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Exploring the Overseas Environmental and Social Risk Management by Financial Institutions under

"The Belt and Road"Initiative

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Executive Summary

Economic globalization has benefitted many countries, but global capital profit flows have also redirected, and in some cases locked in, a developing country's capabilities for technological development as well as their economic structures. Meanwhile, profit-driven globalized development has failed to account for resource limitations and the value of ecological services. There is now unprecedented pressure on global resources and the environment due to an economic model that has held economic growth above all else, the lagging response of the Bretton Woods system to the needs of sustainable development, and a lack of transparency throughout the processes of global financial governance. The global linkages emanating from the world's major economies are becoming broader and tighter as a result of decades of expanding economic ties from investment, trade, and finance. This increased interconnection has serious implications for global environmental governance, community development, biodiversity, and the global response to climate change.

In 2015, the UN Sustainable Development Summit set 169 specific goals for sustainable development that are to be achieved by 2030[1] demonstrating the international community's commitment to promoting sustainable development amidst the challenges of the modern era. These goals not only represent a step forward for the world's "development strategy," but also a framework that will necessitate a paradigm shift for our models of production, living, and thinking. The following Paris Agreement reached at COP21 set common goals for over 190 member countries, including the limiting global average temperature rise to less than 2°C compared to pre-industrial levels with 1.5°C as an aspirational target and achieving the "de-carbonization" of the global economy by the second half of the century. The achievement of these goals will require a global economic system that prioritizes low-carbon and quality-oriented development, driven largely by targeted financial and investment flows from major global economies.

1 The UN Sustainable Development Goals: http://www.un.org/sustainabledevelopment/sustainable-development-goals/

Sustainable global governance can only exist with the support of economic and financial activities. In recent years, the development financing of developing countries has been increasing steadily, but to achieve global development goals, more capital will be needed for the construction of low-carbon projects and sustainable infrastructure in the coming decades. In this context, China launched the "Belt and Road Initiative" (BRI), aiming to promote interconnection and extensive cooperation among BRI countries in terms of trade, infrastructure, finance, and culture, helping them to achieve independent, balanced, and sustainable development. Many BRI countries are still early on in their development. In the coming decades, the capital demand for infrastructure construction will be huge; among the more than 60 BRI countries in Central Asia, East Asia, South Asia, West Asia, and North Africa there is infrastructural demand for such projects as railways, ports, highways, power grids, energy infrastructure, oil and gas pipelines, and cross-border power transmission lines. In the face of such a robust investment demand, financial support for development along the BRI region is still insufficient, in part due to difficulties in establishing and improving investment risk management systems and credit systems. Further assistance is needed from financial institutions like regional multilateral development banks, commercial banks, equity funds, and other investment institutions to help host countries actively control risks and accelerate the realization of sustainable development.

Social risk is the primary focus of risk control in project investment. BRI host countries are mostly emerging economies and developing countries with inadequate environmental governance and social security mechanisms. Many of these countries are currently facing political and economic transitions. Political instability exists across Southeast Asia, South Asia, Central Asia, West Asia, and North Africa, and therefore, investments will face political risks. Furthermore, the BRI region encompasses both Eastern and Western cultures, possessing potentially complicated religious, ethnic, and racial conflicts. For new enterprises entering this region that are not familiar with the environmental, land, and labor regulations of host countries, their projects face compliance risks and potential economic losses due to resistance or boycotting from local communities.

Beyond social risk, investment projects must commit to serious environmental risk management. BRI countries and regions possess both vulnerable environments and ecological systems, with complicated topography and severe soil and water loss. Climate change and biodiversity protections have added new challenges for overseas investment projects, which now must look towards international experiences for guidance on how to respond to these issues. BRI countries are home to abundant biodiversity, internationally important endangered and migratory species, and different conservation zones, all of which may come into conflict with project construction. The management of environmental risks is a key challenge to investment and sustainable development along the BRI. It will thus be critical that there is capacity building and deepened cooperation in knowledge-sharing and policy development among multilateral development banks and the financial institutions of BRI countries.

Environmental and social risk management is being strengthened at both a global and a national level. From a global perspective, under advice and supervision from stakeholders, the World Bank, Asian Development Bank and regional development banks have pioneered policies for mature environmental and social security mechanisms, information disclosure, and appeal mechanisms that will hold noncompliant projects accountable. Global voluntary principles for sustainable investment such as the

"Equator Principles," the "United Nations Global Compact," the "Global Reporting Initiative," and the "Extractive Industries Transparency Initiative" have served as references for global investors and financial institutions to guide environmental and social risk management policy formulation for companies or for specific projects.

At a national level, financial regulators in many countries are enhancing environmental and social risk management in financial institutions, ensuring that public and private capitals are being channeled into green sectors. For China, the Chinese Banking and Regulatory Commission issued the "Green Credit Guidelines" in 2012,[2] with Clause 21 in the Guidelines requiring banking financial institutions to strengthen environmental and social risk management for credit lending to overseas projects, and requiring that project sponsors abide by the environmental, health, and safety laws and regulations of the host country. The Green Credit Guidelines also adds that financial institutions should promise to apply international standards and practices when granting credit to overseas projects, making sure credit issuance is fundamentally in line with global best practices.

As a dialogue platform for regional economic governance, G20 plays a vital role in promoting international financial reform and in realizing the 17 Sustainable Development Goals (SDGs) of the 2030 Agenda for Sustainable Development and the Paris Agreement. Emphasizing environmental and social risk management for overseas investments will help to minimize or avoid investment losses for financial institutions, but it will also help developing nations to build diversified, responsible investment models that will account for development needs while minimizing ecological impact and carbon footprints. Therefore, we advise influential nations to promote the following reforms domestically, through the bilateral financial institutions, or through the multilateral financial institutions that they participate in:

1

Adopt international standards and abide by domestic regulations for overseas investments. Understanding and adopting international standards and industry norms will help enterprises to integrate into the international system and improve competitiveness; newly established multilateral development banks can use experiences from existing multilateral financial institutions to build and implement better tailored and innovative environmental and social risk management systems. While investments under BRI focus on the infrastructural demands of host countries, they should take every measure to be green and low-carbon.

2 Notice on Green Credit Guidelines, China Banking Regulatory Commotion. [2012] No.4

2

Establish a guide for environmental and social risks for foreign investments based on best international practices and national and local conditions. Strengthen the identification and evaluation of environmental, climate and social risks in these nations. Good environmental and social risk management requires specific and implementable measures and tools. Evaluation tools should quantify the environmental and social risks and assess the likelihood of a loan defaulting from prospective borrowers. This will help financial institutions to improve resource allocation and control credit risk through environmental and social risk management.

3

Fully disclose environmental and social risk information of investing financial institutions and enterprises, strengthen public engagement. Investing financial institutions should require their borrowers to disclose environmental and social risks, especially in countries and regions where regulatory systems are underdeveloped, the rule of law is weak, or corruption risks are high. Strengthened information disclosure requirements will prevent suspicion and distrust among relevant parties. Information disclosure and transparency is essential for promoting fair and competitive markets as well as constructive public engagement.

4

Fully consider the challenges that global climate change mitigation poses to capital allocation and distribution. Under a 2°C temperature rise control target, financial institutions should identify, disclose, and manage climate and carbon risks. For example, quantitative targets for climate performance should be added to environmental, social, and governance indicators. The finance community should also understand the respective investment demands for developing the clean and low-carbon energy transition entailed by each nation’s "Nationally Determined Contributions." Not only will this lower the risk of stranded assets[3] caused by new environment laws, stronger carbon management, or adjusted energy demands, but by engaging more with the future of clean energy, investors can seize investment opportunities arising from efficiency and carbon emissions reduction technologies.

3 Stranded assets: impaired assets due to accidental or earlier written-off, depreciation or conversion to liability.
http://www.smithschool.ox.ac.uk/research-programmes/stranded-assets/

5

Expand environmental liability insurance to new enterprises entering the overseas market, encourage insurance agencies in emerging economies to design environmental insurance products. Environmental liability insurance can benefit the overseas investments of enterprises by minimizing financial risks of accidents while strengthening the enterprises' ability to bear responsibility for risk.

6

Encourage financial institutions to collaborate with third parties institutions, including local communities and NGOs. Third party institutions can provide enterprises with local information and professional support in order to reduce these environmental and social risks. By communicating and collaborating with local think tanks and non-profit organizations, enterprises can better consult and build trust with local communities, allowing for a smoother rollout of investment projects.

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Section 1. "The Belt and Road" Initiative and Key Financial Institutions

This section will introduce a background of "The Belt and Road" Initiative (BRI), as well as the investment priorities and capital demands driven by the Initiative. It will also briefly introduce the key financial institutions that will provide capital for BRI.

1.1. "The Belt and Road" Initiative: Global Investment and Financing Demands

In 2013, during his visit to Central Asia and Southeast Asia, Chinese President Xi Jinping outlined the initiatives of the "Silk Road Economic Belt" and the "21st Century Maritime Silk Road",[4] which have been abbreviated as "BRI" or "Land and Maritime Silk Road Initiative" respectively. In 2015, the National Development and Reform Commission (NDRC), Ministry of Commerce, and Ministry of Foreign Affairs jointly released "The Vision and Action for Joint Build-up of the Silk Road Economic Belt and the 21st Century Maritime Silk Road" (referred to as "Vision" hereunder).[5] The Vision laid out the primary and key areas of BRI, including infrastructure construction, investment and trade cooperation, finance flows, cultural exchange, and tourism.[6] Cooperation in infrastructure is a key component of BRI, particularly for the key channels, links, and projects for transport infrastructure, as well as trading post and harbour port infrastructure. Energy infrastructure is also an important component of BRI, including oil and gas pipeline construction, cross-border power transmission, and grid upgrading.

BRI can meet the infrastructural demands of host countries while promoting economic development throughout the region. BRI will extend across the Eurasian continent to countries of all development stages: ranging from developed countries, to rapidly-developing emerging countries, and least developed countries. Because of the development needs of this region, infrastructure investment and economic development and transformation will be the thrust of BRI. An important reference for this project, the "Global Competitiveness Report (2015-2016),"[7] released by the World Economic Forum, used 12 indicators to evaluate and rank the overall competitiveness of 140 countries and regions. These indicators included legal and administrative structure, infrastructure, the macroeconomic environment, financial market development, technology, and innovation. Infrastructure, the second indicator, accounted for 25% of the overall variation in competitiveness. This underscored the imbalanced economic strengths of the countries encompassed by BRI.[8] For example, Singapore (2), Germany (4), the Netherlands (5), and Hong Kong (7) have strong overall competitiveness, while Lebanon (101), Kyrgyzstan (102), Mongolia (104), Egypt (116), Pakistan (126), and Myanmar (136), rank among the bottom 40 with the weakest competitiveness. According to the report, "extensive and effective infrastructure plays a critical role in ensuring the effective functioning of an economy. Efficient transport, such as road, railway and port, etc., could enable entrepreneurs to transport goods to markets in a fast, timely and safe way". Therefore, by promoting infrastructure construction, BRI will enhance the overall competitiveness of host countries.

Domestic and Overseas Investment and Financing Demands

Most BRI countries are rich in energy reserves but are still in the earlier development stages, with strong demands for infrastructure construction. The capital demand for infrastructure in around 60 BRI

4 Source: http://en.xfafinance.com/html/OBAOR/Main%20Step/list_105_3.shtml
5 Full text: http://zhs.mofcom.gov.cn/article/xxfb/201503/20150300926644.shtml
6 Extensive reading: http://www.piffle365.com/plus/view.php?aid=55486
7 Original link: http://www3.weforum.org/docs/gcr/2015-2016/Global_Competitiveness_Report_2015-2016.pdf
8 Figure in ( ) refers to the ranking of the country in national comprehensive competitiveness.

countries has been estimated to reach around USD 2.5 trillion.[9] According to the Asian Development Bank's calculation, the total demand for infrastructure investment in Asia between 2010 and 2020 will be USD 8 trillion. Such demand is mainly driven by sectors such as railway, port, highways, and power grids in Central Asia, East Asia, South Asia, West Asia and North Africa. China's huge capital and advanced technologies in high-speed rail, road, nuclear power, hydro-power, and equipment manufacturing could help countries with these demands improve and enhance their infrastructural development. The current annual financing from multilateral development financial institutions such as World Bank and Asian Development Bank (ADB) totals less than USD 20 billion, which fails to meet the huge capital demand for infrastructure construction in Asia, and thus hindering the economic development in Asia.[10]

The financial institutions that China has initiated or is participating in will provide strong financial support for the establishment of BRI. These financial institutions include the Asian Infrastructure Investment Bank (AIIB), the BRICS Development Bank (BRICS Bank), and the Silk Road Fund, as well as Chinese policy banks, guarantee institutions, and state-owned commercial banks. Within China, the BRI will also involve several provinces and cities, including Xinjiang, Shaanxi, Fujian, Chongqing, Ningxia, Jiangsu, and Inner Mongolia, with infrastructure investment demand mainly for railways, road construction, airports, and water conservancy. Despite the huge demand for capital, both domestically and overseas, financial support for BRI regions is still lacking. Capital flows to emerging markets are still limited and there are relatively few channels for enterprises to mobilise direct financing. As a result, financial support for large scale public projects has been insufficient. Furthermore, given that BRI investments will involve many countries and currencies, there is a need for a framework for bilateral and multilateral financial cooperation. Thus far, the establishment and improvement of investment risk management and credit systems has been hindered by the geopolitical and environmental complexity of BRI encompassed countries.

1.2. Key Financial Institutions Supporting "The Belt and Road" Initiative

Financing is a cornerstone of BRI; it is critical for project development. The Vision proposed that while establishing BRI, the governments should set up frameworks for collaboration, like an inter-bank alliance, to provide special loans, set up investment cooperation funds, and to establish development finance. This will ensure that there will be financial support to drive cooperation between China and BRI countries.

Currently, there are four major types of financial institutions that are providing financial support for BRI: 1) global multilateral development financial institutions, such as the World Bank; 2) regional multilateral development financial institutions, such as ADB, the China-led AIIB, BRICS Bank, as well as the European Bank for Reconstruction and Development; 3) Chinese national policy and development banks, such as the China Development Bank and the Export-Import Bank of China; 4) commercial banks and other financial institutions in several countries, including the Insurance Investment Fund, China-ASEAN

9 Source: Pressure mounts on AIIB for greater clarity on green lending,
https://www.chinadialogue.net/article/show/single/en/8554-Pressure-mounts-on-AIIB-for-greater-clarity-on-green-lending
China's 'One Belt, One Road' looks to take construction binge offshore.http://www.reuters.com/article/china-economy-silkroad-idUSL5N10H1XR20150906
10 Source: Asian Development Bank, 2009, Infrastructure for a Seamless Asia, http://mddb.apec.org/documents/2009/MM/FMM/09_fmm_011.pdf.

Investment Corporation Fund, Gold Fund, Green and Ecological Silk Road Investment Fund, which focuses on low-carbon development and renewable energy investments, and the Silk Road Fund, which promotes infrastructure, resource development, and capacity cooperation in BRI.

Figure 1-1. Financial Institutions Supporting BRI

Types of Financial Institutions	Name	Description and Scale of Support
Multilateral Development Financial Institutions	Asian Infrastructure Investment Bank (AIIB)	AIIB is a regional multilateral development bank, with USD 100 billion of registered capital and its first batch of loans granted in mid-2016. AIIB mainly grants loans to support projects in infrastructure-related sectors, largely in host countries encompassed by BRI.
	BRICS Development Bank (BRICS Bank)	BRICS Bank is a regional multilateral development financial institution, with USD 50 billion in registered capital, with equal contributions from five BRICS member states. It mainly finances infrastructure construction in BRICS countries and other developing countries.
	World Bank (WB)	The World Bank participates in investments of projects in BRI countries through joint financing with AIIB and the BRICS Bank.
	Asia Development Bank (ADB)	ADB is a regional multilateral development bank. It participates in project investment in BRI countries through joint financing with AIIB and the BRICS Bank.
Chinese Policy Banks	China Development Bank (CDB)	CDB serves Chinese national economic and diplomatic strategies, supporting the international business expansion of Chinese enterprises as they "go global." CDB plans to provide strategic planning consultation as well as comprehensive financial services such as project planning and incubation to promote the cooperation between China and host countries encompassed by BRI. It has signed more than 70 planning and cooperation agreements with more than 60 countries. Currently, CDB has established a BRI pipeline project database, covering 64 countries with 900 projects in sectors including transportation, energy, and resources. Total investments of CDB exceed USD 800 billion.[11]

11 Source: http://news.xinhuanet.com/live/2015-05/24/c_127835411.htm

Types of Financial Institutions	Name	Description and Scale of Support
Chinese Policy Banks	Export-Import Bank of China (Export-Import Bank)	The Export-Import Bank supports the "going global" projects of China's export and import trade and enterprises. By the end of 2015, Export-Import Bank's loan balance in host countries under BRI exceeded RMB 520 billion. The Export-Import Bank has loan-balances for over 1000 projects across 49 countries, covering sectors such as roadways, railways, ports, power, and telecommunication. The Export-Import Bank also launched and set up the China-ASEAN Investment Corporation Fund, the China-CCE Investment Cooperation Fund, and the China-Eurasia Economic Cooperation Fund to provide additional channels for financial support and services for BRI projects. [12]
China's State-Owned Commercial Banks	Bank of China (BOC)	By the end of June, 2015, the Bank of China had set up branches in 16 host countries under BRI, with 300 key projects overseas with total investments of over USD 250 billion. In 2015, BOC planned to grant no less than USD 20 billion in credit lines to support BRI project construction, with an expected accumulated investment of USD 100 billion in the upcoming three years.[13]
	Industrial and Commercial Bank of China (ICBC)	ICBC established a business development leadership team at its headquarters to actively promote implementation of related projects under BRI.[14]
	China Construction Bank (CCB)	CCB has accumulated 268 key projects in BRI countries, with USD 460 billion in total investments, covering enterprises "going global" from sectors like power, construction, mining, transport, oil and gas, and telecommunications.[15]

12 Source: http://www.eximbank.gov.cn/tm/Newlist/index_343_27977.html

13 Source: http://news.cnstock.com/news/sns_bwkx/201508/3539749.htm

14 Source: http://www.icbc.com.cn/icbc/ 工行风貌 / 工行快讯 / 工行积极支持一带一路海外项目建设 .html

15 Source: http://www.chinanews.com/cj/2015/08-27/7493405.shtml

Types of Financial Institutions	Name	Description and Scale of Support
China's State-Owned Commercial Banks	Agricultural Bank of China (ABC)	ABC will grant a credit volume of 100 billion RMB (about USD 15.4 billion), focusing on building up the economic base of the Silk Road Economic Belt in Xinjiang.[16]
Funds	Silk Road Fund	The Silk Road Fund is a sovereign investment fund with over USD 40 billion. Its investments in BRI countries are mainly in sectors related to infrastructure construction, energy, iron and steel, power and telecommunications.[17]
	China Insurance Investment Fund	The China Insurance Investment Fund adopts the limited partnership (LP) model, with the total capital volume of 300 billion RMB raised mainly from insurers. It invests directly in equity and debt, while also functioning as a parent fund for investments in various onshore and offshore investment funds. Its first fund of 40 billion RMB has been invested in offshore BRI projects.[18]
	China-ASEAN Investment Corporation Fund	China-ASEAN Investment is an offshore USD equity investment fund and direct investment fund launched by Export-Import Bank of China. Together with multiple domestic and overseas investment institutions, it serves as a leading issuer with around USD 1 billion in capital.[19] Its funds will be mainly invested in infrastructure, energy, and natural resources in the ASEAN region, including sectors like transportation, power, renewable energy, utilities, telecommunications infrastructure, pipelines, minerals, public facilities, oil and gas, and forestry.

16 Source: http://finance.chinanews.com/fortune/2015/10-11/7563534.shtml

17 Source: http://www.baidu.com/link?url=rPJO-IVEtPYvJKW5-Xwtq64WW3WXNlXSdHmNScn5tagdYmAn06ISxp-5BSzixqWR&wd=&eqid=b633a3cb0000f5810000000457034087

18 Source: http://finance.ce.cn/rolling/201601/05/t20160105_8048508.shtml

19 Source: http://news.163.com/15/0121/03/AGF226ED00014AED.html

Types of Financial Institutions	Name	Description and Scale of Support
Funds	China-CCE Investment Cooperation Fund	The China-CCE Fund is a limited partner fund launched and set up by the Chinese government in 2013. The limited partners include Export-Import Bank of China, Export-Import Bank of Hungary, and an investment advisory team. The Fund has a planned volume of USD 500 million for its first tranche, with USD 435 million invested in its first closed tranche with a 10-year maturity period. The first tranche was formally launched in early 2014 (the second tranche with a planned volume of USD 1 billion is currently being raised). The China-CCE Fund will support Chinese enterprises with their investment and financing business in central and eastern Europe, with an increasing focus on BRI areas.[20]
	China-Eurasia Economic Cooperation Fund	The China-Eurasia Economic Cooperation Fund was jointly launched by the Export-Import Bank of China and BOC with a total volume of USD 5 billion. The Fund targets sectors like agricultural development, logistics, infrastructure, cutting-edge information technology, and manufacturing. The Fund will be an active backer of the Silk Road Economic Belt, deepening investment cooperation between China and Eurasian countries, while promoting economic and social development throughout the Eurasian region.[21]
	Silk Road Gold Fund	The Silk Road Gold Fund has 35% of its shares owned by the Shandong Gold Group, and 25% of its shares owned by the Shaanxi Gold Group. Its remaining shares are held by other financial institutions. The Fund plans to raise USD 16 billion over the next five to seven years for investment in gold mining and related businesses in countries along the Silk Road.[22] It aims to foster new core industrial clusters for the gold industry.[23]

20 Source: http://www.qdbofcom.gov.cn:8080/zwfb5zyzt/212390.htm
21 Source: http://www.eximbank.gov.cn/tm/Newlist/index_343_27951.html
22 Source: http://finance.sina.com.cn/stock/s/20150606/013922363084.shtml
23 Source: http://finance.sina.com.cn/china/20150525/052222255563.shtml

Types of Financial Institutions	Name	Description and Scale of Support
Funds	Green and Ecological Silk Road Investment Fund	The Green and Ecological Silk Road Investment Fund is a general equity fund established by Chinese private enterprises. It has a total raised capital of 30 billion RMB for investment mainly in ecologically-friendly sectors like solar power, clean energy development, ecological restoration, and ecological agriculture in China and other countries along the Silk Road Economic Belt. [24]
Chinese investment companies	CITIC Limited (CITIC Bank)	CITIC Bank provided RMB financing of over 400 billion RMB, covering over 200 key projects under BRI. These projects are managed by 24 subsidiary branches of CITIC Bank. [25]
	China Export and Credit Insurance Corporation (Sinosure)	Sinosure is a policy insurance company specializing in export credit insurance. Sinosure currently works to insure China's exports, investments, and contracted projects throughout BRI host countries. It signed the "Cooperation Framework Agreement on Serving 'The Belt and Road' Initiative Strategy and Supporting Chinese Enterprises in 'Going Global'" with the Silk Road Fund. Both parties will boost financial support for BRI projects to promote China's "going global" strategy. [26]

The above table is a brief summary of the Chinese financial institutions that plan to support or are currently supporting BRI. To date, the major financial backers of BRI are AIIB, Silk Road Fund, and BRICS Development Bank; these financial institutions have drawn wide attention within China and overseas. AIIB and BRICS Bank have signed a joint financing framework agreement with the World Bank[27] and have announced to the public their first round of financing projects. AIIB and the Silk Road Fund have launched projects throughout BRI countries, including natural gas and power sector projects.[28] In mid-April 2016, the BRICS Bank announced its first round of financing projects, all of which were new energy projects, implemented throughout its five member countries of Brazil, Russia, India, China, and South Africa. Beyond this, the BRICS Bank also issued its first tranche of RMB green bonds to support green development and promote green financing.[29] In summary, the investment and financing activity of these three institutions is closely related to the development of BRI.

24 Source: http://finance.ifeng.com/a/20150310/13541886_0.shtml

25 Source: http://news.xinhuanet.com/fortune/2015-06/24/c_127945969.htm

26 Source: http://news.xinhuanet.com/fortune/2015-12/11/c_1117430511.htm

27 Details: http://m.21jingji.com/article/20160414/herald/388d2d3424d422755a94e0b89894b596.html

28 Details in official website of the Silk Road Fund: http://www.silkroadfund.com.cn/cnweb/19930/19938/4c122807/index4.html

29 Source: http://money.163.com/16/0405/21/BJTTBBHB00253B0H.html

1.2.1. Asian Infrastructure Investment Bank

The newly-established Asian Infrastructure Investment Bank (AIIB), initiated by China, has provided strong financial support for the development of BRI. AIIB is a multilateral development bank established to support infrastructure construction mainly in Asia, with USD 100 billion of registered capital.[30] AIIB was first proposed in October 2013 by Xi Jinping during his visit to Southeast Asia.[31] In December 2015, AIIB was formally established, with China's Jin Liqun appointed as the first AIIB president. In April 2016, AIIB announced its first round of investment projects and signed cooperation memos with multilateral financial institutions such as the World Bank,[32] ADB, the European Bank for Reconstruction and Development, and the European Investment Bank. These joint members have helped AIIB to expand partnerships and develop joint financing.

AIIB's main investment priority is infrastructure construction,[33] positioning it as a key broker of BRI development.[34] As mentioned earlier, the huge existing demand for infrastructure in host countries encompassed by BRI has not been met by internal domestic financing, and thus there is a real need for external capital. AIIB, as a multilateral development bank, stands to become the investment and financing platform for BRI infrastructure construction and development in Asia and across other regions, thus enhancing the investment environment of BRI countries. The missions of AIIB and BRI are synergistic; both will be key to the other's success.

The successful operation of AIIB will expand the investment and financing channels available to infrastructure construction as well as other industries in Asia. AIIB will also enable the "going global" of Chinese enterprises in the fields of infrastructure, transportation, energy, power sector, water conservation, and agricultural development under BRI.

1.2.2. Silk Road Fund

In November 2014, President Xi Jinping announced the establishment of the Silk Road Fund. In December of that year, the Silk Road Fund was formally registered in Beijing with joint funding from China's Foreign Exchange Reserve, the China Investment Corporation, the Export-Import Bank of China, and China Development Bank (CDB). Silk Road Fund has USD 40 billion in total funding, with USD 10 billion in its first capital round. In this first round, China's Foreign Exchange Reserve, China Investment Corporation, Export-Import Bank of China, and CDB contributed USD 6.5 billion, USD 1.5 billion, USD 1.5 billion and USD 0.5 billion, respectively.

Silk Road Fund is a mid-term and long-term development investment fund established by China to support BRI. It mainly conducts equity investments in BRI projects in infrastructure, resources development, and financial and industrial cooperative ventures. The financial instruments used by the Silk

30 Source: http://www.aiib.org/html/aboutus/introduction/aiib/?show=0

31 Source: http://news.xinhuanet.com/overseas/2015-12/27/c_128570892.htm

32 Source: http://www.worldbank.org/en/news/press-release/2016/04/13/world-bank-and-aiib-sign-first-co-financing-framework-agreement

33 Source: http://www.aiib.org/html/2015/NEWS_0826/16.html

34 Liu Xiangfeng, AIIB and "Belt and Road" Strategy, China Finance, Issue 9, 2015, http://www.cnfinance.cn/magzi/2015-05/12-21482.html

Road Fund include equity, debt, funds, and loans. The Silk Road Fund can also launch joint investment funds with international development institutions as well as onshore and offshore financial institutions for asset custody management and external mandated investment, etc.

1.2.3. BRICS Development Bank

BRICS Development Bank is another financial institution that supports infrastructure construction in BRI emerging economies. BRICS Bank is a multilateral development bank jointly initiated by BRICS countries at a BRICS summit in Durban, South Africa, on March, 2013.[35] BRICS Bank was formally announced in July 2014, and in July 2015, it became operational.[36] The headquarters of the BRICS Bank is based in Shanghai with an African Regional Center in South Africa. According to the "Fortaleza Declaration" issued at the sixth BRICS summit, the BRICS Bank has USD 100 billion in authorized capital, with USD 50 billion in initial paid-in capital contributed by its five founding members.[37]

BRICS Bank has announced its first round of lending projects, totalling USD 911 million. These loans will mainly support renewable energy projects in China, India, Brazil, South Africa, and Russia, thus marking the formal commencement of the BRIC Bank's commercial operation. Beyond this, BRICS Bank also issued RMB three billion in five-year green bonds in China's domestic inter-bank market.[38] The proceeds from these green bond issuances will reportedly support green projects, including clean energy, transportation, resource protection and recovery, pollution control, and climate change mitigation.

The goal for the BRICS Bank is to supplement the existing multilateral and regional financial institutions, to better allocate resources to infrastructure and sustainable development projects among BRICS countries and other emerging economies and developing countries and to promote global economic growth and development. While BRICS Bank was not established solely for BRI, its activities supplement the current global financial system and support infrastructure construction and sustainable development in developing countries, thus aligning itself with BRI's mission.

Beyond these three major multilateral financial institutions, Chinese policy banks also play a significant role in the development of BRI projects. CDB mainly provides mid-and long-term loans with maturity periods of 10-15 years, while Export-Import Bank of China mainly provides support for importing, exporting, and external projects for their mechanical and electrical products and other equipment needs. As BRI has ramped up, commercial banks have also expressed interest in investing in related projects. For example, in 2015, Bank of China announced that it would try to grant more than USD 20 billion to support BRI projects, promising a total of USD 100 billion in credit in the following three years.[39] Since 2014, ICBC has led financing support for four Chinese-led enterprise power infrastructure project contracts in Bangladesh, lending a total USD 1.3 billion.[40] CCB also expressed interest in making

35 Source: http://news.xinhuanet.com/world/2013-03/27/c_124506675.htm

36 Source: http://news.xinhuanet.com/world/2014-07/17/c_126762039.htm

37 Source: http://www.guancha.cn/politics/2014_07_17_247457.shtml

38 Source: http://www.chinabond.com.cn/Info/24028228

39 Source: http://www.bankofchina.com/aboutboc/bi1/201508/t20150820_5479552.html?keywords= 中国银行 + 一带一路

40 Source: http://www.chinanews.com/gn/2015/04-03/7184076.shtml

investments in BRI-related projects, while ABC announced it would launch cooperation with the Silk Road Fund in agriculture-related sectors.

Beyond banks, financial support for infrastructure, energy, mining and agriculture projects in ASEAN and Southeast Asian countries can also come from insurance investment funds and BRI funds, such as China-ASEAN Investment Cooperation Fund. In addition, Chinese investment companies have also launched investment and financing ventures in alignment with BRI development. These investment companies include CITIC, China Investment Corporation, and Minsheng Investment Limited.

Together, multilateral financial institutions, Chinese policy banks, commercial banks, and investment companies provide the financial underpinning for BRI development projects.

Section 2. Environmental and Social Risks under "The Belt and Road" Initiative Financing and Risk Management for Chinese Banks

This section introduces the potential environmental and social risks involved in investment in BRI countries. Among China's financial institutions, banks play an important role in promoting national economic development and facilitating economic structural reform. BRI encourages and supports Chinese enterprises to "go global". This process will be facilitated by various Chinese banking institutions, including the three policy banks of CDB, Export-Import Bank of China, and Agricultural Development Bank of China, along with China's major commercial banks, through special loans and joint financing. This section uses the experiences of Chinese commercial banks as examples to introduce their practices in managing environmental and social risks in credit lending. This section will then elaborate on how Chinese banks use their credit processes and policies to address the range of risks they face in overseas investment and financing.

2.1. Financing Host Countries in BRI: Environmental and Social Risks in Key Industries

Most countries encompassed by BRI are developing countries, facing political, economic, and social challenges. These countries are also often situated in complex geopolitical and environmental contexts. Extending to regions with Eastern and Western cultures, BRI must confront potential conflicts related to religion, nationality, and ethnicity. Furthermore, BRI covers regions with serious environmental issues and fragile ecosystems. When compared with developed countries, environmental protection law systems in many BRI host countries and regions are in their fledgling stages, with poor track records in enforcement. As a result, Chinese financial institutions need to fully assess the environmental and social risks and take appropriate measures when financing or investing in BRI projects in order to ensure its financial capital security and the smooth progress of their project investments.

Social risks generally refer to the possibility of causing social conflict or threatening social stability and order, and are thus a key area of focus in investment risk management by financial institutions. For financial institutions, social risks normally refer to the possibility of financial loss caused by social conflicts or disruptions in the regions where the project is based.

Environmental risks refer to the likelihood of human-induced environmental degradation or the combination of human action and forces in nature that result in environmental degradation. Environmental risks are also a key focus of investment risk management. For many countries encompassed by BRI, local NGOs and social groups are strongly influential and will help local communities and residents to participate in environmental protection campaigns and will help to safeguard such things as their land rights. The ability of financial institutions, as well as investors and stakeholders, to communicate with locals will directly impact an enterprise's reputation and project progress. If environmental risk is not handled with care, project investments may cause conflict with local communities, which could cause direct and long-term economic losses.

Environmental and social risks in host countries encompassed by BRI may be impacted by the following factors:

Vulnerable Ecological and Environment Systems in Host Countries Encompassed by BRI

Many BRI host countries possess complicated topography and suffer from severe soil and water loss. Therefore, environmental factors should also be considered when finding the site for a new project. It is also extremely important that projects lay out plans for the prevention and mitigation of environmental damage, or if environmental harm is unavoidable, there should be a project plan in place for environmental compensation and ecological recovery. For example, many countries in West Asia and North Africa are composed mainly of plateaus and deserts, with little vegetation and singular and fragile ecosystems. These Arabian countries have forest coverage far lower than the world average. According to 2013 data released by the World Bank, only Lebanon, Morocco, and Somalia had national forest coverage rate of over 10%, while forest coverage in other Arabian countries generally hovered around 2%.[41]

41 Source: http://data.wordbank.org.cn/topic/environment

Climate change and biodiversity protection have added new challenges for overseas investment projects. International experience sharing is urgently needed to ensure that BRI projects appropriately address potential environmental risks. For example, climate change is exacerbating droughts, water shortages, and increasing the incidence rate of extreme weather events in South Asia and Central Asia. Countries encompassed by BRI are home to abundant biodiversity, including many endangered and important migratory species. Conservation zones in host countries also have the potential to come into conflict with project development.

Environmental Challenges of Natural Resource Development

Many BRI projects will place pressure on local natural resources, thus creating the potential for a range of environmental risks. First, biodiversity can be impacted by infrastructure construction, with possible ecosystem fragmentation resulting from projects like roads, railways, and pipelines. Second, in the past few years, China has been investing overseas in resource exploration for oil, natural gas, ferrous and non-ferrous metals, and coal. The development of such resource extraction projects carries high short-term risk for environmental impact, but these projects also carry long-term risks embedded in the necessary ecological recovery needed after sealing the resource extraction project. These longer-term environmental risks could easily turn into economic and social risks for project implementation and operation.

Water resource distribution and consumption is another serious challenge to overseas collaborative projects, especially given host countries encompassed by BRI often have insufficient systems in place for safeguarding water resources. As China’s "State Council’s Guidelines on Promoting International Capacity and Equipment Manufacturing" points out, projects in the iron and steel, non-ferrous metals, and chemicals sectors are very water intensive.[42] Water resource development and distribution projects on international rivers can also easily trigger conflicts among countries or regions.

Social Crises Triggered by Political Instability

Many BRI host countries have emerging economies in the early stages of economic and social development. These countries are often faced with challenges presented by political, economic, and social transformation. Countries throughout Southeast Asia, South Asia, Central Asia, West Asia, and Central and Eastern Europe are embroiled in political strife. Power conflicts in Iran, Syria, and Ukraine have triggered a series of social issues including a refugee crisis, all of which present social risks to China’s investments.

Chinese Enterprises Lack the Sufficient Preparation for the Environmental and Social Risks Associated with Overseas Projects

Under the BRI strategy, Chinese enterprises are investing in developing countries that may be politically unstable and may bring with them a range of social and environmental challenges. For example,

42 Source:http://www.gov.cn/zhengce/content/2015-05/16/content_9771.htm

overseas investment projects may have to confront the social risks that arise from land appropriation, demolition, or involuntary resettlement. If overseas investments fail to meet the long-term economic and development needs of the local community, local stakeholders may act to block, disrupt, or boycott investment projects. In addition, Chinese enterprises lack the awareness and preparation to deal with emerging social issues related to cultural heritage preservation, poverty reduction, and gender equality. This is particularly an issue with enterprises who see themselves only as foreign investors, taking few measures to learn about and integrate into the local society. With this attitude, enterprises may frequently cultivate hostilities from local residents and government officials, thus increasing social risks for investments. These problems also reflect the challenges in communication between Chinese enterprises and local communities, civil society, think-tanks, and NGOs.

As myriad international experiences have demonstrated, overseas investment projects that fail to consider the above environmental and social risks can often lead to direct or indirect negative impact on local residents, government interests, and the investors themselves.

2.2. Chinese Financial Institutions' Credit Policies and Compliance Processes

Risk control, to ensure smooth and safe project development, is integral to the operation and business model of Chinese commercial banks. It is thus critical that financial institutions adapt to overseas conditions when investing in BRI projects; this entails internalizing international best practices and experiences, improving environmental, climate, and social risk management in host countries, and tailoring the risk management process in investment and financing according to local conditions. Doing this will not only help mitigate or avoid any potential negative investment impact on locals, it will also ensure the safety of the investments for financial institutions.

This section will introduce the credit approval and compliance management processes of China's current banking institutions, focusing on credit management principles, key procedures, management structure, credit policy, and guidelines for credit review and approval. This section will illustrate how such processes incorporate environmental and social risk management into their design.

2.2.1 Credit Approval and Compliance Management in China's Commercial Banks

A wide range of Chinese banks are participating in project investment and financing under BRI. In particular, policy banks play a major role both as financers and as financial advisers, providing low-cost credit services for large infrastructures led by Chinese enterprises that are "going-global." Large-scale Chinese commercial banks with overseas branches are also providing convenient financing through capital settlement and joint guarantees or commercial loans between onshore and offshore institutions. Issuing credit is a principle function of banks, and it is also responsible for much of the banking sector's profits. Banking credit management involves a series of processes that focus on risks avoidance, profitability, and capital security. Understanding, managing, and controlling risk is a symbol of professionalism for the banking sector, and it is critical for smooth financial operations overseas.

Generally, banks' business management departments abide by the existing operating procedures to reduce risk and maximize benefits through a multi-stage process. The credit and compliance management process of Chinese domestic banks usually includes: 1) case management initiation, 2) project investigation and review, 3) approval, 4) loan issuance, and 5) post-lending management. There are two important principles in this review process. The first is "lending and review separation." This principle is clearly stated in the "Law on Commercial Banks" and in the "General Rules for Loans," which requires that for a loan application, the investigation and review process be separated from the final approval process of the loan application, thus minimizing credit risks. A second principle is to have a multi-level review process. According to Article 35 of "Law on Commercial Banks," "The commercial banking loans shall be reviewed by different levels with reviewing separated from lending."[43] According to Article 41 of "General Rules for Loans," "Lenders should determine the necessary approval authority level for a loan application according to business volume, management level, and loan risks. Higher levels of approval authority shall assess loans when the authority level of lower levels in insufficient."[44]

To respond to these principles, the banking sector has introduced a management structure consisting of a board of directors, various risk management committees, a management president, and a hierarchy of professionals. Traditionally, most loans were granted by the client manager (the front-desk staff) of the branches, producing a natural conflict of interests: as a grass-root client manager, his or her key responsibilities are to promote banking products, expand the bank's customer base, and push forward project execution. Therefore, the client manager cannot be a disinterested party in the project investigation and loan approval process. By separating the review process from the lending process, and by establishing a multi-tiered management structure, banks can better address project risk.

2.2.2. Operating Guidelines for Credit Policy and Credit Business Investigation and Approval

Credit policy generally guides how banks conduct their own credit business. Banks formulate guidelines and measures to shape their lending operations. These guidelines will reflect governmental macroeconomic policy, industrial policy, regional economic development policy, and investment policy, along with existing development and industrial cycles, in order to achieve its operational goals. Credit policy provides detailed guidance and measures for the safety, liquidity, and profitability of a bank's lending operations, often entailing client policy, product policy, industrial policy, regional policy, etc. Client policy reflects the bank's promotion of its own business in accordance with the government's macroeconomic policy, industrial policy, and regional development policy. Product policy governs how banks manage their own innovative financial products or risk management according to a range of temporal and market conditions. A bank's industrial and regional policy specifically target bank activity during specific industrial cycles or in regions with specific development needs. Industrial and regional policy are often very important during a bank's credit assessment and approval processes.

Under review and approval policy, a banks' credit review and approval process usually consists of compliance review, industrial analysis, operation status, financial analysis, credit use and solvency analysis. The required compliance review investigates the integrity of loan applicant's provided information, the product and guarantee access, as well as whether the loan meets external laws and regulations and internal management rules. The bank's industrial analysis of a potential project looks

43 Source: http://www.kuaiji.com/fagui/2893066

44 Source: http://gw.yjbys.com/shouze/12817_2.html

at the project's operating status, production, sales, consumption patterns, technologies, industrial competitiveness, market competitiveness, and the industrial policy of the project's host country. Industry access, industrial risks, and views of industrial experts are key factors for the result of the approval process. Projects which pass the basic requirements of the compliance and industrial review are then subject to further inspection, with the final loan approval decision dependent upon the project's corporate operating profile, financial profile, use of credit, and solvency.

Even if banks have formulated sound reviewing and approval policies and operating guidelines, project risks can still be difficult to fully manage. This is because there is huge variation in potential risk across industries and host countries. Bank credit review and approval processes, therefore, must not only be familiar with the project financials, but also relevant profiles of specific industries and host countries. For example, the coal, iron, and steel industries are heavily dependent upon government policies, and banks must be aware of these policies during their review processes. If banks fail to recognize the potential impact of relevant policies, the credit-granted project may be in violation of government guidelines and policies, thus preventing project implementation and thereby causing financial losses for the bank.

2.2.3. Bank Lending: Environmental and Social Risks

The review processes and policies summarized above help to control and manage risks associated with bank lending. The following section will cover the categories of risk that are considered by banks during their review process. All of these categories of potential risk must be considered if banks are to adequately address environmental and social risks.

When an enterprise that is applying for a loan is affected by special circumstances, due to specific social, industrial, regional, or macroeconomic conditions, banks will need to conduct a more thorough credit review to assess the external, systematic risks facing by the enterprise. Often when Chinese financial institutions review risk, the "environmental" risk is not just the "ecological environment" that gets referred to in traditional development finance. "Environmental" risk is impacted not only by the atmosphere, water, and flora and fauna, but also some non-material factors like ideology, societal systems, and behaviour. In a narrow sense, the "environment" refers not only to the ecological environment, but "environment" can also refer to the combination of all natural environmental factors facing human society. In this report, the "environment" referred to by "environmental and social risks" follows the narrow meaning, while the environmental risks considered by the banks often refer to the overall environment of the country that will host the financed project, such as political, economic, and societal factors. Thus, the environmental risks for project financing considered by Chinese financial institutions include:

> **Country risk.** As stated in the "Guideline on Management of Country Risk in Banking Financial Institutions," issued by the China Banking Regulatory Commission (CBRC)[45], country risk refers to "the risk of the economic, political or social changes in a specific country or a region that cause the national or regional borrower or debt receiver to be unable or unwilling to repay debts to banking

45 Source: http://www.cbrc.gov.cn/chinese/home/docDOC_ReadView/20100623371380EBFDBEA477FF6924F3C61D3900.html

financial institutions, or that causes other financial losses to the lending financial institution." Country risk includes "transmission risks, sovereignty risks, disease epidemic risks, currency risks, macroeconomic risks, political risks and indirect national risks. These risks could be increased by deteriorating economic conditions, political or social instability, asset nationalization or appropriation, the debt defaults of a government, foreign exchange restrictions, or currency depreciations.

Regional risk. Regional risk encompasses risks related to the regional economy and natural environment, including regional natural resource conditions, industrial institutions, the stage of economic development, the degree of marketization, the strength of law implementation, economic policy, government behaviour, and levels of government credit.

Industrial risk. Industrial risk refers to the potential uncertainties that could cause industrial production, operation, and investment to perform below expectation following credit issuance, leading to financial losses. Such risks encompass such uncertainties as economic cycles, economic growth, industrial connectivity, market concentration, industrial barriers, and macroeconomic policy. The framework for industrial risk analysis focuses on industrial maturity, market competition, product substitution, barriers to market entry, and policy regulation.

Reputational risk. As stated in the "Guideline for Management of Reputation Risks of Commercial Banks," released by CBRC,[46] reputation risks refer to the risk of reputational loss resulting from negative interactions with local stakeholders, due to imperfect project operation, management, and other behaviours, as well as external events. Currently, reputation risks considered by banks usually focus on the impact of project financing on environmental pollution, global warming, and deforestation. Reputation is important to banks as it impacts the bank's ability to retain existing clients and attract new clients. Bank risk management of the above risks is closely related the environmental and social risks emphasized in this report. Risk management that comprehensively addresses all of these issue also represents a policy breakthrough for organizations which have been tracking bank compliance with environmental and social compliance.

It is generally understood that the profit model of financial institutions is dependent upon risk management and control. However, the risk prevention systems of Chinese financial institutions often have relatively weak oversight of how the impact of ecological and environmental risks on credit asset safety and sustainable operations. Traditionally, when Chinese financial institutions considered credit risks, they usually focused on economic, social and environmental risk as a whole in the overall credit risk assessment and management systems, among which natural ecological and environmental risks were often ignored as non-essential factors.

However, as the energy resource constraints and ecological environmental challenges become more serious, the sustainable economic and social development can only be achieved when environmental protection, climate change, and energy management are included as critical tasks and goals in macro-

46 Source: http://3y.uu456.com/bp_0lh7d4yluw2xzhu2l5cw_1.html

regulation. Given that finance is the lifeblood of the modern economy, the banking sector plays an integral role in social and economic activity. Banking regulatory policies should help channel capital flows so as to achieve national macro-goals by having impact on the profits of banks in different market behaviours. By influencing the profitability of banking activity in different sectors, financial capital can be channelled so as to realize the goals of government macro-policy. Therefore, by including the principles of environmental protection and green development into the credit management systems of financial institutions, regional and national economies can be shaped to achieve goals in sustainable development and climate change mitigation. In recent years, the international community has attached increasing emphasis on environmental issues, including green finance, ecological and environmental protection, climate change, and energy management. With the increasingly apparent impact of ecological and environmental risks on sustainable operations of banks, more and more Chinese financial institutions are including the necessary environmental risk assessment procedures into their credit lending processes.

As modern financial institutions focus on so-called "environmental risks," they must deal with credit-receiving enterprises that are damaging the environment by exceeding natural resource carrying capacity or causing environmental and ecological deterioration, thus facing punishment and condemnation by the government, local community, and broader public. Such negative behavior can impact normal production and operation, increasing financial risks for the involved financial institutions. The possibility that a polluting enterprise that is unable to repay its loan represents the most obvious example of environmental risk. However, environmental risk extends beyond debt defaulting. If laws and regulations extend joint liability to the bank itself, the victims of the negative environmental impacts may seek compensation, leading to lawsuits and reputation risks for the banks. Banks may also face punishment by regulators for lending to polluting enterprises, and may also lose market share due to other associated social risk factors.

Currently, the environmental risk assessment and management systems of Chinese financial institutions are still in their early development stages, with much room for improvement. For example, environmental risk assessment often depends on assessment from the environmental authorities, effective public policy, procedures, and standards, all which may not be firmly in place yet. Furthermore, there is a need for innovative financial products which can transfer environmental risks.

Beyond the social factors embedded in the environmental risk covered above, financial development institutions often refer to social risks that are triggered by the potential environmental impact of the financed project. For example, if environmental harm caused by the project influences the quality of life and public health of the local community, local stakeholders may resist, disrupt, and boycott the financed project. Currently, Chinese banks have failed to sufficiently address these challenges. With inadequate information disclosure policies, communication channels, and complaint mechanisms, these banks are unable to fully dialogue with impacted communities. In recent years, these issues have been apparent in China’s overseas investments, causing not only increased investment risks for Chinese financial institutions and enterprises, but also by impacting China’s image and reputation as an overseas investor.

2.3. Conclusion

China’s BRI investment strategy involves economic activity across a range of countries and regions. The region, country, and industry risks which need to be assessed are very complicated. To reduce regional and social risks, development projects need to be well suited to the social, environmental, and resource contexts of a given host country or region. If we are to achieve sustainable development, we need not only governments that are actively helping to better allocate resources, but also an effective set of rules to allow the market to optimize resource allocation. Under BRI, countries can adjust their economic structure through conducting market-based measures, while also benefitting from high-level international agreements pushed forward by BRI.

With the help of government participation and market support, as Chinese financial institutions "go global," they must internally prepare an improved risk management system. At the same time, Chinese financial institutions should welcome collaboration with local governments, local commercial banks, and local civil society to appropriately mitigate risks. Furthermore, banks must allow for assistance and monitoring from third parties to assess and control various risks during their project financing assessment processes. As Chinese banks consider the political and economic factors in their investments under BRI, they should also focus on the potential challenges presented by ecological, environmental, and social factors. They can do this by embedding environmental and social risk management into their credit and compliance policies to ensure compliance during project implementation. As China increases its business linkages overseas, Chinese financial institutions need to pay special attention to environmental and social challenges, by strengthening its own management systems, by strengthening risk assessment, and by attaching greater importance to the role of finance in environmental and social responsibility.

Section 3. Practices of Financial Institutions in Environmental and Social Risk Management Policies

The environmental and social safeguard policies in BRI host countries are still improving. As countries develop, overemphasis on financial activity and investment may contribute to economic growth, but it will also place great pressure on local resources and the environment. The resulting resource depletion, environmental degradation, and social conflict will lead to risks for financial activities and investments.

These investment risks require financial institutions to consider environmental and social challenges before granting loans to projects. Meanwhile, to demonstrate corporate responsibility and respond to increased momentum in global green finance and responsible investment, financial institutions need to establish corresponding mechanisms to control and reduce risks caused by environmental and social challenges. International financial development institutions that are leading on environmental and social issues have used mechanisms including: environmental and social risk management policies, information disclosure, accountability and supervision mechanisms, and policy formulation for specific industries operating in environmentally vulnerable or resource-dependent areas. This section focuses on the policies created by financial institutions meant to address the environmental and social risks. The financial institutions mentioned include traditional multilateral development financial institutions, emerging multilateral development financial institutions, and policy banks.

3.1. Environmental and Social Risk Management Policies

In coping with environmental and social risks, multilateral development financial institutions have developed a set of safeguard policies including complaint and supervision mechanisms to ensure implementation of these policies.

Financial institutions create environmental and social risk management policies to use during project approval and compliance in order to tackle the environmental and social risks arising from certain projects. Risk management policies generally encompass a large range of issues including gender, labour rights, community health, property security, personal safety, ecosystem conservation, environmental and social assessment, and governance plans, as well as natural habitat protection, pollution prevention, involuntary resettlement, and indigenous rights. Current risk management policy for multilateral financial institutions often have the following characteristics: policy formulation takes a relatively long time, policies are revised and improved continuously according to economic and social changes, and policy structure is relatively complete with wide coverage.

Figure 3-1. Safeguard Policies Development in Multilateral Development Financial Institutions[47]

Time	Major Progress
1960s-1970s	Multilateral development banks and non-governmental organizations place more attention on environmental protection
1984	WB issues the "World Bank Work Environment Regulations"
1992	WB issues the "Business Policy" and "WB Procedures"
1995	ADB issues the "Involuntary Resettlement Policies"
1997	WB consolidates its 10 "Operating Policies" into specific safeguard policies
1998	ADB issues the "Indigenous Peoples Policy"
2002	ADB issues the "Environmental Policy"
2002	Equator Principles are formulated[48]
2004	ADB begins to deliberate and revise environmental and social safeguard policies
2009	ADB approves new environmental and social safeguard policies and urges their application at the national level
2010	ADB promises to provide technical support; WB's independent assessment team starts to review safeguard policies

47 Official websites of WB and ADB
http://web.worldbank.org/WBSITE/EXTERNAL/PROJECTS/EXTPOLICIES/EXTSAFEPOL/0,,menuPK:584441~pagePK:64168427~piPK:64168435~theSitePK:584435,00.html
http://www.ifc.org/wps/wcm/connect/Topics_Ext_Content/IFC_External_Corporate_Site/Sustainability+and+Disclosure/Environmental-Social-Governance
https://www.adb.org/site/safeguards/main
48 Equator Principle http://www.equator-principles.com/

Time	Major Progress
2012	IFC (of the WB) issues the "Environmental and Social Sustainability Performance Standards"; WB starts to review and revise safeguard policies
2015	The World Bank continues to review and revise safeguard policies; AIIB issues the "Environmental and Social Framework"
2016	WB publishes the updated "Environmental and Social Safeguard Framework";[49] BRICS Bank publishes the "Environmental and Social Safeguard Framework"[50]

As shown in the table above, there has been a long process of formulation and improvement of risk management policies. WB and ADB are the principal institutions pushing progress in this area. Risk management policies sprouted in the 1960-1970s as the international community started paying more attention to environmental protection. Under such pressure, the World Bank developed and published the "World Bank Work Environment Regulations" in 1984, setting out policies and procedures adopted by the WB for projects, technical assistance, and other work that may have environmental impacts. In 1997, the World Bank consolidated its ten "Operating Policies" into specific risk management policies and developed operational procedures to ensure compliance during project preparation and implementation. Around the same time, ADB issued its "Involuntary Resettlement Policy," "Indigenous Peoples Policy," and "Environmental Policy" in 1995, 1998 and 2002, respectively. These policies established the three sections of environmental and social risk management policies for multilateral financial institutions and set an example for other multilateral financial institutions to develop environmental and social policies.

Figure 3-2. The Major Risk Management Policies and Framework for Several Multilateral Development Financial Institutions

Multilateral Development Banks	Policy Statement	Requirements for Clients	Environmental and Social Assessment	Information Disclosure	Guide and Handbook for Best Practice References
WB (under review)	Operational policy	Environmental and social assessment and management system	Environmental and social assessment and management system	Information access policy	Operational policy
IFC (2012)	Policies for Environmental and Social sustainability	Performance standards	Environmental and societal assessment	Information access policy	Guide:A guide for environmental, society, and security Explanatory documents:Examples of good practices

49 Environmental and Social Framework of the World Bank Group, http://consultations.worldbank.org/Data/hub/files/consultation-template/review-and-update-world-bank-safeguard-policies/en/materials/the_esf_clean_final_for_public_disclosure_post_board_august_4.pdf

50 “Framework” original version: http://ndb.int/pdf/ndb-environment-social-framework-20160330.pdf

Multilateral Development Banks	Policy Statement	Requirements for Clients	Environmental and Social Assessment	Information Disclosure	Guide and Handbook for Best Practice References
ADB (2009)	Statement for risk management policies	Risk management requirements	Operational handbook:process for internal risk management assessment	Policy for communication with the public	Original materials
African Development Bank (AfDB) (2013)	Statement of comprehensive risk management policies	Operational policy	Environmental and social assessment procedures	Policies for information disclosure and publication	Guide (Draft)
European Bank for Reconstruction and Development (EBRD)(2014)	Environmental and social policy	Performance requirements	Environmental and social appraisal (updating)	Information disclosures and stakeholder participation	Client Guide
European Investment Bank (EIB) (2013)	Statements for environmental and social standards and principles	Environmental and social handbook	Process for environmental and social assessments	Transparency policy	Sourcebook on EU environmental law, a guide
Inter-American Development Bank (IDB) (2006)	OP703 (part) Sustainable development framework	Operational policy	A guide for the implementation of environmental and social risk management policies and other similar risk management policies	Information access policy	Tools and handbook

Throughout the improvement and review process, environmental and social risk management policies of multilateral development financial institutions have become systematic and increasingly operational. To serve their business needs, multilateral development financial institutions have gradually established operational policies for environmental and social risk management, environmental and social assessment standards, and information disclosure policies. When comparing different policy systems, we noticed that the World Bank's current risk management policy is organized under a parallel structure where the operating policies of major sectors are independent from one another. The existing risk management policies for other multilateral development banks are broadly divided into general policy statements, operational requirements for clients, environmental and social assessment standards, information disclosure policies, and related guidance.

Policy statements or frameworks are generally used within banks to specify how to conduct project assessments and emphasize the key principles they should follow. Operational requirements for the institutions' clients specify tasks to be completed by the borrower throughout the lending process to ensure that the projects receiving credit or grants continue to be environmentally and socially sustainable. Information disclosure policies require banks to disclose information that includes, but is not limited to, challenges to environmental and social risk management. Guidelines and other reference materials take the form of instructions provided to stakeholders and clients aimed at implementing "best practices". According to the most recent version of the World Bank's environmental and social risk management policy framework,[51] the Ten Operating Policies that were previously implemented independently are now integrated into ten environmental and social standards included within the framework.

Figure 3-3 Areas covered by environmental and social safeguard policies[52]

Area	WB	IFC	ADB	AfDB	EBRD	EIB	IDB
Environmental and Social Assessment (ESA)	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Pollution prevention	Yes	Yes	Incorporated into ESA	Yes	Yes	Yes	Yes
Biodiversity	Yes	Yes	Incorporated into ESA	Yes	Yes	Yes	Yes
Environmental flow	Yes	None	None	Biodiversity	None	None	None
Involuntary Resettlement	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Community Impacts	None	Yes	Yes	Incorporated into ESA	Yes	Yes	Yes
Workforce Environment/ Labour conditions	None	Yes	Incorporated into ESA	Yes	None	Yes	None
Indigenous Peoples	Yes	Yes	Yes	Incorporated into ESA	Yes	Yes	Yes
Cultural Heritage	Yes	Yes	Incorporated into ESA	Incorporated into ESA	Yes	Yes	Yes

51 "Framework": http://consultations.worldbank.org/Data/hub/files/consultation-template/review-and-update-world-bank-safeguard-policies/en/materials/the_esf_clean_final_for_public_disclosure_post_board_august_4.pdf

52 Complied from official websites of these institutions

In general, multilateral financial institutions generally focus on similar areas in their risk management policies. As depicted in the table above, risk management policies of Multilateral Development Banks (MDBs) usually cover gender, labour rights, community health, property and personal safety, ecosystem protection, human rights, environmental and social assessments and governance programs, strategic EIA, natural habitat protection, pollution control, land acquisition and use and involuntary resettlement, and indigenous peoples' rights. Although financial institutions addressed similar concerns with their risk management policies, some institutions will choose to emphasize certain areas more than others. For example, most banks listed in the table above have separate standards and requirements for pollution control and biodiversity protection while the ADB encompasses both of these in its environmental impact assessment standards. In addition, frequent extreme weather incidents and climate change have both become major concerns for many financial institutions.

3.2. Traditional Multilateral Development Banks Environmental and Social Risk Management Mechanisms

In developing risk management policies, multilateral financial institutions are the key driving forces to promote continuous improvement. The World Bank and ADB play key roles in this policy development and improvement process. This section examines the environmental and social policies of multilateral development financial institutions, focusing on the World Bank and Asian Development Bank. This section also includes a brief analysis on the systems and mechanisms of these two banks.

3.2.1. Risk Management Policies of Traditional Multilateral Development Banks

World Bank Operational Policy

Figure 3-4. Existing Environmental and Social Policies in World Bank[53]

Area	Business policy	Specific Sector	Purpose
Environmental Policies	Business Policy 4.01	Environmental assessments	Identify current environmental and social impacts and develop mitigation measures.
	Business Policy 4.04	Natural Habitats	Prevent projects financed by World Bank from harming regions with high animal density but that are not inherently affected by human activities

53 World Bank Website:
http://web.worldbank.org/WBSITE/EXTERNAL/PROJECTS/EXTPOLICIES/EXTSAFEPOL/0,,menuPK:584441~pagePK:64168427~piPK:64168435~theSitePK:584435,00.html

Area	Business policy	Specific Sector	Purpose
Environmental Policies	Business Policy 4.36	Forests	Set minimum standards for forest projects financed by the World Bank, and provide financing to conditional commercial slashing and farming development
	Business Policy 4.09	Pest management	Encourage use of biological means and environmental control to manage insect pests while reducing dependence on chemical pesticides
	Business Policy 4.37	Dam Safety	Advise the World Bank staff and borrowers to hold discussion on strengthening dam safety mechanisms and regulation framework in project location and when requiring borrowing countries to carry out projects in line with the World Bank's mechanisms and framework
	Business Policy 7.50	International Waterway	To avoid tensions between borrowers and host countries arising from international waterways; the World Bank requires countries along waterway to reach consensus on water usage.
Social Policies	Business Policy 4.11	Cultural Resources	Avoid negative impact on cultural resources arising from WB-financed projects
	Business Policy 4.12	Involuntary Resettlement	Avoid involuntary resettlement and reduce environmental and social impacts of the project at hand; to prepare resettlement plans and submit them to the World Bank for approval before the launch of the project
	Business Policy 4.10	Indigenous Peoples	World Bank staff and borrowers, in order to respect the cultures of indigenous peoples that are involved, are asked to consult with indigenous peoples to ensure they are able to participate in and benefit from the proposed project.
Others	Business Policy 7.60	Disputed Regions	Improper handling of projects located in a disputed area may affect the World Bank's relations with borrowers and countries located in those areas. The policy intends to reduce the impacts of this potential outcome.
	Business policy 4.00	National System Consideration	Fully use the national system to lower impacts arising from the proposed project.

As the World Bank has a large number of investments and is financing various projects across different countries and industries, its existing environmental and social risk management polices were gradually developed based on environmental policies, social policies and the legal systems of the proposed host countries. Additionally, the World Bank developed procedures to ensure compliance during project preparation and implementation. Given that the water resources development and allocation projects along international rivers may cause conflict among the involved countries and regions, the World Bank developed a separate policy for projects related to dam safety and international rivers. This separate policy was developed in an attempt to avoid international disputes and negative environmental and social impacts. Smooth implementation of risk management policies is closely related to the legal system in place where the project is located. Therefore, the World Bank's risk management policy must be integrated with the local legal system of the host country to ensure effective implementation of the project. As a result of these considerations, the World Bank developed specific operating policies to better cooperate with the legal system of the host country and reduce potential negative impacts arising from the project.

The World Bank's existing risk management policies help to raise environmental requirements and improve people's standard of living. Meanwhile, the communities affected can also safeguard their rights through communication and complaints. Therefore, the World Bank's environmental and social risk management policies and standards have become the international standard, leading other development financial institutions to establish and improve their environmental and social risk management policies. However, the World Bank's environmental and social risk management policies are not perfect. The current risk management policies are obscure, complicated, and difficult to implement, often leading to project delays. The risk management policies can also be inflexible when it comes to implementation.

ADB Environmental and Social Risk Management Policies

Figure 3-5 ADB Environmental and Social Safeguard Policies[54]

Document	Scope	Specific policy	Details
Safeguard Policy Statement	Environmental protection; Involuntary resettlement; Indigenous peoples	Risk Management Policies 1: Environment	Ensure project safety and sustainable development
		Risk Management Policies 2: Involuntary resettlement	Research and design plans to reduce involuntary resettlement
		Risk Management Policies 3: Indigenous peoples	In project planning and implementation, identify indigenous peoples and respect their cultures

54 ADB website: https://www.adb.org/documents/safeguard-policy-statement

Document	Scope	Specific policy	Details
Safeguard Policy Statement	Environmental protection; Involuntary resettlement; Indigenous peoples	Risk Management Policies 4: Special Requirements for Different Finance Modalities	Environment categorization: Category A; Category B; Category C; Category FI.
Risk Management Policies	Environment	EIA and IEE	Initial Environmental Examination (IEE)
			Environmental Assessment and Review Framework (EARF)
			Environmental Impact Assessment (EIA)
			Social and Environmental Audit Report
			Environmental and Social Management System (ESMS)
		Other	Initial Poverty and Social Analysis (IPSA)
	Involuntary resettlement		Resettlement Plan
			Resettlement Framework
		Other	Initial Poverty and Social Analysis (IPSA)
	Indigenous peoples		Framework for Indigenous Peoples
			Plan for Indigenous Peoples
		Other	Initial Poverty and Social Analysis (IPSA)

ADB's risk management policy aims to assist developing countries in addressing environmental and social risks and minimize the negative impact of the financed project on people and the environment. Approved and implemented by the ADB Board of Directors in July 2009, the Safeguard Policy Statement has evolved into three policies focused on environment, involuntary resettlement, and indigenous peoples. All projects supported by ADB are required to follow these three policies. The ADB's risk management policy also provides communication and participation channels for communities and other stakeholders that are affected by the proposed project. Stakeholders can protect their own interests through relevant channels in the process of designing and implementing the project.

By comparison, the World Bank have different risk management policies. In terms of policy structure, risk management policies from other multilateral development banks in the World Bank have a horizontal structure and operate independently from each other. Risk management policies for other multilateral development banks are developed hierarchically with some policies and governance principles taking priority over others. As to the content of these policies, risk management policies in multilateral development banks usually include policy summaries, operating conditions, environmental and social assessment procedures, information access policies, and guidance documents. The World Bank's environmental policy framework includes several operational policies that are run independently. The role of the environmental assessments in the World Bank are similar to the overarching procedural policies in other multilateral development banks which evaluate the performance of other project procedures. The multilateral development banks tend to enhance their environmental and social risk management by using two to three operational policies, standards and requirements.

Specific policies and the scope of these environmental and social risk management policies are usually determined by the features and industrial distribution of the credit-receiving projects. The World Bank develops a corresponding safeguard policy system based on whether the project is public or private. While other multilateral development banks, such as the ADB and the African Development Bank, mainly lend to the private sector, their risk management policies for the public and private sectors are the same. Moreover, these banks focus more on the specific situation of each project's location, and are thus more willing to adjust their policies according to national conditions. Therefore, the multilateral development banks have different approaches in specific risk management policies.

3.2.2. Complaint Mechanisms

Development financial institutions not only create and improve high standard risk management policies, but also establish independent complaint mechanisms to deal with project-related complaints and protect residents in the project's location from rights infringement or other negative impacts arising from the project. For example, the World Bank has the Inspection Panel which is an independent dialogue platform that provides stakeholders of financed projects opportunities to raise their voice. ADB has set up the Accountability Mechanism (AM) which includes two separate offices: the Office of the Special Projects Facilitator (SPF) which is responsible for problem solving and the office of Compliance Review Panel (CRP), which is responsible for compliance audits. The International Finance Corporation (IFC) of the World Bank has a Compliance Adviser Ombudsman (CAO) to handle complaints.

Figure 3-6. Complaint Mechanisms of Major Developmental Financial Institutions

Institutions	Complaint Mechanism	Function
WB	Inspection Panel (IP)	Problem Solving; Compliance Review
IFC	Compliance Adviser Ombudsman (CAO)	Dispute Settlement; Compliance; Advisory

Institutions	Complaint Mechanism	Function
ADB	Accountability Mechanism (AM)	Problem Solving: SPF; Compliance Review: CRP
AfDB	Independent Review Mechanism (IRM)	Compliance Deliberation (Investigation); Problem Solving (Intervention)
EBRD	Project Complaint Mechanism (PCM)	Compliance Review; Problem Solving Initiative
EIB	Complaints Mechanism (CM)	Compliance Review; Problem Solving
IDB	Independent Consultation and Investigation Mechanism (MICI)	Advising; Conducting Investigation

The complaint mechanism refers to a formal, legal or non-legal complaint mechanism for individuals, workers, communities, or civil organizations adversely affected by certain commercial projects. The complaint mechanism can also be referred to as a "dispute," "complaint," or "accountability" mechanism. For instance, the EBRD complaint mechanism is known as a Project Complaint Mechanism (PCM) and the ADB complaint mechanism is known as an Accountability Mechanism (AM). In general, the complaint mechanism covers factors at the project level, business level, regional, national, and intergovernmental level. Complaint mechanisms at different levels vary in terms of objectives, means, target groups, sources of support, duration of appeals process, and costs arising from the complaint process. International financial institutions, multinational corporations, and international organizations have established complaint mechanisms. Some of these mechanisms involve supervising the companies directly, while others require fulfilling national obligations to protect the interests of the citizens from third-party infringement at the project location.

Different policy mechanisms handle complaints differently. Some mechanisms settle disputes through promoting dialogue or getting involved in an existing dialogue, while others address disputes by identifying facts and providing recommendations or statements without direct involvement in the dialogue. Other mandatory mechanisms may result in the withdrawal of project funds when an investigation and assessment reveals that the impact of the project is in violation of the relevant risk management policies and related guidelines. More often, most complaint mechanisms have multiple functions. For instance, the IFC Compliance Advisory Ombudsman (CAO) deals with IFC complaints with three functions: dispute resolution, compliance investigation, and consultancy.

The mechanisms for stakeholder complaints have provided a channel for greater communication and have broadened stakeholder participation. The complaint mechanism help stakeholders to initiate complaints in order to mitigate, or correct some commercial practices that may negatively impact the general population. The complaint mechanism can also help initiate official verification procedures and conduct policy compliance investigations. In addition, initiation of complaints will help to raise public awareness and attract media attention, which plays an important role in persuading policy makers - such as government officials, investors, and other stakeholders-to consider the various interests and demands represented in the complaints when making their investment decisions as well as in project operation. To some extent, the complaint process can also improve policy-making and help institutions realize sound corporate practices.

However, in various cases, there are limitations in the existing complaint mechanisms for developmental financial institutions. For example, complaint mechanisms often do not meet basic performance criteria, i.e., accessibility, predictability, fairness, transparency, and independence. Confidentiality provisions of some institutions also have the potential to affect the extent to which arbitrators can be involved. The effectiveness of complaint mechanisms can also be affected by the willingness of the involved parties to cooperate. Moreover, it is important to note that appeals may not ensure that the relevant enterprises will correct their business practices according to the final agreement.

3.2.3. Implementation of Environmental and Social Risk Management Mechanisms in Multinational Development Banks

Figure 3-7. IFC Operating Procedure for Environmental and Social Safeguard Mechanisms[55]

Initial screen	
IFC talks to clients in terms of environmental and social risks	IFC exclusion list for project selection

↓

Review and following procedures	
Due diligence: information disclosure and public consultation	Review: post-approval monitor

↓

Continuing monitor and disclosure	
Evaluation/tracking: periodic report	CAO provides additional supervison

55 IFC Website:
http://www.ifc.org/wps/wcm/connect/Topics_Ext_Content/IFC_External_Corporate_site/Sustainability+and+Disclosure/Environmental-Social-Governance/Sustainability+Framework

The complaint and accountability mechanisms, together with the risk management policies listed above, generally operate as part of the environmental and social risk management processes of multilateral development banks. In the case of IFC and the CAO under the IFC, Figure 3-7 shows the process that IFC uses as its risk management policy and complaint mechanism during project selection and operation. During the initial selection phase, an exclusions list is used for screening; during the review stage, the relevant requirements for due diligence and information disclosure are also shown. After the project has been approved for implementation, continuous monitoring and disclosure are required. CAO is important in monitoring and reporting at this stage, and provides the affected communities or individuals the opportunity to make complaints, resolve disputes, or conduct any compliance investigations as necessary.

In summary, although the World Bank and other multilateral development financial institutions are different in formulating environmental and social safeguard policies at different policy levels, they all cover visions and objectives, framework arrangements and requirements on clients as well as other areas of concern in safeguarding policies. After environmental and social due diligence standards are met, the follow-up EIA and editorial review will be conducted according to project classification. In order to monitor compliance of the risk management policies, banks will establish a supervisory authority to ensure the implementation of these policies as well as independent complaint and accountability mechanisms to handle project-related complaints.

3.3. Environmental and Social Governance of Financial Institutions under "The Belt and Road" Initiative

Figure 3-8. Environmental and Social Risk Management Policies of Financial Institutions Involved in BRI

Financial Institutions	Environmental and Social Risk Management Policies
AIIB	"Environmental and Social Risk Management." [56]
BRICS Bank	"Environmental and Social Risk Management Framework." [57]
Silk Road Fund	Complies with internationally accepted standards and guidelines, abides by the laws and regulations of China and the countries where the investment is located, pays attention to green environmental protection and sustainable development, and actively assumes social responsibility. [58]

56 Framework original version: http://www.aiib.org/uploadfile/2016/0226/20160226043633542.pdf

57 Framework original version: http://ndb.int/pdf/ndb-environment-social-framework-20160330.pdf

58 Source: http://www.silkroadfund.com.cn/cnweb/19854/19878/index.html

Financial Institutions		Environmental and Social Risk Management Policies
Silk Road Gold Fund		The Fund is led by the Shanghai Gold Exchange, and jointly launched by Shandong Gold Group and Shaanxi Gold Group as well as Industrial Bank. They will raise and manage a parent fund and a number of sub-funds and integrate gold resources in countries along "The Belt and Road" Initiative to strengthen gold market cooperation. There is no publicly available information related to environmental and social risk management mechanisms.[59]
Green Silk Road Equity Fund		Invests in the green industry along the Silk Road and promotes ecological environment and the development of green economies for countries along the Silk Road.[60] The fund has no specific environmental and social risk management policies.
China Insurance Investment Fund		Operates in accordance with market principles and commercial sustainability. The fund mainly invests in shantytown renovations, urban infrastructure sites, major water conservancy projects, transportation facilities in central and western regions, and international capacity cooperation under the BRI.[61] There is no publicly available information related to environmental and social risk management mechanisms.
China-ASEAN Investment Cooperation Fund		The China-ASEAN Fund focuses on sustainability of potential investment projects and uses the environmental and social standards advocated by the World Bank to standardize the environmental performance of its investment projects.[62]
Chinese Policy Banks	National Development Bank	There is no publicly available information related to environmental and social risk management mechanisms. The bank mostly follows relevant international standards and national policies: • Joined UNEP FI.[63] • National policy: Ministry of Commerce and Ministry of Environmental Protection jointly issued "Environmental Protection Guide in Foreign Investment Cooperation" in 2013; CBRC issued "Green Credit Guidelines" in February 2012; and China Banking Association issued "Corporate social Responsibility Guidelines for China's Banking Institutions" in 2009.

59 Source: http://kuaixun.stcn.com/2015/0523/12260394.shtml; http://www.guancha.cn/economy/2015_05_28_321304.shtml; http://finance.sina.com.cn/stock/s/20150606/013922363084.shtml

60 Source: http://www.elion.com.cn/article/16

61 Source: http://money.163.com/15/0626/18/AT2AOAO100254TI5.html#from=keyscan;

62 Source: http://www.asean-china-center.org/2012-05/11/c_131582354.htm; http://finance.sina.com.cn/hy/20131219/114017686516.shtml

63 Source: https://www.unpri.org/

Financial Institutions		Environmental and Social Risk Management Policies
Chinese Policy Bank	National Development Bank	• Bank policy: In 2013, after carefully studying the "Air Pollution Prevention and Control Action Plan" issued by the State Council, China Development Bank and the Ministry of Environmental Protection jointly formulated the "Working Plans to Support Air Pollution Prevention and Control." In this document, the organizations outlined key support areas and made clear that smog-emitting industries will not be supported. Moreover, specific requirements of relevant projects during the assessment phase were put forward to effectively guard against the potential risks.
	Export-Import Bank of China	In 2007, EIBC issued the Guidelines for Environmental and Social Impact Assessments of the China EXIM Bank Loan Projects. In the Guidelines, environmental information is listed as a requirement before loan approval. In 2015, EIBC issued its green credit guidance and set specific requirements to strengthen risk management on environmental and social impact in terms of structure, policy systems, process management, and internal control as well as information disclosure.[64] However, EIBC didn't publish its environmental and social risk management policy.
Major Commercial Banks in China	Bank of China	Implementing Green Credit Guidelines issued by CBRC; "Guide on Information Disclosure of Listed Companies" issued by Shanghai Stock Exchange [65] ; the "Guide on Environmental, Social and Governance Report" issued by Hong Kong Stock Exchange; [66] "Global Reporting Initiative Sustainability Reporting Guidelines (GRI4.0)" issued by International Organization for Standardization.[67]
	Industrial and Commercial Bank of China	Implemented the "Green Credit Guidelines"; "Energy Conservation and Emission Reduction Policy and Initiative."
	China Construction Bank	"Green Credit Guidelines."
	Agricultural Bank of China	CBRC's "Energy Efficiency Credit Guidelines"; "Guidelines for Agricultural Bank of China's Green Financial Bond Use of Proceeds."[68]

64 Source: http://www.bj.xinhuanet.com/hbpd/jrpd/jrpd/2016-06/17/c_1119063401.htm

65 Source: http://www.sse.com.cn/lawandrules/sserules/listing/stock/c/c_20150912_3985851.shtml

66 Source: http://www.ngocn.net/column/2015-12-23-a3ec9ad0e79abf5b.html

67 Source: BOC 2015 social responsibility report: http://www.boc.cn/investor/ir5/201603/t20160330_6627628.html

68 Source: ABC 2015 social responsibility report: http://www.abchina.com/cn/AboutABC/CSR/CSRReport/201603/P020160407315742267844.pdf

Financial Institutions		Environmental and Social Risk Management Policies
Chinese investment corporations	China Investment Corporation	No information related to environmental and social safeguard mechanisms obtained from public sources.
	China Minsheng Investment Co, Ltd	No information related to environmental and social safeguard mechanisms obtained from public sources.
	CITIC Limited	No information related to environmental and social safeguard mechanisms obtained from public sources.

The above figure presents a brief overview of environmental and social policies and systems either of Chinese financial institutions or financial institutions with Chinese participation. Overall, Chinese or China-led financial institutions have insufficient information disclosure in response to their overseas environmental and social risks. Existing management mechanisms also require improvement. Generally speaking, the annual CSR reports issued by large, state-owned commercial banks only mention the environmental and social impacts of their overseas investments and will only introduce their own initiatives such as charitable activities in the country in which they hold investments. This is especially true for investments or activities taking place in developing or less developed countries. These financial institutions consider environmental and social impact activities as a social responsibility that lies outside their financial business performance rather than as a part of their risk management policies and mechanisms. Therefore, these banks feel less need to pay more attention to these endeavours. For institutions that consider environmental and social impacts as risks, proper methods for identification and management are still lacking.

China's central government has a relatively complete set of guiding principles and policies when it comes to managing environmental and social risks. The logic behind China's response to environmental and social risks is: recognize the relevant international rules under which related departments in other countries operate and, based on this, formulate guiding principles and policies. The Ministry of Commerce and the Ministry of Environmental Protection jointly issued the "Environmental Protection Guide in Foreign Investment Cooperation" in February 2013. The CBRC issued the "Guidelines on Green Credit" in February 2012. The China Banking Association issued the "Corporate Social Responsibility Guidelines for China's Banking Institutions" in January 2009. The existence of these various guidelines indicate that China's regulators have attached great importance to the environmental and social impacts associated with overseas investments by Chinese institutions. Building on national policies, policy banks in China usually develop institutional policies according to their own standards and needs. For example, after carefully studying the "Air Pollution Prevention and Control Action Plan" issued by the State Council, China Development Bank and the Ministry of Environmental Protection jointly formulated the "Work Plans to Support Air Pollution Prevention and Control" where they listed key areas of support and made it clear that high-polluting industries will not be supported. Moreover, specific requirements for relevant projects during the assessment stage were put forward to effectively guard against potential risks. Compared with policy banks, commercial banks will follow government policies and guidelines while recognizing international rules, but they rarely formulate policies and frameworks to review a project's environmental and social impacts.

The AIIB and Silk Road Fund were established to make up for the funding gap in the development of the BRI. ADB and other emerging banks can also contribute their thoughts to building sustainable systems. For instance, these banks can consider how to focus international discussion on promoting sustainable development and green investment. However, regarding China's financial institutions, the international community continues to keep a close eye on how the AIIB, Silk Road Fund, and other financial institutions will establish and improve their own governance and tools for multilateral participation. International communities will also examine how China can promote sustainable development and green investment. As a national representative of development financial institutions, the China Development Bank has set up methods to manage the environmental and social impacts of projects. These actions of the China Development Bank have influenced commercial banks and other financial institutions in China. Therefore, this section will analyze environmental and social risk management policies and the various operational mechanisms of the AIIB, Silk Road Fund, and National Development Bank.

3.3.1. AIIB Environmental and Social Risk Management Framework

At present, the AIIB has set "lean, clean, and green" as their governance philosophy.[69] At the 49th annual ADB meeting in early May 2016, Jin Liqun specifically mentioned that AIIB-supported projects must meet three criteria: sustainable return on investment, environmental friendliness, and social inclusion. These three criteria correspond to the sustainable economic development, environmental, and social standards put forwarded by the UN.[70]During its establishment, the AIIB committed to sustainable development on a variety of occasions. These commitments sent a positive signal to the global community in terms of green and responsible financial governance. However, the AIIB still needs time to show how these sustainable standards will be implemented into their projects.

At the beginning of September 2015, AIIB published the draft of the Environmental and Social Risk Management Framework (the "Framework") and initiated a stakeholder consultation process. After less than two months, the consultation process was ended at the end of October. In February, 2016, the AIIB adopted some of the feedback collected from its consultation process and published the final version of the "Framework." In the Framework, AIIB put forward "three goals to support the Paris Agreement and strengthen the global response to climate change." These three goals are the "mitigation, adaption, and the adjustment of financial flows" coupled with the "willingness to finance and help clients in achieving their national contribution plans in the context of sustainable development and also support clients to develop a long-term greenhouse gas emissions reduction strategy through financing."

69 Source: http://www.aiib.org/html/2015/NEWS_0826/16.html

70 Source: http://www.eias.org/wp-content/uploads/2016/03/EIAS_Report_2016_ADB_Annual_Meeting_Erik_Famaey.pdf

Beyond structuring policy, the ADB also actively seeks cooperation with existing international multilateral development banks. During their development phase the ADB, with assistance from the World Bank experts, formulated their environmental protection policies. In 2016, ADB signed a joint investment agreement with the World Bank which established that cooperation projects will adopt the World Bank's protection polices in procurement and environmental and social risk management. In addition, ADB also signed a Memorandum of Understanding with the European Investment Bank (EIB), a bank which provides the world's largest proportion of lending for climate change projects. In 2015, the EIB's proportion of lending to climate change projects outside Europe accounted for 30% of its total lending.[71] The ADB can learn from EIB's experiences in climate financing as well as other institutions involved in climate financing. Through joint investment, AIIB can also learn, among other things, how to establish environmental and social risk management policies, gain effective accountability tools, and make up for the climate financing gap.

Though financing for the first round of projects has begun, ADB has yet to announce its industrial investment policies for environmental and climate-sensitive industries. Greenpeace, an international NGO, applied prudent requirements under the Framework to some existing environmentally and socially controversial projects and found that the ADB may have still given financing to these projects. However, cooperation among existing multilateral development financial institutions may provide references for the ADB to better implement and improve its existing environmental and social policies and establish an effective accountability mechanism.

3.3.2. Silk Road Environmental and Social Governance

The Silk Road Fund has priority in terms of servicing the interconnection needs for BRI. The Silk Road Fund will focus on coordinating development strategies and planning the allocation of investments among countries and regions. While abiding by international standards, guidelines, and regulations in China and host countries where investments are allocated, the Silk Road Fund will mainly invest in infrastructure, resource development, production capacity, and financial cooperation with emphasis on environmental protection and sustainable development. Currently, the Silk Road Fund has not yet established any set management standards or policies regarding sound, systematic environmental and social risk assessments.

Since the Silk Road Fund is relatively new, the relevant policy systems need to be improved, while incomplete information disclosure means little available information. Given these constraints, we can only conduct a brief analysis on the Silk Road Fund's environmental and social risk management, with information drawn from the fund's investments and already financed projects. In April 2015, during President Xi's visit to Pakistan, and under his facilitation, the Silk Road Fund and Three Gorges Group initiated the first overseas investment by signing a Memorandum of Understanding on Hydropower Cooperation in Pakistan with a Pakistani electric power association. In addition to the involvement of the Silk Road Fund and Three Gorges Group, the International Finance Corporation of the World Bank

71 Source: http://epaper.21jingji.com/html/2016-06/01/content_40970.htm

also took part in the project. The project was jointly financed by the Silk Road Fund and IFC, therefore, the project adopted the IFC's environmental and social standards. The World Bank conducted regular inspections and audits of the project during its operation. In its current stage, the project is operating well, which may be attributed to a few factors. The project is a high-quality, clean energy project recommended by Pakistan and thus the political uncertainty and environmental and social risks are lower. Furthermore, the involved investors had a deep understanding of local social conditions and could also draw on the IFC's management experiences.

The following table lists the foreign investment and financing cooperation projects since the establishment of the Silk Road Fund. As the table shows, the Silk Road Fund tends to work with leaders or government agencies in project-based countries, which enables effective control and management of country or industry risks, thereby reducing legal risks. The lenders in host country and industries usually have better environmental and social compliance management.

Figure 3-9. Financing Projects under the Silk Road Fund, and Associated Established Funds.[72]

Time	Parties	Agreement Signed/Fund Established	Industry
June 2015	ChemChina	Joint Investment in Pirelli	Chemical
September 2015	Russian Development and Foreign Economic Bank and Russian Investment Fund	Investment Memorandum of Understanding	Financial Cooperation
December 2015	Kazakhstan Export Investment Agency	China-Kazakhstan special fund agreement on production capacity	Production Capacity Cooperation
	Russian Novatek	Yamal LNG Integration Project Agreement	Energy Cooperation
January 2016	Saudi Arabia International Power and Water Companies	MOU on Joint Investment and Development of Power Stations in UAE and Egypt	Renewable Energy

3.3.3. CDB Environmental and Social Governance

Under BRI, CDB plays an important supportive role. As one of China's development financial institutions, it operates commercially while following national policies and strategies. There is limited available information on its environmental and social risk management policies. For businesses that may have an environmental impact, CDB stated in its annual report and corporate social responsibility report that it will strictly abide by the relevant national policies and guidelines including the "Environmental

72 http://www.silkroadfund.com.cn/cnweb/19854/19874/index.html

Protection Guide in Foreign Investment Cooperation" issued by Ministry of Commerce and Ministry of Environmental Protection in 2013, the "Green Credit Guidelines" issued by CBRC in February 2012, and the "Corporate Social Responsibility Guidelines for China's Banking Institutions" issued by the China Banking Association in 2009. Besides national policy requirements, CDB has committed to complying with relevant international principles, such as the United Nations Environment Programme's Financial Initiative (UNEP FI), emphasizing considerations for environmental factors in the risk assessment process. Compared with international multilateral development financial institutions such as the World Bank and the ADB, CDB is still in transition from a policy bank to a development bank. According to disclosed information, the CDB's policies closely follow the national policy guidance, so it hasn't formed a policy system covering all sectors or key environmental and social problems.

Figure 3-10. CDB Policies and Initiatives.[73]

Year	Policy
2012	"Guidance on Environmental Protection and Emissions Reduction Business" and initiated the "Sustainable Development Initiative" with 16 members
2011	"2011 China Development Bank Work Plan on Credit Granting to Environmental Protection and Emissions Reduction Business", "Environmental Benefits Index System for Green Projects "
2010	"Guidance on Financial Business Supporting Emission Reduction Projects", "Guidance on Forest Ownership Mortgage" jointly issued by China Development Bank and State Forestry Bureau
2009	"Development Financial Cooperation Agreement" signed in conjunction with the Ministry of Environmental Protection; "2009 Guidance on Credit Granting to Energy Conservation and Emissions Reduction"
2008	"Guidance on the 2008 Newly Reviewed Project and Use of Loans", "China Development Bank Work Plan on Financing Sewage Disposal".
2007	"CDB Guidance on Environmental Protection Project Development and Review", "CDB Guidance on Lengding to Energy Conservation and Emission Reduction", "Guidance on Implementation of Loan Reviews on Energy Conservation Projects"

As can be seen above, CDB policies lack consistency. For example, CDB issued two energy saving and emissions reduction related guidances in 2007, but in 2009 it issued a similar guidance again, and it updated these guidances in 2010, 2011, and 2012. Policy inconsistency will lead to incomplete implementation by project stakeholders since stakeholders cannot treat the guidance as an established

73 All documents extracted from CDB social responsibility reports from 2008 to 2012: http://www.cdb.com.cn/shzr/kcxfzbg/shzr_2015/

standard for fear that there may be more changes that will disrupt previous plans and work and cause unnecessary losses. As a result, the banks will continue to issue guidances, while stakeholders cannot fully implement them. Moreover, compared with development banks in other regions, CDB needs to further improve its information disclosure and complaint mechanisms.

We will analyze a CDB-financed project to show the importance of environmental and social risk management policies for financial institutions.

The Stanari thermal power project, located in the Republic of Bosnia and Herzegovina, was financed largely by CDB. After the project proposal was submitted in 2008, and following the completion of the project Environmental Impact Assessment (EIA) based on their original project plan, CDB approved the proposal.[74] However, in 2010, when the project underwent major changes, the implementing party did not conduct a new EIA, nor did they consult with the public. As a result, this project violated the Law on Environmental Protection of the Republic of Bosnia and Herzegovina.[75] Moreover, in the long term, the project also ran counter to the goals of limiting coal-fired power plant financing. Over the past few years, the World Bank, EIB, and EBRD, as well as export credit agencies in the US, United Kingdom, and Netherlands, have committed to reducing financial support to most coal-fired power plant projects.[76] In summary, this project exposed many potentially ubiquitous issues including lack of information disclosure, violation of host country laws, and the violation of environmental protection.

These issues can be resolved if project implementing enterprises and financial institutions that support the project can act together through active communication with stakeholders. Corporate compliance pressure comes in part from financial institutions providing financial support. Therefore, financial institutions need to develop policies that urge companies to revaluate environmental factors so that these companies make adjustments and comply with laws and regulations in host countries throughout the process of project implementation. At present, the laws, regulations, and economic capacities of developing countries have failed to serve the energy transformation as developing countries depend heavily on fossil fuels. Since countries along the Belt and Road are mostly developing countries that have large energy demands for economic and social development, some of the construction funds will inevitably be invested in the energy sector. Therefore, it is crucial for financial institutions to manage and control environmental and social risks in order to avoid significant impacts on BRI countries.

74 Source: http://www.eft-group.net/index.php/news/single/68 /

75 A local government, the Republika Srpska, permitted the use of an environmental permit that is not updated. Failure to reevaluate environmental impacts of projects after changes violated the Environmental Protection Law of the Republic of Bosnia and Herzegovina. According to Article 21 of the Green Credit Guidelines, CDB shall ensure that project sponsors abide by relevant laws and regulations in environmental protection, land, health, and safety in countries or regions where each project is located

76 Source: http://www.scientificamerican.com/article/world-bank-wades-into-climate-fight/

Section 4. Recommendations on Environmental and Social Risk Management for Financial Institutions Supporting BRI

Considering complicated and diverse investment environments along BRI, financial institutions face various risks and challenges in overseas credit and financing business. These challenges are similar to those faced by Chinese enterprises as they launched their "going global" strategies in 2000. However, the difference now is that, in the past five years, China's green finance has developed rapidly. In 2012, the CBRC issued their "Green Credit Guidelines," and Article 21 of the Guidelines made a special statement on overseas investment risk management, requiring financial institutions to adopt international practices and rules. Although there is room for financial institutions to understand and implement the Guidelines, it is an important warning to financial institutions from a higher regulatory level in order to strengthen environmental and social management in overseas investment.

In 2016, green finance was included in the G20 Communique for the first time, guiding countries to establish better green financial systems. In addition, the Communique attaches importance to the role of multilateral development banks in infrastructure investment and financing and urges multilateral banks to consider social and environmental impacts when pursuing high-quality infrastructure investments. These measures will reinforce the roles of multilateral development finance institutions in high-quality infrastructure investment and will also be important to the development of the BRI.

However, in order to make development financial institutions play a more important role in environmental and social impacts governance, it is necessary to improve national laws and regulations as well as environmental and social risk management mechanisms. This report presents a number of recommendations through desktop research and interviews with financial institutions, academics, and industry experts:

International Communities and Countries along the Belt and Road:

1. International communities should actively prevent and control potential negative environmental and social impacts of financial and investment activities, strengthen the formulation and implementation of related policies, and promote actions for the realization of the UN sustainable development goals and implementation of the Paris Agreement. Specifically, the international financial governance platforms and mechanisms, including the G20 and IDFC, should reach consensus on their approach to deal with environmental and social issues, integrate sustainability and resilience into global investment guidelines, and form a structure similar to the Equator Principles, the United Nations Global Compact, and the Extractive Industries Transparency Initiative as well as other industry standards;

2. Countries should integrate sustainable finance and investment into their national growth strategies, develop sustainable investment strategies and policies for the energy sector, phase out financing for the fossil fuels, and encourage low carbon and sustainable infrastructure construction projects;

3. Countries should enhance the information disclosure and transparency of financial institutions and enterprises in environmental, social, and climate impacts; countries should ensure stakeholders consultations and supervision, including providing these services to communities and civil organizations. For example, countries can incorporate information disclosure into laws and regulations, requiring financial institutions and enterprises to develop and implement independent policies for information disclosure and public communication; strengthening supervision and enforcement of information disclosure as well as a content review and examination of information disclosure; and specifying the legal effect of public participation so as to ensure mechanisms for public supervision. Besides requiring financial institutions to disclose information, listed companies along the Belt and Road should also implement mandatory information disclosure, expand mandatory disclosure on environmental, social, and corporate governance (ESG) information to improve corporate transparency;

4. Countries should strengthen the capability of the market to allocate financial resources to environment and climate-friendly projects and low-carbon industries and to channel public funds

and social capital into green projects. These green projects can include developing green credit, green bonds, and green insurance as well as social responsibility indexes related to sustainable development that strictly define the "greenness" of financial products and services. This will ensure effective emissions reduction and environmental protection;

5. Countries should take into full consideration the impacts that climate change will have on their investments. Countries should identify and manage investment risks arising from climate polices and carbon risks. After the Paris Agreement took effect, most countries along the Belt and Road began working toward their goals under the countries' National Determined Contribution (NDC), while key investment areas along the BRI are now involved in a large number of infrastructure and energy partnerships. Therefore, such considerations as which emissions standard should be applied and investment in which sector may become a stranded asset will not only impact project operations, but will also influence the implementation of the host country's national strategy.

Financial Institutions

1. Financial institutions should abide by and implement international standards and national policies, formulating tailored implementation standards accordingly. For example, financial institutions should strictly follow "Green Credit Guidelines" issued by the People's Bank of China (PBOC) and CBRC in 2012, especially requirements on environmental and social risks management in overseas investments set in Article 21;

2. Financial institutions can draw on industry policies including the Equator Principles, the United Nations Global Compact, and the EITI to formulate mining and energy industry policies. Understanding and adopting international standards and industry norms will help enterprises to quickly integrate into the international environment and enhance their own competitiveness. Participating Chinese multilateral development banks can draw on the experiences of existing multilateral development financial institutions to form a set of environmental and social risk management systems that are suitable for themselves but also can be innovated. While satisfying the financing needs of national infrastructure construction projects along the BRI, these countries should promote green and low carbon investments;

3. Financial institutions should strengthen their ability to assess the environmental and social risks of countries along the BRI. Specific operational tools are needed to manage these risks. Financial regulatory authorities may lead or commission industrial associations or related research institutions to design country-based environmental social assessment systems according to key investment sectors and projects and make these systems open to all financial institutions and enterprises. These tools can quantify environmental and social risks, assess the likelihood of defaulted loans, and help financial institutions to improve their allocation of resources and control credit risk through management of social risks.

4. Financial institutions should also enhance disclosure and transparency regarding ESG. Strengthening ESG information disclosure lays a foundation for corporations to improve their

corporate transparency and fulfil their corporate social responsibility. Following principles of high transparency disclosure will help promote fair and healthy competition and create methods of social supervision. Third-party professional organizations can help Chinese enterprises by providing local information and professional support to reduce the risks associated with ESG. Financial institutions should openly cooperate with third parties to disclose environmental information on local projects in a timely manner and enhance communication with relevant stakeholders. In addition, with the help of private channels such as think tanks and non-profit organizations, it is easier for financial institutions, credit enterprises, and local communities to establish mutual trust so as to smooth construction and operation of the project.

Other institutions

1. Chinese insurance companies should design environmental liability insurance for Chinese enterprises facing overseas risks. No matter how well risk management operates, it cannot protect against all risks. There are many sound practices in environmental liability insurance internationally. In overseas investment, enterprises can use environmental liability insurance as a tool to reduce potential financial risks caused by accidents as well as increase the capacity of enterprises to manage risks.

2. Civil societies and civil organizations in countries along the BRI should maximize their supervisory role and urge financial institutions to establish sound complaints and oversight mechanisms and to disclose information in accordance with national laws and regulations. It is also necessary for civil organizations to strengthen communication and build and improve communication platform for stakeholders.

From a wider perspective, government departments, financial institutions, non-financial enterprises, and civil organizations should strengthen communication and cooperation amongst themselves regarding how to reduce the environmental and social impacts of projects. These groups should jointly promote the establishment of a global investment and financing model with minimum ecological footprint and realize global, sustainable development goals.

China's Ministry of Finance, National Development and Reform Commission, Ministry of Environmental Protection, China Banking Regulatory Commission, China Securities Regulatory Commission, and China Insurance Regulatory Commission have jointly issued the "Guidance on Building a Green Financial System,"[77] which has been included in China's "13th Five-Year Plan." The guidance aims at providing institutional support for improvements in environmental quality and has made Chinese commitments made during the G20 more substantial. As an important method of financing support for the BRI, Chinese financial institutions are expected to drive green construction and lead a low-carbon path along the BRI. The China-led AIIB and China-initiated BRICS Bank will play important role in global financial governance and the promotion of global sustainable development.

77 Source : http://politics.people.com.cn/n1/2016/0901/c1001-28682534.html

Appendix: Expert Opinions (excerpt)

The project team interviewed experts from the legal, banking, and academic fields as well as civil organizations and financial regulatory authorities on how to carry out responsible investment and financing as well as green leadership in China.

Experts interviewed from governmental departments believe that environmental protection and social development should be emphasized in both the BRI and China's "going global" strategy. An expert from the Ministry of Environmental Protection stated that local enterprises and private enterprises make up the bulk of China's overseas investors. Having local and private enterprises as China's main overseas investment projects has resulted in potential risks and difficulties: some enterprises seek economic gains while lacking awareness in corporate responsibility and environmental protection; enterprises operating with insufficient research on local laws, regulations, customs, and culture; neglecting public relations and information disclosure. Therefore, in order to better serve enterprises, the government needs to improve the systems it uses to understand the needs of enterprises that participate in overseas investments rather than simply issuing guidelines for these enterprises to follow. The government must build environmental protection platforms and systems and improving laws, regulations, and related systems of evaluation. The government should also strengthen systems for overseas investment including relevant business training and information and decision-making support. As the process of overseas investing becomes longer, it is important to keep up to date with relevant changes in environmental law. An expert from the National Center for Strategic Studies on International Climate Change and International Cooperation, believes that financial institutions should clearly define the interests of stakeholders and participate in more comprehensive communication in future cooperation along the BRI.

Banking experts also reiterated the importance of environmental and social risk management for financial institutions and stressed the urgency for improving national policies. Through interviews, we can see that China's domestic banks are improving their environmental and social policies, but information disclosure is still insufficient.

The "Green Credit Guidelines" issued by CBRC and the "Green Credit Evaluation Index" released thereafter provided the CDB with a set of stringent standards on how to control environmental and social risks in domestic and overseas infrastructure businesses. According to recent proposals made by various social organizations for overseas projects, the CDB is improving its system including adding environmental and social risk requirements in the due diligence stage, further clarifying requirements in fund allocation, project approval, and post-loan supervision. In terms of future steps, the CDB will continue to work with countries and, through knowledge gained from experiences in those countries, the CBD will meet and improve the host country's environmental and social risk management requirements.

As one of the major banks to support China's "going global" initiative and the BRI, the Import-Export Bank strongly supported the construction of railways, highways, ports, and other infrastructural projects along BRI. An expert from the EIBC, responsible for banking businesses, elaborated on the EIBC's sustainability policy from the perspective of "targeted poverty alleviation". "Targeted poverty alleviation" can be understood as three steps to finance sustainable infrastructure construction projects: identification, targeted support, and precise management. Precise management means that a bank not only has a separate system to review and grant loans, but must also produce a corresponding EIA report, economic feasibility analysis report, and must introduce an independent third-party advisory body to provide advice for the project. The approval process is also managed by an independent project review committee. After the loan is granted, the bank will also manage the loans according to project process to ensure that it is environmentally and socially sustainable.

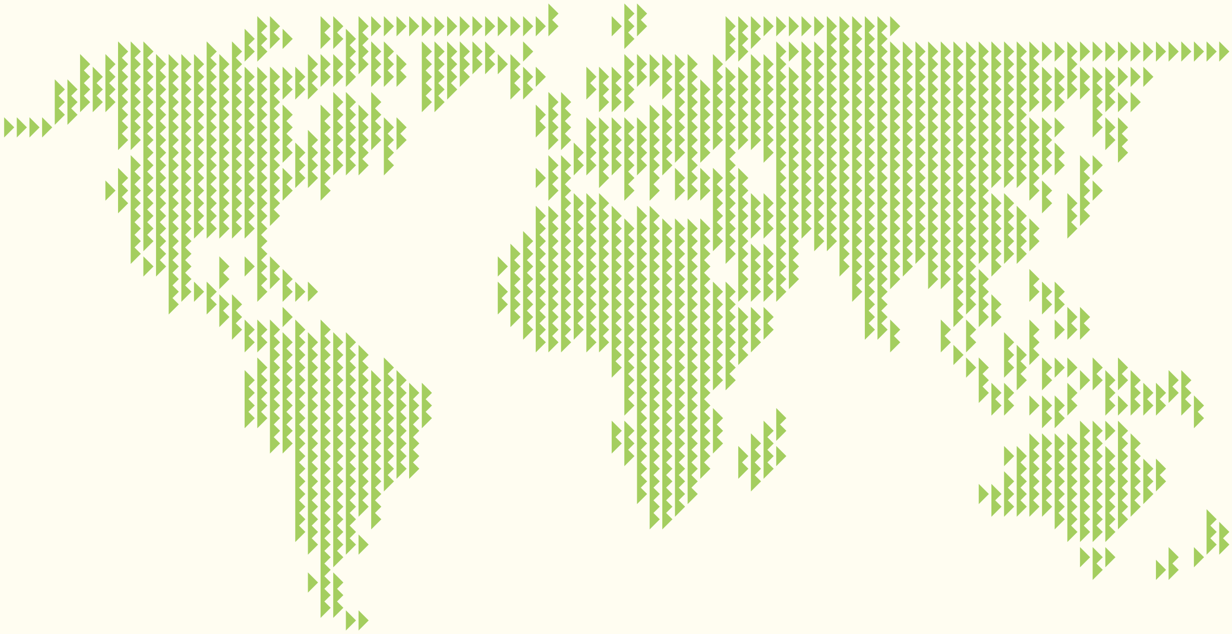
In addition, the banking industry realizes the importance of understanding a host country's national system. An expert from a Chinese state-owned commercial bank said that banks do face many issues in "going global", but the primary concern is first the country risk, then the social risk, and the lastly the environmental risk. According to the expert, first and foremost the banks are not familiar with specific laws and regulations including systems and local regulatory requirements. One of the reasons is that these banks cannot apply domestic regulatory and credit assessment mechanisms when operating relevant businesses in countries where investments are allocated. The credit evaluation system of Chinese banks is only applicable to domestic enterprises and lacks experience in handling overseas institutions and projects. Therefore, the banks should enhance their understanding of these projects, the host countries and these countries' customs. Banks should also be forward-looking when designing their projects. In terms of long term investment, commercial banks, regulators and third-party agencies can work together to make China's "going global" initiative go farther and operate better. Meanwhile, commercial banks also need to take full account of investment risks, not only market risk, operational risk, interest rate risk, legal compliance risk, and other traditional risks, but also risks associated with specific countries in the BRI including political, social, ethnic, religious, environmental, climate, and even risks related to war.

An expert also suggested that foreign exchange policy research should be included in the research agenda of the BRI, because foreign investment and financing activities are highly-correlated. However, policy research needs to be consistent due to changes in foreign exchange policy each year.

Meanwhile, the banking industry also proposed that third-party agencies cooperate in risk control management. Financial institutions will face greater risks when "going global", so these financial entities need third-party institutions, including legal professional services agencies, for effective risk control. Combined with the banks' own credit risk control, this will ensure a smoother business operation. In overseas investment, it is necessary to integrate scientific and rationalized processes into green system building and to carry out due diligence with third-party certification or verification organizations to evaluate the rationality of project and to mobilize the public in playing a supervisory role.

Foreign banks pay more attention to information and policy disclosure by relevant departments. On the one hand, the BRI brings more business opportunities for foreign banks as they have many branches in Southeast Asia, with India and Indonesia under investment outreach. Therefore, foreign banks' understanding of the local community serves as a reference for risk assessment. On the other hand, risk assessment involves three levels of laws and regulations, which would potentially be confusing for private enterprises and financial institutions, especially foreign financial institutions. It's expected that relevant departments and research institutions would share more information and have risks disclosed, not only focusing on standards and documents, but also on practical cases, so that financial institutions can learn more and better manage risks.

Academic institutions made recommendations on system building for the AIIB and BRICS Bank. There are differences between the environmental and social risk management policies under the AIIB and BRICS Bank as opposed to those of the World Bank .This can be attributed to the different mindsets of respective the population breakdown of the overall member states. The AIIB and BRICS Bank are populated mostly by developing countries while World Bank is dominated by developed countries. Under the World Bank model, shareholders and borrowers are completely separate with one party providing the standards and the other adopting the standard. The AIIB and BRICS Bank operates under a different model in which a country is both a lender and a borrower. At the same time, standards applied to the borrowers are made through joint discussion instead of by a single party. From studies to date, a lot of valuable ideas are worth being applied to practices that are continually being improved. Applying the World Bank model mechanically will limit our thoughts and practices. Therefore, the BRICS Bank and the AIIB should consider environmental and social risk management frameworks from the perspective of developing countries and balance developmental demands with social and environmental needs.



Greenovation Hub

Greenovation Hub is a grass-root environmental NGO with a global outlook. G:HUB believes development should be ecological, and only by collaborative effort can environmental problems be solved. We provide innovative tools to enable wider public participation in environmental protection and foster joint power of civil society, business and government to accelerate China's green transition.

G:HUB Policy Centre promotes the development and implementation of sound climate-and environmental-friendly policies through conducting in-depth analysis and research, as well as fostering dialogue among stakeholders, to drive China's green transition towards a sustainable, equitable and resilient future, contributing to the reduction of global ecological footprint.

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