IDFC International Development Finance Club

IDFC SDG Framework Report : Towards SDG Alignment

In November 2020, the “Finance in Common” Summit will take place in Paris bringing together about 450 public development banks around the theme of the sustainable development goals (SDGs). One of the main issues that will be discussed during the event will be the pivotal role that development banks can play in aligning their activity with the SDGs and promoting sustainable development investment. IDFC conducted an internal survey in October 2019 on “existing approaches by IDFC members to characterize SDG compatibility of the activities and investment” from which the Club decided to establish a new SDG Alignment working group. A key work stream of this working group has been the SDG Framework sub-WG aiming at analyzing and enhancing the existing approaches. To that end, the aforementioned group administered another survey focusing on IDFC members SDGs taxonomy methodology and targeted follow-up questions to acquire a better understanding of each member’s situation.

The survey first offers (section 1) a view of how the 17 SDGs are covered. This view is completed by the result of a parallel work carried out using an artificial intelligence tool in collaboration with the OECD (“SDG tracker”). Section 2 analyses the answers describing the SDG analysis tools used by members, showing where members currently are in the transition from classical environmental and social diligences to the use of modern SDG-alignment tools in financing operations. Last section provides recommendations on fundamental pillars of an ideal methodology to be endorsed by IDFC’s members.

The SDG taxonomy survey was administered to IDFC members in April 2020. 10 development banks responded[1]: AFD (Agence française de développement – France), Bancoldex (The Bank of Foreign Trade), BICE (Banco de Inversión y Comercio Exterior S.A – Argentina), BNDES (Banco Nacional de Desenvolvimento Econômico e Social – Brazil, DBSA (Development Bank of Southern Africa – South Africa), ICD (Islamic Corporation for the Development of the Private Sector – Islamic world), JICA (The Japan International Cooperation Agency – Japan), KfW (Kreditanstalt für Wiederaufbau – Germany), PT-SMI (PT Sarana Multi Infrastruktur – Indonesia), and TSKB (Industrial Development Bank of Turkey – Turkey).

The questionnaire included four parts as follows: (i) “general information” with information about the institution’s location, main sectors and type of clients, (ii) an “introduction” comprising a short description, the scope of the tool and the characterization and accounting for negative impact, (iii) “the use of methodology” which indicates the phase of the project cycle in which the tool is used (ex-ante, ex-post, or both), the use made of this tool internally, and the types of instruments to which the member’s taxonomy is applicable, and (iv) “global SDGs” which seeks to determine whether or not the member’s tool is based on or inspired from other existing international SDG framework.

In addition, a series of targeted questions was sent to several members with a view to obtain further and more specific information, especially on the nature of the member’s SDG tool and its use in financing activities.

1- SDG coverage

1-1 Scope of the SDGs in the survey

Since 2015, SDGs have occupied a growing position in development institutions’ and development financial institutions’ strategy, especially through the rising importance of SDG-friendly financial operations. The ten responses to the survey show a high level of commitment from IDFC members to the SDGs: six institutions – namely AFD, BNDES, DBSA, JICA, KfW, and TSKB[2] – target directly or indirectly all 17 SDGs whereas the four others, Bancoldex, BICE, ICD and PT SMI focus on at least 10 SDGs.

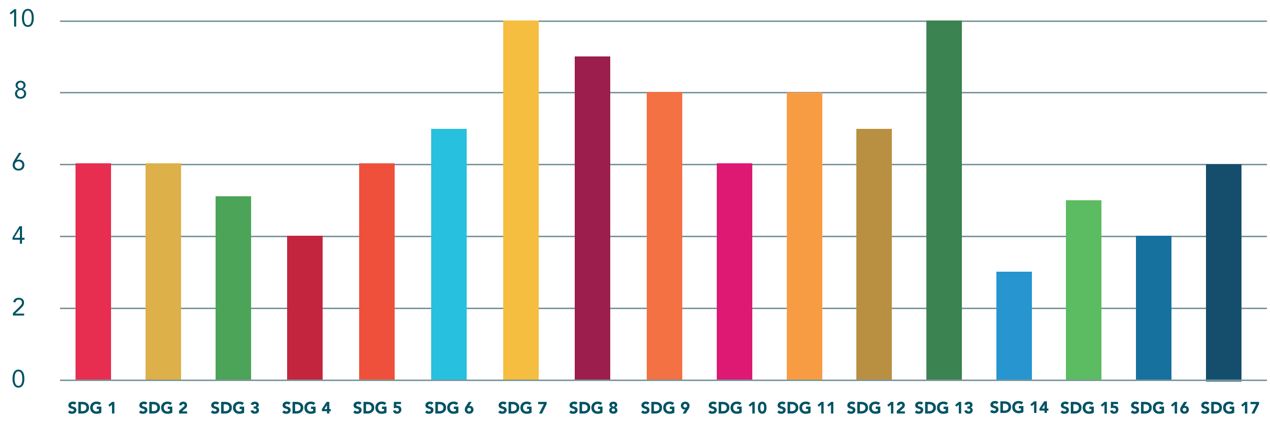
1 It is worth mentioning that the participation level is not satisfactory, since the response rate for both 2019 and 2020 surveys were less than 50% of IDFC members, although it is true that all 10 members of the SDG Framework sub-Working Group responded to the latter survey. In addition, many members have provided ICD with answers which were sorely lacking precision and development. The low response rate and the lack of accuracy reduce the chances for generalizability which is a key factor to design future results-based solutions.

2 As an example, TSKB launched the SDG Mapping in 2019 to assess the bank’s impact to SDGs. Through this project, the Bank’s loan appraisal and assessment processes have been enhanced in order to match the financed sub-projects with the SDGs. A matrix table has been developed to link the outstanding credit themes of the Bank with 17 SDG targets.

There is no "perfect" coverage of the SDGs, and it is normal that not all members "cover" all SDGs: some members have a clearly universal aim, others are more targeted onto specific sectors. The issue is more at avoiding (i) "orphan" SDGs in some countries or regions, (ii) indirect effects detrimental to some SDGs, in particular social and environmental. The following graph highlights the SDGs that are reported as directly covered by IDFC members in the survey.

Some areas may look somewhat "orphan": SDG 3 (good health and well-being), SDG 4 (quality education), SDG 14 (life below water), SDG 15 (life on land) and SDG 16 (peace, justice and strong institutions) are tackled by not more than half of the members surveyed. On the other way around, SDG 7 (affordable and clean energy), SDG 8 (decent work and economic growth) and SDG 13 (climate action) are mentions by all or almost all members.

Figure 1: Scope of coverage of SDG's by IDFC members



1-2 Another mapping : a view from the SDG-"tracker"[3]

In parallel with the survey work, 14 members accepted to submit documents[4] to a text-based machine-learning algorithm developed by the OECD, the SDG Financing Lab.

In a few word[5]: the algorithm associates SDGs to sentences in a text. It initially "learned" the vocabulary associated with each SDG from thousands of examples from OECD and UN's descriptions of projects, to which SDGs were manually labelled. It can then "read" any sentence and associate words to the SDGs. Applied over long reports, the number of those associations (which we call "mentions") is aggregated for each SDGs. This provides indicators of SDG orientation, with percentages of mentions of each SDG across the report. **IDFC members' documents were not always comparable, but six themes can be highlighted from the analysis (done by the OECD team) :**

1. **On average "economic" objectives are the most mentioned by IDFC members:** SDGs 9 (Industry, innovation, infrastructure) and 8 (Economic growth and decent work) are the most mentioned in IDFC members' sustainability reports, respectively with 12% and 15% of mentions. In 10 out of 14 cases, one of those two is the most mentioned SDG in the reports. Admittedly, they tend to be very broad, covering interventions from large infrastructure programs to micro-finance projects. Nevertheless, this does show that IDFC members' view their main activities as fostering economic development.

3 This section draws substantially on work realised by the OECD through its SDG Financing Lab algorithm. Those results can be found in OECD (Forthcoming), "Holistic or specialised? Assessing the International Development Finance Club's SDG priorities through machine learning", OECD Insights Brief.

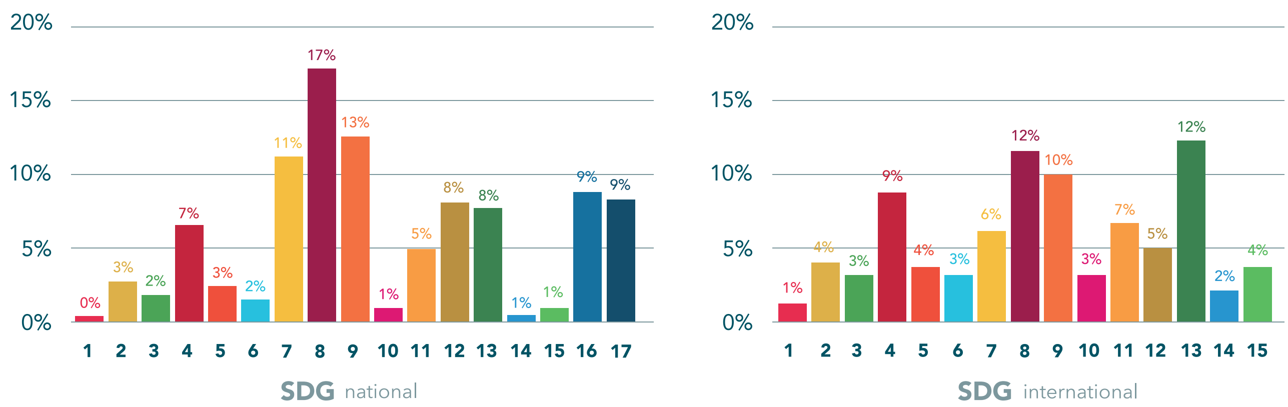
4 Most institutions shared at least one recent "Sustainability report" or similar, which provide the base for the present summary. But other types of reporting made available complement this picture. Annual reports or company-wide strategies tend to focus on a narrower set of SDGs, centred around economic impact and corporate governance. Some institutions submitted reports specifically around climate change efforts, which can also highlight those specific aspects of their impact.

5 For a more detailed description of the methodology, see Pincet, Okabe and Pawelczyk (2019), "Linking Aid to the SDGs: A Machine Learning Approach", OECD Working Paper. For the platform of results on OECD data, see: https://sdg-financing-lab.oecd.org/

2. **Environmental objectives make the second important area of intervention in reports.** SDGs 13 (Climate action) and to a lesser extent 12 (Responsible consumption and production) are the most important focus for many institutions which submitted reports. When different years were available, there is often some evidence that those objectives are increasing over time. SDG 7 (Clean and affordable energy) is also one important aspect of those reports. The integration of Paris-aligned criteria is likely to be behind this evolution.

3. **However, it is important to look beyond averages at the great diversity of goals for all institutions:** The diversity of institutions' emphases is remarkable. Some IDFC members target only 2 or 3 goals and barely mention the others; while some reports have a remarkable breadth of targets. This underlies a diversity in the way to approach SDGs: either as a holistic framework where all aspects need to be managed, or as a menu of options. One source of heterogeneity is linked to the geographic orientation of IDFC members[6]. The former tend to focus more on infrastructure and economic development (SDGs 7-9) while the latter have on average more mentions of environmental and social goals **(Figure 2)**. Interestingly, even among environmental SDGs, international institutions are more focused on SDG 13 (and to a much lesser extent, biodiversity) while national ones mention more SDG 12. Finally, International institutions often seek to have a holistic approach, which is not necessarily the case for their national counterparts.

Figure 2: IDFC members' Sustainable Development Goals mentions by type of institution



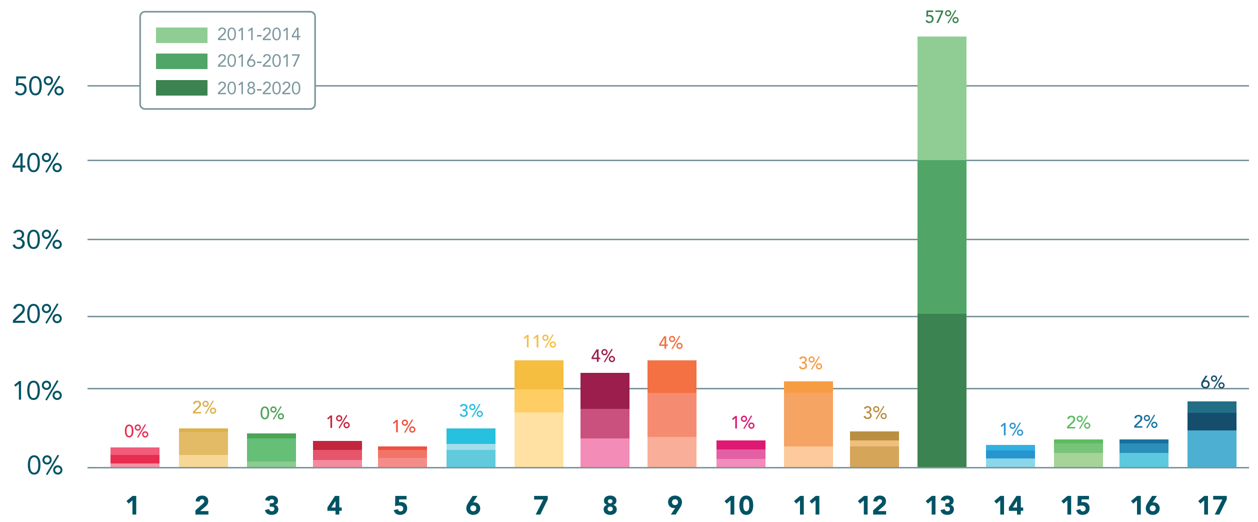
4. **Partnerships and governance matter very concretely:** Despite the fact that SDG 16 is the most important focus in only one case, SDGs 16 (Governance) and 17 (Partnerships) represent together an important share of IDFC's targets. SDG 17 represents the importance of collaboration across levels of government – most institutions work with regional or urban authorities. SDG 16 reflects the attention to corporate governance issues when investing, but also contexts where corruption risks or conflict areas exist.

5. **Some goals remain orphans, in particular social goals and biodiversity:** While there are considerable variations across institutions, social SDGs (SDGs 1-6) are never the most important focus of IDFC members. Only SDG 4 (Education) is mentioned significantly, more than 10% in two cases. In contrast, others are rarely mentioned more than 5% of the time. Similarly, SDG 10 (Inequalities) is one of the least emphasised. With the COVID-19 crisis, it is likely that mentions of SDG 3 ("Good health and well-being") will become a more important area. In addition, SDG 1 ("No poverty") and SDG 10 ("Reduced inequalities") are surprisingly two of the least emphasised. This apparent paradox is linked to the nature of the algorithm, which only takes into account the vocabulary in reports and not their intended impact: indeed more reports describe actions taken in favour, for example, on access to electricity, but not the "second" of later round effects, which can occur, say, on poverty. Another set of "untouched" SDGs are related to biodiversity: apart from a couple of exceptions, SDGs 14 and 15 are not mentioned more than 3% of the time.

6 Among the 14 reports analysed here, 8 come from institutions with a focus primarily on their own country, and 6 from institutions with a focus outside of their borders (including one regional bank). See Annex for the list.

6 **IDFC as a club mobilizes around climate finance:** The algorithm was also used to analyse all documents issued by IDFC as a club published on its website. The results show that as a club, the focus on communication has overwhelmingly been SDG 13 (Climate change), and increasingly so in the last years. This difference between IDFC's aggregate efforts of members and that of the Club can be interpreted as the role of the Club to leverage on its mission and vision through a collective positioning, which has been historically focused on climate change.

Figure 3: IDFC as a club: dominance of SDG 13 ("Climate Action")



Note: All selected documents on IDFC's "News" section (with attachments when available), excluding those produced by non-IDFC institutions. There are 62 documents in the end,, representing 930 pages of documents in total

To sum up: the analysis shows the diversity of IDFC members in their objectives and in their methods. Some are specialized in a few SDGs and, others emphasised the breadth of their impact. Some report more on their economic of infrastructure-led development, while others emphasize environmental SDGs.
This matches the diversity of their mandate and of their institutional status, but also provides direction for collaboration across institutions on reporting. IDFC, as a collective, plays this role by emphasizing environment-related SDGs. In addition, reports tend to ignore social aspects, in particular poverty, inequalities or even health. This could change as the consequences of the COVID-19 crisis continue to unfold. Biodiversity SDGs, also closely linked to the emergence of COVID-19, could also warrant more attention in the future.

2- From social and environmental safeguards to SDG-alignment tools

2-1 Accounting for positive and negative impact

Assessing and addressing the possible unintended negative impact of future projects has long emerged as a necessity for all development banks. Former surveys showed that several IDFC members do have some kind of social and environmental safeguard system, as an integral part of every project appraisal. The present survey questioned IDFC members on the specific **tools** they use to characterize the full SDG-alignment of their operations, i.e. their positive and negative impact on the full range of SDGs. Answers varied.

ICD, for example, sends a "development effectiveness" questionnaire to be filled by the client and ICD's project officer during the due diligence mission and, after disbursement, conducts evaluation missions to mature projects. A comparison is then made between the data collected during approval and the actual findings during the evaluation mission. In the same vein, DBSA's Development Results Reporting provides development impact results after project completion. KfW's Impact Management System (under implementation) will provide a large range of indicators and could eventually be mapped to the SDGs.

BNDES, BICE and Bancoldex assess only positive social and environmental effects of their projects. AFD and TSKB pay special attention to the potential risks and impacts arising from their projects on environmental and social issues. AFD created in 2013 a Sustainable Development Analysis and Opinion mechanism (SDAO), and updated it in 2017 to include the bank's Climate and Development Strategy and SDGs. It is today in constant evolution according to AFD's strategic developments. This mechanism is designed to include cross-cutting sustainable development concerns in AFD's financial operations.

Likewise, concerning the environmental and social risks related to loan facilities, TSKB developed its own Environmental and Social Risk Evaluation tool (ERET) in 2005 to identify and rate risks associated with the clients and projects. Complementary to TSKB SDG's mapping tool which has enabled to develop a matrix table to link the outstanding credit themes of the Banks with the SDGs targets, the ERET functions as an evaluation model that rates projects by seeking answers to questions under separate headings, which are in compliance with the IFC Performance Standards. By using this tool, it is aimed to mitigate the negative impacts and risks of the proposed sub-projects by designing tailor made action plans on the basis on the ERET results.

2-1 The SDG tool in the project cycle

Five out of the ten members who replied, have tools they apply in both ex-ante and ex-post phases. Bancoldex, DBSA, ICD, PT SMI, and TSKB use different instruments but make a comparison between ex-ante and ex-post data. JICA has introduced a tool to present the linkage between projects and the SDGs in both ex-ante and ex-post evaluation phases. In addition, regarding the ex-post phase, the agency is preparing the application of text mining methods in studying approximately 1800 ex-post evaluation reports and clarifying how SDG goals/targets have been taken in the implemented projects. Besides, JICA has introduced a SDG sector code into its internal operational systems to quantitatively grasp how much amounts were committed or disbursed in its technical and financial cooperation by SDG goal. KfW, BICE, BNDES all use their tools for ex-post evaluation only. AFD's SDAO focuses on ex-ante, and AFD uses other instruments for monitoring and ex-post evaluation, with no direct link with the ex-ante SDAO analysis.

Ex-ante methodologies include development results template, project design, identification, preparation and approval by several departments, or, in the case of Bancoldex, the use of the bank's SARAS analysis (Environmental and Social Risks Analysis System). Ex-post methodologies include completion reports, monitoring and evaluation indicators, evaluation reports, annual surveys, SDG mappings (at local, regional or national scales according to the institution), as well as evaluations of social and environmental impacts. However, this would need to be clarified as IDFC members' answers in this part of the survey lacked accuracy. Nonetheless, this allows one to identify important differences on the use made by every member of their SDG instruments, therefore highlighting a deficit in harmonization.

2-3 In-house tools

All 10 development banks surveyed have indicated that their SDG tool is an in-house instrument, developed by each member on its own. **Only a few have used international standards as a basis to build their own mechanism:**

- BICE is using, as a preliminary exercise to be deepened, an own methodology that is comprised of a mix of the criteria used when analyzing its portfolio for the issuance of the Sustainable Bond (validated by the second opinion party) and some methodologies used by some international institutions.
- ICD uses international indicators such as the Harmonized Indicators for Private Sectors Operations (HIPSO) and the Global Impact Investing Network (GIIN);
- And AFD collaborates with the OECD to implement the "SDG-tracker" analysis (Cf. §1.2) to provide a mapping of the SDGs at the strategy level (sectoral and geographical) and within the project portfolio. But, on the other side, the ex-ante "SDAO" tool is a 100% in-house tool.

So, members have a wide variety of tools to measure the alignment of their operations with SDGs (i) with no common basis; (ii) without strong connection to international standards in most cases. There is room for improvement on these two aspects.

2-4 Exhaustiveness of the tools

The study reveals that almost all development banks surveyed have generalized the use of the tool, if they have one, to all sectors in which they are involved. All have also indicated that they applied their tools on loans. On the contrary, guarantees, bonds and term finances are not covered by an important majority of the members. The survey outlines the discrepancies between members' SDG methodologies, as shows the graph below.

Figure 4: Type of instruments related to SDG taxonomy methodology

2-5 Multidimensionality of the tools

Most respondents indicated that their tools include social and environmental analysis, in addition to economic, financial and legal aspects, but do not specify furthermore. Actually, the questionnaire did not directly pose the question. A couple of members nevertheless indicated some specific areas (ICD : human rights, health, job safety and employment of children), or specified the criteria of their Green and Social Bonds (Bancoldex: SDGs 3, 6, 7, 8, 9, 11, 12, 13 and 15 for Green Bonds, impacts of microfinance in the areas of small business and self-employment, gender parity and rural economies for Social Bonds).

The only detailed example of multidimensional analysis tool is given by AFD's SDAO, which is done through six sustainable development dimensions, covering most SDGs: (i) sustainable growth and resilient economy; (ii) gender equality; (iii) sustainability of project impact and governance framework; (iv) conservation of biodiversity, management of environment and natural resources; (v) social well-being and reduction of social imbalances; and (vi) fight against climate change and its impacts (mitigation and adaptation).
In future surveys, this aspect should be more detailed.

2-6 Few tools have a clear rating role

All members have taken a mixed approach combining quantitative and qualitative data.
However, there is a general aspect that most tools lack: the capacity to give a grade to a project, according to its alignment to SDGs and its development impact. BNDES is planning to develop a methodology to evaluate how the projects contribute to SDGs, but has no grading matrix at the moment. AFD only uses a grading system. AFD's SDAO turns the qualitative approach of its six sustainable development dimensions into a -2 to +3 grading scale, estimating the potential positive and negative expected impacts of the project under each dimension. However, the choice was done not to have a final overall quantified mark, synthetizing the whole analysis of each project through the 6 dimensions together. Only a final "opinion" is given; positive, positive with reserves, or negative.

This issue of synthetizing the marks given in the various areas of analysis is a difficult one: simple average, weighted average, exclusion of any negative mark, possible offsetting of negative marks by higher positive marks in various other areas? Many options are possible. As of today, only one member is confronted to this question, but in the future, if more members adopt multidimensional quantified analysis, it will become a central issue. Adopting a rating system allows the bank to have an explicit and quantified general overview of the various impacts of a project. If done ex-ante, on the expected impacts, it can lead to the correction of the identified weaknesses, during the project preparation process, or to an informed analysis of the balance between positive and negative impacts.

2-7 Few tools are used at decision level

The relevance of an SDG-alignment tool mainly rests on its capacity to influence the decision-making process. Actually, most responses have indicated that members' tools did not have a major influence on the Board's decisions, if any. However:

- BNDES's future methodology will make possible to present how a project contributes to the SDGs in the assessment report delivered to support the Board's decision, allowing the tool to play an indirect role.
- TSKB's SDG Mapping project makes possible to present how the loan portfolio contributes to the SDGs in an assessment report that is submitted to the Board. A preliminary an alysis has been already submitted to the Board that have been prepared by the project team.
- According to the responses received, only AFD's SDAO plays a direct role in the final decision. Risks are identified at the beginning of the project preparation cycle helping the preparation team to solve the issue during the project appraisal. Unless exceptional circumstances justify it, AFD's board does not accept any project with any negative mark.

3 - Recommendations

Progressively, most or all development banks' activity should become entirely SDG-compatible. IDFC members, in particular, are working together to further align financial flows with the SDGs. To do so, members need to transform their classical social and environmental safeguards into modern ex-ante and ex-post SDG-alignment tools.
Members who have taken part in this survey have outlined that they currently are at diverse steps of this transition. The lack of homogeneity and consistency among members is to be taken as an interesting opportunity to learn from each other. A difficulty to overcome is the difference of developmental languages among institutions, which sometimes creates confusion and/or misunderstanding, but working together to utilize the available indicators, metrics, glossaries will foster better comprehension. To speed up this transition towards effective SDG-alignment tools, a couple of main recommendations arise from this study.

SDG scope and mapping.
The promising results of the scope dimension in section 1 reflect the dedication of IDFC members towards the achievement of SDGs. Members could more systematically undertake mapping exercises, e.g. through tools such as the OECD-initiated "SDG-tracker". **Mapping is not alignment, does not identify any potential or actual negative impact, but is relatively easy to carry and is quite useful:**

- As a first, quite intuitive, step to discover what SDGs represent in an organization, i.e. as a mobilization tool.
- As an analytic tool, regarding the portfolio of a development bank, e.g. to identify the strengths, as well as orphan sectors.

SDG-alignment tools: standardization and harmonization.
Members should increase their collaboration about measuring development impact, all along their internal processes and systems (identification, assessment, monitoring and evaluation). This could include steps such as (i) conducting a comprehensive literature review of existing indicators, (ii) categorizing IDFC members in groups based on their activities, investments and operations, (iii) identifying the cross-groups indicators and groups' specific indicators, (iv) testing the applicability of the identified indicators, (iv) updating the indicators lists as required. If IDFC members share similar SDG taxonomy, monitoring indicators and impact methodologies, communication efficiency and global knowledge will improve. This aims to allow members to end up with a certain level of standardization while also having some flexibility according to their mandate, activity, and specific strategies. It will also contribute, internationally, to characterize a class of investments with a guaranteed level of SDG-consistency (sustainable development investment or SDI).

SDG-alignment tools: ex-ante AND ex-post.
To be fully SDG-compatible, all members should be able to guarantee that their decision committees are informed of the SDG-characteristics of all projects. This requires an ex-ante assessment tool, beyond simple E&S safeguards.

On the other way around, ex-post assessment tools are also extremely useful, to assess actual impacts, not only expected ones. They are also useful to fine-tune parameters used in ex-ante assessments. Therefore, all IDFC members should aim at having and using SDG-alignment tools in both the ex-ante and the ex-post phases of the project cycle and build a strong link between both.

SDG-alignment tools: make them used. To be really useful, members should make efforts to assure that alignment tools are:

- Covering the entire financing and investment activity portfolios;
- Consistent, in their methodology, with the multi-dimensional impacts of the SDGs;
- Providing quantified synthesis (yes/no, marks or grades), reflecting the potential positive or negative impact of a project or an investment, and therefore facilitating the final decision;
- And finally influencing the final Board decision.