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Emerging Trends in ESG Investing and Sustainable Finance

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FOREWORD

The financial markets have had the concept of socially responsible investment (SRI) since the first half of the 20th century, but ESG investment focusing on the environment, society, and governance is a more recent concept that has spread worldwide since the Principles for Responsible Investment (PRI) were launched in 2006. The United Nations' introduction of Sustainable Development Goals (SDGs) in September 2015 has contributed to more widespread awareness of the importance of sustainable finance. In the Asian region, including the Association of Southeast Asian Nations (ASEAN) member countries , the concepts of ESG investment and sustainable finance generally are still in their early stages of development, but we have already seen a number of important ESG-related initiatives mainly in the three areas outlined below.

First is the strengthening of corporate governance by listed companies. On a regional level, the ASEAN Capital Markets Forum (ACMF), with the support of the Asian Development Bank, introduced the ASEAN Corporate Governance Scorecard in 2011, based on the Organisation for Economic Co-operation and Development (OECD) Principles of Corporate Governance. At the individual country level, financial regulators have introduced corporate governance codes and corporate governance blueprints to promote greater awareness of the importance of corporate governance among listed companies.

Second is the issuance of green bonds to fund environment improvement projects. One impetus for green bond issuance in the ASEAN region in recent years has been the Paris Agreement, which was adopted at the 21st Conference of the Parties to the United Nations Framework Convention on Climate Change (COP 21) in December 2015 and establishes an international framework for dealing with global warming after 2020. The ASEAN countries are signatories of the Paris Agreement and are endeavoring to reduce greenhouse gas emissions. Green bond issuance has also been supported by the introduction of the ASEAN Green Bond Standards in 2017 by the ACMF based on the Green Bond Principles of the International Capital Market Association (ICMA).

Third is the publication of sustainability reports by listed companies. Sustainability reports disclose what companies are doing to help realize a sustainable society. By increasing the transparency of nonfinancial information and reporting their initiatives to improve the environment and contribute to society, companies can enhance their appeal to investors as well as improve their competitiveness. In the ASEAN region, the status of the introduction of regulations concerning sustainability reports varies from country to country, but in general countries have either adopted the "Comply or Explain" method or plan do so.

ESG-related efforts in each country help attract a wider range of issuers and investors and are therefore extremely important for building sustainable capital markets, which in turn can be expected to lead to sustainable growth of national and regional economies. This issue of Nomura Journal of Asian Capital Markets features articles that present the current state of ESG-related efforts as well as the key issues and prospects for future development of ESG investment and sustainable finance in ASEAN countries' capital markets.

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ESG Bond Market: Current State & Outlook

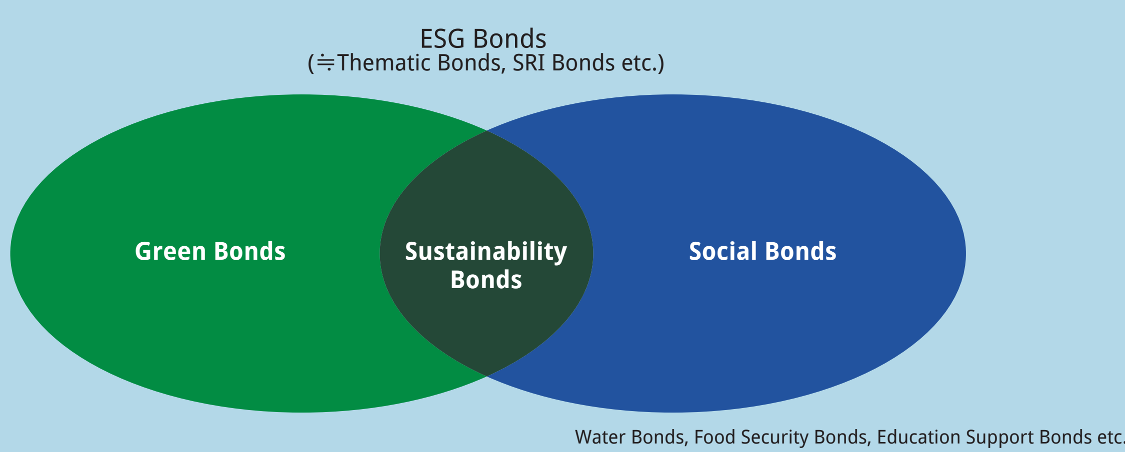
What Are ESG Bonds?

ESG is an acronym for environment (E), society (S), and governance (G). The financial markets have had the concept of socially responsible investment (SRI) since the first half of the 20th century. More recently, consideration of ESG factors as an investment concept has spread rapidly since the Principles of Responsible Investment (PRI) launched in April 2006 under the initiative of former Secretary-General Kofi Anan at the United Nations (UN). Consideration for ESG in Japan's financial markets, including both the equity and fixed income markets, has risen markedly among investors, issuers and other market participants since Japan's Government Pension Investment Fund (GPIF) became a PRI signatory in September 2015.

The history of ESG in the fixed income market dates back to the latter 2000s, when the issuance of bonds aimed at solving ESG-related issues began with bonds classified under such categories as thematic bonds, SRI bonds, and social contribution bonds. In January 2014, Green Bond Principles (GBP) developed in a joint effort by green bond market participants were announced and became the basis for the development of ESG bonds.

As at end-May 2019, principles and guidelines have been established for three types of ESG bonds: (1) green bonds, (2) social bonds and (3) sustainability bonds (Figure 1). This article focuses on

Figure 1: Scope of ESG Bonds (Image)



Source: Nomura Institute of Capital Markets Research

ESG bonds that fall within the scope of the bonds shown in Figure 1. This paper presents the main characteristics of ESG bonds, their issuance status, investor base and market infrastructure, as well as the major supportive measures that have been taken by governments. Lastly, the paper will examines future issues for ESG bonds.

Main types of ESG bonds

Green bonds are bonds issued to raise funds required by projects aimed at bringing about improvements in the environment. The concept is established since the announcement of the GBP in January 2014. GBP was initially developed by four banks in Europe and the United States (US), and the International Capital Market Association (ICMA) was later appointed as Secretariat, assuming administrative duties and providing guidance for the governance of the principles. Several organisations have established green bond standards and guidelines other than the GBP. In Japan, the Ministry of the Environment announced its "Green Bond Guidelines 2017 Edition" in March 2017. From a more international viewpoint, the European Commission is developing an EU Green Bond Standard (EU GBS), and the International Organization for Standardization (ISO) is currently preparing for the establishment of an international standard on green bonds (ISO 14030). Green bond issuance is considered to have started with the Climate Awareness Bond issued by the European Investment Bank (EIB) in June 2007. In 2008, The World Bank issued the world's first bond to be called a "green bond."

Social bonds are bonds issued to fund projects that respond to social issues. The ICMA has published its Social Bond Principles (SBP) and the Association of Southeast Asian Nations (ASEAN) Capital Markets Forum (ACMF) has issued its Social Bond Standards (ASEAN SBS). The vaccine bond issued by the International Finance Facility for Immunisation (IFFIm) in November 2006 is regarded as the first social bond.

Sustainability bonds are bonds issued to raise funds for projects that contribute to the environmental and social development. The ICMA has established its Sustainability Bond Guidelines (SBG) and the ACMF has published its Sustainability Bond Standards (ASEAN SUS). The first sustainability bond is considered to be a bond issued by the former French administrative région Nord-Pas-de-Calais (now Hautes-de-France) in December 2008.

ESG bond types

ESG bond types include standard ESG bonds, revenue bonds, project bonds, and securitised bonds. The standard bonds have achieved the greatest market penetration. Standard bonds are used to fund ESG-related projects, but the bond repayment source for such bonds is not limited to the cash flow generated by the project but also effectively includes the issuer's whole cash flow. The pricing of standard ESG bonds theoretically is in line with other bonds from the same issuer as issuer creditworthiness and seniority of bonds are similar. However, issuers are able to demonstrate to investors their commitment to ESG-related projects through the issuance.

External evaluations

One difference between ESG bonds and ordinary bonds is the existence of external valuations for the former. There are several kinds of external evaluation, including second-party opinions, but these evaluations are typically conducted by an independent institution that provides an objective evaluation of the issuer's ESG bond framework. External assessment providers include the Center for International Climate Research (CICERO) in Oslo, Norway; Sustainalytics in the Netherlands; and Vigio Eiris in Europe. Auditing firm–related organisations and credit rating agencies are also providing evaluations.

ESG bonds' merits and demerits

For issuers and investors, the merits of issuing and investing in ESG bonds include the ability to use their issues or investments as public relations (PR) opportunities to appeal to their proactive support of ESG-related issues. For investors, ESG bonds (especially in the Japanese market) also offer greater price stability on the secondary market because many investors tend to hold the bonds until maturity.

On the other hand, the demerits of ESG bonds for issuers include more costly and time-consuming reporting and external evaluations than is the case with normal bonds. The demerits for investors include (1) relatively more costly and time-consuming screening and monitoring because ESG bonds are relatively new financial products and (2) the possible exposure to reputation risk if the project funded by the ESG bond runs into problems and/or fails to its stated goals.

ESG Bond Issuance to Date and Investor Base

ESG bond issuance to date

ESG bond issuance began in the late 2000s, with issuance centering on green bond issues in the US and Europe. According to Bloomberg data as at end-May 2019 (excluding US municipal bonds and securitised bonds), green bonds accounted for around 86% of ESG outstanding issues (approximately USD612.7bn). Issuance gradually increased from the late 2000s and then expanded substantially from around 2015, when the UN adopted the Sustainable Development Goals (SDGs) and the Paris Agreement was adopted by 195 countries. Financial institutions account for about 20% of total outstanding issuance, followed by government agencies, supranationals, and utilities. China has accounts for the largest share of outstanding issuance at about 16%, followed by France, the Netherlands, supranationals, Germany and the US. Japan's share is about 2%. By currency, issues denominated in the euro accounted for about 47% outstanding issuance, followed by the US dollar at about 26%. Lastly, Bloomberg data shows the weighted average maturity of outstanding issues is about ten years.

Japanese issuers' share of current outstanding ESG bond issuance is only about 2% but has been steadily increasing since around 2017. While this rise reflects broader trends in the international financial markets, it also has been driven by the Ministry of the Environment measures supporting green bond issuance, as will be discussed later. Outstanding issuance of ESG bonds by Japanese issuers currently totals about USD13.9bn, of which about 72% are green bonds, 20% are sustainability bonds, and the rest are social bonds. Issuance amounts have increased steadily since 2017. Financial institutions and government agencies account for almost 70% of outstanding issues. As for currencies, the yen is the most popular for Japanese issuers, with a share of about 38%, but issues denominated in the euro and US dollar also account for a significant share of outstanding issues. While five years is the single most popular maturity for ESG bonds issued by Japanese issuers, the weighted average maturity for outstanding issues is about seven years (Figure 2).

Current status of investment in ESG bonds

The investor base for ESG bonds, including green bonds, is a diverse group, ranging from major institutional investors to investors specialising in ESG and SRI and individuals. Major institutional investors that have declared investments in green bonds include Zurich Insurance (USD5bn as at November 2017), Deutsche Bank (EUR1bn as at February 2015) and Germany's Kreditanstalt für Wiederaufbau (KfW, EUR1bn as at April 2015). Japanese investors also have been proactively investing in green bonds. For example, Nippon Life Insurance's current medium-term management plan (FY17-20) targets ESG investments totaling JPY700bn, and the insurer has announced its investments to date include green bonds issued by the City of Paris, environmentally friendly bonds issued by Transport for London, and Tokyo Green Bonds issued by the Tokyo Metropolitan Government (TMG). Dai-Ichi Life Insurance has disclosed its investments in ESG-themed bonds issued by supranationals and green bonds issued by TMG and the Japan Railway Construction, Transport and Technology Agency (JRTT).

Pension funds are the core investors in green bonds. The World Bank's first green bond issuance in 2008 was motivated by Scandinavian pension funds desire for fixed income financial products to support the transition to low-carbon, more climate-resilient world. Thereafter, many other pension funds began proactively investing in green bonds. In Japan, GPIF and the World Bank Group released a joint research report entitled "Incorporating Environment, Social and Governance (ESG) Factors into Fixed Income Investments". Taking into consideration the result of that research, in April 2019 the International Bank for Reconstruction and Development (IBRD) and the International Finance Corporation (IFC) announced that they would propose opportunities for investments in ESG bonds to the investment management companies used by the GPIF. These recent developments indicate that ESG bonds are likely to further penetrate the Japanese financial markets.

Meanwhile, ESG bond funds provide investors with another way to invest in ESG bonds. Such funds generally (1) enable investors to invest small amounts, (2) provide a diversification effect, (3) are managed by experts, and (4) secure transparency through publication of reference values and other indicators. Reflecting rising demand for investments in ESG bonds, we have witnessed a continuous trend in ESG bond funds being established since around 2015.

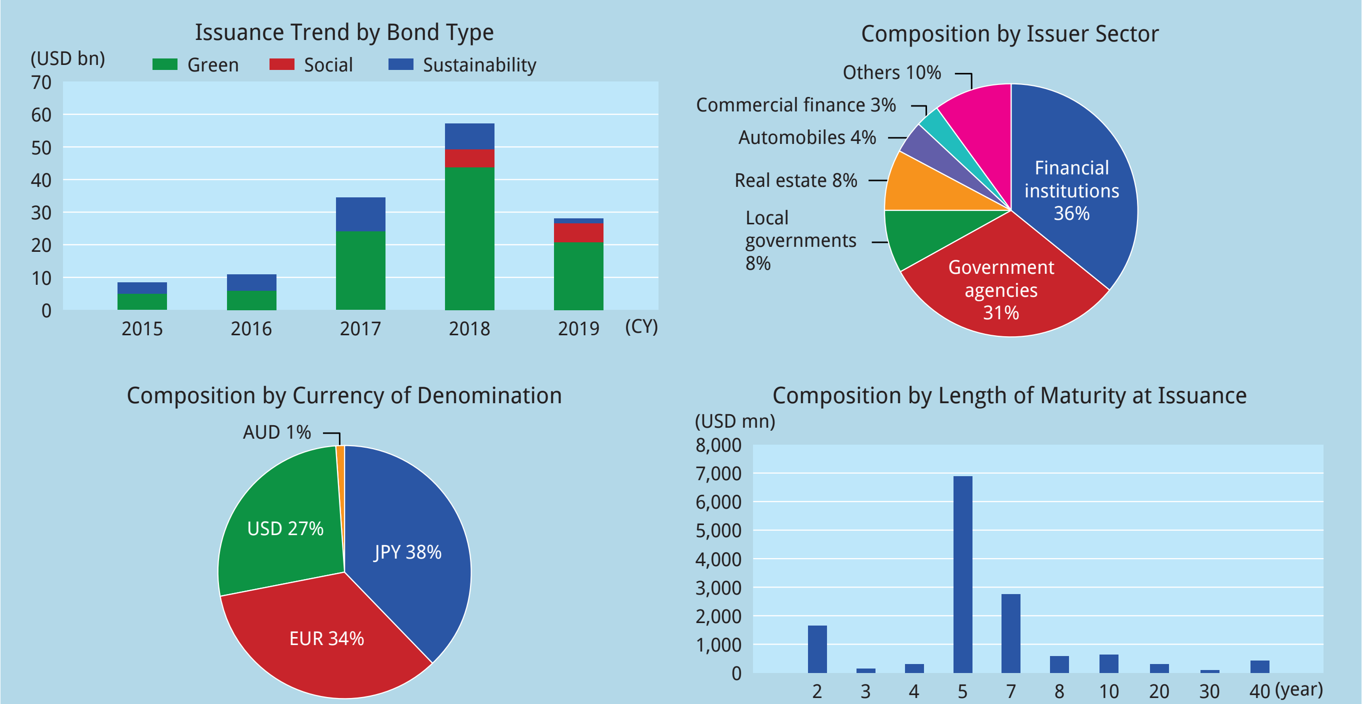
ESG Bond Market Support Infrastructure

ESG bond indices

ESG-related bond indices are one of two types. The first are indices comprising ESG bonds (at present, mostly green bonds). This type of index makes it relatively easy for market participants to understand the overall movement in the market for green bonds. In addition, bonds considered appropriate for inclusion in such indices tend to have higher liquidity, which contributes to the development of the green bond market.

The second type of index is one that is based on an existing bond index but changes the weighting of the components in the index based on their ESG rating and other factors. The similar methodology is used by eq-

Figure 2: ESG Bonds Issued by Japanese Issuers



Note: Issuance amount (as at 31 May 2019) is based on green bonds, social bonds and sustainability bonds defined by Bloomberg. Value is on a US dollar basis.
Source: Bloomberg, Nomura Institute of Capital Markets Research

uity ESG indices. The performance of these indices enables investors to grasp the effectiveness of taking into consideration ESG factors in their bond investment decisions.

While Japan does not yet have any ESG-related bond indices, Nomura Securities and the Nomura Research Institute announced in April 2019 that they had begun joint research targeting the establishment of a sub-index to the Nomura Bond Performance Index (NOMURA-BPI). The sub-index has been tentatively named NOMURA-BPI SDG Bonds.

ESG bonds and securities exchanges

In some countries, bonds are listed on securities exchanges, and in some cases ESG bonds are issued as listed bonds. According to the Sustainable Stock Exchanges (SSE) Initiative, as at end-September 2018, 15 securities exchanges have bonds listed in the sustainability bond category.

In Japan, the Tokyo Stock Exchange launched a dedicated platform for green and social bonds on its TOKYO PRO-Bond Market in January 2018. The platform allows issuers, at their discretion, to post information pertaining to their green and/or social bond issues, such as the use of bond proceeds, post-issuance disclosure reports, and reviews by external evaluators. As at end-May 2019, the Japan International Cooperation Agency (JICA) has posted information on its social bond issues. In Japan, most bonds transactions are conducted over-the-counter, not on securities exchanges. Accordingly, as of end-May 2019, JICA's social bonds and green bonds issued by Bank of China Tokyo Branch are the only ESG bonds listed on the Tokyo PRO-BOND Market.

Securities exchanges are expected to support development of the ESG bond market by establishing guidelines, improving market transparency, creating lists of ESG bonds, providing information that contributes to creation of ESG indices and exchanged traded funds (ETFs), and through other activities that contribute to greater awareness and understanding of ESG bonds.

Government Initiatives in Support of ESG Bonds

Governments around the world are promoting the issuance of and investment in ESG bonds, especially green bonds, and in some cases governments also provide financial support for ESG bonds. These government initiatives have included measures supporting issuers, investors, and the financial instruments themselves (Table 1).

The major initiatives supporting ESG bonds in Japan include the Ministry of the Environment's Pilot Project for Green Bond Issuance and its Green Bond Issuance Promotion Platform (issuer support business). The Pilot Project for Green Bond Issuance was started in fiscal 2017 and aims to promote green bond issuance by creating and widely disseminating examples of issues that conform to the "Green Bond Guidelines, 2017", and can be considered models for the issuance of green bonds. This project solicits applications from prospective green bond issuers. Model issues are then selected from the applications submitted and checked for alignment with the 2017 Green Bond Guidelines, after which a pre-issuance report is prepared and information disseminated. Since the project's start, five model issues have been selected, including one by JRTT.

The Financial Support Programme was started in fiscal 2018. Under the programme, the Ministry of the Environment provides subsidies for expenses required by those who support companies, local governments, and other entities that work to issue green bonds, in the form of the issuance support (granting external reviews, consultation on establishing a green bond framework, etc.) In fiscal 2018, many issuers, mostly corporates, took advantage of the programme to issue green bonds. Since the programme was put in place, approximately 70% of the green bonds that met the requirements for receiving subsidies had made use of the subsidies.

Table 1: Main Initiatives in Support of ESG Bonds

Country / Region	Details
Japan	• In addition to its "Green Bond Guidelines, 2017", the Ministry of the Environment (MOE) started its Pilot Project for Green Bond Issuance and the Financial Support Programme for Green Bond Issuance. • The MOE has also implemented other measures to promote green bond issuance. One such initiative is the Japan Green Bond Award, which recognises entities making pioneering efforts related to the issuance of green bonds. Another is subsidies for research on such topics as the pricing, risks, and impact of green bonds and other ESG bonds.
Singapore	• In June 2017 the Monetary Authority of Singapore (MAS) established a programme to provide subsidies to partially cover the expense (up to SGD100,000 per issue) of third-party evaluations of green bonds listed on the Singapore Exchange (SGX).
Hong Kong	• In June 2018, the Hong Kong government announced the establishment of its Green Bond Grant Scheme (GBGS) to provide subsidies to green bond issuers to cover the cost of external evaluations required to obtain certification under the Green Finance Certification Scheme (GFCS) established by the Hong Kong Quality Assurance Agency (HKQAA). A subsidy of up to HKD800,000 per issue is available for issues with a minimum size of HKD500mn (or equivalent in foreign currency).
Malaysia	• Capital Markets Malaysia, an organisation established by Malaysia's Securities Commission (SC), established a Green SRI Sukuk Grant Scheme in January 2018.The scheme will subsidise 90% (up to RM300,000 per issue) of the expenses required for acquiring an external valuation for green sukuk bonds issued in Malaysia.
United States	• The US formerly had systems promoting the issuance of clean renewable energy bonds (CREBs) and qualified energy conservation bonds (QECBs). The systems provided investors in the bonds with tax deductions or issuers received subsidies supporting issuance. However, both systems were terminated on 1 January 2018 as part of the Trump administration's 2017 tax reform.However, investors holding previously issued bonds and the issuers of those bonds will continue to receive the promised benefits for the life of the bonds.
Luxembourg	• In July 2018, Luxembourg put in force a new law establishing a new type of covered bond, i.e. green covered bonds), which are backed by loans or assets linked to renewable energy.

Source: Nomura Institute of Capital Markets Research

Issues for Future Development of the ESG Bond Market

In recent years, countries around the world have been making efforts to achieve the goals laid out in the UN's SDGs and the Paris Agreement. It is generally thought that a large amount of financial resources will be required to achieve these goals. Accordingly, it will be important to supplement public-sector resources with private-sector funds made available through the financial markets.*[1] With the concepts underlying SDGs and the Paris Agreement closely related to ESG issues, ESG bonds are expected to take on greater importance as an effective means for raising funds from the private sector. Meanwhile, every year an increasing number of investors are becoming PRI signatories and are making ESG one of the factors they consider when investing. The ESG market, including bonds, is therefore expected to continue expanding.

Moving forward, issues related to the development of the ESG bond market will be debated from various perspectives. However, there is already broad agreement about the need for (1) standardisation of guidelines and reporting and (2) the accumulation of issuance data and example cases. Greater standardisation is expected to facilitate the comparison of issues and enhance investment convenience. Green bond guidelines have already been established by the ICMA and several national governments. In addition, the ISO and EU are preparing their own guidelines. Actions taken by governments and other authorities to establish and revise guidelines that take into consideration financial market conditions in each region and seek to harmonise international standards will likely influence investor confidence in ESG bonds and determine the growth potential of the ESG bond market.

In addition, standardisation of reporting on ESG bonds will contribute to greater investment convenience. For example, reporting of greenhouse gas reductions, one type of project eligible for green bond issuance, takes various forms depending on the issuer. However, in November 2015, a group of 11 public financial institutions, including the World Bank, released a document outlining a harmonised framework for reporting on the impact of projects to which green bond proceeds have been allocated.*[2]

Compared to ESG as a factor in the equity market, ESG is a relatively new concept for fixed income products. ESG bond issuance and investment is still at development phase, largely due to relative lack of data, example cases and empirical research. While there are several databases on green bonds, a limited number of information providers are accumulating data on social bonds and sustainability bonds. Desirable actions include issuers clearly labelling bonds as ESG bonds before issuance and industry groups and governments strengthening their efforts to accumulate and provide data and example cases. The provision of such information to both issuers and investors will be crucial to the development of the ESG bond market. Although this market is currently in its very early stage of development and has many issues to overcome, many market players are working to resolve these issues. Accordingly, future developments bear watching closely.

The ESG bond market is a new market that helps bring environmental and social issues closer to the forefront of the financial markets. That said, it is also necessary to continue developing this new market into one that will be able to ride out disruptions and turmoil that occasionally strike the financial markets. Toward that end, all financial market stakeholders need to tackle these ESG issues head on with concrete action that will contribute to the sustainable development of the ESG bond market.

Notes

*1 For example, the International Energy Agency (IEA) estimates that achieving 2°C target will require total funding of USD75trn during 2016–2040 (USD40trn for energy supply and USD35trn for needed additional improvements to energy efficiency). The UN estimates that the funds needed to achieve its SDGs will come to USD5-7trn annually during 2016–2030, including USD3.3-4.5trn annually in developing countries. (International Energy Agency, *World Energy Outlook 2016*, 16 November 2016; United Nations Conference on Trade and Development, *Development and Globalization Facts and Figures 2016*, July 2016, p.165)

*2 World Bank et al., *Green Bonds Working Towards a Harmonized Framework form Impact Reporting*, November 2015.

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Otoritas Jasa Keuangan

Sustainable Finance in Indonesia: How the Financial Services Industry Contributes to Environmental, Social and Governance Issues

The Roadmap for Sustainable Finance in Indonesia

Indonesia, a G20 member and an archipelago comprising more than 17,000 islands with 270 million inhabitants, has the potential to become an ideal example of how economic growth can be accomplished responsibly and sustainably. In 2014 Indonesia's Financial Services Authority (Otoritas Jasa Keuangan, OJK) together with the support of a number of prominent contributors established the first phase of a strategic roadmap of sustainable finance for the years 2015-2019. Based on the 3-P Principles, Profit, People and Planet, the roadmap was designed to strategically and systemically guide Indonesia's financial services industry (FSI) to play an active role and contribute positively in the process of sustainable development (OJK, 2014).

The roadmap acts as a guideline to support Indonesia's effort in achieving the United Nations Sustainable Development Goals (UNSDGs) 2015-2030 and also in fulfilling the Paris Agreement on Climate Change for 2015-2030, among other objectives. The ultimate goal is to combat climate change and to intensify actions needed for a sustainable low-carbon future. Although the first phase of the roadmap covers 2015-2019, the roadmap is a medium to long term initiative of 10 years and is meant to be part of the global initiative established by a number of institutions worldwide to supporting sustainable development.

Such global initiatives include the RIO+ Agreement, which commits developed countries to reduce greenhouse gas emissions globally and to help developing countries undertake environmentally friendly economic development programs (RIO+, 2016), and The Equator Principles (EP), observed by 70 financial institutions committed reject loans to projects worth USD10 million or more if the prospective debtor does not comply with prevailing social and environmental regulations and follow procedures established by the EP (Equator Principles, 2017).

Under the roadmap (Table 1), strategic activities to implement sustainable finance in Indonesia comprise of three focus areas which are:

1) Increase supply of environmentally friendly financing;

2) Increase demand for environmentally friendly financing products; and

3) Increase oversight and coordination of sustainable finance implementation.

These strategic activities will be implemented gradually in the medium and long term. Firstly, activities in the medium term, from 2015 to 2019, focus on the basic regulatory framework and reporting system, increase understanding, knowledge and competence of the human resources in the FSI, and provide incentives and coordination with related agencies. Secondly, the longer term from 2020 to 2024 will focus on integrated risk management, corporate governance, bank rating, and the development of an integrated sustainable finance information system.

Since the roadmap was enacted, its implementation has been progressing positively through a number of financial products, regulations, and initiatives.

Promoting Sustainable Finance through Issuance of Green Bonds

Due to sustainability and development challenges faced by Indonesia as well as the investment opportunities offered by clean development, OJK has issued a series of sustainable finance policies to encourage the shift in the Indonesian economy towards sustainable and low-carbon economic growth.

Table 1: Strategic Activities to Implement Sustainable Finance

Strategic Goals		2015 – 2020-2024
Increase supply of sustainable financing to strengthen competitiveness of Indonesian financial services industry	Through provision of incentives to financial services institutions to increase green products portfolio, encourage innovation, increase competency, information sharing and increase access to global public fund	Prudential Incentives Requirement on portfolio for Sustainable Finance Sustainable Finance Award Fiscal and non-fiscal incentives Development of green finance products, green bonds and green index Training and National Seminars on Sustainable Finance Green lending models for priority sectors Research and Development Information Hub Increase access of financial services institutions to Global Public Funds
Increase demand of environmentally friendly financing products	Through raising the public awareness and education on green investment and green financing	Campaign program to potential investors on green financial products
Increase oversight and coordination of sustainable finance implementation	Through the strengthening of risk management, corporate governance in environmental and social aspects, as well as the acceleration of the implementation of the Environmental Law	Regulation on Principles and Definition of Sustainable Finance in Indonesia Regulation on Risk Management in Environmental and Social Aspects Sustainability Report Forum on Sustainable Finance at National and Regional Levels

Source: Otoritas Jasa Keuangan

On 21 December 2017, OJK issued a regulation on green bonds that was geared towards raising capital for green projects. OJK Regulation Number 60/POJK.04/2017 (POJK 60) set out the standard for green bonds issuance in Indonesia (OJK, 2017b). This standard is an amalgamation of globally accepted green bond standards, such as the Green Bonds Principles, the Association of Southeast Asian Nations (ASEAN) Green Bonds Standards and the Climate Bonds Initiatives, with adaptation specific for the Indonesian capital market.

As with any other type of bond, issuers of green bonds must adhere to Indonesia's capital market regulations on debt securities. According to POJK 60, there are four additional characteristics of a green bond. First, green bonds can only be issued to finance eligible green projects, 11 types of which are specified by regulation including renewable energy, energy efficiency, biodiversity conservation, clean transportation, climate change adaptation, and sustainable waste management (OJK, 2017b).

Secondly, the regulation stipulates a minimum of 70% of proceeds from green bond sales shall be used to finance the agreed green projects. Third, issuers of green bonds have to manage the proceeds and report on the use of proceeds, and issuers should create a separate account to manage the proceeds or disclose the use of the proceeds in a specific note in the financial statement.

And lastly, the environmental benefit of the projects should be clearly defined and verified by an independent third party. The review should cover the performance of the green bond and projects by an independent third party and the result shall be reported annually to OJK. In the case that the underlying projects no longer meet the green project criteria, the issuer shall define an action plan for remediation and will be given one year to execute the action plan. In the case that the action plan fails to restore the green eligibility criteria of the project, the bond holders may demand the issuer to buy back the green bond or to increase the coupon rate.

OJK's effort to promote sustainable finance with green bonds through the enactment of POJK 60 was also based on consideration of the growth of green bonds globally. Since the first green bond was issued in 2007 by the European Investment Bank for USD807.8 million, green bond issuance has experienced phenomenal growth, reaching USD147.5 billion as of December 2017, although growth slowed in 2018 with total issuance of USD138 billion due to rising interest rates that weighed on debt issuance in the global market (Pefindo, 2019).

We view that strong market growth is attributable to growing demand for green financial instruments. This is because both investors and issuers are in need of investment diversification and seek innovative investments that pursue desirable environmental and social outcomes. Green bonds are attractive as they create opportunities for investment in environmental change, delivering environmental and financial returns. Therefore OJK predicts green bond markets in Indonesia and around the world will continue to grow.

Government green bond issuance

Indonesia's government has also been complimented for efforts in promoting sustainable finance. Through the Indonesian Ministry of Finance Climate Budget Tagging mechanism, it has identified more than IDR78 trillion (USD5.7 billion) in the national budget for fiscal year 2017 that was related to climate change impacts. This amounted to a 32% increase over the amount in the fiscal 2016 budget (Badan Kebijakan Fiskal Kementerian Keuangan Republik Indonesia, 2018).

This finding has encouraged relevant ministries and wider partners to also engage in environmentally responsible investment. As a result of active participation in the green bond market Indonesia made history as the first Asian country to sell a sovereign green sukuk (Islamic bond). The issuance successfully raised USD1.25 billion in February 2018 to fund a number of environmentally friendly projects such as renewable energy, green tourism, and waste management projects.

Due to this success, issuance of a second sovereign green sukuk with the total amount of USD2 billion was done in February 2019. A global sukuk was issued in the amount of USD750 million with a return of 3.9% annually and 5.5 years maturity (the "Wakala Sukuk") and a USD1.25

billion Trust Certificates issue with a yield of 4.45% per year and 10 years maturity will be listed on the Singapore Exchange and Nasdaq Dubai. This transaction took advantage of a window within a period of heightened volatility in the global capital markets and successfully priced the global sukuk with an oversubscription of close to 3.8 times (Direktorat Jenderal Pengelolaan Pembiayaan dan Risiko, 2019).

Public green bond issuance

After POJK 60 was issued, the state-owned infrastructure financing company, PT Sarana Multi Infrastruktur (Persero) (SMI), was the first company in Indonesia to issue green bonds. With 100% of the proceeds to be used to finance eligible projects, it exceeded the minimum 70% regulatory requirement. SMI issued the bonds under the shelf registration issuance scheme for a maximum of IDR3 trillion. It realised IDR500 billion in the first phase of issuance, against an initial target of IDR1 trillion. SMI offered a three-year interest rate of 7.55% and five-year rate of 7.8% (Pefindo, 2019).

Closely behind SMI's green bond issue, PT. Bank OCBC NISP Tbk. became the first commercial bank to successfully issue a green bond in 2018 with a value of USD150 million. On their first emission, International Finance Company (IFC) became the sole investor in the green bond.

Indonesia's FSI expanded beyond issuing green bonds in 2019 when one of the biggest banks in Indonesia, PT. Bank Rakyat Indonesia Tbk. (Bank BRI) became the first Indonesian company to issue a global sustainable bond. With the total value of the bonds offered at USD500 million, the bond issuance is viewed as a success, having been oversubscribed by more than 8 times or USD4.1 billion.

Aside from being in such high demand, the bond is also seen as a success due to the relatively low coupon which is 3.95% with 5 years maturity. With the coupon, the spread is only 168 bps or 35 bps higher than United States Treasuries and the Government of Indonesia's global bond respectively. This is a tantalising spread that has been achieved by a public company in Indonesia.

The low spread also reflects the low risk of default. Naturally, this is also due to Bank BRI's investment grade rating from Fitch Rating and Moody's. A few weeks after the bond issuance, the rating agency Standard and Poor's (S&P) also raised the rating of Bank BRI to investment grade.

There are strong prospects for growth in the supply of green bonds in Indonesia. In the future we hope other companies besides financial services will also issue them to finance projects that meet the green criteria. Potential enterprises such as the National Electricity Company (PLN) may use the proceeds to finance renewable energy power plants, and banks may propose them with the proceeds distributed to loan activities that are environmentally friendly or have environmental benefits.

Challenges in developing green bonds

Even though it has considerable potential, there are also challenges in developing green bond as a new investment product in the domestic market. One challenge is because there is still a limited track record of repayment and investment return for investors. Also, POJK 60 requires a buyback should the green criteria not be maintained which in return raises additional concerns about the prepayment risk.

The green bond market in Indonesia has strong potential to grow further. Current moderate penetration indicates it needs to be further developed as it faces challenges to reach a comparable scale with conventional investment. Therefore, to seize the opportunity, OJK needs to actively educate stakeholders and society to increase awareness of green investment, which may stimulate supply and demand in the green bond market in the medium term.

Also in the same period, taking into account the green bond market is still in the early stages of development, we expect the green criteria will likely evolve and find its most accurate criteria. Defining these criteria is also a challenge, as they may not meet every investor's definitions and needs. To date, there is also no common and broadly accepted standard for determining what is categorised as green.

Another challenge is to maintain the environmental benefits of the investment by ensuring the proceeds are used for designated projects and are properly managed throughout the lifecycle of the bond. This raises the need for assessment or review by an independent third party. In our opinion, promoting integrity through providing such reliable and transparent information should gain trust among investors and facilitate a credible green bond market. We envision to promote the development of the market in Indonesia in the medium term, including providing incentives or directing investors to allocate a minimum investment portion in green products as in the minimum requirement of government bonds.

Enhancing Corporate Governance of Listed Companies

Through sustainable finance, Indonesia's financial services institutions are naturally encouraged to improve governance. This is reflected in the roadmap as in the Long Term (2020-2024) when financial services institutions are expected to have integrated environmental and social aspects in their risk management and corporate governance practices, while also providing regular progress reports on sustainable finance implementation to the public (OJK, 2014).

The improvement of corporate governance aims to enhance the competitiveness of the FSI in the development of sustainable finance in Indonesia which eventually will increase the supply of sustainable financing. This increase in supply requires regulatory support and incentives to increase the volume of sustainable financing in priority economic sectors, namely sectors that have a high multiplier effect such as agriculture in the broadest sense, manufacturing, infrastructure, small and medium-sized enterprises (SMEs) and energy, to encourage innovation in developing environmentally friendly products, to improve the quality and provision of access to information and to improve access to the use of global public funds.

Incentives for implementing sustainable finance

In the long term, we have planned incentives linked to the implementation of the sustainable finance program to support the financial services institutions in enhancing their corporate governance especially in the priority economic sector. First is to develop incentives, both fiscal as well as non-fiscal, including conducting assessments on the establishment of incentive funds and instruments that address sustainable financing or investment needs in the priority economic sector. These incentives also aim to increase the efficiency of the funding process from financial services institutions to their clients. Second is to develop workshops and training to enhance the competencies of the industry to increase financing or investment activities in the sustainable finance priority economic sector (OJK, 2014).

Third is to develop financing or investment products and/or schemes with the aim to increase the sustainable finance portfolio including product assessment, development of the financing or investment guideline to support the financial services institutions' staffs in conducting analysis of the feasibility of implementing sustainable financing or investment in the priority economic sector. Fourth is to give out annual awards to financial services institutions deemed to have set the highest standard in implementing sustainable finance.

And lastly is the necessity to support sufficient infrastructure in the form of information technology system to facilitate the effective implementation of the sustainable finance program. The information technology system should focus on establishing interconnectivity of information between OJK and other relevant ministries.

Oversight of the sustainable finance program

Together with the incentives, the roadmap has also identified the need for proper oversight of the sustainable finance program to effectively improve corporate governance. The oversight will be done through the strengthening of risk management, corporate governance in environmental and social aspects, as well as the acceleration of the implementation of the Law No.32 of 2009 concerning Conservation and Management of the Environment.

The general policy shall comprise of first, establishing policies on sustainable finance principles that govern the obligations of financial services to observe the balance of the 4Ps (pro-growth, pro-jobs, pro-poor, and pro-environment), protection and management of natural resources, as well as participation by all parties in all financing activities in Indonesia (OJK, 2014).

Second, the general policy shall include policies governing the obligations of financial services to issue a sustainability report together with the annual report based on which the implementation of this policy will be adjusted to line up with each oversight division's level of readiness. And third, risk management policies governing the environmental and social aspects of financial services institutions financing activities shall be included.

The execution of the above mentioned policies requires an assessment that will result in specific policies or regulations to support the effective implementation of the sustainable finance program in each oversight division. The oversight especially needed in the banking and non-banking financial services industry such as risk management policy or regulation, target to increase the sustainable financing portfolio in the priority economic sectors, reporting as well as on the implementation of the sustainable finance program and evaluation on the level of soundness. With respect to capital market supervision, there is a requirement for specific policies and regulations governing the reporting mechanism on sustainable financing.

Collaboration among other institutions

As it involves multidimensional issues spanning environment, finance and also both domestic and international society, a number of the aforementioned incentives and oversight policies are carried out in collaboration with the relevant ministries and agencies including issuers in the capital market sector and the Indonesia Stock Exchange (IDX) as well as international agencies. This is to ensure effective integration and synergy among the ministries as well as between the national and sub-national governments. Seamless inter-agency coordination will help prevent the occurrence of bottlenecks that potentially come hand in hand with development activities.

Among others relevant to the sustainable finance program are the Ministries of Industry, Agriculture, Cooperatives and SMEs, Energy and Mineral Resources, Finance, National Development Planning (BAPPENAS), and Public Works and also such organizations as IDX and law enforcement agencies.

Some of the key issues that require coordination with respect to the implementation of sustainable finance in Indonesia are: first, solution to bottlenecks faced by each of the relevant ministries in implementing the sustainable finance program; second, determination of the sustainable financing or investment target for each priority economic sector on an annual basis; third, monitoring and evaluation of periodic achievements, including identifying the need to develop a supporting information technology system to supervise the implementation of sustainable finance; fourth, policy and regulatory coordination is expected to generate concrete action points to promulgate rules and policies that support the effective implementation of the sustainable finance program; and fifth, development of incentives, both fiscal as well as non-fiscal incentives, including conducting assessments on the establishment of incentive funds and instruments that address the sustainable financing and investment needs in the priority economic sector.

To facilitate the coordination and exchange of information relating to sustainable finance as well as to gauge feedback from the Financial services institution and other relevant stakeholders to refine the policy/regulation, it is necessary to establish a periodic sustainable finance forum. This sustainable finance coordination forum could be held at the national and regional levels. In addition, such a forum can also serve as a vehicle to monitor and evaluate the implementation of sustainable finance by the financial services sector.

Sustainability Disclosure by Financial Services Institutions

The third principle of the sustainable finance program in Indonesia is Environmental and Social Governance and Reporting Principle. This principle is carried out by implementing robust and transparent environmental and social governance practices in the financial services Institutions' operational activities. One form of transparency is by ensuring that the same practices are implemented by the financial services institutions and the progress of its implementation is periodically disclosed to the public.

Due to its significance, transparent practices also become one focus under the roadmap's medium term, for the years 2015 to 2019. During this period, the roadmap's strategic activities are focusing on the basic regulatory framework and reporting system (OJK, 2014).

It is expected that within this period, the basic regulatory framework and reporting system to be established and running well. A system to monitor the increase in financing volume of priority economic sectors that adopt sustainable finance principles is expected to be established, along with increased understanding, knowledge and competence regarding sustainable finance by human resources in the financial services sector. The provision of incentives and coordination with related agencies is also expected to be well executed and carried out regularly.

Reporting requirements

As already stated in the roadmap, to establish a reporting system the plan is to gradually enforce the issuance of a sustainability report as part of the integrated report for transparency to the wider public and for OJK supervision. Based on this, Indonesia has issued OJK Regulation Number 51/POJK.03/2017 (POJK 51).

POJK 51 on Application of Sustainable Finance to Financial Services Institutions, Issuers, and Public Companies acts as the Sustainable Finance Umbrella Policy to provide guidance to Indonesia's whole financial system. The rule requires the FSI to fulfill a set of criteria to implement sustainable finance in their operations (IFC, 2019). To implement sustainable finance, financial services institutions need to prepare and execute a Sustainable Financial Action Plan (OJK, 2017a).

The action plans are required to be submitted by each financial services institutions to OJK annually, carried out effectively by the financial services institutions and actively communicated to shareholders and all levels of organisation within the financial services institutions. Financial services institutions that implement sustainable finance effectively could be awarded with incentives by OJK.

To oversee and ensure effective implementation of sustainable finance, POJK 51 also requires financial services institutions to submit a sustainability report. As an integrated report, the sustainability report is announced to the public and contains economic, financial, social and environmental performance of financial services institutions, issuers, and public companies in carrying out a sustainable business (OJK, 2017a). The required report recognises and adheres to international reporting standards specifically related to sustainable finance reporting initiatives such as The Global Reporting Initiative (GRI).

GRI is one international sustainable finance initiative and its guidelines were adopted from the UN Environment Program, funded by the UN Development Fund. It serves as a guideline in developing sustainability reports, which it defines as a report made by a company in order to disclose or communicate to all stakeholders on its economic, environmental and social performance accountably (GRI, 2019).

Conclusion

Sustainable finance in Indonesia still holds untapped potential. This is apparent as the concept of sustainable finance is still in a relatively early stage of development. Despite the existence of a sustainable finance roadmap, rules, and financial products which have created positive traction in the development of sustainable finance domestically, the concept of sustainable finance still is not yet widely known both in society in general and in the business world. Therefore, to fully embrace the potential of sustainable finance, a detailed second phase of the roadmap which is for years 2020-2024 needs to be established with the right regulation and policies from the regulator, and also an active role of all parties involved to create an impactful sustainable finance in Indonesia.

As an integral part of the Republic of Indonesia, OJK consistently plays an active role in achieving the commitment of economically sustainable growth through its sustainable finance program. The program is carried out through the cooperation of various parties to create financial support to industries that practice sustainable finance principles. The sustainable finance program not only seeks to increase financing but also to increase the durability and competitiveness of financial services institutions, thus it can support a more resilient economy.

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Sustainability Initiatives of the SEC Philippines

Introduction

Safeguarding the future through sustainable finance

In November 2013, one of the strongest and most disastrous tropical cyclones, Typhoon Haiyan, wreaked havoc on the islands of the Philippines. With maximum sustained winds reaching 235 kilometres per hour at its core, it was ranked the worst typhoon to ever hit the country in terms of damage to property. It was responsible for more than 6,300 lost lives, 3.4 million affected families, and property damage amounting to USD 2.2 billion. Typhoon Haiyan was only the 23rd of 25 tropical cyclones that entered the Philippine area and 9th to make landfall in 2013. But this was not a once-in-a-decade occurrence. A research project in 2016 found that since the late 1970s, typhoons in Asia have intensified by 12-15%, and that the share of category 4 and 5 storms doubled or even tripled. In addition, the Global Climate Risk Index 2019 identified the Philippines as the fifth most-affected country by weather-related losses in the period 1998 to 2017, with total losses amounting to USD 2.93 billion.

In the words of Secretary Dominguez during a green finance forum held at the Bangko Sentral ng Pilipinas in the beginning of 2019, "Winter is here and it will wipe out not only the people of Westeros but of the entire planet. So goes the theme of the Game of Thrones and like the series, while everyone is busy fighting their own battles – Brexit, the budget here, the wall in the United States – no one is paying attention to Climate Change."

Climate change is real and we need to face it. Although sustainable investing is not the first thing that comes to mind when thinking of climate change solutions, it may be key to ensuring the continued growth of the Philippine economy. However, as this concept is fairly new to the Philippine market, many have initially dismissed sustainable financing as simply "environmental advocacy" or "grandstanding," and not really useful to real finance. As such, the Securities and Exchange Commission (SEC) of the Philippines has taken important steps in increasing focus on innovative financial products that address sustainability issues, as well as on the importance of environmental, social, and governance (ESG) risks disclosures.

Philippine capital market development

The Philippine capital market is both old and young. Its stock market is one of the oldest in Asia. The Manila Stock Exchange (MSE) and the Makati Stock Exchange (MkSE) were established on 8 August 1927 and 27 May 1963, respectively. Both exchanges eventually merged to form the present-day Philippine Stock Exchange on 23 December 1992. Despite the early beginnings however, the market is still in the early stages of development. The SEC is currently regulating only three types of financial products: equities, corporate bonds and mutual funds.

By the end of 2018, The Philippine Stock Exchange (PSE) had only 267 listed companies and a total of 322 issuances – which is not much different from the 223 listed companies and 303 issues twenty years prior. Unlike the stock market however, the country's bond market, while still quite underdeveloped, has been growing at a rapid pace. According to the Asia Bond Monitor report of the Asian Development Bank, the Philippines has the fastest growing bond market in emerging East Asia with a recorded 11.4% year-on-year expansion in the fourth quarter of 2018.

Although the Philippine capital market is currently doing well, there is still a need for further development. Other than the issue of limited availability of financial products in the market, another major reason for some difficulty in promoting the growth of the capital market is the fact that the country's financial sector is largely dominated by banks. Financial literacy, especially knowledge of the capital market, is still lacking. Companies, more often than not, would turn to banks for funding rather than raise funds in the capital market. Likewise, individuals would dismiss potential investment opportunities in the capital market due to lack of awareness and knowledge. In 2018, total assets of the Philippines banking system amounted to USD 320.84 billion;

while assets of non-bank financial institutions (i.e., investment houses and financing companies) totalled only USD 5.35 billion.

The SEC recognises the importance of a developed and well-functioning capital market and has renewed its efforts into deepening the Philippine capital market to increase local private investments, attract global investors, and enhance financial stability. Considering the astonishing amount of global capital looking for sustainable investments – which is currently estimated at USD 89 trillion (representing the assets under management of more than 2,000 firms who have signed on to the United Nations (UN) Principles for Responsible Investment) – the SEC could leverage on this opportunity to deepen the capital market and increase market participation.

Corporate Governance and Philippine Publicly Listed Companies

In the advent of the East Asian Financial Crisis in 1997, corporate governance (CG) was a major focus in the reform packages associated with the rescue programs for the countries. On closer inspection, key players in the market saw its relevance to the Philippines considering that the country had similar bad CG practices as Indonesia and Thailand, and strived to reform CG in the Philippines. Although introducing a corporate governance reform process in the Philippines did not come without challenges, with the cooperation of CG advocates, the private sector and the Philippine Government, good corporate governance was able to take root in the industry. Good corporate governance became one of the SEC's principal advocacies when it issued its first Corporate Governance Code in April 2002. The 2002 Code was applicable to corporations whose securities are registered or listed, grantees of permits / licenses and secondary franchise by the SEC, public companies and branches and subsidiaries of foreign corporations operating in the Philippines whose securities are registered or listed. The Code was issued to aggressively promote corporate governance reforms that aimed to increase investor confidence, develop the capital market and help the corporate sector achieve long term viability that will have a positive direct impact to the economy.

To further strengthen corporate governance in the country, the SEC then released the Revised Code of Corporate Governance (RCCG) that took effect in 15 July 2009. The noticeable difference between the 2002 Code and the RCCG is the deletion of branches and subsidiaries of foreign corporations operating in the Philippines whose securities are registered or listed. It is also in the RCCG that the SEC reintroduced the concept of stakeholders. In its amendment in 2014, the RCCG recognized the vital role that the stakeholders play in the corporate or business ecosystem.

Aware of the constant changes and developments in the global practice of corporate governance, the SEC released the SEC Corporate Governance Blueprint in 2015. This Blueprint is the SEC's roadmap for the five years to 2020 with the aim of raising Philippine corporate governance standards to a level at par with the global standards. The first action item for implementation in the Blueprint was the drafting of the 2016 Code of Corporate Governance for Publicly Listed Companies (PLCs). Following the recent developments, especially with the release of the 2015 G20 / Organisation for Economic Co-operation and Development (OECD) Principles of Corporate Governance, the 2016 Code's main features are: the increase in board responsibilities, competence and commitment of directors, protection of shareholders and other stakeholders, and promotion of full disclosure and transparency in both financial and non-financial reporting. Although the SEC Corporate Governance Blueprint only mentioned in passing the importance of sustainability reporting and that the regulator had not yet issued reporting guidelines that are specific to sustainability other than the Corporate Social Responsibility (CSR) Act, the 2016 Code fully addressed sustainability concerns through Principle 10, Recommendation 10.1. The Recommendation states that the Board should have a clear and focused policy on the disclosure of non-financial information with emphasis on the management of economic, environment, social and governance (EESG) impacts of the company's business, which underpin sustainability. Companies should adopt a globally recognized framework in reporting sustainability and non-financial issues.

Few but significant factors drove the SEC to come up with Principle 10. First, an increase in external pressures, including resource scarcity, globalisation and access to information, pushed the regulator to look at how businesses integrate sustainable practices in their operations. Secondly, it was brought to the attention of the SEC that sustainability reporting is already being practiced by 93% of the world's largest 250 companies and 75% of the top 100 companies in 49 countries. Regrettably, only less than 22% of publicly listed companies in the Philippines have published a report on their sustainability impact and performance. On a positive note, this handful of PLCs did not publish their sustainability reporting because of regulation. They were driven by either accidental awareness of sustainable business practices or by pressure from their institutional investors and stakeholders. Even so, it is important to note that this 22% of the total 275 PLCs in the country will not even make a dent in the sustainability reporting arena.

For the past decade, the SEC has done its part to promote good governance to its regulated entities as evidenced in the numerous Codes, Circulars and Rules and Regulations it has issued since 2002. Unfortunately, the exclusion of non-financial information, particularly on economic, environmental and social (EES) impacts, from the PLCs' submission of mandatory reports to the Commission can be attributed to the lack of regulation pertaining to non-financial disclosures with emphasis on EES. With the national programs and policies such as AmBisyon Natin 2040 which was pegged to the universal targets on sustainability like the UN Sustainable Development Goals (UN SDGs), agencies in the Philippine government are now aligning initiatives, rules and regulations towards the achievement of ESG universal and national targets.

Moving Towards a Sustainable Philippine Capital Market

Promoting sustainable finance in the Philippines

Sustainable finance has made substantial progress in the Philippine market. Currently the market is valued at USD 1.49 billion – with seven labelled green bond issuances and one labelled sustainability bond issuance (Table 1). Notably, five of these transactions have been in Philippine pesos or linked to Philippine pesos (about USD 775 million equivalent), which is critical to induce other Philippine firms to seek sustainable investors and grow the market.

The first Philippine labelled green bond was issued by AP Renewables, Inc.

(APRI) in 2016. It was a landmark transaction for climate finance as well as for capital market development in the Philippines. The innovative structure of the issue was able to pave the way for financing large infrastructure projects and enhancing bankability of projects. This transaction also won the recognition of the international market. The deal was awarded the 2016 Bond Deal of the Year by Project Finance International magazine of Thomson Reuters, and the Best Renewable Deal of the Year at the Alpha Southeast Asia Awards. It also received the title of "first" in a number of areas: first labelled-green bond in the Philippines; first Climate Bonds Initiative (CBI)-certified green bond in the Asia Pacific; first CBI-certified green bond for a single project in Emerging Markets; first project finance notes issued in Philippine pesos in the power sector, specifically for on-shore market; first credit-enhanced project notes in Southeast Asia (excluding Malaysia) since the Asian Financial Crisis; and first transaction of the Credit Guarantee and Investment Facility (CGIF) in the Philippine market.

With this ground-breaking issuance, the SEC, together with other regulators of the Association of Southeast Asian Nations (ASEAN) Capital Markets Forum (ACMF) recognised the potential of green finance in furthering the group's objective of supporting sustainable growth in the region and attracting greater global investments. As such, following the 25th meeting of the ACMF on 8 September 2019 in Jakarta, Indonesia, the ACMF committed to taking a leadership role in identifying green finance standards that can be applied in the ASEAN region and established the ACMF Green Finance Working Group. The working group is currently chaired by the Securities and Exchange Commission, Philippines (SEC Philippines) and the Securities Commission Malaysia (SC Malaysia).

As its first project, the group developed the ASEAN Green Bonds Standards (AGBS). And to ensure that the ASEAN Standards are in line with international principles, the ACMF engaged with the International Capital Markets Association (ICMA) and built the ASEAN Standards from the ICMA Green Bond Principles. The ASEAN Standard drafters also extensively consulted other specialists in this market, including investment banks, funds, multilateral development banks and even non-government organisations and ESG ratings providers. ASEAN then decided to take a step further by explicitly excluding fossil fuel power from the eligible use of proceeds under the AGBS. Fundamentally, the goal of the AGBS is to provide a framework that ensures transparency. In this way, investors would be able to determine for themselves, based on the disclosures required by the ASEAN Standards, if a particular offering qualifies under their mandate for green investments. Further, second-party opinions on an issuer's green framework, provided by firms with established expertise in this sector, likewise provide an additional tool for investors to make informed judgements regarding an offering's "green-ness."

Just a few months after the SEC adopted the AGBS through Memorandum Circular No.12 series 2018 on August 2018, the Rizal Commercial Banking Corporation (RCBC) became the first Philippine ASEAN green bond, and the sixth in the region. RCBC's listing of their 15 billion peso Green Bonds (USD 287 million) on 1 February 2019 represented two significant milestones for the Philippines: (i) it is the first peso-denominated green bond issued by a universal bank in the country, and (ii) it is the first bond in the Philippines to be issued under the ASEAN Green Bond Standards.

Feedback from investors regarding this issuance has been remarkable. Although RCBC is the first bank to issue a Green

Table 1: Philippine Green, Social, and Sustainability Bond Issues

No	Name of Issuer	Type of Project	Issue Size (million)	Issue Year	Tenure (years)
1	AP Renewables Inc.	Renewable Energy	PHP 10,700 [USD 225]	2016	10
2	BDO Unibank	Climate-smart projects including renewable energy, green buildings, and energy-efficient equipment	USD 150	2018	–
3	International Finance Corp.	IFC Climate Projects; climate-smart projects including renewable energy, and energy efficiency	PHP 4,800 [USD 90]	2018	15
4	Sindicatum Renewable Energy Co. Pte. Ltd.	Philippine renewable energy projects	PHP 1,060 [USD 20]	2018	10
5	China Banking Corporation	Climate-smart projects, including renewable energy, green buildings, energy efficiency and water conservation	USD 150	2018	–
6	Rizal Commercial Banking Corporation	Renewable energy, green buildings, clean transport, energy efficiency, pollution prevention & control	PHP 15,000 [USD 287]	2019	1.5
7	AC Energy Finance International Limited	Renewable energy	USD 410	2019	5 / 10
8	Rizal Commercial Banking Corporation	Renewable energy, green buildings, clean transportation, energy efficiency, pollution prevention and control, sustainable water management, environmentally sustainable management of living natural resources and land use, affordable basic infrastructure, access to essential services, employment generation, affordable housing and socioeconomic advancement and empowerment	PHP 8,000 [USD 154]	2019	2

Note: As of June 2019
Source: Securities and Exchange Commission, Philippines

Peso Bond, and only the fourth bank to issue bonds under Bangko Sentral ng Pilipinas (BSP) Circular 1010, its ASEAN Green Bond was three times over-subscribed. Furthermore, RCBC was able to achieve the lowest cost of borrowing of any bank as of its listing, at 6.7315%, for its 1.5-year paper. It also appears that RCBC's issuance has benefited from many of the ancillary advantages that green bonds are generally known to provide. One key benefit is a broadening of the investor base and higher visibility to ESG-oriented investors. For this specific RCBC ASEAN Green Bond, retail investors, particularly new retail investors, came out in force – comprising more than 60% of the issue.

Through RCBC's green bond issuance, the SEC gained proof of concept for ASEAN Green Bond Standards in the Philippines. The SEC was able to know for certain that:

1) Supply for green investment exists: local banks have green assets in their portfolios and have customer demand to justify raising green funds;

2) Competitive demand exists: particularly on the retail side, there is demand for banks to issue bonds under BSP Circular 1010;

3) The process of identifying existing green assets and obtaining the ASEAN Green label can recognise untapped value and provide better information to manage risk;

4) Overall development of the capital market: with a wider investor base available to fund a greater range of borrowers.

Following the success of the ASEAN Green Bond Standards, both locally and within the region, the SEC together with the other ACMF members again worked to develop the ASEAN Social Bond Standards (ASBS) and the ASEAN Sustainability Bond Standards (ASUS) to complement the AGBS that was launched in November 2017. Once again, the ASEAN regulators engaged with ICMA and built the ASEAN Standards from the globally-accepted ICMA Principles and were able to launch both ASEAN standards in October 2018 during the 2nd ASEAN Capital Conference.

To further support the Philippines' sustainable development needs, the SEC adopted the ASBS and ASUS through Memorandum Circular No.9 series 2019 (ASBS), and Memorandum Circular No. 8 series 2019 (ASUS) in April 2019. Again, RCBC was the first mover and issued the first Philippine ASEAN Sustainability Bond in June 2019. From the initial USD 96 million offer, RCBC upsized their issuance to USD 154 million due to the strong demand they received from retail investors.

Through these transactions, the SEC saw that green funding attracts clients looking to finance sustainable solutions. A loan portfolio that includes sustainable assets is generally less exposed to risks posed by new environmental regulations (e.g., carbon tax; increased emission standards), technological obsolescence (e.g., coal fired power vs energy storage in batteries, distributed generation) and climate change (e.g., damage wrought by increasingly violent weather). These features make green funding a good risk management strategy for both sides of the balance sheet, with greater diversification on the liability side and healthier loans or other assets on the other side. As such, the SEC is continuously engaging the market to promote awareness of sustainable investment and encourage greater investment in country.

Promoting sustainability reporting in the Philippines

Hand in hand with the promotion of green, social, and sustainable finance, the SEC also recognised not only the growing global interest, but also the importance of ESG transparency in achieving a sustainable market. And so, on 15 February 2019 the SEC issued SEC Memorandum Circular No. 4, Series of 2019 or Sustainability Reporting Guidelines for Publicly Listed Companies. The intention is to promote sustainability reporting that: is both relevant and value-adding to the Philippine PLCs; will help PLCs identify, evaluate and manage their material EES risks and opportunities; will help them to assess and improve their non-financial performance across EES aspects of their organization to optimize business operations; will improve competitiveness and long term success; will provide a mechanism to allow companies to communicate with stakeholders, including current and potential investors; and will enable PLCs to measure and monitor their contributions towards achieving universal targets of sustainability, such as the UN SDG and national policies and programs, such as AmBisyon Natin 2040. The Guidelines include a Sustainability Reporting Framework that builds upon four globally accepted frameworks: Global Reporting Initiative's (GRI) Sustainability Reporting Standards, International Integrated Reporting Council's (IIRC) Integrated Reporting (IR) Framework, Sustainability Accounting Standards Board's (SASB) Sustainability Accounting Standards and the recommendations of the Task Force on Climate-related Financial Disclosure (TCFD). Sustainability Reporting Principles, Management Approach Component and Materiality Assessment Process are also included in the Guidelines to assist PLCs in identifying what indicators or topics are material to them and should be disclosed using the Sustainability Reporting Template that the SEC prescribed.

In addition, the Guidelines and the template also provide for a section related to the 17 UN SDGs. Disclosure would be required on how companies' products and services contribute positively and negatively to the UN SDGs. The Guidelines and the template omit the required disclosure on the governance of the organization as companies are already required to report this to the SEC through the Integrated Annual Corporate Governance Report (I-ACGR).

The Guidelines adopted a "comply or explain" approach for the first three years after implementation. This means that companies would be required to attach the Sustainability Reporting Template to their Annual Reports but they could provide explanations for items on which they still have no available data. The first submission shall be attached to the PLCs' 2019 An-

Figure 1: ASEAN Green Bond Standards Development

Source: Securities and Exchange Commission, Philippines nual Reports to be submitted in 2020.

The SEC hopes that the guidelines will boost both the quantity and quality of sustainability reporting in the country, provide current investors with more actionable information that will assist them in their investment decisions, and attract additional investors including those from overseas to invest in Philippine companies.

The Future of ESG in the Philippines

Challenges to drive ESG initiatives in the Philippines

When the SEC first began to promote sustainable finance in the Philippine market through the issuance of the Guidelines for ASEAN Green Bonds, the reception was lukewarm. Operating in an emerging economy, Philippine investors and issuers are just concerned with their bottom lines. And the SEC often faced the question: “What’s in it for me?” However, recently the SEC is seeing that corporations are increasingly concerned with the sustainability of their companies and are paying third parties to have their ESG scores assessed. Likewise, investors are demanding more information on their investments and the risks they are exposed to over the medium and long term.

Some of the key challenges that the SEC, as well as other regulators of the financial industry, will have to address include:

1) How to effectively facilitate an enabling environment where innovative financing solutions like green bonds and transparency through ESG disclosures are encouraged.

2) How to effectively create awareness of sustainability reporting for PLC boards and management.

In this regard, it is ideal for a Sustainability Champion to come from the board level. Leadership and commitment should come from the top for the initiative to have a trickle-down effect on employees. It is easier for the organization to push forward with its ESG reporting if there is full support from the board. However, there should be awareness on the part of the board and management to get their buy-in on this initiative.

The times are changing, and the Philippines will be forced to adapt or be overcome by the effects of a global phenomenon that cannot be overturned. The ESG initiatives that the SEC has been promoting so far are critical tools in helping to ensure a resilient Philippine economy. These initiatives represent the SEC’s understanding that markets will flourish when transparency requirements enable investors to make informed governance, management and investment decisions.

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RAPEE SUCHARITAKUL

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How ESG Can Contribute to the Development of the Thai Economy

Introduction

Sustainability has significantly caught the attention of legislators, governments, regulators, asset managers and investors worldwide as indicated by the increasing amount of funds being allocated to sustainable finance in recent years. The matter was spurred by international agendas, particularly the Paris Agreement and the United Nations (UN) Sustainable Development Goals (SDGs) which have guided many countries to develop their own regimes such as the EU Action Plan on Financing Sustainable Growth, the UK Stewardship Code, the Financial Stability Board (FSB) Task Force on Climate-related Financial Disclosures (TCFD) and China's green credit ratings. The UN Principles for Responsible Investment (UN PRI) recorded a 31% increase in assets under management (AUM) from USD68.4 trillion in 2017 to USD89.7 trillion in 2018. Furthermore, the International Organization of Securities Commissions (IOSCO) report also indicates an upward trend in commitment to incorporate Environmental, Social and Governance (ESG) elements in terms of investment analysis and process by institutional investors. The growth in sustainable investing has been driven by both retail and institutional investors, as seen in their concern with the impact of climate-related risks and opportunities on investment returns. In response to these demands, providers of market information, including MSCI, FTSE, STOXX and Dow Jones, have developed sustainability indices and financial products such as green bonds to serve investors' needs.

The opportunities and benefits of sustainable finance have been recognized by policy makers, regulators and market participants in the Association of Southeast Asian Nations (ASEAN) capital market. The region is in the process of allocating and creating viable projects for ESG investment to achieve a holistic ecosystem and create an ESG investment destination through the ASEAN Capital Markets Forum (ACMF) framework. Meanwhile, domestic interests will be formed to serve investors' demand such as an alignment with ESG-related standards. With the objective of having ASEAN-listed companies as an investable vehicle, in 2011 the ACMF launched the Corporate Governance (CG) scorecard, which includes ESG elements in the methodology for CG scorecard assessment in ASEAN in order to raise the CG standards and practices of publicly listed companies in ASEAN. Furthermore, the ACMF, in cooperation with the International Capital Market Association (ICMA), adopted ASEAN Green, Social and Sustainable Bond Standards in 2017 and 2018.

Thailand's capital market has been keeping up with various changes and fast paced developments to universalize its standards on sustainability and supervision of market participants along with increasing the public's awareness of ESG. The Stock Exchange of Thailand (SET) has been promoting the quality of Thai listed firms through establishing the Thailand Sustainability Investment (THSI) list and the SETTHSI Index in 2015 and 2018, consecutively. These initiatives include listed companies which achieve outstanding performance on an annual assessment of ESG standards.

Listed companies have long been considered the backbone of Thailand's economy, accounting for 103% of the country's gross domestic product (GDP), and 18% of ASEAN's GDP in terms of market capitalization in 2018. As they have been gaining global recognition, Thai listed companies have pursued an integral role in contributing to the economy's sustainability by emphasizing the importance of ESG practices as they move from basic CG to issues of environmental and social responsibility.

Thai listed companies have been encouraged to operate their businesses on a sustainable basis with a focus on social responsibility and good governance in order to inspire other businesses in the move towards sustainability. They are required to disclose information that reflects social responsibility in their sustainability reports, annual reports, or the annual registration statements as well as to provide information on greenhouse gas emissions and measures of greenhouse gas reduction since this information will be useful to investors who are increasingly interested in companies with a sustainable business growth strategy. In 2018, there were a total of 704 companies listed on the stock exchange with a combined profit of USD29 billion, accounting for 5.9% of the country's GDP. The total revenue of Thai listed firms has grown constantly from 2016, reaching USD406 billion in 2018, which is equivalent to over 80% of the country's GDP. Consequently, incorporating ESG efforts in the agenda of listed companies will create sustainability for the whole system, as listed firms are still of prime importance to the economy.

The ongoing challenges for listed companies are to quickly respond to investor demand and changing trends in the capital market and real economy as well as to maintain accountability to attract global investors to support sustainable economic growth in the region.

Building the Supply Side through Sustainability of Listed Companies

The core of ESG development is to have listed companies embrace ESG issues for the sake of their own sustainability. In this regard, the board of directors of listed companies can play a crucial role by recognizing the importance of ESG and considering it when formulating the company's strategy, risk management, and monitoring plans thereby putting the company on a sustainability pathway. Rather than adding regulations to force listed companies to adopt ESG concepts, the Securities and Exchange Commission, Thailand (SEC Thailand) has played the role of providing guidance, as well as raising awareness, disseminating knowledge and providing training and education on sustainability issues.

CG in substance and CG Code

To pave the way for the sustainable development of listed companies, the SEC Thailand has encouraged listed companies to put good CG into practice, or, as it is called, "CG in substance". In 2016, the SEC Thailand together with SET and representatives from listed companies developed a revised version of the CG Code as a guideline for boards of directors of listed companies.

This CG Code was based on the SET Principles of Good Corporate Governance for Listed Companies 2012 and revised to reflect current international standards and trends by focusing on the roles and responsibilities of boards of directors. The revised CG Code consists of 8 principles (Table 1).

The revised CG Code was launched in 2017 on an 'apply or explain' basis whereby company boards are encouraged to apply each Principle and Sub-Principle that are suitable to the company's business. If any of the Principles or Sub-Principles cannot be applied or are not applicable, the board shall provide an explanation.

After launching the CG Code, the SEC Thailand conducted a survey of listed companies in 2017 and found that 68% of 167 respondents would adopt the revised CG Code. It is hoped that this initiative encourages boards of directors to adopt CG in substance. The outcome of this initiative is expected to be revealed to the public in early 2020.

Framework for disclosure

CG disclosure is another mechanism initiated by the SEC Thailand. Prior to 2018, companies had been required to disclose information in the annual report and Form 56-1 in accordance with the CG principles on a 'comply or explain' basis, so that investors could easily access the information presented in an easy to understand format. In accordance with the CG Code launched in 2017, from 2018 onwards companies are required to disclose information in accordance with the revised CG principles on an 'apply or explain' basis.

Visibility enhancement

- **Corporate Governance Report:** Domestically, the Corporate Governance Report (CGR) developed by the Thai Institute of Directors (Thai IOD) has encouraged listed companies to focus on improving their CG. Evaluation is based on the extent of compliance with the CG principles and publicly disclosed information. The CGR gives ratings of one to five stars and discloses the names of companies with three stars and above. In 2018, of over 700 listed companies, 139 (125 in SET (main board) and 14 in Market for Alternative Investments (MAI)) received 5 stars, while 238 received 4 stars and 174 companies received 3 stars.

- **SETTHSI Index:** In 2018, with development support from other organizations including the SEC Thailand, SET launched the SETTHSI Index which is comprised of listed companies selected from THSI list. Companies on the THSI list must score above 50% on the voluntary sustainability assessment or have already been included in the Dow Jones Sustainability Indices (DJSI), one of the most globally recognized sustainability indices. They are also required to meet criteria on CGR, company qualifications, shareholder equity, net profit and impact on ESG.

  SET has steadily promoted the THSI list and the SETTHSI Index as

Table 1: CG Code Principles

	Description
Principle 1	Establish clear leadership role and responsibilities of the board.
Principle 2	Define objectives that promote sustainable value creation.
Principle 3	Strengthen board effectiveness.
Principle 4	Ensure effective CEO and people management.
Principle 5	Nurture innovation and responsible business.
Principle 6	Strengthen effective risk management and internal control.
Principle 7	Ensure disclosure and financial integrity.
Principle 8	Ensure engagement and communication with shareholders.

Source: Corporate Governance Code for Listed Companies 2017 (SEC Thailand) well as announcing the next series. In 2018, number of listed companies included in the THSI increased to 73 with total market capitalization of USD320.9 billion, representing 59.8% of the combined SET and MAI market capitalization of USD536.7 billion (as of October 2018). In June 2018, SET announced the list of 45 companies to be included in the SETTHSI Index.

- **Dow Jones Sustainability Index:** In terms of visibility in international markets, Thai listed companies have been included in the DJSI since 2012. Between 2012 and 2018, the number of listed companies included in the DJSI World index increased from 2 to 8 and in the DJSI Emerging Markets index increased from 3 to 20.

  Market capitalization of Thai listed companies in the DJSI World index tripled from USD45.8 billion in December 2012 (12.3% of total market capitalization) to USD138.2 billion in December 2018 (27.5% of total market capitalization) (Figure 1).

  Meanwhile, market capitalization of Thai listed companies included in the DJSI Emerging Markets index increased over four times from USD55.5 billion in December 2012 (15% of total market capitalization) to USD231.1 billion in December 2018 (46% of total market capitalization).

Promoting Green, Social and Sustainability Bond Issuance

Green bond

Global challenges such as climate change, air pollution and poverty have been recognized by various industry bodies, including bond markets. In 2007, the first ever green bond was issued by the World Bank after a group of European pension funds wanted to invest in climate-friendly products. The World Bank connected the dots and created a new way to direct financing from investors to climate projects. Since the first green bond was issued, the value of global green, social and sustainability bonds issuance amounts to around USD150 billion, with ASEAN issuance accounting for USD4 billion.

Over the past few years, Thailand has made significant improvements related to green bonds. In 2018, the SEC Thailand developed green bond regulation, based on the ICMA Standard which has four components including:

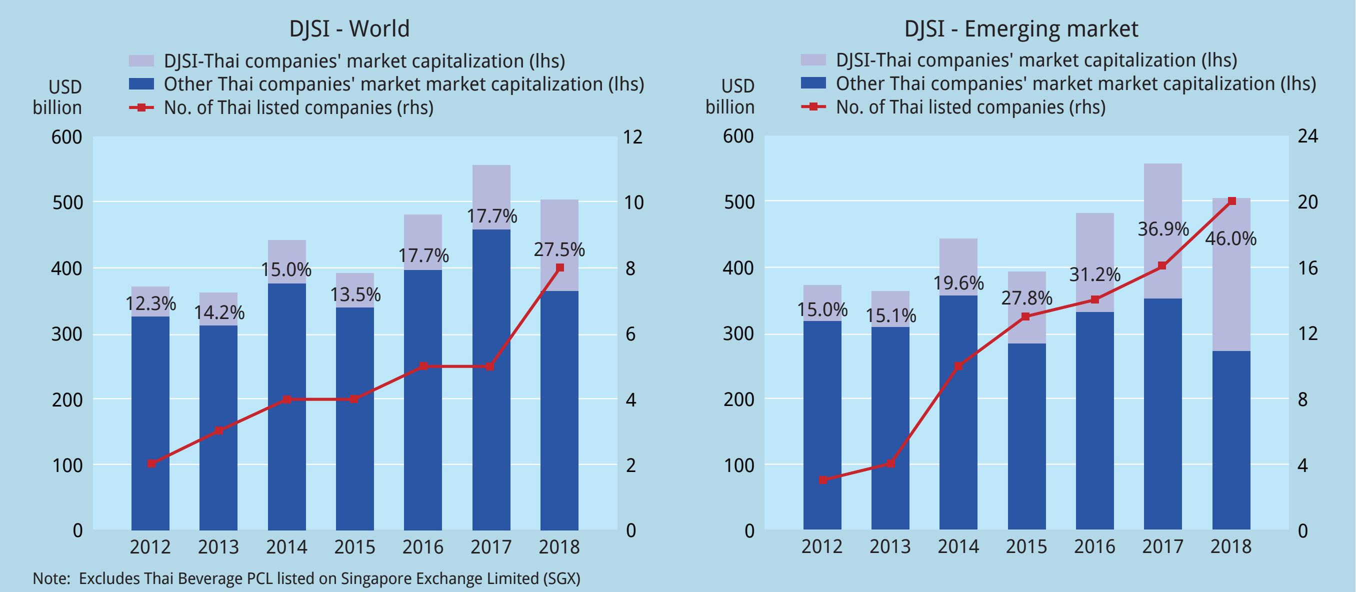
1) Use of proceeds;
2) Process for project evaluation and selection;
3) Management of proceeds; and
4) Reporting.

In December 2018, B. Grimm Power Public Company Limited (BGRIM), one of Thailand's leading private power producers was the first private company in Thailand to launch a green bond, with an issue worth USD161 million purchased entirely by the Asian Development Bank (ADB). BGRIM was also the first Thai private company issuer that was certified by Climate Bonds Initiative (CBI), a not-for-profit international organization working for climate change solutions. TMB Bank Public Company Limited (TMB) was the first commercial bank to launch a green bond with an issue worth USD65 million and sold to International Finance Corporation (IFC), a member of the World Bank Group in 2018.

The way forward for social and sustainability bond

To encourage the issuance of bonds to raise capital for social and sustainability projects in Thailand, the SEC Thailand is developing regulations for social and sustainability bonds, including the issuance process and disclosure requirements, in line with international standards such as the ASEAN Social and Sustainability Bond Standards under the ACMF and ICMA. The regulations will come into effect by the

Figure 1: Number and Market Capitalization of Companies Included in DJSI



Note: Excludes Thai Beverage PCL listed on Singapore Exchange Limited (SGX)
Source: The Dow Jones Sustainability Indices, The Stock Exchange of Thailand

end of 2019. The SEC Thailand believes that clarity of products labeled "green," "social" or "sustainability" can increase investor demand for, and consequently supply of, products. Currently, the first sustainability bond aligned with ASEAN Sustainability Bond Standards under the ACMF was issued in 2018 by Kasikorn Bank Public Company Limited (KBANK) worth USD100 million. The whole amount was offered to institutional investors via the bank's Hong Kong branch.

Creating Demand and Market Force from Institutional Investors

Investment Governance Code (I Code)

Recognition of the importance of institutional investors in driving the governance of listed companies has significantly increased around the world, including in Thailand. In Q1/2019, local Thai institutional investors held 12% of the value of SET, almost double their share in 2012 (Figure 2). Institutional investors have become one of the most significant equity owners and key influencers in the capital market.

The global market recognized the importance of institutional investors and started to adopt a stewardship code as a guideline to promote an active role for institutional investors to act for the best interests of their beneficiaries. The code includes obligations in a number of key governance areas such as conflicts of interest and also the consideration of ESG.

The SEC Thailand has also recognized the importance of a stewardship code and adopted the I Code in 2017. The I Code was modeled on the UK Stewardship Code which contained investment governance principles and guidance reflecting current international standards and best practices for responsible and effective stewardship over investments by institutional investors (Table 2). Engagement with stakeholders such as the Office of Insurance Commission, Government Pension Fund, Social Security Office, the Association of Investment Management Companies, directors and management of asset management companies was carried out before developing this I Code.

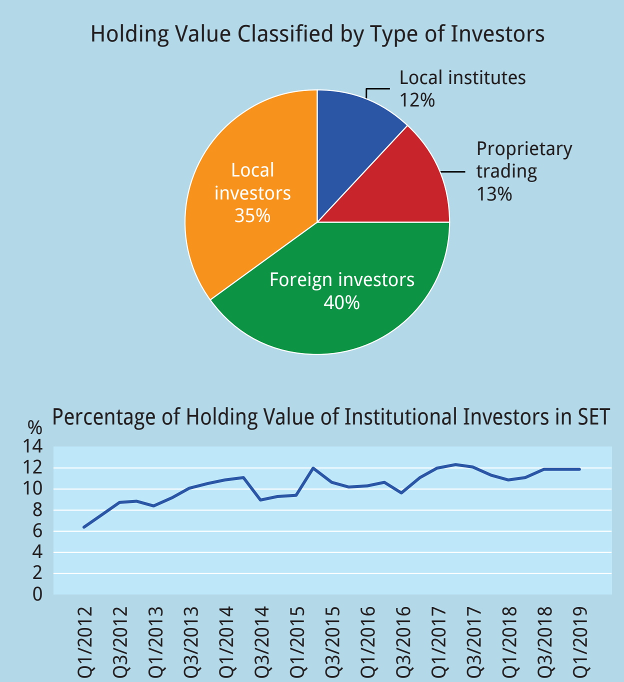
I Code signatories

Since it was launched by the SEC Thailand in 2017 the I Code now has 59 signatories, including 26 asset management companies, 14 life/non-life insurance companies, 11 provident funds, 3 securities companies and 5 government agencies/association/other institutes. These 59 signatories have total AUM of around USD307 billion, or approximately 61% of GDP. The signatories regulated by the SEC Thailand are required to notify their I Code disclosures and any updates to the SEC Thailand. The list of the SEC Thailand-regulated signatories will be published on the SEC Thailand website for the benefit of the investors.

Thai CG Fund

In 2017, the Federation of Thai Capital Market Organizations (FETCO), a group of asset management companies, Thailand Development Research Institute (TDRI), and organizations and foundations that work in the area of corporate governance launched the "Thai CG Fund". The fund has a policy to invest in listed companies in both SET and MAI that have good CG and have passed the screening by CG Scoring rank of the Thai IOD and Collective Action

Figure 2: Holding Value of Institutional Investors



Note: As of March 2019
Source: The Stock Exchange of Thailand

Table 2: The Principles of the I Code

	Description
Principle 1	Adopt a clear written investment governance policy.
Principle 2	Properly prevent and manage conflicts of interest and prioritize advancing the best interest of clients.
Principle 3	Make informed investment decisions and engage in active ongoing monitoring of investee companies.
Principle 4	Apply enhanced monitoring of and engagement with the investee companies if monitoring pursuant to Principle 3 is considered insufficient.
Principle 5	Have a clear policy on exercising voting rights and disclosure of voting results.
Principle 6	Act collectively with other investors and stakeholders as appropriate.
Principle 7	Regularly disclose the investment governance policy and compliance with the policy.

Source: I Code for Institutional Investors (SEC Thailand)

Coalition of the Private Sector Against Corruption (CAC) companies. Currently, 11 asset management companies have joined this initiative with a net asset value of USD191 million, or approximately 1.4% of overall net asset value of funds in Thailand (Table 3).

ESG Development under the ACMF and the Way Forward

At the ASEAN level, the importance of integrating the ESG factors into investment decision-making and risk management processes of listed companies has been well recognized among ASEAN capital market regulators. In 2011, the ACMF with support from the ADB introduced the ASEAN Corporate Governance Scorecard (ASEAN CG Scorecard) based on the Organisation for Economic Co-operation and Development (OECD) principles with the key objectives of raising CG standards and practices, enhancing visibility and investability of ASEAN listed companies, and promoting ASEAN as an asset class as well as improving investor confidence. In response to the update of OECD principles and recommendations on CG, the ACMF has revised the methodology with the introduction of independent external validation in addition to the existing peer-review process. The group has also put great effort into enhancement of the CG of listed companies in ASEAN via the creation of the ASEAN CG Conference and Award which is seen as a key mechanism to raise awareness and promote the high quality of ASEAN listed companies. The top 50 ASEAN listed companies announced in 2018 were selected from 570 participating listed companies from Indonesia, Malaysia, the Philippines, Singapore, Vietnam and Thailand, up from 555 companies in the previous round.

Sustainability/ESG indices have been developed in ASEAN capital markets such as FTSE4Good Bursa Malaysia Index, SRI-KEHATI Index, SGX Sustainability Index. In April 2016, FTSE Russell together with ASEAN Exchanges initiated the new ESG index called FTSE4Good ASEAN 5 Index, which consists of the listed companies on the five ASEAN exchanges with recognized sustainability and ESG practices, namely Singapore, Indonesia, Malaysia, the Philippines and Thailand. At present, the countries with the largest presence in the 104-company index of ASEAN listed companies are Thailand and Malaysia, with 33 companies each (Figure 3). However, market size, stage of development of the companies and cost of assessment remain key challenges for small firms to be included in the asset class.

Table 3: CG Fund Thailand Report

Asset Management Company	Fund Code	NAV (as of Dec. 2018) (USD million)	NAV (as of Jan. 2019) (USD million)
BBL Asset Management	B-THAICG	15.0	15.6
Bangkok Capital Asset Management	BMSCG	16.7	18.0
Kasikorn Asset Mangement	KTHAICGRMF	5.6	6.1
Krungsri Asset Management	KFTHAICG	4.0	4.2
Krung Thai Asset Management	KTBTHAICG-A	25.0	25.8
MFC Asset Management	M-SELECTCG	2.7	2.7
SCB Asset Management	SCBTHAICGP (for institutional investors)	1.0	0.02
TISCO Asset Management	TISESG-A	1.4	1.5
TMB Asset Management	TMB-THAICG	50.0	51.7
UOB Asset Management	UTHAICG	50.3	53.2
Talis Asset Management	TLEQ-THAICG	0.8	0.8
	Total	187.1	191.7

Note: As of 12 February 2019
Source: CG Fund Thailand Report

Other than the equity element, the ACMF, in cooperation with ICMA, adopted the ASEAN Green Bond Standards in 2017 and Social and Sustainability Bond Standards in 2018. Currently, there are 8 issuances aligned with ASEAN Green Bond Standards from the Philippines, Singapore, Malaysia and Thailand as well as 1 issuance aligned with ASEAN Sustainable Bond Standards issued by a Thai company in 2018. Throughout 2018, The ACMF also held stakeholder engagement sessions throughout 2018 including conferences, roundtables, and roadshows to promote and enhance awareness about the ESG initiatives of the ACMF.

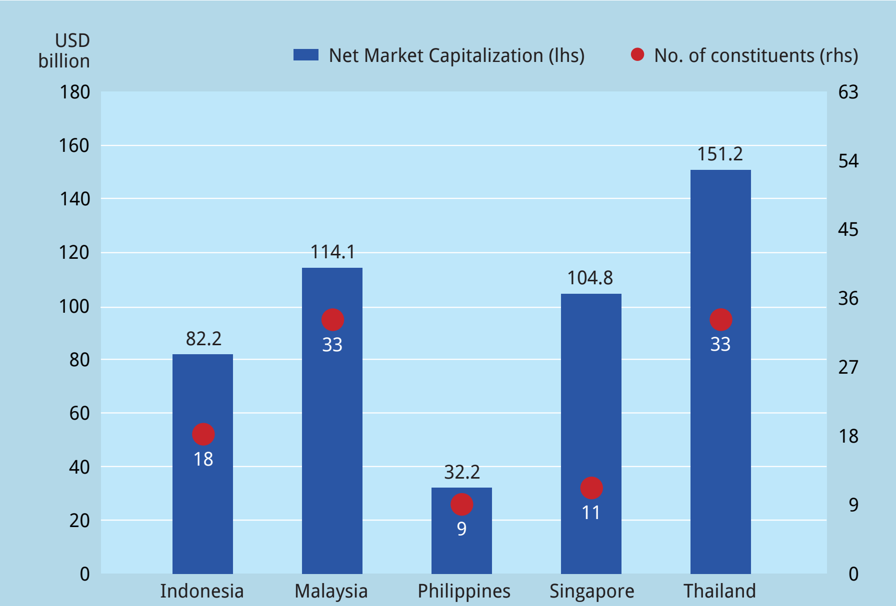
In 2019, the year of Thailand's ASEAN Chairmanship, under the theme of "Advancing Partnership for Sustainability" and its goal to enhance connectivity, sustainability and resilience as key pillars of financial cooperation in ASEAN, the ACMF proposed a building block to strengthen sustainable capital markets as a driver for sustainable growth in the regional economy by creating the Roadmap for ASEAN Sustainable Capital Market (the Roadmap). The Roadmap will set a concrete direction for regulators to create an ecosystem for sustainable capital markets as well as to enhance the capital market. In this regard, in April 2019, the 23rd ASEAN Finance Ministers' Meeting (AFMM) also endorsed the development of the Roadmap and its future implementation.

The Roadmap has been built on 3 broad strategic directions that may be revised in accordance with the changing environment and development of capital markets as well as 5 mechanisms to build market force and ASEAN-wide participation as follows:

- **3 Broad Strategic Directions**
  1) To define common sustainability elements that could be applied by ASEAN market players in catering to the needs of investors worldwide.
  2) To work with capital market information providers and institutional investors to create products that promote market force for sustainability.
  3) To enable companies of all sizes and economies of all stages of development to benefit from the initiatives.

- **5 Mechanisms**

Figure 3: Breakdown in FTSE4Good ASEAN 5 Index by Country



Source: FTSE Russell Factsheet, March 2019

In response to the 3 broad strategic directions as well as to eventually build market force and to create ASEAN-wide participation in the capital markets for sustainable development, 5 mechanisms are therefore derived. The proposed mechanisms include ESG information and disclosure standards, analytics tools, investor engagment, soft intervention and inter-agency coordination and education. The examples of both existing and potential initiatives to serve each mechanism have been discussed and subject to further feasibility study before integrating into the ACMF implementation plan. (Figure 4). As for the next step, the ACMF will continue the existing and on-going initiatives already agreed among the members and conduct further feasibility study of potential initiatives under the Roadmap with an aim to ensure the efficiency of the implementation stage.

Conclusion

Continued development of the Thai economy is driven to a very large extent by activities of companies that are listed on SET. In this connection, it is of utmost importance that these companies play key roles in the sustainability of the economy and the country itself. But in order to drive forward the issues of sustainability there must be a multi-pronged approach to promote awareness from within the companies themselves and to develop a complete ecosystem that will create a long-term roadmap in this area. Regulations alone cannot provide all the answers. Rather, all the stakeholders, whether they be companies that raised funds from the public, market intermediaries who facilitate both-fund raising and investment from the public, investors both institutional and retail, all have significant parts

Figure 4: 5 Mechanisms to Drive Sustainable Capital Market

To build market force and create ASEAN-wide participation

ESG information & disclosure standards	Analytics tools	Investor Engagement	Soft intervention	Inter-agency cooperation & education

Existing initiatives and examples of potential initiatives*

ESG information & disclosure standards

- ASEAN Green, Social and Sustainability Bond Standards
- Common elements or standardization of corporate disclosure
- Listing of bonds in exchanges
- Private placement corridor/bond information platforms

Analytics tools

- ASEAN CG scorecard
- Screening & metrics/ scorecards/ indices
- Sustainability/ green fund standards

Investor Engagement

- Roadshow & Investor Engagement
- Guideline for ESG investment disclosure
- Institutional investor's role enhancement

Soft intervention

- Centralized grant scheme
- Green infrastructure investment (e.g. guarantee, subsidy)
- Catalyst mechanism (e.g. Credit enhancement)
- Policy alignment with commercial purpose

Inter-agency cooperation & education

- Coordinating with banking regulator and Ministry of Finance to ensure alignment of initiatives
- Awareness of supply and demand side (e.g. capacity building, education)

*Subject to further feasibility study and agreement from all members

Source: ASEAN Capital Markets Forum

to play. Government agencies and central banks as well as capital market regulators also need to join hands in creating proper incentives and encouragement so that the issues of sustainability will be placed on the national agenda. Only then can we ensure that the capital market will succeed in its mission of creating a sustainable economy for the well-being of the people of the country.

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RAPEE SUCHARITAKUL

Former Secretary-General, Securities and Exchange Commission, Thailand
Former Chairman, Capital Market Supervisory Board

Mr. Sucharitakul was Secretary-General of the Securities and Exchange Commission, Thailand (SEC Thailand) from May 2015 to April 2019 and also served concurrently as the Chairman for Capital Market Supervisory Board during his term.

Mr. Sucharitakul joined the SEC Thailand at its establishment and devoted 13 years of his career to capital market development and supervision. He left the SEC Thailand in 2005 to take on several positions in private and public organizations, where he gained extensive experience in policy making, consultancy and management. Some of his previous posts include member of the Board of Governors of the Stock Exchange of Thailand, director of the Thailand Futures Exchange, director of the Federation of Thai Capital Market Organizations, director of the Thai Institute of Directors Association, director of KASIKORNBANK Plc., executive chairman of KASIKORN Securities Plc. and KASIKORN Asset Management Company Limited, advisor to the President of Muang Thai Life Assurance Plc., and independent director of Big C Supercenter Plc. He was also a member of the State Enterprises Policy Committee before rejoining SEC Thailand as a Secretary-General in 2015.

Mr. Sucharitakul earned an LLM in Commercial Law from the University of Bristol, and an LLB (with honors) from the University of Essex in the United Kingdom.

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The Value of Corporate Social Responsibility: Decomposing Positive and Negative Deviations from the Norm

Introduction

Classical finance theory suggests that the primary purpose of companies is to maximise shareholders' value (Berle and Means, 1932; Friedman, 1970). However, there is a growing counter-argument that firms should also be more socially conscious, consider wider stakeholder opinions and follow a more balanced business model that can benefit both the bottom line and society (Freeman, 1984).

What is the voice from corporates? A joint study by the United Nations Global Compact and Accenture in 2018 found that 95% of 1,000 surveyed chief executive officers (CEOs) in 108 countries across 26 industries as participants around the globe feel a personal responsibility to ensure their company has a core purpose in society, and 80% believe that demonstrating a commitment to societal purpose is a differentiator in their industry. Lacy et al. (2010) also found that 93% of the 766 surveyed CEOs believe that Corporate Social Responsibility (CSR) will be an "important" or "very important" factor for their organization's future success.

Investors are also demanding more corporates to take up their social responsibility. The Forum for Socially Responsible Investing in the United States (USSIF) showed that socially responsible investing (SRI) currently expanded to US$12 trillion at the start of 2018, representing 26% of all assets under management in the United States (USSIF, 2018). Moreover, there are 2,372 organizations such as asset owners, investment managers or their service providers around the world have become the signatories of the Principles for Responsible Investment (PRI) agreement with US$86.3 trillion assets under management as of March 2019 (PRI, 2019).

Various governments have also started to roll out concrete rules and regulations related to CSR. For example, since 2014, the Indian government has required each firm to set aside 2 per cent of its net profits for social development. Starting from 2019, the Singapore government would impose a green tax of SG$5 per tonne of greenhouse gas emissions by the corporates. Starting from the financial year ending December 31, 2017 onwards, the Singapore Exchange (SGX) has made it mandatory for all listed companies to report their environment, social and governance practices. Ioannou and Serafeim (2017) found supporting evidence that the increased transparency in sustainability reporting is effective at improving corporate value using data from China, Denmark, Malaysia and South Africa.

Despite the enthusiasm from managers, investors and regulators, companies still need to understand the specific costs and benefits of engaging in various CSR activities. Jensen (2001) suggested that the main challenge for firms to take on a stakeholder's approach is to produce a single-valued score to capture superior performance if the firm deviates from the shareholder's value maximization mentality. Campbell (2007) also emphasized that institutional conditions such as public and private regulations, independent monitors for corporate behaviors, institutional norms and firm characteristics play an important role in shaping firms' socially responsible decisions.

In order to understand what the right approach is, we will conduct a reduced form analysis in this study. Specifically, we explore whether a firm's valuation can be positively or negatively affected if its CSR activities deviate from its historical norm around the world. This deviation from the norm measure is constructed based on country, industry and time series averages for each firm. Given that most of the firms around the world have already engaged in some level of CSR activities, we study the consequence on a firm's valuation if it chooses to systematically deviate in either the positive or negative direction, being a positive or negative trend.

Literature Review

Growth of research interest in corporate social performance

Figure 1 shows the time trend of the usage of the term "business and society" versus the term "corporate social performance" following the approach by Kemper and Martin (2010). We used the scholar.google.com search engine to find the number of articles after keying in the two terms respectively. It is obvious that both were on a rising trend (except in the current decade which is incomplete), but exponential growth of the term "corporate social performance" began at the turn of the century and it overtook "business and society" in the current decade, after the global financial crisis.

Benefits and costs of CSR in the U.S.

Historically, the main research focus is about whether a firm can benefit from better CSR performance. More recent empirical evidence seemed to suggest more value creation for individual companies from CSR activities. Ferrell, Liang and Renneboog (2016) found a positive relation existed between CSR and firm value. The economic channel seems to be related to the reduction in agency costs measured in terms of cash abundance, pay-for-performance, control wedge and minority protection as well as CEO turnover. Other benefits of CSR include building social capital and trust with stakeholders. Lins, Servaes, and Tamayo (2017) documented that the firms with higher CSR intensity had 4% to 7% higher return than others during the global financial crisis. These firms also experienced higher profitability, growth, and sales per employee and raised more debt. Such positive impact is more manifested when the overall environment for trust is low such as in crisis times. Edmans (2011) also found that firms with higher employee satisfaction generated an abnormal return of 3.5% from 1984 to 2009. In the traditional measure of CSR activities, employee welfare is one of the key components.

What are the costs of not doing enough CSR? Cao, Liang, and Zhan (2019) found that the passage of a close-call CSR proposal and its implementation are followed by the adoption of similar CSR practices by peer firms. Negative stock returns would incur for peers who had more difficulty to catch up. Lam, Zhang and Jacob (2015) also found that the U.S. firms which had worse CSR performance had more negative abnormal returns compared to other firms. One comforting result, however, is that these firms could still redeem themselves by engaging in more positive CSR activities as the market is very forgiving. Another recent study by Sulaeman and Varma (2018) also found that geographical norms seem to shape institutional investors' preference for firms with negative environmental practices: firms located in "green" cities receive substantially lower market valuations if they are identified as having environmental concerns.

International evidence

International evidence on the relation between firm value and CSR activities is much more recent as past data limitations have been overcome. Liang and Renneboog (2017) found that a firm's CSR rating and its country's legal origin are strongly correlated: firms from common law countries have lower CSR than companies from civil law countries. Firms in countries with Scandinavian civil law have the highest CSR ratings. Moreover, firms operating under civil law are more responsive to CSR shocks than those operating under common law.

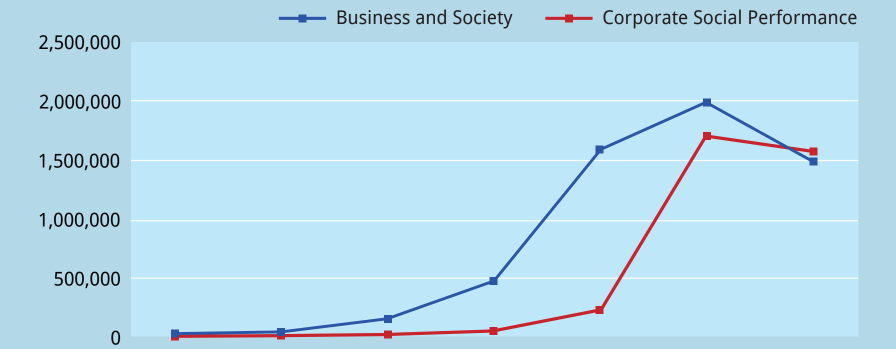
Other stakeholders in a firm can also be affected significantly by its CSR practices. Dai, Liang and Ng (2018) used CSR ratings from 50 countries and found that customers' CSR ratings are associated with suppliers' subsequent CSR performance, but not vice versa and that their locations matter. The economic channel is through the bargaining power of firms and their network connectedness. Moreover, they also found that increasing collaborative CSR efforts between customers and suppliers help improve their operational efficiency and firm valuations.

Given that firms varied significantly from country to country, Lam, Zhang and Chieh (2018) further documented that the positive CSR-firm value relationship is enhanced by the quality of a country's economic, financial and government institutions.

There are plenty of country-specific studies that found a positive relationship between firm performance and CSR activities in Asian emerging markets including Thailand and Indonesia (Cheung et al, 2010). As for China, the main focus is still on the regulations and monitoring by the state on many firms' CSR decisions (Marquis and Qian, 2014). In more developed Asian economies such as Hong Kong and Singapore, studies showed that local market players largely ignored the sustainability reporting enforced by regulators as they perceived it mainly as tick box compliance (Liu, Demeritt and Tang, 2019). India, on the other hand, after the enforcement of the corporate donations since 2014, CSR activities failed in translation of national CSR policy goals to firm-level strategies and lacked clear assessment of stakeholders needs and clear communication (Subramaniam, Kansal and Babu, 2017).

Taken altogether, the literature generally found that the CSR-firm value relation varied significantly across firms, industries, countries, and geographical regions. Hence, in this study we would explore the cross-country variation by taking into account the different levels of CSR activities in each firm by benchmarking them with the industry average within their home countries.

Figure 1: Time Trend of Research Articles



Source: Compiled by the authors by using the search engine under scholar.google.com.

Data and Key Variables

In this study, we employ the MSCI ESG data from 1,444 unique companies from 35 countries during the period 2009 to 2014. Firm characteristics variables are extracted from FactSet Research Systems (hereafter, FactSet) and merged with MSCI's ESG database. To be included in our dataset, we require firms to have non-missing ESG scores.

We construct the key independent variables by computing the standard deviation of the positive (*PSTD*) and negative difference (*NSTD*) of each company's ESG score scaled by the industry average in its country over the previous 36 months. Specifically, we follow Segal, Shaliastovich and Yaron (2015) to define *PSTD* and *NSTD* as follows:

$$PSTD_{i,j,t\text{-}1} = \sqrt{\frac{\sum_{n=1}^{36} \| \left((ESG^*_{i,j,t\text{-}n} - \overline{ESG^*_{i,j}}) \geq 0 \right) (ESG^*_{i,j,t\text{-}n} - \overline{ESG^*_{i,j}})^2}{N \| \left((ESG^*_{i,j,t\text{-}n} - \overline{ESG^*_{i,j}}) \geq 0 \right)}} \quad \cdots (1a)$$

$$NSTD_{i,j,t\text{-}1} = \sqrt{\frac{\sum_{n=1}^{36} \| \left((ESG^*_{i,j,t\text{-}n} - \overline{ESG^*_{i,j}}) < 0 \right) (ESG^*_{i,j,t\text{-}n} - \overline{ESG^*_{i,j}})^2}{N \| \left((ESG^*_{i,j,t\text{-}n} - \overline{ESG^*_{i,j}}) < 0 \right)}} \quad \cdots (1b)$$

where ‖ (.) is the indicator function, $ESG^*_{i,j,t}$ is firm *i* in country *j*'s ESG score that is scaled by its industry average ESG score, in month *t*, and $\overline{ESG^*_{i,j}}$ is the average of $ESG^*_{i,j,t}$ over the 36-month period from *t*-36 to *t*-1. We require N ≥ 6 during the 36-month period. Figures 2A to 2D show the average of our key constructs *PSTD* and *NSTD* for the overall ESG score, Environment score (E), Social score (S), and Governance score (G) for different subsamples of firms.

The economic rationale for these two variables is to capture the positive or negative deviation of a firm's CSR performance from its historical norm. The norm is adjusted for country and industry trends given the scaling factor as the denominator. Given that the decomposition takes into account the various intuitional norms at country-, industry- and firm-specific levels, the deviation would then capture the significant deviation in either direction that makes our research approach clean and sharp.

Figure 2A shows that both the positive and negative deviations in the overall scores are greater for Asian firms compared to the average of firms in all countries. However, the deviations of firms domiciled in developed countries in general are smaller than those in developing countries, while the opposite is true for firms in developed countries in Asia compared to those in Asian developing countries. We also reported the numbers for firms located in China, India, Japan, Korea and the U.S.. Among the five countries, the biggest positive and negative deviations come from the U.S. firms followed by Chinese firms. The deviations of firms located in the other three countries are largely the same.

The deviations for the three subcomponents of the ESG scores are reported in Figure 2B (Environment), 2C (Social) and 2D (Governance) respectively. There are significant variations in *PSTD* and *NSTD* across regions and individual countries. For the Environment score, the U.S. firms displayed

Figure 2A: Positive and Negative STD of Overall Score

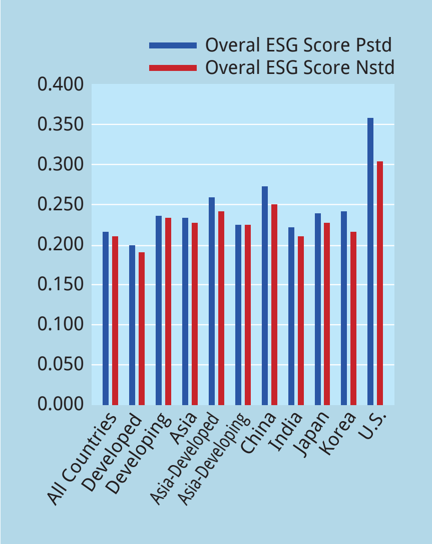


Figure 2B: Positive and Negative STD of Environment Score

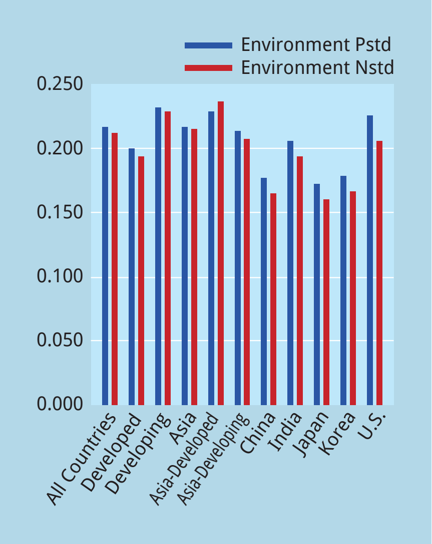


Figure 2C: Positive and Negative STD of Social Score

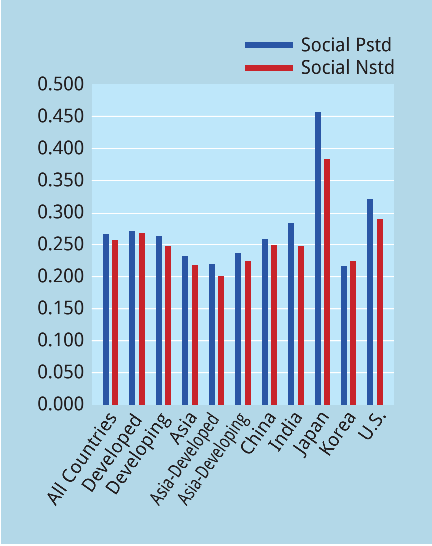
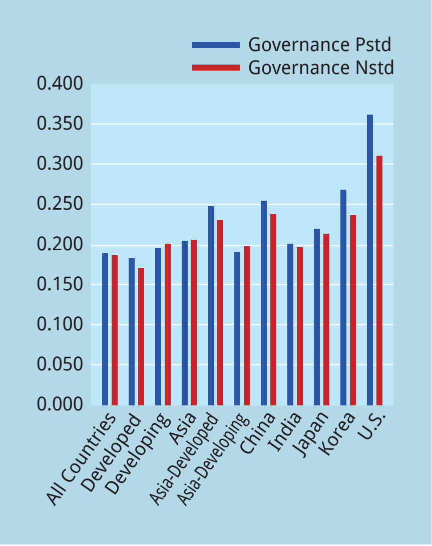


Figure 2D: Positive and Negative STD of Governance Score



Source: Authors' calculation following equation 1a and 1b based on the raw ESG scores from MSCI.

the largest deviations followed by Indian firms (Figure 2B). For the Social score, Japanese firms displayed the largest deviations followed by the U.S. firms (Figure 2C). As for the Governance score, the U.S. firms have the largest deviations followed by Korean and Chinese firms (Figure 2D). These significant variations justify our research approach to examine the impact of the deviation on firm valuation across geographical locations. The *PSTD* and *NSTD* variables are not highly correlated, with correlation coefficients of 0.172, 0.229, 0.189 and 0.185 for the four sets of ESG scores (Overall, Environment, Social and Governance scores) respectively.

The key dependent variable is Tobin's Q, which is defined as the market value of equity minus the book value of equity plus the book value of total assets divided by total assets. To mitigate the effect of outliers, we winsorize Tobin's Q at the 2.5 and 97.5 percentiles. Empirically, we estimate the following equation

$$Tobin's\ Q_{i,j,t} = \beta_0 + \beta_1\, PSTD_{i,j,t\text{-}1} + \beta_2\, NSTD_{i,j,t\text{-}1} + control\ variables_{i,j,t\text{-}1} + \varepsilon_{i,t} \qquad (2)$$

for firm *i* in country *j* in month *t*, and where the control variables include return on assets, leverage to equity ratio, capital expenditure to assets ratio, cash to assets ratio, year on year sales growth, advertising expenditure to total assets ratio, log of total assets, and a dummy variable if the firm paid out dividends. For all the regressions, we control for year-fixed effects, country-fixed effects and industry-fixed effects.

In the null hypothesis, we would expect the coefficient $\beta_1>0$ and the coefficient $\beta_2<0$, suggesting that the firm value will increase when the firm has deviated from its historical norm in the positive direction, and vice versa if the firm deviated from the historical norm in the negative direction.

Empirical Findings

In this section, we report two sets of results after performing the regression analysis specified in equation (2). Table 1 presents the results for different geographical locations and Table 2 shows the results for five individual countries. The green cells represent statistically significant results at the 10% significance level consistent with value-creation/destroying interpretations. That is, positive deviation in CSR performance from the past norm increases firm value and negative deviation from the norm destroys value. The grey cells represent statistically significant results at the 10% significance level with the opposite interpretation: positive deviation destroys firm value and negative deviation enhances firm value.

Geographic differences

We find that overall, *PSTD* increases firm valuations while *NSTD* reduces firm valuations. The economic magnitude for *PSTD* (which is computed by multiplying the coefficient with the standard deviation of *PSTD*) on firm value is about 0.25% of the average level of Tobin's Q if *PSTD* increases by one standard deviation, shown as Model 1 in the table. The magnitude is slightly higher for developed countries at 0.27% as shown in Model 2. For Asian firms, we find that both *PSTD* and *NSTD* have significant impacts on firm valuation at the 10% significance level. The economic magnitude is the greatest for Asian developed countries at 0.74% and -0.57% respectively when *PSTD* and *NSTD* increase by one standard deviation as shown in Model 5.

Results for the Environment sub-component of the ESG score in Models 9, 10 and 12 show that positive deviations (*PSTD*) create value and negative deviations (*NSTD*) destroy value for firms in developing countries as a whole and in all Asian, and Asian developing countries.

In terms of the Social score, we also consistently find that *PSTD* and *NSTD* are statistically and economically significantly related to firm valuations. The results are largely similar across all categories of firms including those in developing and developed countries as shown in Models 13 to 16 in Table 1.

Table 1: Results for Firm Value and Deviations in CSR Scores

Dependent Variable: Tobin's Q						
	All Countries	Developed	Developing	All Asia	Asia-Developed	Asia-Developing
Overall ESG Score						
	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
PSTD	0.0699 (3.59)	0.0935 (4.26)	-0.0242 (-0.61)	0.0478 (1.69)	0.1165 (4.01)	0.0271 (0.55)
NSTD	-0.0276 (-1.29)	-0.0374 (-1.53)	-0.0160 (-0.36)	-0.0788 (-2.64)	-0.1192 (-3.73)	-0.1118 (-2.27)
N	48,498	36,795	11,703	20,346	11,793	8,553
Adj. R^2	0.63	0.62	0.74	0.67	0.58	0.74
Environment Score						
	Model 7	Model 8	Model 9	Model 10	Model 11	Model 12
PSTD	-0.0179 (-1.07)	-0.0973 (-5.12)	0.1943 (5.74)	0.1567 (6.80)	0.0253 (1.32)	0.2317 (5.24)
NSTD	0.0121 (0.64)	0.0290 (1.31)	-0.1641 (-4.81)	-0.0740 (-3.00)	-0.0500 (-2.34)	-0.2239 (-4.89)
N	47,558	36,037	11,521	20,045	11,580	8,465
Adj. R^2	0.64	0.63	0.74	0.69	0.67	0.76
Social Score						
	Model 13	Model 14	Model 15	Model 16	Model 17	Model 18
PSTD	0.0806 (5.54)	0.0703 (4.24)	0.0735 (2.59)	0.0835 (4.28)	-0.0285 (-1.33)	0.0367 (1.11)
NSTD	-0.0531 (-3.94)	-0.0679 (-4.31)	-0.0584 (-2.44)	-0.0511 (-2.84)	-0.1025 (-4.79)	-0.0306 (-1.10)
N	46,056	34,798	11,258	19,818	11,483	8335
Adj. R^2	0.63	0.62	0.74	0.66	0.59	0.75
Governance Score						
	Model 19	Model 20	Model 21	Model 22	Model 23	Model 24
PSTD	-0.0189 (-0.96)	-0.0068 (-0.31)	0.0384 (0.88)	-0.0248 (-0.99)	-0.0183 (-0.79)	0.0158 (0.31)
NSTD	0.1429 (6.41)	0.1317 (5.31)	0.2687 (0.64)	0.0701 (2.47)	0.0648 (2.43)	0.2043 (3.56)
N	48,419	36,656	11,763	20,276	11,724	8,552
Adj. R^2	0.63	0.62	0.74	0.67	0.58	0.76

Note: t-statistics are shown in parentheses.
Source: Authors' calculation.

In the estimates for the Governance score with the exception of Model 21 (All Developing Countries), negative deviations (*NSTD*) from the past increase firm valuation at the 10% significance level for firms in general and in Asia. These results indicated that most firms around the world have achieved decent compliance in corporate governance.

In sum, our results reveal that it is important to understand what aspects of improvement in CSR activities compared to the historical norms would increase firm valuation, and what aspects of deterioration will lead to most value losses, for firms in Asia or in the world in general and for firms in both developed and developing countries.

Individual countries

We also analyzed the relationship between firm value and deviations in CSR scores for firms located in the five individual countries mentioned before, and the results are shown in Table 2.

When we examined the Overall ESG score, we find that valuations of Indian and the U.S. firms were higher the more positively they deviated from their past performance (Models 2 and 5) while Chinese firms experienced lower valuations the more negatively they deviated from the past (Model 1).

In terms of the Environment score, valuations of Korean firms were higher when they deviated positively from the past (Model 9) and valuations of Chinese firms were lower when they deviated negatively (Model 6). On the Social score, valuations of Chinese and Korean firms were higher if they deviated positively (Models 11 and 14). Also, on the Social score, negative deviations from the past were associated with lower firm valuations in four out of the five countries except China (Models 11 to 15). Lastly, in terms of the Governance score, the only country for which positive deviations from the past resulted in higher firm valuations was India (Model 17).

In sum, our results showed that performing better than the past norm can enhance firm value and performing worse than the past norm can destroy firm value. However, geographical location and country-specific factors also matter significantly for the relationship between deviations from the norm and firm valuation. Hence, managers should take into consideration these factors when they choose to improve their CSR activities or when they fall below their past norm.

Table 2: Results for Firm Value and Deviations in CSR Scores in Selected Countries

Dependent Variable: Tobin's Q					
Countries	China	India	Japan	Korea	U.S.
Overall ESG score					
	Model 1	Model 2	Model 3	Model 4	Model 5
PSTD	0.0207 (0.90)	0.4993 (2.48)	0.0094 (0.30)	-0.0758 (-0.99)	0.0884 (2.75)
NSTD	-0.1248 (-4.57)	0.0475 (0.28)	0.0889 (2.56)	0.2010 (2.51)	-0.0419 (-1.17)
N	1,751	1,389	10,727	1,902	16,608
Adj. R^2	0.66	0.83	0.55	0.80	0.62
Environment Score					
	Model 6	Model 7	Model 8	Model 9	Model 10
PSTD	-0.0762 (-2.92)	0.1331 (0.87)	-0.0363 (-1.84)	0.2414 (3.00)	-0.1947 (-6.18)
NSTD	-0.1673 (-4.91)	-0.1941 (-1.31)	-0.0282 (-1.25)	-0.0462 (-1.25)	0.1209 (3.08)
N	1,754	1,350	10,538	1,845	16,327
Adj. R^2	0.65	0.83	0.64	0.80	0.62
Social Score					
	Model 11	Model 12	Model 13	Model 14	Model 15
PSTD	0.1440 (5.97)	-0.1961 (-1.74)	0.0089 (0.41)	0.1057 (2.82)	0.0195 (0.73)
NSTD	0.0843 (4.36)	-0.3859 (-4.34)	-0.0536 (-2.15)	-0.0664 (-2.43)	-0.1191 (-4.69)
N	1,725	1,350	10,461	1,814	15,648
Adj. R^2	0.67	0.80	0.55	0.81	0.61
Governance Score					
	Model 16	Model 17	Model 18	Model 19	Model 20
PSTD	-0.0896 (-3.78)	0.5931 (3.08)	0.0158 (0.67)	-0.1561 (-2.11)	-0.0685 (-2.07)
NSTD	-0.0340 (-0.97)	0.2716 (1.56)	0.0895 (3.30)	0.0186 (0.22)	0.1500 (3.94)
N	1,769	1,410	10,659	1,868	16,632
Adj. R^2	0.66	0.84	0.56	0.81	0.61

Note: t-statistics are shown in parentheses.
Source: Authors' calculation.

Conclusions

In this study, we demonstrate that the deviation from the historical norms in CSR practices affect the firm valuations. However, there are significant differences in responsiveness to these deviations among economic regions and countries. Hence, it is important to understand what would be the right value driver when adopting certain CSR practices rather than blindly generalizing the results across all countries. For Asian countries, putting more effort toward better environmental and social practices would pay off with higher firm valuations. Firms in developed Asian countries should be careful not to fall below their past norms in environmentally and socially responsible activities to avoid value losses.

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Nomura Foundation (the Foundation) is a public interest incorporated foundation formed in 2010 from the combined resources of three existing foundations established by Nomura Group, Japan's largest securities company. The Foundation aims to support a dynamic and sustainable economy and society by promoting the social science disciplines, enhancing international understanding, and fostering young academic and artistic talent. It focuses on four program areas: Social Sciences, Foreign Student Scholarships, Arts and Culture, and the World Economy.

The World Economy program supports research, conferences, and publications related to the macro economy and capital markets.

In the macro economy area, the Foundation has organized conferences together with experts from the Brookings Institution (US), Chatham House (UK), the Development Research Center of the State Council (China), and Bruegel (Belgium) as well as Nomura Securities and Nomura Institute of Capital Markets Research to share research on such topics as monetary and financial institutions, fiscal stability, and demographic change and sustainability.

In the area of capital markets, the Foundation has organized conferences

Panel Discussion at the 2015 Forum

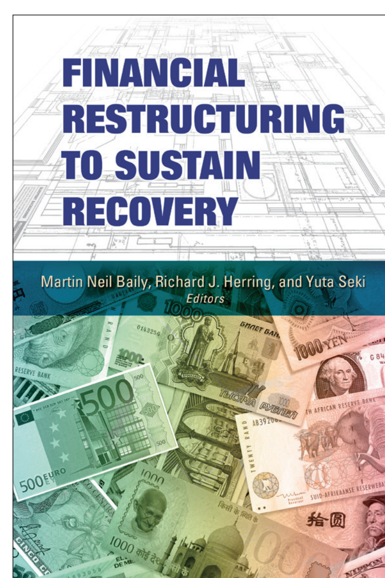
and roundtable discussions in conjunction with the Brookings Institution, the Wharton School, the Development Research Center of the State Council (China), China's Center for International Knowledge on Development and Nomura Institute of Capital Markets Research. It has also provided financial backing for several conference volumes published by the Brookings Institution, *Capital Markets in India* published by Sage, Inc., and the quarterly Japanese-language journal *Chinese Capital Markets Research*.

Research papers and presentations prepared for conferences and the content of print publications are available on the Foundation's website http://nomurafoundation.or.jp/en.

With the expanding importance of Asia in the 21st century global economy, the Foundation has been increasing its support of intellectual interactions among experts at think tanks, universities and government agencies in the region. As part of this effort and recognizing the importance of capital market development in promoting economic growth and prosperity in Asian countries, the Foundation started publishing *Nomura Journal of Asian Capital Markets* in 2016.

Cover of *Chinese Capital Markets Research*


Lord Mervyn King at the 2015 Forum



Cover of *Financial Restructuring to Sustain Recovery*

Introducing Nomura Institute of Capital Markets Research

Established in April 2004 as a subsidiary of Nomura Holdings, Nomura Institute of Capital Markets Research (NICMR) builds on a tradition begun in 1965 of studying financial and capital markets as well as financial systems, structures, and trends. NICMR offers original research and policy proposals by specialists based upon its knowledge of actual business practices.

NICMR publishes some of its research output in Japanese in the magazine *Nomura Capital Markets Quarterly*, and it posts some items in Japanese, English and Chinese on its website.

In Japan, structural changes in the economy and society have rapidly progressed. Population aging is in progress and is having a major impact on economic and social systems. Japan faces a number of challenges, including the need to reform its social security, tax, and public finance systems. As a front-runner of aging society, Japan has to overcome these challenges to develop further.

As a mature economy, one of Japan's most valuable resources is its JPY 1,800 trillion household financial assets. Whether this is used effectively will be critical to the country's future. We recognise that Japan must establish a market mechanism-driven money-flow in order for its economy to further progress. Our core mission is to contribute to financial system and securities market reforms in order to help establish such a market-structured financial system.

NICMR research encompasses not only Japanese issues, but also covers timely issues concerning international capital markets. In addition to research offices in New York, London and Beijing, NICMR established a research office in Singapore in 2015 to strengthen its Asian research platform.

The continuous growth of China and the other Asian countries is generating huge funding needs for their infrastructure and it means that this region requires not only indirect financing systems but also robust capital markets. There is an urgent need to promote development of Asian capital markets, which are a key for the future of Asian financial systems and their economies.

Since the global financial crisis, people have become increasingly aware of problems that spread beyond national boundaries. As financial regulators around the world cooperate more closely, there is a greater need for recognition of regional differences. The role of Asia from the perspective of rulemaking and global standards is also increasingly important.

Our mission includes generating financial and capital market-related policy recommendations for Asian countries based upon fundamental analysis and comparative studies of experiences in Japan and other developed countries. We believe that there are lessons to be learned from Japan's experience when it comes to issues such as the need to increase the availability of direct finance and the need to increase the availability of investment services to cater to the growing number of middle-income households.

We will continue to review such developments and strive to be even more timely in our studies and proposals. As a member of the Nomura Group, a global financial group based in Asia, we hope to continue to contribute to the development of financial markets in both Japan and the rest of Asia.

Cover of *Nomura Capital Markets Quarterly*

BACK ISSUES

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