Suruhanjaya Sekuriti
Securities Commission
Malaysia

SUSTAINABLE AND RESPONSIBLE INVESTMENT ROADMAP FOR THE MALAYSIAN CAPITAL MARKET

SUSTAINABLE AND RESPONSIBLE INVESTMENT ROADMAP FOR THE MALAYSIAN CAPITAL MARKET

Suruhanjaya Sekuriti
Securities Commission
Malaysia

DISCLAIMER

This book aims to provide a general understanding of the subject and is not an exhaustive write-up. It is not intended to be a substitute for legal advice nor does it diminish any duty (statutory or otherwise) that may be applicable to any person under existing laws.

CONTENTS

FOREWORD

BY DATUK SYED ZAID ALBAR
CHAIRMAN, SECURITIES COMMISSION MALAYSIA

Corporations and businesses are increasingly motivated to adopt environmentally friendly and sustainable practices. This resulted from greater awareness of businesses' responsibilities to stakeholders, including the social impact of their operations, as well as the need to conserve scarce or non-renewable resources. As companies adapt to the demands of tomorrow, a well-developed financial sector is essential to support their needs. The capital market is hence uniquely placed to answer the call for sustainable finance in supporting the long-term growth of the economy.

The Securities Commission Malaysia (SC) has long been cognisant of the need to promulgate and develop sustainable finance as it aligns closely with the principles underlying our Islamic capital market. To this end, we have established facilitative regulatory frameworks to support sustainable and responsible investment (SRI) as well as green financing. We also continue to play an active role in developing SRI at the regional level.

Globally, the increase in market-based instruments linked to green, social or sustainable goals signifies rising investor interest and a huge potential for the SRI segment in Malaysia.

In charting a strategic direction vis-à-vis this evolving market landscape, we have developed the *Sustainable and Responsible Investment Roadmap for the Malaysian Capital Market* (SRI Roadmap), which serves to guide our efforts to accelerate the growth of this segment.

The 20 recommendations contained in the SRI Roadmap are mapped to five overarching strategies aimed at driving the development of a vibrant SRI ecosystem for Malaysia as well as the region. These strategies serve to expand the range of SRI instruments, issuers, investors and ancillary services, while strengthening disclosure and governance by drawing synergies from our existing global leadership in the closely-aligned field of Islamic finance.

The SRI Roadmap also reflects the aspirations of our domestic and international stakeholders for the SRI segment in the Malaysian capital market. Their invaluable feedback has been instrumental in the formulation of the recommendations which underpins the SRI Roadmap. I would like to acknowledge and express my sincere appreciation to everyone involved for their contributions in bringing the SRI Roadmap to fruition.

It is our hope that the SRI Roadmap will further accelerate the growth of the Malaysian capital market as well as foster a greener, more sustainable and inclusive nation in line with the United Nations' 2030 Agenda on Sustainable Development.

Datuk Syed Zaid Albar
November 2019

ACKNOWLEDGEMENT

The *Sustainable and Responsible Investment Roadmap for the Malaysian Capital Market* (SRI Roadmap) is a product of extensive research, engagements and discussions with Malaysian and international stakeholders.

The Securities Commission Malaysia (SC) would like to express its sincere appreciation to the various industry representatives, associations and regulatory bodies who have provided valued opinions and feedback as part of the SRI Roadmap development.

The SRI Roadmap would not have been possible without the collaborative and tireless efforts from the staff of the Corporate Affairs, Corporate Bonds & Investment Products and International Affairs departments, the Islamic Capital Market Development business group, as well as guidance from the SC's senior management team.

Overall development and production of the SRI Roadmap was led and co-ordinated by the Markets & Products department of the Market Development business group of the SC.

CHAPTER 1

GLOBAL SUSTAINABLE INVESTMENT LANDSCAPE

Sustainable development has been globally recognised as an imperative, with commitments being made to address relevant issues by nations including Malaysia. Accordingly, the availability of finance supported by efficient capital markets would play a crucial role in ensuring that the global sustainable development needs are adequately supported.

1.1 GLOBAL POLICY SHIFTS TOWARDS SUSTAINABLE DEVELOPMENT

Since the introduction of the sustainable development concept[1] in the *Brundtland Report*[2] in 1987, the awareness on ensuring that economic growth and development should not be made at the expense of the environment and society, has seen a gradual increase. Subsequently, the Millennium Development Goals (MDGs) was introduced by the United Nations (UN) in 2000 which commits world leaders to address eight goals including extreme poverty, hunger, disease, environment, sustainability and women empowerment.[3] The world's collective commitment to address sustainable development continued with the introduction of the Sustainable Development Goals (SDGs) by the UN in 2015, under the 2030 Agenda for Sustainable Development.

Source: UN

1 Sustainable development aims to meet the needs of the present without compromising the ability of future generations to meet their own needs, *Brundtland Report 1987*.
2 World Commission on Environment and Development, 1987, *Our Common Future* (also known as the *Brundtland Report*).
3 UN, 2015, *The Millennium Development Goals Report.*

The SDGs, which came into effect in January 2016, was agreed by 193 Member States of the UN, including Malaysia. The SDGs, which include 17 goals and 169 targets, is a call for action for the 'people, planet and prosperity' through global partnership to ensure the three dimensions of sustainable development are achieved: (i) economic, (ii) social; and (iii) environment.

Globally, there is also recognition of the urgent need to address pressing environmental issues and challenges including climate change. *The Paris Agreement on Climate Change* (Paris Agreement), signed in 2016 within the United Nations Framework Convention on Climate Change (UNFCCC), sets out global action to keep the global temperature rise to well below 2°C above pre-industrial levels and to pursue efforts to limit the temperature increase even further to 1.5°C.[4] This was the first-ever universal and legally binding global climate agreement dealing with greenhouse gas (GHG) emissions, mitigation, adaptation and finance. As of September 2019, 195 countries, including Malaysia have become signatories to the Paris Agreement. Under the Paris Agreement, Malaysia has committed to reduce GHG emissions by 45% by 2030, relative to the 2005 level.

In pursuing economic growth, the externalities caused by increasing population, urbanisation and consumption demand patterns would place heightened pressure on limited natural resources such as land, air and water. The impact of climate change has also resulted in disruptive implications on social well-being, production, agricultural output, economic development and financial stability of a country. To address these issues, companies are transitioning towards low carbon industries and technologies which in turn, would lead to issues of stranded assets and impaired assets resulting from reduced investments in carbon-based activities.

"The *Paris Agreement on Climate Change* (Paris Agreement), signed in 2016 within the United Nations Framework Convention on Climate Change (UNFCCC), sets out global action to keep the global temperature rise to well below 2°C above pre-industrial levels and to pursue efforts to limit the temperature increase even further to 1.5°C."

4 UN, 2015, Paris Agreement.

Impact of Environmental Degradation

Economic loss

Direct economic loss arising from weather-related disasters worldwide **rose by 151% from US$895.0 billion (RM3.7 trillion)** between 1978 and 1997 to **US$2.2 trillion (RM9.2 trillion)** between 1998 and 2017[5]

Loss of GDP

Global GDP **will decrease by 7% by 2100 if** global temperatures continue **to rise by 0.04°C per year**[9]

Air pollution

Premature deaths due to air pollution in 2013 cost the global economy **US$225.0 billion (RM913.3 billion)** in lost labour income and about **US$5.1 trillion (RM20.7 trillion) in welfare losses worldwide**[6]

Economic sector

Climate change **may negatively affect transport infrastructure, tourism, electricity grids** and **will decrease productivity and economic growth**[10]

Land degradation

The **global economy will lose US$23.0 trillion (RM 90.9 trillion) by 2050** through land degradation[7]

Increasing temperature

Human induced warming reached approximately **1.0°C above pre-industrial levels in 2017**, with an **increase of 0.2°C for every decade. Global warming is likely to reach 1.5°C between 2030 and 2052** if it continues to increase at the current rate[11]

Rising sea levels

The **sea level rose** by about **3mm per year (3.7mm in 2018**, outstripping the average annual increase of **2.1mm** over the past three decades), and **could rise by 65cm by the end of the century**, with serious implications for coastal cities and small islands[8]

Impact of disasters

Between 1998 and 2017, **climate-related** and geophysical disasters killed **1.3 million people** and left a further **4.4 billion injured, homeless, displaced or in need of emergency assistance worldwide**[12]

Source: Data from the UN and World Bank.

5 Centre for Research on the Epidemiology of Disasters (CRED) and United Nations Office for Disaster Risk Reduction (UNISDR), 1998-2017, *Economic Losses, Poverty & Disasters.*
6 World Bank and the Institute for Health Metrics and Evaluation (IHME), 2016, *The Cost of Air Pollution: Strengthening the Economic Case for Action.*
7 United Nations Convention to Combat Desertification, 2018, *Poor Land Use Costs Countries 9 percent Equivalent of their GDP.*
8 National Oceanic and Atmospheric Administration (NOAA) Climate, 2019, *Climate Change: Global Sea Level.*
9 National Bureau of Economic Research, 2019, *Long-Term Macro Economic Effects of Climate Change: A Cross Country Analysis.*
10 The Intragovernmental Panel on Climate Change (IPCC), 2019, *Special Report: Global warming of 1.5°C.*
11 *Ibid.*
12 *Ibid.*

As such, given these real impacts, pursuing economic growth in tandem with environmental protection is key to ensure the sustainability of economic growth, well-being of the people and country's resilience against climate change and disaster. These global paradigm shifts towards sustainable development and addressing climate change are key factors that will influence policymaking decisions and actions in ensuring the well-being of current and future generations.

1.2 SUSTAINABLE INVESTMENTS TO FUND THE WORLD'S SUSTAINABLE DEVELOPMENT NEEDS

In realising the world's sustainable development needs, a significant amount of funding is required. Based on estimates by the United Nations Conference on Trade and Development (UNCTAD), SDGs face global funding needs of around US$5.0 trillion (RM16.1 trillion) to US$7.0 trillion (RM22.5 trillion) per annum[13] from 2015 to 2030. During the same period, the SDGs investment needs in developing countries are around US$3.3 trillion (RM10.6 trillion) to US$4.5 trillion (RM14.5 trillion) annually[14], mainly for basic infrastructure[15]. To reach the goals of the Paris Agreement, US$12.1 trillion (RM38.9 trillion) is needed for investments in new renewable electric power generation over the next 25 years[16], and as much as US$500 billion (RM1.5 trillion) of new investments annually by 2030 to adequately limit the GHG emissions of developing countries.[17]

Due to the enormous funding requirements, public sector financing alone will be insufficient given the strains it will impose on public finances. As such, the deployment of private sector investments through the capital market will be critical in financing sustainable development needs. This represents opportunities for the capital market to play a crucial role in the transition towards a sustainable economy.

These pressing funding needs coupled with greater awareness and appreciation of the sustainability agenda has led to the acceleration of the growth momentum of sustainable finance globally. Both the public and private sectors are channelling more investments towards meeting the SDGs through the capital market, as evident from the increasing issuances of fixed income instruments for financing green, social and sustainable projects, and commitments for sustainable investments from responsible investors. In addition, investors and stakeholders are increasingly placing importance on the extent to which companies incorporate environmental, social and governance (ESG) factors in their business practices.

---

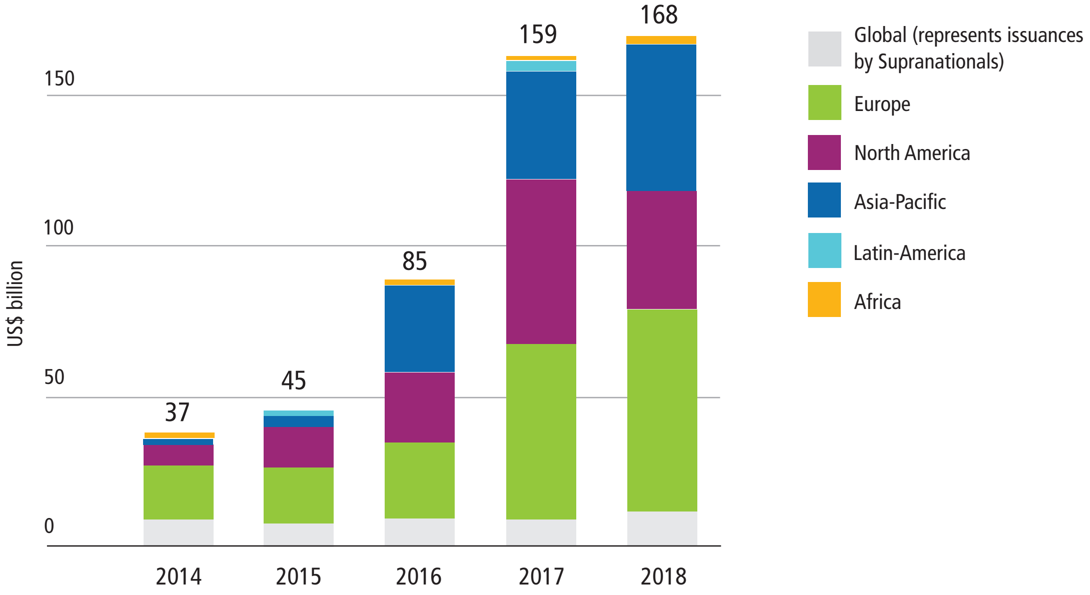
13 UNCTAD, 2014, *World Investment Report.*
14 *Ibid.*
15 Roads, rail and ports; power stations; water and sanitation, food security (agriculture and rural development), climate change mitigation and adaptation, health and education.
16 Ceres and Bloomberg NEF, 2016. *Mapping the Gap: The Road from Paris 2016.*
17 World Resources Institute, *Climate Finance and the Private Sector.*

Fixed Income Instruments

Growth in sustainable finance can be particularly observed in the green bond market. From 2007 when the world's first green bond was issued, to the end of 2018, the cumulative issuances of green bonds stood at US$521.0 billion (RM2.1 trillion), with a total increase of 46.0% in issuances in the most recent 5-year period.[18] In 2018 alone, issuances reached US$167.6 billion (RM658.8 billion).[19]

Chart 1

Green Bond Issuances According to Region



Source: Green Bonds: The State of the Market 2018, Climate Bonds Initiative (CBI)

In addition to green bonds, other thematic bonds such as social and sustainability bonds have also been issued, with an issuance amount of US$14.2 billion (RM58.1 billion) and US$21.0 billion (RM85.9 billion) in 2018, respectively.[20]

---

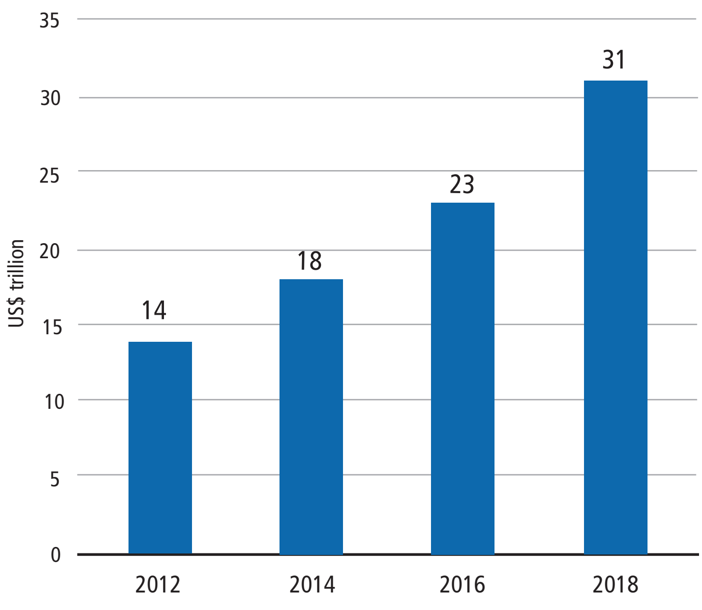
[18] CBI, *Green Bonds: The State of the Market 2018.*
[19] *Ibid.*
[20] *Ibid.*

These instruments present an ideal avenue for the financing of green, social and sustainability projects and offer attractive investment options to investors. While there have been mixed findings on whether these instruments could lead to lower cost of capital, research shows that green bonds certified by an external reviewer are traded at a lower green discount.[21] This may therefore suggest that greater transparency is key to investor confidence in the market for green, social and sustainability bonds.

Fund Management

The demand for sustainable asset classes continues to grow as more investors are shifting towards sustainable investments. Sustainable investing assets in the five major markets[22] observed by Global Sustainable Investment Alliance (GSIA) recorded a 14.5%[23] increase to US$30.7 trillion (RM125.1 trillion) from US$13.6 trillion (RM42.2 trillion) between early 2012 and early 2018.[24] These sustainable investment assets made up 33% of the total professionally managed assets in these five major markets as at 2018.[25]

Chart 2
Growth of Global SRI Assets



Source: Global Sustainable Investment Review 2012 – 2018, GSIA

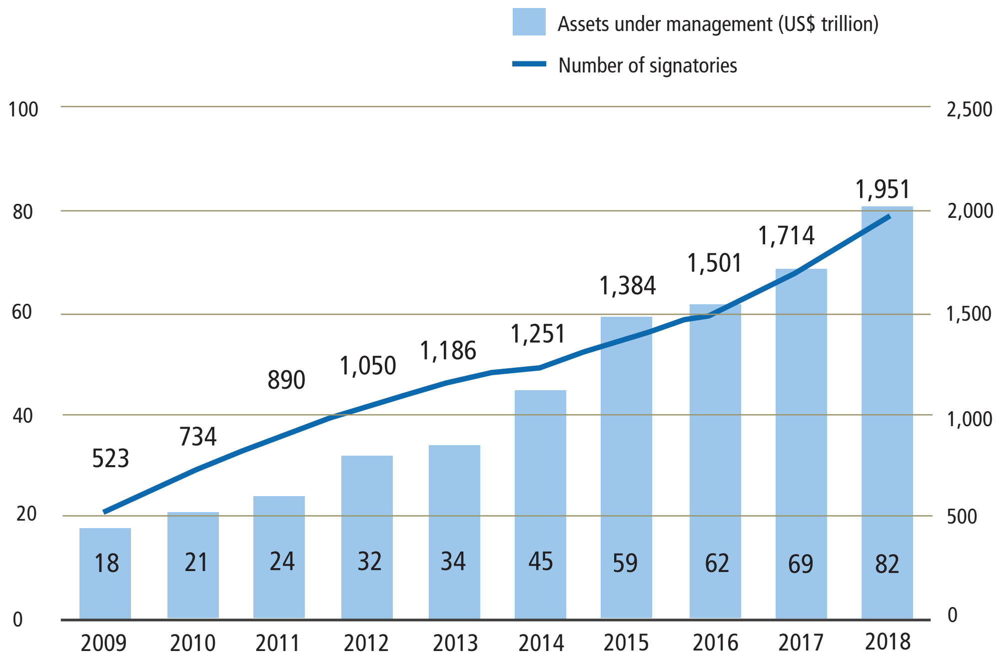
---

21 Asian Development Bank, *Asia Bond Monitor June 2018*.
22 The five major markets include Australia and New Zealand, Canada, Europe, Japan and United States of America.
23 Compound annual growth rate (CAGR).
24 GSIA, *Global Sustainable Investment Review 2018*.
25 *Ibid*.

The increasing sustainable investment trend is also reflected in the increase in the Principles for Responsible Investment (PRI) members from 523 signatories in 2009 to 1,951 signatories in 2018.[26] As signatories, the members are committed towards incorporating ESG into their investments and practices. Collectively, the signatories to the PRI represent US$81.7 trillion (RM338.1 trillion) assets under management (AUM) as compared to US$18.1 trillion (RM62.0 trillion) AUM in 2009.[27]

Chart 3

Growth of PRI AUM and Signatories



Source: PRI

The interest in sustainable investments is also becoming more apparent among individual investors who want to invest in accordance with their ethical motivation. According to the *Natixis Investment Managers ESG Cross Survey Report* conducted in 2018, 7 in 10 individual investors believe it is important to make a positive social impact through their investments.[28] These demonstrate that investors globally are more committed towards sustainable investments.

---

[26] PRI Database.

[27] *Ibid.*

[28] Natixis Investment Managers, 2019, *Natixis Investment Managers ESG Cross Survey Report.*

1.3 DEVELOPMENT OF SUSTAINABLE AND RESPONSIBLE INVESTMENT IN THE MALAYSIAN CAPITAL MARKET

The SC had identified early on that the global trends towards investments that address climate change and social issues would become a major force in the financial landscape. The SC's *Capital Market Masterplan 2* (CMP2), a 10-year strategy blueprint for the period 2011-2020, recognises the role of the capital market in supporting the sustainability agenda.

The CMP2 advocates the expansion of the capital market to create market-based solutions to mobilise investments in technology and ventures that promote sustainable and inclusive development. It also recognises that the capital market is capable of bringing scale, financial discipline and commercial accountability to social and community-based enterprises as well as projects.

Leveraging Malaysia's global leadership in the Islamic capital market (ICM), and given the similarities in the underlying principles between Islamic finance and Sustainable and Responsible Investment (SRI), Malaysia is well-positioned to champion the SRI agenda encompassing green, social and sustainable asset classes as well as investments. Towards this end, the SC introduced the 5*i*-Strategy in 2014 to develop a facilitative SRI ecosystem in the Malaysian capital market.

5*i*-Strategy

Developing a Facilitative SRI Ecosystem in the Malaysian Capital Market

WIDENING THE RANGE OF SRI ***INSTRUMENTS***	INCREASING SRI ***INVESTOR*** BASE	BUILDING A STRONG SRI ***ISSUER*** BASE	INSTILLING STRONG ***INTERNAL GOVERNANCE*** CULTURE	DESIGNING ***INFORMATION ARCHITECTURE*** IN THE SRI ECOSYSTEM
Facilitate the development of new SRI capital market products to widen and deepen the SRI asset classes	On the buy side, there is a need to attract institutional and individual investors to increase the SRI investor base, and thus demand for SRI products	On the supply side, efforts need to focus on building a strong and diversified issuer base consisting of listed and unlisted companies and multilateral organisations	Development of metrics and disclosures to measure sustainability in facilitating investment decisions to inculcate good governance practices in the SRI space	Development of platforms which provide SRI data to investors, thereby enabling better assessment of investment opportunities to ensure transparency and accessibility to the SRI market

Since 2014, several initiatives have been introduced by the SC, including the development of the SRI Sukuk Framework to facilitate the financing of projects that benefit the environment and society. Benchmarked against the *Green Bond Principles (GBP)* issued by the International Capital Market Association (ICMA) and the Social Impact Bonds issued in the UK, the SRI Sukuk Framework was designed to be versatile, providing the framework for the issuance of green, social and sustainability sukuk, thereby facilitating greater financing options for issuers. The introduction of the SRI Sukuk Framework represents a significant milestone in capital market product innovation that integrates both SRI and ICM.

Notable issuances under the SRI Sukuk Framework include the inaugural SRI sukuk issued in 2015 by Ihsan Sukuk Bhd, a unit of Khazanah Nasional Bhd. This was the first social impact sukuk issued in Malaysia, where proceeds from the RM1 billion SRI sukuk programme were to be utilised for education purposes (trust schools). In July 2017, the world's first green SRI sukuk of RM250.0 million was issued in Malaysia to finance a 50 megawatt solar project.

To encourage the issuances of SRI sukuk, several incentives are provided. These include income tax deduction on the issuance costs of SRI sukuk and a RM6.0 million Green SRI Sukuk Grant Scheme, which is tax exempted[29], established by the SC to offset the external review cost incurred by the issuers. As at September 2019, cumulatively, there have been seven issuances of green SRI sukuk and one issuance of a social impact SRI sukuk, with the total issuance amounting to RM3.5 billion.

Through the ASEAN Capital Markets Forum (ACMF)[30], the SC also plays a significant role in the development of sustainable finance in the region as the Co-Chair of the ACMF's Sustainable Finance Working Group[31]. The ACMF has introduced the *ASEAN Green Bond Standards* (ASEAN GBS) in 2017, followed by *ASEAN Social Bond Standards* (ASEAN SBS) and *ASEAN Sustainability Bond Standards* (ASEAN SUS) in 2018. These were intended to help create a sustainable asset class, particularly towards meeting the region's infrastructure and social development financing needs. Developed based on ICMA's GBP, *Social Bond Principles* (SBP) and *Sustainable Bond Guidelines* (SBG), the ACMF standards are tailored to the ASEAN's financing needs. The inaugural ASEAN green bond, which was dually recognised as a green SRI sukuk, was issued in Malaysia in 2017 to finance the construction of a green building.[32]

---

29 The income tax deduction on issuance costs of SRI Sukuk first provided from the Year of Assessment (YA) 2016 to YA 2020 and extended for three years from YA 2021 to YA 2023. The tax exemption on the Green SRI Sukuk Grant Scheme is provided for grant applications received by the SC from 1 January 2018 to 31 December 2020.

30 ACMF was established in 2004 under the auspices of the ASEAN Finance Ministers Meeting. Its primary responsibility is to develop and implement capital market integration initiatives in ASEAN.

31 The ACMF's Sustainable Finance Working Group is co-chaired by the SC and Securities and Exchange Commission Philippines.

32 The Warisan Merdeka Tower is a green building that will be the third tallest building in the world upon completion.

As at September 2019, the cumulative issuance for ASEAN green bonds and ASEAN sustainability bonds amounts to US$3.1 billion (RM12.8 billion), out of which almost 20% of the issuances were from Malaysia (by issuance amount). In addition, Indonesia became the first country to issue a sovereign green sukuk amounting to US$1.3 billion (RM5.1 billion) in 2018, based on its national green bond and green sukuk framework. This issuance was also aligned with the GBP and ASEAN GBS.

On the international front, the SC's leadership in sustainable finance is reflected in its involvement as co-chair of the International Organization of Securities Commissions' (IOSCO) Growth and Emerging Markets Committee Working Group on Sustainable Finance, together with the National Securities Commission of Argentina. The Working Group developed a report on *Sustainable Finance in Emerging Markets and the Role of Securities Regulators*, which was published in June 2019. In addition, the SC is a member of the IOSCO Sustainable Finance Network, which encourages the exchange of experiences and sharing of regulatory development among IOSCO members in the area.

To provide more visibility and profiling of ESG-compliant companies, Bursa Malaysia launched the FTSE4Good Bursa Malaysia Index for the Malaysian market in December 2014. Companies that meet a variety of the ESG inclusion criteria are eligible to be included. The criteria are consistent with the global ESG model that FTSE has developed, and it draws strongly from the leading global disclosure frameworks such as the Global Reporting Initiative and Carbon Disclosure Project. As at 30 September 2019, there are 71 constituents of the Index, with a market capitalisation of RM510.4 billion[33].

Another significant development in the SRI market was the introduction of the *Guidelines on Sustainable and Responsible Investment Funds* (Guidelines on SRI Funds) in late 2017 to facilitate and encourage greater growth of SRI funds in Malaysia. Although Islamic funds are widely considered part of the SRI universe, the issuance of the Guidelines on SRI Funds provides opportunities for greater alignment of Islamic funds with SRI. The Guidelines on SRI Funds is aimed at widening the range of SRI products in the market and attracting more investors to the SRI segment, which are instrumental in developing and branding Malaysia as a regional SRI centre.

---

33 FTSE Russel, 2019, FTSE4Good Bursa Malaysia Index.

The new *Malaysian Code on Corporate Governance* (MCCG) issued in April 2017 further enhances the ecosystem for SRI in Malaysia. Greater internalisation of a corporate governance culture as envisaged under the MCCG supports the sustainability agenda through more responsible and proactive practices. The MCCG emphasises that the board should ensure the company supports long-term value creation and includes strategies on environmental considerations underpinning sustainability. In addition, the Comprehend, Apply and Report (CARE) approach that entails a shift from 'comply or explain' to 'apply or explain an alternative'

Notable SRI Initiatives in the Malaysian Capital Market

2018

- Establishment of **RM6 million Green SRI Sukuk Grant Scheme** which is **tax exempted**
- Issuance of **ASEAN SBS and ASEAN SUS**

2017

- Launch of the SC's ***Islamic Fund and Wealth Management Blueprint***
- Issuance of **social impact sukuk** by Khazanah (2nd tranche) with retail portion
- Issuance of **world's first green sukuk under SRI Sukuk Framework**
- Issuance of the **ASEAN GBS** followed by **inaugural ASEAN Green Bond**
- Issuance of the SC's **Guidelines on SRI Funds**
- **Tax incentive for SRI funds** for three years from YA 2018 to YA 2020, and extended for another three years from YA 2021 to YA 2023 (2020 Budget)
- Launch of the SC's revised **MCCG**

2016

- **Tax incentive for SRI Sukuk issuers** for five years from YA 2016 to YA 2020, and extended for another three years from YA 2021 to YA 2023 (2020 Budget)

2015

- Inaugural issuance of **social impact sukuk** under SRI Sukuk Framework by Khazanah
- Introduction of **Sustainability Reporting** through *Bursa Malaysia Listing Requirements*

2014

- Issuance of the SC's **SRI Sukuk Framework**
- Launch of **FTSE4Good Bursa Malaysia Index**
- Issuance of **MCII**

aims to encourage companies to put more thought and consideration when adopting and reporting their corporate governance practices, elevating it beyond a mere box-ticking exercise.

Management of material economic, environmental, social risks and opportunities as well as enhancement of sustainability disclosures by listed issuers are crucial to sustainable development. To address this, Bursa Malaysia in October 2015 launched a Sustainability Framework, comprising amendments to the Listing Requirements and the issuance of a *Sustainability Reporting Guide and Toolkit*. This has enhanced the sustainability practices, adding clarity from reporting on corporate social responsibility activities to sustainability.[34]

To reinforce investors' commitment in adopting ESG practices and goals for the long term within their decision-making process, the SC and the Minority Shareholder Watch Group (MSWG) launched the *Malaysian Code for Institutional Investors* (MCII) in 2014, a code and set of best practices collectively developed by Malaysia's largest institutional investors. Commencing from 2016, signatories to MCII are expected to report annually their application of the MCII's principles on their websites, or in their annual reports and other publicly accessible documents. As at September 2019, there are 22 signatories to the MCII.[35]

To encourage and facilitate further growth of the SRI segment, Malaysia needs to ensure the orientation of its policies are in line with international practices and global developments, particularly as policymakers, regulators and market players are adopting policies towards sustainable investments.

The development of the SRI Roadmap will therefore be pivotal in charting the strategic directions and identifying recommendations in accelerating the growth of SRI to further strengthen Malaysia's value proposition as a regional centre for SRI.

[34] This was introduced in a phased approach, starting with large market capitalisation companies listed on the Main Market. Currently, all listed companies on the Main Market and ACE market are required to disclose their sustainability statements for annual reports issued for the financial year ending on or after 31 December 2018.

[35] The total AUM of the 22 signatories to the MCII exceeds RM1.8 trillion as at June 2019 (SC estimates).

CHAPTER 2

STRATEGIES AND RECOMMENDATIONS TO DEVELOP MALAYSIA AS A REGIONAL SRI CENTRE

Since its introduction in 2014, the 5*i*-Strategy has been the overarching framework for the development of the SRI ecosystem and various related initiatives introduced in the Malaysian capital market. The recommendations of the SRI Roadmap, therefore, are aimed at developing and enhancing each component of the 5*i*-Strategy over the next five years.

2.1 WIDENING THE RANGE OF SRI INSTRUMENTS

2.1.1 Promote alignment to international standards and principles

Following the introduction of the first green bond in 2007, the global sustainable investment market has seen other thematic bonds such as social and sustainability bonds gaining traction over the last decade in funding sustainable development needs. One of the important factors that led to the creation of the green, social and sustainability bond markets is the introduction of ICMA's GBP, SBP and SBG which have been widely accepted as the underlying framework for the issuances of these bonds.

In the global green bond market, 320 issuers from 44 countries have issued green bonds which are aligned with the GBP as at April 2019[1]. While the GBP serves as the main guiding principles for the issuance of green bonds, many jurisdictions have developed their own national green bond framework that are aligned or based on the GBP. An example is the ASEAN GBS introduced by the ACMF, which are aligned with the GBP to ensure greater harmonisation with the international principles. The Final Report issued in 2018 by the European Union High-Level Expert Group on Sustainable Finance (EU HLEG)[2], identified the development of official European sustainable finance standards, starting with the development of an official *EU Green Bond Standard.*

With the issuance of the world's first green sukuk under the SC's SRI Sukuk Framework in 2017, and Malaysia as the leader in the global sukuk market with a 49% share of global sukuk outstanding as at end August 2019,[3] there is significant potential to be unlocked through the internationalisation of the SRI sukuk market. The 2016 report by the UN's High-Level Panel on Humanitarian Financing, estimated the global humanitarian financing gap

1 CBI Database.
2 EU HLEG was established under the European Commission (EC) to help develop an overarching and comprehensive EU Roadmap on Sustainable Finance.
3 Malaysia International Islamic Financial Centre (MIFC) estimates.

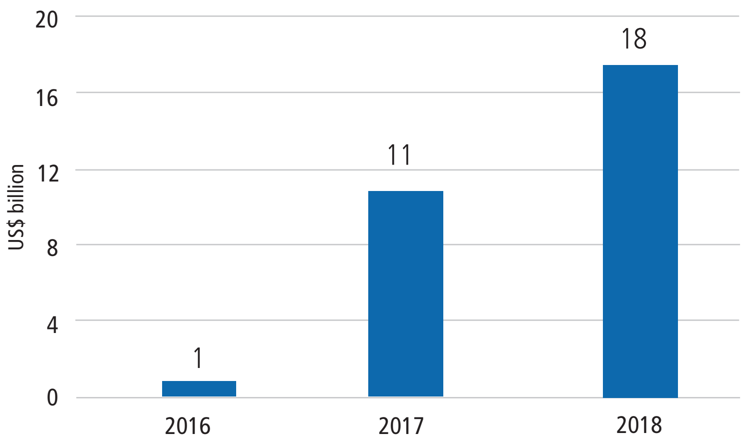
to be US$15.5 billion (RM67.4 billion) per annum and found that Muslim countries will be the most affected from humanitarian crises. In addition, given the importance of ensuring sustainable development and addressing the impact of climate change in its Member Countries, the Organization of Islamic Cooperation (OIC), has adopted the 2030 Agenda for Sustainable Development and the SDGs at the OIC's 13th Islamic Summit in 2016.

As such, to increase the profiling and branding of the SRI Sukuk Framework internationally, and thereby strengthening the role of Islamic finance in funding sustainable development needs, the alignment of the SRI Sukuk Framework to international standards and principles will be further enhanced. This is aimed at attracting international issuances of SRI sukuk to meet Shariah-compliant sustainable financing needs and encourage the issuances of more innovative SRI-themed sukuk under the SRI Sukuk Framework.

2.1.2 Encourage issuances of sovereign green, social or sustainability sukuk

Since the issuance of the world's first sovereign green bond of US$850.0 million (RM3.5 billion) in 2016 by Poland under its national Green Bond Framework, the total size of sovereign green bond issuances as of end 2018 amounted to US$17.5 billion (RM71.8 billion),[4] which demonstrates the various governments' commitment in funding climate-friendly projects to realise the Paris Agreement's agenda. Several developing countries have also issued sovereign green bonds such as Fiji's US$50.0 million (RM202.4 million) and Nigeria's US$29.7 million (RM122.7 million) issuances in 2017. In 2018, Indonesia became the first country to issue a sovereign green sukuk amounting to US$1.3 billion (RM5.1 billion) based on its national green sukuk framework.

Chart 1
Total Annual Issuance of Sovereign Green Bonds



Source: Green Bonds: The State of the Market 2018, CBI

4 CBI, *Green Bonds: The State of the Market,* 2018.

As Malaysia is committed towards meeting the SDGs and Paris Agreement targets, future developmental spending, which is projected to be RM45.0 billion from 2021 to 2025,[5] will take into account the potential impact of those investments to the economy, society and environment. The Shared Prosperity Vision 2030 (SPV30) blueprint[6], introduced by the Malaysian government, will be instrumental in shaping future Malaysia Plans to embody the essence of the SDGs.

Given the national policies towards sustainable development and the amount of financing required, sovereign green, social and sustainability bonds as well as sukuk represent attractive funding options which enable the mobilisation of private sector financing towards sustainable infrastructure projects. The issuance of sovereign green, social and sustainability bonds and sukuk by the government will provide greater signalling of the Malaysian government's commitment towards the sustainable agenda.

Having a framework for the issuance of green, social or sustainability bonds and sukuk is key to encourage transparency of the issuance process, safeguard the utilisation of proceeds towards designated eligible projects and ensure accountability of the issuers. To this end, the issuances of sovereign green bonds are either based on the respective national green bond framework, or the globally accepted GBP. As such, the SC's SRI Sukuk Framework can be leveraged as an underlying framework for the issuance of sovereign green, social and sustainability sukuk. The use of the national framework does not preclude the issuer from disclosing its compliance with other global standards as a dual or even multiple-labelled bond will appeal to and attract a larger investor base.

2.1.3 Develop SRI taxonomy for the capital market

As sustainable investments develop globally, market practitioners and investors are demanding for more clarity and guidance to identify sustainable investment assets. Having a common taxonomy will enhance the standardisation and comparability of sustainable investments assets, which in turn will further accelerate the development of this asset class.

In a report published in March 2018[7], the EC identified the establishment of a European Union (EU) classification system for sustainable activities, i.e. EU taxonomy as one of its action plans. Subsequently, the EU Technical Expert Group on Sustainable Finance, tasked to undertake the development of the EU taxonomy, published its first report in June 2019, which sets out the basis of the EU taxonomy, including the technical screening criteria for activities and sectors that can make a substantial contribution to climate change mitigation,

---

5 Keynote Address by the Minister of Economic Affairs, 2019, (Kick-off Conference of the Twelfth Malaysian Plan, 2021 – 2025).

6 On 5 October 2019, the Prime Minister launched the government's new vision SPV2030, a blueprint for the direction of the country in the next decade. It aims to make Malaysia, a country which is developing sustainably with fair and equitable distribution of economy, with equitable growth at all levels of income, ethnics, regions and supply chains by 2030.

7 EC, *Action Plan: Financing Sustainable Growth*.

methodology and guidance. Following the EU's direction, several jurisdictions including Bangladesh and China have also introduced their respective taxonomies of activities that are environmentally sustainable.

Given the global developments in this area, an evaluation of how such a classification system could be implemented for the Malaysian market is required. A taxonomy that is aligned to global standards creates a uniform and harmonised classification system that serves as a useful reference point for issuers, market practitioners, investors and other stakeholders both domestic and international. Such common classifications are essential in avoiding market fragmentation and green washing.

With the formation of the Joint Committee on Climate Change (JC3), the SC and Bank Negara Malaysia (BNM) as JC3 co-chairs will explore co-ordinated solutions to address issues in building climate resilience, including providing greater harmonisation of classifications through the development of a taxonomy that can be universally applied in order to provide better clarity in the capital market, banking and insurance sectors.

2.1.4 Facilitate the issuance of more SRI products

While the introduction of the SRI Sukuk Framework and the Guidelines on SRI Funds provide regulatory guidance to the market in issuing SRI-related products, efforts should be made to expand the breadth and depth of SRI products in the Malaysian capital market. The creation of a wider range of SRI products will attract the buy-side, both institutional and retail investors looking to invest with a purpose.

The Malaysian bond and sukuk market continues to mature over the years with RM1.4 trillion of bond and sukuk outstanding as at 2018. Therefore, the industry is encouraged to develop more innovative SRI sukuk and bond structures to capitalise on the current stage of growth of the Malaysian bond and sukuk market, taking it to the next level. Instruments that could be considered include those utilising structures such as securitisation and pooled finance.

In the equity space, while the FTSE4Good Bursa Malaysia Index provides greater profiling of ESG-compliant securities, the creation of more sustainability indices such as a Shariah-

“...the industry is encouraged to develop more innovative SRI sukuk and bond structures to capitalise on the current stage of growth of the Malaysian bond and sukuk market, taking it to the next level.”

compliant SRI index and a green index will provide more investment choices for investors, including fund managers and asset owners. In addition, a variety of SRI fund products such as SRI exchange-traded funds, *waqf* funds and green real estate investment trusts (REITs) will increase the range of SRI fund product offerings in the Malaysian capital market.

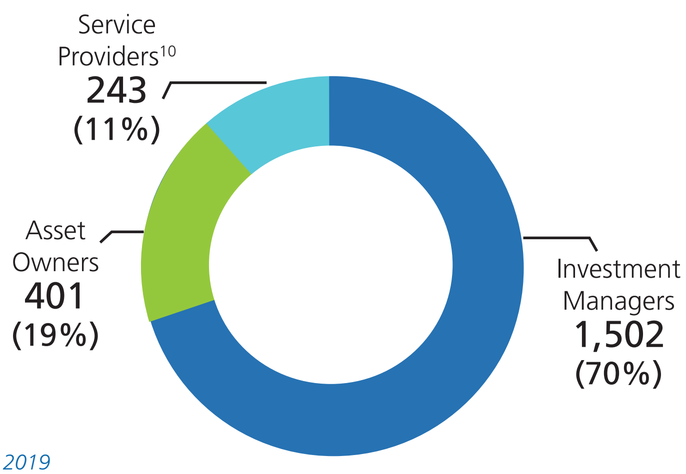
2.2 INCREASING SRI INVESTOR BASE

2.2.1 Enhance the role of government-linked investment companies and institutional investors in SRI

Government-linked investment companies (GLICs) and institutional investors (IIs) have been a strong proponent of sustainable investments as demonstrated by their commitments towards this agenda. Globally, 401 asset owners have signed up to the PRI, which represent 19% of the total signatories who cumulatively command US$81.7 trillion (RM337.4 trillion) AUM as at 2018.[8] The majority of IIs globally believe sustainability is set out to play a more important role within their portfolios over the next five years,[9] and consider ESG compliance as part of their fiduciary duties.

While most asset owners and pension funds in the European region have been advocating sustainable investments and driving the sustainability behaviours of the investee companies, GLICs and IIs in Malaysia are now beginning to place greater importance in this area, given

Chart 2
PRI Signatories Category (2018)



Source: PRI 2019

---

8 PRI Database.
9 *Schroders Institutional Investor Study 2018.*
10 Service providers include index providers, rating agencies, external reviewers, investment consultants and banks.

the long-term value and impact of sustainable investments. This is reflected where national pension funds such as the Employees Provident Fund[11], Retirement Fund (Incorporated)[12] and the sovereign wealth fund, Khazanah Nasional Bhd have become signatories to the PRI. The shift by these major IIs towards sustainable investments will encourage other GLICs and IIs to also commit to this agenda and become signatories to the PRI.

The MCII launched jointly by the SC and the MSWG in 2014, sets out broad principles of effective stewardship by IIs such as disclosures of their stewardship policies, monitoring and engagement with investee companies and managing conflict of interests. In order to foster stronger sustainable investment culture among IIs, the MCII should emphasise the integration of ESG considerations in investment and divestment decisions as well as disclosures. In line with this, the Institutional Investors Council can then play a more proactive role in advocating sustainable investments among its members.

As sustainable investments may still be at a nascent stage for some of the GLICs and IIs in Malaysia, outsourcing of SRI mandate to experienced external fund managers could be considered. This will allow GLICs and IIs to leverage the external fund managers' SRI expertise, particularly fund managers who are signatories to the PRI. Over time, this will enable GLICs and IIs to accumulate sufficient knowledge and capabilities, thereby strengthening the SRI ecosystem in Malaysia through their position of influence. In addition, a dedicated allocation of SRI mandates by the GLICs and IIs will further encourage more external and licensed fund managers to build up their SRI capabilities.

2.2.2 Attract international investors

Demand for sustainable investments from global investors continues to grow with certain regions recording stronger growth as compared to others. For example, sustainable investing assets in Japan have increased from US$8.0 billion in 2014 (RM33.0 billion) to US$2.2 trillion (RM9.1 trillion) in 2018, while Europe recorded an increase from US$11.1 trillion (RM45.8 trillion) in 2014 to US$13.8 trillion (RM57.0 trillion) in 2018.[13] However, in terms of market share, Europe still commands 49% of the global sustainable investing assets in 2018.[14]

Asset owners such as pension funds and sovereign wealth funds are significant drivers of sustainable investments and have demonstrated their commitment by becoming PRI signatories. By adopting the principles, the PRI signatories contribute towards developing more sustainable and responsible practices. Although a majority of the signatories are based in Europe and US, in 2018, Asia recorded a 29% increase in the number of signatories over the previous year.[15]

---

11 Kumpulan Wang Simpanan Pekerja.
12 Kumpulan Wang Persaraan (Diperbadankan).
13 GSIA, *Global Sustainable Investment Review 2018.*
14 *Ibid*.
15 PRI, 2018, *Annual Report 2018.*

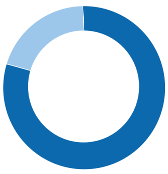
Although Malaysia's efforts to promote SRI has been progressing steadily over the years, and while we continue to build scale on the supply side, initiatives should be concentrated on attracting investors. This could be through direct investments in Malaysia's SRI market as well as the intermediation of SRI mandates through fund managers in Malaysia. Strategic dialogues with identified markets and roundtable engagements with targeted investor groups will provide an effective platform to foster closer interaction, attracting them to the Malaysian SRI market.

Thought leadership events provide excellent opportunities to increase the profiling of Malaysia as a regional SRI centre and showcase its early successes in this segment. The SC has been active in organising various international and regional SRI-related conferences as well as producing publications of SRI articles together with identified partners such as the Oxford Centre for Islamic Studies (OCIS), World Bank Group, IOSCO, ICMA, CBI and PRI. Industry players will also be encouraged to play their part through various joint initiatives with the SC such as conducting roadshows. These contribute towards greater promotion of Malaysia at both regional and international levels and over time attracting more SRI investments to the country.

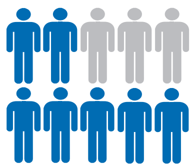
2.2.3 Encourage SRI investments by retail investors

Findings from international studies have indicated that there is increasing interest and demand for sustainable investments from retail investors globally.

Global Retail Investors' Interests in Sustainable Investments

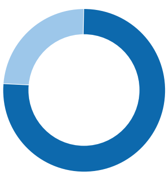


78%
Investors believe **sustainable investing** is more important to them now than five years ago

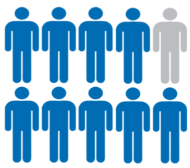


70%
Millennials have **increased their investments** in sustainable funds

Source: Schroders' Global Perspectives on Sustainable Investing 2017 Report



75%
Respondents **showing interest** in sustainable investing



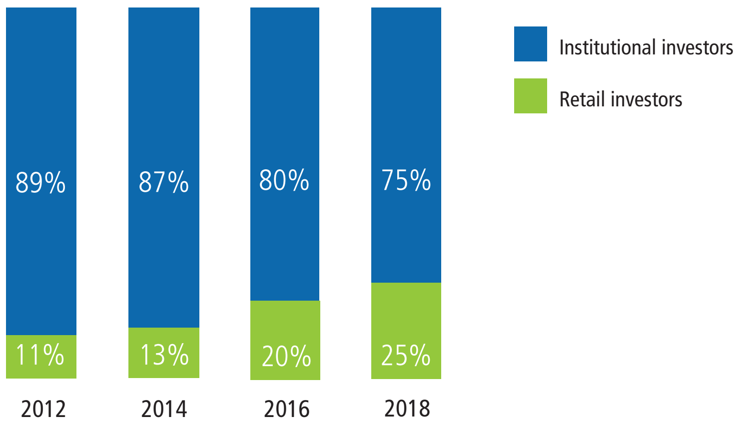
86%
Millennials **showing interest** in sustainable investing

Source: Morgan Stanley's Sustainable Signals Individual Investor Survey 2017

The *2018 Global Sustainable Investment Review* by GSIA presented that although IIs tend to dominate the investment size, interest by retail investors in sustainable investing has been steadily growing since 2012, when retail investors held 11% and IIs held 89% of sustainable assets then. In 2018, the sustainable assets held by retail investors increased to 25%, while IIs held 75%.

Chart 3

Global Shares of Retail and Institutional Sustainable Investing Assets 2012-2018



Source: Global Sustainable Investment Review 2012 – 2018, GSIA

Among the Malaysian populace, sustainable investment is still nascent. As such, greater understanding and awareness of SRI products need to be increased among the retail segment, particularly the significance and long-term impact of sustainable investing. This will be done through existing touchpoints of the investor empowerment chain from engagements between capital market professionals with their retail clients to educational events and content provided by regulators, and other relevant organisations including non-governmental organisations (NGOs). Enhancing the skills of professionals and information providers on SRI matters is key to effectively educate the investing public.

Retail investors, when equipped with the relevant knowledge pertaining to sustainable investments, are then able to embed underlying social and environmental values within their investment decisions, thereby motivating them to consider factors beyond just financial returns when formulating their investment strategies.

2.2.4 Enhance investment managers' SRI intermediation capabilities

Globally, more investment managers are committed towards sustainable investments, as evident from 1,502 investment managers that made up 70% of PRI signatories in 2018.[16] However, only five of the global investment managers who are PRI signatories have presence in Malaysia and very few Malaysian fund managers[17] are PRI signatories as at October 2019.

As the demand for SRI grows beyond IIs to a broader group of investors, investment managers need to enhance their SRI intermediation capabilities as they play a crucial role in connecting investors with SRI products. Furthermore, to ensure competitiveness vis-à-vis other regions and other international investment managers, Malaysian-based investment managers need to provide value-added SRI services such as incorporating big data and artificial intelligence in the SRI screening for their clients.

In addition, fund managers need to design suitable SRI products to cater to the investment needs of investors. The SC's definition and strategy with regard to SRI covers all related segments, addressing ESG and ethical concerns, thereby also appealing to Muslim investors, other faith-based funds and philanthropists as well. Towards this end, the development of a facilitative and conducive SRI ecosystem will support more product innovation and strengthen the ability of investment managers to offer a wide range of services to meet the demand from various investors.

It is therefore important for investment managers to be equipped with the necessary skills and technology that will enhance their SRI intermediation capabilities and increase intermediation efficiencies, taking into account the ESG risks of the investments as well as to their own operations. Such enhanced capabilities will provide opportunities for investment managers to capitalise on the investors' preferences or objectives that seek to achieve social and environmental good in addition to financial returns, including to manage the relevant IIs' SRI mandates. Foreign fund managers should leverage their group sustainability policies and global network to strengthen the SRI expertise of their Malaysian office. Meanwhile, domestic investment managers need to enhance their SRI intermediation capabilities by collaborating with SRI service providers, developing in-house SRI capabilities, or investing in new technologies and securing expertise on SRI.

"As the demand for SRI grows beyond IIs to a broader group of investors, investment managers need to enhance their SRI intermediation capabilities as they play a crucial role in connecting investors with SRI products."

[16] PRI Database.
[17] These include BIMB Investment Management Bhd and Singular Asset Management Sdn Bhd.

2.3 BUILDING A STRONG SRI ISSUER BASE

2.3.1 Widen access to SRI through alternative funding avenues

Micro, small and medium-sized enterprises (MSMEs) contribute significantly to the growth, employment, innovation and social cohesion in an economy, and have the potential to play an important role in the transition to a low-carbon, circular and green economy. However, access to finance remains a continuing challenge for the MSME sector as a whole, including for green and social enterprises.

The United Nations Environment Programme (UNEP) has identified that the green and sustainable finance agenda for MSMEs essentially comprises two core priorities[18]

Enabling finance
for conventional MSMEs to enhance their sustainability performance

Allocating finance
for MSMEs that are dedicated on generating sales of sustainability-related goods and services

Currently, green companies or projects as well as social enterprises in Malaysia continue to rely on government grants and bank financing as their main source of funding. Specifically, for green technology companies or projects, the government has introduced the Green Technology Financing Scheme (GTFS), with the first phase of RM3.5 billion financing available through participating financial institutions from 2010 to 2017, followed by the second phase of GTFS with RM2.0 billion from 2019 to 2020.

Given the various stages of these companies and their financing needs, alternative capital market funding avenues such as venture capital (VC), private equity (PE), equity crowdfunding (ECF) and peer-to-peer (P2P) financing platforms can channel the required funding to MSMEs, and provide at-risk capital for many of these young and innovative companies. Suitable VC and PE investors are able to inject their expertise together with appropriate risk capital into MSMEs to help them grow, improve and achieve strong financial returns, which in turn will benefit the development of promising nascent technologies.

[18] United Nations Environment Programme, 2017. *Mobilising Sustainable Finance for Small and Medium-Sized Enterprises.*

"The emergence of financial technology has given rise to the use of ECF and P2P financing platforms to democratise financing for MSMEs, including companies and projects that contribute towards making a positive impact to the environment and social community."

The emergence of financial technology has given rise to the use of ECF and P2P financing platforms to democratise financing for MSMEs, including companies and projects that contribute towards making a positive impact to the environment and social community. These platforms allow funders to participate in sustainable investments, providing opportunities for project developers to tap into the wealth of a new pool of retail investors. As at 2018, Malaysia has seen several green and social companies successfully raise funds through the ECF platforms with funding size ranging from RM0.3 million to up to RM1.5 million. While the amount is relatively small, there is significant potential for this segment to grow. However, concerted efforts are required to increase greater awareness of alternative capital market funding avenues among MSMEs.

2.3.2 Support the development of an initial public offering pipeline for green and social impact companies

The conventional funding route of tapping into the capital market via an offering of equity becomes a viable prospect as green and social impact companies seek to expand and require more substantial sources of financing. In addition, flotation of the company's shares as a viable exit strategy for VC and PE investors increases the attractiveness of investing in green and social impact MSMEs.

However, there are challenges that need to be addressed to facilitate the listing of green companies. Among them is the difficulty in meeting existing thresholds in the initial public offering (IPO) review and listing requirements for the Bursa Malaysia's Main Market, given the uniqueness of green industries and their business models. Furthermore, the ambiguity of what 'green' means and the difficulty in assessing the continuity of the company's greenness throughout its business life cycle poses a challenge in maintaining a green listing status.

Nonetheless, several companies with green business focus have been listed on Bursa Malaysia's Main, ACE and LEAP Markets, and it is estimated that there are 7,257 social enterprises[19] among the 907,065 SMEs[20] in the country. As such, efforts should be made to encourage suitable green and social impact companies to progress through the capital market towards an IPO, thereby developing a pipeline for the eventual listing of such companies.

Towards this end, the capital market intermediaries play a significant role in identifying and advising such companies in the IPO process. This will not only widen the financing options through the capital market for these companies, but in turn, will create a natural pipeline for them to be included in the FTSE4Good Bursa Malaysia Index. Thus, the exchange needs to closely collaborate with other sectoral regulators and agencies in creating greater awareness on IPO opportunities among these companies.

2.3.3 Enhance the roles of financial institutions in SRI

The role of financial institutions is integral to the growth of sustainable investments, particularly in the green bond market, where they continue to lead the market. This is evidenced by the fact that green bond issuances by financial institutions globally passed the US$100.0 billion mark in 2018, with 127 institutions having issued green bonds since 2012.[21] In addition to conventional financial institutions, development financial institutions (DFIs) are also natural issuers of social and sustainability bonds given their objectives of fundraising towards projects that contribute to socio-economic development.

In 2018, HSBC Amanah Malaysia Bhd issued the world's first SDG Sukuk with an issuance size of RM500.0 million to support projects that contribute towards seven selected SDGs. On October 2019, CIMB Bank Bhd also issued an SDG bond which is recognised as an ASEAN Sustainability Bond, worth US$680.0 million (RM2.9 billion) to fund projects related to the SDGs. Following the increasing issuances of green, social and sustainability bonds by financial institutions globally, there is a need to ensure a facilitative framework for the issuance of SRI sukuk by financial institutions. As issuers typically tap into the SRI sukuk and green, social and sustainability bonds market to finance projects of at least RM200.0 million, financial institutions can act as aggregators between small borrowers and the capital market.

Financial institutions also play several roles such as bond and sukuk structuring agents as well as underwriters and principal advisers for IPOs. In order for financial institutions to adequately execute these roles in relation to the SRI products and services, their expertise and capabilities in this segment need to be improved.

---

19 British Council, 2018, *The State of Social Enterprise in Malaysia.*
20 Department of Statistics Malaysia, 2019, *Small and Medium Enterprises (SMEs) Performance 2018.*
21 CBI, *Green Bonds: The State of the Market 2018*.

2.3.4 Collaborate with multilateral development institutions

Multilateral development institutions play a significant role in mobilising finance towards the SDGs and Paris Agreement. In 2018, climate financing by the world's largest multilateral development banks (MDBs) in developing countries and emerging economies rose to US$43.1 billion (RM178.3 billion), an increase of 22% from US$35.2 billion (RM145.5 billion) in 2017.[22] Cumulatively, these MDBs have committed US$237.0 billion (RM978.8 billion) in climate finance since 2011 in developing and emerging economies.[23] The MDBs reported US$68.1 billion (RM281.3 billion) in co-investments from the public and private sector, thus raising the total climate finance in 2018 to US$111.2 billion (RM459.3 billion).[24] Where social bonds are concerned, several MDBs have issued series of bonds to fund various social initiatives as highlighted below:

Social Bonds: Funding by MDBs

Inter-American Development Bank		International Finance Corporation		African Development Bank	
2014	US$500.0 mil (RM2.0 bil)	2017	US$500.0 mil (RM2.0 bil)	2017	US$578.0 mil (RM2.3 bil)
2018	US$1.5 bil (RM6.0 bil)	2018	US$221.0 bil (RM914.1 bil)		

Source: Impact Invest Lab, The Social Bond Market: Towards A New Asset Class

In 2015, these MDBs, together with the International Development Finance Club (IDFC)[25] agreed on a set of Common Principles for climate change mitigation and adaptation financing. Collectively, the MDBs command total assets of US$1.5 trillion (RM6.2 trillion), while the IDFC members hold total assets of US$3.8 trillion[26] (RM15.7 trillion). As the focus spending areas of MDBs and IDFC members are aligned with the SDGs, there are more opportunities to be explored.

MDBs and DFIs can be the intermediaries to bridge public and private sector financing towards sustainable development needs, given their clear mandates in supporting development-related projects. In addition, MDBs have the expertise and track record in structuring a wide range of financial instruments and managing projects as well as robust risk management processes.

---

22 *Joint Report on Multilateral Development Banks' Climate Finance, 2018*. This report is prepared by a group of MDBs, composed of the African Development Bank, Asian Development Bank, European Bank for Reconstruction and Development, European Investment Bank, Inter-American Development Bank Group, Islamic Development Bank and World Bank Group.
23 *Ibid.*
24 *Ibid.*
25 Founded in 2010, IDFC comprises 24 development bank members, representing a diverse array of development finance institutions that as a group is particularly well suited to play a leadership role on the SDGs.
26 Center for Global Development, 2018, *The IFDC and the SDGs Impact, Opportunities, and Challenges*.

Given their mandate and extensive capabilities in development finance, MDBs and DFIs can play important roles to support investments that contribute towards sustainable development through financing solutions such as co-financing, credit enhancements and risk mitigation instruments. Notably, MDBs and DFIs are issuers of green, social and sustainability bonds. As there is already a facilitative ecosystem for the issuance of green, social and sustainability bonds, Malaysia is well positioned to be the preferred jurisdiction for the issuances of such bonds, where proceeds can be utilised for the ASEAN region.

MDBs and DFIs contribute in accelerating the development of sustainable investment through research and capacity building as key knowledge partners. In 2017, the SC had established a Technical Working Group with BNM and World Bank Malaysia to drive awareness programmes, stakeholder engagements and technical assistance on green SRI sukuk. At the ASEAN level, the Asian Development Bank (ADB) has been a valued partner of the ACMF since the latter's establishment in 2004. The ADB extends technical advice via its officials and experts as well as Technical Assistance (TA) programmes to fund the ACMF's initiatives, which include the introduction of the ASEAN GBS, ASEAN SBS and ASEAN SUS.

2.4 INSTILLING STRONG INTERNAL GOVERNANCE CULTURE

2.4.1 Strengthen sustainability disclosures of PLCs

Investors are increasingly demanding that companies articulate a long-term value creation strategy that outlines not just growth opportunities but also related risks. Sustainability matters are recognised as critical in the evaluation of a company's full risk profile and how prepared it is for the future. Sustainability reporting enables a company to be more transparent about its risks, mitigation measures as well as opportunities.

In recognition of this, several measures have been undertaken to facilitate sustainability disclosures. For example, in 2018, the Global Reporting Initiative (GRI) and the UN Global Compact released the *Practical Guide on Integrating SDGs into Corporate Reporting* (Practical Guide),[27] that discourages corporates from selecting the SDGs and related targets based merely on ease of reporting, and suggests the reporting of both positive and negative impacts on the SDGs. Many regulators have introduced sustainability reporting frameworks for listed companies, some of which have used the GRI as a benchmark. In addition, the Financial Stability Board (FSB) has identified the need for better information to support informed investment and lending decisions as well as improve understanding and analysis of climate-related risks and opportunities.

---

[27] The Practical Guide is built on the *Ten Principles of the UN Global Compact, UN Guiding Principles on Business and Human Rights and GRI Sustainability Reporting Standards.*

In 2017, a report by the FSB Task Force on Climate-Related Financial Disclosures[28] (TCFD), outlined recommendations to help address climate-related disclosure challenges through four key areas: (i) Governance; (ii) Strategy; (iii) Risk Management; and (iv) Metrics and Targets. As at September 2019, TCFD has 867 supporters, including regulators, companies and other organisations that represent a broad range of sectors. Both the SC and Bursa Malaysia are TCFD supporters since 2018, and Bursa Malaysia has recently incorporated the TCFD recommendations into the 2018 revision of its *Sustainability Reporting Guide*.

TCFD Recommendations

GOVERNANCE	STRATEGY	RISK MANAGEMENT	METRICS AND TARGETS
The organisation's governance around climate-related risks and opportunities	Actual and potential impacts of climate-related risks and opportunities on the organisation's businesses, strategy and financial planning	The processes used by the organisation to identify, assess and manage climate related risks	Used to assess and manage relevant climate-related risks and opportunities

Source: TCFD, Final Report: Recommendations of the TCFD

To strengthen sustainability disclosures of listed companies in Malaysia, Bursa Malaysia in collaboration with relevant stakeholders must continue to enhance the capacity of listed companies to provide quality disclosures. This includes advocating for listed companies on Bursa Malaysia to adopt recognised sustainability reporting frameworks (e.g. GRI, TCFD recommendations) to strengthen comparability and rigour of the sustainability information and data presented. In addition, the SC is also working together with Bursa Malaysia to enhance the Sustainability Reporting Framework by identifying critical economic, environmental and social (EES) indicators to be included in the listed companies' annual reports.

Periodic reviews on the quality of disclosures should also be undertaken to address any gaps. For the review to be robust, it should take into consideration sector-specific disclosure expectations.[29]

Continuous dialogue is also critical to understand the investors' expectations in relation to disclosure, and address any communication gap between investors and companies on sustainability matters.

---

[28] Following the directive by G20 Finance Ministers and Central Bank Governors, the FSB established the TCFD to develop recommendations for more effective climate-related disclosures.

[29] In November 2018, the Sustainability Accounting Standards Board released standards for 77 specific industries.

2.4.2 Promote the adoption of sustainable business practices including disclosure among small and medium enterprises

Small and medium enterprises (SMEs) play a key role in national economies around the world. Globally, SMEs comprise up to 90% of all businesses, 63% of total employment and up to 35% of the GDP in emerging economies.[30] SMEs account for 99% of business establishments in Malaysia, contributing to Malaysia's GDP at 38% in 2018, up from 37% in 2016.[31] Given their significance, SMEs have an important role to play in the realisation of SDGs, which include addressing climate change and its impacts. Although the individual impact of these SMEs may be low, their aggregate impact can, in some sectors, exceed that of large companies, and in some cases can even individually cause severe impact to the environment. As such, the integration of the sustainability mindset and practices within SMEs is vital to promote more sustainable patterns of production and consumption among SMEs.

According to the UN Global Compact database, a total of 5,777 SMEs have adopted the UN Global Compact[32] as at October 2019. Despite this encouraging development, sustainability reporting among SMEs remain relatively uncommon. In 2018, SMEs accounted for only 19% of the total number of sustainability reports in the GRI Sustainability Disclosure Database.

To facilitate this, measures need to be implemented to strengthen understanding of sustainability issues among SMEs, and the ability to integrate sustainability considerations in the business operation, and manage material sustainability risks to make the necessary disclosures. This requires capacity building programmes for SMEs which includes providing them with guidance and tools to facilitate the adoption of sustainability practices.

2.4.3 Enhance board governance on sustainability including climate risks and opportunities

Given its role in addressing financial and non-financial risks and long-term value creation, good governance should intrinsically include the management of sustainability matters as well as climate risks and opportunities. Thus, boards need to address the topic of sustainability with the same rigour as other matters deliberated by them. However, according to a report by the World Economic Forum (WEF) on climate governance, boards are still struggling to address the related risks and opportunities in a holistic manner.[33]

---

30 World Trade Organization, *Levelling the Trading Field for SMEs, World Trade Report,* 2016.
31 Department of Statistics Malaysia, 2019, *Small and Medium Enterprises (SMEs) Performance 2018.*
32 UN Global Compact.
33 WEF, 2018, *How to Set Up Effective Climate Governance on Corporate Boards – Guiding Principles and Questions 2018.*

The report highlighted that the reasons for this can be broadly attributed to competing priorities, where other emerging and strategic risks e.g. industry change, technology, cybersecurity are prioritised; and boards have limited time and capacity to review and address all these strategic topics. The complexity of climate change has made it a relatively difficult risk and opportunity to manage. Companies are also under pressure to deliver short-term results, and climate change issues often extend beyond the typical business planning cycle.

In January 2019, the WEF in collaboration with PricewaterhouseCoopers (PwC) released the guiding principles for effective climate governance on corporate boards, with the goal of providing tools to increase directors' climate awareness and embed climate considerations into board structures and processes to improve navigation of risks and opportunities that climate change poses to business.

Given these challenges, it is critical to enhance the capacity of boards to provide strategic guidance and oversight of sustainability-related matters. The appropriate systems and processes are in place to manage material sustainability risks and opportunities. Thus, board members must have the appreciation and knowledge on issues that are affecting the company, to enable them to discharge their roles effectively. The awareness and understanding of the board will set the tone at the top, driving greater awareness throughout the entire company, which is critical to ensure efforts are holistic and the intended outcomes are achieved.

2.4.4 Enhance risk assessment and supervisory approach on SRI

As more capital is allocated towards sustainable investments, regulators around the world are assessing sustainability risks to the broader financial systems. The IOSCO Growth and Emerging Market Committee's report on *Sustainable Finance in Emerging Markets and the Role of Securities Regulators* recommends the need for the integration of ESG-specific issues in the overall risk assessment and governance of issuers of sustainable investment products and regulated entities.

In addition, the members of the Network for Greening the Financial System (NGFS) acknowledged that climate-related risks are a source of financial risk, and they therefore fall squarely within the mandates of the central banks and supervisors to ensure the financial system is resilient to these risks.[34] The NGFS has also identified steps that can be taken by financial regulators in integrating climate-related risks into financial stability monitoring and micro-supervision.

[34] *A Call for Action: Climate Change as a Source of Financial Risk, NGFS First Comprehensive Report*, April 2019.

> "Regulators need to develop new analytical tools to enable them to assess and identify ESG risks that could pose risks to the financial markets, as well as new supervisory approaches, including those based on forward-looking scenario analysis and stress tests."

In March 2019, the EC agreed to have new disclosure requirements aimed at strengthening and improving disclosure of information by manufacturers of financial products and financial advisors to end-investors. These new rules will provide details as to how financial market participants and financial advisors must incorporate ESG risks and opportunities in their policies, processes and procedures.

In light of these global developments, capital market regulators should also review their existing risk assessment and supervisory approach to take into account ESG risks. In the Malaysian context, the SC continues to collaborate with relevant authorities to identify potential climate-related risk areas within the financial system. Regulators need to develop new analytical tools to enable them to assess and identify ESG risks that could pose risks to the financial markets, as well as new supervisory approaches, including those based on forward-looking scenario analysis and stress tests. In addition, co-ordination of supervisory approaches and knowledge sharing will help to improve the effectiveness and efficiency of supervision for sustainable finance.

2.5 DESIGNING INFORMATION ARCHITECTURE

2.5.1 Enhance transparency of information on SRI products

In response to global investors' demand for sustainable finance, product manufacturers have designed and launched various sustainable investment products to provide investment options for investors. With the proliferation of these products, investors require more transparent information to enable them to assess the features, risks and performance of the products before making any investment decision as well as continuously monitor their investments.

To provide greater profiling and enable access to a wider group of investors, several exchanges have introduced a dedicated green bond segment or platform within the exchange. For example, in 2015, the Oslo Stock Exchange (OSE) became the first stock exchange in the world to have a separate list for green bonds on its webpage, aimed at increasing the visibility of green bonds available to investors. There are 24 listed green bonds on the OSE as at October 2019.[35]

Also in 2015, the London Stock Exchange (LSE) introduced a range of dedicated green bond segments within the exchange. As at October 2019, there are over 200 debt securities admitted to the LSE sustainable bond market, coming from issuers from 18 countries.[36] In 2016, the Luxembourg Stock Exchange launched the Luxembourg Green Exchange (LGX), the world's first exchange dedicated to green bonds. Starting with the initial listing of 114 green bonds, over time, social bonds, sustainability bonds as well as green, social and ESG funds are now also listed on LGX.

To encourage more transparency in the bond and sukuk market, the existing Bond Information Exchange (BIX)[37] will have a dedicated section featuring information on SRI sukuk, green, social and sustainability bonds. In addition, issuers may consider the listing of these bonds on an exchange to promote more transparency and increase their profiling. This will also provide greater access to information, better price discovery and overall ease of trading for investors. Over time, the development of a SRI taxonomy will facilitate more issuances of SRI products in the Malaysian capital market. With a sufficient pool of SRI products, a dedicated SRI exchange may be introduced.

2.5.2 Develop ancillary services for SRI

As sustainable investments continue to grow, there will correspondingly be a rise in the demand for sustainable investment support services such as ESG research and ratings, external reviews for issuances of green bonds and sukuk as well as investment screenings and analysis. Both issuers and investors will therefore increasingly place greater value on such information and data as a means to ensure appropriate integration of sustainability principles into their practices. As a result, more service providers are offering ESG-value added services to the market.

In the green bond market, although an external review report is not a mandatory requirement, almost 90% of green bonds issued in 2018 (by issuance amount) received at least one external review.[38] Second-party opinion continues to be the preferred choice, with 60% of green bonds issued in 2018 (by issuance amount) obtaining this type of external review report.[39]

---

35 Oslo Stock Exchange.
36 London Stock Exchange Group.
37 BIX is a non-profit information platform established to provide free public access to information on bonds and sukuk issued in Malaysia.
38 CBI, *Green Bonds: The State of the Market 2018*.
39 *Ibid*.

However, other options such as certification, ratings and assurance on green bond issuances are gaining wider appreciation from both issuers and investors globally. While the issuances of SRI sukuk and ASEAN green bonds in Malaysia are accompanied by second-party opinions, service providers are encouraged to widen the scope of external review services to provide issuers and investors of SRI sukuk and bonds with wider options as well as post evaluation independent reports.

Service providers will also need to broaden the offerings of sustainable investment support services. The industry is therefore encouraged to continuously enhance their capabilities and knowledge in this area. One such opportunity is the supplementation of expertise of Shariah advisers to enable them to provide SRI-related advice to their clients.

2.5.3 Incorporate sustainability in advisory services

Many surveys have indicated that millennials will be the driving factor for sustainable investments in the years to come, with more than half in that age group surveyed globally having social good, climate change and other sustainability factors in mind when making their investment decisions.

Millennials to Drive Future Sustainable Investments

85%	millennials are **interested in sustainable investing**[40]
75%	agreed that their **investment** decisions can **influence climate change**[41]
52%	of those aged **18 to 34 put money in sustainable investments** rather than funds that do not consider sustainable factors[42]
28%	of those **aged 65 and over, put money in sustainable investments** rather than funds that do not consider sustainable factors[43]

40 Morgan Stanley Sustainable Signal Individual Investor Survey 2017 conducted worldwide.
41 *Ibid.*
42 Schroders Global Investor Study 2018.
43 *Ibid.*

As intergenerational transfer of wealth to the millennial population is expected to occur as early as 2020, which would result in US$24.0 trillion (RM100.3 trillion) to be under the control of millennials[44], there are huge opportunities to be unlocked by sustainable investment managers. Meanwhile, although 86% of high net worth individuals in Asia are currently engaged in sustainable investments, most lack clear understanding of what this entails.[45]

In a final report released in 2018 by the EU HLEG, the HLEG recommends that the EC and the European Securities and Markets Authority (ESMA) require investment advisers to "ask about, and then respond to, retail investors' preferences about the sustainable impact of their investments as a routine component of financial advice". This will ensure that investors are well-informed of the investment options available and the opportunity to align their preference and motivation with their investment goals.

As capital market intermediaries interact closely with potential investors and issuers, their roles will need to be enhanced to incorporate advice on sustainable investments. In line with this, capital market intermediaries must increase their understanding and develop their capabilities in this area to enhance their ability to offer suitable advice on SRI products and services.

2.5.4 Accelerate promotions and profiling of Malaysia as a regional SRI centre

Although Malaysia had an early start in sustainable investments, concerted efforts are required to accelerate the promotion and profiling of Malaysia as a regional SRI centre. This is essential given that other financial centres are also focusing their priorities on this agenda. As such, a collaborative and integrated approach between the government, regulators, institutional investors, financial institutions, investment managers and other stakeholders is required.

"Although Malaysia had an early start in sustainable investments, concerted efforts are required to accelerate the promotion and profiling of Malaysia as a regional SRI centre."

[44] Refinitiv, *Sustainable Investing for Millennials, 2019.*
[45] Standard Chartered Private Bank, *Asia Sustainable Investing Review 2018.*

Towards this end, the establishment of a multi-stakeholder entity to conduct business development initiatives such as engaging with issuers and investors, increasing awareness and conducting promotional activities as well as capacity building efforts, including organising workshops and publication of articles, will effectively increase the profiling of Malaysia. Such entity will also need to establish more international linkages with other global organisations that are leading the sustainable development and investments agenda.

CHAPTER 3

CONCLUSION

This SRI Roadmap provides the strategic directions and recommendations for the creation of a facilitative ecosystem to accelerate the development of Malaysia as a regional SRI centre. In charting the SRI Roadmap, thorough assessment of the global sustainable investment markets as well as the domestic landscapes has been undertaken to formulate the recommendations.

However, as sustainable investment is rapidly developing globally, there may be new factors and emerging trends that will influence the implementation of the recommendations presented in the SRI Roadmap. Thus, the recommendations have been designed to provide a degree of flexibility to enable appropriate adjustments to ensure that Malaysia will be able to respond and react accordingly towards any realignment.

Internally within the SC, more resources will be allocated towards developing SRI expertise and capabilities. In line with this, an SRI unit has been created to lead the formulation of SRI policies for the capital market, oversee the implementation of this SRI Roadmap and co-ordinate sustainable finance initiatives undertaken by the SC at the international levels including at ACMF and IOSCO.

The implementation will be carried out in a phased approach with cohesive participation from various stakeholders to ensure effective and efficient operationalisation of the SRI Roadmap’s strategies and recommendations.

ACRONYMS AND ABBREVIATIONS

ACMF	ASEAN Capital Markets Forum
ADB	Asian Development Bank
ASEAN GBS	*ASEAN Green Bond Standards*
ASEAN SBS	*ASEAN Social Bond Standards*
ASEAN	Association of Southeast Asian Nations
ASEAN SUS	*ASEAN Sustainability Bond Standards*
BIX	Bond Information Exchange
BNM	Bank Negara Malaysia
CAGR	Compound annual growth rate
CARE	Comprehend, Apply, and Report
CBI	Climate Bonds Initiative
CMP2	*Capital Market Masterplan 2*
DFI	Development financial institution
EC	European Commission
ECF	Equity crowdfunding
ESG	Environmental, Social and Governance
ESMA	European Securities and Markets Authority
EU	European Union
EU HLEG	European Union High-Level Expert Group on Sustainable Finance
FSB	Financial Stability Board
GBP	*Green Bond Principles*
GDP	Gross domestic product
GHG	Greenhouse gas
GLIC	Government-linked investment companies
GRI	Global Reporting Initiative
GSIA	Global Sustainable Investment Alliance
GTFS	Green Technology Financing Scheme
ICM	Islamic capital market
ICMA	International Capital Market Association
IDFC	International Development Finance Club
II	Institutional investor
IOSCO	International Organization of Securities Commissions
IPO	Initial public offering
LGX	Luxembourg Green Exchange
LSE	London Stock Exchange
MCCG	*Malaysian Code on Corporate Governance*
MCII	*Malaysian Code for Institutional Investors*
MDB	Multilateral development bank
MDG	Millennium Development Goal
MIFC	Malaysia International Islamic Financial Centre
MSME	Micro, small and medium-sized enterprise

MSWG	Minority Shareholders Watch Group
NGFS	Network for Greening the Financial System
NGO	Non-governmental organisation
OCIS	Oxford Centre for Islamic Studies
OIC	Organization of Islamic Cooperation
OSE	Oslo Stock Exchange
P2P	Peer-to-peer
PE	Private equity
PLC	Public-listed company
PRI	Principles for Responsible Investment
PWC	PricewaterhouseCoopers
SBG	*Sustainability Bond Guidelines*
SBP	*Social Bond Principles*
SC	Securities Commission Malaysia
SDG	Sustainable Development Goal
SME	Small and medium-sized enterprise
SPV30	Shared Prosperity Vision 2030
SRI	Sustainable and Responsible Investment
REIT	Real Estate Investment Trust
TA	Technical assistance
TCFD	Task Force on Climate-Related Financial Disclosures
UNCTAD	United Nations Conference on Trade and Development
UNFCCC	United Nations Framework Convention on Climate Change
VC	Venture capital
WEF	World Economic Forum

REFERENCES

African Development Bank, Asia Development Bank, European Bank for Reconstruction and Development, European Investment Bank, Inter-American Development Bank, IDB Invest, IDB Lab, Islamic Development Bank, World Bank, 2018, *2018 Joint Report on Multilateral Development Banks' Climate Finance.*

Asian Development Bank, 2018, *Asia Bond Monitor June 2018.*

Bloomberg NEF, Ceres, 2016, *Mapping the Gap: The Road from Paris.*

British Council, 2018, *The State of Social Enterprise in Malaysia.*

Climate Bonds Initiative, 2018, *Green Bonds: The State of the Market 2019.*

Climate Bonds Initiative Database.

Center for Global Development, 2018, *The IDFC and the SDGs Impact, Opportunities, and Challenges.*

Centre for Research on the Epidemiology of Disasters (CRED) and UN Office for Disaster Risk Reduction (UNISDR), 1998-2017, *Economic Losses, Poverty and Disasters.*

Department of Statistics Malaysia, 2019, *Small and Medium Enterprises (SMEs) Performance 2018.*

EU Financial Stability, Financial Services and Capital Market Union, 2018, *Commission Action Plan: Financing Sustainable Growth.*

EU High-Level Expert Group on Sustainable Finance, 2018, *Final Report.*

FTSE Russel, 2019, *FTSE4Good Bursa Malaysia Index.*

Global Compact Database.

Global Sustainable Investment Alliance, 2012, *2012 Global Sustainable Investment Review.*

Global Sustainable Investment Alliance, 2014, *2014 Global Sustainable Investment Review.*

Global Sustainable Investment Alliance, 2016, *2016 Global Sustainable Investment Review.*

Global Sustainable Investment Alliance, 2018, *2018 Global Sustainable Investment Review.*

Impact Invest Lab, 2019, *The Social Bond Market: Towards A New Asset Class.*

Keynote Address by the Minister of Economic Affairs, 2019, (Kick-off Conference of the Twelfth Malaysian Plan 2021-2025).

London Stock Exchange Group Database.

Malaysia International Islamic Financial Centre (MIFC) estimates.

Morgan Stanley, 2017, *Sustainable Signals: New Data from the Individual Investor.*

Natixis Investment Managers, 2019, *Natixis Investment Managers ESG Cross Survey Report.*

National Bureau of Economic Research, 2019, *Long-Term Macro Economic Effects of Climate Change: A Cross Country Analysis.*

Network for Greening the Financial System, 2019, *A Call for Action: Climate Change as a Source of Financial Risk.*

National Oceanic and Atmospheric Administration (NOAA) Climate, 2019, *Climate Change: Global Sea Level.*

Oslo Stock Exchange Database.

Principles for Responsible Investment, 2018, *Annual Report 2018.*

Principles for Responsible Investment Database.

Refinitiv, 2019, *Sustainable Investing for Millennials.*

Schroders, 2018, *Schroders Global Investor Study 2018.*

Schroders, 2018, *Schroders Institutional Investor Study 2018.*

Standard Chartered Private Bank, 2018, *Asia Sustainable Investing Review 2018.*

Task Force on Climate-Related Financial Disclosures, 2017, *Final Report: Recommendations of the Task Force on Climate-Related Financial Disclosures.*

The Intragovernmental Panel on Climate Change (IPCC), 2019, *Special Report: Global Warming of 1.5°C.*

UN, 2015, *Paris Agreement on Climate Change.*

UN, 2015, *The Millennium Development Goals.*

UN Commission on Trade and Development, 2014, *World Investment Report 2014.*

UN Convention to Combat Desertification, 2018, *Poor Land Use Costs Countries 9 Percent Equivalent of Their GDP.*

UN Environment Programme Inquiry, 2017, *Mobilising Sustainable Finance for Small and Medium Sized Enterprises.*

UN Global Compact Database.

UN High-Level Panel on Humanitarian Financing, 2016, *High-Level Panel on Humanitarian Financing Report to the Secretary-General.*

World Bank and the Institute for Health Metrics and Evaluation (IHME), 2016, *The Cost of Air Pollution: Strengthening the Economic Case for Action.*

World Commission on Environment and Development, 1987, *Our Common Future (also known as the Brundtland Report).*

World Economic Forum, 2018, *How to Set Up Effective Climate Governance on Corporate Boards – Guiding Principles and Questions.*

World Resources Institute, 2019, *Climate Finance and the Private Sector.*

World Trade Organization, 2016, *World Trade Report, 2016, Levelling the Trading Field for SMEs.*

Securities Commission Malaysia
3 Persiaran Bukit Kiara I Bukit Kiara I 50490 Kuala Lumpur
Tel: +603 6204 8000 I Fax: +603 6201 5078
Websites: www.sc.com.my www.investsmartsc.my

MIX
Paper from responsible sources
FSC® C104284
www.fsc.org

The Securities Commission Malaysia promotes sustainability practices. This publication is printed with FSC Certified recycled credit paper.