Sustainable Finance in China

Newsletter 3, March 2009

This is the bi-monthly newsletter following developments in sustainable banking in China. It offers updates on what Chinese banks, Chinese government regulatory departments, civil society and international stakeholders are doing to promote sustainable finance initiatives for China's financial sector. We invite these stakeholders to read the below updates and contribute their own information on relevant sustainable finance work in China.

We hope you find this update useful to your work and encourage you to send any feedback to Adina Matisoff.

IN THIS ISSUE

SUSTAINABILITY AT CHINESE BANKS

1. Chinese financial institutions bankroll green stimulus

According to reports, China has already spent RMB 120 billion of its RMB 4 trillion (USD586 billion) stimulus package in the fourth quarter of 2008. About 10 percent of that money went to energy saving and ecological projects. This year, RMB 350 million, or nearly 9 percent of stimulus funds, is planned for ecological projects in nine municipalities and provinces. Many of the projects address water shortages, wastewater treatment and sea water desalinization. (http://cleantech.com/news/4074/chinas-stimulus-package-boosts-water-desal-recycling)

In the report "A Climate for Recovery: The colour of stimulus goes green," HSBC ranks the environmental aspects of stimulus packages around the world seeking to reverse the current economic downturn. HSBC named China as having the greenest stimulus package, with USD 221 billion, almost 40% of stimulus funds, allocated to "green" themes, most notably rail, grids and water infrastructure, along with dedicated spending on environmental improvement. The report is available from HSBC Global Research at www.research.hsbc.com.

However, another analysis of stimulus spending found that China approved or started energy projects worth at least US $35 billion since November 2008; including power plants, a liquefied natural gas storage facility, new coal mines, and petrochemical plants throughout the country. For more on the stimulus, see Item #3. (http://steelguru.com/news/index/2009/02/23/ODM2NzM%3D/Stimulus_plans_-_China_investing_USD_35_billion_in_energy.html)

2. Top Chinese banks audited for illegal conduct

China's National Audit Office found evidence of irregularities totaling RMB 6 billion in the lending procedures of China's top three state-owned commercial banks — Industrial and Commercial Bank of China, Bank of China, and China Construction Bank. The auditors found that loan application procedures, particularly at the branch level, are not being strictly reviewed when loan officers knew the applicant they were reviewing. The bank audits were initiated after the audit bureau found that half of the top 20 cases of "serious illegality and economic crime" came from the three banks. (http://uk.reuters.com/article/rbssFinancialServicesAndRealEstateNews/idUKPEK20263520090219?pageNumber=1&virtualBrandChannel=0; http://www.syntao.com/E_Page_Show.asp?Page_ID=11098)

China Development Bank was also reportedly involved in a corruption scandal in February, as the bank's vice-president was fired for taking bribes. His illegal earnings were confiscated and he may face charges. (http://uk.reuters.com/article/rbssFinancialServicesAndRealEstateNews/idUKPEK20263520090219)

POLICY DEVELOPMENTS

3. Chinese banks lend record amounts

Per government directives, Chinese banks have substantially increased lending while the country faces the global financial crisis, with a total of RMB 1.1 trillion of new loans through February. Loans are mainly being provided for government-supported industries and projects, including infrastructure construction, after-quake building, mergers and acquisitions as well as technological innovations.

Bank of China's outstanding loans stood at nearly RMB 1.6 trillion (USD 235.3 billion) by the end of January, up RMB 87.29 billion compared with the beginning of the year. The bank gave a RMB 60 billion credit line to Aviation Industry Corp. of China Ltd. on Feb. 6 after the State Council approved a support package for the aerospace industry. Industrial and Commercial Bank of China extended RMB 117.1 billion (USD 17 billion) of new loans in February, equal to 22% of the total loans for all of 2008. Loans went to develope power grids, roads, hydroelectric power projects and public works. China Construction Bank in December promised to offer RMB 380 billion of loans to Guangdong province for its energy, transportation and infrastructure needs. (http://www.bloomberg.com/apps/news?pid=20601087&sid=aJa5F9H248.g&refer=home; http://news.xinhuanet.com/english/2009-03/06/content_10955571.htm)

China Development Bank has entered into lending agreements with at least seven provinces, each for over RMB 100 billion. Additionally, in February the bank announced that it granted RMB 185.4 billion of loans to 105 Chinese state-owned enterprises in 2008. Loans were disbursed to SOEs working in petroleum, petrochemical, telecommunication, power, railway, chemical, construction and coal industries. (http://www.tradingmarkets.com/.site/news/Stock%20News/2192040/; http://www.tradingmarkets.com/.site/news/Stock%20News/2160253/)

However, members of the Chinese People's Political Consultative Conference (CPPCC), China's top political advisory body, have warned against this lending bonanza. Ahead of its March annual meeting, the CPPCC urged the government to make better use of its RMB 4 trillion economic stimulus package and avoid wasteful construction. A spokesperson for the group said the money should be used "accurately and rationally," to avoid such things as duplicating projects. (http://www.bloomberg.com/apps/news?pid=20601089&sid=a3SXJdeWSm9E&refer=china)

4. China pushes international banks to join lending spree

The Shanghai branch of the China Banking Regulatory Commission in February urged foreign banks to increase lending to the country's small firms. Analysts say that if foreign banks heed the government's calls, they will be exposing themselves to risky investments, as domestic banks are first in line for safer government-backed infrastructure projects. (http://www.bloomberg.com/apps/news?pid=20601087&sid=aJa5F9H248.g&refer=home)

5. China's investments in polluting projects fell in 2008, cautious in 2009

The Ministry of Environmental Protection in January released statistics on China's pollution abatement efforts in 2008, saying the country had made "great progress." Among the highlights were rejection of 156 energy-intensive or highly polluting projects worth RMB 473.7 billion; more than RMB 51 billion invested in 881 projects to control pollution on eight of China's major rivers; and RMB 500 million used for environmental protection programs in rural areas. (http://www.china-wire.org/2009/01/china-punishes-15000-enterprises-over-pollution-in-2008/)

However, MEP warned that factories with backward facilities may revive using the excuse of the country's stimulus plan to boost domestic demand, or firms running at a loss may suspend the operation of pollution-treatment facilities to lower operational costs. (http://www.china-wire.org/2009/01/ministry-to-monitor-pollution/)

6. Chinese regulators step up oversight of overseas investments

The China Banking Regulatory Commission (CBRC) at the end of February reportedly told China's five biggest lenders that it will step up regulation of overseas acquisitions and investments as it confronts the global financial crisis. This will include examining the quality of new loans and increased monitoring of existing loans. The increased regulation is said to come from fears that risky overseas investments could undermine the health of China's financial institutions, while government pressure to boost lending and bolster the slowing domestic economy could lead to a rise in non-performing loans. (http://www.reuters.com/article/rbssFinancialServicesAndRealEstateNews/idUSSHA17680920090226)

The CBRC notice comes on the heels of new corporate social responsibility guidelines from the China Banking Association that also apply to overseas investments. The CBA guidelines require Chinese companies to get approval for overseas investment of more than US$100 million; approval for cross-border infrastructure projects and special purpose incorporations overseas. Highlights of the guidelines include stipulations for "independent on-site investigation and audit for the environmental impacts of financed projects, and make their judgments not solely on clients' own environmental impact assessment reports and data." The guidelines also encourage financial institutions to adopt "people-oriented principles" for their employees and to promote the social development of impacted communities. The guidelines refer to the Equator Principles, but no other specific international environmental or social standards. (http://www.china-wire.org/2009/01/china-to-regulate-overseas-investment/)

An unofficial translation of key parts of the guidelines is available on the International Rivers' website at: http://www.internationalrivers.org/en/node/3831

China Development Bank in particular is playing a key role in China's acquisition of overseas natural resources as the country seeks to capitalize on falling demand during the economic crisis. Three of the largest recent deals include a USD 10 billion loan to Brazil and a USD 25 billion loan to Russia, both in return for oil. Also, in February, The Aluminum Corporation of China (Chinalco) announced that CDB will provide USD 19.5 billion to finance the company's bid to increase its stake in mining giant Rio Tinto. (http://www.china-briefing.com/news/2009/03/02/china-sector-watch-energy.html and http://www.ft.com/cms/s/0/7b389e4a-0371-11de-b405-000077b07658.html?nclick_check=1)

CIVIL SOCIETY ACTIVITIES

7. *Greenpeace-China* warns of poor disclosure for listed forestry companies

Greenpeace-China released a new report exposing the loopholes in the Hong Kong Stock Exchange's rules on environmental disclosure for listed forestry companies on 18 February. The report, "In *the Green or In the Red? Environmental Concerns and Risks for Forestry Listings in Hong Kong*," analyzes the listing documents of several companies in the logging and paper and pulp industries. The report also reviews environmental issues in Asia and China's forestry sector more broadly, with recommendations for both regulators and investors to address the problems with disclosure.

The report is available at: http://www.greenpeace.org/china/en/press/reports/in-the-green-or-in-the-red-en

8. MEP reopens public consultation of APP subsidiary IPO application

China's Ministry of Environmental Protection (MEP) on 2 March published a statement hinting that its six-month evaluation of the IPO application of a pulp and paper company that has been fined for massive pollution may be wrapping up (see past newsletters). The statement reported in detail the follow-up actions MEP took after receiving information from six Chinese NGOs about the company's poor environmental practices during a public consultation period in August 2008. The statement said that MEP believed that Gold East Paper, a subsidiary of Asia Pulp & Paper, had addressed its environmental wrong-doing, including spending RMB 100 million on environmental clean-up over the past two years. MEP then invited public consultation on these findings before it makes a final decision. (http://www.zhb.gov.cn/cont/gywrfz/hbhc/gsqk/200903/t20090302_134756.htm)

Greenpeace, one of the Chinese NGOs that submitted comments during the initial public consultation period, said that it was encouraged that MEP seemed to be taking the environmental accusations seriously. However, citing specific examples of on-going environmental issues, it was concerned that Gold East Paper would in fact stop harming China's forests and illegally polluting its waters. (http://www.greenpeace.org/china/en/news/APP-forest-China-listing)

INTERNATIONAL COOPERATION AND SUSTAINABLE FINANCE DEVELOPMENTS

9. Chinese banks lose strategic investment partners

Once looked to as a potential source of leadership and environmental risk management know-how for Chinese banks, several international banks have begun selling their shares of Chinese peers in an effort to generate much-needed cash. In recent months, Bank of America sold part of its stake in China Construction Bank, Royal Bank of Scotland and UBS AG both sold all of their stakes in Bank of China, and recently reports have surfaced that Citigroup is considering liquidating some of its stake in Shanghai Pudong Development Bank. In February, China Banking Regulatory Commission (CBRC) warned Chinese commercial banks that they should prepare to lose some foreign strategic investors as share lock-up periods expire. (http://www.reuters.com/article/rbssFinancialServicesAndRealEstateNews/idUSSHA17680920090226 and http://money.cnn.com/news/newsfeeds/articles/djf500/200903030702DOWJONESDJONLINE000281_FORTUNE5.htm)

10. HSBC China releases 2008 CSR report

In January, HSBC released its third corporate social responsibility report detailing its activities in China. The report covers various aspects of the bank's CSR practices, including ethical banking and protecting the environment. HSBC is the first locally incorporated foreign bank to release such a report in China, and it abides by CSR guidelines release by the Shanghai branch of the China Banking Regulatory Commission and the China Banking Association earlier this year. The report is less comprehensive than CSR reports released by HSBC's branches outside of China. The report is available at: http://www.hsbc.com.cn/1/2/hsbc-china/hsbc-china/community

11. Private Equity Council members adopt guidelines for responsible investment

In February, the Private Equity Council (PEC) announced that its members adopted a set of voluntary responsible investment guidelines covering environmental, social and governance issues. The guidelines will apply to companies' pre- and post-investment processes. They were developed under the auspices of the United Nations Principles for Responsible Investing (PRI).
(http://www.privateequitycouncil.org/press-releases/2009/02/10/private-equity-council-members-adopt-guidelines-for-responsible-investment/)