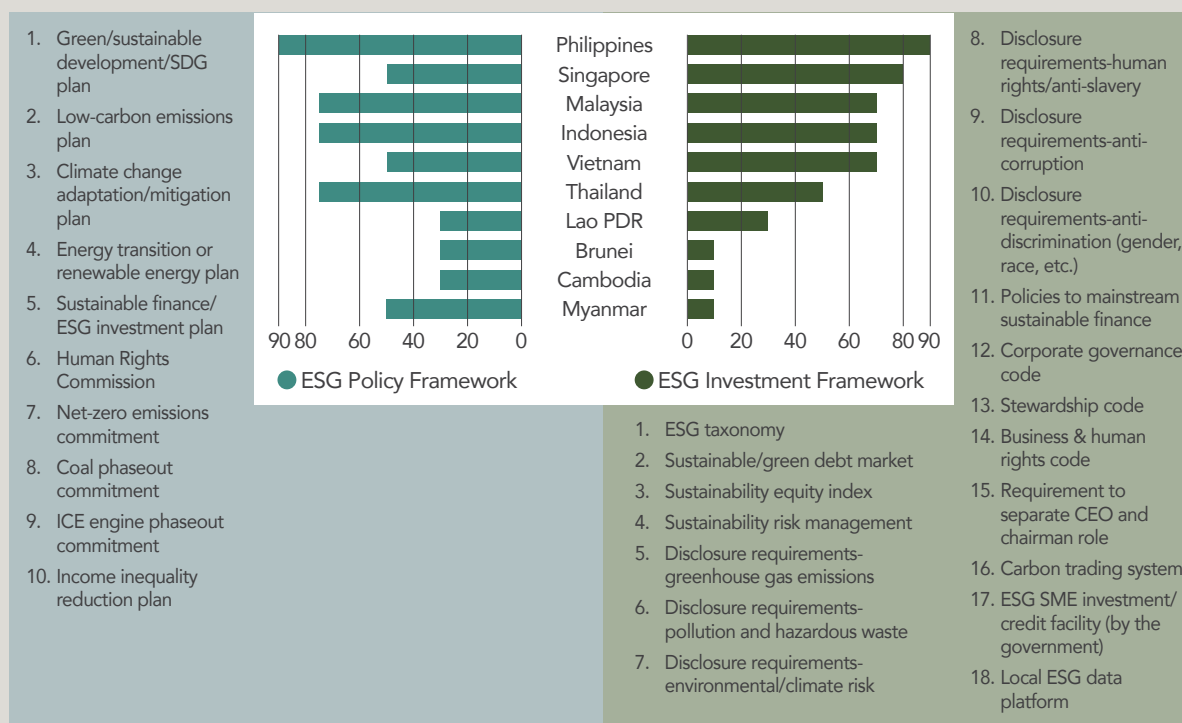


Diagram II: ASEAN Initiatives on Sustainable Practices¹

¹ Modified from the ESG Practices in ASEAN and Korea: Pathways towards sustainability, 2023

In the world of sustainability, one word that has dominated a lot of conversations is taxonomy. In simple terms, taxonomy is a dictionary of sustainable activities. It is designed to steer companies as they adapt their business strategies to climate change, as well as classify their activities based on their environmental performance. Taxonomies serve as foundational frameworks by facilitating investors and FIs to identify and evaluate sustainable investments more easily.

The European Commission has published its Sustainable Finance Taxonomy, serving as a significant reference point for other taxonomies. In ASEAN, Malaysia was the first country to publish a taxonomy in 2021 followed by the ASEAN Taxonomy Version 1.



Sustainable Finance Taxonomy: Regulation 2020/852, June 2020
ASEAN Taxonomy Version 1, November 2021
ASEAN Taxonomy Version 2, March 2023

Diagram III illustrates the flavour of sustainability taxonomy adopted across the ASEAN region:



Diagram III: Taxonomies Development in ASEAN Countries

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Kickstarting with Labuan IBFC's Sustainability Taxonomy

As a midshore centre within the region, Labuan IBFC has a role to play to intermediate, grow and promote a sustainable financial market alongside the broader Asia's sustainability agenda. It is indispensable for the Centre to fulfil the Asia ESG needs and support Malaysia's sustainability game plan. This will confer opportunities for the Centre to refine its reputation as a market that promotes long-term viability, and contributes towards national and regional sustainability goals. In this regard, Labuan FSA is guided by two main thrusts as outlined in Diagram IV:

- Firstly, fostering ESG Market Enablers; and
- Secondly, inculcating ESG cultures and best practices.



Diagram IV: ESG Initiatives for Labuan IBFC

To kick-start the sustainability culture within the Centre, Labuan FSA has issued the Sustainability Taxonomy to the market for their feedback aimed at providing Labuan financial institutions (LFIs) with the means of identifying and classifying activities that are deemed as “green” or “green-transitioning”. The operational mechanism of the Sustainability Taxonomy involves classifying economic activities based on their environmental and societal impact. It lays out the parameters for LFIs to identify and develop innovative and sustainable financial products and instruments, and align LFIs’ decision-making towards green or sustainable goals. The assessment steps under the proposed Labuan IBFC’s Sustainability Taxonomy are reflected in Diagram V:

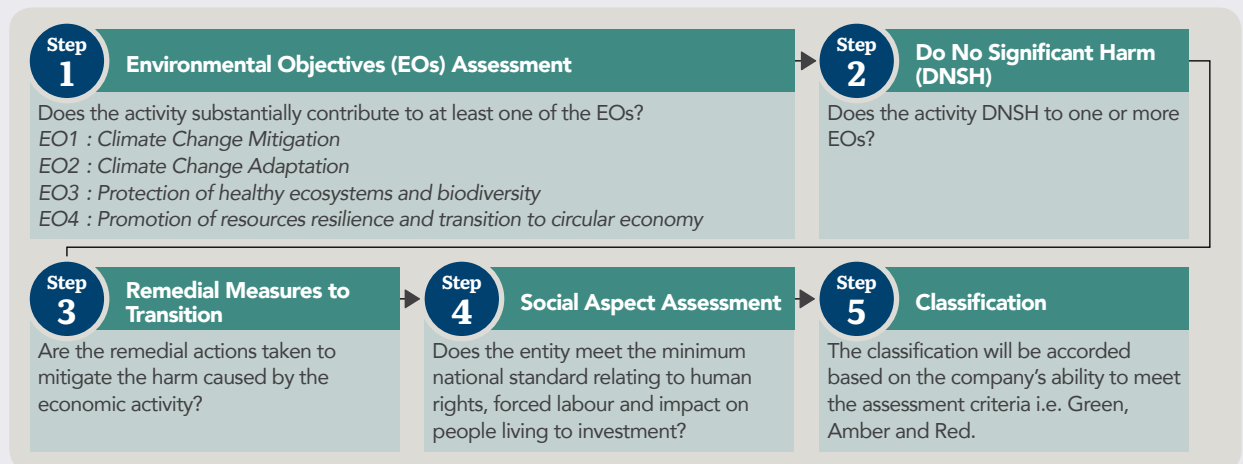


Diagram V: Sustainability Taxonomy Assessment

There are three levels of economic activity classification provided under the Sustainability Taxonomy. The criteria for each category are elaborated under Diagram VI as follows:

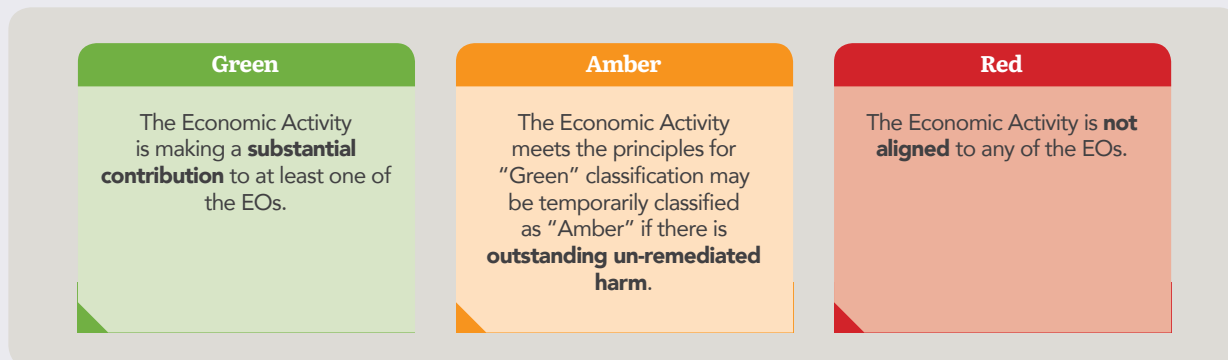


Diagram VI: Color-coded classification of economic activities

Striding Forward

Sustainability is vital as financial institutions are expected to operate in an ethical and sustainable manner, and consumers have been increasingly demanding sustainable financial products and services. By embracing sustainable practices and investing in sustainable business models, LFIs can reap the benefits through:



Labuan FSA is committed to creating a sustainable midshore market that promotes embedment of ESG principles into Labuan FIs' business activities. In transforming the Centre into a sustainability hub, several key initiatives will be rolled out through close collaboration with the Labuan financial industry and other key stakeholders for capacity building and policy implementation. With a conducive ecosystem, Labuan IBFC has and will continue to attract investors, financial institutions, and businesses, especially within Asia.