Interim Report:
Data Challenges relating to ESG and Sustainable Finance in Asia Pacific

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Introduction

Future of Sustainable Data Alliance

The Asia Securities Industry and Financial Markets Association (ASIFMA) is a partner of the Future of Sustainable Data Alliance (FOSDA) and is leading the workstream to understand data challenges for environmental, social, and governance (ESG) and Sustainable Finance in the Asia Pacific region.

FOSDA seeks to address the following question:

What data do investors and governments need to meet the requirements of regulators, citizens and market demand for sustainable investments and portfolios to 2030?

FOSDA's key objectives:

1. Articulate future ESG data requirements of investors and governments to accurately integrate ESG data into decision making;
2. Promote new technology capabilities and data by highlight the key role that new technology and data sets must play in the transition to sustainable development; and
3. Address UN Sustainable Development Goals (**"SDGs"**) related data needs and how to satisfy them for investors wanting to take greater account of SDG-related risks and impacts.

Virtual Event: 'Navigating ESG and Sustainable Finance in Asia'

On 14 July 2020, as part its workstream, ASIFMA and FOSDA organised a virtual panel discussion 'Navigating ESG and Sustainable Finance in Asia' (click here for the video recording), attended by 300 stakeholders including market participants from the buy side and sell side, specialists and consultants in ESG and Sustainable Finance, and regulators.

In addition to audience members attending the event, ASIFMA is grateful to the Speakers and Panellists who took part in the event:

Introduction:

- Matthew Chan, Head of Public Policy and Regulatory Affairs, ASIFMA
- Julia Walker, Global Head of Government and Industry Affairs for Sustainable Finance, Refinitiv

Keynote Addresses

- Paul Andrews, Secretary General, IOSCO
- Jason Wincuinas, Senior Editor, Thought Leadership Asia, Economist Intelligence Unit

Panel Discussion:

- Wang Yao, Director General, International Institute of Green Finance, Central University of Finance and Economics (Beijing)
- Amar Gill, Managing Director and Head of Investment Stewardship, APAC, BlackRock
- Elree Winnett Seelig, Head of ESG, Markets & Securities Services, Citi
- Grace Hui, Head of Green and Sustainable Finance, Markets Division, Hong Kong Exchanges and Clearing Limited
- Satoshi Ikeda, Chief Sustainable Finance Officer, Japan Financial Services Agency

This paper is based on discussion from the event as well as research referenced during the session, notably two papers presented by Jason Wincuinas of the Economist Intelligence Unit (**"EIU"**):

- Sustainable and actionable: An ESG study of climate and social challenge for Asia
- Green intelligence: Asia's ESG investing, data integrity and technology

We will continue to develop this paper further as part of the FOSDA Asia Pacific workstream, both in the lead-up to, and following, a second virtual event focused on Technology aspects of ESG and Sustainable Finance in Asia Pacific, scheduled for late October 2020.

Definition

For the purposes of this report, we define 'sustainable finance' broadly, including climate, green and social finance, as well as the consideration of longer-term economic sustainability of organisations being funded, as well as the role and stability of the overall financial system. As such, this broader definition also includes ESG investment, and is in line with IOSCO, GFMA and ICSA[1].

[1] ICMA. Sustainable Finance High-level definitions (May 2020) https://www.icmagroup.org/assets/documents/Regulatory/Green-Bonds/Sustainable-Finance-High-Level-Definitions-May-2020-110520v4.pdf

Overview of Sustainable Finance in Asia

The Covid-19 pandemic highlights the importance of ESG and sustainable finance, with one panelist noting that inflows into high-ESG products globally being up 40% in Q1 2020 as ESG continues to become mainstream[2]. At the same time, climate risks are rising in Asia, with Bangladesh, China, Indonesia, Japan, India and Vietnam all particularly exposed to rising sea levels and with potential exposure to higher credit risk[3].

In parallel, ESG and sustainable finance has become increasingly important in Asia for some time, with EIU research noting the following, based on a 2019 survey of senior and C-suite drawn from sovereign and pension funds, investment banks and insurance funds across Asia[4]:

- 95% of respondents believe ESG investing is important to their firm, with 92% saying it will become even more important in coming years, and 80% saying ESG has a positive impact on returns; yet
- This contrasts with the situation just a decade ago, with pressure for ESG coming from today's investors, especially foreign, along with regulators and exchanges which see sustainable finance as a growth business.

The 2020 EIU report notes that regional distribution is uneven, with East Asia trailing other markets, at just 5% of AUM invested in sustainable projects, compared to 30% in North America; however, the same report notes that this is changing as institutions such as Japan's Government Pension Investment Fund (**"GPIF"**) and MUFG Bank adopted wide-scale ESG criteria, encouraging the overall trend, with ESG integration into the investment process, from analysis investment decision, becoming more prevalent.

As we learnt from our panel discussions, key developments in Asia include:

- Japan is taking a leadership position in Asia, with FSA (which is part of both the Network for the Greening of the Financial System and IOSCO's Taskforce Sustainable Finance), playing a key role in promoting sustainable finance and ESG.
    - Policy-wise, Japan has taken a principles approach, which has helped accelerate scaling of the market and is reflected in the FSA's 2020 revision of its Stewardship Code for corporate governance[5].
    - Through the code and other measures the FSA is encouraging institutional investors to focus on ESG and corporates to enhance disclosure standards.
    - The FSA has also been fostering dialogue between institutional investors and corporates on implementing FSB Task Force on Climate-related Financial Disclosures (TCFD) standards for consistent climate-related financial risk disclosures, including data challenges and the enablement of greater granularity in what is measured.
- In Hong Kong, as part of our commitment to sustainability, HKEX has launched its Sustainable and Green Exchange (STAGE), an online portal to provide information transparency on sustainable, green and social investment products.

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[2] ASIFMA/FOSDA. Virtual Event: Navigating ESG and Sustainable Finance in Asia. (2020) https://youtu.be/E-SiPlJc8CM

[3] EIU. Sustainable and actionable: An ESG study of climate and social challenges for Asia. (2020) https://perspectives.eiu.com/sites/default/files/sustainable_and_actionable_report_2.pdf

[4] EIU. Green Intelligence: Asia's ESG investing, data Integrity and technology. (2019) https://perspectives.eiu.com/sites/default/files/sustainable_and_actionable_report_2.pdf

[5] FSA. Finalization of Japan's Stewardship Code (Second revised version). (24 March 2020) https://www.fsa.go.jp/en/refer/councils/stewardship/20200324.html

  - This is intended to encourage dialogue between issuers, asset managers, investors and professional advisers on sustainable and green finance.
  - STAGE will promote transparency and accessibility across all product types and asset class, and is believed to be one of the first of its kind in Asia[6].
- In China, ESG is increasingly a focus for investors and asset owners[7]. From a policy perspective, the PBOC consulted the market on updating its 2020 Green Bond Endorsed Project Catalogue recently, with the proposed changes bringing it more in line with other international taxonomies in relation to fossil fuels[8].
  - This is part of China's efforts to further promote green finance, starting with top-down policy with cross agency efforts being led by the PBOC.
  - Other initiatives include standardising green credit guidelines, and green trust fund and insurance standards, whilst encouraging innovation, and green pilots spanning policy and other measures to foster green transition at the provincial level[9].
  - Other efforts include supporting international cooperation, with PBOC active in NGFS and platforms such as IFC's sustainable banking network[10] and Green Finance Principles in 'One Belt One Road' countries[11].
  - Disclosure of ESG is in transition from a voluntary to a mandatory regime, with CSRC expected to launch settings on this soon, with ESG index providers now numbering.

More generally, there is significant growing emphasis on integrating sustainability into general decision-making, with climate and sustainability risks seen increasingly as part of broader financial risk, with implications for cost and availability of capital for firms and projects. There is also a broadening of perspective from looking at sustainability through a risk lens towards seeking investments with explicit societal benefits and social upside from business models[12].

On the Fixed Income front, Asia stands at the forefront, according another piece of EIU research[13], with green-labelled instruments playing a role in funding renewable energy projects. According to the EIU, The International Energy Agency estimates that emerging markets will add about 4,000GW of new capacity by 2040, representing two-thirds of the global increase and of which half is attributable to China and India alone.

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[6] HKEX. HKEX's Sustainable & Green Exchange. (2020) https://www.hkex.com.hk/eng/stage/index.htm

[7] ASIFMA/FOSDA. Virtual Event: Navigating ESG and Sustainable Finance in Asia. (2020) https://youtu.be/E-SiPlJc8CM

[8] ASIFMA. ASIFMA Response to Consultation of 2020 Green Bond Endorsed Project Catalogue. (2020) https://www.asifma.org/wp-content/uploads/2020/06/asifma-response-to-china-2020-green-bond-catalogue-consultation-final-eng-chn.pdf

[9] ASIFMA/FOSDA. Virtual Event: Navigating ESG and Sustainable Finance in Asia. (2020) https://youtu.be/E-SiPlJc8CM

[10] IFC. Sustainable Banking Network. (2020) https://www.ifc.org/wps/wcm/connect/topics_ext_content/ifc_external_corporate_site/sustainability-at-ifc/company-resources/sustainable-finance/sbn_whatsnew

[11] The Belt and Road Initiative (BRI). The Belt and Road Initiative. (2019) https://green-bri.org/tag/green-investment-principles-gip

[12] ASIFMA/FOSDA. Virtual Event: Navigating ESG and Sustainable Finance in Asia. (2020) https://youtu.be/E-SiPlJc8CM

[13] EIU. Sustainable and actionable: An ESG study of climate and social challenges for Asia. (2020) https://perspectives.eiu.com/sites/default/files/sustainable_and_actionable_report_2.pdf

Since 2013, a variety of green and social bonds have come to the market in Asia, including:

- Social Bonds
- Sustainability Bonds
- *Sukuk* Bonds
- Transition Bonds
- Sustainability Bonds

Regulation and Policymaking

ASIFMA published a paper in March 2020, titled 'Sustainable Finance in Asia Pacific: Regulatory State of Play'[14]. It calls for greater harmonisation of standards, frameworks and policymaking to shift the financial system to a more sustainable footing, in addition to industry participants having a role to play alongside the official sector in developing capabilities and market structures to support the growth and scaling of sustainable finance and the transition to a low-carbon global economy.

To achieve this, ASIFMA encourages policymakers and regulators to:

- Engage directly with the private sector in their own markets through transparent consultation processes during the development stage of taxonomy, prudential requirements, and ESG reporting and disclosure requirements; and
- Ensure that they take a coordinated regulatory approach internationally, with commitment from regulators in all major jurisdictions to achieve greater international consistency, ranging from approaches towards taxonomies and corporate disclosure to measurement of climate related risks and use of incentives and other mechanisms to prevent market failure.

In addition to consistent and representative taxonomies, the ASIFMA paper calls for coherent disclosure frameworks on key material factors connecting all segments of the investment cycle – from companies to investment management companies, to their shareholders and clients. This will ensure transparency and comparability between sustainability metrics throughout the economy, but requires clear thinking between the private and public sector about the data needed to support this.

IOSCO

IOSCO has acknowledged the rising importance of ESG matters and sustainable finance more generally, and is focused on related investor protection and transparency in markets as well as in mitigating systemic risks. In October 2018, IOSCO established its sustainable finance network (**"SFN"**) as a platform to connect interested IOSCO members and to exchange information and experiences. In January 2019, IOSCO issued a statement on ESG disclosures by issuers[15] and published, through its Growth and Emerging Markets Committee a report related to sustainable finance in emerging markets [16]. A further report on the overarching role of IOSCO and securities regulators was published in April 2020[17], and identified three key concerns:

1. Multiple and diverse sustainability frameworks and standards;
2. Lack of common definitions of sustainable activities; and
3. Greenwashing and other investor protection challenges.

[14] ASIFMA. Sustainable Finance in Asia Pacific Regulatory State of play. (3 March 2020) https://www.asifma.org/wp-content/uploads/2020/03/sustainable-finance-in-asia-pacific.pdf

[15] IOSCO. Statement on Disclosure of ESG Matters by Issuers. (18 January 2029) https://www.iosco.org/library/pubdocs/pdf/IOSCOPD619.pdf

[16] IOSCO. Sustainable finance in emerging markets and the role of securities regulators. (June 2019) https://www.iosco.org/library/pubdocs/pdf/IOSCOPD630.pdf

[17] IOSCO. Sustainable Finance and the Role of Securities Regulators and IOSCO. (April 2020) https://www.iosco.org/library/pubdocs/pdf/IOSCOPD652.pdf

As a result of the SFN's work, the IOSCO Board agreed in February 2020 to establish a Board-level Task Force on Sustainable Finance (STF), aimed at enabling IOSCO to play a driving role in global efforts to address the issues described in its 2020 report.[18]

IOSCO's current efforts to address ESG and the above challenges include exploration by the STF of the following:

(i) **Improving sustainability–related disclosures by issuers (WS1).** WS1 will explore avenues for improving sustainability disclosures made by issuers – with a focus on climate change-related disclosures in the first instance. This work will include engaging with and influencing initiatives underway by sustainability disclosures standard setters that are exploring ways to reduce fragmentation in disclosure frameworks and standards and considering how existing standards can provide the basis for a unifying system that can serve providers of capital and stakeholders more widely.

(ii) **Promoting investor protection with regard to asset management matters, including addressing greenwashing (WS2). WS2** will identify relevant practices and experiences in relation to the consideration of climate change as a financial risk and the use of sustainability-related factors in the investment decision process of asset managers. WS2 work will aim to result in specific metrics that can be arranged into relevant categories of disclosures, which could support investor protection.

(iii) **Addressing ESG ratings and data providers (WS3).** WS3 will assist members in understanding the implications of the increasing activity of the ESG data providers, including CRAs with regard to ESG ratings. WS3 will look into methodologies for ESG ratings and indices and supervisory practices relating to ESG ratings, with a particular focus on their climate-related aspects.

IOSCO is committed to work in collaboration with other international bodies in an effort to avoid duplicative efforts and to enhance coordination of relevant regulatory and supervisory approaches.

[18] IOSCO. IOSCO steps up its efforts to address issues around sustainability and climate change (14 April 2020) https://www.iosco.org/news/pdf/IOSCONEWS564.pdf

FUTURE OF SUSTAINABLE DATA ALLIANCE

Data and Sustainable Finance in Asia

Data Practices Today

In broad terms, investors and investment managers in Asia use a combination of information to inform ESG investment, including disclosed information, data from third parties, and raw data which needs to be sourced and analysed in-house. This is then further analysed to inform investment decisions. Approaches to data analysis can be a source of competitive advantage for asset managers.

Measuring E, S and G

For ESG investment specifically, according to the EIU's 2019 study[19], nearly half (48%) of the 2019 EIU survey respondents said they weighted Environmental (E), Governance (G), and Social (S) factors equally. 24% said they weighted E factors highest, 19% weigh S factors highest, and 15% weight G factors highest. A major driver, as noted by EIU, is mainland China's increasing focus on environmental protection, perhaps far more so than other jurisdictions in the region.

According to the 2019 EIU study, the top metrics used to quantify E factors include:

- Environmental technology contribution (47% of survey respondents);
- Environmental information disclosure (35%); and
- Climate action (31%).

Meanwhile the same study found the top S metrics to include:

- Safety Management (44%);
- Diversity and Inclusion practices (44%);
- Sustainable cities and communities goals (42%);
- Standard certification (37%);
- Health and Wellbeing (35%); and
- Quality education (30%).

Top metrics to quantify G factors include:

- Efficiency of capital (51%);
- Anti-money laundering (AML) compliance 36%;
- Related party transactions (conflict of interest) (36%); and
- External Auditing (33%).

The 2019 EIU study notes significant overlap between E, S, and G factors in practice. For example, climate change can have both E and S implications and, as a result, some practitioners may resist classifying metrics into separate categories[20], suggesting a fundamental divergence in analytical approach.

Data Sources and Analysis

Today, according to the EIU research, ESG data is gathered from a wide range of sources, from official disclosures and third-party sources, to NGO reports and social media. Other sources include bilateral meetings. Since much of this information is unstructured, Artificial Intelligence (AI) is becoming more prevalent in use.

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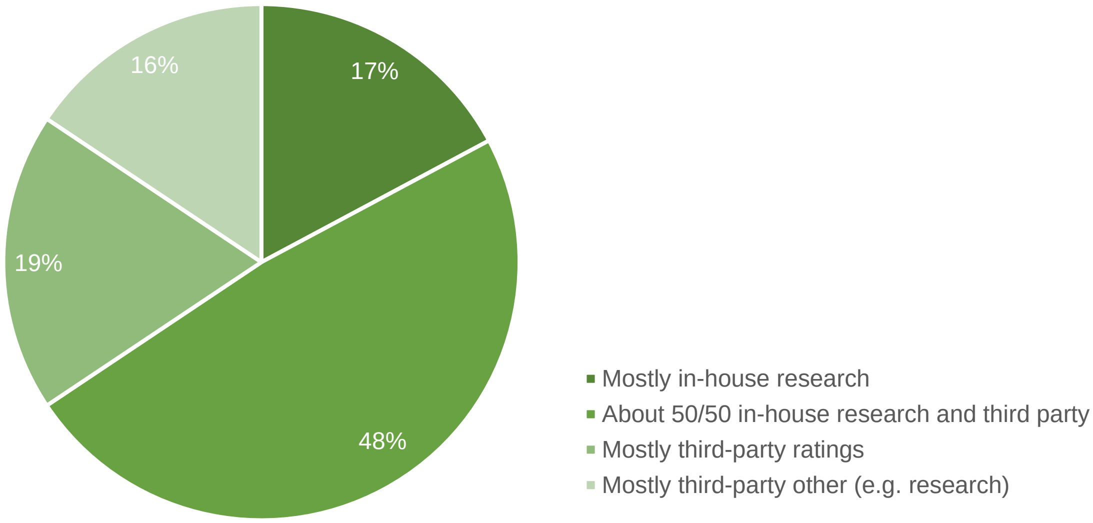
[19] EIU. Green Intelligence: Asia's ESG investing, data Integrity and technology. (2019) https://perspectives.eiu.com/sites/default/files/sustainable_and_actionable_report_2.pdf

[20] EIU. Green Intelligence: Asia's ESG investing, data Integrity and technology. (2019) https://perspectives.eiu.com/sites/default/files/sustainable_and_actionable_report_2.pdf

When asked what type of data their firms are using for ESG assessment, nearly half of respondents to a 2020 ASIFMA/FOSDA poll reported using an equal amount of in-house and third-party sources, whilst 17% used mostly in-house and 19% used mostly third-party ratings[21].

Figure 1. *If your firm is undertaking ESG assessment what type of data is it using? (Source: ASIFMA Virtual Event Poll, 2020)*



Data Challenges

According to the 2019 EIU study, future growth of ESG investment in Asia is *inextricably linked* to data. When asked to list the general obstacles to further developing ESG integration, respondents continually refer to data challenges overall:

- 32% nominated inadequacy of ESG data;
- 31% said there is not enough ESG data to make consistent decisions;
- 30% said a lack of clarity around ESG standards, terminology and metrics; and
- 26% mentioned ESG ratings and data applications being inconsistent; and
- 24% mentioned low transparency with regard to ESG-data sources.

In contrast, the only two non-data related barriers raised by respondents were lack of awareness and understanding of ESG (36%) and lack of client demand (20%)[22].

Lack of Standardisation and Comparability

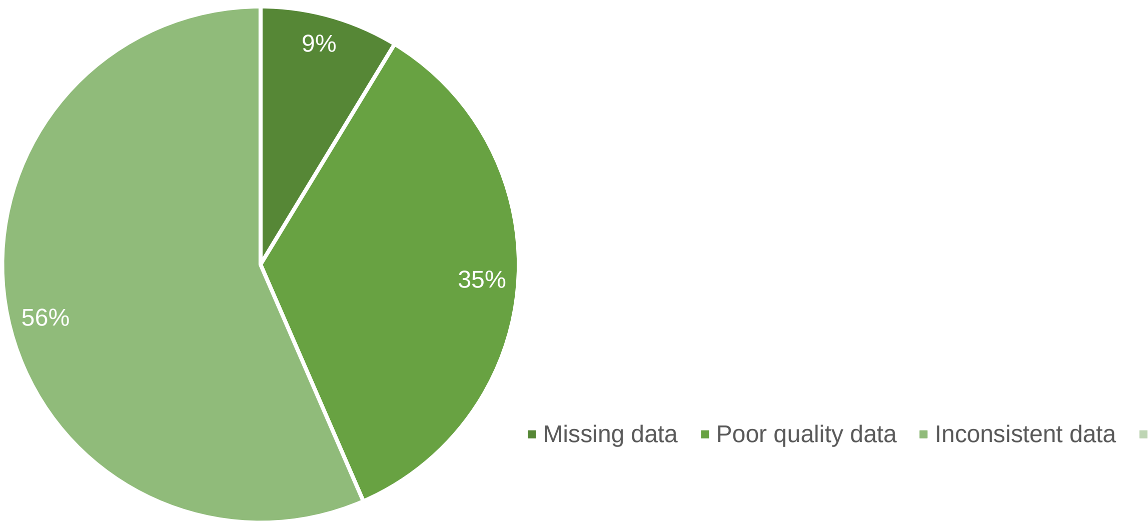
Significantly, there is no standardisation to measurement of E, S, and G factors. According to the 2019 EIU study, S factors in particular are the most difficult to measure, with analysts needing to weigh the value of very unstructured data (e.g. a complaint on social media, which may or may not portend fundamental issues)[23]. Additionally, individual ESG metrics vary not only between industries

[21] ASIFMA/FOSDA. Virtual Event: Navigating ESG and Sustainable Finance in Asia. (2020) https://youtu.be/E-SiPlJc8CM
[22] EIU. Green Intelligence: Asia's ESG investing, data Integrity and technology. (2019) https://perspectives.eiu.com/sites/default/files/sustainable_and_actionable_report_2.pdf
[23] EIU. Green Intelligence: Asia's ESG investing, data Integrity and technology. (2019) https://perspectives.eiu.com/sites/default/files/sustainable_and_actionable_report_2.pdf

and markets, but also between companies in the same industry, with the quality of company disclosures differing widely[24]. This results in difficulties in a lack of comparability between projects, companies, industries and markets[25] as well as market distortions and skewed investment decisions[26], while the 2020 EIU report notes this also leads to greenwashing, against which investors perceive a lack of contractual protection[27]. This is compounded when third-party data is used, with many vendors using different methodologies for even the same metrics[28].

When asked to nominate the greatest data challenge in ESG and sustainable finance, 56% of respondents to a 2020 ASIFMA/FOSDA poll reported 'inconsistent data'[29]. EIU notes that this complexity in itself is a disincentive for companies to issue green securities[30].

Figure 2. *What is the greatest data challenge for ESG/sustainability? (Source: ASIFMA Virtual Poll, 2020)*



The industry notes the UNDP's current work with the NGFS to tighten the UN SDGs, capturing the evolution and maturing of sustainable finance since 2016 and tightening standards. In this area too, there has been a proliferation of standards and initiatives, resulting in accountability concerns, efficiency challenges and comparability issues.

[24] ASIFMA. ASIFMA Response to Bank Negara Malaysia's Discussion Paper on Climate Change and Principle-based Taxonomy. (2020) https://www.asifma.org/wp-content/uploads/2020/04/asifma-response-to-bnm-climate-change-taxonomy-dp-v20200331-final-draft-clean4.pdf

[25] ASIFMA/FOSDA. Virtual Event: Navigating ESG and Sustainable Finance in Asia. (2020) https://youtu.be/E-SiPlJc8CM

[26] Green Intelligence: Asia's ESG investing, data integrity and technology. (2019) https://perspectives.eiu.com/sites/default/files/green_intelligence_eiu_e_fund.pdf

[27] EIU. Sustainable and actionable: An ESG study of climate and social challenges for Asia. (2020) https://perspectives.eiu.com/sites/default/files/sustainable_and_actionable_report_2.pdf

[28] EIU. Sustainable and actionable: An ESG study of climate and social challenges for Asia. (2020) https://perspectives.eiu.com/sites/default/files/sustainable_and_actionable_report_2.pdf

[29] ASIFMA/FOSDA. Virtual Event: Navigating ESG and Sustainable Finance in Asia. (2020) https://youtu.be/E-SiPlJc8CM

[30] EIU. Sustainable and actionable: An ESG study of climate and social challenges for Asia. (2020) https://perspectives.eiu.com/sites/default/files/sustainable_and_actionable_report_2.pdf

Disclosure

Firms and investors are navigating a confusing landscape of disclosure frameworks, incentive structures, data collection methods, and external assessments developed and implemented in various markets and jurisdictions by both the public and private sectors. From a disclosure perspective, this variation exists in both substance and form. Variation is evident not only between markets, but also within markets. As an example, in China, the 2019 EIU report notes that while there are different reporting requirements by province, the format in which data can be provided also varies between PDF, Word and JPG file formats[31].

Other issues relate to the quality and integrity of data provided by corporates themselves. For example, an international power utility may provide only metrics of its carbon emissions in one market that it operates, where standards may be higher (e.g. Hong Kong), whereas metrics from other markets (e.g. China) representing the majority of its activities may be excluded. This gives a distorted and misleading account of its activities[32]. This can only be partially addressed through more direct engagement between, say an investment manager and investee companies.

Tightening disclosure standards will improve quality issues, which was nominated by over a third of respondents to the 2020 ASIFMA/FOSDA poll, above.

Taxonomy

Currently, there exists no single binding global taxonomy, while classification systems for 'green' assets or products differ widely across jurisdictions and industries. While the EU's leadership in establishing its taxonomy is a step forward in scaling green finance, there is uncertainty as to how this, which has been constructed from a European perspective, may impact the Asia Pacific region if it were to become the *de facto* global standard without taking into account the needs and nuances of a region like Asia where there are countries of varied levels of economic development. Also, EU taxonomy and disclosure regulations have been described as binary, classifying economic activities as 'green' and 'non-green', but providing no incentive for transitional activities[33].

The industry welcomes leadership of jurisdictions like China and Malaysia's efforts to define taxonomies, but calls for greater regional and global harmonisation, interoperability between jurisdictions, and principles-based approaches[34]. An international taxonomy will help address the data-comparability concerns of the 56% of respondents to the 2020 ASIFMA/FOSDA poll above.

Data Availability

When asked to nominate the greatest data challenge in ESG and sustainable finance, 35% cited 'poor quality data'[35]. The 2019 EIU study notes that S factors in particular are hardest to quantify, yet the category currently thought to have the most capacity to drive negative returns in Asia. On the other hand, G factors are subject to a greater degree of mandatory disclosure, resulting in greater availability of useable data. Therefore, there is a mismatch between data availability by factor vis-a-

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31 EIU. Green Intelligence: Asia's ESG investing, data Integrity and technology. (2019) https://perspectives.eiu.com/sites/default/files/sustainable_and_actionable_report_2.pdf

32 ASIFMA/FOSDA. Virtual Event: Navigating ESG and Sustainable Finance in Asia. (2020) https://youtu.be/E-SiPlJc8CM

33 ASIFMA. Sustainable Finance in Asia Pacific Regulatory State of play. (3 March 2020) https://www.asifma.org/wp-content/uploads/2020/03/sustainable-finance-in-asia-pacific.pdf

34 ASIFMA. ASIFMA Response to Consultation of 2020 Green Bond Endorsed Project Catalogue. (2020) https://www.asifma.org/wp-content/uploads/2020/06/asifma-response-to-china-2020-green-bond-catalogue-consultation-final-eng-chn.pdf

35 ASIFMA/FOSDA. Virtual Event: Navigating ESG and Sustainable Finance in Asia. (2020) https://youtu.be/E-SiPlJc8CM

vis which factors are weighted highest (E) and/or thought to drive negative returns (S)[36].
This can manifest in a lack of comparable data to compare different projects – it may be available for one project but not another.

Another issue raised in our virtual discussion was the imbalance between data on ESG risk for ESG return, which is a challenge as firms increasingly want to assess the upside social return of investments, whereas the historic emphasis in ESG has been on downside risk[37].

Reliability of Third Parties

The 2020 EIU report notes that third-party data from vendors can be problematic, starting with reliance on a single data source often resulting in volatile indicators over time. In addition, data from some vendors can be more accurate or reliable than others. Another source of error lies in the compatibility between the vendor's methodology and metrics, and what the investor is trying to monitor. In our virtual event discussion, one of our of speakers spoke of the trade-off between data quality, sector coverage, and specificity within sectors and geographies[38].

The EIU notes that whilst credit rating agencies are regulated, ESG ratings agencies are not. To overcome some of the reliability issues, some investors have started to create their own in-house ESG scores, an avenue mostly only open to larger investors[39].

Forward- vs Backward-looking Perspectives

A fundamental issue is the fact that current data is currently backward-looking (e.g. existing or past environmental impact), with limitations at play when historical data is used to predict future factors. However, according to the 2019 report by EIU, more predictive and forward-looking data becoming available, such as supply-chain factors and other lead indicators[40].

Accessibility and Interpretability

Given the complexity of ESG data, interpreting it for research and analytical purposes can be particularly challenging. It has been noted by some commentators that much data often exist in unstructured form, for example, information gleaned from site visits, or even those methodically recorded in call reports. The 2019 EIU study further notes that data to support interpretation of 'S' factors, in particular, was the most difficult to obtain. To that end, investors and firms are looking increasingly for commercial advantages, and of the 300 respondents surveyed by EIU, a vast majority said they were using artificial intelligence (AI) either *always or often* to improve ESG analysis and increase efficiency by helping to consolidate data and analyse unstructured and structured data in meaningful ways[41].

[36] EIU. Green Intelligence: Asia's ESG investing, data Integrity and technology. (2019) https://perspectives.eiu.com/sites/default/files/sustainable_and_actionable_report_2.pdf
[37] ASIFMA/FOSDA. Virtual Event: Navigating ESG and Sustainable Finance in Asia. (2020) https://youtu.be/E-SiPlJc8CM
[38] ASIFMA/FOSDA. Virtual Event: Navigating ESG and Sustainable Finance in Asia. (2020) https://youtu.be/E-SiPlJc8CM
[39] EIU. Sustainable and actionable: An ESG study of climate and social challenges for Asia. (2020) https://perspectives.eiu.com/sites/default/files/sustainable_and_actionable_report_2.pdf
[40] EIU. Green Intelligence: Asia's ESG investing, data Integrity and technology. (2019) https://perspectives.eiu.com/sites/default/files/sustainable_and_actionable_report_2.pdf
[41] Green Intelligence: Asia's ESG investing, data integrity and technology. (2019) https://perspectives.eiu.com/sites/default/files/green_intelligence_eiu_e_fund.pdf

According to the study, 85% of asset and wealth management firms use AI *always or often*, compared to 65% of investment banks, (re)insurance companies and global financial firms, while number of analytics firms are now offering a range of AI tools[42].

Interoperability with Financial Risk Assessment

The EIU notes that while credit rating agencies assess the material impact ESG factors may have on probability of default, ESG scores may profile an issuer, and not an individual issue, and do not necessarily capture the financial implications of factors such as credit risk exposure to ESG factors[43]. There is a need for harmonisation and interoperability between ESG standards, green finance and climate-risk management standards to which financial institutions are increasingly being held[44].

In a response to the MAS's consultation on environmental risk management for banks, ASIFMA noted data challenges that would benefit from further supervisory guidance, including the need for standardised environmental and climate related data (or minimum standards) that banks should require corporate clients to disclose (including data from corporate clients), environmental and climate related metrics that banks should look towards assessing and in turn, what banks would be required to disclose, and benchmarks for environmental risks and key climate scenarios which could be used for risk management purposes[45].

[42] Green Intelligence: Asia's ESG investing, data integrity and technology. (2019) https://perspectives.eiu.com/sites/default/files/green_intelligence_eiu_e_fund.pdf

[43] Sustainable and actionable: An ESG study of climate and social challenges for Asia. (5 August 2020) https://perspectives.eiu.com/sites/default/files/sustainable_and_actionable_report_2.pdf

[44] ASIFMA. Sustainable Finance in Asia Pacific Regulatory State of play. (3 March 2020) https://www.asifma.org/wp-content/uploads/2020/03/sustainable-finance-in-asia-pacific.pdf

[45] ASIFMA. ASIFMA Response to The Monetary Authority of Singapore's Consultation Paper on Proposed Guidelines on Environmental Risk Management (Banks). (2020) https://www.asifma.org/wp-content/uploads/2020/08/asifma-response-to-mas-erm-guidelines-banks-v20200807-final.pdf

Conclusion

As we emerge from the Covid-19 pandemic, it is an opportune time to fine tune ESG and sustainable finance. ESG performed well during the pandemic, both in terms of inflows and asset performance, whilst many regulators and investors have re-committed to ESG and sustainable finance with greater focus on systemic risks related to climate and social concerns.

At the same time, it is important for Asia to focus on the data requirements for supporting ESG, to ensure data asymmetries – where regions like Europe have progressed further on ESG and data standards and availability – do not stall efforts to developing sustainable finance in the region.

Interim Recommendations

Based on the above, as well as discussions with stakeholders including at our virtual event, we have drawn up the following recommendations:

1. A greater convergence towards a principles-based global (or at least regional) taxonomy
2. Higher, more consistent (mandatory) disclosure standards between jurisdictions and sectors
3. Encouragement of higher standards of analysis, with incentives for more holistic and robust approaches to ESG measurement and analysis
4. Support for innovation such as in AI to support ESG and sustainable finance capability
5. A focus on education and skills to support ESG and sustainable finance capability
6. Higher standards and accountability for ESG ratings providers, potentially including regulation and integration with credit rating
7. Harmonisation between ESG standards and frameworks such as UN SDGs, and policy on climate change and bank supervision at systemic level, including on climate risk
8. Ongoing partnership and dialogue between the public and private sectors, as well as between stakeholders such companies and investors on disclosure and reporting standards

Next steps

ASIFMA and FOSDA will continue to seek comments from stakeholders and interested parties on this analysis and further refine the above recommendations, with a view to finalising its recommendations by the end of 2020, for inclusion in FOSDA's broader work at the international level.