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Influence of Sustainability on Regulation and Credit Risk Management among Commercial Banks in Kenya

By Lilian K. Nyamongo

Abstract

This paper assesses the influence of sustainability on regulation and credit risk management among commercial banks in Kenya. Drawing from the concepts of risk and sustainable banking and the market signaling theory, primary data through questionnaires was collected supplemented by secondary data available from the banks' annual and sustainability reports on their respective sites. The study has shown that commercial banks in Kenya have embraced different attitudes and are at different stages in embedding sustainability in the credit risk management systems. The study has also confirmed that most banks are taking the precautionary approach in their credit risk assessment process by ensuring they meet the minimum legal requirements. It has become quite clear that they are meeting the required reporting requirements by the regulator but very few have embedded sustainability reporting as part of their standard financial reporting.

Key Words: *Green Credit, Sustainability, Kenya*

1.0 Introduction

In his 2016 speech, Bank of England Governor and G20 Financial Stability Board Chairman Mark Carney noted that there is a growing consensus that climate change is unequivocal. There is mounting evidence on the role of human activity in increasing the greenhouse gas (GHG) emissions, the leading cause of global warming since mid-20th century.

Hence, he referred to climate change as the tragedy of the horizon- the impact of climate change will impose costs on future generation that the current generation is not directly incentivized to fix. These costs exceed business cycles, political cycles and horizon of technocratic authorities like central banks who are bound by mandates (Carney, 2016)

Climate change and by extension environmental sustainability affect financial stability through three broad channels. First, physical risks that affects today's insurance liabilities and the value of financial assets that from climate-and weather-related events such as floods and storms. Second, liability risks whose impacts could arise in the future if the parties who have suffered losses seek compensation from those responsible Third, transition risks could arise from the process of shifting towards a lower-carbon economy. Changes in policy, technology and physical risks could prompt a reassessment of the value of a large range of assets as costs and opportunities become apparent (Carney, 2016).

For a developing country like Kenya, integrating climate and environmental risks into financial decision making is crucial to long-term investment as these risks affect return on investments at various levels (Buhr et al, 2018). The impact of natural disasters is magnified by structural factors (weak adaptation capacity, high share of rain-fed agriculture in GDP, high levels of absolute poverty and limited financial sector development) that limit the countries' capacity to respond adequately and develop resilience. Climate change further exacerbates these challenges and impedes efforts towards attaining the sustainable development goals (IMF, 2016).

National governments, financial policymakers and regulators have acknowledged these issues and begun to embrace various policies and measures to promote green and sustainable finance. McDaniels and Robins (2018) identify the key trends in greening regulation (see Box 1) and predict that there will be increased measures to link financial regulation and sustainability factors. Their study differentiates between developed and developing countries without providing country-specific information. Therefore, this paper aims to provide a more country-specific information on the links between green policies and the financial system.

Box 1: Current trends in Greening Financial Regulation

- **Globally, the number of sustainable finance measures has doubled:** Between the end of 2013 and the end of 2017, we estimate that the number of sub-national and national-level policy and regulatory measures doubled from 131 in 43 jurisdictions to 267 in 53 jurisdictions.
- **International measures to promote sustainable finance have quadrupled:** In 2013, there were just eight international measures to incorporate sustainability into the international rules of the game for finance. By the end of 2017, these had grown to 33, with notable examples including the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD), the G20's Sustainable Finance Study Group and the Sustainable Insurance Forum (SIF).
- **Developed and developing countries have different priorities:** Developed countries have consistently accounted for the majority of measures, with just under two thirds in 2017. The different structures of respective financial systems are reflected in the measures that these countries adopt: in the developed world, the focus is on investment followed by securities, while in the developing world, banking is in the vanguard followed by securities.
- **Europe and Asia account for nearly two thirds of the measures:** Europe and Asia account for 62% of the measures introduced to date.
- **The sectoral pattern has changed significantly:** In 2013, measures taken in securities markets led the way with just under a third of the total, followed by investment, banking, insurance and system-wide actions (such as national roadmaps). By 2017, system-level measures had become the most significant at over a quarter of the total, up from just 10% in 2013.
- **Slightly less than half of measures (44%) are mandatory in nature:** Roughly half of the measures taken by developing countries are mandatory, with developed countries making 42% of their measures binding on affected financial institutions. These are followed by voluntary compliance, hybrid measures and measures without stipulations for compliance.

Banks' role as financial intermediaries gives rise to implicit social contracts which requires an element of corporate responsibility in terms of the process by which the services emerge as a solution to consumers' problems (Decker 2004; Krasodomska 2015; Lauesen 2013). The credit market is characterised by transactions, a set of promises exchanged by the lenders and borrowers in the presence of information asymmetry. Therefore, banks have the implicit responsibility for the nature of financial advice and prudent management of customer funds through the "know your customer" (KYC) requirements (Decker, 2004). However, 2007-8 global credit crunch was the clarion call for the financial services industry to re-write "the rules of the game" and renew its professional purpose towards long-termism (Robins and Krosinky, 2009)

Though the Kenyan banking industry was only slightly scathed by the financial crisis, it has faced a number of its own internal challenges in the bid to reach its developmental aspirations. Globalisation and information dissemination has seen the structure of the banking public becoming more complex especially with increased customer awareness (Achua, 2008). Innovation among traditional and unconventional financial services providers as well as the asymmetric credit regime introduced by the Banking (Amendment) Act 2016 has led to the decline in differentiating factors. In order to remain competitive with a long-term business view, banks have to distinguish themselves through value addition, build their reputational capital while attenuating potential risks. Moreover, banks are more vigilant in credit risk assessment to curb to the growth of non-performing loans (NPLs). Nonetheless, this has seen a decline in the growth of private sector credit which has led to increased financial exclusion.

Commercial banks can bridge the credit gap through sustainable lending, extending credit to borrowers who account for the environmental, social and governance (ESG) impacts of their operations (Calderon and Chang, 2014). Though most financial institutions are cognizant of the importance of sustainable banking; most have taken the piecemeal approach to implement sustainability policies and practices that require minimum resources and commitments. While those that have been embedding it to their credit functions tend to investigate ESG issues only at the loan application stage (Calderon and Chang, 2014). Therefore, banks have not fully played their role in the market mechanism to influence MSMEs to implement environmentally friendly and socially responsible practices throughout the loan tenors. Though regulation such as Basel III is said to bringing back a sense of prudence through corporate governance, mechanisms, some practitioners are skeptical about these superficial changes until the occurrence of the major business scandal or environmental disaster (Lenssen et al 2014).

By using data mining tools, commercial banks can further tailor their credit products towards sustainable lending and subsequently collate the information for financial and sustainability disclosures to court

further sustainability-specific potential funding opportunities. It should be noted that banks and other financial institutions have not been absent in revealing their non-financial performance, however they were not reporting their activities in a way that would raise alarm over their "normalized" practices and little ESG impact (Lauesen, 2013). Understanding the role of sustainability performance in assessing credit eligibility will enable the formation of sector specific guidelines for borrowers especially in agriculture, energy and petroleum and manufacturing that are key in the delivery of the government's big four agenda. Banks and other financiers may offer limited products across the enterprise life cycle (e.g. early stage) and focus on specific opportunities. There is lack of awareness and technical expertise by both financiers and MSMEs about sustainability issues as means to lower costs and increase competitiveness (UNEP Inquiry, 2017). For practical considerations, this study focuses on environmental sustainability. Though social and governance aspects will be worth investigating in future.

1.2 Problem Statement

There is growing literature that links the importance of embedding sustainability into credit risk management in developing countries including Nigeria and South Africa but with scanty information on Kenya (Weber et al 2010; Mengze and Wei 2015; Weber et al 2015; UNEPFI-ATF 2007; Hu and Scholtens 2014). Studies that have published about sustainability have focused more on its corporate social responsibility (CSR), corporate governance and its linkages with financial performance and institutional dynamics in the Kenyan outside of the banking context (Muthuri and Gilbert 2011; Tarus 2015). In addition, the majority of the studies have shown the link between project finance and sustainable lending but with little focus on how the extent to which ESG features in the credit assessment policies. Many banks now integrate Equator Principles into their project finance as a framework for environmental and social risks but are yet to integrate them into sustainability into more widespread credit products (Zeidan et al 2014). Recent research by Kariuki (2015) has demonstrated that Kenyan banks have adopted sustainability programs as well as embraced the Kenya Sustainable Finance Guiding Principles. The emerging question is whether the commercial banks are implementing their commitments over their rhetoric.

1.3 Key Hypotheses

Based on the research motivation, conceptual and theoretical frameworks, this research will test the following hypotheses:

- Commercial banks in Kenya have embraced different attitudes or at different stages in embedding sustainability policies in the business models
- Most banks take the precautionary approach in their assessment process by meeting the minimum legal requirements.

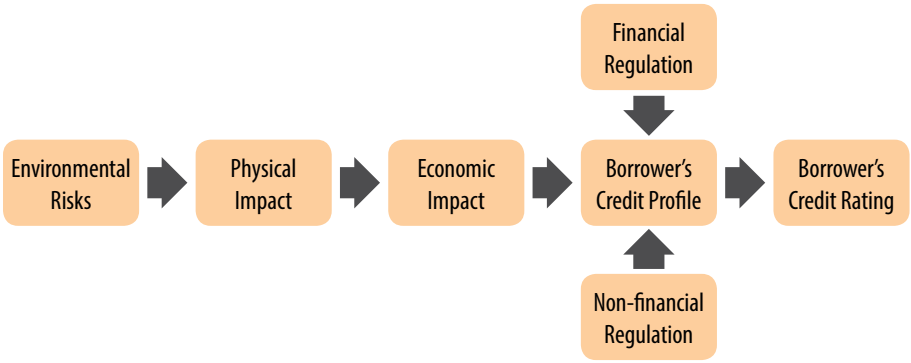
- Most banks are meeting the minimum sustainability requirements in their reporting.

1.4 Organization of the Study

This study is structure as follows. Section 2 the conceptual framework illustrating the nexus between financial regulation, sustainability practices and credit management. Section 3 provides the theoretical framework. In Section 4 the literature review is presented and in Section 5 and 6 the study findings and conclusion are discussed.

2.0 Conceptual Framework

Figure 2: Linking Sustainability, Regulation and Credit Risk Management



The effects of physical climate change are transmitted through four primary channels to borrowers' credit profiles: first, the potential economic impact such as lower economic activity due to decreased agricultural production. Second, destruction of infrastructure caused by climate shocks. Third, rising social costs caused by health crisis or food security concerns. Lastly, population shifts resulting from displacement resulting from climate change. These mean that the borrowers will not be able to meet their debt obligations and taint their credit profiles.

Emerging sustainability issues particularly from the environment necessitates the formulation of both financial regulation and non-financial regulation. Sustainability policies are embedded to already existing policies to mitigate physical, liability and transitional risks by guiding financial service providers in their credit disbursements. Non-financial regulation are policies and regulations that apply to other industries but have credit implications. In the current interest rate cap regulatory regime, new borrowers will not be able to readily access bank credit due to the stringent credit policies. This in turn lead borrowers to seek alternative sources of financing.

2.1 Definition of Terms

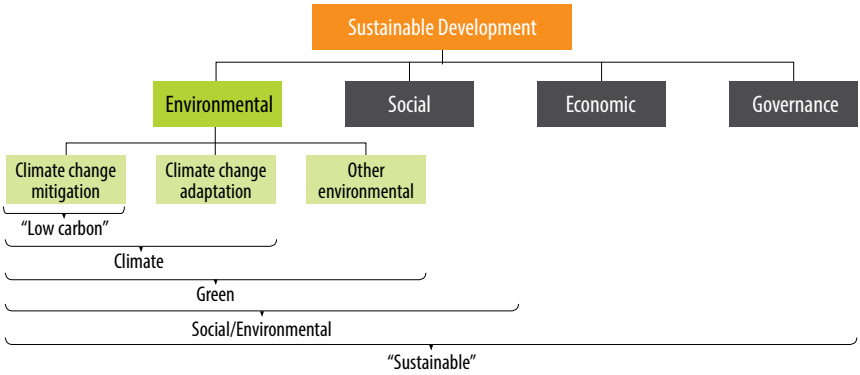
2.1.1 Sustainability

The term "sustainability" has overlapping and slightly confusing meanings. For International Finance Corporation (IFC, 2007), it is about ensuring long-term business success while contributing towards economic and social development, a healthy environment and a stable society. When applied to financial institutions, this definition of sustainability encompasses four dimensions of good business performance:

- **Financial:** longevity of financial institutions and its clients so that they continue to contribute to national development
- **Economic:** longevity of projects and companies financed by financial institutions through their contribution to host economies
- **Environmental:** preservation of natural resources
- **Social:** improved living standards, poverty reduction, community welfare and respect for key human rights

This means that financial institutions ought that ensure that they provide financial capital and risk management products to projects that promote economic prosperity, environmental protection and social protection. Bouma, Jeucken and Klinkers (2001 in IFC 2007) support this notion noting that banks can be labelled as sustainable when their products and services take into consideration environmental and social impacts of their customers' activities. Therefore, environmental sustainability has two components: managing risks and identifying opportunities for product development. This paper will focus on the environmental dimension of sustainability and therefore considers environmental, social and governance issues where they are directly related to environmental factors.

Figure 3: Clarifying Sustainable Finance



Source, McDaniels and Robins (2018)

2.1.2 Sustainability Risk and Criteria

Sustainability risks contributes to the credit risk of a financial institution directly, indirectly or by affecting its reputation. Direct risk may involve a firm incurring direct liability such cleaning up contamination after an insolvent borrower. Indirect risk may be incurred when the borrower engages in an activity that damages the borrower's ability to repay loans and is reduced to financial penalties impairing its profitability and cash flows. A bank's reputation may be marred when it is seen to be financing firms that are not in compliance with the law (Mengze and Wei, 2015).

Sustainability criteria can be broadly defined as the standards and indicators on specific sustainability issues such as biodiversity, climate change, labour rights, human rights and social justice. (van Gelder and Stichele, 2011). Its application varies by industry and national context. In the financial services industry, they need to be formulated to a give clear direction on how to avoid environmental consequences of their investments. They should also indicate how they can focus on investments that contribute to environmental sustainability and social justice (van Gelder and Stichele, 2011). In reaching the final lending decision, bankers should not be seen as surrogate environmental regulators. But they should at least be informed of the key environmental business drivers and how they translate to the appropriate benchmarks and thresholds. Therefore, liaising with environmental specialists will enrich their business decisions (Bray, 2003).

2.1.3 Regulation

Generally, regulations are laws or orders prescribed by an authority such as governments to control behavior or activities within a given jurisdiction. Baldwin et al (2012) claims that motives for passing regulation can be differentiated from their technical justifications. Governments as the ultimate regulators may regulate for several motives including being influenced by the economically powerful to act in the interests of the regulated industry or to ensure a particular stance in order to be re-elected (Baldwin et al 2012; Beare et al 2014).

Market failures are normally perceived as instigators for the various rationales for regulation. However, they are not sufficient to justify the range of regulatory activities that are commonly undertaken, and they would also need to be anchored on rights and social based rationales (Baldwin et al, 2012). Beare at al (2014) suggested that governments are increasingly being seen as sustainability drivers by enacting policies and regulations to encourage responsible behavior for business. Through the multi-stakeholder approach, they have called for increased corporate accountability by either passing legislation or by supporting voluntary disclosures. Governments can use multiple policies to address sustainability issues. In addition to legislation, Prakash and Kollman (2004) in Beare et al (2014) identified five environmental policy categories: Command and control, Market-based, Information disclosures, business-government

partnerships, private voluntary codes. Sustainability public policy may be subtler and more due to cultural norms. For instance, Swedish state-owned firms disclose more sustainability information than private companies which was attributed to the Swedish tradition for transparency in the public sector. In addition, sustainability agendas, vary from country to country (Beare et al 2014)

2.1.4 Financial Regulation

Finance performs four main functions in society and the economy-the payments systems, matching borrowers and lenders, managing personal finances across lifetimes and generations and controlling risk. The utility of financial innovation is measured by the degree to which it advances these goals (Kay, 2016). By granting and/or withholding credits, commercial banks play an important role in the development of the real economy and its regulation. Financial regulation ensures that the banking industry performs its social function in an optimal manner (van Gelder and Stichele, 2011). Goodhart (2010) argues that regulation should focus on two issues contagion and consumer protection. Information asymmetry makes it difficult to obtain information that would increase vulnerability of both the financial institutions and its depositors. Externalities or market spillovers caused by the actions of one or more individuals especially systemically important banks may not be captured by the market pricing mechanisms. Some commercial banks may exert dominant power or monopolies and have the ability to exploit their market power.

The financing gap for the sustainability ventures remain wide particularly after the credit crunch of 2007/8. The situation is further exacerbated by that traditional financiers like commercial banks shy away from these ventures due to high risks despite also having high ESG impact. Financial innovation and technology fuelled the emergence and mainstreaming of social finance-alternative lending and investment approaches that generate both ESG and finance returns such as crowdfunding and cryptocurrency (Rizzi et al 2018; Khalamayzer 2017). Nonetheless, efforts to increase financial stability will not be sufficient to evade future financial crises if they contradict ESG principles. Risk management is conducted case by case and uncertain in the outcome (van Gelder and Stichele, 2011). Regulation in the banking industry fall into prudential and conduct of business categories. Other forms of regulations stem from these two main categories such as consumer protection, safety and soundness, credit allocation.

2.1.5 Prudential Guidelines

Prudential regulations ensure stability of financial institutions by safeguarding capital and liquidity adequacies as well as risk management. Integrating a sustainability criterial will strengthen their credit risk management by reducing their liability risks and avoiding reputational risks. After the financial meltdown in 2007/8, the Basel Committee introduced Basel III reforms to bolster the industry. However, some have questioned whether these reforms take into consideration systemic environmental risks. On one hand, some argue that lowering capital and

liquidity requirements would encourage sustainability financing. After interviewing banking regulators in China, Brazil and Peru found that Pillar 1 has marginal impact on the financing of environmental sustainability issues, Banks were more likely to issue credit for green initiatives based political and economic considerations. Nonetheless, some countries Like China, Brazil and Peru have incorporated various initiatives into the macro prudential framework.

2.1.6 Conduct of Business Regulation

The conduct of business regulations ensure that the financial institutions conduct business with their customers in a fair, transparent and honest way for both the internal and external stakeholders. Financial regulation will prevent financial institutions from making misleading claims such as greenwashing by fully informing their customers of their product specifications to avoid mis-selling. Banks are required not only required to offer fair interest rates but also be transparent in their investments. In response, financial institutions are developing sustainable policies and publishing their sustainability disclosures. The quality and implementation of these practices may be thorough or limited to a very specific niche market. In our digital world, customers are more conversant with their consumer rights and boycott organisations that support controversial weapons, polluting the environment and employing child labour.

2.1.7 Non-Financial Regulation

Since the adoption of the sustainable development goals, many governments have embedded sustainability into their constitution and subsequently the national policy frameworks. These have propelled policy innovations in various sectors and have indirectly been used by financial service providers in allocating credit. As highlighted in preceding sections, banks' carbon footprints are physically related to their customers which historically has been a bone of contention with policymakers. However, governments are now shifting their focus on the banks' intermediary role in the achievement of environmental policies (Jeucken and Bouma, 1999).

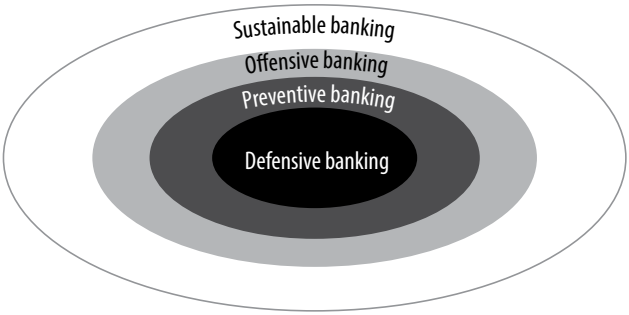
3.0 Theoretical Framework

3.1 Sustainable Banking

Jeucken and Bouma (1999) posit that in addition to their financial intermediary role, banks act as risk assessors. They are more equipped to analyse risk than other industries as they collect borrower information over time to mitigate information asymmetry.

In this unique positon, they are able gather information inaccessible to outsiders and play a key role in determining whether certain clientele will receive additional future financing (Calderon and Chong, 2014). However, due to their critical position in developing economies, banks are more likely to spread risk of a larger scale. It is their risk attitude that determines their sustainability actions. Hence, Jeucken and Bouma (1999) identified four typologies with: in defensive banking, banks are not keen to take action, or they lag in adopting any sustainability initiative to support environmental legislation. In the second stage, preventive, they implement simple internal measures such as environmental due diligence in their credit risk assessment. In the offensive banking stage, banks implement both internal and external measures that promote the environment. Finally, the sustainable banking involves engaging in borrowing and lending operations that are not detrimental to the environment while maintaining ESG values.

Figure 4: Typology of Banking and Sustainable Development. Source, Jeucken and Bouma (1999)



According to UNEP-FI (2005), sustainability banking in Africa is on the rise due to a number of drivers. Regulatory requirements are making banks and investors liable for their ESG impacts and are creating incentives to incorporate sustainability into risk assessments. The expansion of international standards, guidelines and corporate governance codes has compelled financial institutions to recognize that they are not independent from the society and environment that they operate in. In turn, their stakeholders demand greater transparency and disclosures, knowing that external pressures can affect their financial viability. They are also cognizant of the potential for competitive advantage through product innovation to increase new market opportunities.

Research shows that financial institutions are more cognizant of the importance of environmental sustainability. However, their hodge-podge implementation at different levels may have been influenced by ambiguity and diversity of definitions and standards in the sustainability realm (Perez-Lopez et al 2015; Beare et al 2014), cultural factors (Bouvain et al 2013), lack of resources and data (UNEP Inquiry, 2017).

Macroeconomic factors have also contributed greatly. Prevailing evidence suggests a significant role for financial intermediation in mitigating the adverse economic costs of natural disasters. Disasters cause systemic losses that tend to increase demand for investment- as the absolute level of physical capital falls its marginal product rises. Among other factors, it has been found that recovery is positively influenced by the size of the local credit markets but unaffected by stock markets, suggesting that financing for households and MSMEs may be particularly important for facilitating recovery (Collier, 2014).

Political risks such as terrorism and civil strife may impede daily bank operations which deters both local and international investors. The regulatory framework, which will be discussed further below, will enable or discourage product development. The government's capacity should to enforce laws has been considered weak in various African countries. As discussed above, banks possess a vantage position in conducting risk assessment, but it should also be noted that there is limited understanding of ESG risk in the financial sector. In addition, few banks have incorporated environmental management standards and best practices such as ISO 140000 into their lending policies (UNEP-FI, 2005). Therefore, this study will aim to assess the extent to which commercial banks in Kenya have been able to tailor sustainability policies and practices to their credit risk management systems.

3.2 Credit Risk Management

Credit risk management is the process of attempting to limit default risk by those owing money to banks. Bank credit is known to be traditional risk averse and it would seem natural that banks would consistently integrate ESG issues in their policies to protect their value and minimise risks. In any case, the overriding objective of credit risk management is to avoid bad

debt (UNEPFI-AFT, 2007). Bank officials, more so credit and loan officers are gatekeepers to the capital. Adopting sustainability criteria enables credit officials to be more thorough in the vetting process and shield the financial institutions' reputation. (UNEPFI-AFT, 2007). Commercial banks tailor their credit risk policies, processes and methods following with guidance from external regulators such as the central banks and national laws. In addition, financial institutions are increasingly incorporating ESG screening procedures before they approve and disburse credit to their clients so that they can protect their own interests as well as their clients.

4.0 LITERATURE REVIEW

4.1 Rationale for Sustainable Banking

The main focus of the sustainable banking has been big-ticket projects (Weber and Acheta, 2016). But in order for to address the challenges of climate change, it would be imperative to have all sectors on board.

Collier (2014) found that literature has four main documented findings on credit access among MSMEs in developing countries. First, they tend to be informationally opaque and vulnerable to significant risk. Second, lending to MSMEs motivates financial service providers to specialise whether in terms of geography or product offerings. Third, lending to MSMEs increases capital market frictions for financial intermediaries. Due to information scarcity in the MSME sector, their asset portfolios are difficult to value and this motivates investors to fund financial intermediaries with fixed income liabilities. This has created strong preferences for debt instruments and given rise specialised segments like impact investing that is heavily expanding in under developing markets. Lastly, the challenge of supervising MSME lenders motivates a strong reliance on minimum capital requirements.

He further argues that while MSMEs contribute substantially to developing economies, they remain the most difficult credit market for lenders to reach. Formal SMEs account for approximately 45% of the manufacturing labour force and 30% of GDP in developing countries. About 50% of MSMEs in developing countries identify access to financial services as an operational constraint and 40% report on having any access to credit from a financial institution. These developing countries market gap is over USD 2 trillion (Collier, 2014).

4.2 The Need for Sustainable Banking in Kenya

Kariuki (2015) draws our attention to numerous drivers of sustainable finance in Kenya. First, banks offer large-scale finance need to avoid reputational risks. Second, investment portfolios can be negatively affected when projects do not undergo ESG screening. Third, sustainable finance provides banks with the opportunity to

develop innovative products. Fourth, banks adopt ESG standards in order to access finance from development financial institutions.

Figure 6: Drivers for Banks to Adopt Sustainable Finance Practices

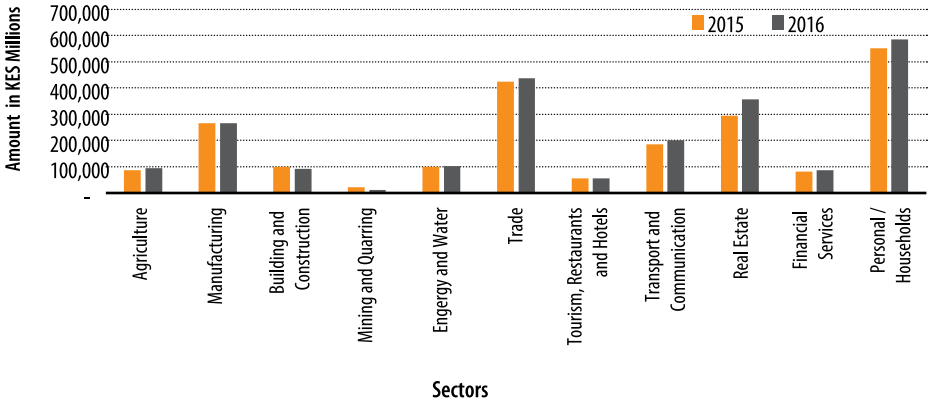
Source: KBA SFI Needs Assessment Report, 2014.

*The survey assessed 12 Commercial Banks, ranging from large multinationals to a local microfinance.

Commercial banks are the main source of finance in the Kenyan economy (See Chart 1 below). Notably, agriculture, mining & quarrying, tourism, energy & water received the lowest shares in terms of credit. Additionally, MSMEs in Kenya play a pivotal role in the Kenyan economy as they comprise 33.8% of all businesses in the country (KNBS, 2017). Hence reducing their environmental impact of the MSMEs is crucial both in manufacturing sector and in the greening of the economy. Their willingness and capability to adopt MSME sustainable practices and seize green opportunities relates to resource constraints, skills deficit and knowledge limitations. Their lack of resources often makes them risk-averse and less willing to embrace and invest sustainable projects, because of the uncertainty about the payback period (UNEP Inquiry, 2017).

Most financiers have shied away from financing rain-dependent projects especially in the agricultural sector as they are more likely to result in low returns. On the other hand, real estate sector has maintained over 13% share of gross loans over the two years which should propel financiers to embed sustainability screening methods to shield themselves from loan defaults. Hence it is imperative that they implement both financial and non –financial regulation to reap the benefits of sustainable finance.

Chart 1: Sectoral Distribution of Gross Loans 2015 & 2016 Source: CBK Bank Supervision Reports



4.3 Regulation

The economic environment has been challenged by ESG issues that have forced central banks across the world to reassess their conventional roles. However, little has been done to address these risks despite the material risks that they pose for real economies and financial stability. (UNEP-FI, 2017). International banking guidelines such as the Basel Accord are yet to include environmental guidelines in their frameworks. Hence, sustainability related guidelines and regulations have remained at national discretion.

Table 2: Examples of Environmental/Social Measures by National Banking Regulators (Alexander, 2015)

Country	Date	Measures	Drivers
Brazil	2014	Mandatory regulation (Resolution N.4.327) issued by the Central Bank of Brazil (BACEN), requiring the establishment of social and environmental responsibility policies (including on the management of environmental risks).	Catering to the impact of socio-environmental risks on financial system efficiency and stability.
China	2007	Mandatory regulation(Green Credit Policy - GCP) issued by the China Banking Regulatory Commission (CBRC), covering: environmental and social risk management structures, information disclosure.	Addressing community concerns by limiting finance for high pollution, high resource use sectors.
Peru	2015	Mandatory regulation (Resolution 1928) released by Superintendence of Banks, Insurance and Pension Funds (SBS), covering environmental & social risk management.	Avoiding spill-over effects linked to the externalities created by major projects.
UK	2014	Banking of England One Bank Research Programme, including climate change as a fundamental driver of change that could affect economic and financial stability, covering the physical impacts of public policy, technological and other drivers of innovation that could 'strand' carbon-intensive assets.	Better understanding of the potential consequences of climate change on the financial system.

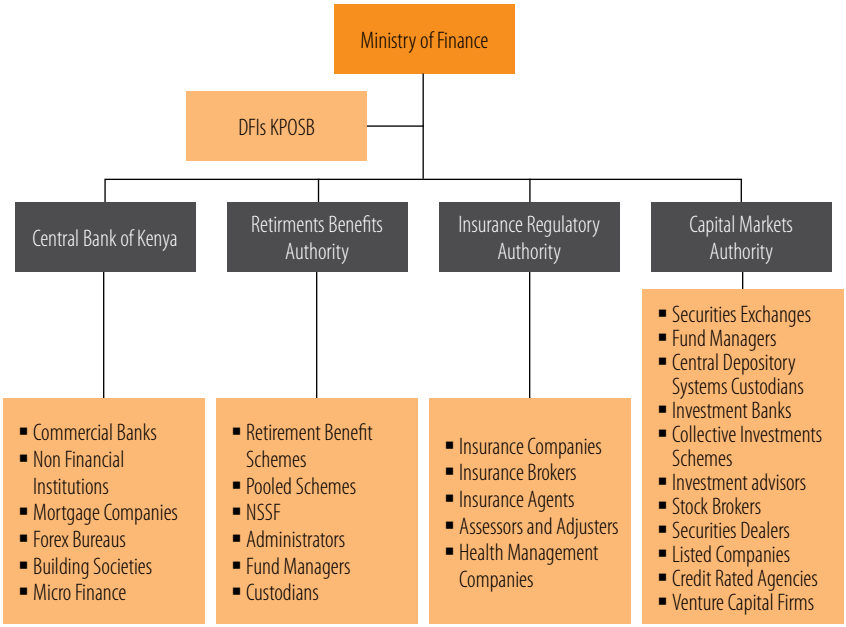
4.4 Financial Sector Sustainability Codes of Conduct

It has been noted that the financial sector has the one of the highest frequency of codes of conduct. The most renown ones include UNEP Financial Initiative, UN Principles for Responsible Investment and the Equator Principles for project finance (Weber et al 2016) The Global Alliance for Banking Values (GABV) was recently introduced which highlights on the positive sustainability impacts on financial institutions. Their strengths and weaknesses of these voluntary codes are discussed on the basis of the conducts themselves, leaving out the actual impact on sustainability performance of financial institutions (Weber et al 2016).

Kenya

Under Article 10 (2) (d) of the Kenyan Constitution, sustainable development is a national value and a principle of governance that binds every person and state organ. The Constitution further obligates all citizens to co-operate with state organs to preserve natural resources. Government organs including those in the financial services industry have adopted this national value albeit in different strides.

Figure 7: Structure of Financial Regulation in Kenya, Source Mutuku 2008



Kenya is a bank-led economy that comprises of the Central Bank of Kenya as the chief regulator of 42 Commercial banks, one mortgage finance company, 8 representative offices of foreign banks, 13 microfinance institutions, 3 credit reference bureaus, 74 forex bureaus and 19 money remittance providers. (CBK, n.d.a). The main laws governing the sector are the Constitution of Kenya 2010, the Banking Act, the Banking Amendment Act, the Companies Act, the Building Societies Act, the Prudential Guidelines of the Central Bank of Kenya and the Consumer Protection Act (2012) (CBK, n.d.b). Notably, the Central Bank of Kenya has not explicitly offered guidelines on environmental risks that are linked with monetary policy but is currently involved in various initiatives to promote environmental sustainability including the Kenya Green Bond Programme. The National Treasury acts as the manager of public funds with the mandate of formulating, implementing and formulating macroeconomic policies that involve revenue and expenditure, In addition, these macroeconomic policies should facilitate socio-economic development in conjunction with other national entities (National Treasury, n.d.).

The National Climate Change Action Plan 2013-2017 (NCCAP) was developed in 2012 by an inter-ministerial taskforce to provide a framework for the implementation of the National Climate Change Response Strategy, the 2010 Constitution, and the attainment of Vision 2030 goals. The draft National Climate Change Action Plan 2018-2022 also includes the implementation of the Green Economy Strategy and Implementation Plan (GESIP). Both NCCAP and GESIP have outlined to mobilise funding from the public and private sector in order to address climate change and related environmental challenges. The Climate Change Act of 2016 establishes the National Climate Change Fund to provide long-term finance to infrastructure developers which will be disbursed through commercial banks. NCAAP proposes the Fund to provide concessional credit lines to banks who will extend it on favourable terms and build on existing programmes (Kariuki, 2015). Banks and other financial institutions will be incentivised to adopt sustainable finance to access the Climate Change Fund and to attract additional investments from DFIs and other global climate funds.

The Kenya Bankers Association (KBA) carried a benchmark study to gauge banks' implementation of sustainability principles. The findings showed their adoption was disparate and lacked a unitary structure, which led to the industry association drilling down to their top three priorities and eventually the formulation and adoption of the Kenya Sustainable Finance Principles. In addition, KBA in association with FMO and DEG partners are conducting an industry wide sustainable finance e-learning course that has been undertaken by over 24,000 bank employees (KBA, 2017)

Figure 8: Kenya Sustainable Finance Guiding Principles Framework

Sustainable Finance Priorities

- Comprehensive Risk Management
- Business Practice, Leadership & Governance
- Growth through Inclusivity, Innovation and Technology

Sustainable Finance Guiding Principles

- Financial Returns vs Economic Viability
- Growth through Inclusivity and Innovation
- Managing and Mitigating Associated Risks
- Resource Scarcity and Choice
- Business Ethics and Values

4.5 Non-Financial Regulation

4.5.1 The Case of Netherlands

The Dutch government established national environmental targets for several sectors in the National Environmental Policy Plan (NEPP) and the National Environmental Policy Plan Plus (NEPP+) including agriculture, transport, industry and consumers in the late 1980s and early 1990s. While NEPP and NEPP+ were not laws per se, they were authoritative documents that guided all aspects of Dutch business going forward. As a result of compliance with these environmental standards, new industries emerged and evolves that specialised in environmental technologies. Under NEPP+, banks were considered indirect stakeholders in the designing environmental policies but were confronted with their customers' clean-up costs. While these financial burdens did not lead to bankruptcies, banks became offensive and created a special fund to cater for to this emerging business demographic (Jeucken and Bouma, 1999).

Again, in the NEPP+, banks were not directly involved in the voluntary agreements between governments and industry. However, when implementing the "Policy Document on Environment and Economy" a life-cycle approach has been integrated into the environmental policy in order to decrease direct involvement and increase the responsibility of the polluting target groups in reaching objectives. For the first time, commercial banks were considered as a direct player in designing environmental policy (Jeucken and Bouma, 1999). The Dutch government took up the role of promoting environmental sustainability by stimulating, facilitating, monitoring and actively coordinating using a variety of tools such as providing financial support in product development, developing an environmental information exchange system, financial instruments such as green investments, eco-labelling, exploring lifecycle methodologies and eco-indicators, green procurements and stimulating sustainable consumption. (Jeucken and Bouma, 1999).

4.5.2 The Case of Kenya

Environment-related legislature from other sectors have mandated banks to revisit their credit risk assessment and disbursement. The Environmental Management and Coordination Act of 1999 requires any person who is considering a project must apply for an environment impact assessment (EIA) licence before financing or seeking financing. Such projects include those relating to urban development, transportation, dams, mining, agriculture, manufacturing and processing industries (Kariuki, 2015). Kenyan banks are perceived to be the key source of financing for most infrastructure development projects. Hence, they are also required to ensure the enforcement of this law by incorporating it in its credit risk assessment.

The Energy (Solar Water Heating) Regulations of 2012 that was recently implemented requires all industrial, commercial and large residential buildings in urban areas to be fitted with solar water heating

systems to ease the pressure on the national grid. The law prohibits Kenya Power (KPLC) from connecting electricity to any property owners who fail to install solar panels, Moreover, a KES 1 million fine or one-year jail term will be imposed on manufacturers, vendors and contractors who fail to comply with the Energy Regulatory Commission (ERC) specifications (Omondi 2018; ERC 2018). This implies that banks will not be able to provide project loans or mortgages to clients who have not explicitly proven that they have compiled with these laws.

In the same vein, The Environment Management and Co-ordination Act 2017 led to the ban on manufacture, importation and use of plastic bags in commercial and household packaging. Knoblauch et al (2018) noted that since 1991, 51 countries and sales adopted a ban on the production, sale or use of plastics and another 39 have adopted a tax on the sale as at April 2018. In Kenya, this policy was supported by a number of factors including the fact that in 2014, the UN estimated that the natural capital cost of plastics from environmental degradation, climate change and health to be about USD 75 billion annually with 75% of the environmental costs occurring at the manufacturing stage. More recent analysis indicates the capital cost could go up to USD 139 billion (Barra and Leonard, 2018).

As part of the Climate Change Act 2016, there was a proposal for the climate change fund that has led to the Draft Public Finance Management (Climate Change Fund) Regulations 2018 that had the initial capital of Kshs 500 million for financial year 2018/9 that is yet to be disbursed. The main purpose of the climate change fund is to provide financing mechanisms to priority climate change actions and interventions. Since, the banking industry is at the core of the Kenyan economy, then it will suffice to say that the money will be channelled directly and indirectly through its system. Overall, there are conscious efforts by the national government and the legislature to prioritise environmental issues. Nonetheless, good intentions will remain intentions if funds earmarked for environmental issues are not channelled to the appropriate initiatives.

5.0 Research Findings

Primary data was collected through semi-structured questionnaires targeting heads of credit and heads of compliance from a sample of 40 banks of whom are signatories of Kenya Sustainable Finance Guiding Principles 15 banks responded.

5.1 Influences on Governance and Environmental Credit Risk Assessment

On what drives implementation of environmental credit risk assessment among banks and licensed MFIs and how it is linked to regulation. 13 out of the 15 respondent banks indicated that reputation risk management as the leading motive for conducting sustainability credit risk assessment (see Figure 9). This is closely followed by wider demand by the society that they operate in. In third position, banks seem to be motived by their desires to protect the value of their securities, reduce the default rate, transparent reporting and to meet stakeholder demands. Seven (7) banks indicated that their third-party affiliations influence their conduct on governance and environmental credit risk assessment. Most of them cited their ties to multinational and development financial institutions such as AFD, International Finance Corporation (IFC), DEG, European Investment Bank (EIB) as well as reporting frameworks such as UN Global Compact, UNEP-FI, and Global Reporting Initiative (GRI).

5.2 Policies and Structures

This second section sought to understand the policies and structures in banks that support sustainable credit risk assessment (SCRA). 11 out of the 15 (73%) banks indicated that they have an organisation wide sustainability policy. Most of them had sustainability principles embedded into their credit policy and began implementation in 2010-2016

Figure 9: Motives for Embedding Sustainability in Credit Risk Assessment

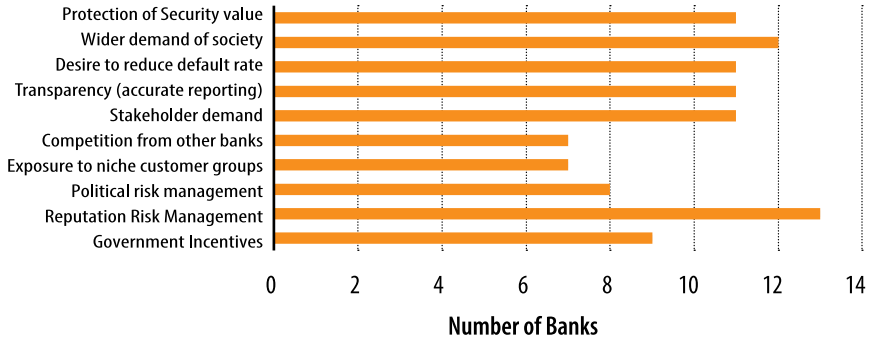


Table 3: Responsibility vs Accountability of Sustainability Policies

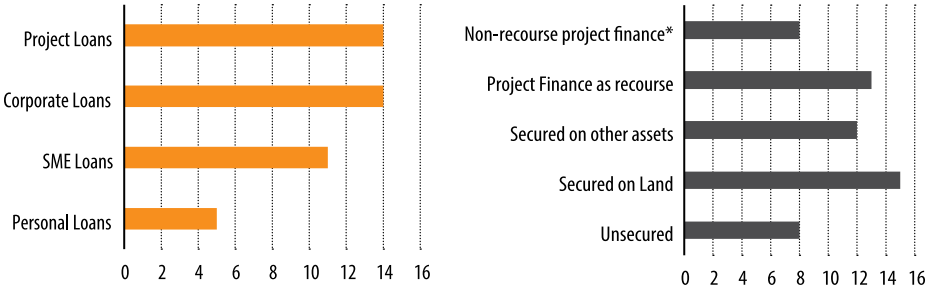
	Ultimate Responsibility	Ultimate Accountability
Board of Directors	8	5
Heads of Risk	2	1
Head of Credit		1
Heads of Both Credit and Risk		1
Designated E &S Champion or Co-ordinator	2	
Head of Corporate and Regulatory Affairs	1	
Management Team		1
CEO/MD		2
Didn't Answer	1	4
	15	**15**

Eight (8) of the respondents quoted the Board of Directors being ultimately responsible for implementing the policy while two cited the chief risk officer in their organisation. One the other hand, 5 banks stated the Board of Directors as the ones accountable for implementation of sustainability policies in their banks.

Responsibility and accountability seemed to be conflated. Responsibility is about maintenance and implementation of the ESG credit risk policy which is handled by senior credit risk officers and then cascaded to the investment officers and credit officers. Therefore, it can be delegated. On the other hand, accountability encompasses responsibility and being answerable for the organisation's actions (the buck stops with them). 10 of the 15 respondents stated that their sustainability policies were internal, proprietary documents that were not accessible to the public. 3 banks stated that their sustainability policy was available as part of their published financial statements as guided by their reporting standards such as integrated reporting. Banks seemed to apply environmental credit assessments across all their product categories but favoured corporate and project loans as compared to the SMEs and the personal loans and insurance premium finances, which some banks have concluded to be difficult to monitor. Banks seemed to favour credit applications that were secured with land and least favoured unsecured loans. This is because they are more dependable and secure form of assets as compared to other movable assets. However, it is not clear whether banks go the extra mile to secure those land and associated buildings to ensure that they are environmentally sound.

When the banks were queried about waiving their policies under certain circumstances, 2 banks indicated that the bank policies relaxed some of the policies like with personal and IPF products as well as those clients with minimal environmental risks. Conversely, 8 banks indicated that they did not relax their policies under any circumstances. 5 banks indicated that they have environmental and social-specific products; Four (4) banks indicated that they offer environmental products that support energy efficiency, clean technology and solar energy. They can impose these criteria based on their contracts with the service providers and DFIs that they are collaborating with. One bank is a fully-fledged Islamic bank argued that by default their policies support E&S credit, hence all their products are screened inherently.

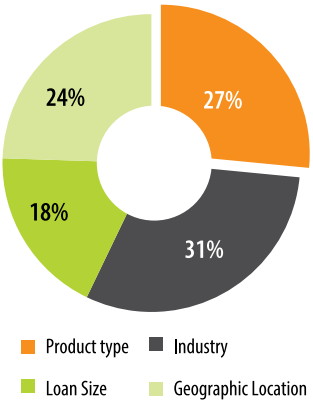
Figure 10: Credit Assessment by (a) Product Category and (b) Type of Financing



5.3 Methods of Implementing Sustainable Credit Risk Assessments

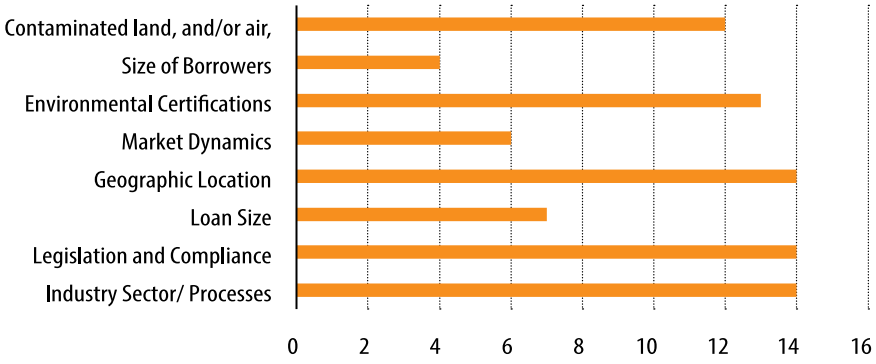
The objective of third section was to gain an understanding of how SCRA is applied within the specific organisation. Banks indicated that the leading trigger for the application of the sustainability credit risk assessment is the industry that the client is involved in (31%). This followed by the bank product that the client would like to purchase (27%) and then the geographical location (24%) of the business and lastly the loan size (18%). It is quite clear that the industry sector/processes, legislation and compliance issues and the geographical location of the business are the top priorities during sustainability credit risk analysis. These factors are closely followed by environmental certifications and then after contaminated land, and/or air, water. The least likely issue to influence sustainability credit risk analysis is the size of the borrowers.

Figure 11: Triggers for Implementing SCRA:



Banks cited the following factors as "triggers" that would establish the need to proceeds to a higher level of risk analysis: loan size and the E&S rating that the application receives above a particular amount threshold; sector approach e.g. agriculture, transport,

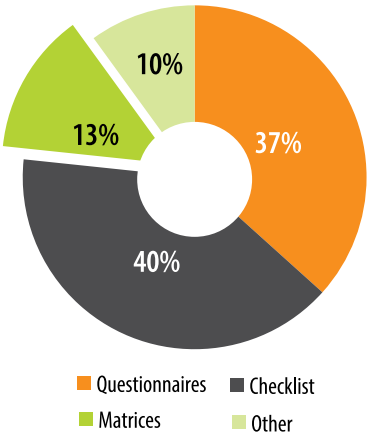
Figure 12: Priority Issues in Sustainability Credit Analysis



manufacturing, tobacco, construction, service; increased pressure from customers; NGOs and other stakeholders regarding the business relationships they pursue and the projects or companies that they provide financing to.; legislation and best practice codes locally and internationally.

40% of the respondents indicated that the most commonly used tool used in risk assessment among banks is questionnaires, closely followed by checklists. Matrices are the third most common risk assessment tools at 13% as shown in Figure 13

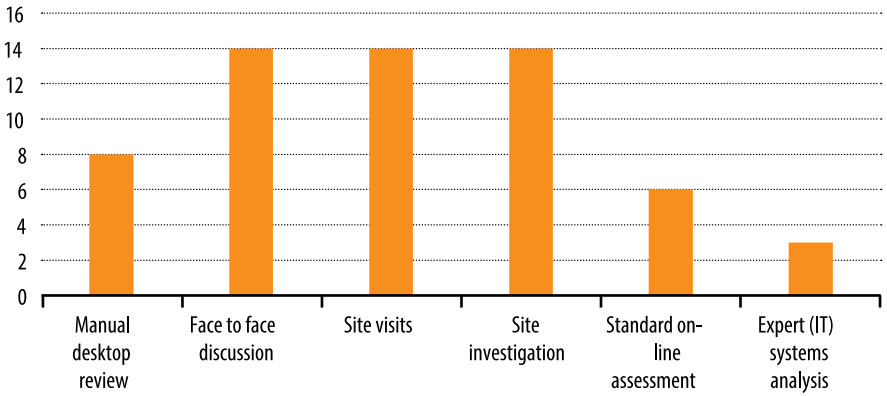
Figure 13: Tools used in Credit Risk Assessment



Most of the banks cited the following environmentally –related standards as their reference points: NEMA regulations because they require Environmental Impact Assessments (EIA) because they are part of national law; IFC Environmental and Social Performance Standards, UNESCO Heritage Sites; Internal bank exclusion lists as well as Kenya sustainable finance principle guidelines Respondents unanimously indicated that they share their results in the form of reports.

The effects the SCRA have on the financing terms and/or nature of the overall client relationship in the following ways. In terms of pricing, 4 banks indicated that they would charge a premium rate depending on the risk rating that the customer receivers. One respondent indicated that the price will also be affected by the current interest rate ceiling. Loan repayments are scheduled based on the nature and frequency of income or phased distribution based on meeting certain conditions. Additional covenants or waivers are signed based on the environmental impact assessment (EIA) reports, the nature of the business and the collateral provided; after receiving approval from the relevant regulatory agencies and licences; The lenders might also cross-selling their other related products or even substitute the current product with another more relevant product based on the clients' needs. In order to disburse credit, most of the respondents cited that they had to conduct some form of initial analysis in tandem with engaging the services of external advisers and consultants such as valuers, lawyers, NEMA-licensed experts as well as other professionals.

Figure 14: Environmental Analysis Methods used in Credit Assessment



Over 90 % of the respondents use face to face discussions, site visits or investigations or a combination of the three methods to conduct their analyses (See Figure 14). Almost 50% of the respondent banks indicated that they formally measure the level of environmental risks. One bank stated that is done on a situational ad hoc basis, whereas the rest indicated that they would use their portfolio exposure reports based on risk categorisation projects that their banks have financed. Sectoral risk exposure is also considered.

Some of the challenges you are faced with in terms of implementing SCRA within your bank:

- Classifying the assets and determining compliance and effects on the environment. lack of resources to implement these green initiatives;
- Lack of adequate and credible information that is preferably readily accessible in databases such as court cases on environmental issues.
- Additional resources required for capacity building among bank employees and subsequent turnover as well as re-training costs.
- Lack of local experts to provide technical support especially in certain unique ventures. Also those that are available charge high fees especially for high profile projects
- Customer reluctance to adopt worldwide sustainability best practice;
- Inadequate banking industry benchmarks and historical financial data for comparison
- Estimating the amount of time required for due diligence

- Availability of credible information; experts in certain unique ventures and high costs
- Challenges encountered in implementing an efficient management information systems (MIS) system for capturing the end to end (E2E) information related to the ESMS.
- Business growth needs against the perceived risk conflict.
- External regulatory factors such as weak regulatory environment where fraudulent licenses are issued by government officers and unreliable reports

5.4 Embedding Sustainability into Credit Risk Assessment

This last section focused on establishing how the banks embedded SCRA within the organisation and how they managed their resources to support policy implementation. It is quite clear that policy and procedural guidance documentation leads in terms of learning resources with 14 out of the 15 responding banks have embedded sustainability standards. These are followed by the handbooks or manuals. Online procedural assessment through the banks' intranet and board member training come third. While whistle blower mechanisms such as fraud and tip-off hotlines come in last. It is important to note these resources do not function mutually exclusively.

The most common form of training provided for those in the banking industry seems to be classes for the experienced lenders, followed by industry-wide courses like the SFI e-learning courses and lastly with classes for the new lending officers. This could be explained by the fact that training is quite expensive and would be offered to those with more years of experience and in specialised roles with directly related sustainability issues.

Figure 15: Learning for Policy Implementation

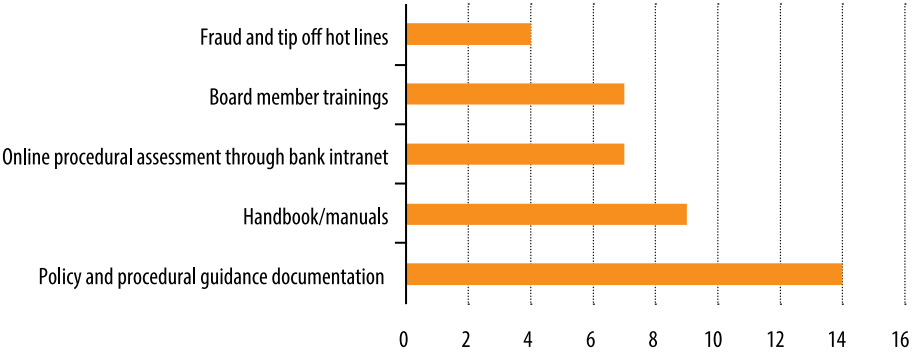
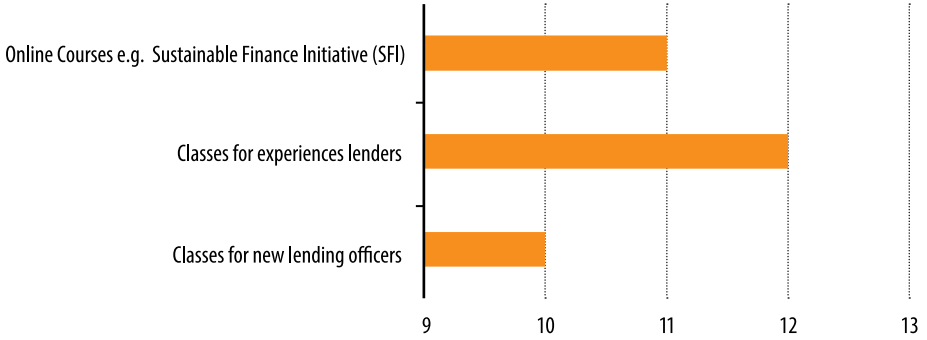
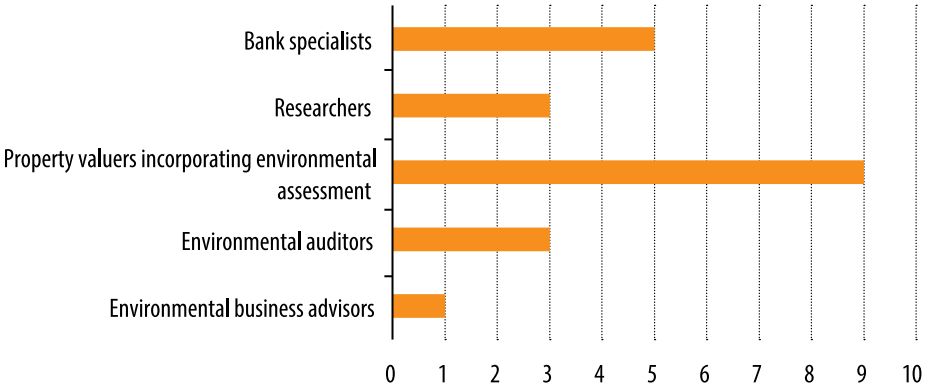


Figure 16: Training of Bank Officers



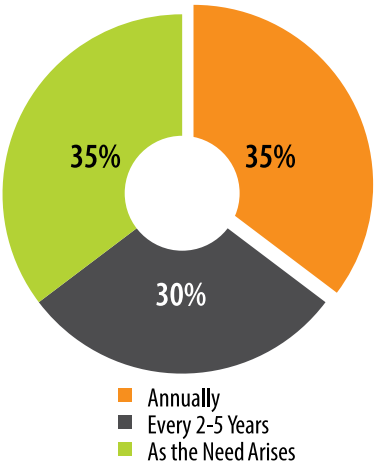
From the respondents have shown **that** the most popular technical support that they receive is from property valuers especially those environmental assessments. Most because they are big-ticket projects that require approval from local and national authorities like NEMA and NCA and it affects the value that you require. These are followed by bank specialists who are clued in to specific (green) standards that are required depending on the present projects.

Figure 17 Technical Support for Bank Officers



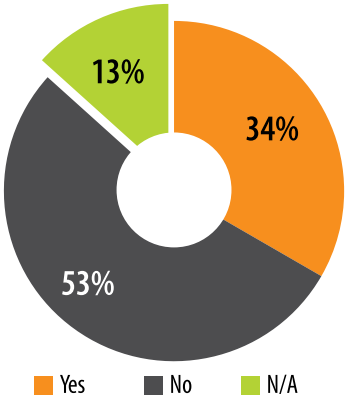
When asked whether set performance targets were part of their policy performance review, 5 of the responded "No", 4 indicated "Yes" while only 1 indicated that it was an on-going process in a that specific bank. The performance indicators and levels included they included were loan book growth; non-performing loans ratios as well as zero-tolerance policies to infractions. One bank also indicated it was in the process of re-classifying of its assets to enable monitoring and compliance of (green) assets. 35% of the responding banks indicated that they review their credit policy and its implementation annually while an equal percentage also indicated that they review it as need arises. 30% of the respondents showed that it is reviewed every 2-5 years.

Figure 18: Frequency of Credit Policy Review & Implementation Review



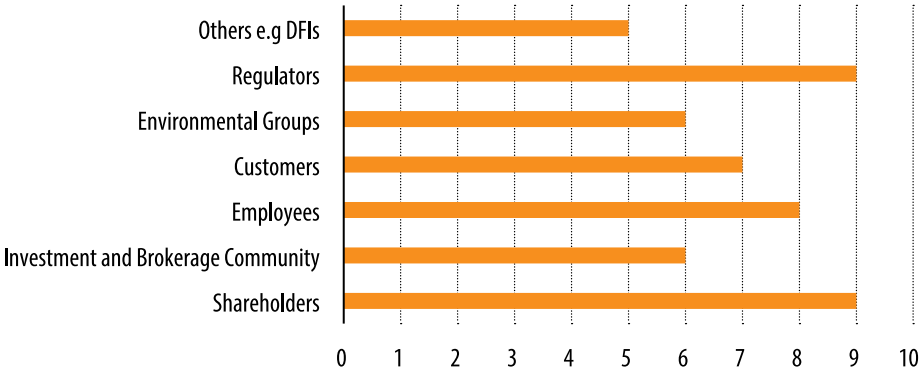
53% of the respondents indicated that they publish their sustainability risk performance internally and/or externally while 34% declared that they do not. Those banks that do disclose their sustainability risk performance refer to three key parameters (3) economic, social and environmental sustainability guidelines. One bank stated that in its internal reporting, it uses risk categorisation.

Figure 19: Publication of Sustainability Risk Performance



The main target audience for bank sustainability publications seems to be shareholders and regulators followed by employees and thirdly by their customers. The least favoured target audience would others such as development financial institutions (DFIs). This would be explained by the fact that banks would be likely prepare this information when they are seeking lines of credit for particular projects and would be required to align themselves to those particular standards.

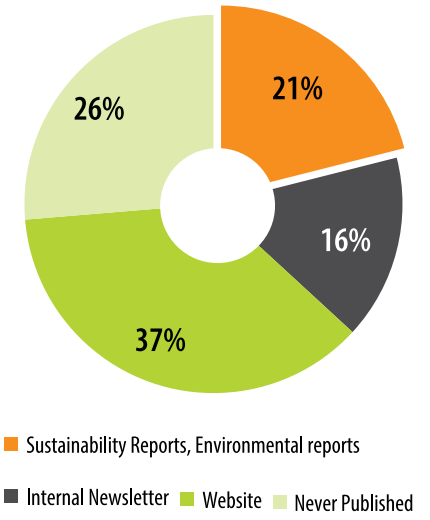
Figure 20: Target Audience for Sustainability Publications



An equal number of respondents (6) stated that they either published sustainability reports (which were mostly included in their audited financial reports) annually or they had never published.

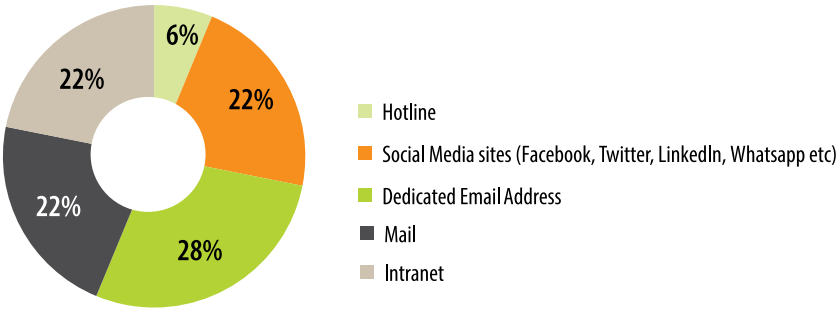
The most common form of medium used to disclose sustainability information seems to be company websites (37%) followed by sustainability and/or environmental reports (21%) and lastly internal websites (16%). Nonetheless 26% of the respondents reported that they have never disclosed sustainability reports. It should be noted that the production and publication of these reports will be subject to the availability of financial and human resources especially if the bank has adopted sustainability reporting format such as Sustainability Accounting Standard Board (SASB), Global Reporting Initiative (GRI) or Integrated Reporting <IR>.

Figure 21: Medium of Disclosing Sustainability Information



Three (3) banks cited the Kenya Sustainable Finance Principles initiated by KBA, IFC Environmental and Social Performance Standards which cover labour and working practices and community health standards, policies and standards set by national and local authorities; IIRC (international integrated reporting committee) for those that practice integrated reporting; banks also tend to benchmark themselves against each other especially when they do not have their procedures and policies set up. The most popular organisational structures or channels for airing grievances or feedback seem to be dedicated email addresses (28%) followed by intranet sites, social media sites and traditional post (22%). The least used channel seems to be hotlines at 6%.

Figure 22: Feedback on Sustainability Issues



However, it is not clear whether these are general customer service sites or dedicated to the sustainability issues. Nonetheless, these are commendable steps in acquiring information and data internally and externally on sustainability issues. In summary, this chapter has attempted to provide a brief summary of the research findings relating to three main hypotheses outlined at the beginning.

6.0 Discussion of Results

6.1 Influence of Governance and Policies on SCRA

It was hypothesized that commercial banks in Kenya bear different attitudes and/or at different stages of sustainable banking. It is quite clear that most commercial banks in Kenya fall in the preventative banking stage in the Jeucken-Bouma sustainable banking typology.

This stage is somewhat inevitable since banks are forced to comply with direct and indirect constraints placed on their activities though legislation and the business covenants that they embark on (Jeucken and Bouma, 1999). This is mirrored by the results in this study with a majority of the respondents implicitly and explicitly stating that their various affiliations and government regulations required them to have embedded certain sustainability procedures in their credit risk management systems.

Few commercial banks in Kenya are in the third stage of offensive banking, where they are considered both their internal and external process. In addition to greening their internal process, they are developing and marketing environmentally friendly products (Jeucken and Bouma, 1999). This was evident among the respondent banks that are offer a few green financial products that support clean technology and efficiency. As mentioned in the literature review that reputation management is a major reason why most organisations pursue sustainability. The findings confirm that reputation management is a top priority for banks when incorporating sustainability practices. However, they would need to be wary not have their efforts be branded as greenwashing. It is also clear that a large number of the banks are driven to implement various governance structures and policies that are sustainability linked because they would like to receive additional resources from multilateral agencies and development finance institutions (DFIs). Most of them require a higher degree of transparency including complying on sustainability reporting.

6.2 Methods Used to Implement Sustainable Credit Risk Management

The results confirmed the study's second hypothesis that most banks are taking the precautionary approach in their credit risk assessment process by ensuring they meet the minimum legal requirements. From the respondents, it is clear that all the banks have embedded some of form sustainability policies in the screening of their clients and their loan applications. They may rely most on questionnaires and checklists as their assessment tools when mostly conducting face to face discussions or site visits and investigations. They frequently cited that that they had to enlist the services of NEMA and NCA licensed professionals in line with the national non-financial regulations. Most of the banks that engaged with large corporate clients or provided project finance also frequently echoed that they had to align their lines with IFC Environmental and Social Performance Standards. This confirms that voluntary mechanisms and self-regulatory mechanisms have been given almost equal importance as the national and local regulations.

They also cited that among their greatest impediments is the presence of information asymmetry as they do not have an industry-wide database where they can refer to see whether some (of their corporate) clients have been blacklisted, have pending court cases or have some form of sanctions-based on their sustainability performance. The respondents cited that though the procured the services of external specialists and professionals in assessing the assets that will be used as collateral, they were only contacted by demand due to their high professional fees or when they were working on big ticket projects. They also cited they were not able to extend to some clients because they did not fully understand their specialised ventures.

6.3 Embedding sustainability

The third hypothesis in this research was most banks are meeting the minimum sustainability requirements in their reporting. The results show that sustainability reporting remains a voluntary exercise among commercial banks in Kenya. Therefore, very few banks have embraced integrated reporting or other reporting frameworks. They have instead opted to disclose their sustainability information on their websites, intranet and internal newsletters. It is notable that sustainability reporting can be a resource intensive exercise even for large commercial banks in Kenya.

Nonetheless, prior studies such as Alonso-Almeida et al (2014) have shown that the adoption of sustainability policies and standards can change internal management practices and be early warnings about future mismanagement. This is important for commercial banks in Kenya that are heavily relying on the policies and procedures as their main learning tool and reference point for sustainability issues. Therefore, they will need to be renewed regularly perhaps on an annual or biannual basis to ensure that they encompass the shifting trends and regulations in the sustainability arena. It was noted that a number of

banks did not disclose their sustainability policies and procedures because they were viewed as proprietary and internal documentation. However, it would be beneficial to their stakeholders for them to share some of their information for the sake of transparency.

In summary, it can be expected that sustainability policies will continue to be adopted by the banking industry given their current industry commitments but at a varying pace. These findings show that certain drivers such as environmental and market conditions, search for investors will accelerate or slow the adoption of sustainability policies in the banking industry, which is used to develop closer and more trusting relations with stakeholders.

07
SEVEN

7.0 Implications, Recommendations and Conclusion

The present study set out to assess the influence of sustainability on regulation and credit risk management among commercial banks in Kenya. The study has shown that commercial banks in Kenya have embraced different attitudes and are at different stages in embedding sustainability in the credit risk management systems.

The study has also confirmed that most banks are taking the precautionary approach in their credit risk assessment process by ensuring they meet the minimum legal requirements. It has become quite clear that they are meeting the required reporting requirements by the regulator but very few have embedded sustainability reporting as part of their standard financial reporting.

The study contributes to the rapidly expanding field of sustainable finance. Evidence in the Kenyan scenario is mostly focused on the process efficiencies or big-ticket projects and the current efforts with the Kenya Green Bond Programme. The findings of this research complement those of earlier studies (such as McDaniels and Robbins, 2018) that developing countries are still face challenges in embedding sustainability as part of their daily operations, mainly caused by lack of adequate resources to facilitate this transition.

The study is limited by the number of responses from the commercial banks and the research timelines. Despite its limitations, the study certainly adds to our understanding the strides that have been in the banking industry since the implementation of the Kenya Sustainable Finance Guiding Principles in 2015. The study should be repeated using more empirical methods since primary data is ordinarily more subjective. The question raised by this study is whether some banks are providing unlabelled sustainable financial products to their corporate and perhaps retail clients. Further research might explore the pricing differentials among labelled and unlabelled environmental and socially marketed financial products in the Kenyan markets. It would also be interesting to further explore the link between sustainability and Islamic banking in the Kenyan scenario.

These findings suggest several courses of action for various stakeholders in the banking industry. One of the respondents indicated that it was in the process of reclassifying its assets. Maybe it is an exercise that other banks would consider based on their business models. Banks will also require re-evaluating whom they assign the sustainability docket and whom they hold accountable. Greater efforts are needing to support capacity building within the financial services to enable bank officials to assess ESG risks. KBA and its partners took the first step in providing the e-learning SFI platform that provides the basics. However, it will require specialised bank officials and not just a designated department under the PR and Corporate Affairs department. Provision of more financial resources will be required implement the sustainability projects and ambitions. As the regulator, the Central Bank of Kenya, may borrow a few leaves from its counterparts in other developing countries and provide more direction in terms of regulatory frameworks and the embedding of sustainability policies.

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