Our Ref.: B1/15C
B9/81C

8 December 2021

The Chief Executive
All Authorized Institutions

Dear Sir / Madam,

Sound practices supporting the transition to carbon neutrality

I am writing to share with the industry some sound practices adopted by banks to support the transition to carbon neutrality.

Climate change is one of the greatest challenges facing the world and is now widely recognised as a source of financial risks. The Hong Kong Monetary Authority ("HKMA") has recently consulted the banking industry on a draft Supervisory Policy Manual ("SPM") module which sets out the key elements of effective climate risk management.

The HKMA has held a series of discussions with banks to understand their approach to and readiness for climate risk management. The information obtained through these discussions is intended to inform the HKMA's future supervisory activities relating to climate risk management. In the course of this work, the HKMA observes that some banks have developed comprehensive climate strategies and are implementing them with respect to their Hong Kong operations. Apart from incorporating climate risk considerations into their risk management framework, these banks have devoted resources and taken measures beyond risk management to support the goals of the 2015 Paris Agreement and contribute to achieving global net zero emissions.

The HKMA considers that these sound practices supporting the transition to carbon neutrality would be of reference value to authorized institutions ("AIs") in formulating their own climate strategies. They are grouped into four areas and summarised below:-

(1) Reducing greenhouse gas ("GHG") emissions of own operations

- Leading banks in the space of climate risk management have taken measures to reduce their GHG emissions from their operations through energy saving, water and waste reduction and green office/branch policies. Targets for GHG emissions reduction are set, and quantitative metrics or key performance indicators are used to keep track of reduction progress. To enhance the transparency of their operations and promote accountability, these banks regularly disclose their GHG emissions reduction progress and measures. By proactively reducing the GHG emissions of their own operations, these banks seek to cultivate a green and sustainability-centric core value among their staff.

(2) Reducing financed emissions through portfolio alignment

- Given their intermediary role, banks can reduce financed emissions through channeling more funds to greener and more sustainable sectors (such as renewables and clean technologies) in their lending and investment portfolios. Leading banks have developed policies to limit their exposures to high-emitting sectors. Some of them have launched a wide range of green and sustainable products, such as green loans and bonds as well as green deposits and mortgages. These practices not only help the banks align their portfolio with net zero targets, but also meet the increasing market demand for green products. Science-based tools and methodologies are used to assess the banks' portfolio alignment against pre-set targets and develop transition pathways to achieve the goals of the Paris Agreement.

(3) Assisting clients to transition

- Banks can catalyse economy-wide decarbonisation through assisting their clients to transition to carbon neutrality. Leading banks in the space of climate risk management provide transition financing to assist their clients, particularly those from "brown" sectors, to progressively transform their operations into greener and more sustainable business models. Transition loans with sustainability-linked pricing structures are offered to high-emitting clients to incentivise changes towards carbon neutrality. This is an important supportive approach that would help avoid disruptive financial exclusion of some of the traditional industries, while encouraging operators in these industries to transition to low carbon more quickly. Separately, through partnership with green certification agencies, some of these banks facilitate their clients to get third-party green certification on the greenness of their projects or usage of the proceeds prior to green financing applications. Bespoke advisory services and capacity building are also offered by these banks to increase their clients' awareness of climate change, and to assist them in integrating climate change-related considerations into their business and financing strategies.

(4) Promoting collective efforts to assist the economy to net zero transition

- Leading banks in the space of climate risk management participate in international or industry climate initiatives, such as the Collective Commitment to Climate Action ("CCCA") and the Net Zero Banking Alliance ("NZBA"), promoting collective efforts to tackle climate change-related challenges. Through delivering concrete progress on their commitments to climate change goals under these initiatives, these banks seek to demonstrate their ambition and responsibility to contribute to achieving net zero globally. This could help them address the increasing expectation of the public and manage the associated reputation risks. Domestically, these banks proactively collaborate with their governments and policymakers to provide suggestions and advice to help shape climate-related policies at the jurisdictional level.

Details of the above sound practices are set out in the **Annex**. AIs are strongly encouraged to enhance their own overall green and sustainability programmes to encompass both the management of climate risk and the above supporting measures to contribute to carbon neutrality. They should consider developing metrics to monitor the progress of adopting these sound practices as part of their business strategy. The progress made should be regularly reported to the board to keep it abreast of the institution's efforts towards green and sustainable banking. The HKMA will consider reflecting elements of these sound practices in its greenness assessment framework, with a view to evaluating the overall green and sustainable landscape of the banking sector.

Yours faithfully,

Raymond Chan
Executive Director (Banking Supervision)

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