The MAS is currently consulting banks, asset managers and insurers on proposed environmental risk management guidelines ("Guidelines") to enhance their resilience to and management of environmental risk.

Environmental risk considerations are a hot topic for the MAS. Last year, the regulator announced it is “working on a comprehensive, long-term strategy to make sustainable finance a defining feature of Singapore’s role as an international financial centre”. The MAS also rolled out its Green Finance Action Plan, aimed at facilitating sustainable finance: the practice of integrating environmental, social and governance criteria into financial services, to bring about sustainable development outcomes.

This push for sustainable finance is backed by a growing recognition of the impact of environmental risk on financial institutions, with the risk potentially transmitting through the following channels:

**Physical risk**
This refers to risk arising from the impact of weather events and widespread environmental changes. This may impair the collateral value of bank loans and revenue generating assets of investee companies, or lead to significant insurance claims.

**Transition risk**
This refers to the risk arising from the transition to an environmentally sustainable economy, by way of changes in policy, technology, or consumer and investor sentiment. This may impair loans and investments in carbon-intensive sectors.

The MAS has emphasised the importance of resilience against such risk, and has set out in its proposed Guidelines sound practices on the governance, risk management and disclosure of environmental risk.
Issues consulted on
We summarise below salient points in each of the Guidelines:

**Scope**

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<th>Banks</th>
<th>Asset managers</th>
<th>Insurers</th>
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<td>The Guidelines will apply to banks, merchant banks and finance companies (together, “banks”). The Guidelines should be applied to banks’ extension of credit to corporate customers and underwriting for capital market transactions, and to other activities that expose it to material environmental risk (e.g. investment activities).</td>
<td>The Guidelines will apply to licensed fund management companies, real estate investment trust managers, and registered fund management companies. The Guidelines should be applied where asset managers have discretionary authority over investment of funds or mandates (even while delegated).</td>
<td>The Guidelines will apply to insurers, including insurers carrying on business in Singapore under a foreign insurer scheme. The Guidelines should be applied to insurers’ underwriting and investment activities, and to other activities that expose it to material environmental risk.</td>
</tr>
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**Governance and strategy**

Board and senior management should maintain effective oversight of their institution’s environmental risk management. They should take environmental considerations into account with regard to their institution’s risk appetite, overall strategy, and business plans. This will include:

- developing and implementing environmental risk management frameworks and policies to identify, monitor, assess and manage the impact of environmental risk on their business;
- regularly reviewing their effectiveness; and
- allocating adequate resources to manage environmental risk.

**Key sector-specific guidance**

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<th>Banks</th>
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<td>Identify and assess material environmental risk on a customer and portfolio level, such as developing sector-specific policies which clearly articulate expectations towards customers. For transactions with higher environmental risk, banks should carry out enhanced due diligence (e.g. site visits to the customer, review by external personnel with environmental risk expertise).</td>
<td>Embed environmental risk considerations in research and portfolio construction. Asset managers should evaluate the impact of material environmental risk on an investment’s return, and employ appropriate tools and metrics to identify sectors with higher environmental risk.</td>
<td>Incorporate environmental risk considerations in their underwriting processes. For customers with higher environmental risk, insurers should consider imposing underwriting conditions (e.g. developing a sustainable transition strategy, adhering to certification standards); pricing in the additional risk; or applying limits on underwriting exposure.</td>
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Implementation approach
The MAS has proposed a transition period of 12 months after the Guidelines are issued, for relevant financial institutions to develop frameworks and processes to comply. They have also highlighted that the Guidelines should be implemented in a way that is commensurate with the size and nature of an institution’s activities, as well as its risk profile.

### Key sector-specific guidance continued

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<th>Banks</th>
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<td><strong>Manage and monitor environmental risk exposures.</strong> Banks should engage with customers to support their transition to sustainable business practices (e.g. by way of financing conditions or covenants in loan agreements); developing quantitative and qualitative tools to measure exposure to risk; and introducing mitigating measures (e.g. scaling back portfolio concentrations in sectors with higher environmental risk).</td>
<td><strong>Manage and monitor environmental risk exposures.</strong> Events such as natural disasters or changes in regulations should prompt a reassessment of the risk or return profile of relevant investments. <strong>Exercise sound stewardship to help shape positive corporate behaviour,</strong> and manage environmental risk associated with investee companies through engagement, proxy voting and sector collaboration.</td>
<td><strong>Manage and monitor environmental risk exposures.</strong> Quantitative and qualitative tools should be developed to monitor underwriting exposures to risk. <strong>Promote responsible business behaviours,</strong> such as supporting investee companies’ efforts in the transition to more sustainable business practices over time and encouraging them to provide environment-related disclosures to foster greater awareness of environmental risk.</td>
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</table>

### Stress testing
The institution should develop capabilities in scenario analysis and stress testing (the latter in respect of banks and insurers) to assess its resilience to financial losses under different environmental risks, where applicable.

### Training
The institution should provide training and equip staff with adequate knowledge to assess, manage and monitor environmental risk effectively.

### Disclosure
The institution should disclose, on an annual basis, its approach to managing environmental risk and any potential impact. Institutions should reference international reporting frameworks, such as the Financial Stability Board’s Task Force on Climate-related Financial Disclosures (“TCFD”) to guide their disclosures. Disclosures can be consolidated at the group or head office level.
Not just a Singapore development

Globally, there is a growing recognition of the impact of climate risk on the financial sector, and the importance of the financial sector's support in a smooth transition to an environmentally sustainable economy:

**Hong Kong SAR**

Last month, the Hong Kong Monetary Authority issued a white paper setting out supervisory expectations on green and sustainable banking in areas such as governance, strategy, risk management and disclosure.

**United Kingdom**

The Prudential Regulation Authority has set out its initial expectations for banks and insurers on managing the financial risks from climate change. This guidance includes encouraging firms, where appropriate, to use scenario analysis to assess the impact of climate change risks on their strategy and risk management.

**European Union**

In the EU, new EU regulations will require firms providing and/or advising on financial products to publish sustainability risk policies among other ESG-related disclosures. Proposed changes to EU law would also require investment firms to take into account ESG considerations when complying with MiFID II risk management rules. Similar changes would require insurers to assess sustainability risks as part of their risk management function. Most recently, the President of the European Central Bank has announced her intention to use the ECB’s asset purchase scheme to pursue green objectives.

Going forward, financial institutions should be prepared for many of their stakeholders – regulators, investors, business partners, consumers – to expect more information on their environmental risk management practices. With COVID-19 accentuating global thought leadership around climate change and sustainability, attitudes in Singapore are likely to move in tandem. This shift in expectation will be fairly dramatic, requiring a deep re-think of “business as usual”, a change in strategy and a departure from more ‘traditional’ areas of business focus, such as financial and resourcing considerations.

Financial institutions in Singapore would do well to start preparing for such a shift now.

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