Sector Update

Research Team

Singapore Banks – Proposed guidelines for a green transition

Singapore Equities

ESG – Greening the Recovery

Investment highlights

The industry taskforce GFIT (Green Finance Industry Taskforce) convened by the Monetary Authority of Singapore (MAS) has issued a proposed taxonomy to support Singapore-based financial institutions in their identification and classification of green activities (https://www.mas.gov.sg/news/media-releases/2021/industry-taskforce-proposes-taxonomy-and-launches-environmental-risk-management-handbook).

A "traffic-light" system has been introduced (green, yellow/in transition and red) to group activities according to the extent they may align with environmental objectives. A key feature in the proposed guidelines is the inclusion of transition activities towards a greener and more sustainable path for institutions, which takes into consideration starting positions and supports inclusive economic and social development. The taskforce has invited feedback on the classification guidelines (insert link), which will *close by 11th March 2021*.

Overall, the MAS has a vision for Singapore to become a leading green finance centre in Asia and is taking active steps to promote sustainable financing, which includes engaging financial institutions to consider ESG criteria in decision making process, supporting the adoption of industry standards, collaboration with counterparts to implement best practices and developing the green bond market in Singapore. MAS' Green Finance Action Plan estimates Asean as a region could provide a potential ~USD200bn per year opportunity for green investments until 2030, which should contribute towards loans demand and profitability of the banking sector. Given that the financial industry is expected to play an important enabling role in catalysing sustainable and green finance in the broad transition towards a low carbon economy, we expect increasing focus and corporate disclosures on this front over time.

In terms of sector progress on ESG initiatives, Singapore banks have included responsible financing principles into their credit approval processes, and ceased the financing of coal fired power plants in 2019. For crude palm oil loans, our understanding is that DBS has reduced its financing scope to RSPO/NDPE certified customers, while UOB does not finance greenfield plantations anymore. Governance metrics are viewed to be robust across the sector, as per latest ESG rankings by MSCI, although UOB has a marginally higher staff attrition rate vs peers. One challenge for the sector we see is the relatively limited renewable energy options in the country, which suggests banks will likely need to reach out to the broader region in order to grow the sustainable financing portion of the book more meaningfully. Within Asean, Singapore banks have already committed to support the TCFD (Task Force on Climate-Related Financial Disclosures, comprises of more than 500 leading corporations) which started in 2015 with the objective of developing and supporting better voluntary disclosures of climate change related financial risks.

Vision to become a leading green finance hub in Asia

The GFIT's mandate to speed up the development of green finance in Singapore aims to develop a more climate resilient and environmentally friendly financial system with close partnership between public-private institutions and collective action across sectors required. Key GFIT initiatives were identified as follows:

1) Develop a taxonomy
2) Enhance environmental risk management practices of financial institutions
3) Improve disclosures
4) Foster green finance solutions

Following the MAS' guidelines published in 2020 encouraging the banking sector to move towards a greener business model, GFIT has also released a handbook on best practices for environmental risk management for asset managers, banks and insurers (https://abs.org.sg/industry-guidelines/responsible-financing). Technological solutions will be explored to support financial institutions in improving the quality of their climate related disclosures, with pilot innovations targeted to solve current challenges to mobilize green finance across sectors.

The next steps will involve work on a combination of principle-based criteria and quantifiable thresholds for activities, to guide financial institutions in their implementation of the taxonomy. GFIT will be partnering industry bodies to hold workshops to raise awareness and help financial institutions improve on their environmental risk management capabilities.

Increasing ESG/climate-related focus

As per the Paris Agreement, Singapore has committed to cap its peak carbon emissions by 2030 at 65 million tonnes of CO_2, which will be further reduced by half by 2050 with the goal of achieving net-zero emissions in the second half of the century. The government has noted in the past that around three quarters of industrial carbon emissions came from the refining and petrochemical sector.

In the Singapore context, as per data from the Meteorological Service Singapore, the mean surface air temperature has increased by about 0.25 degree Celsius per decade on average, which is more than twice the trend in global temperatures, with the key uptick in temperatures observed to have started from mid-1970s as the country's urbanization transformation accelerated. Other well documented concerns on Singapore's vulnerability to climate changes include the country's vulnerability to rising sea levels given that a third of the country's land area considered as low-lying (i.e. within five metres above sea level), limited natural water resources and health impact from climate changes.

Source: Monetary Authority of Singapore

MAS' vision on sustainable finance & implications for banks

The MAS has cited a vision to become a leading green finance centre in Asia and is taking active steps to promote sustainable financing, which includes engaging financial institutions to consider ESG criteria in decision making process, supporting the adoption of industry standards, collaboration with counterparts to implement best practices and developing the green bond market in Singapore.

The financial industry will play an important enabling role in catalysing sustainable and green finance in the broad transition towards a low carbon economy. MAS has defined sustainable finance as the practice of integrating environmental, social and governance (ESG) criteria into financial services to bring about sustainable development outcomes, including mitigating and adapting to the adverse effects of climate change. This includes a process of considering environmental, social and governance (ESG) factors when making investment decisions, which supports increased long-term investments in sustainable economic activities. Relevant issues include climate and environmental impact (such as protecting biodiversity, preventing pollution etc) and social concerns (inequality, promoting access through financial inclusiveness, communities, investment in human capital and human rights issues).

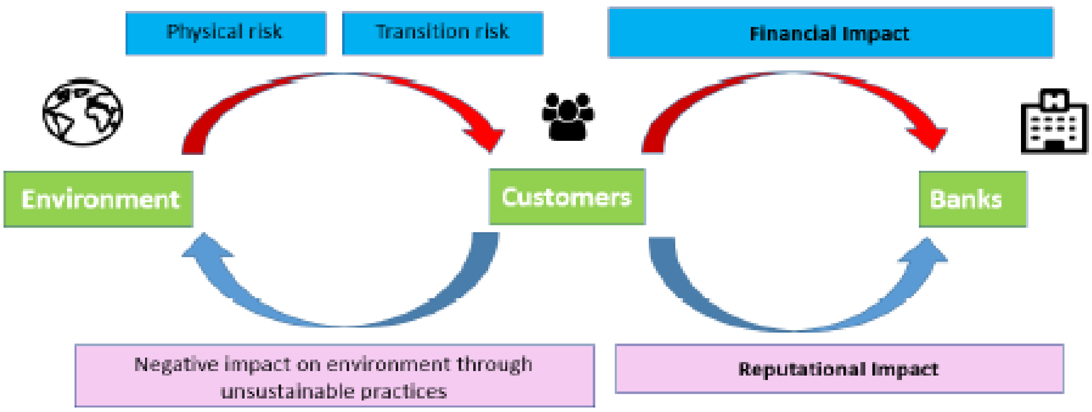
The MAS' Green Finance Action Plan estimates Asean as a potential ~USD200bn per year opportunity for green investments until 2030, which should contribute towards loans demand and support profitability of the sector. Institutions are encouraged to consider ESG criteria in their decision making and adopt industry guidelines, while other efforts include the development of the green bond market. In MAS' June 2020 consultation paper on environmental risk management, climate change was one of the key concerns given the relevance globally and on a national level. It will be increasingly crucial for banks to consider environmental risks during their credit lending decision making process (e.g. extreme weather conditions could impact property values that serve as bank collateral) which could also lead to reputational concerns. Hence, the guidelines require that senior management is involved to oversee environmental risk, and risk factors are considered within a bank's risk appetite. This suggests that the future financing of carbon-intensive sectors is likely to see increased attention as the move to a low carbon economy progresses.

Source: Monetary Authority of Singapore

Singapore banks: Recent sustainable financing disclosures & ESG scores

Singapore banks have included responsible financing principles into their credit approval processes, and have ceased the financing of coal fired power plants in 2019. For crude palm oil loans, DBS has reduced its financing scope to RSPO/NDPE certified customers, while UOB does not finance greenfield plantations anymore. Governance metrics are viewed to be robust across the sector, as per ESG rankings by MSCI, although UOB has a marginally higher staff attrition rate vs peers. One challenge for the sector is the relatively limited renewable energy options in the country, which suggests banks will likely need to reach out to the region in order to grow the sustainable financing portion of the book more meaningfully. Within Asean, Singapore banks have committed to support the TCFD (Task Force on Climate-Related Financial Disclosures, comprises of more than 500 leading corporations) which started in 2015 with the objective of developing and supporting better voluntary disclosures of climate change related financial risks.

Potential financial and reputational impact of environmental risk on banks

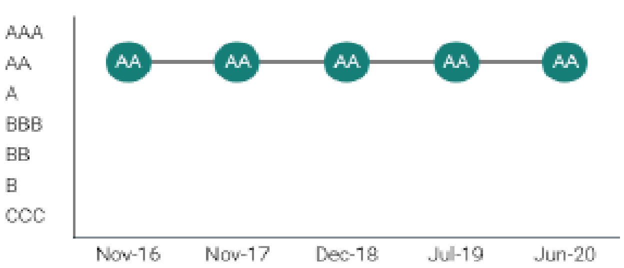


Source: Monetary Authority of Singapore

DBS Group Holdings (DBS SP): Hold, fair value SGD27

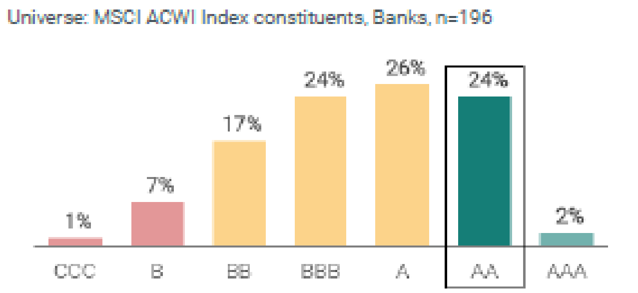
MSCI's "AA" ESG Rating for DBS pegs the bank at the higher end of industry peers, due to its relatively robust corporate governance practices and financial inclusion initiatives (digitalization strategy focused on small medium enterprises and underbanked segment) and a majority independent board (~72.7% of board are non-executive and independent of management, which supports more effective oversight of risk management). Board diversity as of November 2020: Male 72.7%/Female 27.3%.

ESG Rating history



ESG Rating history shows five most recent rating actions

ESG Rating distribution



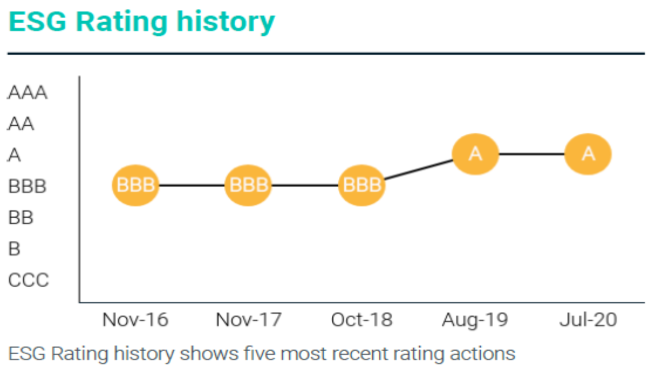
Sources: MSCI, Bank of Singapore

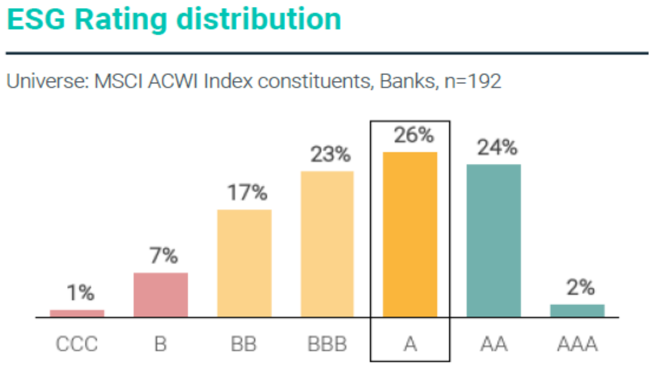
Key highlights

- 2017: Made progress in formalizing ESG risk management programs within its overall credit assessment and capital market policies. Trained relationship managers and credit risk offers on ESG risk assessment to support the enhancement of its overall credit risk assessment scope. Released DBS Green Bond Framework and issued first green bond. Proceeds from the issuance was deployed towards the financing of the Marina Bay Financial entre Tower 3, which was certified Green Mark Platinum by the BCA.
- 2018: Launched its first sustainability linked loan in Asia. Promotes sustainable development by pegging interest rates of loans to a series of ESG metrics that are pre-determined, which allows for lower interest rates if targets are reached (https://www.dbs.com/sustainability/responsible-banking/sustainable-financing/sustainable-linked-transactions?pid=sg-group-pweb-sustainability-sustainability-linked-transactions). Companies it has collaborated with on such loans include Fortune REIT, Swire Pacific, CDL, CapitaLand and Wilmar.
- April 2019: First green loan financing in Singapore for new property developments – Extended a three year green loan of SGD400million to City Developments to finance eligible new green developments (as defined in CDL green finance framework) in Singapore and abroad, this came after CDL's inaugural green bond issuance in 2017 of about SGD100million, which was then allocated to initiatives to enhance energy and water efficiency at its flagship office building in Republic Plaza.
- November 2019: Became a signatory to Equator Principles, an indication of improvement in environmental strategies over project finance loans. While there had been stakeholder opposition in the past to funding of palm oil extraction business, the bank has taken several steps on this front which included the adoption of mandatory requirements for all new lending relationships in the sector to demonstrate alignment with international standards (including No Deforestation, No Peat & No Exploitation/NDPE and Roundtable on Sustainable Palm Oil/RSPO certification).
- Dec 2019: Teamed up with UOB and Standard Chartered Bank (Singapore) to extend an SGD945mn green loan to Allianz Real Estate and Hong Kong private equity firm Gaw Capital Partners to finance the SGD1.575bn joint acquisition of Duo Tower and Duo Galleria (mixed use project in Singapore's Ophir-Rochor precinct) from M+S (national joint venture between Singapore and Malaysia).
- 1H 2020: DBS extended ~SGD4bn of ESG related loans, and ~SGD4.5bn of green and social bonds. May 2020: Green club loan of SGD730mn issued with OCBC Bank & ICBC Singapore Branch for construction of a luxury residential & commercial development at Tan Quee Lan Street (development was a joint venture between GuocoLand and two other subsidiaries of Hong Leong Holdings and marked GuocoLand's first green loan and the industry's largest green loan for a development project in Singapore. Loan proceeds would also finance efforts in adopting immersive urban greenery and landscaping, water and energy conservation.
- June 2020: Launched a sustainable and transition finance framework and taxonomy to support clients, which classifies activities into green/transition/contributing to UN sustainable development goals and provides a list of eligible economic activities. Tiered pricing to provide incentive for pursuing sustainable targets were incorporated in sustainability-linked loans.
- August 2020: SGD40mn facility provided to support the construction of a floating solar photovoltaic system on Tengeh Reservoir (Tuas) which will be completed in 2021 and will be Singapore's first single large floating solar PV system (https://www.straitstimes.com/singapore/tengeh-reservoir-to-house-one-of-worlds-largest-floating-solar-panel-systems).
- November 2020: First issuance by a Singapore bank in India - Issued its first two green loans in India ~Rs10.5bn to CapitaLand to refinance construction financing for development of Phase 1 of International Tech Park Gurgaon and International Tech Park Chennai projects.
- Aims for ~SGD20bn sustainable financing by 2023 (vs ~SGD362bn of total loans in FY19).

United Overseas Bank (UOB SP): Buy, fair value SGD26.30

MSCI's "A" ESG Rating for UOB pegs the bank below DBS but still at the higher end of industry peers. Key positive factors supporting the stable "A" ESG rating include its strong governance performance, specifically pertaining to board structure (majority independent board, separate CEO and chairman roles helps management oversight) and alignment of its accounting and pay practices with shareholder interests. UOB also has a dedicated, majority independent risk committee to help in overseeing risk-taking behaviour among senior decisionmakers. Concerns include a higher than average employee attrition levels (17.8% in 2019 vs. the industry average of 10%), likely implying potential weaknesses in human capital management. Board diversity as of November 2020: Male 90.9%/Female 9.1%.





Sources: MSCI, Bank of Singapore

Key highlights

- 2018: The bank set up a dedicated ESG Committee, a senior management committee that reports directly to the Management Executive Committee (MEC) on the Group's sustainability matters, which helps ensure that ESG factors are given due consideration in all aspects of its operations. The committee members represent the Bank's business and support units, and through their activities, seek to address the potential risks and effects of our operations in relation to the economy, environment and society. Activities performed include the review of material ESG topics, identification of risks and opportunities, evaluation of emerging issues, collation and assessment of relevant data, monitoring of progress of sustainability-related programmes and initiatives.
- 2019: Increased its financing of green projects (renewable energy, energy efficiency, green transport infrastructure, water and waste management). Launched a real estate sustainable finance framework aligned to the Singapore Building Construction Authority (BCA)'s objective of achieving 80% of buildings certified green by 2030. Loans disbursed from this included those supporting specific energy efficiency features and rooftop solar panels. Further disbursement in 2020 included projects that had been certified "Green Mark Platinum" building by the BCA.
- December 2019: Teamed up with DBS and Standard Chartered Bank (Singapore) to extend an SGD945mn green loan to Allianz Real Estate and Hong Kong private equity firm Gaw Capital Partners to finance the SGD1.575bn joint acquisition of Duo Tower and Duo Galleria (mixed-use project in Singapore's Ophir-Rochor precinct) from M+S (national joint venture between Singapore and Malaysia).
- 1H of 2020: ~SGD8bn of total sustainable financing extended (included green/sustainability linked loans and financing for green certified buildings).
- February 2020: Issued the largest green loan (SGD237mn) for any hotel property in Singapore form a single financial institution to Park Hotel Group (marking the group's first green loan) for refinancing the Grand Park City Hall (343-room luxury hotel with Platinum Green Mark, which is the highest rating in Singapore's green building rating system) as part of a mixed use lifestyle precinct with energy and waste consumption reduction measures including a rainwater harvesting system, centralised chilled water system and high performance air to water heat pump and mechanical ventilation fans.
- Aims for ~SGD12bn sustainable financing by 2023 (vs ~SGD269bn of total loans in FY19).

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Co.Reg.no.: 198301152E
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