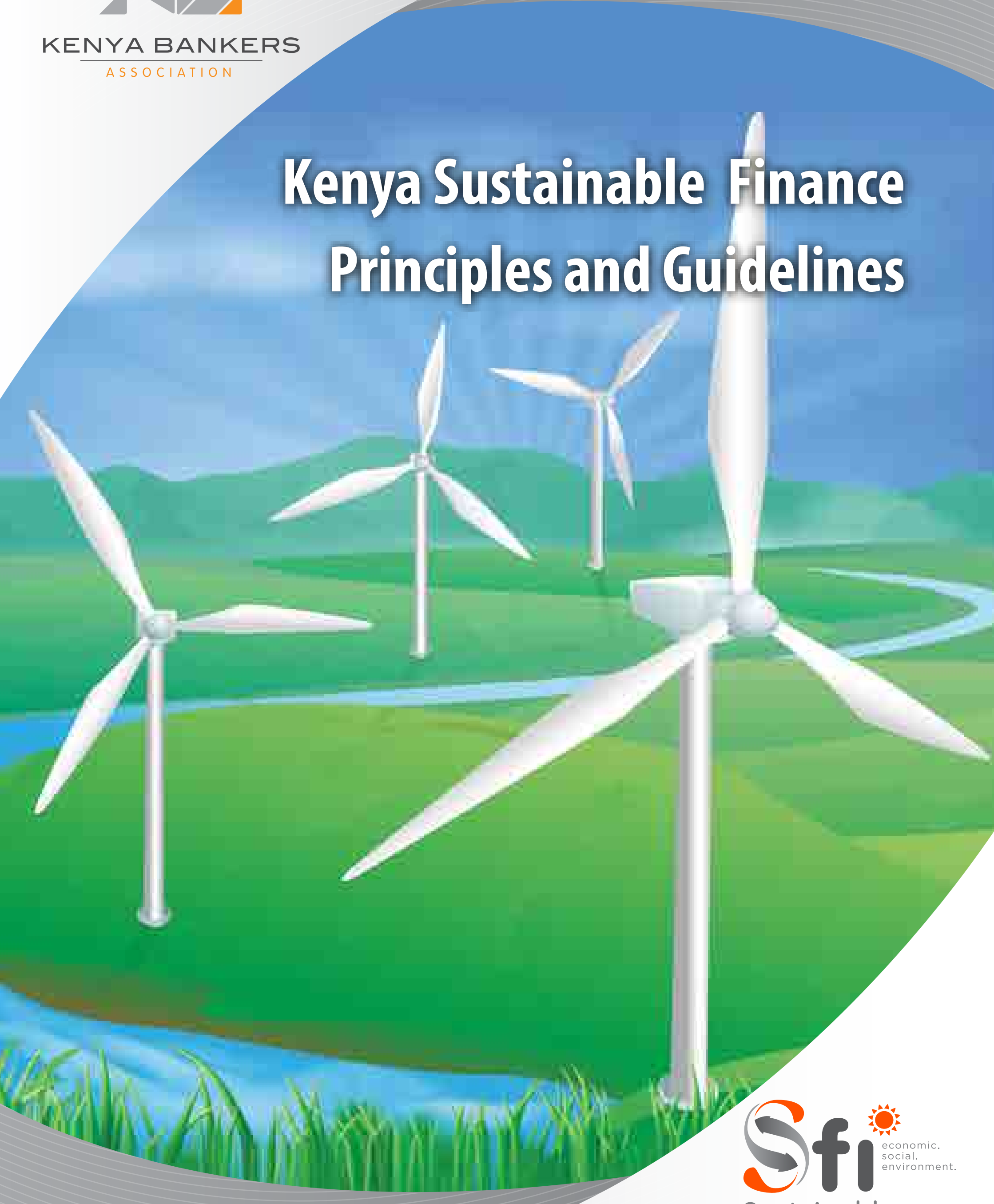
KENYA BANKERS
ASSOCIATION

Kenya Sustainable Finance Principles and Guidelines



Sfi
economic.
social.
environment.

Sustainable
Finance Initiative

A Publication of Kenya Bankers Association

Author: Nuru Mugambi

Editor: Washington Akumu

Design and Layout: Raymond Mabeya

TABLE OF CONTENTS

Foreword

This booklet sets out the theoretical and practical underpinnings behind the quest for the incorporation of sustainable finance principles into local banking practice, under the auspices of the Sustainable Finance Initiative (SFI). Most importantly, the resultant Guiding Principles and Best Practice Standards have been clearly spelt out.

We wish to acknowledge the input of the SFI Working Group which was formed in September 2013, comprising the KBA Secretariat and the 12 banks that volunteered their expertise, and were tasked with the mandate of developing a set of principles to guide the adoption of sustainable finance practices in Kenya's banking industry. This followed a landmark CEO Roundtable convened by the KBA to discuss financial sustainability and find out ways of entrenching the same in the industry.

In this process, the SFI has been keen to ensure that the principles are not only consistent with global best practice, but are also aligned with the risk management policies of individual banks and relevant to the Kenyan and regional context.

It is important to note that KBA's 46 member banks represent not only commercial and microfinance banking activity but also cut across the financial services sector to include the sub-sectors of insurance, investment banking and asset management. Therefore, this body of work would directly contribute to the banking industry as well as the broader financial services sector.

I am thankful to the KBA member banks for having confidence in the Secretariat to spearhead and guide the industry in adopting best practices in Sustainable Finance. I have been privileged to serve as the coordinator of this important work, and look forward to supporting the industry on this journey.

Nuru Mugambi
Secretary – Sustainable Finance Initiative
Director, Kenya Bankers Association

We are proud of the sustained and intensive work the industry has undertaken over the last two years to introduce the principle of sustainable finance in our banks' operations and ensure acceptance and adoption of the same.

KBA is proud to have been in the forefront of this quest whose objective is a banking sector that is not only efficient and profitable, but is also alive to the wider societal concerns of environmental and economic sustainability and social good.

While our members have a critical role to play in the country's development as financiers and facilitators of economic activities, we believe the impact of our contribution greatly hinges on the quality of the decisions we make. Economic viability is vital, but time has come for banks in Kenya and the region to adopt and implement a more inclusive decision-making model that also factors in variables such as environmental impact and social capital in the overall finance equation. KBA's deliberate leadership in the formation of the SFI and the development of the Kenya Sustainable Finance Principles are key milestones in this journey.

KBA's participation in this process was also informed by the industry's desire to make Kenya and the EAC bloc more competitive in the international arena. It is borne out of the realization that for us to win on the global stage, we must be tooled to play by the rules and precepts of other countries and blocs, sustainable banking principles included.

I wish to congratulate the entire SFI structure for a job well done. The SFI Working Group played a crucial role in coming up with the initial recommendations that have ultimately ensured that today, we have Guiding Principles that are attuned to the realities of our East African context. There are also the three Work-streams that have been co-ordinating the various aspects for the SFI, namely Principles and Procedures, Capacity Building and the Green Economy. The import of their input and sacrifice cannot be gainsaid.

Lastly, this work must not end with the distillation and publication of the Kenya Sustainable Finance Principles. The harder, more critical part shall be in ensuring that these guidelines become part of our banking practice in this country and region.

We must make these principles part of our genetic make-up as an industry, as a necessary supplement to existing risk management practice. This is why a structured and sustained Capacity Building program is a key component of our success factors. Such a program must involve all the key players in finance decisions: credit risk managers, business development and strategy heads, operations officers and bank boards.

This work would not have been possible without the support of a number of partners and collaborators who bought into our vision. We thank them. UNEP Finance Initiative (UNEP-FI), DEG (German Investment Cooperation) and Netherlands Development Finance Company (FMO) supported the inaugural CEO Roundtable and have remained committed to the program. We are also thankful for the goodwill received from the Central Bank of Kenya, UN Under Secretary and UNEP Executive Director, Achim Steiner, the IFC (International Finance Corporation) and African Development Bank.

Habil Olaka
KBA Chief Executive Officer

The development of the Kenya Sustainable Finance Initiative by KBA is a watershed in the evolution of our banking industry. It is the first attempt to have a unitary set of principles that banks can rely on to underpin sustainability in their day-to-day operations and decision-making.

While the principle of sustainability is not new among Kenyan banks, its application has always been disparate, uncoordinated and largely at the level of individual institutions.

A recent study commissioned by KBA on the subject showed that there was extant need for a set of "industry-wide" guidelines on sustainable banking. It was the submission of the research that such guidelines apply to all banks and cover all their transactions and operations. The author, Mr. Francis Kariuki, called for sector-specific principles to inform lending decisions involving key sectors such as agriculture, tourism, energy and manufacturing.

The formulation and issuance of the Kenya Sustainable Finance Principles could not have come at a more opportune moment. Since the coming into force of the new Constitution of Kenya in 2010, financial sustainability is no longer a way to court morality, profit or competitive advantage among peers; it is a constitutional imperative. The Kenyan Constitution expressly requires that development be pursued sustainably by all, and that includes financial sector players.

Under Article 10 (2) of the Constitution, sustainable development is a national value and principle of governance, binding every person and state organ. Moreover, Article 69 (2) places an obligation on every citizen to cooperate with state organs and other persons to protect and conserve the environment and ensure ecologically sustainable development and use of natural resources.

While most banks have relied on their traditionally strong suites of corporate social investment (CSI) programs as a way of attaining sustainability, and while not taking away from the immense societal good some of these initiatives have spawned all over the country, corporate philanthropy cannot deliver or lead to sustainable development.

These harmonized guidelines present a great opportunity for the wide and uniform adoption of sustainability practices in the activities and operations of KBA members. This will provide a solid foundation for sustainable development in various sectors of our economy, in pursuit of the industry's role as a facilitator of growth, as outlined in Vision 2030, our flagship national blueprint.

And despite the initial cost of compliance, we believe investment in a sustainable finance infrastructure and culture within our financial services sector is sound strategic business. In the long run, as evidenced by institutional memory and recent experience from the rest of our global peerage, successful banks in the marketplace will not just be those that consistently extend financial services to viable businesses. It will be those banks that have attained an optimal balance between the pursuit of profit and shareholder value on one hand and the health of the planet and the welfare of man on the other.

Joshua Oigara
Chairman, Kenya Bankers Association

KENYA BANKERS
ASSOCIATION

One Industry. Transforming Kenya.

Sustainable Finance for Kenya
Banking Industry Commitment Statement

We, the members of the Kenya Bankers Association (KBA) and representatives of the Kenyan Banking Industry, believe that in order to have long-term business success, there is a need to recognize our environmental and social responsibilities while simultaneously meeting our economic responsibilities and financial objectives. We believe that such an approach can enhance innovation, competitiveness and the quality of the credit portfolio of both individual banks and the industry.

We furthermore believe that the financial sector has a key role to play in achieving Kenya's long-term sustainable development goals as outlined in the Kenya Vision 2030. Through the integration of sustainability issues directly into our core business, we can fundamentally contribute to the greening of business and industry, job creation and social inclusion, thus helping society to address sustainability challenges such as social inequity, climate change, resource scarcity and biodiversity loss. We are prepared to take steps to ensure that our investment activities are carried out in line with international best-practices in Sustainable Finance, and with due regards to the Kenyan context.

We, hereby, commit to:

- **Corporate Sustainability**, which means transparently managing our responsibilities for environmental stewardship, social well-being and economic prosperity over the long term, while being held accountable to our shareholders;

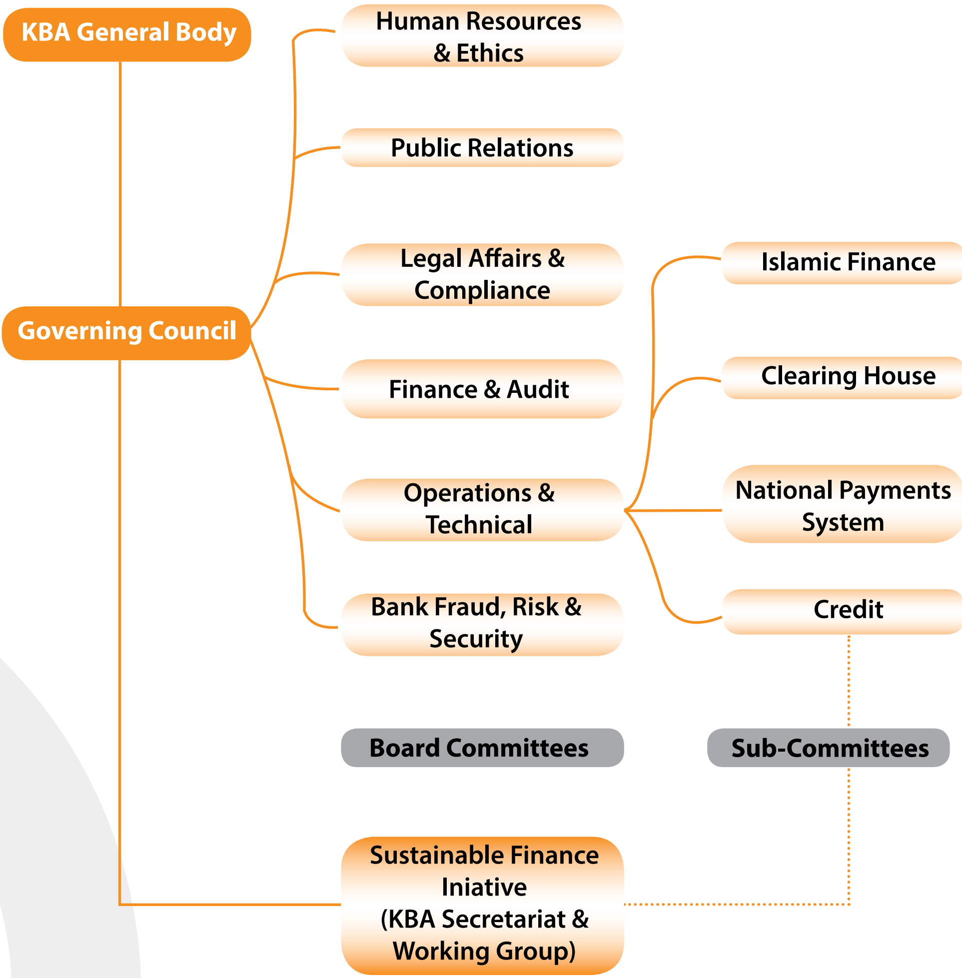
- **Setting up a Working Group (Sustainable Finance Initiative)** to prepare a set of Kenyan Sustainable Finance Principles in the next 12 months, which will be in line with international best practices and consistent with the industry's environmental and social risk management aspirations. The Principles will be relevant to the KBA General Body overall yet responsive to individual banks' credit risk policies. The KBA Secretariat will coordinate the Sustainable Finance Initiative that will report to the General Body via the Governing Council; and

- **Develop Internal Capacity** as required to manage our environmental and social responsibilities, with focus on commercial/ credit risk management.

Version 10 September 2013

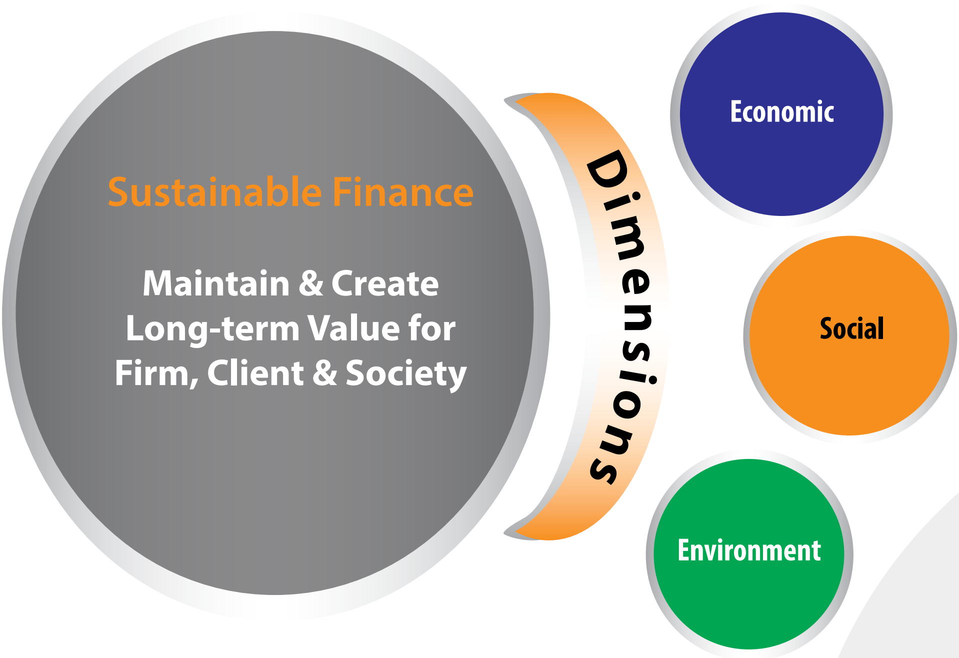
SFI Governance Structure

The Sustainable Finance Initiative (SFI) falls within the KBA Governance structure, reporting to the Governing Council (KBA's Board of Directors).



Defining Sustainability from a Financial Sector Perspective

The process of developing the principles and building industrywide capacity is motivated by the industry's desire to support efforts towards making Kenya and the EAC region more globally competitive. It demonstrates that apart from deepening financial inclusion and contributing towards sustainable economic growth, banks in particular are also concerned about the other challenges that Africa currently faces in the areas of climate change and environmental degradation, social exclusion and resource scarcity.



Defining Sustainable Finance was therefore guided by this ambition and set out to harmonise the divergent views of "sustainability" from a financier's perspective. Economic Sustainability was therefore core, with Social Sustainability and Environmental Sustainability serving as the twin co-focus areas.

Background on Kenya's Sustainability and Role of Financial Services Sector

The role of the financial sector as a facilitator in Kenya's economic development cannot be gainsaid.

It is a role that is recognized and documented in Kenya's flagship economic development blueprint, Vision 2030. Government planners and policy makers would appear to appreciate the fact that the financial sector is a critical player in helping Kenya achieve a sustained 10 per cent-plus growth in GDP, which is the required level to propel the country to middle income status by 2030.

The optimal operation of the financial sector is therefore a key component of Kenya's overall economy.

As currently mobilized, Kenya's financial sector is bank-led, evidenced by their level of invested capital and market engagement in banking activity. It consists of the Central Bank of Kenya (CBK) as one of the regulators, 44 commercial banks and a single mortgage financier. Some seven foreign banks have representative offices in the country, there are nine micro-finance institutions (MFIs), two credit reference bureaus and 101 forex bureaus.

The typical Kenyan bank, besides engaging in commercial banking, is also likely to have units to handle investment, insurance (bancassurance), microfinance, custodial services, private equity ventures and capital raising through the capital markets.

Several parameters can be used to classify Kenyan banks. These include ownership and whether the particular bank is listed on the Nairobi Securities Exchange (NSE). Using shareholding as a differentiator yields three types of banks: foreign owned ones, those with some level of government ownership or those owned by local investors. Among foreign banks, there are those incorporated in other countries; those incorporated in Kenya but partly owned by foreigners and those incorporated elsewhere and fully owned by foreign interests.

Banks continue to make a solid and tangible contribution to the country's economic development in a number of ways. They act as financial intermediaries and also promote financial inclusion and deepening. They are a major employer of all cadres of personnel and also contribute to the Exchequer in the form of taxes. To illustrate the scale of banks' contribution to the economy, they advanced Sh1.78 billion in June 2014, with a material 17.4 per cent going to small and medium enterprises (SMEs). Banks are also major investors in corporate philanthropy, with an allocation of Sh1.4 billion to high-impact corporate social investment (CSI) projects. In 2013, banks paid over Sh37 billion in corporate taxes alone, making the sector one of the highest tax-payers.

With such a heavy involvement in promoting economic development, banks can only be successful and impact optimally if the principle of sustainability is ingrained in their genes. Banks therefore need to stop focusing on financial returns alone, but also give due attention to the economic, social and environmental pillars of development.

Secondly, the pursuit of sustainability can no longer be hinged on voluntarism alone. The Constitution of Kenya expressly requires that development should be pursued sustainably by all.

A benchmark study by the KBA found out that while most banks practice some form of sustainability, adoption remains disparate and lacks a unitary structure. CSI initiatives also tended to be confused with sustainability. And this despite their short-term nature and the fact that they are sometimes largely driven by marketing imperatives. These underlying factors explain the need for a harmonized platform to assist banks incorporate sustainable finance principles into their operations. The study also called for a regulator to enforce compliance through incentives and sanctions while at the same time tracking progress on implementation of sustainability principles. Use of donor money by some banks in CSI initiatives was also questioned.

The initiative spearheaded by KBA, and supported by a number of partner agencies, is therefore the first attempt by Kenya's financial services sector to embrace and adopt sustainable finance practices in its day-to-day operations for the mutual benefit of the firms and society at large.

Background Information and Overview on the Process Towards Developing the Guiding Principles

The development of the Kenya Sustainable Finance Principles started in September 2013 with the convention of a CEO Roundtable at which banks committed to the vision. Critical to this initiative was the support of UNEP Finance Initiative (UNEP-FI), DEG (German Investment Corporation) and the Netherlands Development Finance Company (FMO).

Bank CEOs ratified the launch of the Sustainable Finance Initiative (SFI), putting Kenya at par with countries that have launched similar initiatives led by either regulators or banks.

The next step was the formation of the SFI Working Group consisting of the KBA Secretariat and 12 banks to actualize the vision, with the task of developing recommendations, including those on capacity building and the development of Sustainable Finance Guiding Principles for the East African region.

SFI Working Group Banks

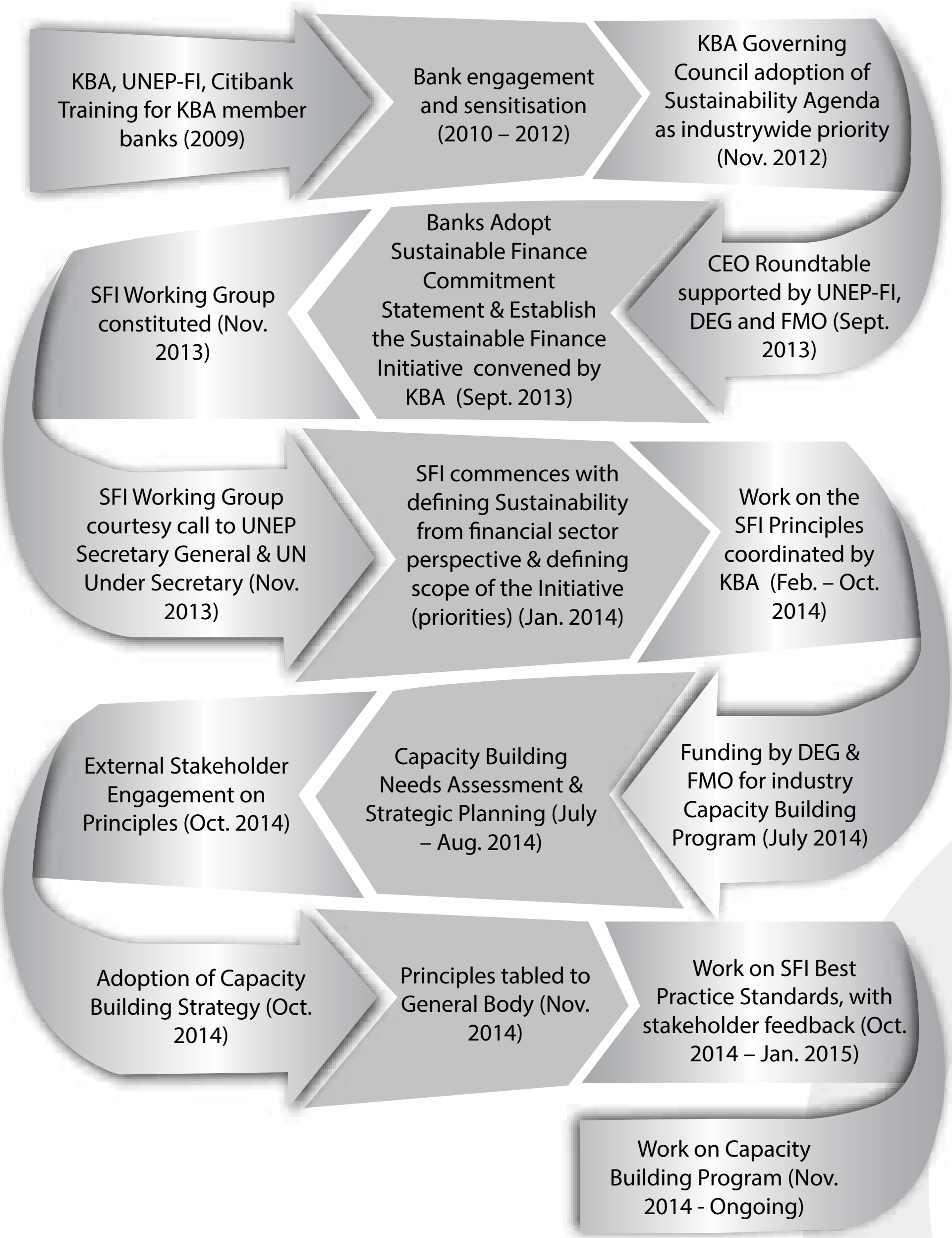
- Bank of Africa
- Commercial Bank of Africa
- Cooperative Bank of Kenya
- Equity Bank
- Gulf African Bank
- Habib Bank
- I&M Bank
- Jamii Bora Bank
- KCB Group
- NIC Bank
- National Bank of Kenya
- Standard Chartered Bank

The SFI Working Group formed three teams to deal with Principles and Procedures, Capacity Building and the Green Economy. The SFI identified its priority areas as comprehensive risk management; business practice, leadership and governance; and growth through inclusivity, innovation and technology.

Subsequently, Five SFI Guiding Principles were drafted and presented for review to the Working Group and the KBA Governing Council.

The SFI's input will also be critical in the development of a structured Capacity Building program. The primary target are credit risk managers, business development and strategy heads and operations officers, before it is escalated into practice-sharing sessions for CEOs and Boards.

SFI Roadmap


KBA, UNEP-FI, Citibank Training for KBA member banks (2009)
Bank engagement and sensitisation (2010 – 2012)
KBA Governing Council adoption of Sustainability Agenda as industrywide priority (Nov. 2012)
CEO Roundtable supported by UNEP-FI, DEG and FMO (Sept. 2013)
Banks Adopt Sustainable Finance Commitment Statement & Establish the Sustainable Finance Initiative convened by KBA (Sept. 2013)
SFI Working Group constituted (Nov. 2013)
SFI Working Group courtesy call to UNEP Secretary General & UN Under Secretary (Nov. 2013)
SFI commences with defining Sustainability from financial sector perspective & defining scope of the Initiative (priorities) (Jan. 2014)
Work on the SFI Principles coordinated by KBA (Feb. – Oct. 2014)
Funding by DEG & FMO for industry Capacity Building Program (July 2014)
Capacity Building Needs Assessment & Strategic Planning (July – Aug. 2014)
External Stakeholder Engagement on Principles (Oct. 2014)
Adoption of Capacity Building Strategy (Oct. 2014)
Principles tabled to General Body (Nov. 2014)
Work on SFI Best Practice Standards, with stakeholder feedback (Oct. 2014 – Jan. 2015)
Work on Capacity Building Program (Nov. 2014 - Ongoing)

Global Best Practice

In the execution of its mandate to formulate sustainable finance principles and guidelines that are relevant to the Kenyan and regional context, the SFI Working Group has drawn from previous work in this arena from other jurisdictions and international best practice. The aim was to come up with principles that not only cover all aspects of sustainability but are also cognizant of the risk management policies and practices of individual banks. The other motivating factor was the need to harmonize, as much as is practical, the resultant guidelines with what obtains in the rest of the world so as to promote the competitiveness of KBA members and enable them play at par with their peers from other parts of the world that have already adopted sustainable finance practices.

Equator Principles

The Equator Principles represent the first voluntary and private effort by banks, on a global scale, to formulate guiding principles for the practice of sustainable banking. Big transnational banks, working together with the International Finance Corporation (IFC) adopted the principles in 2003 as a way of ensuring that the projects they financed were subjected to a social and environmental risk analysis. Under the Equator Principles, projects are graded as either A, B or C depending on severity of their impacts on society and environment, with the first two categories required to undergo mandatory environmental assessment before lending can be authorized. Membership is voluntary and has grown from an initial 10 to 80 as at 2014. About 10 African banks have signed up, while in Kenya representation is still limited to the local units of foreign banks.

IFC Sustainability Principles

The International Finance Corporation has been at the forefront in the global push for sustainable banking. It is one of the DFIs that "incentivizes" banks which have embedded sustainability principles as part of their daily operations. Its environmental and social safeguard policies provided the framework for the Equator Principles, which it played a key role in formulating. Through its Policy on Environmental and Social Responsibility, the IFC gives a commitment to carry out its investment and advisory activities with the intent to "do no harm" to people and the environment, to enhance the sustainability of private sector operations and the markets they work in, and to achieve positive development outcomes.

Nigeria Sustainable Banking Principles

Nigeria is the single African country, outside South Africa, that has pioneered sustainable banking on the continent. The country adopted a hybrid approach, whereby banks, discount houses and development finance institutions were involved in formulation of the principles, but with the support of the Central Bank of Nigeria (CBN). The principles were issued by the CBN in 2012 via a circular and banks directed to fully adopt and implement them. To help the regulator track implementation and adherence, banks and related institutions are also required by the regulator to submit regular reports. The Nigerian experience involved the development of sustainability guidelines for specific sectors like Power and Agriculture.

African Development Report: Towards Green Growth in Africa

The African Development Bank (AfDB) is one of the development finance institutions which offer price incentives to local banks to encourage them to adopt sustainability as part of their core banking operations. This normally takes the form of low interest rates on monies disbursed by the continental DFI to local banks for onward lending to their customers. In the above report produced in 2012, the AfDB places inclusive growth and the quest for green growth at the core of its Ten-Year Strategy (2013-2022). The promotion of green growth is presented in the report as part of a new impetus by the AfDB to push not just for growth, but quality growth on the continent. The bank has also come up with specific products to help the continent deal with the cost of transition to green growth.

Global Reporting Initiative

The Global Reporting Initiative (GRI) has come up with Sustainability Reporting Guidelines that are the most widely used in the world. Launched in 1997 by UNEP, these guide companies and other organizations in reporting their performance based on a number of matrices: economic, environmental, social and governance. The latest (fourth) version was launched in 2013 after a revision that took into account trends in the area of sustainability reporting. The GRI Sustainability Reporting Guidelines provide a standard way for organizations to report on their social responsibility performance, while implementing the guidelines contained in ISO 26000, which is the global standard for social performance. The latter is developed by the International Organization for Standardization (IOS), which is the world's main developer of voluntary international standards.

UNEP-FI Guidelines

The United Nations Environment Program Finance Initiative (UNEP-FI) is a global partnership between UNEP, the UN agency for environmental protection and the financial sector. Started in 1992, its main aim is to ensure that the financial sector factors in environmental and social considerations in financial performance and decisions. It was initiated out of heightened recognition of the link between finance and Environmental, Social and Governance (ESG) challenges and the critical role financial institutions could play in the quest for a sustainable world. Member banks, numbering about 200 and growing, sign the UNEP FI Statement of Commitment, as an undertaking that they shall operate by the guidelines. UNEP-FI is also involved in capacity building and sharing of best practice; relevant research and setting of global standards and principles, among others.

UN Global Compact Principles

This initiative by the UN, established in 2000, aims at having a more sustainable and inclusive global economy. It is a call to action that seeks to harness the capacity of businesses to play their part and measure their impacts on society. The initiative has concretized its vision in 10 Principles to guide the conduct of global commerce with the main focus areas being human rights, environment, labor relations and anti-corruption. The Global Compact has found wide acceptance since launch, recording over 12,000 corporate participants and other stakeholders based in over 145 countries, making it the largest voluntary corporate responsibility initiative in the world.

Draft National Climate Change Framework Policy

The policy is hinged on Kenya's ratification of global conventions on climate like the Kyoto Protocol and the United Nations Framework Convention on Climate Change (UNFCCC) and its own Constitution. The latter specifically makes ecological sustainability mandatory even as the county seeks to achieve its development goals as set out in the Vision 2030 blueprint. The policy focuses on ways of achieving resilience and ability to adapt to climate change, while promoting development options that visit the least harm through carbon emission. Another key consideration is the placement of climate change at the core of development planning at the national, county and sectoral levels, while providing a regulatory infrastructure that ensures adoption and compliance.

Kyoto Protocol

The Kyoto Protocol was a progression from the UN Framework Convention on Climate Change (UNFCCC) which was signed by nearly all countries at the 1992 Earth Summit in Rio. It was a watershed in two ways: first was the acknowledgement that global warming exists and that it was caused by carbon emissions into the atmosphere. Finalized in Kyoto, Japan in 1997, it only came into effect in 2005. It is based on the principle of common but differentiated responsibility, which placed the greatest burden of guilt on developed countries as opposed to their developing counterparts. As a result, the industrialized nations pledged to cut their yearly emissions of carbon by about 5.2 per cent by 2012. Even then, the scorecard has not been impressive: while blocs like the EU were on track to meeting their quotas by 2011, progress has been annulled by the US and China, the two biggest polluters. The US has also never ratified the protocol, blunting its effect and profile internationally.

ISO 26000: 2010

This set of standards is among the over 19,500 developed by the International Organization for Standardization (ISO), the world's largest developer of voluntary standards, since its formation in 1947. Aimed at guiding firms on how they can act in a socially responsible way, it defines social responsibility, helps firms actualize principles while sharing best practice from around the world. The principles are presented in an easy-to-understand language accessible to non-specialists and can be applied to all manner of organizations, regardless of size. The fact that ISO works with national standards bodies from over 160 countries in developing standards also ensures that the guidelines are responsive to regional peculiarities as much as possible. Standards are developed by consensus by experts from participating countries ensuring relevance and applicability.

China Green Credit Guidelines

Issued by the China Banking Regulatory Commission in 2012, these guidelines are aimed at encouraging banks and related institutions to focus on green credit and mitigate environmental and social risk in their operations. The Banking institutions targeted with these guidelines include policy banks, commercial banks, rural cooperative banks and rural credit cooperatives lawfully incorporated within the territory of the People's Republic of China. There is a provision for monitoring and evaluation by the regulator of the sector to ensure compliance with the guidelines. Also given due emphasis is human and system capacity building, and a requirement for public disclosure, supervised by the regulator, CBRC.

International Labour Organization Standard

Given that its primary mandate is the welfare of labour (employees), the ILO is naturally concerned about the principle of sustainability. It has published a number of standards to guide this discourse and its adoption by various industries. The principle here is that worker welfare is best secured in a system that balances economic growth with environmental and social concerns. With demand for new jobs expected to reach 500 million over the next decade, and with youth and women being the majority, there is an undeniable human and social face to sustainable development, and such emergent needs must be included in sustainable development polices.

The "3 P" Approach of the SFI

Sustainable Finance Initiative Priorities (focus areas for the industry)

SFI Guiding Principles (guiding philosophy & industry commitment)

SFI Best Practice Standards (Procedures) & Proposed Policies (how the principles are implemented)

The SFI Working Group approach centered on "3 Ps", namely 1) defining sustainability and setting out the Priorities; 2) harmonising global and regional best practices and defining the 5 core Guiding Principles; and 3) singling out a set of Procedures and Policies that reflect the philosophy and enable the Principles.

Sustainable Finance Initiative – Priorities

The Sustainable Finance Initiative will be grounded in three main priorities, namely equipping the financial services sector to perform optimally in the area of comprehensive risk management; enhancing best business practice, leadership and governance through engagement and capacity building at the board and senior management levels; and promoting industry growth and development by fostering a culture of innovation and inclusivity enabled by new technology.

These Priorities were articulated by the SFI Working Group banks and adopted as the focus thematic areas of the SFI.

1. Comprehensive Risk Management:

While utilising capital responsibly to create value economically and deliver returns to their shareholders, sector players should be effective at the mitigation and management of economic and associated risks in both the short-run and long-term period.

- **Economic Risk:** As custodians of capital, anticipating and responding to the impact of macroeconomic conditions, including fiscal and monetary policy, government regulation and political stability, is core to the viability of the institution as well as the sector at large. Institutions therefore should ensure that their firm is best equipped to respond to economic risks.

- **Associated Risk:** Recognising that the financial services sector is both directly and indirectly impacted by social and environmental factors, through policies and risk assessment procedures, firms should also seek to mitigate social and environmental risks associated with their financing activities.

2. Business Practice, Leadership & Governance:

- **Board Roles & Responsibilities:** Ethical practices and conduct reinforced by corporate values are the foundation of any financial service firm. It is therefore the role of the leadership, which is ultimately represented by the Board and Chief Executive Officer, to set the tone and actively ensure that business practices are ethical and fulfil the established regulatory and corporate governance requirements.

- **Best Practice:** Organisations that openly disclose and embed their core values and priorities tend to have better run institutions. It is therefore proposed that this best practice be adopted within institutional policies and procedures. Reporting is another best practice and key component. As firms work to enhance their reporting policies and procedures; the industry should work to publicize the positive impact of sustainability initiatives that institutions are advocating and achieving in their day to day activities.

3. Growth through Inclusivity, Innovation & Technology:

Increasingly competition within the sector and from competing sectors is driving financial service players to continually innovate and leverage on existing and emerging technology to respond to, and anticipate dynamic market needs. Considering that product and process innovation contributes towards industry growth and development, a culture of innovation and inclusivity enabled by new technology should be fostered at both the firm and industry levels.

Sustainable Financing Initiative – Guiding Principles

The SFI Guiding Principles inform financiers on how to optimise the balancing of their business goals with the economy's future priorities and socio-environmental concerns.

The Guiding Principles are in line with international best practice and consistent with the financial sector's environmental and social risk management aspirations.

They are meant to guide banks in the implementation and adoption of sustainability practices and the incorporation of the same into their day to day operations. They provide a much-needed case and rationale for sustainable banking in the Kenyan and regional context.

Principle 1:
Financial Returns versus Economic Viability.

Financial institutions should consider both financial returns and the economic viability of their financing activities. Economic viability, defined as the ability to realise sustained long-term growth/returns, should be factored into the decision making process, particularly in the financing of commercial activities. The Guiding Principle is that financial viability is necessary from an investment perspective; but is not a sufficient condition for sustainable economic development.

Principle 2:
Growth through Inclusivity & Innovation.

Financial sector players seek to grow and enhance service delivery for the markets they currently serve, as well as reach out into diversified markets with economic potential thereby fostering financial deepening. The Guiding Principle is that financial institutions in pursuit of growth should innovate and leverage on existing and emerging technology to reach current and potential markets while economically empowering communities.

Principle 3: Managing & Mitigating Associated Risks.

Economic development is intertwined with social, humanitarian and environmental concerns; therefore financiers are materially affected by these concerns despite the fact that these risks may be perceived as indirect or secondary. The Guiding Principle is that firms should seek to mitigate social and environmental risks associated with their financing activities through client engagement and effective policies and risk assessment procedures; and in addition, firms should actively measure and report on the financial impact of these risks on their business performance.

Principle 4: Resource Scarcity and Choice.

In meeting present needs, financial institutions should ensure optimal management of resources, including financial resources and natural capital, so as to avoid compromising the future generation's needs. The Guiding Principle is that optimal resource management is realized through productivity and efficient utilization of resources; and is guided by comprehensive opportunity cost assessment.

Principle 5: Business Ethics & Values.

Promoting enhanced oversight of business practices at both the Management and Board levels contributes towards effective, resilient organisations. The quest for ethical practice, efficiency, productivity and waste minimisation should be fostered from the leadership and enabled by adequate governance structures. The Guiding Principle is that the leadership of financial institutions should ensure the organisation to deliver returns in the long term, and in a responsible manner that sees optimal utilisation of resources towards achieving positive externalities.

SFI – Best Practice Standards

Whereas the SFI Principles guide and inform the financial services sector on the philosophy and expectations around sustainability and sustainable finance, the SFI Procedures are best practice standards for the board and management to implement towards realising the SFI Principles.

These are specific actions to be undertaken by various players in banks as a way of ensuring compliance with SF Principles. They provide a list of procedures, a clear roadmap of what needs to be done, by which actor and to what end.

Principle 1: Financial Returns versus Economic Viability

Financial institutions should consider both financial returns and the economic viability of their financing activities. Economic viability, defined as the ability to realise sustained long-term growth/returns, should be factored into the decision making process, particularly in the financing of commercial activities. The Guiding Principle is that financial viability is necessary from an investment perspective; but is not a sufficient condition for sustainable economic development.

- Economic viability of financing activity should be factored into the organisational strategic priorities and business development planning, with the board of directors and management ensuring that the firm demonstrates the realisation of "Sustainable Finance Principle 1: Financial Returns versus Economic Viability".

- The ability to realise sustained long-term growth/returns as envisioned in "Sustainable Finance Principle 1: Financial Returns versus Economic Viability", should be factored into the credit analysis and decision making process undertaken in all commercial lending activity.

- The investment climate and near-term macroeconomic projections influence the viability of financing activity. An understanding of macroeconomic impacts on current and long-term business performance should therefore be formalised with regular monitoring and analysis undertaken by management. This includes establishing at the firm level a process for assessing the impact of national and county-level fiscal and monetary policies, other government regulation, political stability and other factors that both directly and indirectly affect the investment climate. The investment climate reports should be reported to the relevant board committees (advances and credit risk).

Principle 2: Growth through Inclusivity & Innovation

Financial sector players seek to grow and enhance service delivery for the markets they currently serve, as well as reach out into diversified markets with economic potential thereby fostering financial deepening. The Guiding Principle is that financial institutions in pursuit of growth should innovate and leverage on existing and emerging technology to reach current and potential markets while economically empowering communities.

- A process should be established by managemetn to enable and promote the development of innovative products and services that target segments with economic potential, including Small and Medium-sized Enterprises, agriculture, women-owned micro businesses, and the youth segment. Business viable innovations as advocated for in "Sustainable Finance Principle 2: Growth through Inclusivity & Innovation" would be supported by the management within the strategic planning process.

- Business development strategies undertaken by management should seek to also promote job creation; enhance efficiency and service delivery through new technology; and introduce new business lines and products, which by their very nature provide net benefits to the society (for example green credit leasing, or green bonds).

- There is need for the management and board of directors to formerly proactively engage and partner with other economic players so as to be aligned with market and societal expectations, while realising "Sustainable Finance Principle 2: Growth through Inclusivity & Innovation".

- Potential and current customers should be informed and educated about the services offered by the firm. Resources should be allocated towards customer education towards promoting financial literacy and consumer protection.

Principle 3: Managing & Mitigating Associated Risks

Economic development is intertwined with social, humanitarian and environmental concerns; therefore financiers are materially affected by these concerns despite the fact that these risks may be perceived as indirect or secondary. The Guiding Principle is that firms should seek to mitigate social and environmental risks associated with their financing activities through client engagement and effective policies and risk assessment procedures; and in addition, firms should actively measure and report on the financial impact of these risks on their business performance.

- The management should establish an Environmental and Social Risk Management System (ESMS) to strengthen and mitigate impacts as defined in "Sustainable Finance Principle 3: Managing & Mitigating Associated Risks". The credit analysis process should inlcude the review and categorisation of environmental and social risks; and consisit of (a) risk categorization, (b) assessment of risks, (c) benchmarking compliance with the local laws and regulations, and (d) defining the mitigation measures.

- There is a need to develop an internal monitoring system to monitor commercial clients' associated risks over time, and to ensure compliance with agreed environmental, social and corporate governance (ESG) requirements defined in the loan agreement. This includes expanding consideration of indigenous people and protected land and wildlife through proactive engagement (dialogue) and comprehensive risk analysis for commercial projects.

- Procedures should be established by management to ensure compliance with the local laws and regulations on labour standards, including health and safety, persons with disabilities, and labour rights. This also entails the elimination of all forms of forced and compulsory labour; the effective abolition of child labour; and elimination of discrimination in respect of employment and occupation.

• Management should dedicate a resource person(s) towards realising “Sustainable Finance Principle 3: Managing & Mitigating Associated Risks”. The resource person(s) would have designated ESG responcibilities that cut across institutional departments. For large and medium-sized institutions as defined by the Central Bank (Tier I and Tier II), there should be a dedicated resource person(s) with relevant experience in environmental and social risk management. For the Tier III financial institutions, this requirement can be met through shared responsibility roles.

• A grievance and dispute resolution mechanism to receive and facilitate resolution of concerns and grievances about the environmental and social impact of financed activities should be established by the management with reporting of material disputes to the board of directors.

Principle 4: Resource Scarcity and Choice

In meeting present needs, financial institutions should ensure optimal management of resources, including financial resources and natural capital, so as to avoid compromising the future generation's needs. The Guiding Principle is that optimal resource management is realized through productivity and efficient utilization of resources; and is guided by comprehensive opportunity cost assessment.

- The "Sustainable Finance Principle 4: Resource Scarcity and Choice" applies to both financiers and their clients. For financiers, management should establish a process of monitoring, evaluation and third-party validation, of the organisation's operations (including head office, branches and fleets). Through this process, the management should demonstrate optional operational efficiency, while realising minimal carbon emissions and waste reduction.

- The board of directors should define a policy on natural capital, to ensure that the firm through its oranisational planning process, as well as its financing activity, does not invest in or finance operations that adversely impact the country's natural resources. This policy should help guide the management in its decision making framework and opportunity cost assessment.

- In the relationship management process, business units should engage their commercial clients (business and corporate customers), and determine the clients' capacity to reduce environmental and social risks and enhance sustainable development over time. Commercial clients should be provided with relevant information in order to strengthen their capacity.

Principle 5: Business Ethics & Values

Promoting enhanced oversight of business practices at both the Management and Board levels contributes towards effective, resilient organisations. The quest for ethical practice, efficiency, productivity and waste minimisation should be fostered from the leadership and enabled by adequate governance structures. The Guiding Principle is that the leadership of financial institutions should ensure the organisation delivers returns in the long term, and in a responsible manner that sees optimal utilisation of resources towards achieving positive externalities.

- In the board planning process, there is the need for reorienting growth strategies and the organisational vision, mission and objectives to ensure that equal weight is given to the economic, social and environmental dimensions of organisational sustainability.
- The board of directors and management should adopt to publish a comprehensive sustainability report once every two years (at a minimum). Reporting on the institution's contribution to sustainable economic development (beyond financial performance) and progress towards realisation of the "Sustainable Finance Principles" should be incorporated in the annual integrated financial reports.
- The board of directors and management should establish formal governance structures to enable the review and reporting of progress in meeting the "Sustainable Finance Principles" and best practice procedures .
- The board of directors and management should disclose the institutional Values, Sustainability Priority Areas, as well as industry standards on Sustainable Finance, to internal and external stakeholders to facilitate accountability within the institution.
- Institutional Values should include the pursuit of good governance, and corporate citizenship that promotes economic empowerment, and enhances social and environmental aspects in the communities.

SFI – Proposed Policies

Certain policies are required to enable the business to implement the SFI Procedures and for the institution to realise the SFI Principles. These SFI Policies would mostly be incorporated into current institutional policies or created where such requirements are not articulated.

Risk Policies to be Undertaken by Business and Credit Risk Heads in Consultation with Board Risk committees

RISK POLICIES:

- A credit policy that incorporates the review and categorisation of economic, social and environmental risks should be reviewed and ratified at the board level. The board risk, and audit committees would enable the firm in realising the policy objectives and requirements. These committees would report material aspects to the main board and shareholders.

- The board risk committee should in its terms of reference include oversight of the firms non-financial risks, including social and environmental risks.

Human Resource Policies to be Undertaken by HR Heads in Consultation with Management committees

HR POLICIES:

- Incorporation of SFI Principles in recruitment, and induction program for all full-time employees.

- Review of job profiles, roles and responsibilities should incorporate SFI Principles and Procedures across targeted departments, including finance, credit risk, business department, operations and compliance.

- Monitoring of training and capacity building for targeted departments, including finance, credit risk and business department should be factored into the annual budget and incorporated into individual performance development plans.

HR POLICIES

- Compliance with laws, regulations and industry best practices in the area of occupational health and safety, labour rights, as well as accessibility for persons with disabilities should be included in the role responsibilities of management.

- Development and monitoring of an institutional policy regarding Diversity and Inclusion, including creating an enabling environment that is free from discrimination, accommodates persons with disabilities, and promotes talent development and retention.

Governance Policies to be Ratified at the Board level

GOVERNANCE:

- Board and management evaluation and reporting of performance against Sustainable Finance priorities as defined by the board and management through consultation. May include an independent, third-party assessment.

- Board and management capacity building on best practice in Sustainable Finance.

Compliance Policies in line with Local Law and Regulations

COMPLIANCE POLICIES:

- Annual measurement of emissions (green house gases) at the institutional level; business segment level; and branch and fleet operations.

- Formulate, implement, and report on national, regional and local programmes aimed at mitigating climate change and measures to facilitate adequate adaptation to climate change. Priority sectors include agriculture, forestry, energy, extractive industries, transportation and tourism.

Jeremy Ngunze, Vice Chair of Kenya Bankers Association and Country Managing Director, Commercial Bank of Africa opens the Sustainable Finance CEO Roundtable.

Alto Chapota, a Senior Portfolio Management Officer at PTA Bank (far right) with KBA Governing Council Members.

Jane Kilonzo, Bank of Africa GM of Risk & Finance, shares her views during the Roundtable discussion.

Equity Bank COO Dr. Julius Kipngetich presents the business case for Sustainability during the CEO Roundtable.

UNEP-FI Acting Head, Yuki Yasui with Bank of Baroda CEO Vindhya Vittal Ramesh during the Sustainable Finance CEO Roundtable.

Council Member Dhirendra Rana MD of Middle East Bank Kenya shares his views during the discussion.

KBA CEO Habil Olaka presents the industry's commitment statement to the UNEP Executive Director and Under-Secretary Achim Steiner.

SFI Working Group Discussion with the UNEP Executive Director.

SFI Working Group members Rose Kinuthia of KCB with Nahashon Wamugi of Coop and Shameer Patel of I and M bank.

(From L-R) Jaap Reinking, the Director of FMO's Financial Institutions Department, Habil Olaka, KBA CEO, and Eric Kaleja, DEG Regional Director for East Africa, sign a Memorandum of Understanding on a capacity building program funded by the two firms to promote sustainable finance practices among KBA member banks.

SFI Working Group members pose with DEG and FMO teams and the capacity building consultants.

Kenya Bankers Association
13th Floor, International House, Mama Ngina Street
P O Box 73100 - 00200 NAIROBI
Tel: +254 20 2221704 / 2217757 / 2224014 / 5
Cell: +254 733 812770 / 711 562910
Fax: +254 20 2221792
Email: consumerguide@kba.co.ke
Website: www.kba.co.ke