SUSTAINABILITY IN BANKING: **SECTORAL OUTLOOK REPORT**

THE BANKS ASSOCIATION OF TÜRKİYE

2022

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This report has been prepared by Escarus (TSKB Sustainability Consultancy Inc.).

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1. Executive Summary

The finance and banking sector is critical for the development of a sustainable world. Financial institutions play a driving role in making sustainable development-oriented investments, encouraging the green transformation processes of various sectors, adopting practices to combat climate change and bringing technological developments to life. Encouraging their customers, society and all stakeholders to be aware of the issue of sustainability through their awareness-raising activities and guiding role, financial institutions also inspire everyone to take steps towards sustainability through the products and services they offer.

Among financial institutions, banking sector is one of the earliest to adopt sustainability and sustainable finance practices. Sustainability has become an important issue for the banking sector in the last 30 years, as in every sector. With steps such as the establishment of mechanisms for the management of environmental and social risks in financing processes and the development of environment friendly and socially minded financing instruments that will create a positive impact, banks have attained a supportive position in countries' sustainable development journeys.

Today, global sustainability practices are expanding to include the financial and banking sector. Practices for financial institutions are being developed, especially within the scope of international climate policies and decarbonization standards and initiatives. With decarbonization in the banking sector, carbon phase-out policies, sustainable development finance practices in the international development perspective and alike, the financial and banking sector came now to the center of the sustainability agenda. In addition, developments such as the European Green Deal and the EU Taxonomy provide a framework for standardizing the definition of sustainable finance and concretize the criteria for defining it.

In light of these developments, the banking sector is evolving both globally and in Türkiye. Areas such as combating climate change, carbon neutral banking, digitalization and impact investing are among the areas where banks are developing new strategies and practices.

BAT is a professional organization established in 1958 to support the healthy functioning of the banking system and the development of the banking profession. The Association encourages the adoption of sustainability practices and raises awareness in the sector through the trainings it offers to its members, the guidelines it develops and the working groups it presents.

In parallel with practices in the world, banks operating in Türkiye have started to embrace the concept of sustainability. BAT conducted a survey with member banks to understand the sustainability outlook in the banking sector in Türkiye. The results of the study indicate that the majority of banks in the sector adopt sustainable finance practices. It is apparent that most of the banks adopting these practices look at the subject from both environmental and social perspectives. Climate finance and green transformation are among the top priorities of banks. It can be concluded that banks have developed and diversified their practices in this area with mechanisms related to renewable energy, energy efficiency and other themes.

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Banks in Türkiye support sustainability practices not only with their products and services but also with their organizational structures and strategies. Banks that have embraced sustainability have developed a strategy or policy document and have implemented a sustainability governance structure (committee, working group, etc.) that is endorsed by senior management.

In addition to environmental aspects, banks have developed financing packages focused on social development, and are closely following impact financing and digitalization efforts. Digitalization is a phenomenon that is supported not only by the digitalization of banking processes, but also by innovative approaches such as blockchain applications and support for fintech companies. In the coming period, studies in this area are expected to further diversify and expand their impact on the banking sector in Türkiye.

An analysis of the goals and outlook for the future of the sector reveals that banks have already set goals for themselves in terms of sustainability, which include coal phase-out and carbon-free banking. Another notable aspect is the presence of common areas of development for deepening sustainability practices in the sector. The development of a common sustainable finance taxonomy, the creation of the necessary infrastructure systems for data monitoring and supply, access to quality data, and diversification of practices to raise awareness and encourage different stakeholder groups are among the said areas of development. Once introduced, these practices are expected to further accelerate the momentum in the sector.

The banking sector in Türkiye is progressing in line with global sustainability practices. Climate finance and green finance, blue finance, impact investing, digitalization and corporate sustainability make up the foundations of the current state of the sector. If banks take the sector one step further by enhancing their efforts in this area in the coming period, they can make significant contribution to Türkiye's journey towards sustainable development.

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2. Introduction

2.1. About BAT

The Banks Association of Türkiye (BAT - the Association) is a public professional organization established in 1958 as a legal entity that protects the rights and interests of stakeholders in the finance and banking sector, supports the healthy functioning of the banking system and the development of the banking profession. For 64 years, the Association has been working to prevent unfair competition in the finance and banking sector while supporting financial stability, sustainable development and social welfare.

The decision-making body of the Association is the General Assembly, and the executive body is the Board of Directors. The main service departments, namely Research and Statistics, Sectoral Regulations, Professional Development and Training, Corporate Communications, Risk Center, Management Support, Technology and Payment Systems, Customer Arbitration Panel and Support Services, Human Resources and Quality Management, Financial Affairs, Information Systems and Digital Application and Consultancy operate within the General Secretariat, where the decisions of the General Assembly and the Board of Directors are implemented.

BAT has a vision to support the economy and enhance the satisfaction of its stakeholders while maintaining the stability, security, and inclusiveness of the financial ecosystem. The Association's core values include establishing transparent, trust-based and sustainable relationships with its stakeholders, advancing its products and services in a way to increase added value together with its stakeholders by closely following technological developments for continuous improvement, recognizing and appreciating the efforts and expertise of each stakeholder who contributes to the success and reputation of the Association, and producing rational solutions that meet the needs of its stakeholders. BAT prepares its stakeholders for a sustainable future through its corporate strategy, which considers the environmental, social and governance framework that it takes into account in its operations, and has set a number of strategic goals to this effect:

- Contributing to Sustaining Financial Stability
- Strengthening the Perception of the Banking Sector
- Increasing Communication between BAT and the Sector
- Increasing and Improving the Digitalization and Diversity of BAT's Products and Services
- Enhancing Employee and Other Stakeholder Satisfaction
- Conducting Studies on Protection of Information Security
- Conducting Sustainability Studies

2.1.1. Sustainability Practices of BAT

Recognizing that the banking sector has a key role to play in meeting the need for transformation for a sustainable future, works diligently to assess the environmental and social impacts of its operations, analyze these impacts in line with its corporate business processes, and promote sustainability awareness through training and awareness-raising activities. In addition to the environmental and social issues that the Association takes into account in its own activities, it also assumes responsibility for developing sustainability practices in the banking sector and encouraging the sector to adopt sustainable practices that create value.

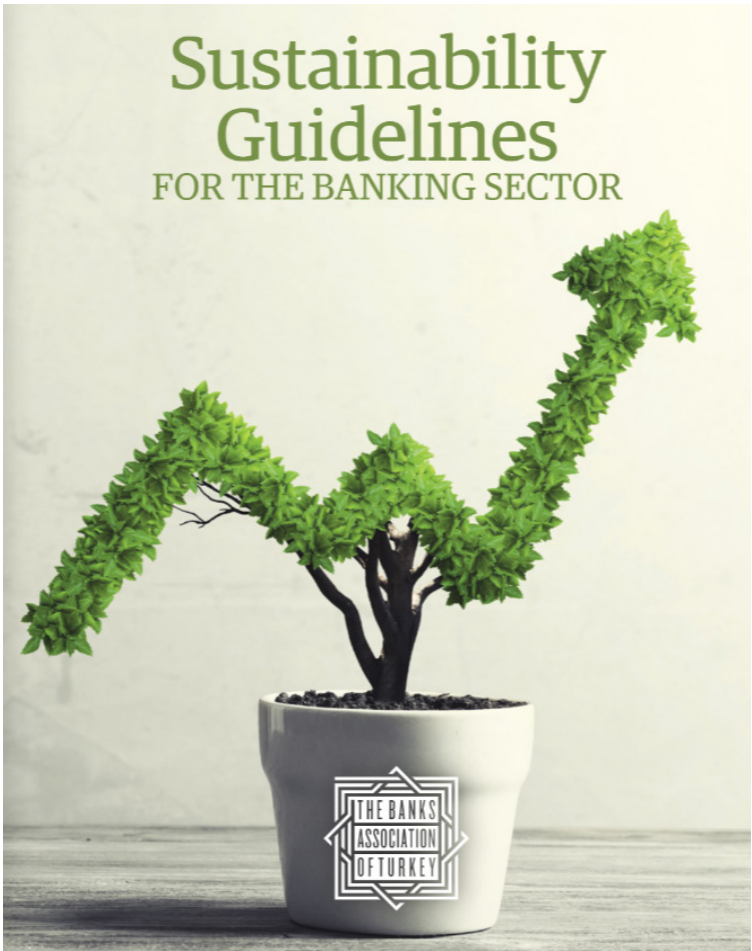
BAT closely monitors developments regarding the role of the finance sector in combating climate change, global sustainability trends, best practices, international sustainability frameworks (GRI Standards, CDP, TCFD, SASB, UN Sustainable Development Goals, etc.), and the practices of initiatives and organizations such as the UN Global Compact, the World Economic Forum (WEF) Global Risks Report, and the United Nations Principles for Responsible Investment (UN PRI).

The Association aims to follow the national and international agenda on sustainable development, climate change, sustainability/climate finance, and to conduct awareness-raising activities for the stakeholders of the banking sector, and to guide banks. In this context, the “Sustainability Working Group”, which guides banks to systematically manage the predictability, transparency, and traceability of environmental and social issues, has been operating within the Association since 2009. This Working Group is composed of member banks and representatives of the Participation Banks Association of Türkiye (TKBB) and Credit Bureau (KKB). The Association also contributes to sustainability efforts through the Working Group on Banking Services for Citizens with Disabilities, the Digital Banking Working Group, and the Education Strategies Working Group.

The Association developed and published a “Sustainability Guidelines for the Banking Sector” in 2014.

The guidelines, prepared by the Sustainability Working Group, provide a pioneering framework to guide the sustainability efforts of the banking sector in Türkiye. In light of new developments, the guidelines were updated in March 2021.

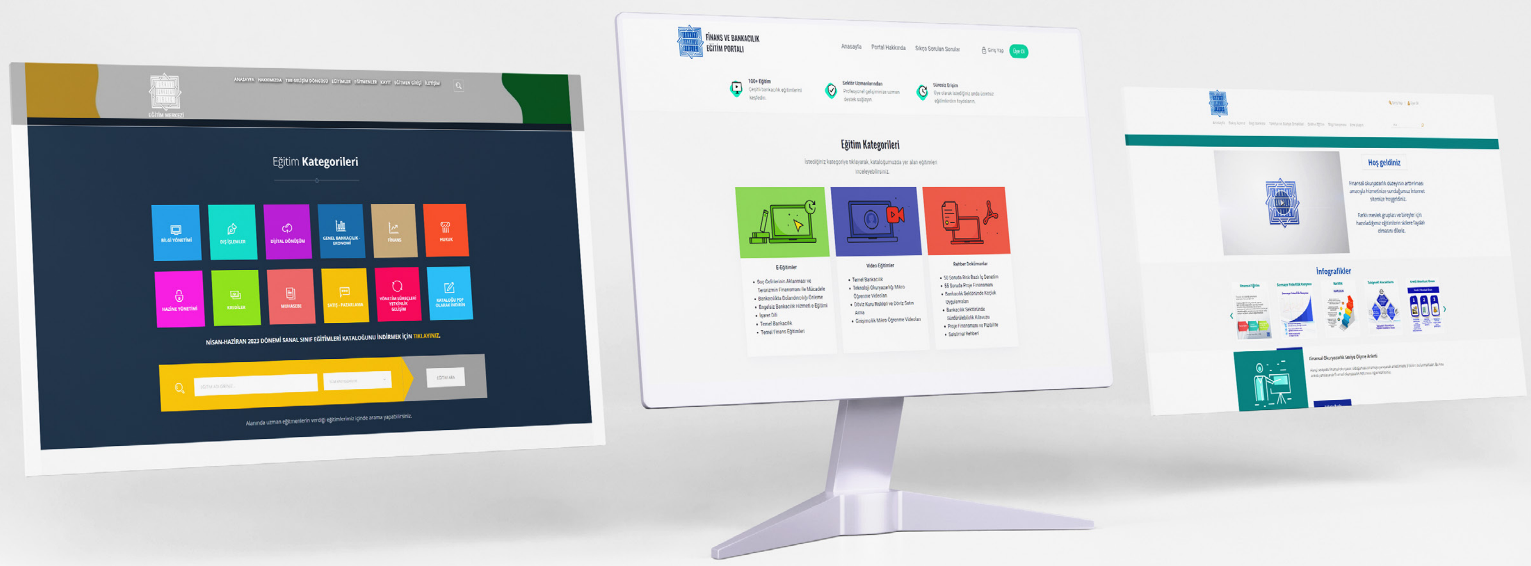
In addition, the Association participates in working groups and events organized by the TR Ministry of Treasury and Finance, the TR Ministry of Environment, Urbanization and Climate Change, and the TR Ministry of Energy and Natural Resources. Besides, BAT responds to their requests for opinions, information, and documents.



It also contributes to the Specialized Working Group on Sustainable Consumption and Production Action Plan and the Specialized Working Group on Zero Pollution Action established within the scope of the Türkiye Green Deal Action Plan. As part of its efforts targeting the European Green Deal, in 2021, the Association hosted the Sustainable Banking Workshop with the Banking Regulation and Supervision Agency (BRSA) and video conferences on “EU Green Deal” and “Potential Impacts of Climate Change-Related Risks and Opportunities on the Banking Sector.”

In addition, the Association offers distance learning opportunities on key topics related to finance and banking through the Finance and Banking Education Portal, which includes free educational content accessible to everyone, especially sector employees. In 2021, digital trainings and guidance documents titled “Basic Sustainability” and “Advanced Sustainability” were added to this portal, which is a digital and dynamic platform. BAT also provides up-to-date trainings for the advancement of the sector through the Training Catalog, which is prepared quarterly.

In 2022, the Training Catalog included trainings on “Climate Finance” and “Sustainable Financing Instruments” to raise awareness of the professionals on sustainability in the banking sector. The trainings planned for 2023 include various sustainability-related topics such as “Climate Finance”, “Assessing Environmental, Social and Governance Risks in Sustainable Finance”, “Sustainable Finance Instruments” and “European Green Deal”.



> In addition to the efforts to prepare the banking sector for a sustainable future, the Association regularly monitors sustainability indicators in its own operations and strives to minimize negative environmental and social impacts.

BAT attaches importance to regularly monitoring performance indicators in impact areas such as waste generation, water and energy consumption and carbon emissions. BAT sends plastic, glass, paper and battery waste collected in recycling bins placed in the Association office for recycling. In order to ensure energy efficiency and reduce electricity consumption in the Association building, BAT uses LED light bulbs in the entire office and has introduced a sensor-activated lighting system in certain departments.

Believing that social welfare is one of the most important building blocks for a sustainable world, BAT has a corporate social responsibility vision that creates sustainable value in the projects it prepares and/or contributes to as a stakeholder. In the projects developed with this perspective, the Association adopts the Sustainable Development Goals (SDGs) as a principle and designs projects that will contribute to these goals and respond to the current needs of the society.

The Association organizes virtual conferences and webinars within the scope of its cooperation with the academia, which aims to strengthen the ties between the banking sector and the finance and banking departments of universities and to inform students and academics in these fields about current developments in the world of finance. To this end, BAT held two conferences in November 2021 and February 2022, and a congress on “Current Developments and Trends Towards the Banking of the Future” in October 2022.

Supporting the “SDG-5: Gender Equality” goal, BAT places importance on equality and inclusion among its employees. The Association sets an example in ensuring gender equality in labor markets, with 55% of its employees being women and 45% men. The share of female executives in senior management is 33%. Beyond the egalitarian working environment it offers within its own organization, the Association supports its member banks to adopt a gender equality and inclusion approach.

It encourages member banks to support women entrepreneurs through specialized financial products, as well as various activities such as mentoring, advisory services and trainings. The Association shares the activities of its members under the “Special Activities of Banks for Women Entrepreneurship” tab to promote inclusive services and good practices for women in the sector.

BAT places great importance on acting responsibly in social development and progress and works with the aim of delivering its added value to the widest possible audience in society. It collaborates with various stakeholder groups to support social investment. In addition to the training and career opportunities offered to its own employees, BAT continues to organize training activities for the finance and banking sector as well as the community, and to increase progress and awareness in the areas it has identified.

2.2. About the Report

BAT aims to present the approach, future targets and best practices of the banking sector in Türkiye in line with the sustainability themes followed worldwide in this Sustainability in Banking: Sectoral Outlook Report. The sustainability trends followed by international banks and banking associations around the world and the practices of banks operating in Türkiye form the basis of the report.

The "3. Sustainability for the Banking Sector" section of the report discusses global sustainability developments, as well as the sustainability approaches adopted by the banking sector in the world and in Türkiye, in addition to the risks and opportunities faced by the banking sector.

As part of the study, BAT conducted a survey to scrutinize the sustainability practices of its member banks operating in the banking sector in Türkiye. The questionnaire consists of 74 open-ended and multiple-choice questions designed to understand banks' current sustainability practices and future goals. A total of 19 banks responded to the survey conducted as part of the study. The focuses and trends in the banking sector in Türkiye were analyzed based on this survey results. The findings of the analysis are presented in the "4. A Detailed Look into Sustainability-Related Trends in The Banking Sector" section of the report.

> "With this report, which demonstrates the sustainability trends of the sector, the Association aims to guide the activities of banks and lead the sector towards a sustainable future."

3. Sustainability for the Banking Sector

3.1. Sustainability Approach of the Banking Sector in the World

The economic, social, and environmental crises and growing inequalities that have become common in recent years, as well as the climate crisis that has brought with massive fires, catastrophic weather events, extreme rainfall and severe droughts, highlight the importance of building a sustainable future. Our planet faces many environmental and social risks, including resource depletion, irreversible climate change, loss of natural areas and biodiversity, increasing poverty and inequality, and social conflict. It has become necessary to transform our business models and lifestyles before an irreversible rupture occurs. Initiating transformation to build a sustainable future by protecting the planet we live on, and all living beings calls for a common approach.

Global climate change driven by human activities requires financial investments in resilient infrastructures, digital solutions, energy efficiency and renewable energy systems. According to the World Bank's October 2019 data, USD 90 trillion of investment is needed by 2030 to build resilient infrastructure to adapt to climate change[1] However, for social development to succeed, there is a need to increase the welfare of societies without leaving anyone behind, improve education and health systems, introduce new employment opportunities, and develop low carbon economy models.

Sustainability has become an important concept for the banking sector in the last 30 years, as in every sector. For sustainable development to succeed, the banking sector needs to review its roles and duties, and the financial system needs to adopt a fair and responsible approach to achieve transformation. Shared solutions are needed to create economic models that take social and environmental considerations into account and deliver social benefits. The banking sector must be part of the vision of creating a desirable, livable, and equitable future. The only way for the sector to fund projects and activities that will build a sustainable future is to produce inclusive and innovative solutions. Therefore, providing financing for projects that support sustainable development and the innovative instruments developed for this purpose have become the most critical agenda items of recent years. A sustainable finance perspective embraced by the banking sector will accelerate the transformation and ensure that the monetary resources needed are channeled to the right places in a way that promotes sustainable development.

Access to finance to tackle the climate crisis and to adapt to the climate change has been at the crux of climate negotiations since the UN Framework Convention on Climate Change (UNFCCC), which was signed at the United Nations (UN) Conference on Environment and Development in Rio de Janeiro in 1992 and entered into force in 1994. Access to finance has vital importance for projects and investments to be undertaken for both combating climate change and adapting to the changing conditions brought about by climate change.

1. UN Financing Climate Action https://www.un.org/en/climatechange/raising-ambition/climate-finance

The debates on where developing countries will find the necessary finance for adaptation to climate change and to what extent developed countries, which have a relatively larger share in global greenhouse gas emissions and thus have a higher impact on climate change, will contribute to this quest for funding have been ongoing since the UN Conference on Environment and Development. Although the UNFCCC was a very important step as it was the first framework agreement in the international arena, the failure to adopt a common approach on a global scale has led to the negative impacts of climate change being felt increasingly.

The Conference of the Parties (COP) is the highest decision-making body of the UNFCCC, which has held every year since its entry into force in 1994. One of the most important of these conferences was the one organized in 1997 (COP 3). The Kyoto Protocol signed at this conference set concrete targets for combating climate change. The Kyoto Protocol, which followed the objectives of the UNFCCC and entered into force in 2005, introduced binding obligations to the countries that are a party to the UNFCCC in their efforts to combat climate change. The Protocol treats climate change as a problem that requires solutions from governments, as well as public financing.

In 2009, the 15th Conference of the Parties (COP 15) decided to establish the Green Climate Fund (GCF), through which developed countries would provide USD 100 billion of annual financing to benefit climate projects in less developed countries.[2]

In 2015, as the reporting period of the Kyoto Protocol was nearing its end, the Paris Agreement, which accelerated global climate change efforts, was signed at the COP 21 in Paris and entered into force in 2016. This Agreement sets out the interrelationship between climate change and human rights, poverty reduction and sustainable development. 194 out of 198 countries that are parties to the UNFCCC are also parties to the Paris Agreement. The Paris Agreement is based on the principle of equitable, common but differentiated responsibilities, reflecting the relative capabilities of the parties under different national circumstances. In this respect, the Paris Agreement allows each country to determine its greenhouse gas reduction commitment to combat the climate crisis, considering the country’s own unique circumstances. In addition to the achievement of sustainable development and efforts to eradicate poverty, the Paris Agreement sets a global goal of keeping the increase in global warming well below 2°C above pre-industrial levels and pursuing efforts to limit it to 1.5°C. Yet another objective of the Agreement is to strengthen financial flows by making them consistent with the trend towards low greenhouse gas emissions and climate-resilient development.[3]

One of the key outcomes of the Agreement is that it envisages that developed countries would provide financing for developing countries that are highly vulnerable and exposed to the impacts of climate change. The Paris Agreement has accelerated the search for climate and/or sustainability-themed financing for projects and investments that aim to meet the greenhouse gas reduction targets, build resilient infrastructure in the context of climate adaptation, ensure energy transformation through renewable energy investments, reduce poverty, and achieve sustainable development.

As all these developments take place, the EU is increasingly emphasizing the requirements of the Paris Agreement by adopting the European Green Deal (the Green Deal) published at the end of 2019 and a series of legislative proposals to achieve at least 55% net reduction in greenhouse gas emissions by 2030[4] and to become a carbon neutral continent by 2050.

2. https://www.oecd.org/climate-change/finance-usd-100-billion-goal/ Accessed January 2023.
3. https://unfccc.int/process/the-paris-agreement/status-of-ratification Accessed December 2022.
4. *T his rate was increased to 57% with the subsequent regulation.*

The Green Deal aims to raise the 2030 and 2050 climate targets, supplying clean, affordable and secure energy supply, mobilising industry for a clean and circular economy, building and renovating in an energy and resource efficient way, achieving zero pollution for a toxic-free environment, preserving and restoring ecosystems and biodiversity, developing fair, healthy and environmentally friendly "farm to fork" food systems, accelerating the shift to sustainable and smart mobility, and financing through the "Just Transition Mechanism".[5] Key among these objectives is the "Just Transition Mechanism", which aims to ensure that no one is left behind when implementing green economy policies and is part of the EU's investment plans. This mechanism, intended to be implemented between 2021-2027, provides financial support and technical assistance to those most affected by the transition to a green economy.

Another key issue among the objectives of the Green Deal is financing. By outlining the necessary investments and the financing instruments that can be used for them, the Green Deal explains how to ensure a just and inclusive transition. To achieve the Green Deal targets, a commitment has been made to mobilize at least EUR 1 trillion for sustainable investments over the next decade.[6]

It is obvious that directing investments to sustainable projects and activities is vital to achieving the Green Deal goals. However, at this point, there is a need to clearly define what is "sustainable" and to create a common language. The Taxonomy Regulation entered into force in 2020 to establish common standards and definitions for sustainable economic activities, marking the beginning of the preparations for the EU Taxonomy. The EU Taxonomy is a framework that provides companies, investors and even policy makers with proper definitions of which economic activities can be considered sustainable. It classifies six environmental objectives and sets performance criteria for each class. The 6 environmental objectives set in this framework are climate change mitigation, climate change adaptation, the sustainable use and protection of water and marine resources, the transition to a circular economy, pollution prevention and control, and protection and restoration of biodiversity and ecosystems.[7] The economic activity being assessed is questioned as to whether it contributes to or causes significant harm to any of these 6 environmental objectives. The taxonomy is intended to guide investors to need-oriented, climate-friendly, and reliable investments, in other words, away from greenwashing.[8]

The acceptance of the classification system introduced by the EU Taxonomy led to developments in the finance and banking sector and influenced the development of the concept of sustainable finance. In the EU, in order for an investment to be considered "sustainable", the project or activity must meet the criteria of the taxonomy. Any project that is not included in the EU Taxonomy or is incompatible with it is not considered within the scope of sustainable finance. In 2021, drawing on the EU Taxonomy, the European Union drafted the EU Green Bond Standard, a standard framework for green bond issuers and investors.

Financing was one of the main agenda items at the COP 26 in Glasgow, Scotland in November 2021. The Conference underlined that all financial institutions should assume great responsibility in combating the climate crisis as well as adaptation to climate change and asked

5. https://commission.europa.eu/strategy-and-policy/priorities-2019-2024/european-green-deal_en Accessed January 2023.
6. Finance and the Green Deal. https://commission.europa.eu/strategy-and-policy/priorities-2019-2024/european-green-deal/finance-and-green-deal_en Accessed January 2023.
7. EU Taxonomy for Sustainable Activities (2022). https://finance.ec.europa.eu/sustainable-finance/tools-and-standards/eu-taxonomy-sustainable-activities_en Accessed January 2023.
8. *Greenwashing refers to cases where marketing and/or communication campaigns 1) claim that a product or service is environmentally friendly, sustainable, or harmless without any proof, or 2) the information provided as evidence does not fully reflect reality or contains incomplete or inaccurate information.*

financial institutions to adopt a responsible approach. The Glasgow Climate Pact adopted at the COP 26 emphasizes the urgency of mobilizing financial flows aligned with the goals of greenhouse gas mitigation and climate-resilient development. The Conference highlighted the “blended finance” approach to mobilize private finance to accompany public resources spent on sustainable development. The establishment of the Glasgow Financial Alliance for Net Zero (GFANZ) was one of the highlights of the COP 26 in relation to finance and banking activities. GFANZ is a coalition of more than 550 financial institutions pursuing the goals of the Paris Agreement, aiming to decarbonize the economy and build a climate-resilient future. It aims to increase the number of financial institutions making net zero commitments and support financial institutions in the transition to net zero to ensure that their goals are achieved through credible actions.[9]

The most recent Conference of the Parties, COP 27, was held in Egypt in November 2022. The prominent topics of the Conference were mitigation and adaptation, losses and damages, financing, energy security and climate policies. The issue of climate finance, promised by developed countries to developing countries under the GCF, has once again come to the agenda, and it has been emphasized that new financing mechanisms should be created to replace GCF and adaptation fund should be increased. Demands centered around increasing the amount of climate finance, creating a wider pool to suit the needs, reducing the cost of funding, and taking into account the high debt burden of countries. In addition, another important issue negotiated at the COP 27 was the establishment of a “Loss and Damage Fund” to provide financial support to developing countries that are vulnerable and fragile to the climate crisis.

Although the decisions of the Conference of the Parties states that at least USD 100 billion should be mobilized annually from developed to developing countries and that this should be done mainly through the GCF, the UN Conference on Trade and Development held in 2021 indicated that the climate adaptation costs of less developed countries will amount to USD 300 billion per year by 2030. The Conference also noted that this amount could rise to USD 500 billion annually by 2050 if the committed emission reduction targets will not be met.[10]

For more than 30 years, since the 1992 summit in Rio de Janeiro, the United Nations Environment Programme Finance Initiative (UNEP FI) has been mobilizing the financial system to create a sustainable global economy and achieve sustainable development. UNEP FI was the first initiative to link the financial sector and sustainability and has developed responsible investment principles for the sector. In addition, it has established the necessary sustainability frameworks to help the financial sector address environmental, social and governance (ESG) challenges. Today, more than 450 institutions in the banking and insurance sectors with assets in excess of USD 100 trillion are signatories to UNEP FI’s Principles for Responsible Banking and Principles for Sustainable Insurance. 7 banks in Türkiye support UNEP FI’s Principles for Responsible Banking.[11]

The Net Zero Banking Alliance (NZBA), established by UNEP FI, brings together banks committed to aligning their loan and investment portfolios with the net zero emissions target by 2050. Announced in 2021, the NZBA comprises 126 member banks representing approximately 41% of global banking assets as of 2023.

9. GFANZ. https://www.gfanzero.com/ Accessed January 2023.
10. United Nations Conference on Trade and Development (2021). Trade and Development Report 2021 From Recovery to Resilience: The Development Dimension https://unctad.org/system/files/official-document/tdr2021_en.pdf Accessed January 2023.
11. UNEP FI (2023). https://www.unepfi.org/about/ Accessed January 2023.

As of February 2023, 4 institutions in the banking sector in Türkiye are included among the said member banks.[12] The NZBA works in line with the activities of GFANZ, one of the COP 26 outputs with a climate-focused approach, and UNEP FI's Principles for Responsible Banking.

Another item on the banking sector's sustainability agenda is the social and environmental risks associated with the projects it finances. This is because the banking sector is held responsible for the potential negative social and environmental impacts of the funded projects. In 2003, a risk management framework called the "Equator Principles" was published to enable banks to manage the risks that may arise in large investment projects. After many revisions, the final version of the Equator Principles, the fourth edition, was published in 2020. In line with the Equator Principles, risk management processes are applied in the financing of projects with an investment cost of USD 10 million or more. Currently, 138 financial institutions from 37 countries are conducting environmental and social impact assessments based on the Equator Principles.[13]

On the other hand, the "IFC Performance Standards" published by the International Finance Corporation (IFC) provide the banking and finance sector with a roadmap for managing the environmental and social impacts of funded projects.

Another development that closely concerns the banking sector is the establishment of the Taskforce on Climate-Related Financial Disclosures (TCFD) in 2015 and the Taskforce on Nature-Related Financial Disclosures (TNFD) in 2021. The financial sector needs transparent and timely information from companies in order to make informed, efficient, and responsible capital allocation decisions and to price assets correctly. The Financial Stability Board (FSB) has identified a need for information on the assessment of climate-related risks and their impact on the financial sector. TCFD was established to enable investors, insurers, and lenders to make decisions by properly analyzing climate-related risks. As of October 2022, TCFD has more than 4000 supporters, of which 1539 are from the financial sector.[14] TCFD's 25 supporters include 5 banks and 2 different financial sector organizations, are from Türkiye.[15] In order to ensure that the risks identified are not limited to the climate crisis but include all environmental issues, the TNFD was established to work with the TCFD to provide a framework for companies to address environmental risks and opportunities.

At a time when the impacts of the climate crisis and the increase in inequalities and vulnerabilities are being felt more and more every day, it is crucial to financially support countries that want to take action to align with the Paris Agreement and the Green Deal. In addition, the need for innovative financing instruments has arisen in order to achieve the SDGs set out by the United Nations and transition to a sustainable economy.

As a result, the banking sector has developed many new products and services. Financing needs with a focus on sustainability can also be met through different financing instruments such as international and national grants, co-financing, low-interest and interest-free loans, concessional loans, sustainable/social/green/climate bonds, green sukuk, debt swaps, and guarantees.

12. Net Zero Banking Alliance (2023). https://www.unepfi.org/net-zero-banking/ Accessed January 2023.
13. Equator Principles. https://equator-principles.com/about-the-equator-principles/ Accessed January 2023.
14. TCFD Status Report (2022). https://assets.bbhub.io/company/sites/60/2022/10/2022-TCFD-Status-Report.pdf Accessed January 2023.
15. TCFD. https://www.fsb-tcfd.org/supporters/ Accessed January 2023.

The use of sustainable debt instruments, primarily thematic bonds and loans has been increasing day by day since the World Bank first issued "green bonds" labeled bonds to institutional investors in 2008.

According to the World Bank (2018) and Oxford Institute for Energy Research (2022), the size of the global green bond market exceeded USD 700 billion in 2020. The revenue generated from this market was mostly used in the energy sector, low-carbon buildings, and transport, respectively. By 2021, green bond markets had grown even further, with the global green bond market exceeding USD 1 trillion. This indicates a 20-fold increase from 2015 and represents 10% of global debt markets.[16]

Looking at the entire market of social bonds, sustainability bonds, sustainability-linked bonds, and transition bonds in addition to green bonds, it becomes apparent that issuances have followed an upward trend since 2017 (Figure 1).[17]

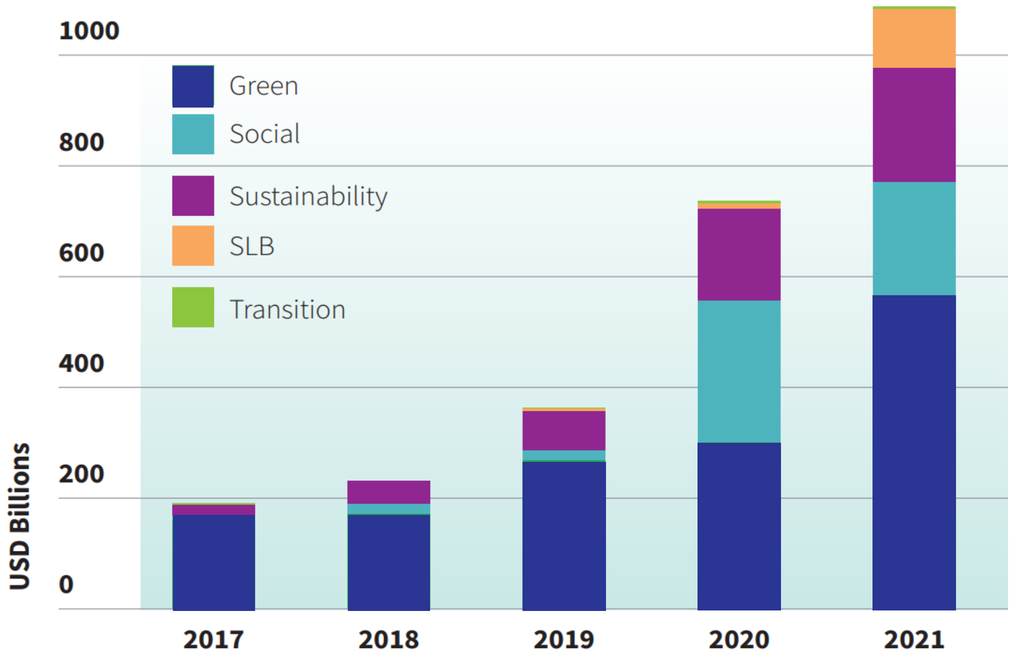


Figure 1: Volumes of Cumulative GSS+ Bonds (Green Bonds, Social Bonds, Sustainability Bonds, Sustainability-Linked Bonds (SLB) and Transition Bonds) until the end of 2021[17]

By the end of 2022, the volume of global GSS+ bond issuances reached USD 3.7 trillion. In 2022 alone, USD 487.1 billion worth of green bonds were issued, with sustainability bonds contributing USD 166.4 billion, social bonds totaling USD 130.2 billion, sustainability-linked bonds USD 76.3 billion and transition bonds USD 3.5 billion (Figure 2).[18]

It is expected that in the coming years, the financial system will expand its thematic product portfolio in the journey towards a sustainable future, offer more advantageous loan options, and in the bond markets, investors will increasingly turn to more environmentally friendly options. All players in the global financial system must assume critical responsibilities on the path to a sustainable and equitable future.

16. ŞİMŞEK, O. & Tunalı, H. (2022). *Yeşil Finansman Uygulamalarının Sürdürülebilir Kalkınma Üzerindeki Rolü: Türkiye Projeksiyonu.* Ekonomi ve Finansal Araştırmalar Dergisi. 4 (1). pp. 16-45.
17. Climate Bonds Initiative (2022). Sustainable Debt Market Summary H1 2022. https://www.climatebonds.net/files/reports/cbi_susdebtsum_h1_2022_02c.pdf
18. Climate Bonds Initiative (2023). https://www.climatebonds.net/2023/01/2022-market-snapshot-and-5-big-directions-sustainable-finance-2023

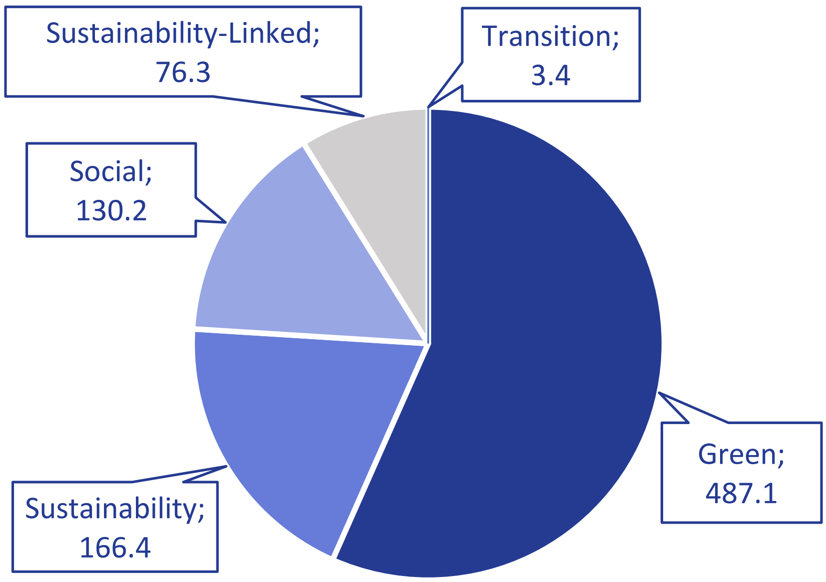


Figure 2: Breakdown of Sustainability-Themed Bond Issuances in 2022 (USD billion)[18]

> All players of the global financial system must assume critical responsibilities on the path to a sustainable and equitable future.

3.2. Sustainability Approach of the Banking Sector in Türkiye

Sustainability efforts in the banking sector in Türkiye are progressing in parallel with international practices. Sustainability activities at banks first started with the disbursement of environment and energy/resource efficiency themed loans obtained from international sources and development finance institutions, and accordingly, environmental-social risk assessment and management processes were developed for lending processes.

Over time, this approach also started to be implemented by banks in their own operations, with banks adopting practices such as energy saving, use of renewable energy, reduction of paper consumption and corporate social responsibility projects in their office activities and direct operations. As a step further, these banks started to produce sustainability-themed reports in order to transparently share their work and performance in the field of sustainability with their stakeholders.

BAT provides guidance to the sector by carrying out various activities to trigger the development of the sector and encourage the sustainability practices of the banks operating in Türkiye. With the "Sustainability Guidelines for the Banking Sector" prepared in 2014, the Association provided a pioneering framework to guide the sustainability efforts of the finance and banking sector in Türkiye. The guidelines, prepared by the BAT Sustainability Working Group, were updated in March 2021.[19]

The sustainability-focused efforts in the finance and banking sector in Türkiye in the recent years are listed in the next page.

19. BAT, Sustainability Guidelines for the Banking Sector, March 2021. https://www.tbb.org.tr/sustainability/index.html

- In October 2020, the Capital Markets Board of Türkiye (CMB) published the "Sustainability Principles Compliance Framework".[20]

- Türkiye accelerated its green transformation, introduced many new regulations and shared the Green Deal Action Plan in July 2021 to comply with the European Green Deal. The Action Plan prepared by the TR Ministry of Trade and the action "3.2.5. Determining a roadmap for the development of sustainable banking" is directly related to the banking sector with the aim of building a sustainable financial system in Türkiye in light of global developments.[21]

- In November 2021, the TR Ministry of Treasury and Finance publicly announced the "Sustainable Finance Framework Document" to be used in international green, social or sustainable bond or lease certificate type borrowing transactions in government bonds.[22]

- In December 2021, the Banking Regulation and Supervision Agency (BRSA) published the "Sustainable Banking Strategic Plan" for the action included in the Türkiye Green Deal Action Plan.[23] The plan emphasizes that the sector would be encouraged to develop sustainable finance and cooperation with relevant parties in the field of sustainable finance would be enhanced. In addition, it underlines that an empowering environment would be created to facilitate banks' access to international funds for sustainability purposes.

- Another important development in 2021 was the establishment of the Financial Sustainability Working Group under the leadership of the TR Ministry of Treasury and Finance, which includes (BRSA), the Central Bank of the Republic of Türkiye (CBRT) and commercial banks.

- In order to further stimulate the sustainable finance market, the CMB published the "Guidelines on Green Debt Instruments, Sustainable Debt Instruments, Green Lease Certificates and Sustainable Lease Certificates" in February 2022.

Another finance-related development in Türkiye was the establishment of the Green Economy and Climate Change Department by the CBRT to limit climate risks and seize climate-related opportunities with the aim of identifying the adverse effects of climate change on the financial system and minimizing the risks. In the 32nd Financial Stability Report published in May 2021, the CBRT expressed for the first time its decision to support green finance practices with a policy in the long run, provided that it does not cause a change in the main objectives of its monetary policy[24] In its Financial Stability Report shared in May 2022, the CBRT stated that the amount and number of green bonds increased significantly compared to previous years and that the private sector's green bond issuances exceeded those of the public sector.[25]

20. CMB, Sustainability Principles Compliance Framework, October 2020. https://www.borsaistanbul.com/en/duyuru/3177/cmb-has-announced-the-sustainability-principles-compliance-framework
21. TR Ministry of Trade, Green Deal Action Plan 2021, Ankara, July 2021. https://ticaret.gov.tr/data/60f1200013b876eb28421b23/MUTABAKAT%20YE%C5%9E%C4%B0L.pdf
22. TR Ministry of Treasury and Finance, Sustainable Finance Framework, November 2021. https://ms.hmb.gov.tr/uploads/2021/11/Republic-of-Turkey-Sustainable-Finance-Framework.pdf
23. BRSA, 2022-2025 Sustainable Banking Strategic Plan, December 2021. https://www.bddk.org.tr/KurumHakkinda/EkGetir/19?ekId=71
24. CBRT, 32nd Financial Stability Report, May 2021. https://www.tcmb.gov.tr/wps/wcm/connect/24492041-9e85-4317-9d84-70a815ce5c9e/FSR32_ENG_Full.pdf?MOD=AJPERES&CACHEID=ROOTWORKSPACE-24492041-9e85-4317-9d84-70a815ce5c9e-nG6F418
25. CBRT, 34th Financial Stability Report, May 2022. https://www.tcmb.gov.tr/wps/wcm/connect/5059ea97-dfff-4fb6-a3d5-eae8e3eafd97/TamMetin.pdf?MOD=AJPERES&CACHEID=ROOTWORKSPACE-5059ea97-dfff-4fb6-a3d5-eae8e3eafd97-oldDyjN

3.3. Sustainability-Related Risks and Opportunities in the Banking Sector

> Changing global conditions due to the climate crisis, increased frequency of natural disasters and growing vulnerabilities bring both risks and opportunities for the banking sector. As global problems such as the climate crisis and pandemics continue to occur, the number of institutions and organizations aiming to create positive value for the environment and society is increasing day by day.

The banking sector is an important stakeholder in preventing the diversion of financial resources to projects that are harmful to the environment, climate and communities. Moreover, developing, multiplying, and expanding appropriate financial instruments for sustainable development is one of the main opportunities for the banking sector. Despite the global challenges, the expectation that the focus of the banking sector in the world and in Türkiye will shift towards sustainability practices and green, social, and sustainable financing instruments is very promising.

In the context of climate change mitigation, Steps taken by institutions and organizations in recent years to reduce emissions, including transition from fossil fuel-based systems to renewable energy systems, increase in energy efficiency practices, measures to reduce energy consumption in buildings, and green technology investments are noteworthy.

Efforts for climate change adaptation require mobilizing financial resources to make infrastructure systems resilient, support the circular economy, and protect marine ecosystems, access to clean water and biodiversity. Therefore, climate transformation finance has become one of the prominent topics in the banking sector in recent years. Another opportunity for the banking sector is to leverage international resources and develop instruments to support projects within the scope of climate transformation finance.

Despite the social challenges of the climate crisis and growing inequalities across the globe, the banking sector's inclusive approach has the potential to accelerate sustainable development. The sector's focus on the social aspects of sustainability will ensure that financial resources are accessible to all segments of society, particularly vulnerable groups.

The sector needs to support activities aimed at promoting financial literacy, supporting education, ensuring gender equality, empowering women, and increasing youth employment. All of these developments provide the sector with various opportunities to develop financial products and services that aim to create social benefits and produce solutions to social problems.

For the banking sector, a digital transformation aligned with global technological developments is one of the biggest areas of opportunity. Supporting technological development and innovation and shaping financing sources, products and services in this direction serve the SDGs. In addition, digitalization of banking services is a practice that both strengthens inclusiveness and increases satisfaction with services.

4. A Detailed Look into Sustainability-Related Trends in the Sector

4.1. Findings

4.1.1. Sustainable Finance Approach

Sustainable finance is an approach that focuses on the consideration of environmental, social and governance issues when providing financing to investors. In recent years, the importance and impact of this approach has begun to be recognized, first in international markets and then in Türkiye. 90% of the member banks of the Association that responded to the survey conducted within the scope of the study indicated that they adopt a sustainable finance approach, including green and social-themed financing. These member banks stated that they have already implemented practices related to sustainability-linked syndication transactions, sustainable bond issuances, development of a sustainable financing infrastructure for SMEs, development of models to analyze the risks which the portfolio is and may be exposed to from an environmental and social perspective, support for sustainable agriculture and promotion of digitalization.

The banks have stated that in addition to issuing green bonds, they also extend loans for renewable energy and infrastructure, energy efficiency, resource efficiency, circular economy, and practices that play an important role in limiting the impacts of climate change. Practices that stand out under the theme of social finance include supporting women and young entrepreneurs, providing loans to alleviate the impacts of the pandemic, extending loans aimed at increasing the share of female employees, SME financing, financing of social infrastructure investments and financing of farmers.

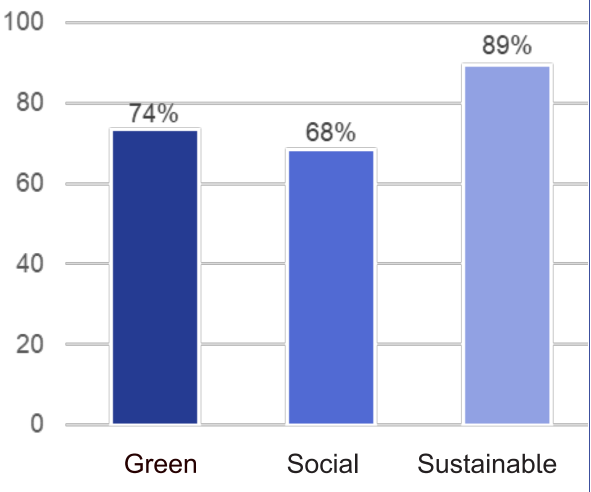


Figure 3: Future Targets of Banks (%)

Banks that currently have sustainable financing practices in place have indicated that they have set future goals for green, social, and sustainable finance. As seen in Figure 3, nearly 90% of the responding banks have set future goals for sustainable finance, 74% for green finance and 68% for social finance. Stating that they aim to closely follow current developments in sustainability and sustainable finance and to improve their current practices, the banks emphasized that they have set goals such as providing more financing towards SDGs, supporting regional development and priority sectors, increasing employment, supporting regions affected by migration, issuing sustainable sukuk, and developing financing resources for emergent green hydrogen technologies that do not yet have any financing opportunities. In addition, some of the banks stated that they aim to systematize the provision of sustainable, social, and green finance and to build internal and external capacity on sustainable finance.

The answers given by most of the member banks of the Association that participated in the study show that today, with national and international developments, banks take not only economic profitability but also social and environmental issues into account. The developments in sustainable finance are considered to be important in solving universal problems by avoiding greenwashing. Therefore, the banking sector in Türkiye, in general, believes that developments in sustainable finance support value-added practices on the one hand and the sustainable development of the national economy on the other. In addition, although banks acknowledged that sustainability-related initiatives in the sector have developed positively, they noted that the fact that approaches are not yet fully standardized and that the rules and measurement system is not yet structured leads to differences in procedures and practices between institutions. They have mentioned that a banking approach that can better manage risks for the banking sector and the acceleration of high value-added activities for society would play a major role in the transition to a low carbon economy. Therefore, it is important to follow current national and international developments.

Most of the member banks that responded to the survey emphasized the need for legal arrangements for tax exemptions in capital markets, making long-term investments mandatory, and strengthening investor confidence, highlighting the importance of supporting the existence of authorized firms in Türkiye for second party opinions in international issuances and the preparation of sustainable finance framework documents, following the initiatives taken in international capital markets, creating sectoral indices as well as special thematic indices in the field of sustainability, diversifying financing sources, increasing mandatory incentives, publishing guidance documents on this issue, increasing awareness and know-how in each segment, publishing a national taxonomy, developing appropriate and accurate data tracking and analysis systems, and adopting the principle of transparency in order to diversify green, social and sustainable finance products and instruments in the future.

Around 80% of the member banks of the Association that contributed to the survey stated that they include environmental and social risks in their risk management processes. In this context, as seen in Figure 4, approximately 90% of the banks that make assessments implement the IFC Performance Standards, 40% implement the Equator Principles and 33% implement the EBRD Performance Requirements, while some banks emphasized that they apply local legislation, approaches such as the OECD Recommendation on Common Approaches for Officially Supported Export Credits and Environmental and Social Due Diligence, the World Bank Environmental and Social Framework, and the United Nations Guiding Principles on Business and Human Rights. Some of the banks that contributed to the assessment have an activity-specific approach for environmental and social risk management, while others have a sector-specific or a combined approach.

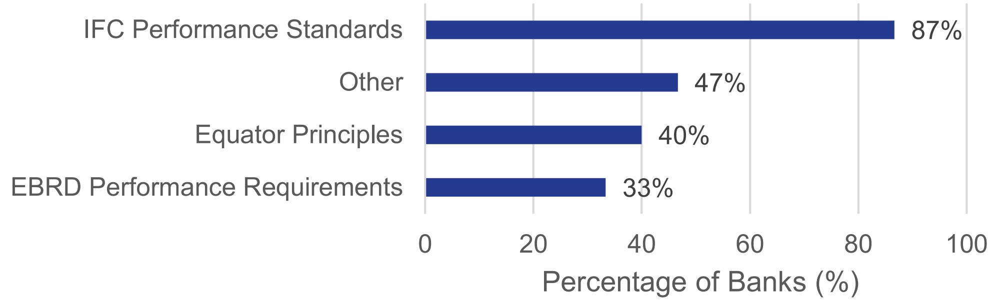


Figure 4: Standards Followed by Banks in Environmental and Social Risk Management (%)

It is seen that 33% of the member banks that contributed to the assessment adopt a credit limit-based or a hybrid approach based on limit and segment for the environmental and social risk assessment approach used in their lending activities, while 27% adopt a sectoral and investment amount-based approach and 7% adopt a segment-based approach (see Figure 5).

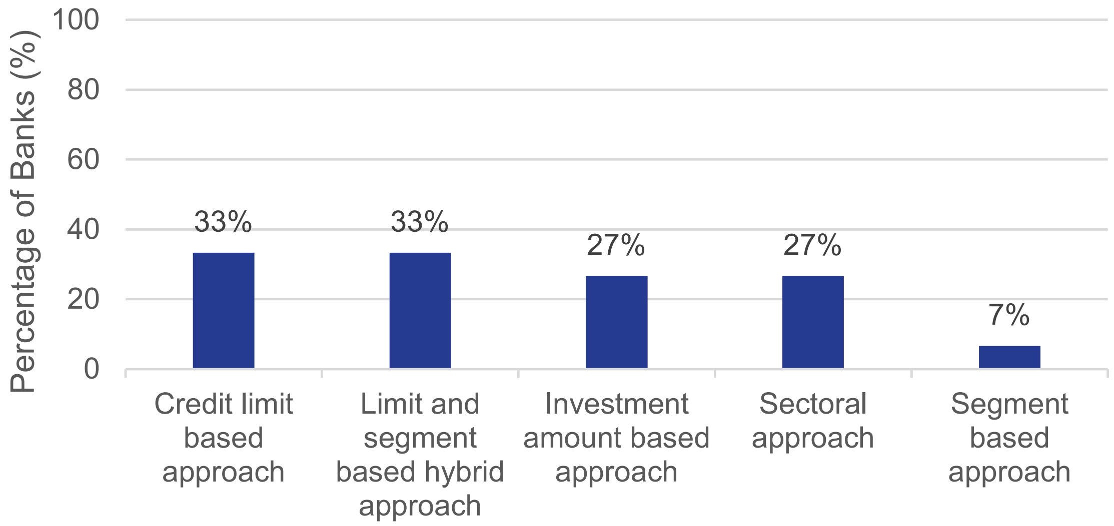


Figure 5: Approach of Banks in Terms of Risk Assessment Model (%)

One of the sustainable finance practices in the sector is to follow local and international initiatives in this area. While most of the member banks that contributed to the assessment stated that they are supporters of the Global Compact Türkiye Declaration of Sustainable Finance, some banks stated that they are included in the FTSE4Good Emerging Index, signatories of UNEP FI Principles for Responsible Banking (PRB), or members of NZBA.

In addition to reporting non-financial risks, 53% of the banks that contributed to the study emphasized that they also manage climate-related financial risks. These banks indicated that they manage climate-related financial risks creating a sectoral risk map, generating a heat map of the portfolio's climate risk, using a tool or software for climate risk of the portfolio, and managing climate-related financial risks through scenario analysis. To this end, they use information such as annual average precipitation and temperature increase/decrease data of the region, as well as UNEP FI scenario analysis approach.

4.1.2. Climate Finance

Climate finance is defined as financing projects and investments for climate change mitigation and adaptation with the aim of keeping the global temperature increase below 2°C compared to the pre-industrialization period and limiting this increase to 1.5°C as stated in the Paris Agreement.

In this context, 80% of the member banks of the Association stated that they keep up with climate finance. The climate finance practices followed by these banks are shown in Figure 6. Accordingly, banks mostly use financing practices in areas related to clean energy transition, energy efficiency, transition to low carbon economy, blue finance, circular economy and waste, sustainable agriculture and food security, and green technologies. They also emphasized that they have practices related to biodiversity, green housing, inclusive and sustainable cities, wastewater and water management.

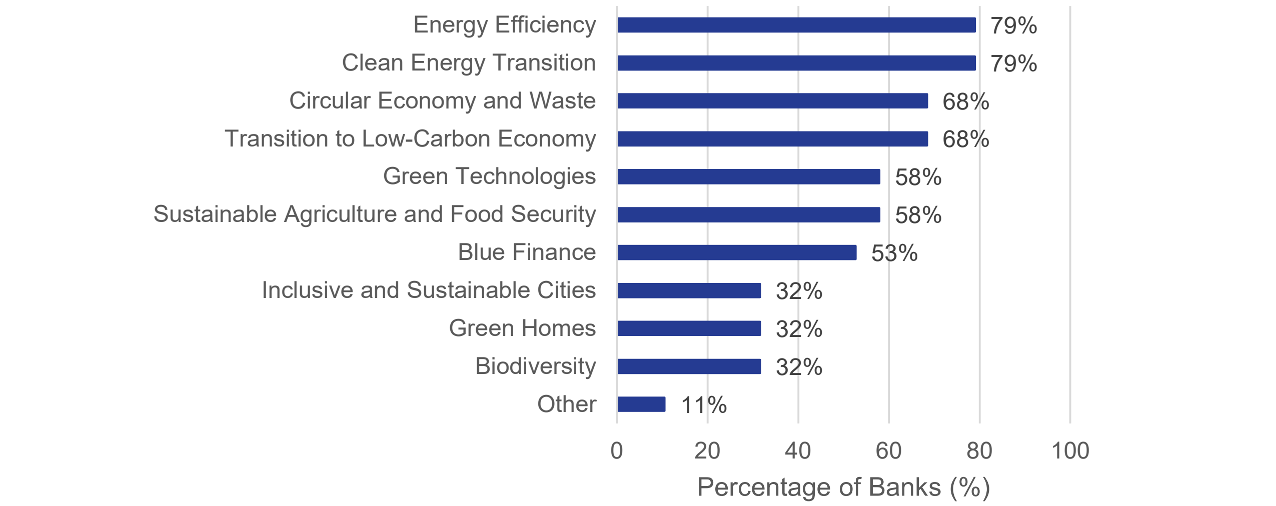


Figure 6: Share of Member Banks' Support for Climate Finance Practices (%)

The banks stated that within the scope of clean energy transition financing, they primarily support renewable energy applications, providing financing for solar energy projects at a rate of 100%, wind and hydroelectric projects at a rate of 94%, biomass projects at a rate of 81%, and geothermal energy projects at a rate of 75%. They also indicated that they support investments in electrification, green hydrogen and tidal energy. Approximately 80% of the banks that participated in the study emphasized that they have financing instruments for energy efficiency in industry, 63% in transportation, 58% in buildings and 53% in agriculture. Some banks also reported financing energy efficiency practices in the context of municipal services, energy supply, energy management and audits.

It is observed that one of the climate finance practices on the agenda of the banking sector is the discussions about phasing out coal finance. Some of the banks that participated in the study stated that they do not provide financing for new coal projects. While some of the banks declared that they do not provide financing for new coal projects within the scope of transition to a low carbon economy, it is observed that banks provide loans for environmentally friendly projects such as the development of the renewable energy portfolio, production of electric and hybrid vehicles, promoting low-carbon transportation methods such as electric charging stations, support for sustainable agriculture, and implementation of practices that increase process efficiency. Some banks that consider environmental and social risk assessment in project and investment loans emphasized that they take into account international criteria in the environmental and social field in project financing processes. In addition, some banks reported supporting practices such as energy storage, circular economy, alternative fuels, new technology investments, sustainable forest management and biogas production. The breakdown of resources used by the member banks of the Association for climate transformation finance is presented in Figure 7.

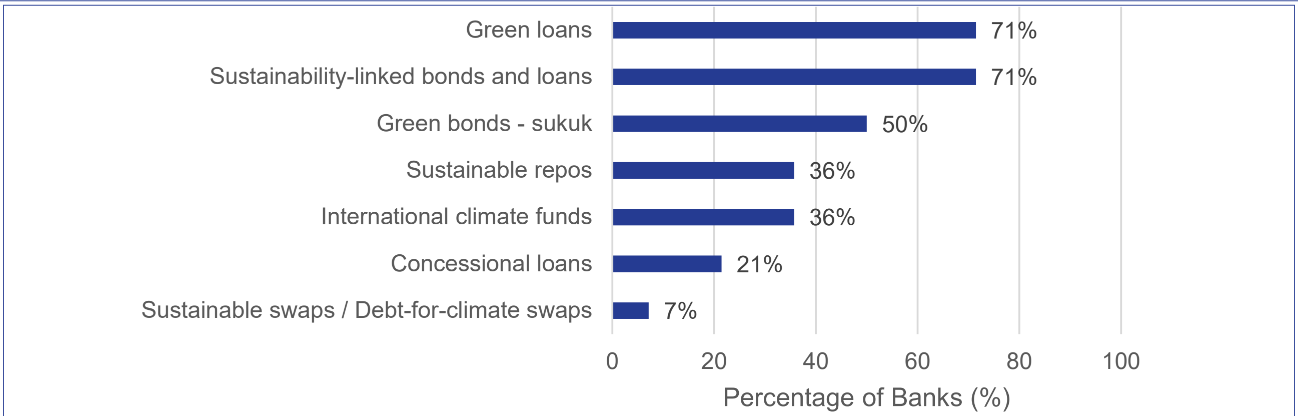


Figure 7: Sources Used by Banks for Climate Finance (%)

The majority of the member banks stated that they use green loans as well as sustainability-linked bonds and loans. Besides, it is understood that the instruments provided by banks for climate finance are likewise mostly green bonds and sustainability-related bonds as seen in Figure 8.

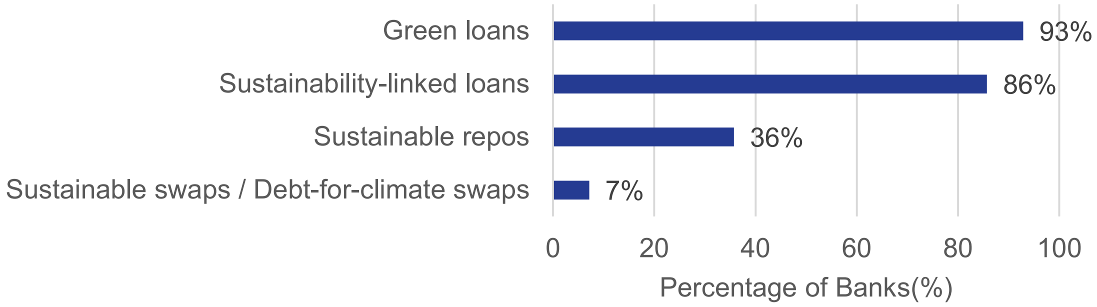


Figure 8: Resources Provided by Banks for Climate Finance (%)

4.1.3. Blue Finance

Under green and sustainable finance, different types of financing are diversified on a topic-specific basis, including blue finance. Supporting practices such as securing access to clean water, protecting underwater environments, promoting nature-friendly marine tourism, using renewable energy on the high seas, and protecting the seas in port activities are considered within the scope of blue finance (see Figure 9). Although it is observed that blue finance is not yet supported in Türkiye to the extent that clean energy transition and energy efficiency investments are supported, banks stated that they mostly support wastewater management investments within the scope of blue finance. It is seen that 53% of the member banks of the Association support blue finance (see Figure 10).

Practices for the protection and efficiency of water resources are projected to increase in importance for Türkiye in the coming period, and banks are expected to diversify their blue finance practices. Continuing to carry out studies to determine the roadmap for blue finance and biodiversity finance applications, banks aim to diversify their products for practices related to the recovery of wastewater in industrial zones, ship ballast water treatment systems and gray water treatment systems as well as the maintenance and repair of these systems, the development of blue finance through sustainable sukuk issuance, increasing the efficiency of water resources, protecting the seas, protecting agricultural lands, preventing the decline of living species and ecosystem degradation.

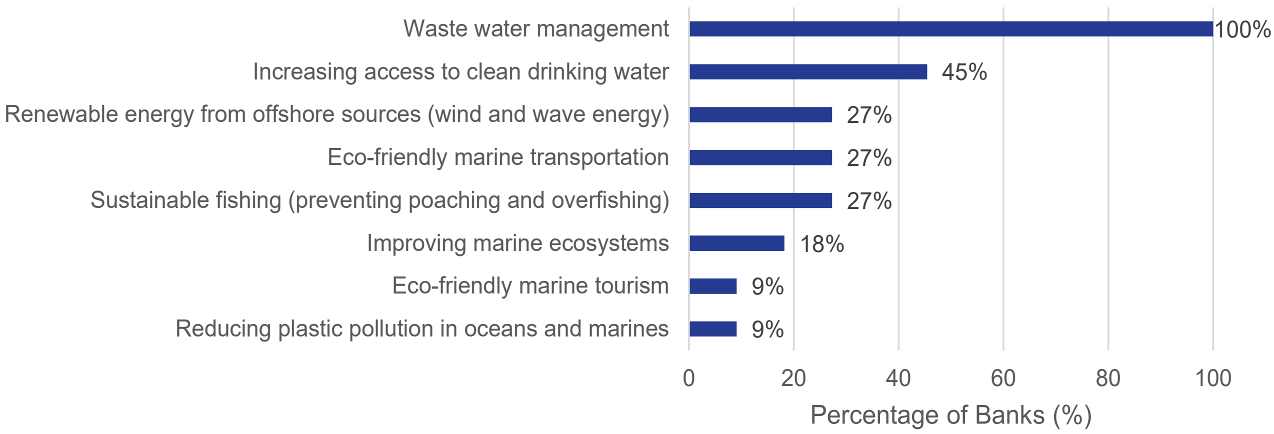


Figure 9: Blue Finance Practices of Banks (%)

4.1.4. Waste Management and Environmental Protection Finance

It is observed that the banking sector also mainly supports activities aimed at protecting the environment under the heading of green finance. It is seen that approximately 70% of the banks that participated in the study provide financing for waste management and circular economy (see Figure 11).

In order to reduce the environmental impact of investments and projects and to live in a sustainable world, member banks ensure the effectiveness of their work with an environmental management system and support activities to prevent, reuse, recycle and recover waste in order to effectively manage hazardous and non-hazardous waste from domestic and/or industrial sources. Banks, which advocate the need to raise awareness on waste management and circular economy, also state that they offer trainings in this context and that they were entitled to receive Zero Waste Certificates in many locations.

4.1.5. Biodiversity Finance

Biodiversity finance plays a critical role in halting biodiversity loss and ecosystem degradation and enabling transformative changes. 32% of the member banks of the Association support biodiversity finance (see Figure 12). Some of the banks stated that they do not finance activities in wetlands identified on the "List of Wetlands of International Importance (Ramsar List)" and activities prohibited under the "Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES)".

Banks that do not have any projects directly linked to biodiversity in their portfolios emphasized that the projects they finance that have a positive environmental impact have an indirect positive impact on biodiversity and that they consider biodiversity in their risk assessment processes, thus supporting biodiversity finance.

Blue finance projects, which cover activities to protect the underwater ecosystem, also align with biodiversity finance. The banks state that agricultural finance is directly oriented towards biodiversity conservation and that they contribute to biodiversity conservation by supporting socially, economically, and environmentally sustainable agriculture with their loan products.

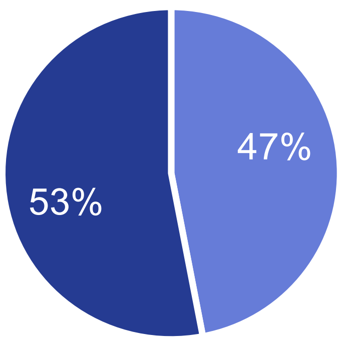


Figure 10: Share of Banks Supporting Blue Finance (%)

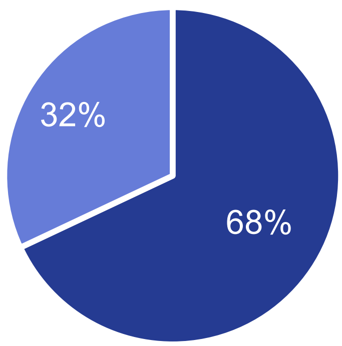


Figure 11: Share of Banks Supporting Waste Management and Circular

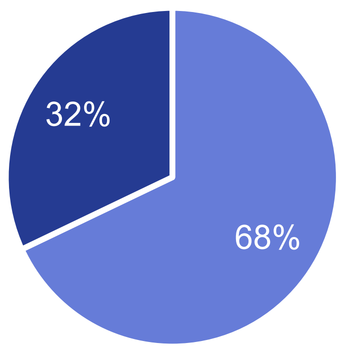


Figure 12: Share of Banks Supporting Biodiversity (%)

■ Supporting Banks ■ Non-supporting Banks

4.1.6. Sustainable Agriculture Finance

Sustainable agriculture and the financing of practices for sustainability in agriculture are also among the practices addressed within the scope of sustainable finance. Approximately 60% of the banks that responded to the survey state that they finance practices for sustainability in agriculture. Preventing damages to the agricultural sector due to the climate change or supporting climate-adaptive agricultural practices are among the prominent examples. Banks with financing packages aimed at ensuring sustainable agriculture and food security offer services for reducing excessive water consumption in agricultural production, effectively utilizing waste, ensuring food security, and obtaining agricultural products with the most efficient methods. The banks offer repayment facilities to meet the needs of farmers, incentives for the modernization of agricultural machinery and equipment (modern pressurized irrigation systems, agricultural mechanization, cold storage rooms, digitalization in agriculture for irrigation, fertilization, and spraying information, etc.), and support for organic agriculture, animal production, aquaculture, seedling cultivation, and biogas production from organic waste in animal farms.

4.1.7. Sustainable Cities and Green Buildings Finance

Member banks of the Association also offer products and services for financing inclusive and sustainable cities and green housing. Some of the banks emphasized that they offer interest rate discounts and discounted loan allocation fees for houses classified as energy class A or B. Some encourage the preference of environmentally friendly home and workplace loans, urban transformation loans, rooftop SPP loans, green building investments and buildings with certain environmental certificates. In addition, a number of banks pointed out that they have financed many sustainable and inclusive projects in cooperation with municipalities and supported initiatives in these areas.

4.2. Targets and Future Outlook for the Sector

Recognizing that the finance and banking sector assumes an important responsibility in the transition to a sustainable economy, the majority of the member banks of the Association pointed out that they have set future targets for international sourcing, service, and product development in the field of climate finance. Some banks that have initiated roadmap studies on climate transformation mentioned that this issue is also included in their strategic goals. Declaring that they will continue to promote projects that serve to minimize and eliminate physical and transition risks related to climate change, the banks state that they aim to raise the awareness of all stakeholders on this issue and to support transformation.

In relation to their future targets, the banks mentioned that they aim to increase and develop low-carbon economy transition, clean energy transition and energy efficiency financing practices both in terms of type and financing volume.

Banks often declare that they aim to generate indirect impact by playing a supportive and transformative role in combating climate change, transition to a net zero economy and energy efficiency. They also stated that they will continue to provide sustainable external financing resources needed by the real sector and work to increase them, prioritize energy efficiency and renewable energy projects in addition to environmentally friendly projects, provide financing for hybrid vehicles and bicycles, focus on support in the alternative energy sector, and refrain from financing some activities that cannot be characterized as sustainable.

Some banks, which have been working on SME support and financial leasing investments within the scope of energy efficiency, emphasized that they aim to issue sustainable sukuk in the coming period, that they will develop studies on the ESCO Model[26] and that they will continue to support the responsible consumption of energy resources by identifying the needs of energy-intensive sectors. The banks attach importance to raising stakeholder awareness on this issue and state that they aim to provide direct and indirect support to their stakeholders in the transition process towards the EU Green Deal. Within the scope of financing the transition to a low carbon economy, NZBA signatory banks have announced plans to align their loan and investment portfolios with zero emission targets by 2050.

The member banks of the Association, which find the developments in the field of climate transition finance in the finance and banking sector pleasing for a sustainable world order, consider that the lack of a single green taxonomy to be followed by all countries or Türkiye, inadequate legal regulations and incentives, lack of infrastructure for reporting and data collection, and continued industrial investments due to Türkiye's status as a developing country are challenges to the development of this field in Türkiye.

The member banks of the Association that contributed to the survey consider the following as the main needs of the sector: contributing to both the development of the sector and informing stakeholders by sharing good practices and experiences with one another, developing standards and legislation to be applied in Türkiye for climate transformation finance, increasing the sanctioning power of regulators by enacting rules into law, increasing training and awareness for mitigating and adapting to the impacts of climate change, and setting sectoral targets.

26. *"Energy Service Companies" and "Energy Performance Contracting" implemented by them.*

4.2.1. Impact Investing

Most of the member banks of the Association that participated in the survey pursue impact investing, which prioritizes creating measurable positive social and environmental impact over financial return. While 58% of these banks have a methodology or tool in place to monitor their environmental and social impacts arising from their direct and indirect activities, 42% do not have a monitoring methodology. Some of the banks that employ a methodology have an environmental and social risk assessment and a list of prohibited activities that support the identification, categorization, monitoring, and remediation of environmental and social risks arising from the firm's operations and the project to be financed, including the requirements set by legislation and bank policies. Some of the banks stated that the impact is analyzed by calculating the emissions resulting from direct and/or indirect impacts, CDP reporting, measuring the exposure of companies and projects to climate risks with a tool, determining the contribution to the SDGs and making assessments with sectoral climate change heat maps and scenario analysis methods.

As shown in Figure 13, under impact investing, nearly 90% of the surveyed member banks of the Association finance areas related to combating climate change, 85% finance areas related to the inclusion of SMEs in the value chain, while only around a third of them finance humanitarian aid. In addition to these areas, banks support gender equality and inclusion, sustainable agriculture, conservation of natural capital, support for quality education, support for young entrepreneurs, microfinance, and spaces for healthy and quality living.

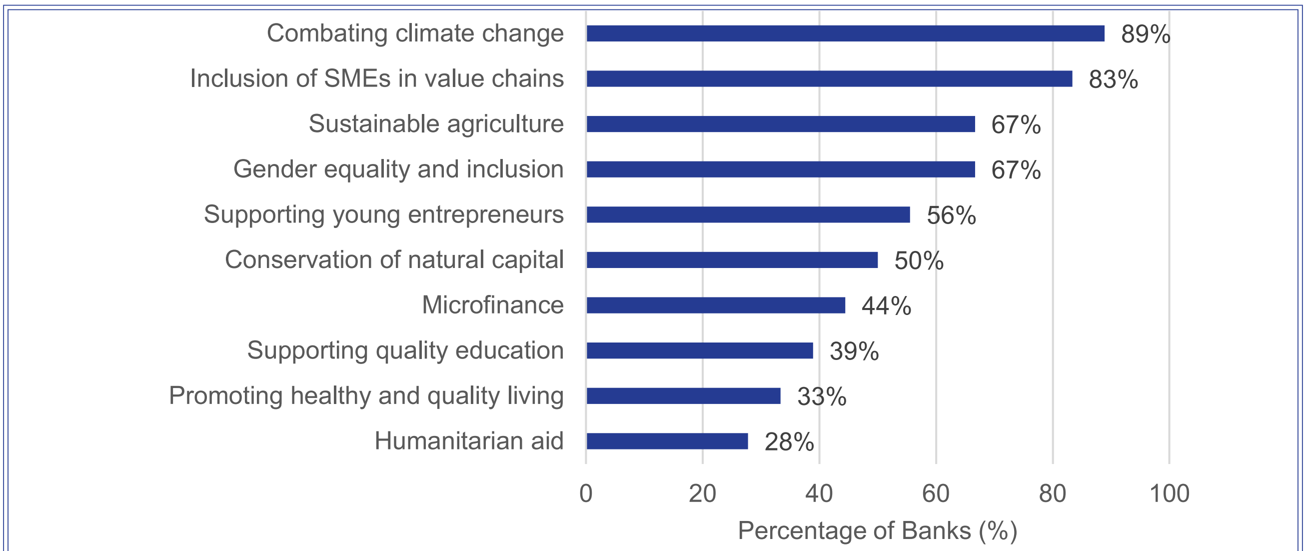


Figure 13: Impact Investing Activities Financed by Banks (%)

As seen in Figure 14, responding banks stated that they use multiple financing instruments within the scope of impact financing, including loans, bonds, equity, and intermediary financing instruments. Banks use loans the most (89%) and intermediary financing instruments the least (17%).

In addition, around 85% of the banks stated that they have set future goals for impact investing and financing. These goals include supporting financial, social, and environmental gains through impact investing by increasing global and local partnerships, improving the environmental and social risk assessment process, increasing financing for impact investing, and improving data collection and analysis so that impact is measurable.

While some of the member banks responding to the survey evaluated the developments in impact investing and impact financing positively, the lack of awareness of the society and SMEs, the prioritization of profitability by companies and banks, and the lack of relevant data were cited as challenges to the advancement of this concept in Türkiye. The needs to address these challenges include designing environmental and social risk assessments in line with the dynamics of all segments, reducing the profitability concerns of companies and banks related to impact investing through various tax exemptions, further developing the market for impact investments, and formulating tools to accurately assess the gains and impacts of potential investments.

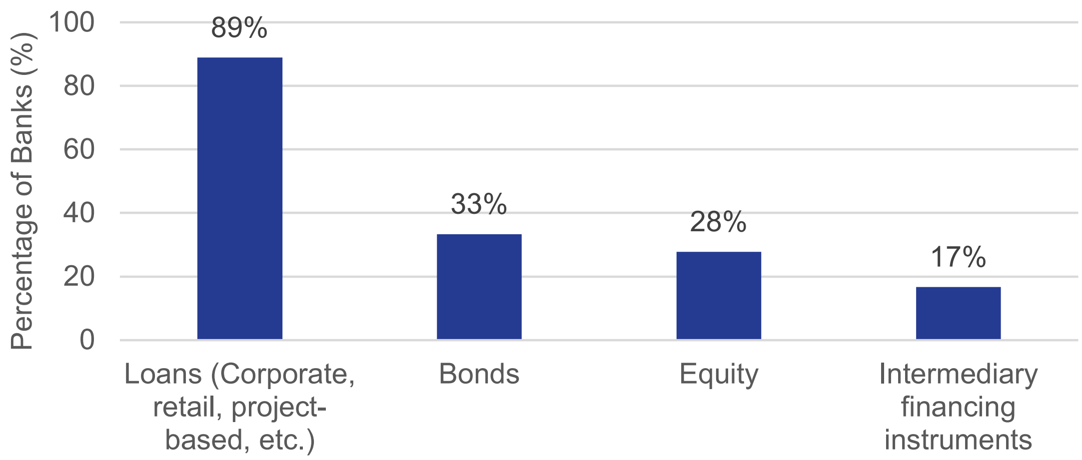


Figure 14: Instruments Used by Banks in Impact Financing (%)

4.2.2. Inclusion

Inclusion is defined as the pursuit of equality for all members of society without discrimination based on belief, gender, age, ethnicity, disability and/or political opinion. It is apparent that inclusion and equality practices are widespread in the banking sector, as 80% of the member banks that participated in the survey stated that they carry out activities in this context. As indicated in Figure 15, survey responses indicate that banks adopt similar and advanced practices in terms of equality and inclusion trainings, measures to prevent harassment and violence in the workplace, supporting local employment, promoting employment of persons with disabilities, equal training and development opportunities, fair and equal remuneration, fair and equal human resources processes and gender equality.

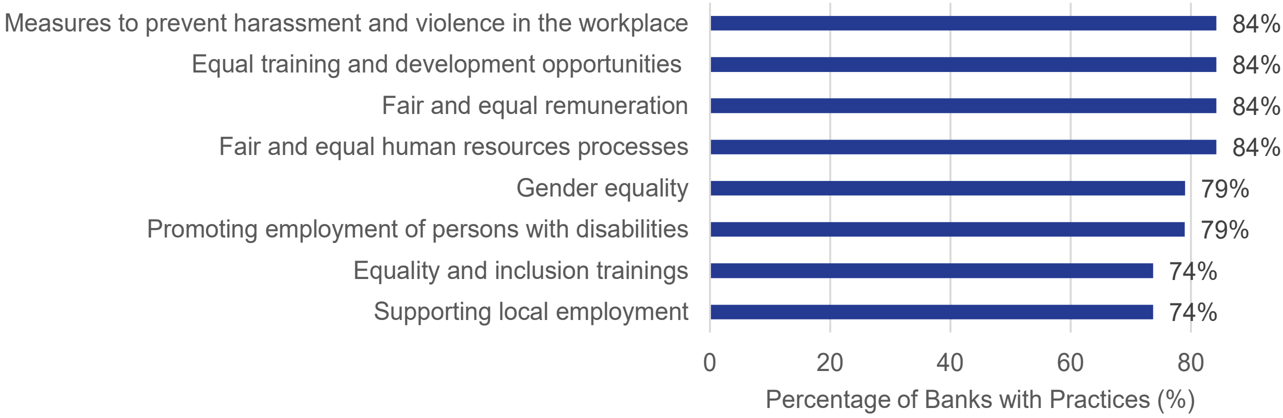


Figure 15: Banks with Inclusion-Related Practices (%)

The finance and banking sector has higher rates of female employees compared to other sectors. According to BAT data for 2021, the average female employment rate in the banking sector is 50%. As shown in Figure 16, more than half of the member banks of the Association that responded to the survey have over 50% female employees. From the perspective of gender equality and women's empowerment, the share of women in managerial and decision-making positions is also among the indicators monitored. In this respect, the share of women in senior management being parallel to the share of female employees in the sector and the average wage gap between male and female employees in the same position are considered important indicators for assessing gender equality. Most of the member banks of the Association that contributed to the assessment stated that they adopt the principle of equal pay for equal work. However, as seen in Figure 17, it is noteworthy that although the share of female employees in the sector is over 50%, the share of female executives in senior management is lower than the sector average.

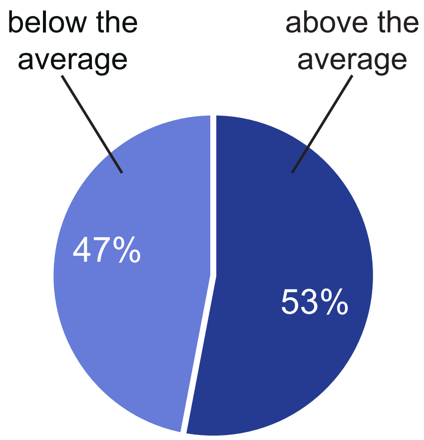


Figure 16: Banks where the Number of Female Employees Exceeds the Sector Average

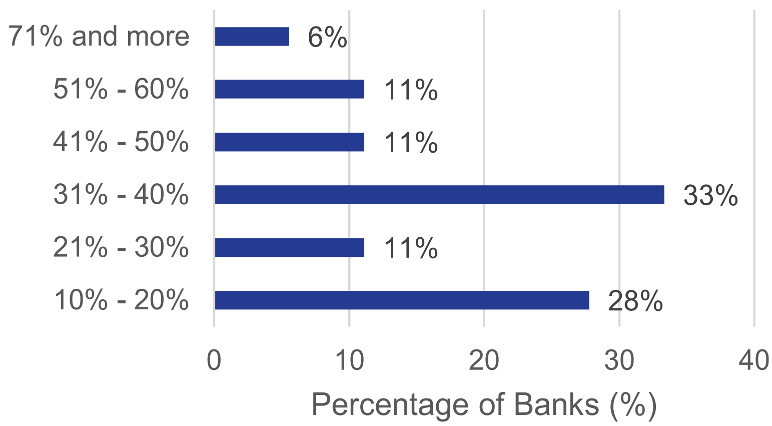


Figure 17: Share of Female Employees in Top Management Positions of Banks (%)

While all of the member banks of the Association that contributed to the assessment have physical facilities that support gender equality in the workplace as indicated in Figure 18, some of them emphasized that they provide support such as daycare centers or flexible working opportunities for employees with children, paternity and maternity leave practices in addition to legal leave, have implementation instructions/procedures on gender-neutral human resources processes management, methods for management of harassment and violence cases at workplace and relevant implementation instructions/procedures, corporate commitment, strategy or policies on gender equality, internal or external communication activities focused on gender equality, and gender equality trainings.

A few member banks stated that they will work on quantitative targets and policies for gender equality in the coming period within the framework of equality and inclusion, provide training to all employees in this context, create an employee platform for employees to raise their voices in an impartial environment, and support women's career development through a leadership program for women and mentoring sessions.

Approximately 90% of the member banks that responded to the survey stated that they carry out Corporate Social Responsibility (CSR) activities/projects in order to create social benefits and find solutions to social problems. Besides, they stated that carry out CSR activities within a specific strategy and predetermined budget.

Figure 18: Share of Banks with Gender Equality Practices (%)

As shown in Figure 19, approximately 85% of the member banks of the Association that contributed to the survey are engaged in activities related to reducing environmental impact, while the majority of them are engaged in sponsoring cultural, artistic and sports activities, raising public awareness on sustainability, increasing access to digital platforms, supporting technology development and innovation, supporting people who have limited access to financial resources, supporting women entrepreneurs and business owners, increasing youth employment, contributing to education, animal welfare and financial literacy.

Approximately three quarters of the member banks of the Association that contributed to the assessment have a corporate volunteering practice where bank employees come together to develop solutions on social issues and carry out volunteering activities led by the organization.

In addition, 90% of the member banks have an easily reachable banking application to facilitate access to banking services for persons with disabilities. 47% of the banks which attended the survey stated that they support persons who have limited access to financial products and banking services. They emphasized that digital platforms and mobile applications facilitate access to financial opportunities for disadvantages groups such as persons with disabilities and persons who live in rural areas.

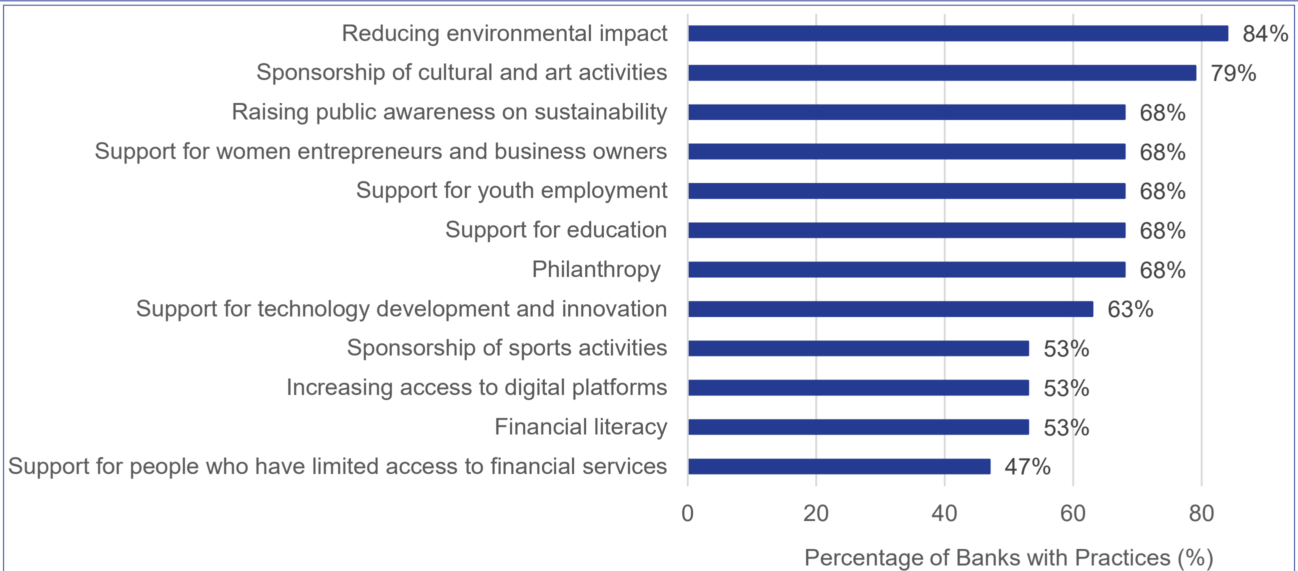


Figure 19: Share of Banks with CSR Activities (%)

As seen in Figure 20, the leading products and services offered by the member banks of the Association within the scope of financial inclusion are support for women entrepreneurs and employers with a share of 85%, followed by support for tradesmen and SMEs, support for agricultural activities and farmers, support for young entrepreneurs, and services for disadvantaged groups with limited access to banking services.

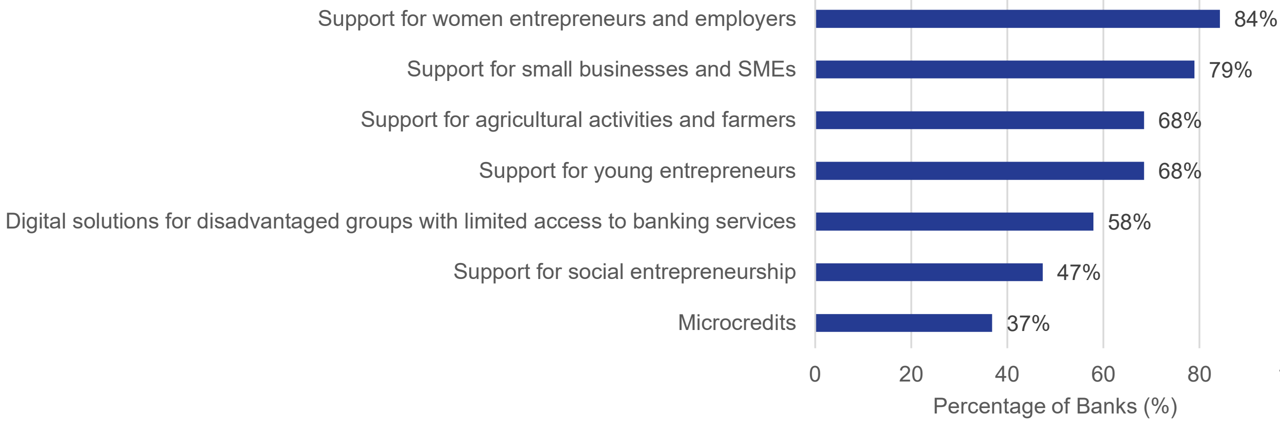


Figure 20: Products and Services Offered by Banks within the Scope of Financial Inclusion

4.2.3. Sustainable and Green Taxonomy

One of the prominent issues in the process of developing sustainable finance practices is sustainable taxonomy and standards. The European Union (EU) has made significant progress in terms of sustainable finance taxonomy as part of its green transformation activities. In order to define and standardize sustainable investments, the EU started to work on the creation of a sustainable finance taxonomy. Six main headings were defined under the EU Taxonomy in 2020. These headings are are climate change mitigation, climate change adaptation, the sustainable use and protection of water and marine resources, the transition to a circular economy, pollution prevention and control, and the protection and restoration of biodiversity and ecosystems.

The banking sector in Türkiye closely follows the said taxonomy. Approximately 80% of the member banks of the Association that participated in the survey stated that they are working on harmonization with the EU Taxonomy. Around 85% of banks tackling compliance with the Taxonomy stated that they were working on internal review of the Taxonomy and its technical annexes, and some of them stated that they were working on calculating the green asset ratio according to the Taxonomy, categorizing the loan portfolio according to the Taxonomy, and collecting data from customers to analyze compliance with the Taxonomy (see Figure 21). Nearly 70% of the banks that participated in the assessment mentioned that they have plans to comply with the Taxonomy.

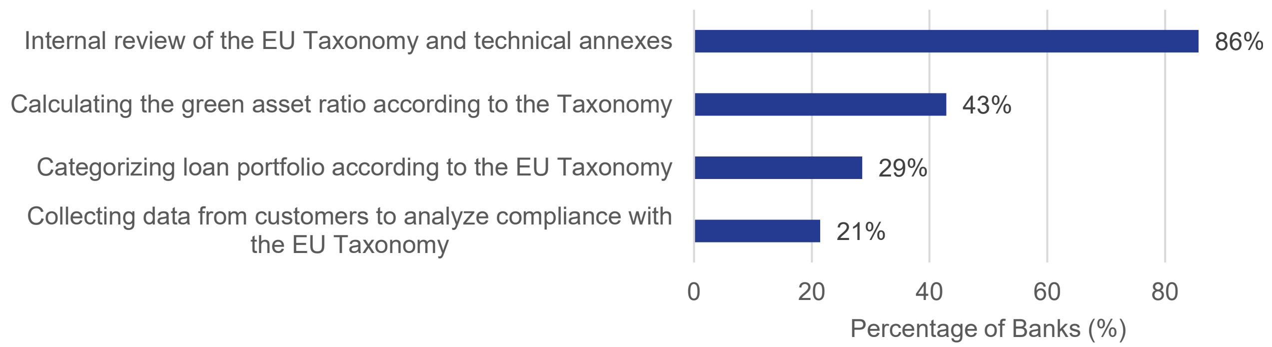


Figure 21: Activities of Banks Towards Compliance with the EU Taxonomy (%)

Member banks that participated in the assessment expressed their views on the level of importance of the EU Taxonomy objectives for the banking sector, as shown in Figure 22. According to the banks, climate change mitigation is of the highest importance, followed by climate change adaptation, transition to a circular economy, protection and restoration of biodiversity and ecosystems, sustainable use and protection of water and marine resources, and pollution prevention and control. These results indicate that climate change is among the highest priority issues for the banking sector in Türkiye, both in terms of mitigation and adaptation.

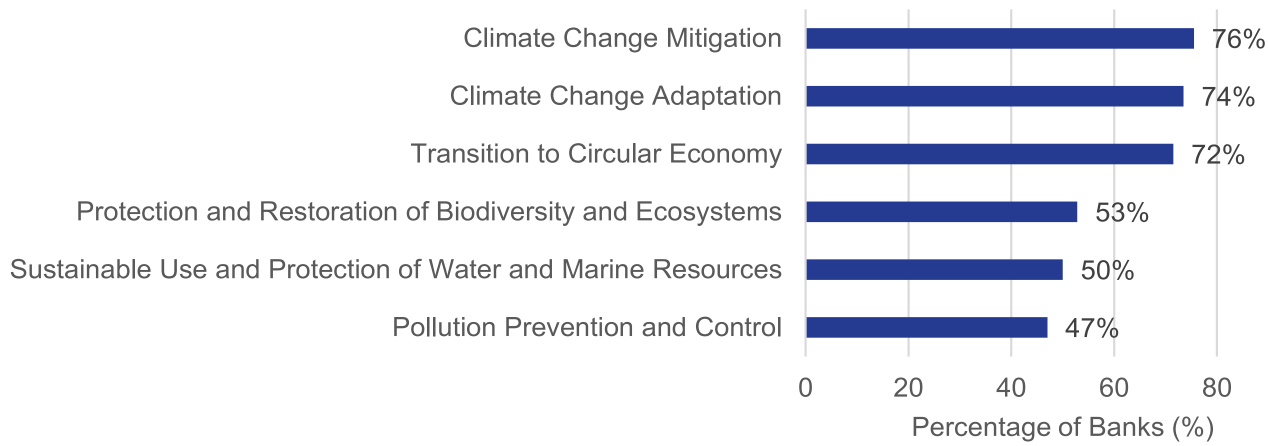


Figure 22: Importance of EU Taxonomy Objectives for the Sector as Rated by the Banks (%)

When the surveyed member banks assessed the obstacles to the classification of economic activities in the banking sector in Türkiye and compliance with the EU Taxonomy, 95% identified the deficiencies in legislation and other relevant legal regulations, nearly 80% identified lack of awareness, and 72% identified inadequate monitoring and supervision as the biggest obstacles. Besides, some banks,cited lack of data and inadequate technical assessment.

4.2.4. Digitalization

Digitalization, which has become widespread with technological developments and corresponds to the transfer of data to the digital environment, is widely used in the banking sector as in every sector. Of the member banks of the Association that responded to the survey, 95% stated that they have digital banking practices and a digital transformation strategy in line with technological developments. As can be seen in Figure 23, the digital banking practices that banks implement are mostly related to payment systems, credit transactions and insurance transactions. In addition, almost 70% of the banks have practices related to digital branches, while 40% stated that they have integrated digitalization into the banking sector for the digital wallet function. It is understood that widespread digitalization due to technological developments has played a role in the digital transformation strategy of approximately 90% of the member banks of the Association that participated in the study.

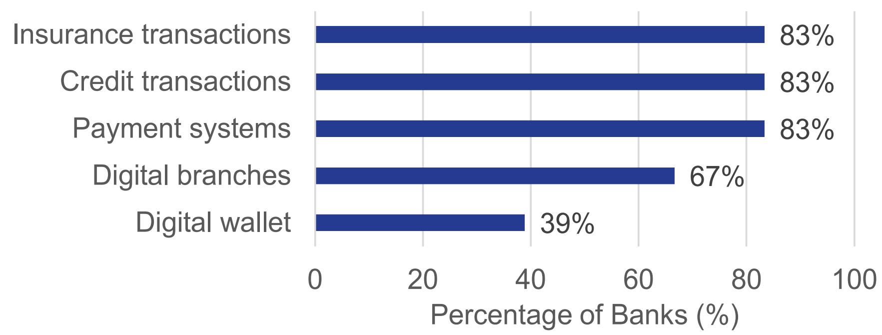


Figure 23: Digitalization Practices of Banks (%)

An analysis of the number of digital customers of the member banks of the Association that responded to the survey shows that the total number of digital customers of all banks increased by 50% in 2022 compared to 2020 (see Figure 24).

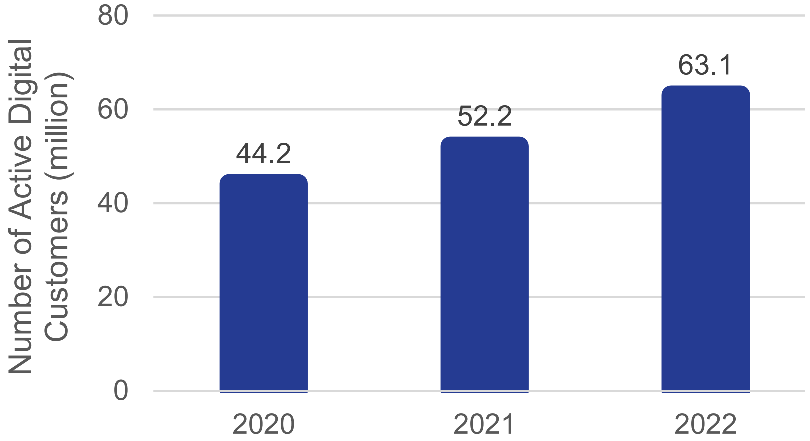


Figure 24: Number of Banks' Digital Customers by Year

Collaborations with fintech companies and startups are among the prominent practices in the digitalization process of the banking sector. Approximately 65% of the member banks of the Association that participated in the assessment stated that they collaborate with fintech companies to provide a wider range of services by creating added value in a digitalized world. In this context, the aforementioned banks digitalize their signature processes and work on issues such as reducing the use of paper and recycling electronic waste. While banks stated that they benefit from new generation technologies in the process of enhancing customer experience and digitalization (see Figure 25), they emphasized that they mostly use robotic process automation, big data and data analytics and artificial intelligence. In addition, they also benefit from technologies such as process automation, machine learning, cloud-based technologies, regulatory technologies, blockchain, deep learning and text analytics.

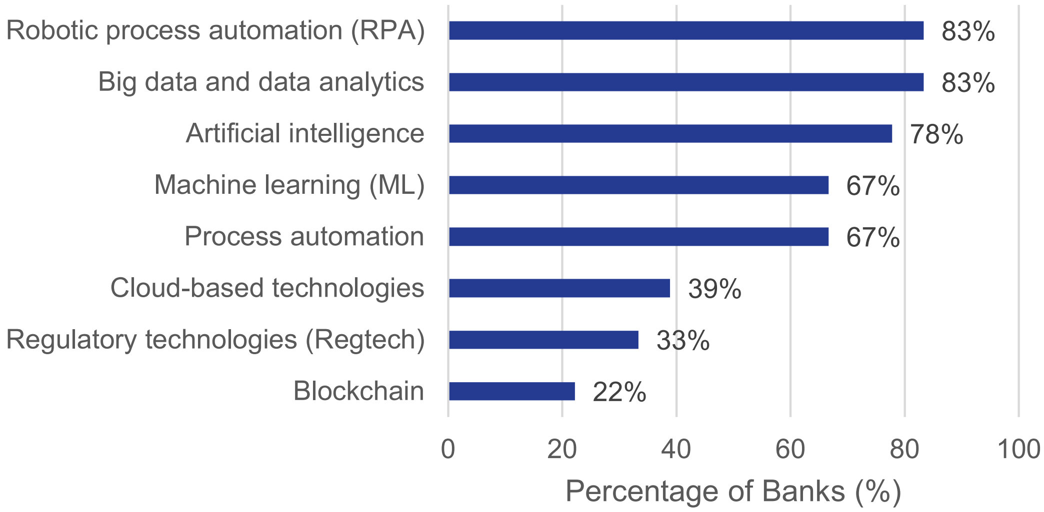


Figure 25: Technologies Used by Banks (%)

Around 65% of the member banks of the Association that responded to the survey offer open banking, one of the biggest global steps towards digitalization. Regarding digitalization practices, half of these banks also reported investing in blockchain technology and having an online supplier portal or platform.

As shown in Figure 26, 95% of the surveyed member banks of the Association aim to respond quickly to customer requests and speed up banking transactions through digital banking services, while around 90% aim to acquire new customers and reduce error rates in banking transactions. In addition, some of the banks stated that they aim to increase financial inclusion, keep records digitally and reduce transaction costs.

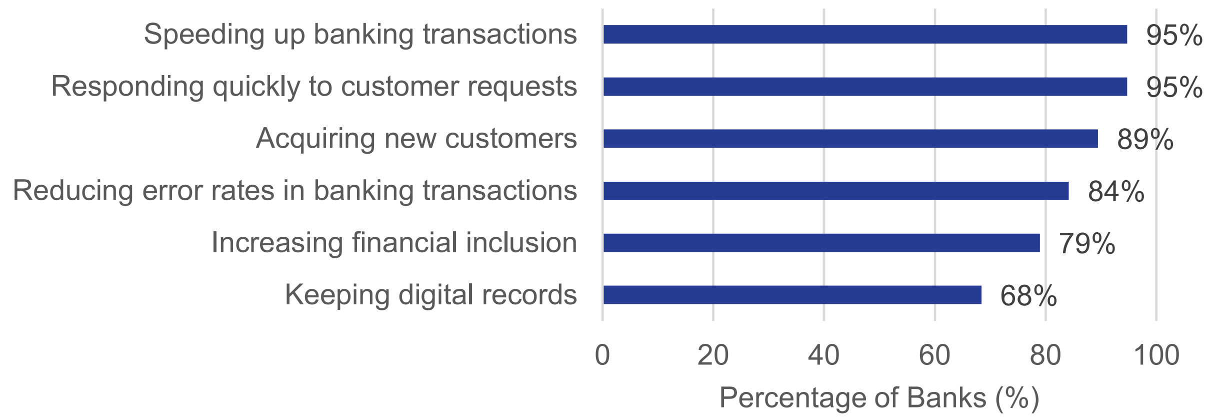


Figure 26: Topics Targeted by Banks with Digital Banking Services (%)

4.2.5. Non-Financial Reporting and Capacity Building

An outcome of the increasing awareness of sustainability, the widespread use of reports that include explanations of the social, environmental, and economic activities of businesses has led the banking sector to take action in this regard. Approximately 70% of the member banks of the Association that contributed to the survey stated that they disclose their sustainability activities to the public through non-financial reporting. While 38% of these banks have been reporting for 10-15 years, their reporting history ranges from 2 to 15+ years as seen in Figure 27.

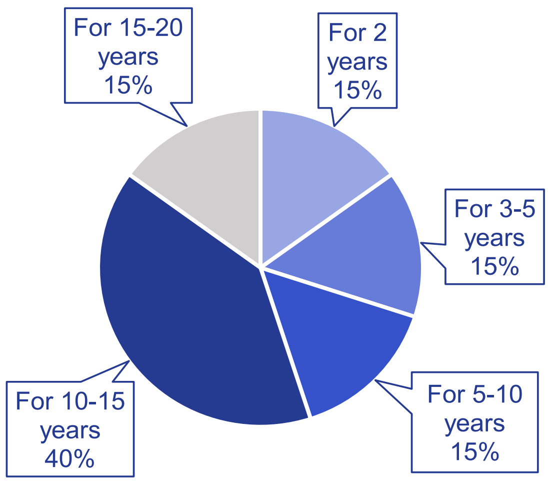


Figure 27: Non-Financial Reporting History of Banks (%)

The types of sustainability performance reports published by banks that contributed to the assessment and prepare non-financial reports are shown in Figure 28. Approximately 80% of these banks publish their sustainability performance through an integrated annual report, 70% through a CDP climate report and sustainability report, 50% through a CDP water report, 25% through an integrated report and 10% through a TCFD report. In addition to the above-mentioned reports, some banks stated that they communicate this information through the Global Compact Progress Report, Women's Empowerment Principles (WEPs) progress report, UNEP-FI Principles for Responsible Banking report and impact report.

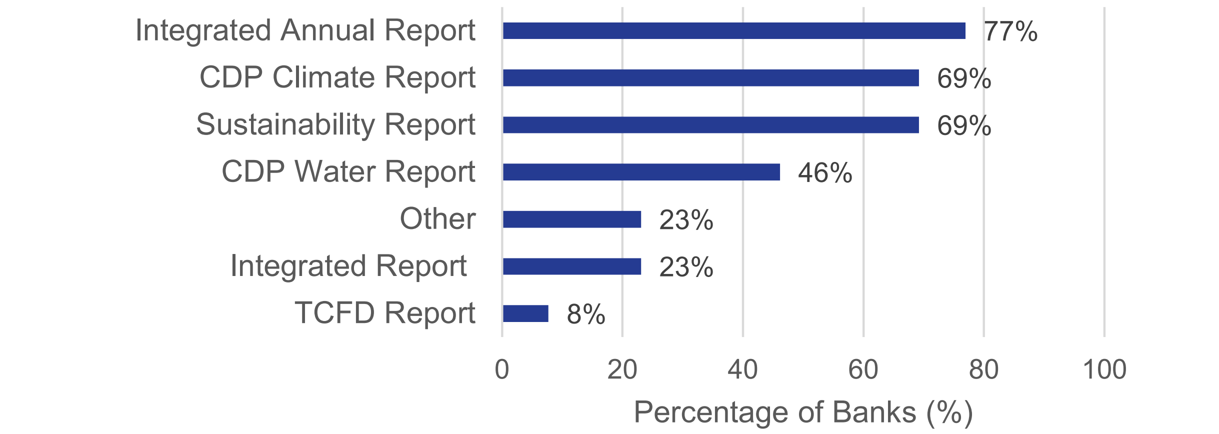


Figure 28: Reports Published by Banks to Share their Sustainability Performance (%)

Of the banks that contributed to the assessment, 95% stated that there is a need to increase the level of knowledge of the finance and banking sector on climate risk management, nearly 90% on climate finance and sustainable financing approach, 85% on impact financing, 70% on managing the environmental and social impacts of lending activities, 65% on sustainability reporting and financial inclusion, 60% on financial literacy, and 50% on equity and inclusion (see Figure 29). In addition, one bank stated that there is a need to increase the level of knowledge on the innovations and investment products the International Financial Reporting Standards (IFRS) will introduce.

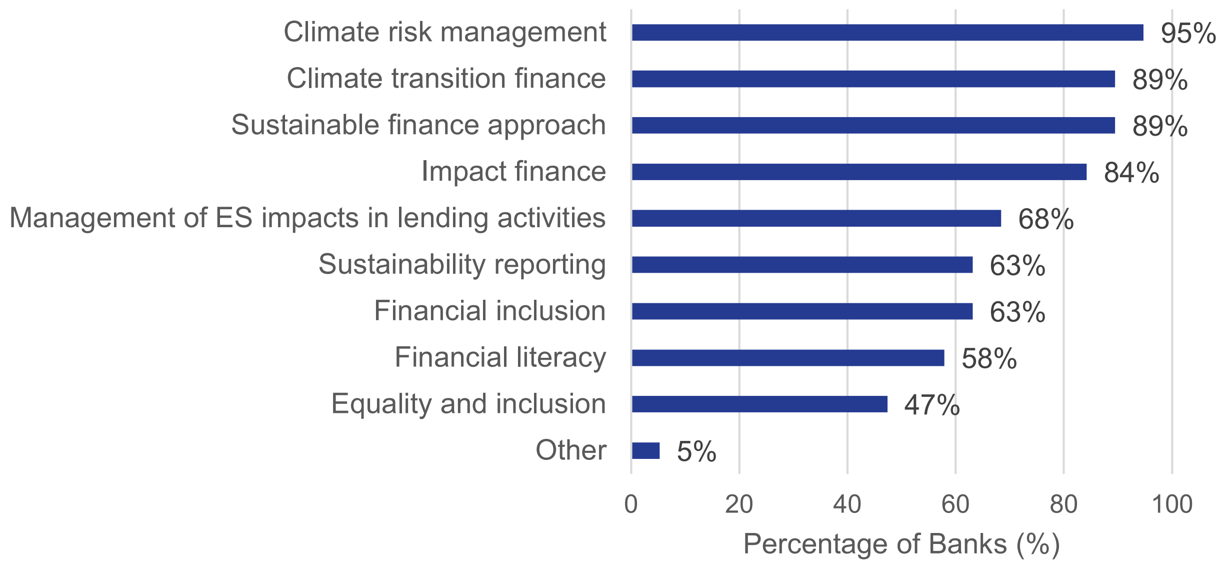


Figure 29: Areas where the Level of Knowledge of the Finance and Banking Sector Needs to be Increased According to Banks (%)

The member banks of the Association that contributed to the assessment state that environmental and social developments will affect economies more and more every year, and that financial solutions that contribute to the sustainability goals of all stakeholders without greenwashing will increase the market volume.

Noting that good practices in the finance and banking sector should be continued and developed in accordance with transparency and ethical values, banks stated that the workshops organized by BAT can be dynamic, informative, and guiding in communicating good practices. While they pointed out that sustainability-related know-how in the banking sector should be shared especially with public institutions, they consider that it would be very beneficial for the banking sector for regulatory bodies to establish a standard on current sustainability-related practices.

5. Conclusion and Assessment: Outlook on the Future of Sustainability in the Banking Sector

Sustainability is an increasingly important issue in the finance and banking sector, as in all sectors. Financial institutions adopt sustainability practices in order to effectively manage the risks that may arise in relation to society, nature, and their own institutions and to leave a better world for future generations.

Banks are among the earliest organizations in the finance and banking sector to take action on sustainability. In particular, managing the environmental and social risks associated with their loans, increasing the positive impact they create through their products and services, and supporting the financing of a carbon neutral economy are among the important incentives in the banking sector. The fight against the impacts of climate change in the world, the Paris Agreement decisions and the subsequent zero carbon banking and financing approaches shape the sustainable finance agenda of international financial institutions. The European Union's sustainable finance Taxonomy and plans for decarbonized development under the European Green Deal also encourage the development of sustainable finance practices around the world.

In parallel with the developments abroad, awareness of sustainability in the banking sector in Türkiye is increasing and practices are diversifying. In order to manage sustainability within a corporate structure, banks have started to address the issue strategically. It is observed that banks that have started to work on sustainability in Türkiye have strategy and/or policy documents that they share with the public, manage sustainability issues through committee or working group structures affiliated with senior management, and thus link the sustainability strategies of their organizations with senior management.

An analysis of sustainability practices in the banking sector in Türkiye reveals that banks carry out activities in both green and social finance, and therefore act with a broad perspective rather than a single focus.

Climate finance is among the leading themes in banks' practices. This approach, which is also in line with international trends, shows that banks have started to further diversify and deepen their green, energy efficiency and renewable energy themed financing and group them under the heading of climate finance. In addition, phasing out coal financing is a theme that is just beginning to be addressed in the sector.

Türkiye is a climate-sensitive country due to the physical impacts of climate change as well as the impact that the transition to a low-carbon economy will have on all sectors. Therefore, it is important for the banking sector to correctly analyze the climate risks and opportunities for the country and offer future-oriented products and services.

It is expected that Turkish banks will diversify their activities in the field of climate finance in this direction in the coming period, deepening both the mechanisms they provide to their customers and providing know-how and capacity in this direction as the markets deepen.

An analysis of the trends and practices in the sector reveals that there are ongoing activities not only in green finance but also in areas such as digitalization and impact financing. Diversifying and supporting digital banking applications is expected to increase the resilience of the banking sector in Türkiye.

Players in the sector state that there are certain areas of development in line with their future targets. Quality data supply and access to data are among the top needs expressed by the sector. Banks need access to quantifiable and comparable data in order to identify and monitor their environmental, social and financial risks and to measure the impact of their climate and sustainable instruments in the future more accurately. The development of different technological solutions to track this data is an issue that can be addressed together with the focus on digitalization.

Capacity building and awareness-raising is another important area of development for the expansion of sustainability practices across the sector. Offering trainings and conducting campaigns to support awareness-raising in areas such as sustainability, climate change and corporate social responsibility among all stakeholder groups, not just banks, will allow the sector to develop faster. To this end, the activities of sector associations and other opinion-leading organizations are also of high importance.

In sum, the banking sector in Türkiye is on a sustainability pathway that both takes into account the country's dynamics and is in line with international developments. Banks are advancing their sustainability journeys to include themes that will be important for Türkiye in the future.The banking sector will play an important role in Türkiye's sustainable development and green transformation. In this regard, every practice, awareness-raising effort, and information sharing in the sector will be of particular importance.

SUSTAINABILITY IN BANKING:
SECTORAL OUTLOOK REPORT

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