

Building Resilience: Sustainable Financing in Emerging Markets

The global response to COVID-19 bears witness to the power of collective action, and how technology can be mobilized to garner and streamline efforts across sectors, including health, education, telecommunication, and more. The pandemic has also exposed how vulnerable and fragile our economy can be; in a matter of months, hundreds of thousands of people died, millions of jobs were lost, and livelihoods shattered. Leading international organizations project global gross domestic product (GDP) growth for 2020 to range between -8.8% and 1%, and the number of those living in extreme poverty to increase by 420 million people.¹ In the wreckage left behind by the coronavirus pandemic, sustainable finance is all the more crucial in paving the way from devastation to recovery.

The next decade presents a 'use it or lose it' moment for emerging markets to reorient the financial sector towards building a more sustainable and resilient future. Investments in infrastructure are expected to reach US\$90 trillion by 2030 to meet the needs of increased populations around the world, and COVID-19 has urged governments to provide large stimulus packages.² This places greater emphasis on the need to invest with a view of environmental, social and governance (ESG) issues, and not just traditional finance metrics. Indeed, for low and middle-income countries, returns on responsible investment is high, amounting to US\$4 on every US\$1 spent on resilient infrastructure.³ Moreover, The Sustainability Report by Morgan Stanley analyzed the performance of more than 10,000 mutual funds to find that sustainable equity met or exceeded median returns of traditional equity 64% of the time.⁴ This proves that there need not be a trade-off between

¹ UNIDO. 2020. *Coronavirus: The Economic Impact*. <https://www.unido.org/stories/coronavirus-economic-impact-4-may-2020>

² The Global Commission on the Economy and Climate. 2016. *The Sustainable Infrastructure Imperative: Financing for Better Growth and Development*. <https://www.un.org/pga/71/wp-content/uploads/sites/40/2017/02/New-Climate-Economy-Report-2016-Executive-Summary.pdf>

³ Hallegatte, S., Rentschler, J. and Rozenberg, J.. 2019. *Lifelines : The Resilient Infrastructure Opportunity*. *Sustainable Infrastructure*. Washington, DC: World Bank. <https://openknowledge.worldbank.org/handle/10986/31805>

⁴ Morgan Stanley. 2015. *The Business Case for Sustainable Investing*. <https://www.morganstanley.com/ideas/business-case-for-sustainable-investing>

financial and non-financial returns. In fact, ESG investments have a higher potential for long term payoffs. As the current pandemic forces a more prudent management of financial resources, sustainable investment options by governments, investors and corporations need to be prioritized.

Sustainable finance is not confined to environmental-linked investments, but extends to all financial products and services that integrate ESG criteria into its decision processes, policies, frameworks, and practice. It is about reducing the financial gap in meeting SDGs to solve major and global problems such poverty, inequalities, and climate change. Seven trends in sustainable finance will transform the future landscape of ESG in emerging markets:

- (1) **Increasing commitments to address climate change.** In order for nations to prevent irreversible damage and stay at the current 1.5 degrees of global warming, global emissions must drop by 50% over the next decade.⁵ A growing green bond market has emerged to help investors align their financial objectives with real economy impact, and to achieve the targets of the Paris Climate Agreement and Sustainable Development Goals. One example is the Real Economy Green Investment Opportunity GEM Bond fund (REGIO) created by HSBC Global Asset Management and leading Development Finance Institutions (DFIs). The fund has raised US\$474 million and aims to aid investors in emerging economies to achieve the long-term SDGs.⁶
- (2) **Intensifying interest in the importance of ESG investment and disclosure.** Making, assessing and managing investments based on ESG factors is gaining momentum worldwide. In 2018, 80% of the world's largest corporations used Global Reporting Initiative (GRI)

⁵ UN Environment. 2019. *Emission Gap 2019 Global Progress Report on Climate Change*.
<https://www.unenvironment.org/interactive/emissions-gap-report/2019/>

⁶ HSBC. HSBC Real Economy Green Investment Opportunity Global Emerging Market. .
<https://www.assetmanagement.hsbc.co.uk/en/institutional-investor/investment-expertise/fixed-income/regio>



standards.⁷ In 2020, the Dubai Financial Market (DFM) launched the UAE Index for Environment, Social and Governance (ESG) to encourage listed companies in the UAE to embrace ESG best practices.⁸

- (3) **Minding the gap through innovative financing.** The financing gap to achieve sustainable development goals (SDGs) by 2030 is US\$2.5 trillion annually.⁹ The challenging landscape of sustainable financing in emerging markets has given space for innovative financing to develop. An example of this is the South African Impact Bond Innovation Fund, which is the first social impact bond focusing on early childhood in the Global South.¹⁰ Another example is Majid Al Futtaim's first Green Sukuk in the MENA region with a value of US\$600 million.¹¹
- (4) **Banks stepping up sustainability- and green-linked loans.** Banks have been increasingly tying loan terms to ESG performance; sustainability-linked loans totaled US\$71.3 billion in the first three quarters of 2019.¹²
- (5) **The quest for data. Sustainable investments require data based on ESG metrics.** However, companies lack adequate and useful data to quantify and measure the impact of their investments, leading to potential inefficiencies. Early this year, Refinitiv launched the Future of Sustainable Data Alliance with the objective of accelerating capital inflows into

⁷ Kell, G. 2018. *The Remarkable Rise of ESG*. Forbes. <https://www.forbes.com/sites/georgkell/2018/07/11/the-remarkable-rise-of-esg/#5c97a3f51695>

⁸ Khan, S. 22 April, 2020. "DFM Launches Index to Gauge UAE List Companies' Commitment to ESG". The National. <https://www.thenational.ae/business/markets/dfm-launches-index-to-gauge-uae-listed-companies-commitment-to-esg-1.1009774>

⁹ Cooper, S. 05 February 2019. *The Evolution of Sustainable Finance*. <https://www.sc.com/en/feature/the-evolution-of-sustainable-finance/>

¹⁰ *ECD Impact Bond Innovation Fund*. Innovation Edge. <https://innovationedge.org.za/project/ecd-impact-bond-innovation-fund/>

¹¹ Majid Al Futtaim. 15 May, 2019. "World's 1st Benchmark Corporate Green Sukuk". <https://www.majidalfuttaim.com/en/media-centre/press-releases/2019/05/majid-al-futtaim-lists-world-s-first-benchmark-corporate-green-sukuk--on-nasdaq-dubai>

¹² Guzman, D. 21 October, 2019. *Growth in Sustainability-linked loans boosts ESG rating firms*. Reuters. <https://www.reuters.com/article/growth-in-sustainability-linked-loans-bo/growth-in-sustainability-linked-loans-boosts-esg-ratings-firms-idUSL2N27615Y>



sustainable finance by providing investors and governments the data needed to assess and identify sustainable investments and products.¹³

- (6) **The quest for taxonomies, regulations, and legislations. Regulations and legislations are considered key drivers to sustainable finance in emerging markets.** Until 2018, sustainable financing was regulated in China only.¹⁴ Increased attention has been given to establishing and standardizing regulations and guidelines that foster capital inflows to sustainable finance. Examples of measures taken by some emerging markets include Indonesia's Green Finance Roadmap, the Banco Central Do Brasil's voluntary requirements for banks to monitor environmental risks, and the UAE's first set of guiding principles on sustainable financing.¹⁵
- (7) **Refocusing sustainable financing post COVID-19.** The recent pandemic has shifted the nations' focus to acute social risks such as health and employment. There is no doubt that economic recovery is a priority for all nations with sustainability and building resilience at its core. It is crucial to keep in mind that the comeback from COVID-19 will take years –the same years that are crucial to ensuring we meet our SDGs and climate change targets and prevent an irreversible catastrophe.

¹³ Evans, M. 29 January, 2020. *New data alliance to drive sustainable finance*. Better Society Network.
<https://bettersociety.net/future-data-sustainable-alliance.php>

¹⁴ Meskin, M. 04 February 2020. *Give us regulation say MENA green leaders*.
<https://www.globalcapital.com/article/b1k62slw8c0zz8/give-us-regulation-say-mena-green-leaders>

¹⁵ Berensmann, K. et al. 23 January, 2020. *Fostering sustainable global growth green finance- what role for G20?* G20 Insights.
https://www.g20-insights.org/policy_briefs/fostering-sustainable-global-growth-green-finance-role-g20/