

# GREEN INCLUSIVE FINANCE

## Case Studies Series on Essential Practices

### Essential Practice No.5:

Managing client or portfolio-level environmental risks and opportunities



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Prepared by Silvia Recupero  
in collaboration with Isabelle Barrès and the e-MFP GICSF-AG

## About the Green Essential Practices Case Studies Series

The “Green Essential Practices Case Studies Series” highlights the experience of Financial Service Providers (FSPs) with good practices in the 8 key areas identified in the Green Index 3.0.<sup>1</sup> The Case Studies under this series offer practical examples of how an FSP developed its practices to inspire and facilitate the journey of others.

The **8 Green Essential Practices (EPs)** provide a roadmap for FSPs to maximise their green impact:

- **EP1:** Define their environmental strategy
- **EP2:** Implement their environmental strategy
- **EP3:** Identify client or portfolio-level environmental risks and opportunities
- **EP4:** Identify institutional-level environmental risks and opportunities
- **EP5:** Manage client or portfolio-level environmental risks and opportunities
- **EP6:** Manage institutional-level environmental risks and opportunities
- **EP7:** Offer green financial products and services
- **EP8:** Offer green non-financial products and services



Each Case Study in the series follows the same structure:

1. **Background** of the FSP and the context in which it operates.
2. **Evidence** of how the FSP is demonstrating good performance in the Essential Practice that is being highlighted. This is the main section of the Case Study and offers – as relevant – a review of what has enabled the FSP to reach its results, and what these results are:
  - *Capacity:* how did the FSP acquire the capacity to implement the activities needed? (e.g., internal training, training through external partnerships, technical assistance, financial support, etc.)

<sup>1</sup> For more details about the Green Index 3.0, refer to these links: [https://www.e-mfp.eu/sites/default/files/resources/2022/11/Green%20Index%203.0\\_final.pdf](https://www.e-mfp.eu/sites/default/files/resources/2022/11/Green%20Index%203.0_final.pdf) and [https://hedera.online/gicsf\\_ag\\_tools/green-index-digital.html](https://hedera.online/gicsf_ag_tools/green-index-digital.html)

- *Tools*: which tools did the FSP use to implement the needed activities? (e.g., indicators, documents, materials, IT solutions, etc.)
  - *Outreach*: what were the FSPs' quantitative results? (e.g., outreach, implementation status, etc.)
3. The FSP's **journey** to implement the identified good practice, and lessons learned.
  4. The FSP's **next steps** – if any – to continue to improve in this area.

## Green Essential Practice No. 5: Manage environmental risks and opportunities at customer or portfolio level

In **Green Essential Practice No. 5 (EP5)**, the focus is on managing environmental risks and opportunities at the client or portfolio level:

- The FSP recognizes identified vulnerabilities of clients or portfolio to environmental risks as well as adverse environmental impacts of clients or portfolio as factors of risks to achieve its social mission or environmental objectives,
  - The FSP incorporates them into its financial risk management policies and processes using a variety of methods to assess vulnerability and adverse impacts, and
  - The FSP has processes in place to manage them.
- The FSP identifies green practices and technologies that create benefits for clients.
- The FSP ensures that the practices or technologies identified are recognized as "green" by an environmental taxonomy and/or comply with clear environmental criteria.
- The FSP recognizes the identified demand and need for green practices and technologies as economic opportunities, and it incorporates them into its credit processes and manuals and its client segmentation.
- The FSP has in place processes to select and propose specific financial or non-financial products and services aiming to address identified needs or demand of each client.

The FSPs highlighted in Case Studies on the **Green Essential Practice No. 5 (EP5)** demonstrate good practices in managing risks and opportunities at the client and portfolio level.

## EP5: Managing client or portfolio-level environmental risks and opportunities at Muktinath Bikas Bank Limited

### A. Background

#### About Muktinath Bikas Bank

Muktinath Bikas Bank Limited (Muktinath Bank) is the leading organization focusing on Nepal's MSME sector and rural finance. It is one of the first banks in the country to have identified customers residing in rural geographies as a potential market segment. To promote financial inclusion in unbanked and underbanked areas, it established the Inclusive Banking (IB) Department.

On January 3, 2007, Muktinath Bank took the first step to establish its banking operation. It got its license from the Central Bank of Nepal (i.e., Nepal Rastra Bank) to operate a Banking Business initially in three districts of the former Western Development Region (currently called Gandaki Province) as a “B” class financial institution. Since inception, Muktinath Bank has adopted the deep-rooted values of financial inclusion and the core principle of “Janata Bank ma Hoina, Bank Janata ma Janu Pardachha” (“People should not come to the Bank; the Bank should go to the doors of the people”). Muktinath Bank prioritized opening branches in rural areas where without any financial institution, people were in dire need of banking services. Customer-friendly products and door-to-door services are the two major factors for Muktinath Bank’s popularity and success among the area's local people.

The institution developed the first green project in 2015, the Multi Stakeholder Forestry Program (MSFP), which was funded by UKaid through the Department for International Development (DFID), the Government of Finland, and the Swiss Agency for Development and Cooperation (SDC) and supported by the Government of Nepal. It aimed to improve the livelihoods and resilience of poor and disadvantaged people in Nepal and “develop the contribution of Nepal's forestry sector to inclusive economic growth, poverty reduction, and tackling climate change”<sup>2</sup>. One of the implementing partners of MSFP is LI-BIRD (Local Initiatives for Biodiversity, Research and Development), which, together with the District Chamber of Commerce and Industries (DCCI) of Myagdi, Baglung and Parbat and Muktinath Bank established the Value Chain Development Fund (VCDF). Through VCDF, Muktinath Bank plays a critical role in providing access to finance to forestry-based entrepreneurs.

Another relevant partnership was launched in May 2015 with the Frankfurt School of Finance & Management and the International Development Enterprise Nepal (iDE Nepal). It was named “Climate Smart Finance” and enabled Muktinath Bank to develop the “Improving Agriculture Loan”. Through this product, farmers were trained and received loans to run their farms. This project was supported by the Development Bank of Austria (OeEB) and the Federal Ministry of Agriculture, Forestry, Environment, and Water Management.

The current annual budget dedicated to green finance by the Bank is EUR 400,000. It is supported by two primary partners: the Dutch Fund for Climate and Development (DFCD) and the SNV, which aims to promote climate-smart agriculture in the Gandaki Province in Nepal.

#### What context does Muktinath Bikas Bank Limited operate in?

The International Finance Corporation (IFC) and the Nepal Rastra Bank (NRB), Nepal’s central monetary authority, have released the country’s first Environmental and Social Risk Management (ESRM)

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<sup>2</sup> <https://landportal.org/community/projects/multi-stakeholder-forestry-programme>

guidelines for the financial sector.<sup>3</sup> The guidelines help financial institutions manage the environmental and social risks that could arise from client transactions.

The traditional risks intrinsic to financial institutions pertain to credit and the market. How financial providers' clients/investees manage the environmental and social impact of their operations can create substantial risks to the financial institutions and, if unmanaged, adversely impact their reputation, lead to an increase in non-performing loans, or result in costly litigation and loss of revenue.

The ESRM guidelines set standards for identifying, assessing, and managing risks and list acceptable environmental and social performance thresholds. They contain general and sector-specific checklists and sector-wise lists of permits and licenses that financial institutions can apply to make their evaluations. Hydropower-related Environmental and Social (E&S) criteria have been given special attention due to the country's reliance on this form of energy. In cases where E&S risks are unavoidable, measures have been suggested to mitigate them to the extent possible.

"Improved E&S risk management practices will help generate business opportunities and boost the regional competitiveness of our banks and financial institutions. This will create increased access to financing for businesses with strong environmental and social performance," said NRB Governor Dr. Chiranjibi Nepal. "Sustainable finance presents a huge opportunity to deliver on the Sustainable Development Goals, to which Nepal is a signatory."

## B. Essential Practice No.5 at Muktinath Bikas Bank

Muktinath Bank manages its indirect environmental risks (i.e., risks borne by its clients) by complying with the ESRM guidelines. This helps them manage the risks linked to adverse environmental impacts on their agricultural clients. The ESRM guidelines were approved at board level in 2022. Currently, the bank's risk management staff is partially involved in the process of compliance with those guidelines.

Thanks to its set of policies, procedures, and tools, Muktinath Bank has internal capacity to identify, monitor and manage its exposure to the risks of agricultural clients. The institution's commitment to environmental management is transversal across its procedures:

1. Identification, assessment, and management of E&S risk of financial transactions.
2. Definition of the decision-making process (roles, responsibilities, and staff capacity/training needs).
3. Documentation and recordkeeping requirements.

The ESRM guidelines are implemented internally through a set of procedures for:

- Screening transactions.
- Conducting environmental due diligence.
- Categorizing transactions based on their environmental and social risk.
- Decision-making process.
- Monitoring the client's/investee's environmental performance.
- Managing a client/investee's non-compliance with the environmental standards at loan approval.
- Monitoring an environmental risk analysis in the institution at headquarters and branches.

Furthermore, Muktinath Bank identifies opportunities to develop and implement green products and services by partnering with HEDERA Sustainable Solutions to conduct research using the framework of the IMPACT-R project and assessment questionnaires based on the following methodologies: the ESMAP Multi-tier Framework (MTF) for energy access, WHO/UNICEF Joint Monitoring Program for WASH, and

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<sup>3</sup> [Sustainable Banking Network \(SBN\) \(www.ifc.org\)](http://www.ifc.org)

FAO Food Insecurity Experience Scale (FIES) for food security. Through the identification of its clients' needs, the institution can prioritize actions and identify the main areas to develop its green offer further.

Muktinath Bank complements the management of its indirect risks with an extensive training program focused on managing its direct risks. Each year, the Bank trains its staff in practices to reduce or avoid adverse environmental impacts (e.g., how to reduce waste and pollution and efficiently use water and electricity, among others). From September 2022 to February 2023, Muktinath Bank conducted 15 trainings with up to 75 participants in each session. These were offered in 7 locations as well as online. While focusing on direct risks, this training also raises staff awareness of environmental risks in general and help support the management of indirect risks from client activities.

## C. Muktinath Bikas Bank's journey with Essential Practice No.5

Muktinath Bank's green agenda continues to evolve. The lessons to share with other FSPs looking to improve their performance around EP5 include:

1. **Know the customer segment.** The institution should know the customer segment it wants to serve and develop green products and services to suit the customer's needs.
2. **Get support from management and Board to get "green" engagement of the institution** (with clients, investors, donors, or other external stakeholders). In order to start something new, an institution should get full support from its management and Board. Here, the Board plays a crucial role as they should convince the shareholders about the importance of focusing on this topic and the potential outcomes.
3. **Develop human resources in line with the management vision and customer segment.** Do not rely only on the existing human resources to start the new green agenda from the first day.
4. **Invest in training and development.** A good investment in training, learning and development should be a priority to raise awareness among the staff on how to manage adverse environmental impact and vulnerability to climate changes.

## D. What's next?

Climate change is a big threat for Nepal. To prepare its clients and community, Muktinath Bank is partnering with different organizations to develop programs to support the effort of the government, communities, and clients to adapt to the changing environment. For example, Muktinath Bank is currently partnering with DFCD/SNV (Dutch fund for Climate Development) to introduce climate smart agriculture value chains to secure a source of income for the community. Muktinath Bank is always looking for opportunities to partner with like-minded organization to improve the lives of its customers and their communities.



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## Learn more

For more information about Muktinath's environmental journey, we invite you to check the following resources:

- Muktinath Bikas Bank's website: <https://www.muktinathbank.com.np/>
- Contact information: Mr. Vijay Kumar Gurung, [Vijay.gurung@muktinathbank.com.np](mailto:Vijay.gurung@muktinathbank.com.np); Ms. Shweta Rai ([Shweta.rai@muktinathbank.com.np](mailto:Shweta.rai@muktinathbank.com.np))

For more information about the Essential Practices, we invite you to check the [Green Index 3.0](#).

## Contribute

We encourage you to take an active part in building the pool of resources available on good environmental practices.

If you are interested to **contribute to the Green Essential Practices Case Studies Series or the Green Map**, we invite you to contact Joana Afonso at European Microfinance Platform (e-MFP) at [jafonso@e-mfp.eu](mailto:jafonso@e-mfp.eu).

### **The e-MFP Green Inclusive and Climate Smart Finance Action Group (GICSF-AG)**

The e-MFP Green Inclusive and Climate Smart Finance Action Group (GICSF-AG) is a unique multi-stakeholder think tank that brings together inclusive finance practitioners and researchers to enhance cooperation, exchange experiences and find a common path to deal with environmental issues, improve knowledge and disseminate findings, seize green opportunities and co-create common standards for the inclusive finance sector and new practical tools to advance green inclusive and climate smart finance. Created in 2013, today it counts today more than 150 members affiliated to more than 75 institutions worldwide and represents the majority of sector stakeholders.

### **The European Microfinance Platform (e-MFP)**

The European Microfinance Platform (e-MFP) is the leading network of organisations and individuals active in the financial inclusion sector in developing countries. It numbers over 130 members from all geographic regions and specialisations of the microfinance community, including consultants & support service providers, investors, FSPs, multilateral & national development agencies, NGOs and researchers. Up to two billion people remain financially excluded. To address this, the Platform seeks to promote co-operation, dialogue and innovation among these diverse stakeholders working in developing countries. e-MFP fosters activities which increase global access to affordable, quality sustainable and inclusive financial services for the un(der)banked by driving knowledge-sharing, partnership development and innovation. The Platform achieves this through its numerous year-round expert Action Groups, the annual European Microfinance Week which attracts over 400 top stakeholders representing dozens of countries from the sector, the prestigious annual European Microfinance Award, and its many and regular publications.

European Microfinance Platform

39 rue Glesener

L-1631 Luxembourg

[contact@e-mfp.eu](mailto:contact@e-mfp.eu)

[www.e-mfp.eu](http://www.e-mfp.eu)

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