

PROVISION



Provision policies help to ensure financial resources for green projects or related climate action activities are provided to qualified beneficiaries, whether through lending policies, refinancing or other financing schemes.

PERU

Rescheduling of retail loan payments in the event of a disaster

MOROCCO

Support to the creation of Innov Investment Fund to support start-ups including renewable energy and cleantech

EGYPT

Required banks to allocate 20% of their portfolio to finance MSMEs including renewable energy and climate-resilient irrigation

ARMENIA

Offered longer term financing to financial institutions to on-lend to MSMEs for products such as renewable energy

JORDAN

Medium-Term Advances to Licensed Banks Program provides subsidized loans for critical development sectors including renewable energy and agriculture

NEPAL

Directed all banks to dedicate 10% of their portfolio to green projects
Refinancing facilities for banks to offer subsidized loans for green technologies and to rebuild from floods and fires



For policymakers, the provision of financial services for climate action has several attractive features: i) it demonstrates the commitment of authorities to climate action; ii) it appears easy to implement even if a clear definition of purpose is needed; iii) it promises quick effect; and iv) it is simple to verify implementation.

LENDING QUOTAS

Arguably, the most direct intervention is mandated lending through quotas. Lending quotas require allocating a specified percentage of a bank's loan portfolio for a particular purpose. The following are some examples of this approach.

- › **Bangladesh Bank** introduced a regulatory target on the annual disbursement of green finance in 2014. Drawing on its experience implementing regulatory targets for SME and agricultural financing, the central bank set a minimum target for direct green finance of five percent of total funded loan disbursements/investments by banks and financial institutions. Other institutions have sought directed lending for similar purposes.
- › **Nepal Rastra Bank** has priority sector lending requirements and has directed all commercial banks to dedicate at least 10 percent of their portfolios to green energy, such as hydropower and other projects.
- › The Reserve Bank of Fiji issued a renewable energy loan ratio in 2012 that required commercial banks to hold two percent of deposits and similar liabilities for renewable energy loans. However, it does not currently sanction banks that fail to comply.
- › The **Central Bank of Egypt (CBE)** has policies in place to support the MSME sector with climate change. From 2016 to 2020, the CBE requires banks to allocate 20 percent of their total credit portfolio to finance MSMEs. This mandatory requirement is balanced by an incentive whereby banks are exempt from the loan reserve requirements against loans or credit facilities to MSMEs, provided that the interest rate on the loans does not exceed five percent. At the time of writing, this rate was approximately 10 percent lower than market rates for similar facilities. Renewable energy and climate-resilient irrigation are sectors covered by the policy.

REFINANCING GREEN LENDING

Refinancing facilities and schemes for green lending primarily offer subsidized credit to commercial banks for loans for a specific purpose or set of products. Credit is extended at preferred terms, but commercial banks make lending decisions themselves and hold all the risk. Several countries have introduced programs that could help individuals and MSMEs finance low-carbon solutions. For instance:

- › **Bangladesh Bank** has used refinancing facilities to promote low-carbon technologies, providing subsidized credit for solar energy, biogas and waste treatment projects. Over the last decade, the resources, green products and scope of the scheme have expanded, with four schemes supporting 50 products in 11 categories.⁶²
- › **Nepal Rastra Bank** offers refinancing facilities for banks to provide subsidized loans (from \$1,700 to \$2,700) for consumers to purchase a range of green technologies, from solar home systems to solar cookers, dryers and water pumps, biogas installations, clean cookstoves and electric rickshaws.
- › Similarly, the **Central Bank of the Argentine Republic** relaxed the conditions for granting loans to agricultural producers who have taken out insurance against climatic events. This incentive reduces the risk of agricultural producers and allows them access to more favorable loans.

REFINANCING RECOVERY AND RECONSTRUCTION

Refinancing facilities and schemes not only encourage green lending, they can also be used to support recovery and reconstruction following extreme climate events.

- › In February 2019, the **Superintendencia de Banca, Seguros y AFP (SBS) Peru** adopted exceptional measures to avoid economic losses experienced as a result of adverse weather conditions associated with El Niño. The prudential measures require financial institutions to reschedule retail loan repayments in the event of specific natural disasters.^{63,64} The measures, which were previously activated in 2017 when similar adverse conditions were experienced, have strict conditions.

⁶² Khan et al., 2017

⁶³ The measures target MSMEs debtors in specific areas declared by the government as in "a state of emergency" due to extreme weather events. The measures are, uniquely, accompanied by a warning about financial institutions' clients and portfolios that may be more sensitive to the impacts of climate change in the future.

⁶⁴ SBS, 2019. and SBS, 2017.

› Environment and climate-related shocks or slow-onset disaster can have adverse effects on entire sectors. In the **Bangko Sentral ng Pilipinas’ Agricultural Value Chain Financing Framework**,⁶⁵ BSP-supervised financial institutions can put disaster contingency mechanisms in place to mitigate the impact of such risks, and provide timely relief to facilitate the recovery of climate-vulnerable MSMEs in the agricultural and fisheries sectors. While the Framework does not specify elements of the contingency mechanisms, BSP-supervised financial institutions have the flexibility to design and implement disaster contingency mechanisms based on their assessment of the inherent risks in these sectors.

The BSP has also adopted a policy that provides temporary regulatory relief measures to banks affected by natural disasters. This was institutionalized with the issuance of Circular No. 1017 dated 10 October 2018.⁶⁶ The regulatory relief aims to assist banks located in areas affected by natural disasters in their recovery and allow them to resume normal operations. The relief includes extending the booking of losses that are a result of loan write-offs on affected loans, write-downs of banks’ premises and acquired assets, waiving annual supervisory fees, flexibility in the relocation of branches and relaxing reporting requirements.

› Following natural disasters like the tsunami of 2004 or droughts and floods, the **Central Bank of Sri Lanka** has put moratoriums on loan repayments for affected borrowers. Banks are also required to provide or facilitate emergency credit after a climate-related disaster, including reconstruction mortgages for



Fishing village residents work to clean their town of mud after flooding brought on by El Niño rains, Cabo Blanco, Peru. February 2017. (Photo by CLJ Giordano/Shutterstock)

individuals, reconstruction mortgages for MSMEs and credit for MSMEs to re-establish businesses operations.⁶⁷ The Central Bank of Sri Lanka introduced a refinance loan scheme in 2017 for Resumption of Economic Activities affected by Disasters (READ), to mitigate the impact of natural disasters. The objective of this loan scheme is to provide concessionary financial facilities with a special focus on small-scale business and self-employed businesses to resume any economic activity affected by natural disasters. The government will provide the funding for the project and identify the disasters and areas to be covered.

INNOVATION INVESTMENT FUNDS

Investment funds help to spark innovation and provide resources for start-ups in specific sectors.

› In 2018, **Morocco** created the “Innov Invest” fund to support startups in fields ranging from fintech to renewable energy, including “cleantech”.⁶⁸ With \$50 million in loans and technical guidance from The World Bank, the fund will support 300 startups over five years. Forward-looking companies can acquire grants or loans on trust, which will help them overcome some of the challenges typically encountered in the early stages of development and consolidation. The fund is overseen by six participating institutions and consists of four seed capital investment funds.

OTHER FINANCING SCHEMES FOR GREEN LENDING

Other financing mechanisms were also provided by financial regulators to support green lending activities. For example:

› The **Central Bank of Jordan’s Medium-Term Advances to Licensed Banks Program** provides subsidized loans for nine sectors deemed critical to development, including renewable energy and agriculture.⁶⁹

› The **Central Bank of Seychelles**, with the Ministry of Finance, provides lower interest loans to MSMEs and to households through the Seychelles Energy Efficiency and Renewable Energy Program (SEEREP) SME loan scheme. Businesses with a turnover of less

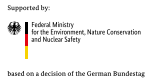
⁶⁵ Bangko Sentral ng Pilipinas, 2016

⁶⁶ Bangko Sentral ng Pilipinas, 2018

⁶⁷ The terms of the emergency credit depend on the type of relief package. In the past, there have been relief packages that include a capital moratorium, capital and interest moratorium, rescheduling of loans and write-offs of interest or loans with the government paying the written-off amount to banks through a repayment scheme. Relief can also be based on concessionary interest rates and concessionary tenors ranging from three months to one year.

⁶⁸ CCG

⁶⁹ Central Bank of Jordan, 2016



than SCR 5 million (\$350,000)⁷⁰ are eligible for the scheme, which includes renewable energy systems, energy-efficient appliances and energy-saving devices (e.g. solar water heaters).⁷¹

- › The **State Bank of Pakistan's (SBP)** offered a financing scheme for Renewable Energy Projects from 2017 to mid-2019. Under the scheme, businesses could receive loans for solar and wind projects at a maximum rate of six percent. The refinancing rate from the SBP was two percent and there was no preferential rate for MSMEs. Compared to the usual rates, which range from 12 percent to 20 percent, the scheme offered good opportunities for MSMEs.
- › In Armenia, the German-Armenia Fund (GAF) founded by the **Central Bank of Armenia**⁷² provides longer term financing in local currency to financial institutions to on-lend to MSMEs for products such as renewable energy.
- › The **Ministry of Finance of Eswatini** has prioritized financial services for climate-smart technologies to build resilience into agricultural supply chains. The Ministry plans to mobilize climate finance for smallholder farmers and rural MSMEs across the country, while also training smallholder farmers in climate information services.

OTHER FINANCING SCHEMES FOR DISASTER REHABILITATION AND RECOVERY

Various financing schemes have been employed by financial regulators to support disaster rehabilitation and recovery. For example:

- › **Nepal Rastra Bank** offers refinancing facilities for subsidized loans of around \$9,000 to rebuild from floods and fires, modelled on a program that supported post-earthquake recovery and reconstruction.
- › **Vanuatu's Natural Disaster Reconstruction Credit Facility** was designed by the Reserve Bank of Vanuatu to assist businesses affected by Tropical Cyclone Pam through concessional lending to commercial banks. Under the facility, commercial banks could access funds at interest rates of one percent that were capped at a maximum of five percent for on-lending to businesses. The fund was initially created with \$4.5 million and offered individual loans of up to \$270,000 that could be rolled over for five years.

The fund was to remain open for six months after Cyclone Pam with an understanding that it could be reopened following other natural disasters.

LOWERING OF BASE INTEREST RATES

Temporary changes to base interest rates can encourage banks to lend in the aftermath of climate-related events.

- › When Cyclone Pam hit Vanuatu in 2015, the **Reserve Bank of Vanuatu (RBV)** lowered the reserve requirement for commercial banks by two percentage points (from seven percent to five percent) to incentivize banks to lend to affected low-income people. The RBV also reduced its base interest rate by 0.5 basis points and tied this reduction to the RBV Notes policy rate. For 91 days, it issued securities notes based on this lower policy rate.

Financial regulators have been creating an enabling environment to mainstream inclusive green finance in the financial system. In some countries, this was the result of past disaster experiences, which necessitated efforts to increase climate and disaster resilience, for instance, by investing in financial resource facilities to support quick recovery and resumption of economic activities. Some regulators have taken a proactive stance to climate action and provided a conducive regulatory environment that encourages direct financing for low-carbon activities or resilience building.

CHALLENGES OF PROVISION POLICIES

While provision policies signal a commitment to climate action, they can be comparatively challenging to monitor. For example, how should the beneficiaries be defined? What constitutes renewable or green products? How does one distinguish between adaptation to climate change and general economic development? How can greenwashing be avoided? Another challenge is finding the resources to finance the provision policies.

There are other questions as well: Should promotions and bonuses for lenders' staff be tied to good performance on green lending programs? How can the system avoid being gamed, distorted or misused?

⁷⁰ USD 1: SCR 34.2, as of 29 December 2019 (www.xe.com).

⁷¹ Under SEEREP, beneficiary contributions were capped at 2.5 percent of the loan amount and the usual loan processing fees were waived under the scheme. Beneficiaries are also allowed a grace period of six months with a flexible repayment period. The SME loan scheme consists of a two-tier interest rate structure where the government provides an interest rate subsidy and the client is charged five percent interest on the first SCR 1 million (\$29,240), seven percent on the next SCR 2 million (\$50,000) and then negotiated for higher amounts.

⁷² GAF's loan programs are funded by the Government of the Republic of Armenia, KfW Bankengruppe, The World Bank, Asian Development Bank and the European Investment Bank.