

Analysis Determinant Factors For Optimization of Distributing & Monitoring Sustainability Linked Loan by Creditor - Case Study Bank X

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Abstract

Sustainability-linked loans (SLLs) represent an innovative financial instrument aimed at fostering sustainable practices by linking loan terms to the achievement of specific sustainability targets set by borrowers. Despite their potential, there remains a paucity of research examining the challenges faced by financial institutions in the disbursement and monitoring of SLLs from the perspective of lenders. This study seeks to identify the key obstacles encountered by Bank X in managing SLLs, which have impeded the optimal implementation of these facilities. By using a qualitative case study approach underpinned by the institutional logics framework, the analysis draws on interview data and the findings of the 2023 ESG audit. The findings reveal several critical challenges, including the absence of established portfolio growth targets for SLLs, inadequate training for personnel tasked with managing SLLs, inefficiencies in the documentation monitoring processes for SLL borrowers, delays in the formulation of relevant policies, and the lack of appropriate flagging mechanisms for SLLs within the bank's systems. To address these issues, it is imperative for Bank X's management to refine its operational methodologies, enhance the competencies of its human resources, and upgrade its information technology infrastructure to ensure the effective disbursement and monitoring of SLLs moving forward.

Keywords: Sustainability-linked loans, Institutional Logics, Sustainable Finance.

Amid a situation full of uncertainty regarding environmental and social aspects, the role of banking in supporting sustainable development has become increasingly vital. Banking has the potential to be the main pillar in supporting this through loans or loans for environmentally and socially friendly projects, so it is hoped that in the future, it will have the power to direct finances in a greener and more sustainable direction.

One of the banking products to support sustainable development is the Sustainability

Linked Loan (SLL). Asia Pacific Loan Market Association (APLMA) defines a Sustainability Linked Loan (SLL) as credit provided to debtors with interest linked to the achievement of measurable and independently verified sustainability targets (APLMA, 2022). This shows that SLL is designed to encourage debtors to improve their sustainability performance and contribute to sustainable development (Asian Development Bank (ADB), 2021).

As one of the state-owned banks that participates in sustainable financing, Bank X has succeeded in supporting this in the form of SLL distribution (International Finance Corporation (IFC), 2021). Bank Sustainability Report Bank X, 2022) trillion in 2022 or an increase of 100% compared to 2021 (Year on Year) towards 2 corporate segment debtors and 1 medium segment debtor (total distribution: 3 debtors). The success of the SLL distribution was also stated by Bank Sustainability Reporting (SR)

which was released in 2023. However, this distribution is still lower than Bank A which has succeeded in distributing SLL amounting to IDR 12.32 trillion to 10 debtors (Sustainability Report Bank A, 2022). Not only that, Bank D which has distributed SLL IDR 58.4 trillion (Sustainability Report Bank D, 2022) in 2022 and Bank E which has distributed SLL IDR 358 trillion (Sustainability Report Bank E, 2022). With details sustainability linked loan each Bank as follows:

Table 1: The disbursement of SLL loans by each bank

No.	Bank	Jenis Bank	Jumlah Pinjaman	Jumlah Debitur	Sumber
1	Bank X	State Owned	5,3 Trillion	3	<i>Sustainability Report Bank X 2022</i>
2	Bank A	State Owned	12,32 Trillion	10	<i>Sustainability Report Bank A 2022</i>
3	Bank B	State-Owned	2,1 Trillion	N/A	<i>Sustainability Report Bank B 2022</i>
4	Bank C	National Private	319 Billion	N/A	<i>Sustainability Report Bank C 2022</i>
5	Bank D	Foreign Private	58,4 Trillion	N/A	<i>Sustainability Report Bank D 2022</i>
6	Bank E	Foreign Private	358 Trillion	N/A	<i>Sustainability Report Bank E 2022</i>

Source: Sustainability Report for each Bank in 2022 (processed by the author)

The lag of Bank X compared to Bank A and foreign private banks in the disbursement of SLL raises a crucial question regarding the determining factors, particularly the challenges or issues faced by Bank X, which have hindered its optimal contribution to the disbursement and monitoring of SLL. To analyze this phenomenon, the researcher employs a case study research method, which is expected to serve as a strategic step in identifying problems and opportunities that can be leveraged to optimize the disbursement and monitoring of SLL by Bank X in the coming years.

Based on the results of initial observations carried out by researchers regarding SLL management and supported by interviews with Bank X's Internal Audit, determining factors were found in the form of internal obstacles faced by Bank The reasons include the lack of

information about the targets and strategies for increasing the SLL portfolio, HR training related to SLL has not been carried out, and the lack of monitoring of the performance of SLL debtors in the form of evaluation results from independent parties or Second Party Opinion (SPO) for achievements Sustainability Performance Target (SPT) in order to adjust loan interest rates (Thornton & Ocasio, 1999).

How to Research, (Du et al., 2023) suggest that it is still an open question the purpose of SLL in supporting sustainable practices as their research results show only *lender* only those who get benefits from this temporary from the side *borrower* has not shown a significant improvement in ESG performance.

Several previous studies have been conducted regarding SLL in supporting sustainable financing. However, previous research has focused more on the debtor's side and has not specifically discussed the constraints and constraints of banks as lenders/creditors in distributing and monitoring SLL. Based on this, the author will discuss in depth the constraints and obstacles of banks as lenders/creditors in distributing and monitoring SLL.

However, despite the potential benefits of SLLs, their implementation presents significant challenges for financial institutions, particularly in balancing traditional financial objectives with sustainability imperatives. One key issue is the ambiguity surrounding sustainability targets, which are often inadequately defined or lack industry-specific relevance. This ambiguity can lead to difficulties in measuring progress and enforcing compliance, undermining the effectiveness of SLLs as a driver of sustainable change. Additionally, many banks, including Bank X, face operational challenges such as insufficient employee training and weak monitoring systems, which further hinder their ability to manage these loans effectively.

The importance of addressing these challenges is underscored by the growing demand for sustainable finance. As corporations seek to improve their ESG performance in response to regulatory pressures and market expectations, banks are increasingly called upon to provide financial products that not only support corporate sustainability efforts but also contribute to their own long-term financial resilience. Yet, without a clear understanding of the barriers to successful SLL implementation, banks may struggle to fully leverage the potential of these instruments.

This study aims to examine the operational challenges faced by Bank X in the distribution and monitoring of SLLs, focusing on specific barriers such as the vagueness of sustainability targets, the adequacy of employee training, and the effectiveness of monitoring systems. By analyzing internal documents, sustainability reports, and interviews with key personnel involved in the SLL process, this research seeks to provide practical insights into the obstacles that banks encounter and to propose actionable recommendations for improving the management of SLLs.

The findings from this study will not only contribute to the academic literature on sustainable finance but will also offer valuable guidance for financial institutions looking to enhance their SLL frameworks. By addressing the identified challenges, banks can play a pivotal role in advancing the global sustainability agenda while maintaining financial performance.

Conceptual Framework

Institutional Logics is a conceptual framework that explains how patterns of values, beliefs, and norms shape actions and decisions within organizations. This concept is rooted in the view that organizations are influenced not only by technical and economic factors but also by social and cultural structures that give meaning to their activities. Within organizations, Institutional Logics are often communicated and reinforced through Symbolic Carriers and Material Carriers, two key elements that complement each other.

In this study, Institutional Logics will be utilized to understand how values, beliefs, and norms within organizations influence related practices and policies. This conceptual framework will include an in-depth analysis of the role of Symbolic Carriers and Material Carriers in shaping and reinforcing Institutional Logics, as well as how their interaction creates a social reality relevant to the organization. The analysis will provide insights into the process of internalizing institutional logics in various contexts and the challenges that may arise in its application. The conceptual framework of Institutional Logics is as follows:

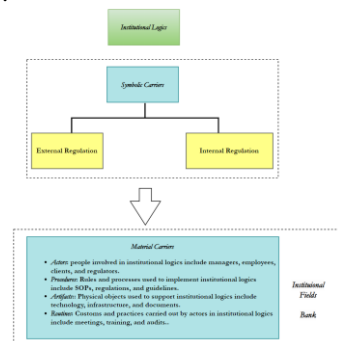


Figure 1: Institutional Logics

Source: Institutional Logics (processed by the author)

Research Methods

Research Strategy

This research will use strategy problem solving because it aims to find a solution to a particular problem. The most suitable type of research for this is a case study. Case studies are an appropriate research strategy because they can explore root cause/determinant factors in the form of internal obstacles/problems faced by the Bank. In addition, this case study is problem-solving because the author explores the obstacles/problems faced by the Bank. The criteria in this research were also developed by researchers based on a review of literature relevant to the case study to be researched.

Research Approach

This research will use a qualitative approach (qualitative method) case study. According to Creswell (2018), a qualitative research approach is a research method that focuses on understanding the meaning behind social and cultural phenomena. The qualitative approach in this research is in order to obtain a comprehensive understanding of the obstacles faced by Bank institutional logic.

Data Collection Techniques

Data source

In research, there are two main data sources that are often used, namely primary data and secondary data (Yin, 2014). The primary data used in this research are the results of interviews, data on the debt balance of debtors' loans from the Bank X system as SLL recipients. Secondary data used in this research are the Policies and SOPs of Bank X as the distributor and monitor of SLL, Sustainability Report Bank X and Sustainability Report others Bank.

Research Instrument

Data triangulation is a research technique that combines data from various sources to increase the validity and credibility of findings/ findings research (Yin, 2014), the scheme can be seen in Figure 2. Data triangulation aims to increase the validity and reliability of research findings by combining data from various sources (Yin, 2014). By data triangulation will help researchers to strengthen the information obtained in the evaluation process.

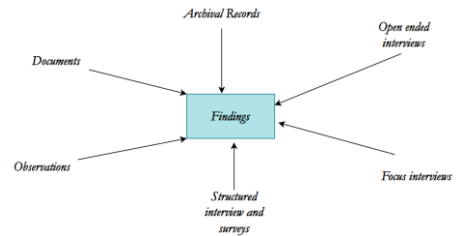


Figure 2 Data Triangulation, Convergence of Evidence
Source: Yin (2014), processed by the author

In this research, several types of research instruments are used which will be combined to produce some findings. interviews like open-ended interviews structured interviews, and documentation analysis.

Research Stages

The research begins with a literature review relevant to the study, followed by the development of the research framework. The framework serves as a guide for the researcher in data collection, both secondary and primary, which is then concluded with data analysis. The primary data collection is divided into several stages, including identifying interviewees, preparing relevant questions for each interviewee, conducting interviews, and confirming the results of the interviews.

Once the primary data is complete, the next step is the collection of secondary data in the form of policies and SOPs regarding the distribution and monitoring of SLL at Bank X, as well as the ESG audit results of Bank X to strengthen the findings from the interviews. This data collection technique is known as triangulation. After both primary and secondary data are complete, thematic data analysis is conducted, leading to findings, and ultimately, the research will provide relevant suggestions and recommendation

Result and Discussion

Bank X, as a state-owned bank committed to sustainable financing, has actively participated in distributing Sustainability Linked Loans (SLL). In 2022, Bank X successfully distributed SLL totaling IDR 5.3 trillion, marking a 100% increase Year on Year. This distribution supported two corporate segment debtors and one medium segment debtor, with a total of three debtors receiving sustainability-based financing. This achievement was highlighted in the 2023 Sustainability Report, emphasizing the bank's role in promoting sustainable business practices among its clients.

However, despite this progress, Bank X's SLL distribution remains relatively small compared to other banks. For example, Bank A distributed SLL worth IDR 12.32 trillion to 10 debtors, while foreign banks like Bank D and Bank E had significantly higher volumes, with IDR 58.4 trillion and IDR 358 trillion distributed in 2022, respectively. This disparity highlights challenges faced by Bank X in the process of distributing and monitoring SLL. Comparison of distribution of SLL each bank shown below in figure 3.

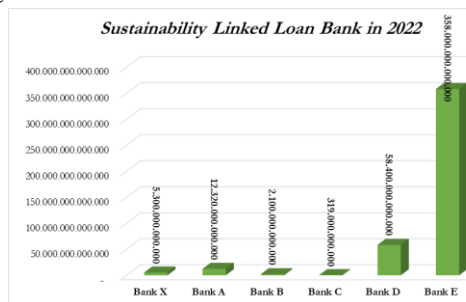


Figure 3 Sustainability Linked Loan Each Bank in 2022

Source: Sustainability Report Each Bank, processed by author

The researcher links these challenges to Institutional Logics, which involves three key elements: Symbolic Carriers (values, norms, and meanings related to sustainability),

Material Carriers (resources and infrastructure supporting SLL distribution), and Institutional Fields (the banking industry environment, including regulations, competition, and stakeholder expectations). The analysis reveals that the primary challenge for Bank X lies in the material aspect, particularly the limited resources and systems not fully supporting successful SLL distribution. This has resulted in less optimal outcomes compared to both domestic and foreign banks. The analysis aims to identify opportunities to strengthen material support and optimize Bank X's strategies for sustainable financing.

Not only that, based on Bank X Business Plan in 2022 and 2023, one of Bank X's products in supporting sustainability is the realization of green financing amounting to IDR 179 trillion (28.5% of the total credit distribution of IDR 629 trillion), which includes the Sustainability Linked Loan (SLL) amounting only IDR 5.3 trillion (or just 0.84% of the entire credit portfolio

as of June 2023). This indicates that Bank X's commitment to supporting sustainability through SLL distribution has not been optimal. The composition of SLL distribution compared to the total credit distribution of Bank X as of June 2023 is depicted in figure 4 below.

Sustainability Linked Loan Bank X compared to Total Credit Distribution in 2022

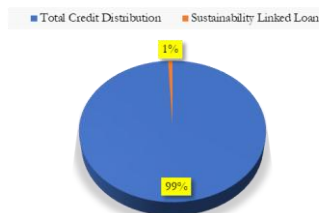


Figure 4 Sustainability Linked Loan Bank X compared to Total Credit

Source: Sustainability Report, processed by author

Determinant Factor

The researcher encountered challenges in the process of distributing and monitoring Sustainability Linked Loans (SLL) at Bank X. Based on interviews with the Environment, Social, and Governance (ESG) Management Department Head Internal Auditor Bank X, several challenges were identified in the distribution and monitoring of SLL at Bank X.

The challenges faced by Bank X, which have led to suboptimal distribution and monitoring of SLL, are categorized into five main topics: Strategy, Policies/SOPs, Human Resources, Monitoring Processes, and IT Support. These challenges are grouped as determining factors in the form of Material Carriers, and ultimately, these five issues are classified as the causes of the suboptimal distribution and monitoring of SLL, as shown in the following table.

No.	Determinant Factor	Category	Not Optimal
1	Determinan 1/Material Carrier 1	Strategy	Disbursement
2	Determinan 2/Material Carrier 2	Policy/SOP	Disbursement
3	Determinan 4/Material Carrier 4	Human Resources	Disbursement
4	Determinan 3/Material Carrier 3	Monitoring Process	Monitoring
5	Determinan 5/Material Carrier 5	IT Support	Monitoring

Figure 5 Determinant Factor

Source: author

Determinan factors related to Institutional Logics and Risk

Based on the analysis of the determining factors discussed before, researcher links the determining factors faced by Bank X as Material Carriers in Institutional Logics and relates them to the challenges in the distribution or monitoring process. Additionally, the researcher also connects these factors to the risks associated with each challenge/issue faced. A summary of the analysis of the determining factors is provided in the following table and diagram below.

Determining Factor	Internal Challenge	Issue	Material Carrier	Impact
Organizational Strategy	Distribution	There is no specific performance target set related to sustainability (ESG), including SLL targets	Routines	Operational Risk: 1. Undiscussed SLL distribution that does not align with the bank's priorities. 2. Difficulty in measuring the progress and effectiveness of SLL distribution.
Policies/SOP	Distribution	Delay in the creation of the SLL SOP, which was only made and approved in December 2023, while SLL distribution started in June 2022	Procedures	Compliance Risk: 1. Potential non-compliance with regulations. 2. Operational Risk: Inconsistent implementation across business units.
Human Resources	Distribution	According to the realization report, all staff managing SLL have not received relevant training on SLL or ESG as per the training data.	Actors	Operational Risk: Potential hindrance to operations due to lack of staff understanding and competence in ESG-related programs, especially SLL.
Monitoring Process	Monitoring	Supporting documents for debitor receiving SLL have not been completed, such as AMDAL, Environmental Permits, Paper Certification, etc.	Routines	Compliance Risk: Exposure to the compliance risk due to failure to meet document requirements as per POJK 18/2023 and SLP based on APJMA 2022.
IT Support	Monitoring	According to the call list, there is no flagging or special code for SLL financing to facilitate monitoring by both the debitor's business unit and ERM as the coordinator for ESG program monitoring	Artefacts	Operational Risk: The distribution of SLL is not well monitored.

Figure 6 Summary of Obstacles Faces by Bank X in Disbursing and Monitoring SLL

Source: author

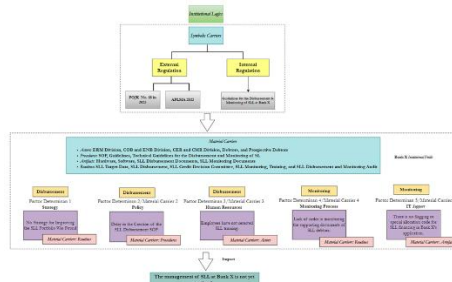


Figure 7 Summary of Obstacles Faces by Bank X in Disbursing and Monitoring SLL using Institutional Logics

Source: author

The researcher concluded that there are five main obstacles faced by Bank X in managing the disbursement and monitoring of SLL, which could potentially affect the effectiveness of the implementation of sustainability-based financing programs. These obstacles are identified by the researcher as the causes of the determinant factors that hinder the optimal disbursement

and monitoring of SLL. These determinant factors are related to organizational strategy, policies/SOPs, monitoring processes, human resources, and information technology support. Each of these factors is identified as a Material Carrier within the Institutional Logics framework, which exposes risks that could affect the operations and compliance of Bank X. The determinant factors are as follows:

CONCLUSION

This study provides valuable insights into the operational challenges faced by banks, particularly Bank X, in implementing and managing Sustainability-Linked Loans (SLLs). Despite the growing adoption of SLLs as a financial tool aimed at promoting environmental and social sustainability, several key barriers remain. These include vague sustainability targets, insufficient employee training, weak monitoring systems, and delays in adjusting interest rates based on borrowers' sustainability performance

The findings suggest that clearer sustainability metrics, tailored to specific industries, are essential for improving the effectiveness of SLLs. Additionally, robust monitoring systems and continuous employee training on sustainability-related matters are critical to ensuring compliance and maximizing the impact of these loans. To address the identified challenges, banks should also consider refining their incentive structures, ensuring that financial rewards and penalties are more closely tied to the achievement of sustainability goals.

Overall, this study highlights the importance of aligning traditional financial objectives with sustainability imperatives. By addressing the operational gaps identified in this research, banks can enhance their ability to contribute to broader sustainability goals while maintaining financial performance. Future research should further explore the development of industry- specific sustainability frameworks and the role of technological innovations in improving the monitoring and enforcement of SLLs.

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