



Technical Assistance Consultant's Report

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Knowledge and Support Technical Assistance (KSTA)

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GREEN LOAN LIFECYCLE REVIEW & RECOMMENDATIONS

Green Finance in Mongolia Final Report

This consultant's report does not necessarily reflect the views of ADB, or the Government concerned, and ADB and the Government cannot be held liable for its contents.

Asian Development Bank

CURRENCY EQUIVALENTS

Currency Unit	–	togrog (MNT)
MNT1.00	=	\$0.0003482
\$1.00	=	MNT3,482

ABBREVIATIONS

Abbreviation	Meaning
BOM	Bank of Mongolia
CBA	Cost Benefit Analysis
CB	Central Bank
CBFSA	Central Banks Financial Supervisory Authorities
CBI	Climate Bonds Initiatives
COP21	21 st Conference of Parties on Climate
EMDCs	Emerging and Developing Countries
ESG	Environmental Social Governance
EU	European Union
FRC	Financial Regulatory Commission
GHG	Greenhouse Gases
ISSB	International Sustainability Standards Board
IR	Integrated Reporting
MET	Ministry of Environment and Tourism
MOF	Ministry of Finance
MSFA	Mongolian Sustainable Finance Association
NBFI	Non-Banking Financial Institution
NDC	Nationally Determined Contribution
NFRD	Non-Financial Reporting Directive
PPP	Public Private Partnership
SASB	Sustainability Accounting Standards Board
SFDR	Sustainable Finance Disclosure Regulation
TCFD	Task Force on Climate related Financial Disclosures
TDBM	Trade and Development Bank of Mongolia

Abbreviation	Meaning
TEG	Technical Expert Group
TNFD	Task Force on Nature related Financial Disclosures
UNPRI	United Nations Principle for Responsible Investments
BOM	Bank of Mongolia

CONTENTS

1. INTRODUCTION.....	5
2. GREEN LOANS IN MONGOLIA	7
2.1. Context – Market Overview	7
2.2. Institutional Framework	8
3. GREEN LOAN LIFECYCLE IN MONGOLIA.....	10
3.1. Green Loan Issuance – Commercial Banks	10
3.2. Green Loan Issuance – Non Banking Financial Institutions	13
3.3. Green Loan Reporting & Monitoring	15
4. STAKEHOLDER DISCUSSIONS.....	17
4.1. Needs to be addressed	19
5. KSTA RECOMMENDATIONS	21
5.1. Enhancement of Green Taxonomy	22
5.2. ESG-Oriented Approach to Lending Criteria.....	24
5.3. Capacity Building and Knowledge Dissemination Initiatives.....	26
5.4. Non-Financial Disclosures for Borrowers.....	27
5.5. Network for Greening the Financial System (NGFS)	29
5.6. United Nations Principle for Responsible Investments (UNPRI)	30
6. CONCLUDING REMARKS	31

1. INTRODUCTION

ADB Green Finance KSTA

The Asian Development Bank (ADB) approved the Knowledge and Support Technical Assistance (KSTA) for the Green Finance Policy Framework in Mongolia in November 2019. The KSTA aims to support the Government of Mongolia in advancing the green finance policy and regulatory framework and in undertaking capacity development to enhance capability to develop green finance projects and products.

Since 2019, the Mongolian green finance regulatory environment has witnessed some developments. For instance, the Mongolian Government have adopted several legislative changes encouraging introduction or scale-up of green finance products such as green bonds or green insurance (2021). In addition, regulatory and policy documents – most important of which is “National Green Taxonomy of Mongolia” (2019) - have been adopted by various Mongolian authorities. Other recently published documents include “Mongolia Sustainable Finance Roadmap” and “ESG & Sustainability Reporting Guidance for Mongolian Companies” (both adopted in 2022) and “Methodology for Assessing and Managing Risks associated with ESG of a Bank” (adopted in 2023).

Adoption of these legal, regulatory and policy documents has led some of the local stakeholders such as Mongolian Sustainable Finance Association (MSFA) and international partners of the Mongolian Government to step up efforts to achieve objectives and goals set out in these documents. One such objective of the government is to increase the share of green loans in the country to 10% of the total loan portfolio of commercial banks and NBFCs by 2030.

Objective of the Report

This report aims to support the government stakeholders in Mongolia through a comprehensive review of green loan lifecycle in the country, stakeholder discussions to identify key needs across the green loan lifecycle and recommending suitable interventions to address the same as per the international best-practices, so as to promote green loans in the country.

Below mentioned areas are covered as part of this report across various chapters.

Chapter	Description
Green Loans in Mongolia	This chapter provides the sector content and overview of the institutional framework for green loans in Mongolia, including roles of the various agencies across the value-chain.
Green Loan Lifecycle	This chapter provides as-is mapping of green loan lifecycle in Mongolia, across the green loan issuance (including the various green loan products) by commercial banks and NBFIs and green loan reporting & monitoring process.
Stakeholder Discussions	This chapter provides a list of stakeholder discussions done with regards to green loan lifecycle and identified needs & challenges to be addressed to promote green loans in the country.

<i>Chapter</i>	<i>Description</i>
<i>KSTA Recommendations</i>	This chapter provides KSTA recommendations, including proposed steps & interventions by BOM to address the identified needs, as per international best practices.

2. GREEN LOANS IN MONGOLIA

2.1. Context – Market Overview

A majority of large commercial banks in Mongolia are offering green loan products to the market. Among them, the most active banks are Xac bank, Khan Bank, and Trade and Development Bank. Xac bank is one of the leading banks for green loan product development and the first green Climate Fund-accredited entity in Mongolia. The bank started issuing green loans in 2007. Since then, green loan product options have expanded, and product quality has improved. Other Mongolian commercial banks are actively working to developing more green products and looking for new market opportunities. For example, Khan Bank, the largest national commercial bank, issued Mongolia's first green bond to the international market and attracted investment.

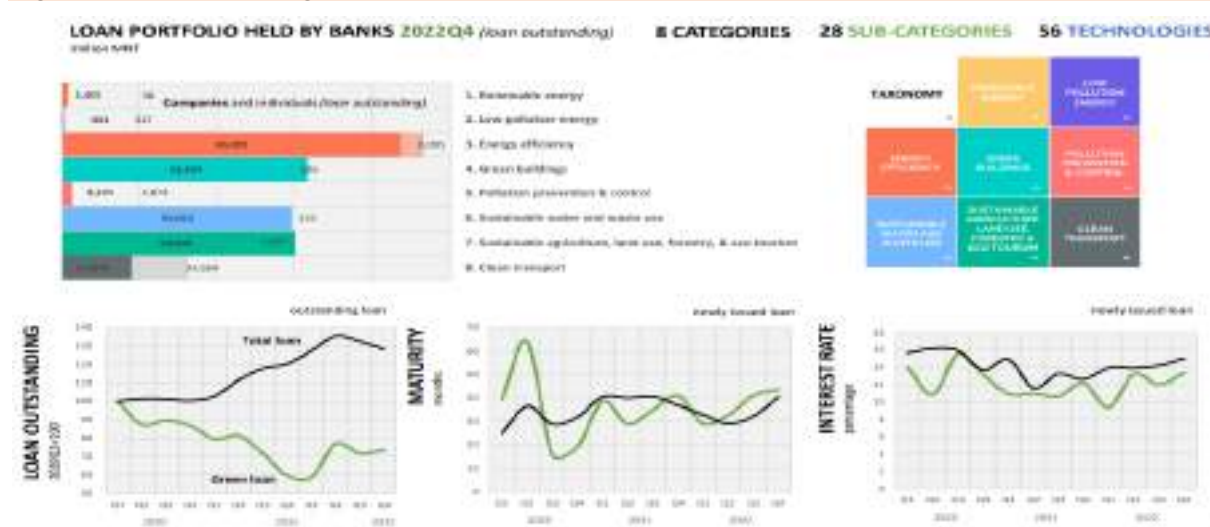
According to the National Sustainable Financial Roadmap approved by the Financial Stability Council in 2020, **the target green loan portfolio (as a percentage of overall loan portfolio) has been set at 10% in banks and 5% in non-bank financial institutions.**

Mongolia has agreed to reduce greenhouse gas emissions by 22.7% by 2030 in accordance with the Paris Agreement. Banks' green loan portfolios have been increased from 1.4 percent to 10 percent in order to keep this pledge.

The Bank of Mongolia (central bank) monitors and collects green loan reports from commercial banks for green loan in Mongolia. As of Q4 2022, the outstanding balance of green loans was MNT 315 billion, accounting for 1.4 percent of commercial banks' loan portfolio. Approximately half of all green loans were funded by international sources, 49% by banks own, and only 1% by the government.

Green loans outperform other types of loans in terms of loan repayment performance. Non-performing loans account for approximately 7% of total loans, while green loans account for approximately 4%.

Figure 1: Green loan categories and performance in commercial banks



Source: Central Bank

2.2. Institutional Framework

This section provides a review of the institutional framework and key agencies involved across the green loan lifecycle in the country.

Table 1: Institutional Framework – Green Loans in Mongolia

Agency	Role in Green Loan Lifecycle
Bank of Mongolia (BOM)	<ul style="list-style-type: none"> In 2019, the Mongolian Green Taxonomy was approved by Financial Stability Council in cooperation with other relevant organizations in order to create a classification of green loans for banks and a database. Green loan reports from commercial banks are collected quarterly by BOM and reported to the public within the framework of green taxonomy. BOM also conducts research and supports policy development and decision-making in the areas of green loan and climate change impacts. Recently, BOM has approved ESG risk assessment and management methodology, due to which the risk assessment has been standardized and benchmarks have been established in the banking sector.
Ministry of Finance (MOF)	<ul style="list-style-type: none"> Strengthening the capacity of financial and budget management, reorganizing and improving the structure and operations Carrying out financial sector regulation and restructuring policies Organizing, coordinating and refining the implementation of foreign-funded projects and measures, providing unified control over implementation, strengthening external and internal debt management.
Financial Regulatory Commission (FRC)	<ul style="list-style-type: none"> Developed guidelines for Developing Environmental and Social Risk Management Procedures for Non-Banking Financial Institutions; Working in the field of organizing training and providing policy support in the field of green finance for NBFIs Green loan reports from non-banking financial institutions are collected quarterly and reported to the public within the framework of green taxonomy since beginning of 2022.
Commercial Banks	<ul style="list-style-type: none"> Recommend and issue green loan products to consumers Commercial banks prepare quarterly green loan reports and submit them to the Central Bank in accordance with the central bank's format. Designing and introducing green loan products to the customers. Attracting green loan resources from international banking and financial institutions and lending them through green loan products
Mongolian Sustainable Finance Association (MSFA)	<ul style="list-style-type: none"> Participation in the development of long-term financial public policy and support for its implementation Trainings and seminars to build members' capacity, as well as internal and external information on sustainable finance To positively inform the public about green finance and green business, as well as to provide correct understanding and knowledge; Green project preparation and capacity building for green project implementation.

Agency	Role in Green Loan Lifecycle
Ministry of Environment and Tourism (MET)	<ul style="list-style-type: none"> • Developing and approving laws, policies and programs related to the environment, green development, and tourism in line with the country's sustainable development, providing policy guidelines, and creating a favorable legal, economic, and social psychological environment that supports them • Developing policies, programs, projects, and providing policy guidelines for introducing clean technologies, scientific achievements, investment, production, and leading management methods to support low-carbon development and green development • Loan subsidies are provided to people living in ger areas with the support of the Ministry of Environment and Tourism and the National Committee for Environmental Pollution Reduction in order to reduce air and environmental pollution

3. GREEN LOAN LIFECYCLE IN MONGOLIA

3.1. Green Loan Issuance – Commercial Banks

In Mongolia, there are currently 12 commercial banks (table 4),¹. Out of them, total 7 banks offer green loan products to consumers. Golomt bank, Khan Bank, Trade and Development Bank (TDBM), State Bank, Xac Bank, Arig bank and Capitron bank offer green loan products to the customer.

Table 2: List of Banks in Mongolia that provide Green Loans

Golomt Bank	Khan Bank	Trade and Development Bank	State Bank
Xac Bank	Capitron Bank	Arig Bank	

Source: Authors

Xac Bank has been providing loans aimed at supporting environmentally friendly and green businesses since 2007, and in 2009, it established the first Eco Bank department within Bank in Asia. Since then, commercial banks now provide a substantially greater variety of green loan products than they did in previous years. The interest rate varies based on the loan's source.

Green loans typically have slightly lower interest rates than other loan types. Loans provided by the Ministry of Environment and Tourism and Air and Environment pollution committee are among the lowest-cost loans because they provide interest subsidies to consumers. However, the amount of funding is small. Banks provide most of the loans from the resources of foreign financial institutions and their own resources. In some cases, some banks also issue loans in a blended manner. As of the third quarter of 2022, banks provided 48.5% of total loans from their own sources, 49.8% from international sources, and 0.7% from government sources

The table below lists the various green loan products available in Mongolia, as offered by different commercial banks.

Table 3: Green loan products in Mongolian commercial banks

Bank name	Loan name	Max loan size /million MNT	Annual interest rate /%/	Max loan term /months/
Xac bank	eco consumer loan for heating	50	16,8	30
Xac bank	Cooking, Heating, Insulation, Product and Service (CHIPS) package project loan	3,2	16,8	30
Xac bank	Loan for energy efficient house	200	12	240

1

<https://mba.mn/%d0%b3%d0%b8%d1%88%d2%af%d2%af%d0%bd%d1%87%d0%bb%d1%8d%d0%bb%d0%b8%d0%b9%d0%bd-%d0%bc%d1%8d%d0%b4%d1%8d%d1%8d%d0%bb%d1%8d%d0%bb/%d0%bc%d0%b0%d0%bd%d0%b0%d0%b9-%d0%b3%d0%b8%d1%88%d2%af%d2%af%d0%b4/>

Bank name	Loan name	Max loan size /million MNT	Annual interest rate /%/	Max loan term /months/
Xac Bank	Loan for air and environment pollution reduction	0.3-200	8	3-60
Xac Bank	Business loan for GHG reduction		15	60
Khan bank	Project loan with MET	40	3	30
Khan bank	Green loan	20	14.4	30
Khan bank	Green loan for family	40	12	30
Khan bank	Green project investment loan	5000	12-13.2	36-60
Khan bank	Green project finance rent	500	12-13.2	36-60
Khan bank	Green loan for current asset	1000	12	36
TDB	Reduce air and soil pollution and promote eco consumption	10	16.8	30
TDB	Eco vehicle loan		15.6	30
TDB	Loan for green house	100	15.6	240
TDB	Green loan for business		15	36

Source: Bank Websites

The tables below provide more details of select green loan products by commercial banks to citizens and businesses in Mongolia.

Table 4: Green loan product for the businesses in Khan Bank

Name of green loan products	Loan max size	Downpayment	Loan duration	Loan interest rate /annual/
Green project investment loan	Up to 5 billion MNT	20%	36 months	12.0%
			37-60 months	13.2%
Green Project Financial leasing	Up to 500 million MNT	15% of rent payment	36 months	12.0%
			37-60 months	13.2%
Working capital loans for green projects	Up to 1 billion MNT	-	36 months	12.0%

Source: Bank Websites

The green lending process differs depending on the loan policy, structure, and size of the bank. In general, major Mongolian banks' green loan processes are as per figure below.

Figure 2: Green loan issuance in Mongolian commercial banks



Source: Stakeholder discussions with Commercial Banks

Some key points with regards to loan issuance process, as per stakeholder discussions, are listed below:

- Credit risk and legal risk assessments for green loans are performed by commercial banks, primarily based on the loan amount. For example, Khan Bank, Mongolia's largest bank, conducts risk and legal assessments if the loan amount exceeds 500 million.
- All mining related projects must undergo aggressive environmental assessments, and typically do not qualify for green loans unless the end proceeds qualify as "green". E.g., purchase of electric vehicles.
- There is no significant difference in terms of collected information from borrowers between green loans and other loans. Only a few sectors require additional information. For example, documents are required to confirm energy efficiency in buildings for construction sector.
- Once the loan application is received from the customer, the relationship manager makes the first loan evaluation. The relationship manager is given permission to begin the loan investigation once the green banking department has determined whether the loan is green or not.
- Foreign lender institutions may provide technical assistance on additional green loan validation in some cases. If it is not provided, the bank bears responsibility and must have suitable documentation to ensure that end proceeds of the loan are "green" as per the Green Taxonomy of Mongolia. For technical assistance, foreign borrowers hire consulting firms that work with local consultants and auditors.

3.2. Green Loan Issuance – Non Banking Financial Institutions

As mentioned earlier, the Financial Regulatory Commission oversees capital market policies as well as non-banking financial institutions. Green loan reports are collected quarterly from non-bank financial institutions beginning in 2022 by FRC. As of the third quarter of 2022, 21 NBFIs had 4,102 borrowers totaling 78.3 billion MNT in outstanding green loans. NBFIs green loan balance accounts for 2.9% of total loans.² Low carbon vehicle loan balance is forming, accounting for 69.8% of the balance of green loans, or 54.7 billion MNT.

There are no outstanding loans in the renewable energy sustainable water and waste sectors. Total loan balances are 94.9% normal, 3.1% attention, and 1.9% non-performing. The Green Building sector has the highest loan balance, or 3.1%, and was classified as poor quality.

Currently, 11 non-bank financial institutions are members of the Sustainable Finance Association (SFA) and provide Green Loan products in the country, as shown in table below.

Table 5: List of Non-Banking financial institutions that are members of the MSFA.

Tavan Bogd Finance NBF	GSB capital NBF	Invescore NBF	Zeel.mn NBF
Bull Capital NBF	Gyals Credit NBF	Numur NBF	Lend.mn NBF
BID NBF	Net Capital NBF	Trans Capital NBF	

Source: MSFA

The SFA member NBFIs are committed to contributing to sustainable development and inclusive green economy by introducing “Sustainable Finance” principles in their business and financial operations. Among these institutions, there is currently one of leading NBF “Trans Capital” provides green loans on the market as listed in table below.

Table 6: Trans Capital NBF's green loan products

Green Loan Products >>	Housing Loan	Eco-automobile loan	Eco-appliances loan
Loan amount	More than MNT one million	up to MNT 50,000,000 (new), up to MNT 25,000,000 (used)	MNT 500,000 –MNT 3,000,000
Loan terms /months/	Up to 60	Up to 24 + up to 36 with immovable collateral	Up to 24
Interest Rate /per month/	2.4%-3%	2.70%	2.70%
Collateral	Immovable or movable assets, automobiles		Purchasing appliances, furniture, movable assets
Service fee	0% - 1%	0% - 1%	1%

² http://www.frc.mn/resource/frc/Document/2022/11/10/wlritt73sycy9kyo/negtgel%202022Q_site.pdf

Green Loan Products >>	Housing Loan	Eco-automobile loan	Eco-appliances loan
Insurance	Immovable assets and life insurances /for loans with more than 36-month terms/		
Downpayment		20.00% (new), 40%(used)	20% / 0% down payment for loan less than MNT 2,000,000/

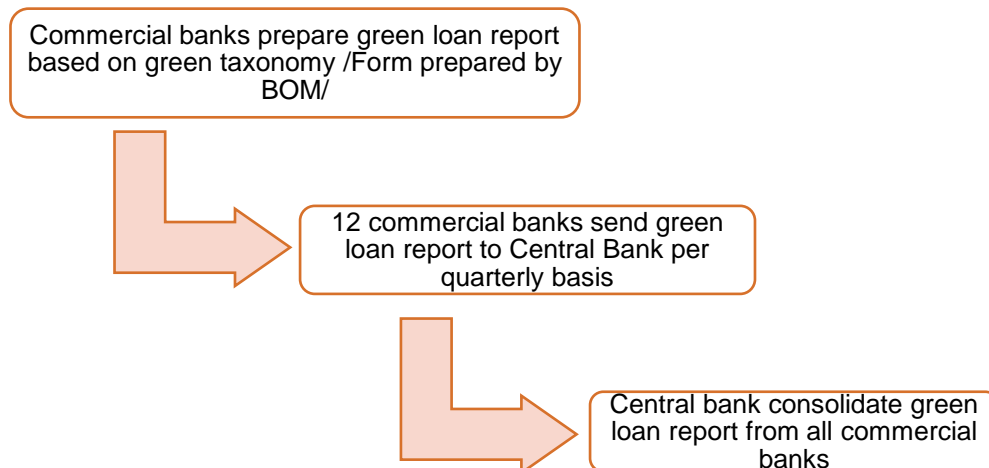
Source: Transcapital NBFi

Other non-bank financial institutions are developing products to issue green loans in future. Hybrid used automobiles make up the majority of the green loan portfolios for non-bank financial organizations.

3.3. Green Loan Reporting & Monitoring

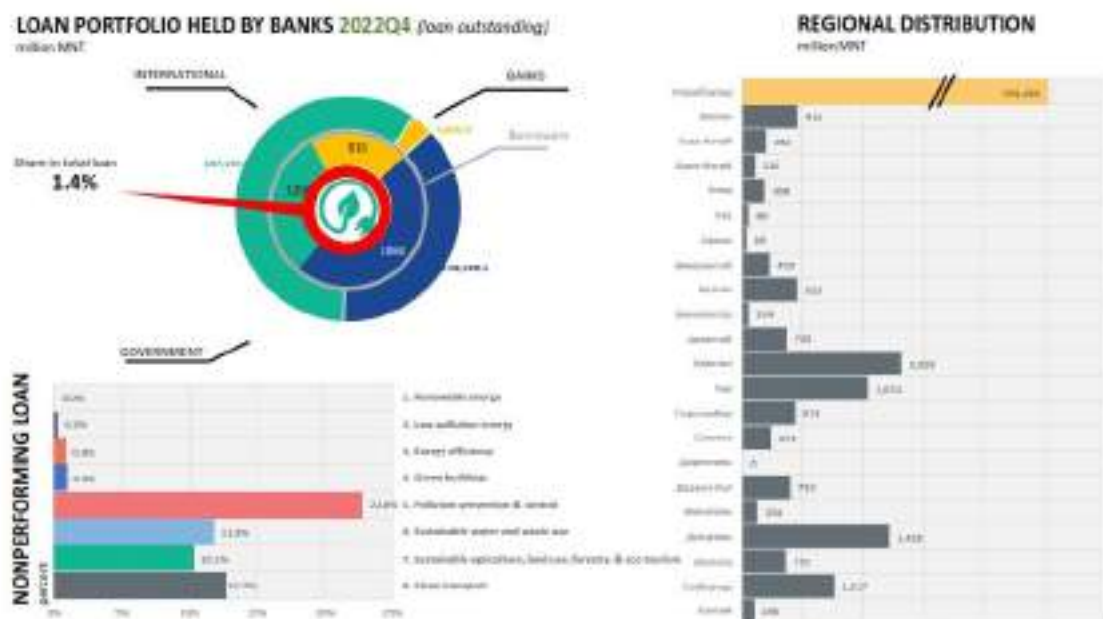
The Central Bank created a green loan reporting & monitoring format based on the Mongolian Green Taxonomy in 2020. Since then, the central bank has received quarterly green credit reports from various commercial banks in this format. The central bank compiles the received reports and makes them publicly available on its website.

Figure 3: Green loan reporting process



Some of the key highlights, as per the latest report on green loans in Mongolia are provided below.

Figure 4: Green Loan Monitoring Report - Q4 2022



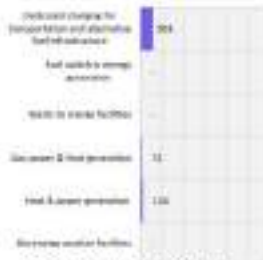
LOAN PORTFOLIO HELD BY BANKS 2022Q4 (loan outstanding)
million MYR

56 TECHNOLOGIES

1. Renewable energy



2. Low pollution energy



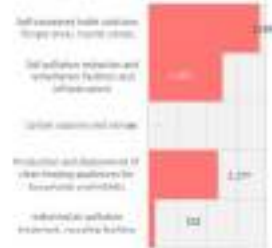
3. Energy efficiency



4. Green buildings



5. Pollution prevention & control



6. Sustainable water and waste use



7. Sustainable agriculture, land use, forestry, & eco tourism



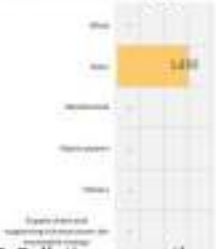
8. Clean transport



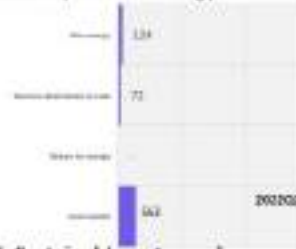
LOAN PORTFOLIO HELD BY BANKS 2022Q4 (loan outstanding)
million MYR

28 SUB-CATEGORIES

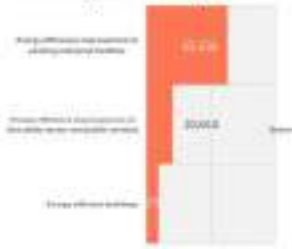
1. Renewable energy



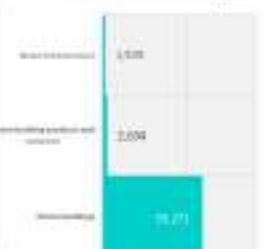
2. Low pollution energy



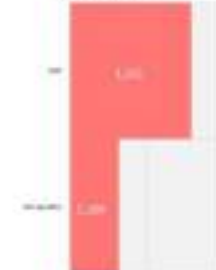
3. Energy efficiency



4. Green buildings



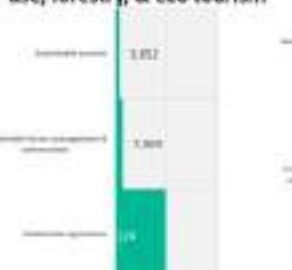
5. Pollution prevention & control



6. Sustainable water and waste use



7. Sustainable agriculture, land use, forestry, & eco tourism



8. Clean transport



4. STAKEHOLDER DISCUSSIONS

As part of the KSTA, a number of stakeholder discussions were held with different government agencies/ stakeholders who are part of the green loan lifecycle in Mongolia. Based on those discussions, this chapter provides a list of incentives that have been proposed by these stakeholders for possible implementation in Mongolia, along with certain rationale.

Given below is the list of various stakeholders that were consulted by the KSTA team.

Table 7: Stakeholder Discussions - Green Loan Lifecycle Review

#	Meeting date	Organization	Attendees	Designation
1.	14-Dec-22, 10-Mar-23	Bank of Mongolia	Gan-Ochir Doojav	Chief economist
2.	14-Dec-22	Bank of Mongolia	N.Urgamalsuvd	Head of Monetary Policy and Modeling Division, Monetary Policy Department
3.	14-Dec-22, 10-Mar-23	Bank of Mongolia	Munkhbayar Gantumur	Officer of Monetary Policy and Modeling Division, Monetary Policy Department
4.	10-Mar-23	Bank of Mongolia	Ninjin Namkhajantsan	Senior Supervisor, Banking Policy Division, Banking Resolution and Policy Department
5.	1-Jan-23	Bank of Mongolia	Tsenddorj Dorjpurev	Senior Economist, Research and Statistics Department, Statistics Division
6.	7-Mar-23	Tenger Insurance	Baatarbold Jukov	Chief Retail Insurance Officer
7.	7-Mar-23, 16 Mar-23	XacBank	G.Sarnai	Project Development Officer, Eco-Banking Division
8.	2-Feb-23	Khan Bank	E.Bulganchimeg	Project loan manager (Green finance), Credit Policy and Regulations Department
9.	24-Jan-23	Trade and Development Bank	Nyamsuren Davaatseren	Head of Green Funding Office
10.	22-Dec-22 14-Mar-23	Financial Regulatory Commission of Mongolia	O.Byambasuren	Senior Officer, Policy Coordination Division, Insurance Department
11.	27-May-22, 23-Jun-22, 11-Oct-22, 27-Feb-23	Mongolian Sustainable Finance Association	Nomindari Enkhtur	Chief Executive Officer
12.	9-Mar-23	Mongolian Sustainable Finance Association	Bilegsaikhan Byambadorj	Senior Business Development and Partnership Manager

#	Meeting date	Organization	Attendees	Designation
13.	2-Feb-23	Khan Bank	B.Suvd	Senior project loan manager (Green finance), Policy and Regulations Department

Based on the stakeholder discussions and information collected, the subsequent sections provides a list of proposed, planned and under consideration incentives for green loans in Mongolia by various key agencies as listed in the table above.

4.1. Needs to be addressed

As part of stakeholder discussions, certain key considerations and needs have been identified across the green loan lifecycle which need to be addressed to ensure more issuance of such green loans and to achieve the target of green loans being 10% of total loan portfolio of banks in Mongolia.

Need for clear classification of “Green” Loans

There are inconsistencies regarding the evaluation process across commercial banks & NBFIs on how a loan is classified as “green”, which also impacts the accuracy of green loan reporting & monitoring by Bank of Mongolia.

Some key observations in this regard are below:

- The Mongolian Green Taxonomy is a very good starting point for determining which categories of investments are actually beneficial to the environment, but most sectors must be more fully defined, and performance standards are lacking in sectors.
- Lack of detailed industry classification and technical criteria in taxonomy makes it difficult to define green loan precisely.
- All banks & NBFIs which were part of stakeholder consultations had a different understanding of green loan due to the general classification of the taxonomy. For example, some banks classify registered hybrid car loans as green loans, while others did not.
- Some banks also use their own tools for green loan specifications. For example, The Trade and Development Bank (TDBM) evaluates green loans using its own greenhouse gas reduction measurement tool developed with the assistance of an external organization and the Sustainable Finance Association. Similarly, Khan Bank uses their own tool and lender’s criteria instead of taxonomy for green loan classification.

Need for Uniform Green Lending criteria

As per stakeholder discussions, it was observed that there are no uniform lending criteria across commercial banks in Mongolia for green loans, and the criteria for verification of borrowers/ risk assessment also vary significantly.

Some key observations in this regard are below:

- Banks apply their own internal criteria and criteria applied by external lenders to borrowers when issuing loans.
- Some foreign lending financial institutions provide assistance with verification and others do not. In case of non-presentation, the bank is responsible for it. In this case, the bank works with external audits and consultants on green loan verification of borrowers.
- Given that green lending activity is still considered in nascent stage in Mongolia, there is a lack of organizations, technical capacity and human resources in this area.

Need for Capacity Building & Awareness about Green Loans

Various stakeholders and institutional agencies across the green loan lifecycle need to take initiatives for capacity building and knowledge dissemination about green loans in Mongolia, especially to remove

certain myths about green loans among the potential borrowers. This will also facilitate larger green loan lending in the country.

Some key observations in this regard are below:

- Green loans are only seen as concessional terms by consumers due to a lack of understanding. It is pertinent to mention here that the policy interest rate in Mongolia is around 13%³. This implies a high loan basis interest rate and hence, these loans may not be very high difference in interest rates compared to commercial loans, unless there is concessional financing available.
- The stakeholders also face challenges due to limited awareness about green loans amongst potential borrowers. There is a general lack of understanding about what green loans are and what their benefits are. For example, Khan Bank employs over 6,000 people and accounts for 30% of the total green loan portfolio in Mongolia. They stressed that they spend a significant amount of time and cost to ensure that all employees and customers understand these aspects.
- In order to make green loans cheaper, some Mongolian banks are attracting international funds which can be directed towards green business loans. However, there is a lack of capacity within commercial banks on how international funding can be procured and they need guidance in this regard, including determining the base rate, economic conditions, and exchange rate risk for such borrowings.

Need for improvements in Green Loan Monitoring Process

There is a need to improve the process of reporting & monitoring of green loans in Mongolia, to ensure accuracy in terms of loans issued and to enable the country reach its green loan target.

Some key observations in this regard are below:

- Besides the quarterly reporting of green loans to Bank of Mongolia, there is not a defined or standard process of supervision and monitoring of green loans. Instead, the Central Bank monitors commercial banks on an informal basis
- Commercial banks provide the central bank with project numbers rather than project details.
- Only when a sudden increase or decrease of certain types of green loans is observed from the previous period, the loan information is re-examined by monitoring activities.
- Since the Bank of Mongolia has weak control over bank green loan reports, some banks' total green loan portfolio is overestimated.
- Due to inconsistencies in classification of green loans, some banks were not sure if their reporting is indeed correct and are looking for standardized guidelines or enhancements in Mongolian Green taxonomy.

5. KSTA RECOMMENDATIONS

Based on a detailed assessment of green loan lifecycle and needs identification through stakeholder consultations, this chapter describes KSTA recommendations which can be implemented in Mongolia, so as to improve the green loan dissemination in the country. Each recommendation includes the relevant implementation mechanism & specific case-study examples from other countries as per international best-practices.

The table below provides a summary of recommended actions across the green loan lifecycle in Mongolia, as elaborated in subsequent sections.

Table 8: Recommendations for Green Loan Lifecycle in Mongolia

#	Recommendation	Brief Description
1.	<i>Enhancement of Green Taxonomy</i>	Enhancement of Mongolian Green Taxonomy by defining the sectors more precisely and by creating sector specific technical criteria, to enable clear classification of green loans by commercial banks.
2.	<i>ESG-Oriented Approach to Lending Criteria</i>	Incorporation of certain E,S,G elements in lending criteria for green loans, to develop a standardized risk assessment/ lending criteria for such loans by commercial banks, and to assist in verification of borrowers of such loans.
3.	<i>Capacity Building and Knowledge Dissemination Initiatives</i>	To build capacity in area of green finance and disseminate knowledge on green loans across various stakeholders such as policy-makers, regulators, commercial banks and borrowers.
4.	<i>Non-Financial Disclosures for Borrowers</i>	Non-financial disclosures by borrowers who take green loans above a certain threshold limit, will help prevent greenwashing and
5.	<i>Network for Greening the Financial System (NGFS)</i>	BOM can consider to become part of NGFS, which will enable the central bank to enhance its capability for green loan monitoring & supervision. It can also help to mobilize concessional funding for green loans due to enhanced credit worthiness of the economy at the international platform.
6.	<i>United Nations Principle for Responsible Investments (UNPRI)</i>	BOM can consider implementing UNPRI, so as to employ responsible investment strategies for reserves management at the strategy, policy and asset class levels

For each of the proposed recommendation as per table above, the subsequent sections provide a detailed description, implementation mechanism and case study examples to demonstrate the impact of the incentive in promoting green loans, which can be applied in Mongolia.

Additional proactive norms to mitigate the challenges in the green loan lifecycle process are discussed after the above section on policy addressal to the challenges faced by the Mongolian economy.

5.1. Enhancement of Green Taxonomy

As per international standards and comparison with some of established taxonomies, Mongolian taxonomy could be enhanced by defining the sectors more precisely by creating sector specific standards. Some of the considerations to enhance the exiting green taxonomy are below.

- Harmonizing the Green Taxonomy with international taxonomies like EU, England, France, China, CBI etc. while considering specific domestic circumstances could really prove beneficial for Mongolia.
- Regulators have a significant role here to provide a technically sound justification for the activities and investments considered 'green'. This is very important even to facilitate the **'verification of borrowers'** at a later stage.
- Central Bank has a role to establish new standards, upgrade existing norms and standards, measures in the implementation of the green economy, to align disclosures and reporting with the taxonomy; and establish national measurement, reporting & verification system.
- Inclusion of clear performance thresholds for each activity to meet key sustainability objectives to enable clear classification of green loans

Implementation Mechanism

The enhancements in taxonomy can be implemented when objectives of the current taxonomy can be crystalized in terms of clear objectives under sub-classification, ranging from biodiversity protection and pollution preventive activities to climate change adaptation and mitigation.

The enhanced Green Taxonomy can thus contribute to directing capital flows towards sustainable green investments and help increase the financial disclosure of public and private market actors, hence reducing the information asymmetries and increasing financial transparency.

The implementation of forward-looking advanced taxonomy in Mongolia can start with answering the below questions.

- Which environmental-friendly green lending/ borrowing objectives does the taxonomy addresses or plan to address?
- Are technical screening criteria (TSC) for economic activities that contribute substantially to the green loan incentivizing objectives already defined? If yes, are quantitative metrics and dynamic thresholds provided or only descriptive metrics used?
- Are 'do not significant harm' (DNSH)⁴ criteria for other ecofriendly investment practices defined? For example, EU taxonomy has defined six green classifications and contribution to one will prove to be DNSH to the other five –
 1. Climate change mitigation
 2. Climate change adaptation
 3. Water protection
 4. Circular economy
 5. Pollution prevention
 6. Biodiversity and ecosystems

Similar classification, standards and metrics can help Mongolian taxonomy towards customized specific 'green' definition and practices to enable BOM in clear identification to facilitate the process of green loans.

⁴ The DNSH criteria means an economic activity that contributes substantially to one of the specified green objectives without disturbing or impacting the other environmental objectives.

International Case Reference - Green Central Banking Policy Taxonomy

Green Central Banking Policy Taxonomy⁵ has been recently published by New Economics Foundation for Emerging and Developing Countries (EMDCs). In contrast to advanced economies where central bank mandates are predominantly focused on price stability, many of the central banks in EMDCs have a wider remit to support sustainable development and the government's economic policy agenda.

Given the diverse needs and contexts of emerging economies, this guide avoids one-size-fits-all definitions and standards. It shall present ways to develop a taxonomy based on the environmental objectives relevant to a country's sustainable development priorities and agenda.

Three different categories of intervention are regularly used in these countries to address the challenge of green finance and climate change:

- Green credit allocation instruments that have the objective of allocating credit to green sectors,
- Green regulatory (prudential and macroprudential) instruments for safeguarding financial stability,
- Other green central banking activities, such as developing green finance guidelines or setting up green bond markets.

With regard to green growth and credit allocation, existing traditions of financial intervention shape the country's approach. Central banks that have in the past been engaged in centralized credit allocation policies have added categories to their existing priority loan program for green projects, in particular renewable energy projects. In Bangladesh, for instance, it is estimated that around 10% of the population has been supported by the central bank's green refinancing program in installing home-solar power systems.

We understand from stakeholder discussions that the current Taxonomy is now being expanded to become the SDG Finance Taxonomy, but details are not yet available. Thus, the Mongolian economy should adopt a customized specific taxonomy (over general taxonomy without sub-classifications for the green activities) with facilitating features of some of the established taxonomies (such as EU, China) to enhance the green loans access, reach, and availability.

5 Available at <https://neweconomics.org/uploads/files/Green-Central-Banking.pdf>

5.2. ESG-Oriented Approach to Lending Criteria

An ESG-oriented approach to lending criteria will be specific in terms of climate and social objectives to be examined under E, S and G, typically categorizing them as high risk, medium risk, and low risk. It is measurable in terms of quantitative, semi-quantitative or qualitative data to which scoring can be allotted. Such an ESG-oriented approach can assist banks in investment and green lending decisions.

Each of the buckets, i.e., E, S and G, include certain parameters, each of which are measured by metrics.

- Environmental bucket typically includes parameters related to the state of the environment, climate, and natural ecosystems.
- Social bucket includes parameters that look at the relationship of the business with various stakeholders.
- Governance bucket covers parameters related to fair conduct and accountability of the business.

To gauge which are the most critical parameters for any bank, the materiality mapping exercise is a good place to start. Materiality mapping exercise identifies the key issues affecting a bank, as per their importance to stakeholders and to the business, and these issues are the most critical for the bank to manage.

ESG integration involves two primary aspects, as listed below.

1. First aspect is to incorporate ESG issues into the financial institution's own risk management, governance, disclosure, business strategy, branch network, training, and capacity building, and updating data systems such that it leverages KYC and due diligence processes to collect more information on ESG issues.
2. Second aspect is to assess the underlying counterparty's business value drivers like competitive position, growth prospects, ability to sustain in long run, and financial condition, so that the resultant financial analysis on the counterparty reflects the impact of non-financial risks and opportunities.

Implementation Mechanism

For banks and credit oriented financial institutions looking to consider ESG issues in their lending decisions, they might build an ESG assessment framework in four parts.

- 1) The first involves conducting the materiality mapping exercise to identify critical issues over short- and long-term periods, and then identifying the most crucial ESG-related issues of a potential counterparty that the financial institution seeks to analyze.
- 2) The second piece relates to calculating an ESG risk rating or scoring using quantitative or qualitative inferences (preferably rules-based) on the material ESG issues, on similar lines like the ESG rating process highlighted in the previous slide.
- 3) The third piece relates to developing specific ratios that help financial institutions analyze, and compare, if they are meeting sustainability objectives.
- 4) The last piece relates to adjusting the financial institution's products, policies, and people in line with the sustainability objectives. In the case of products, it implies introducing products/features like green mortgage, sustainability-linked loans, sustainable letter of credit in trade finance, green loans (to green sectors), etc.

With the growing awareness of investors and customers on the ESG issues, financial institutions who do not start factoring ESG within their decisions may face higher credit risks and unfavorable terms for funding in the medium to long term.

International Case Reference - Sustainability Linked Loan Principles (SLLP)

To facilitate and support environmentally and socially sustainable economic activity and growth through sustainability-linked loans, loan market associations, namely the LSTA, LMA and APLMA jointly published the Sustainability Linked Loan Principles (SLLP), and new roles such as sustainability coordinator/structurer have emerged in the loan market.

Lenders currently use the SLLP framework for big-ticket deals, and lessons learnt from these deals should be used when there is an opportunity to work on KPIs for a deal in the middle market or SME segment.

At the initial credit due-diligence level of looking at the borrower profile, common KPIs as set out in SLLP and sector-specific KPIs can be built in as part of sanction terms. There could be a financial outlay for borrowers for complying with additional ESG-related reporting requirements in the form of ESG audit reports/sustainability reports; borrowers could be incentivized through stepped-up margins.

Commercial lenders could also include ESG performance as a parameter in their internal rating systems, along with existing financial and operating parameters. Incorporating ESG considerations in stress testing and ESG keywords/negative triggers/greenwash alerts into the borrowers' related-party surveillance systems helps better integrate ESG criteria into commercial lending products across segments.

5.3. Capacity Building and Knowledge Dissemination Initiatives

Access to green finance is much bigger agenda than matching climate projects to funding sources and includes policy coherence, integration into budgeting, basic project finance, blending instruments, catalyzing private finance. Climate change and related societal threats underscore the imperative for accelerating learning and developing capacity within the green finance sectors of developing countries.

For most developing and emerging countries there is a lack of awareness and capacity for green technologies and activities across the policy and investment spectrum. It is essential to build capacity in the area of green finance and disseminate knowledge on green loans across various stakeholders such as policy-makers, regulators, commercial banks and borrowers.

Implementation Mechanism

Where influence of the financial sector is possible, support mechanisms for capacity building play an important role and are mainly provided by Development Finance Institutions (DFIs). Mechanisms such as technical assistance, guarantees, concessional loans (longer tenors or subsidized interest rates), need to be critically evaluated.

Disbursement channels are important factors in the success of green finance. As developing country governments and other stakeholders develop relevant capacity and experience in designing green financial incentives and national systems for monitoring and evaluation, they can increasingly direct international resources to complement and supplement domestic resources for implementation of national financing strategies, plans and programs for green or climate investments.

International Case Reference – Green Finance Capacity Building in China

China has promoted the mainstreaming of green finance to move the needle forward in short period of time. The country has institutionalized effort to build capacity as a key towards green growth finance.

It has identified & implemented capacity building in three distinct areas:

1. Dissemination of knowledge and capacity enhancement of Banks & FIs on the available tools to assess environmental CBA.
2. Capacity building by developing and innovating green financing products.
3. Making the understanding of government officials and local levels on the fundamentals of green finance and how the capacity could be enhanced at sectoral level.

Such policy measures in the area of capacity building could prove to be stepping stone for Mongolian central bank, DFIs, and other FIs to disseminate, and deepen the knowledge of green loans to promote the same in the economy.

5.4. Non-Financial Disclosures for Borrowers

It is recommended to ask borrowers of green loans, who borrow above a certain threshold amount, to implement non-financial disclosures as part of their governance & reporting framework.

Between 1997 and 2013, several non-financial disclosure frameworks came out in the market which are being used by companies and financial institutions even today to prepare their sustainability reports. These include GRI, Sustainability Accounting Standards Board (SASB) and Integrated Reporting (or IR).

During this period, certain principles that laid guidelines on how to analyze and screen investments have also been notified. These include the Equator Principles, which focused more on the banking sector and the PRI, which focused on institutional investors.

Listed below are the key benefits of such non-financial disclosures by borrowers of green loans:

- It helps understand the link between financial and non-financial performance.
- It helps influencing long term business strategy, policies, and management priorities.
- It helps benchmark sustainability performance against established norms & principles.
- It helps avoid damage to reputation and brand, from negative publicity.
- It helps improve employee motivation and making the firm an employer of choice for employees.
- It helps governments and regulators understand the business landscape in context to ESG risks.

With the growing pledges around net-zero and carbon neutrality, both at corporate and company level, it is perhaps all the more critical to scale up the quantity and quality of non-financial disclosures in line with the targets and pathways laid out by the pledges.

Such climate mandates and disclosures could prove beneficial for the developing countries like Mongolia to create sustainability practices' awareness, to ensure compliance and prevent greenwashing.

Implementation Mechanism

Given the growing focus on climate, the Financial Stability Board (FSB), in 2017, released climate-related financial disclosure framework called TCFD, which aimed to help financial institutions and corporates better understand the climate risks and opportunities related to their business.

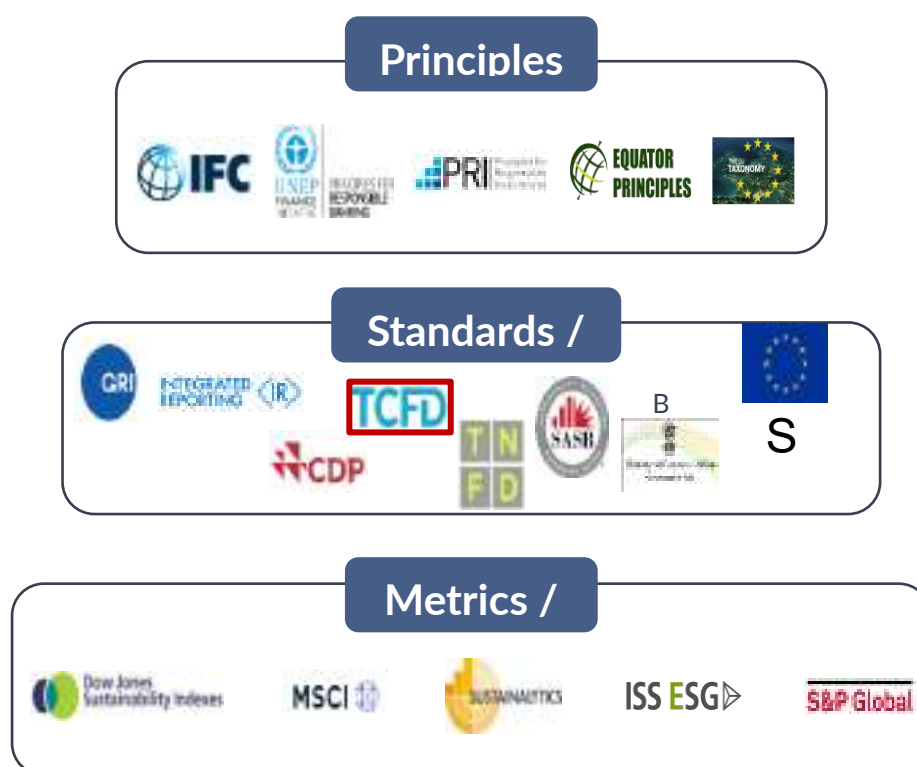
In 2019, UNEP FI brought out guiding principles specific to the banking industry, with the PRB. Another milestone occurred with the EU Green Taxonomy notification in 2020, which set out a common classification system for economic activities that are sustainable, low-carbon, and resource-efficient.

This classification system was useful in green tagging of assets for financing and reduce chances of inadvertent greenwashing in sustainable finance.

International standards and Regulators Support



Decoding TCFD Concept



Source: Authors' depiction from TCFD Reports

Lastly, due to the challenges around multiple non-financial disclosure frameworks in the market, five organizations that are involved in setting disclosure standards, i.e., CDP, CDSB, GRI, IR and SASB, issued a “Statement of Intent to Work Together Towards Comprehensive Corporate Reporting” in 2020. As part of this, SASB and IIRC merged in 2021 to form the Value Reporting Foundation. This would focus on a standardized corporate reporting system. CDP is expected to consolidate soon into this.

To summarize the international developments, there has been a growing pressure to step up non-financial disclosures as the awareness around sustainability and climate risks to businesses builds up. The push is coming not just from regulators, but also from the capital markets to raise capital from green pools of capital.

5.5. Network for Greening the Financial System (NGFS)

The Bank of Mongolia can consider to be a part of Network for Greening the Financial System (NGFS), which facilitates discussions on how best to address climate risks and scale up sustainable finance across member countries. In particular, NGFS' (NGFS, 2019a) six workstreams encourage its members to -

1. integrate climate risks into financial stability monitoring and micro supervision;
2. integrate sustainability factors into own-portfolio management;
3. bridge data gaps;
4. build awareness and intellectual capacity and encourage technical assistance and knowledge sharing;
5. achieve robust and internationally consistent climate and environment-related disclosure; and
6. support the development of a taxonomy of economic activities.

Further, as NGFS conducts periodic surveys to gauge members' progress on green initiatives, this could motivate Mongolian central bank to benchmark themselves against peers. This may also help BOM to mobilize concessional funding for green loans due to enhanced credit worthiness of the economy at the international platform. As of June 2021, out of 95 NGFS members, 19 are from the Asia-Pacific region, as listed in table below.

Table 9: Asia-Pacific CBFS which are NGFS and SBN members

	Network for Greening the Financial System (NGFS)	Sustainable Banking Network (SBN)
Australia	*	
Armenia	*	
Bangladesh		*
Cambodia	*	*
China	*	*
Fiji		*
Georgia	*	*
Hong Kong, China	*	
India	*	*
Indonesia*	*	*
Japan*	*	
Kazakhstan		*
Kyrgyzstan		*
Lao PDR		*
Maldives		*
Malaysia	*	
Mongolia		*
Nepal		*
New Zealand	*	
Pakistan		*
Philippines	*	*
Republic of Korea*	*	
Russian Federation	*	
Samoa		*
Singapore	*	
Sri Lanka		*
Thailand	*	*
Turkey		*
Viet Nam		*
Total	19	20

Source: WP Series Dec 2021, UNESCAP from NGFS and IFC (2021)

5.6. United Nations Principle for Responsible Investments (UNPRI)

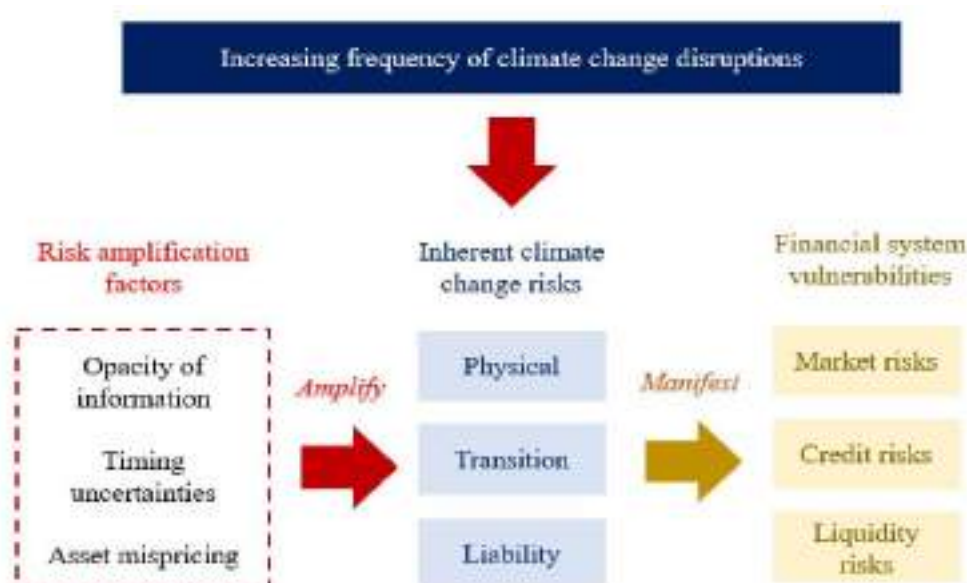
The UNPRI urges central banks to employ responsible investment strategies for official reserves management. Whilst safeguarding investment returns, central banks can also help drive sustainability by establishing responsible investment frameworks for reserves management at the strategy, policy and asset class levels (Gerritsen, 2019).

Signatories of the UNPRI are committed to six core principles (UNPRI, 2021b), including -

1. incorporating ESG issues into investment analyses and decisions;
2. integrating ESG issues into ownership policies and practices;
3. seeking appropriate disclosure on ESG issues by investee entities;
4. promoting acceptance and implementation of the principles within the investment industry;
5. working together to enhance effectiveness in implementing the principles; and
6. reporting on activities and progress towards implementing the principles.

By following the principles of responsible investments by UN, central banks could address the transmission associated climate risks due to financial system (FS) shocks.

Figure 5: Transmission Channels from Climate Related Risks to FS vulnerabilities



Source: UNESCAP 2021, adapted from Brunetti and others

As of June 2021, the Hong Kong Monetary Authority is the only Asia-Pacific Central Banks Financial Supervisory Authorities signatory of the UNPRI. Such affiliations could enable Mongolian Central Bank, BOM to implement widely used international best practices.

6. Concluding Remarks

As part of the Knowledge and Support Technical Assistance (KSTA) by The Asian Development Bank, this report aims to contribute towards enhancement of the Green Finance deployment in Mongolia and support implementation of the Mongolia Sustainable Finance Roadmap in the country. This TA aims to support the Government of Mongolia in advancing the green finance policy and regulatory framework and in undertaking capacity development to enhance capability to develop green finance projects and products.

As per the objectives of the Report, a set of six (6) recommendations have been provided for consideration by Ministry of Finance, Bank of Mongolia and other relevant stakeholders to increase the share of green loans in the country to 10% of the total loan portfolio of commercial banks and NBFCs by 2030.

These recommendations are based on international best practices, and the Report provides the specific benefits of proposed measures to address the various challenges and needs to be addressed across the green loan lifecycle, as identified through extensive stakeholder discussions. Proactive steps and by central banks and financial supervisory authorities to address the identified challenges will enhance their ability to promote green loans in the country, and also address the climate risks that face emerging economies like Mongolia.