CENTRAL BANK
OF THE REPUBLIC OF AZERBAIJAN

Sustainable Finance Survey

RESULTS

February 2025

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About the survey

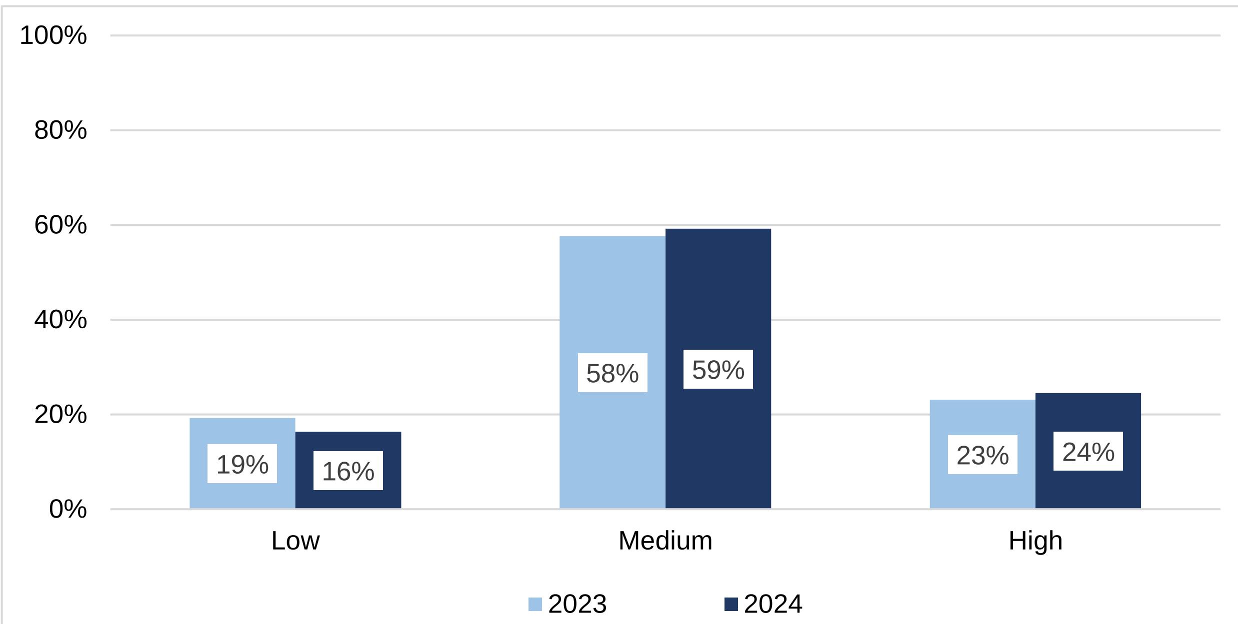
The purpose of the Sustainable Finance Survey is to measure financial institutions’ (banks, insurance companies and investment companies) awareness of sustainable finance and environmental, social and governance (ESG) principles, to explore the actions taken and planned to be taken in this direction, and to collect data. The results of the Survey, consisting of 4 sections and a total of 32 questions, have been analyzed for the financial markets in general and separately for banks, insurers and investment companies. The final part of the report presents the main findings of the Survey analysis and the next steps to be taken.

The Survey is conducted annually and aims to assess the implementation of sustainable finance and ESG principles in the financial sector. The results of the assessment are taken into account in the formulation of the Central Bank's policy on the development of sustainable finance in the financial sector. At the same time, the results of the Survey are made public in order to raise awareness among sector participants and to show market trends.

1. Financial sector overview

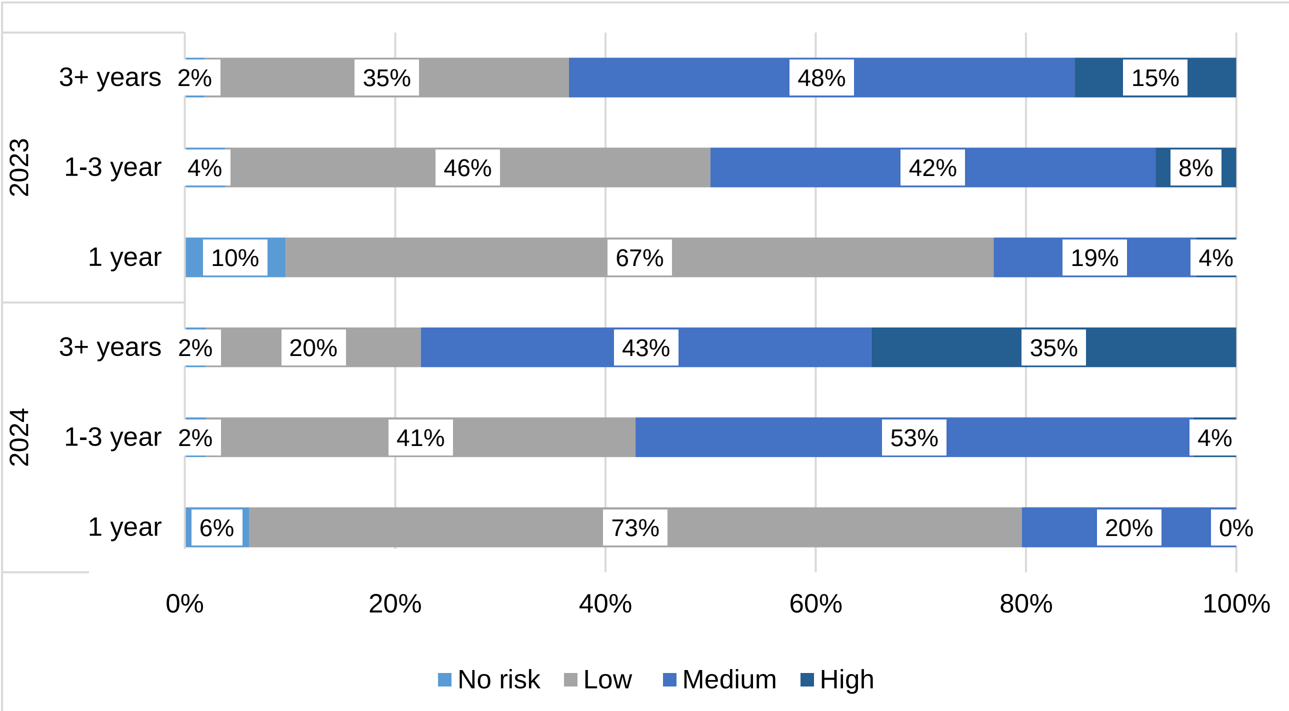
A total of 49 financial institutions participated in the Survey, including 21 banks, 12 investment companies, and 16 insurance companies. Based on the results of the Survey, more than 80% of financial institutions rated the importance of climate change and ESG risk management as medium and high (Chart 1). This indicates that market participants are aware of the importance of ESG risks in the financial sector and that the sector's awareness of these risks is increasing.

Chart 1. Financial institutions' assessment of the importance of climate change and ESG risk management in financial markets



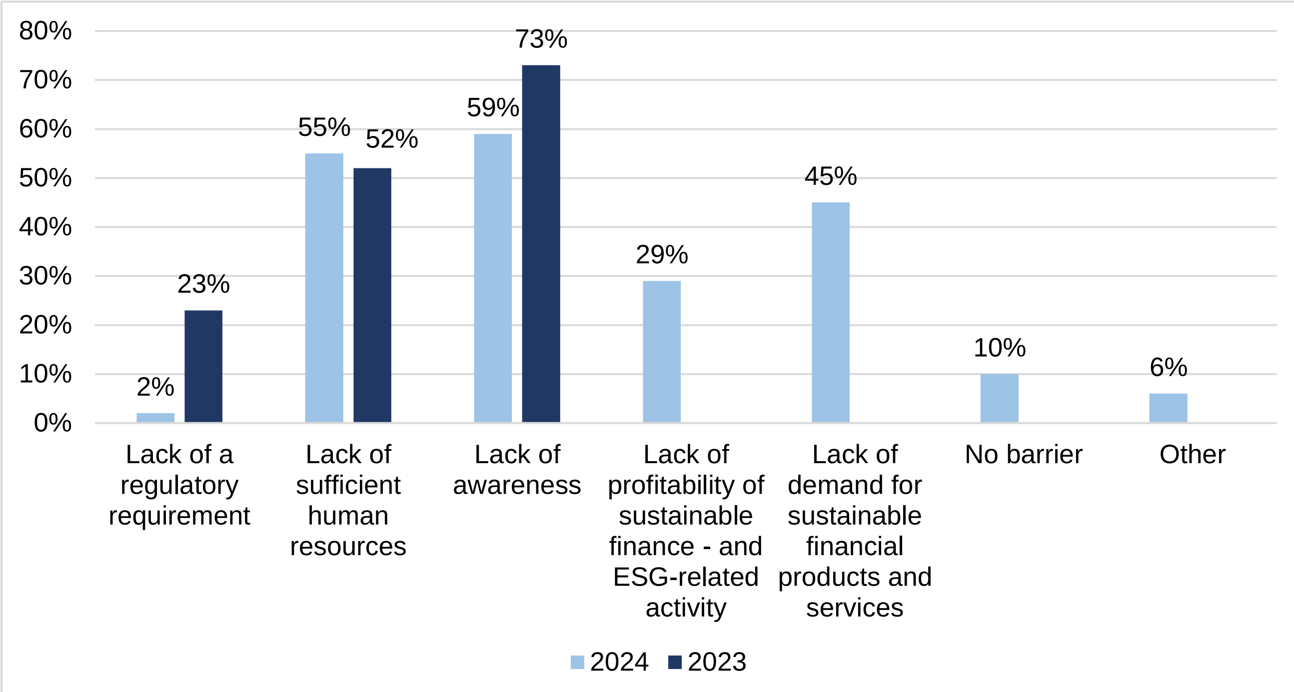
At the same time, the impact of climate change and ESG risks on the financial sector was assessed differently by sector participants over different time periods. 73% of financial institutions rated the impact of climate change and ESG risks as **low** in the short term (one year), while 53% of participants rated the impact as **medium** in the medium term. In the long term, 35% of financial institutions rate these risks as high and predict that the impact could be more significant (Chart 2). More financial institutions believe that climate change and ESG risks could have a high impact on the sector in the long term compared to last year's results. This is an indication that financial institutions consider the impact of climate-related and ESG risks on financial stability to be more significant in the long term.

Chart 2. Financial institutions' expectations regarding the impact of climate-related and ESG risks (no risk, low, medium, high)



Among the key challenges financial institutions face in implementing sustainable finance, insufficient human resources and lack of awareness remain the main obstacles, as last year. In addition, limited demand for sustainable financial products and services is another factor hampering the sector's development (Chart 3). Compared to last year's results, the lack of regulatory requirements is no longer cited as a major obstacle by most financial institutions. However, the need to strengthen human resources and raise awareness remains a critical factor in promoting the widespread adoption of sustainable finance.

Chart 3. Key barriers to sustainable finance implementation as reported by financial institutions



Women make up 42% of the financial sector workforce. Women accounted for 37% of new hires in the past 12 months. Beyond these figures, the numbers are low at senior management level, with a lower representation of women in senior management positions.

The banking sector has made significant progress in implementing ESG principles in line with the Central Bank's Sustainable Finance Roadmap 2023-2026. Approximately more than 70 percent of the banks have developed plans to comply with the Roadmap and have started to integrate ESG factors into their practices for the development of credit and non-credit products.

In terms of transparency and accountability in sustainability, the banking sector is also making significant progress. Work is continuing on the development and strengthening of the accountability framework. Embedding ESG principles at a management and strategic level is increasingly on banks' agendas.

The insurance sector is at an early stage of alignment with ESG principles. 12 out of 16 respondents indicated that they do not have an action plan in line with the Central Bank's Roadmap on Sustainable Finance. While several insurance companies have integrated ESG factors into their long-term business strategies, overall this process is not widespread across the sector.

Investment companies are less advanced than other segments in implementing ESG principles. The development of Roadmap compliance plans and the formulation of ESG strategies are not widespread in the sector.

Overall, there is a growing general awareness of the principles of ESG and of sustainable finance in the financial sector. This is mainly due to the banking sector. The first initiatives in this direction can be seen in the interest shown by some investment companies in issuing sustainability-related securities. Although a number of sustainable finance initiatives can also be observed in the insurance sector, work in this area needs to be intensified. In order to fully develop a sustainable finance ecosystem, it is important that all participants in the sector become more actively involved in the process.

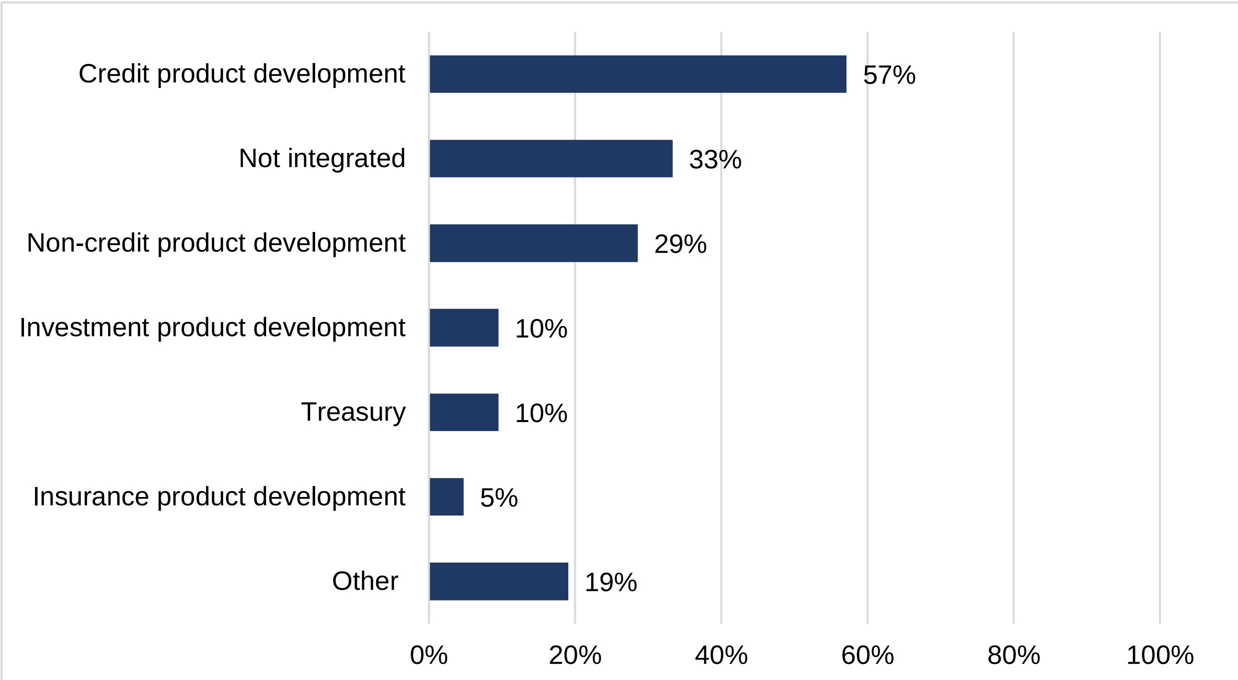
2. Banking sector

2.1 Business strategy

15 of the 21 banks surveyed have an action plan in place to implement the activities outlined in the Central Bank's Sustainable Finance Roadmap, while others have announced that they will develop such a plan during 2025.

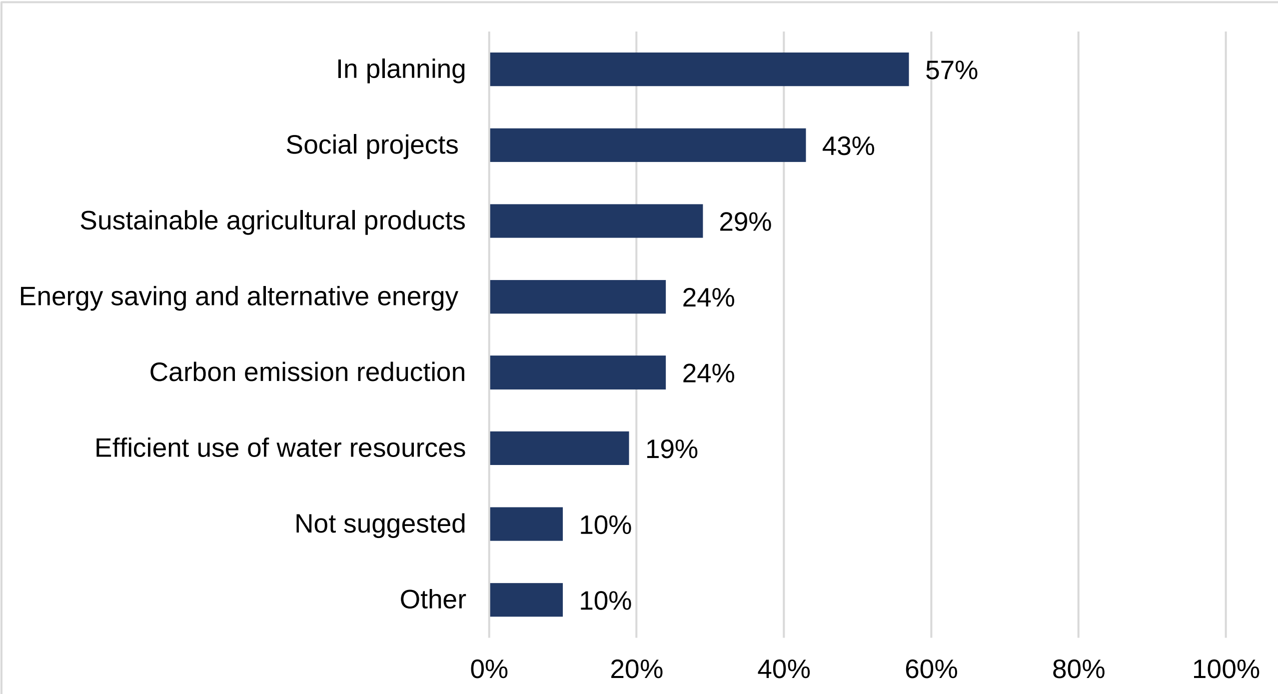
In most banks, ESG factors are integrated into the decision-making process for creating credit products. In addition, ESG factors are integrated into the decision-making processes for the creation of non-credit, treasury and investment products. 7 banks reported that they have not integrated ESG factors into their decision-making processes (Chart 4).

Chart 4. Integration of ESG factors into banks' decision-making processes



43% of banks offer products focused on social projects such as economic inclusion, affordable housing and gender equality. At the same time, 57% of banks said they plan their activities in this direction. This indicates that social responsibility is increasingly being implemented in the banking sector. However, the limited number of financial products offered in environmental areas is striking: energy efficiency and alternative energy (24%), carbon emission reduction (24%), sustainable agricultural products (29%) and efficient use of water resources (19%). Overall, the current picture shows that demand for environmental products and services is low and that there is a need to promote environmental projects in this direction (Chart 5).

Chart 5. Product areas incorporating ESG



Incentive differentiation for sustainable goods is currently used to a limited extent in the industry. 48% of respondents say they offer discounts on interest rates, while 19% offer discounts on interest-free terms. Many banks also present interest rate discounts for the financing of hybrid and electric vehicles as an important incentive mechanism.

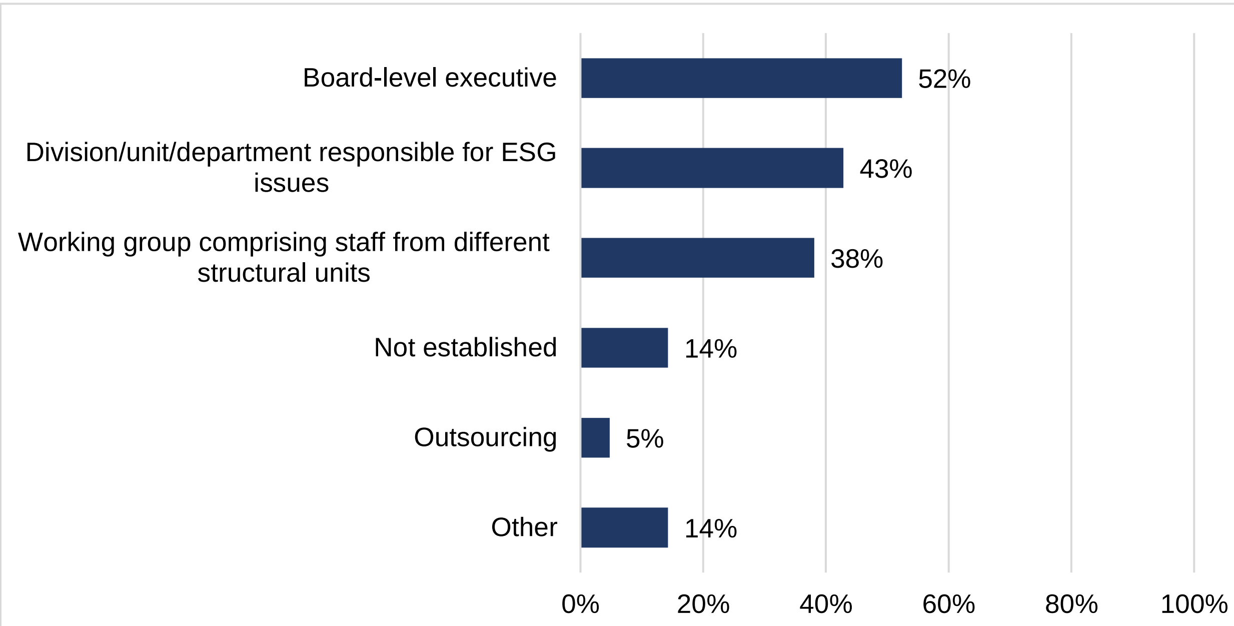
More than 70% of banks have started to cooperate with international organizations in various directions towards sustainable finance. Multilateral development banks play a key role in this cooperation. Cooperation with global companies in terms of consulting and training is also on the rise. Currently, 4 banks have started to attract funds from international foundations to combat climate change and to promote sustainable development. These initiatives demonstrate the existing international integration in sustainable finance and the prospects for developing the sector.

Resource efficiency has been considered in the strategic approach of many banks. The majority of respondents identified energy, water and paper savings as a priority in their operations. These results indicate that banks are focusing on managing resources according to sustainability principles in their operations.

2.2 Corporate governance

The integration of ESG principles into the corporate governance of banks has made significant progress. Thus, 52% of banks have appointed board-level ESG officers. 43% of banks have established a structural unit responsible for ESG, and 38% have set up working groups comprising staff from different structural units (Chart 6).

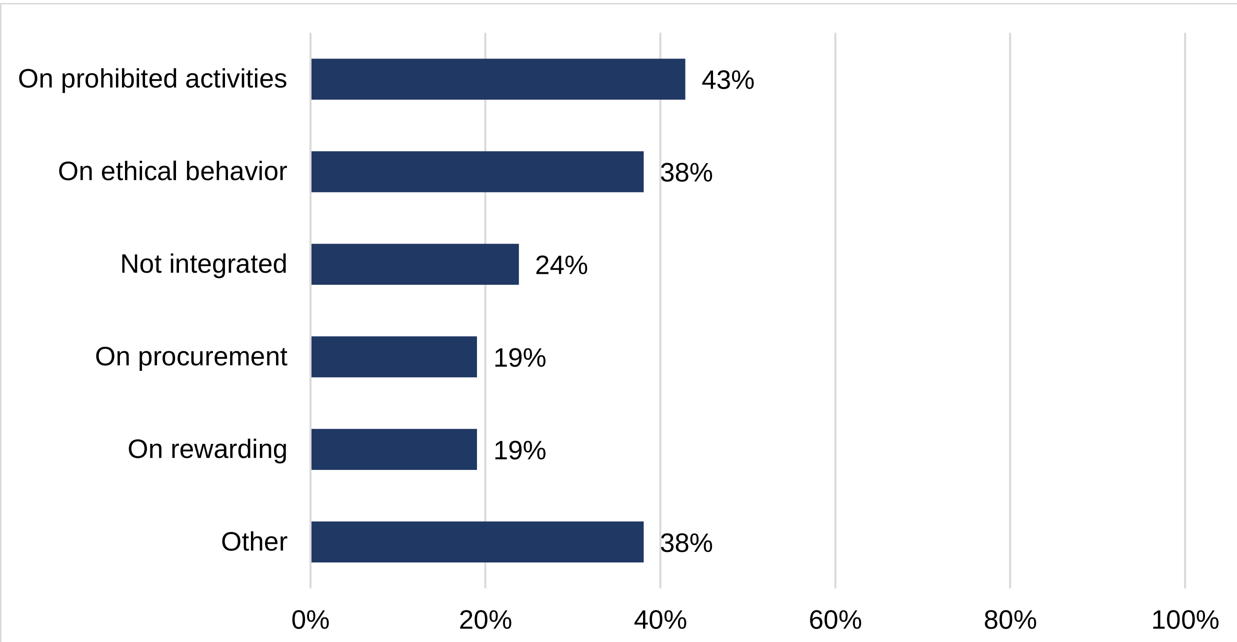
Chart 6. Integration of ESG and sustainability activities into the organizational structure in the banking sector



There has been some progress in managing sustainable finance and ESG risks at the bank supervisory board (SB) level. For example, 10 banks' SBs have defined the appropriate segregation of duties and authorities for implementing sustainable finance investments, and 12 banks' SBs have defined the appropriate segregation of duties and authorities for managing climate change and ESG risks. Most financial institutions have started to implement training and education programs to develop qualified human resources on climate change, ESG risk management and sustainable financial instruments. For example, 15 of the respondents indicated that they have defined programs in this direction. However, the participation of SB members in trainings on climate change and ESG risks is limited.

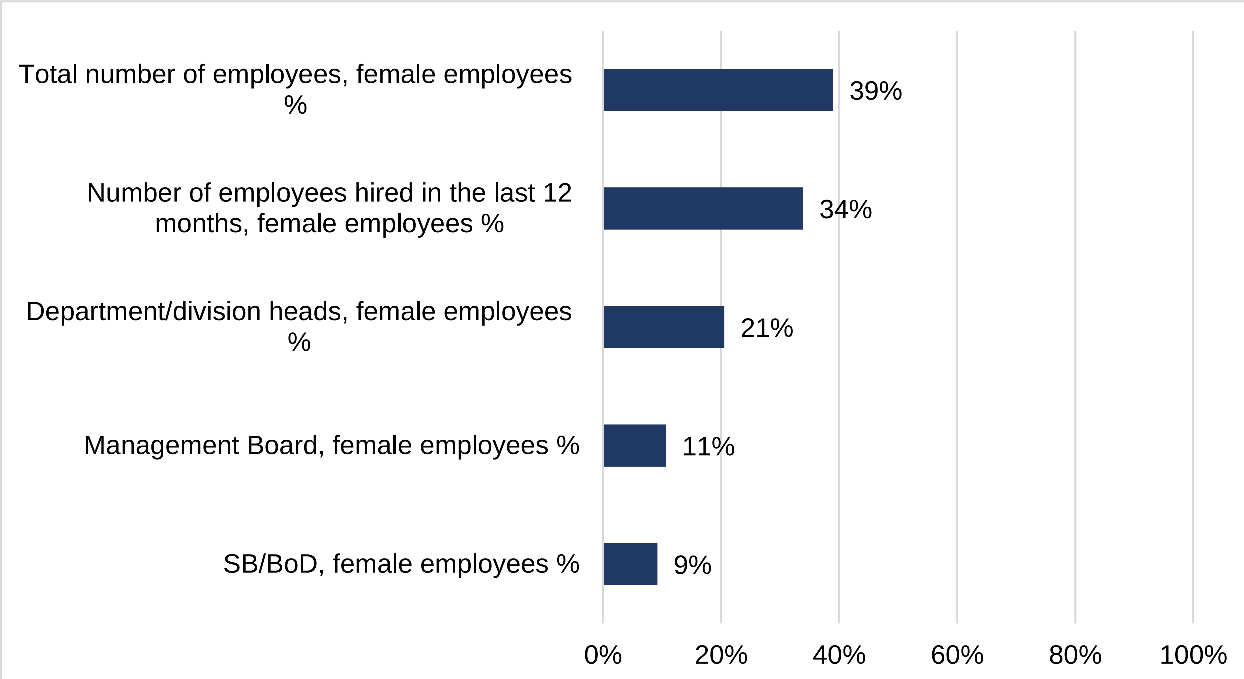
Banks have integrated ESG factors into their internal policies in several areas. The most frequently mentioned areas include regulations on prohibited activities (9 banks), on ethical conduct (8 banks), remuneration (4 banks) and procurement policies (4 banks). In addition, some banks reported integrating ESG factors into their credit decision-making processes and into the formulation of corporate social responsibility policies (Chart 7). Overall, while significant steps have been taken to integrate ESG principles into various internal policies, the sector needs to apply these principles more broadly.

Chart 7. Integration of ESG factors into banks' internal regulations



There has been no significant change in the total number of women employed in the banking sector and in the statistics of those hired in the last 12 months compared to the previous year. Women represent 39% of the total workforce and 34% of those hired in the last 12 months. This compares to 38% of the total workforce last year. Women are less represented at the management level. The proportion of women among department and division heads is 21%, and among members of the SB and the Management Board (MB) it is 9% and 11%, respectively. Internal requirements to consider gender diversity are reflected in the documents of only 8 banks, indicating the need for additional steps to promote gender equality at management level (Chart 8).

Chart 8. Share of female employees in the banking industry

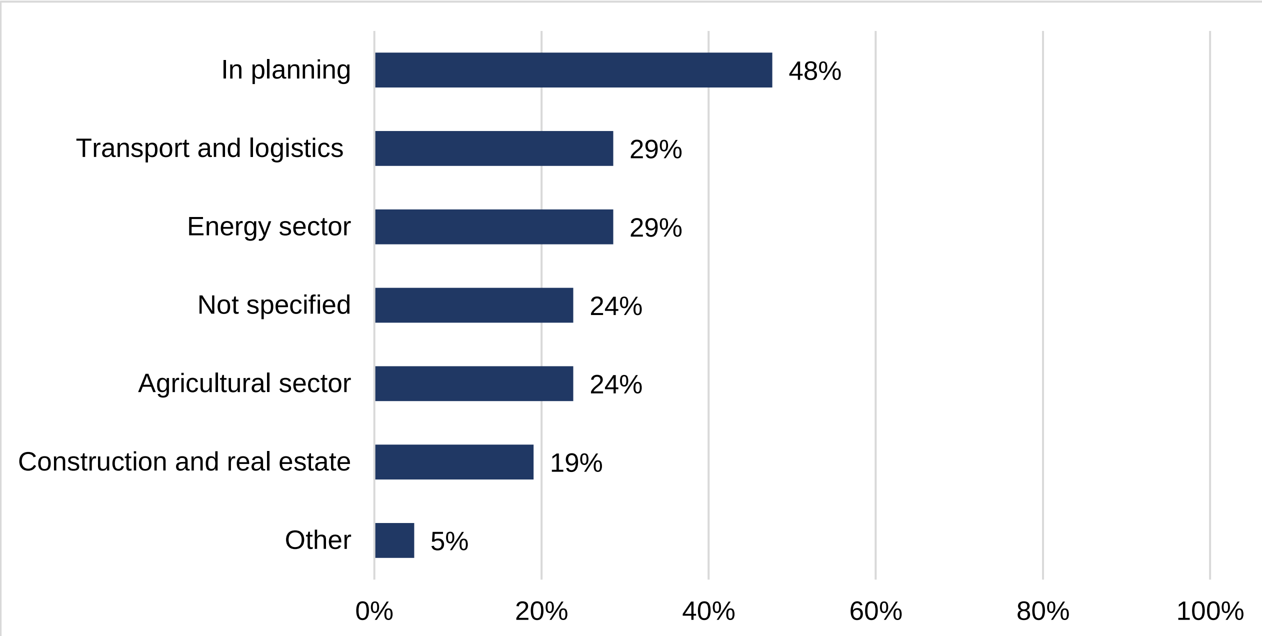


Some banks have started to strengthen their internal audit function to implement ESG principles and monitor the implementation of targets, as shown by the responses to the question on internal audit plans for 2025. For example, 12 banks reported that they have incorporated ESG issues into their internal audit plans. This is an indicator of progress in integrating ESG principles into corporate governance.

2.3 Risk management

In terms of integrating ESG factors into the risk management process, several banks identified physical and transition risks, as well as the list of economic sectors sensitive to transition risks. 5 banks identified physical risks and 6 banks identified the potential impact of transition risks, as well as the list of economic sectors that may be exposed to transition risks. Within this classification, the energy, transport and logistics sectors came to the fore. On the other hand, 15 banks indicated that they do not currently have a classification in this area, but that they plan to conduct such an assessment in the future (Chart 9).

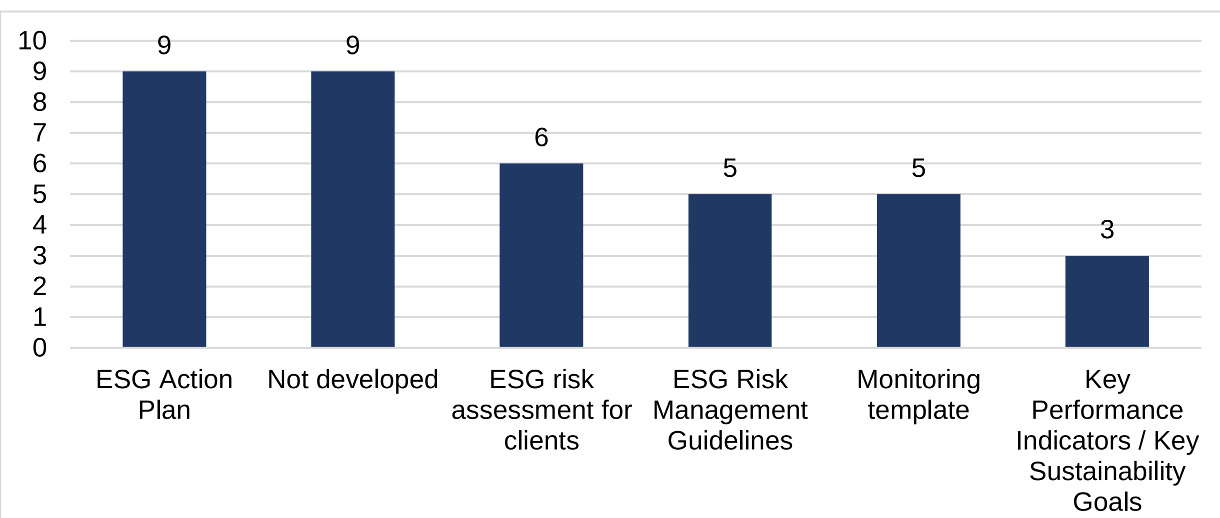
Chart 9. Identification of economic sectors vulnerable to climate risks



The integration of physical and transition risks into the stress testing framework is currently limited. Only 2 banks reported having integrated transition risks into the stress testing framework. The majority of banks surveyed indicated that they plan to do so in the current year (2025). At the same time, only 2 banks have experience in setting limits for physical and transition risks.

A number of banks have policies and procedures in place to manage ESG risks. Banks noted the existence of documents such as ESG risk assessment and management guidelines, action plans, and monitoring templates. A number of banks were found to lack such policies and procedures (Figure 10).

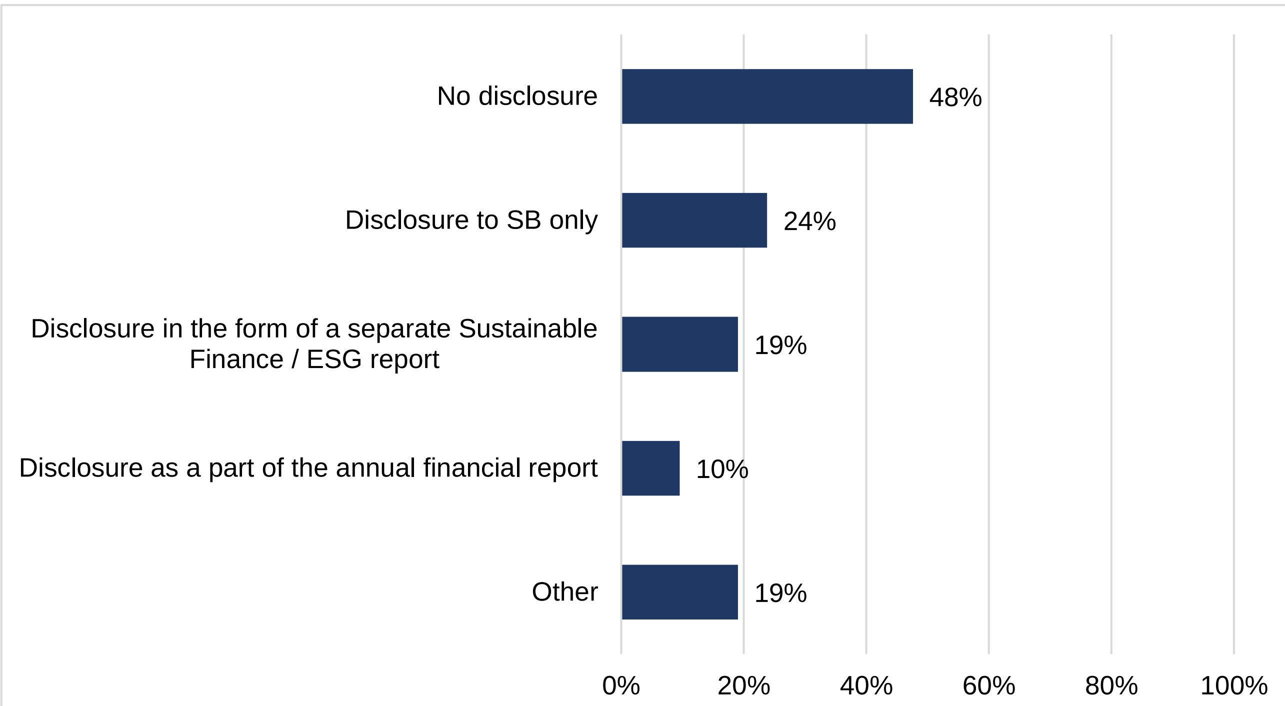
Chart 10. Policy and procedures



2.4 ESG Reporting

Half of the banks **report on their ESG strategies and sustainability activities.** These banks mainly report on ESG for stakeholders and through sustainability reports. However, about half of the banks surveyed do not report on ESG strategies, commitments and progress against Key Performance Indicators (Chart 11).

Chart 11. Disclosure of ESG strategy and activities



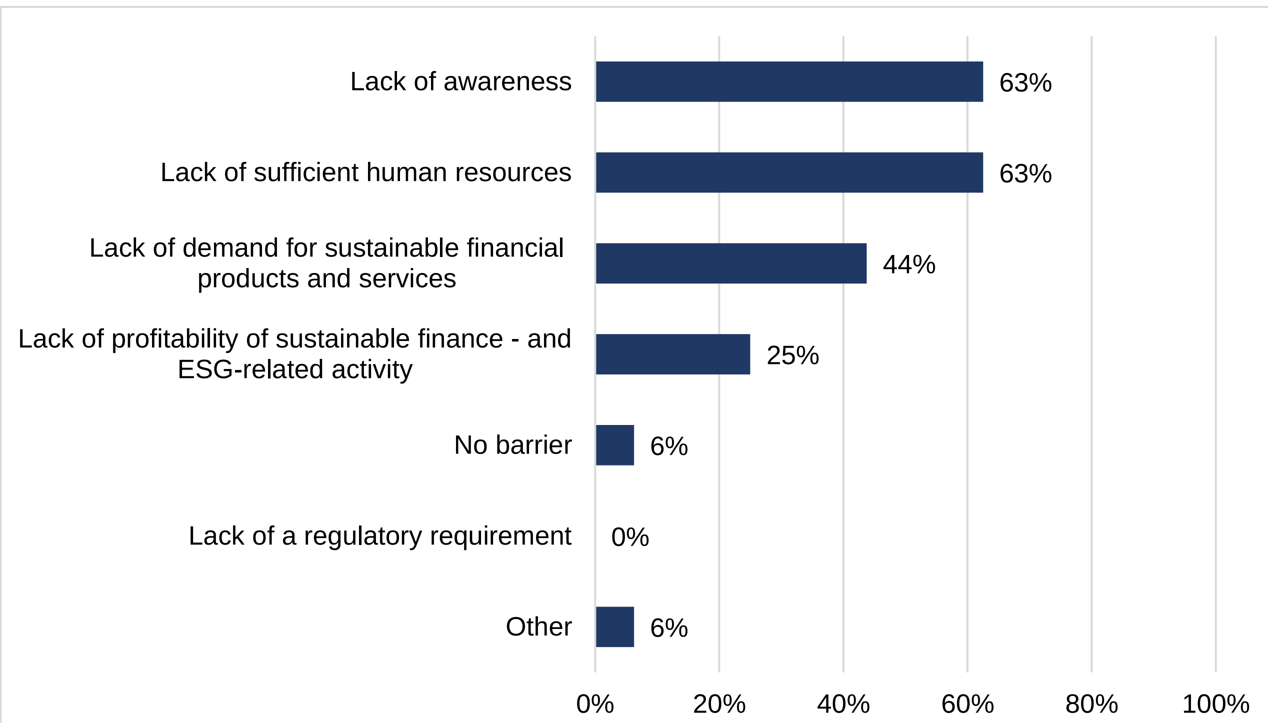
Established and published greenhouse gas (GHG) reduction and resource efficiency targets for the banking sector are not yet widespread. Only 5 banks reported measuring and disclosing Scope 1 and 2 GHG emissions. Only 1 bank reported measuring Scope 3 GHG emissions. However, 10 banks reported that they plan to measure and take actions on carbon emissions in the next period.

3. Insurance sector

3.1 Business strategy

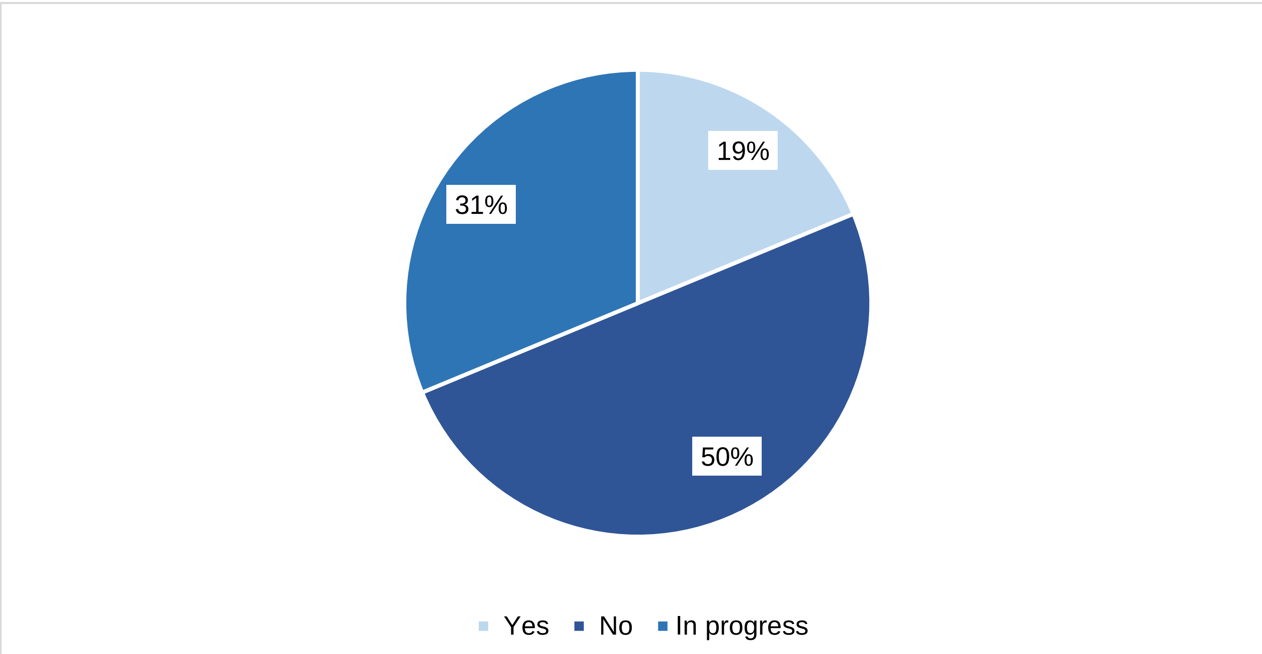
The integration of sustainable finance principles and ESG factors in the activities of the insurance sector is limited. Only 1 insurance company has a relevant plan to comply with the Central Bank's Sustainable Finance Roadmap. Lack of awareness and insufficient human resources were identified as the main barriers to the implementation of sustainable finance principles among insurance companies. Limited demand for sustainable finance products and services and the lack of profitability of such activities were also identified as challenges (Chart 12).

Chart 12. Key barriers to sustainable finance implementation as reported by insurers



The integration of ESG factors into long-term business strategy and decision-making processes in the insurance sector is limited (3 companies). Although a small number of companies reported integrating these factors into their strategy, most companies indicated that this process was at an early stage. In terms of decision-making processes, ESG factors were mainly considered in the area of insurance product design. These findings suggest that further action is needed to ensure that the sector applies ESG principles more widely (Chart 13).

Chart 13. Integration of ESG factors into the long-term business strategy of insurance companies



The insurance sector does not engage extensively with international organizations on environmental and social issues. Only 13% of companies reported participating in trainings organized by international organizations and 19% reported using consulting services. These results point to the need for the expansion of international co-operation and exchange of experience in the sector.

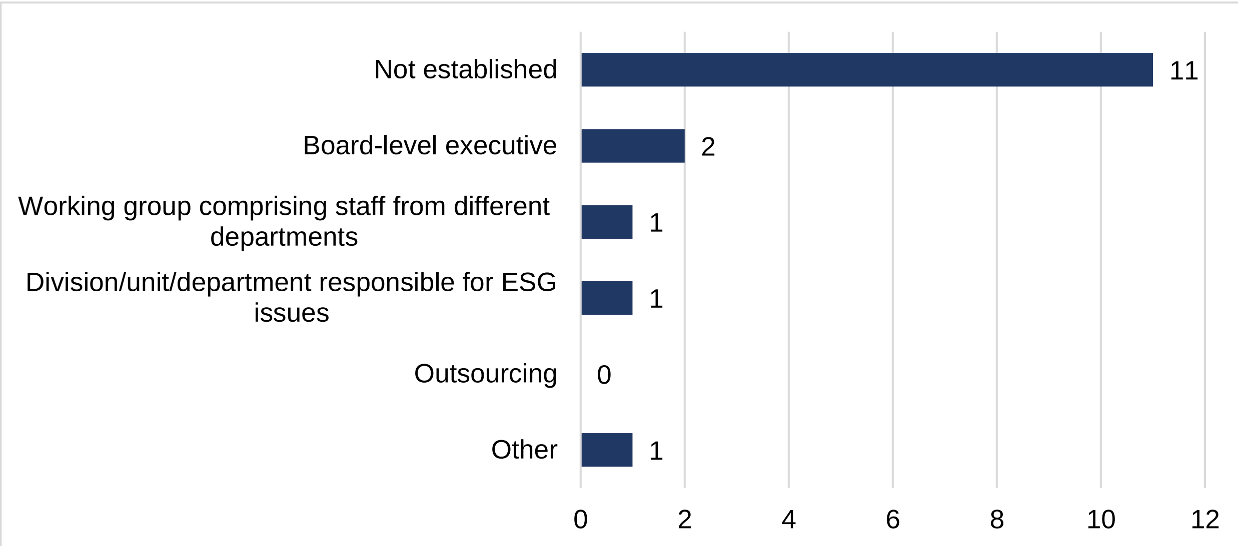
Paper reduction was the most frequently cited area in insurance companies' resource efficiency strategies (15 companies). In addition, 6 companies identified energy and water conservation as top targets. Only one company said it had no resource efficiency targets.

3.2 Corporate governance

The integration of ESG factors into corporate governance in the insurance sector is also limited. Only 2 companies reported that the Board of Directors (BoD) has implemented a shared responsibility and authority for managing sustainable financial investments and risks. In addition, 5 companies reported that at least one member of the BoD had received training on

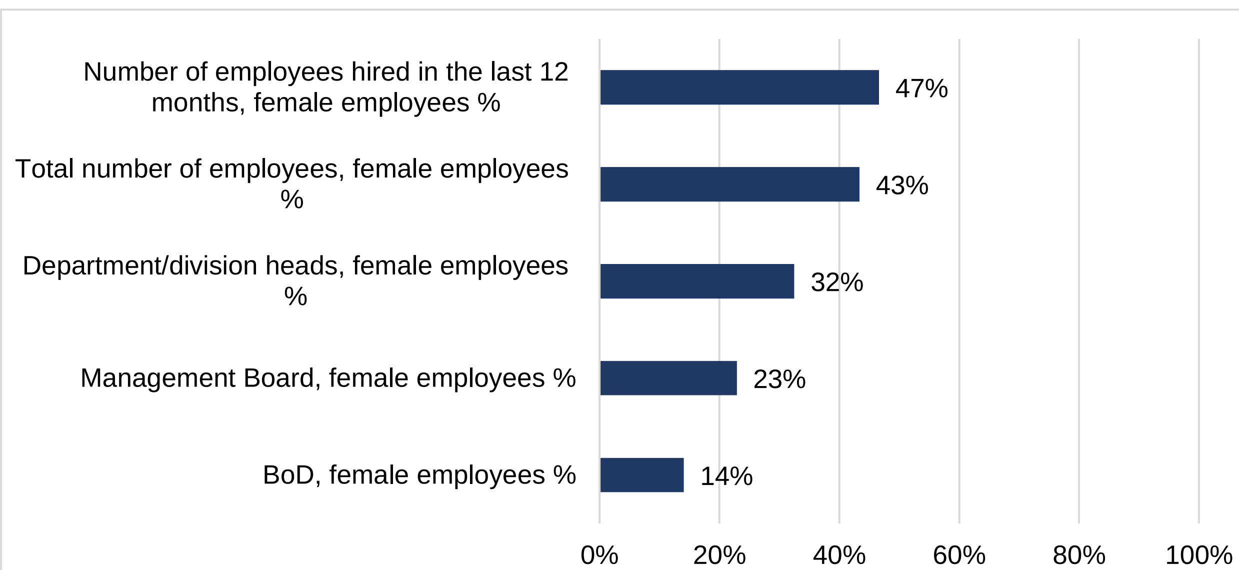
ESG risks and opportunities. Only 2 companies have appointed a person responsible for sustainable finance issues at board level (Chart 14).

Chart 14. Governance framework for sustainable finance in the insurance industry



There are some positive indicators regarding gender diversity in the insurance sector. Women represent 43% of the total workforce and 47% of those hired in the last 12 months, which is a positive trend in terms of gender equality in the sector. Women also represent 31% of department and division heads, 14% of board members and 23% of senior management, which is a positive trend in the financial sector (Chart 15).

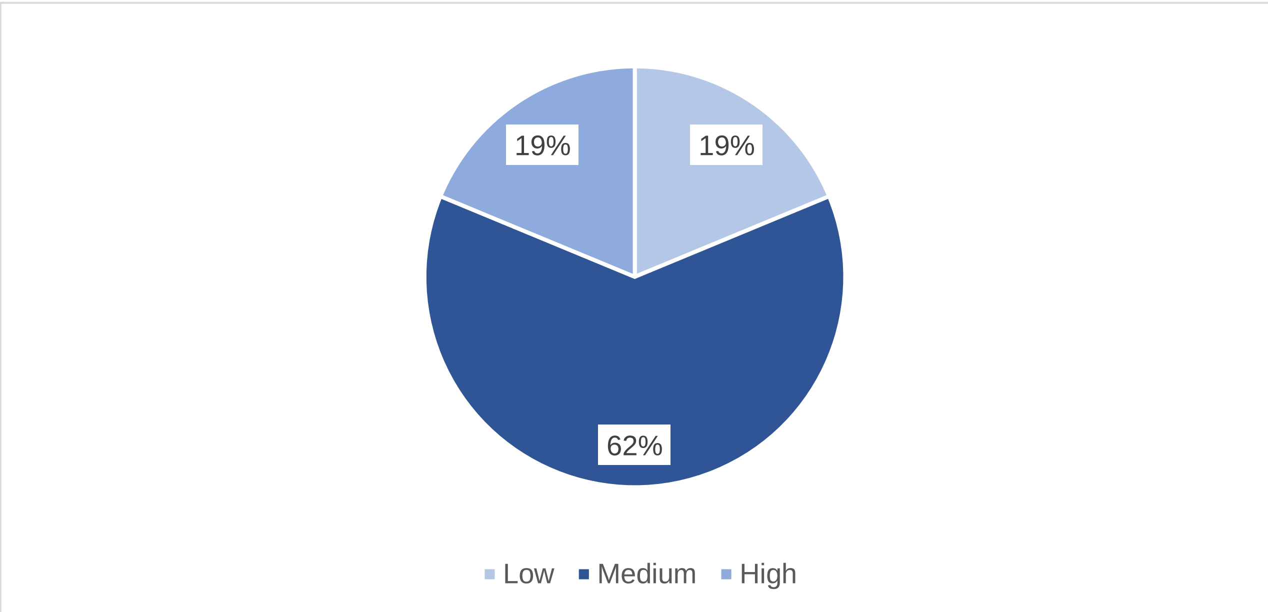
Chart 15. Share of female employees at different levels of management in the insurance industry



3.3 Risk management

The insurance sector rated the importance of ESG risks at a medium level. According to the results of the Survey, only 19 percent of the insurance companies stated that climate change and ESG risks are of high importance in the financial markets of Azerbaijan. Over 60% of companies considered these risks of medium importance (Chart 16).

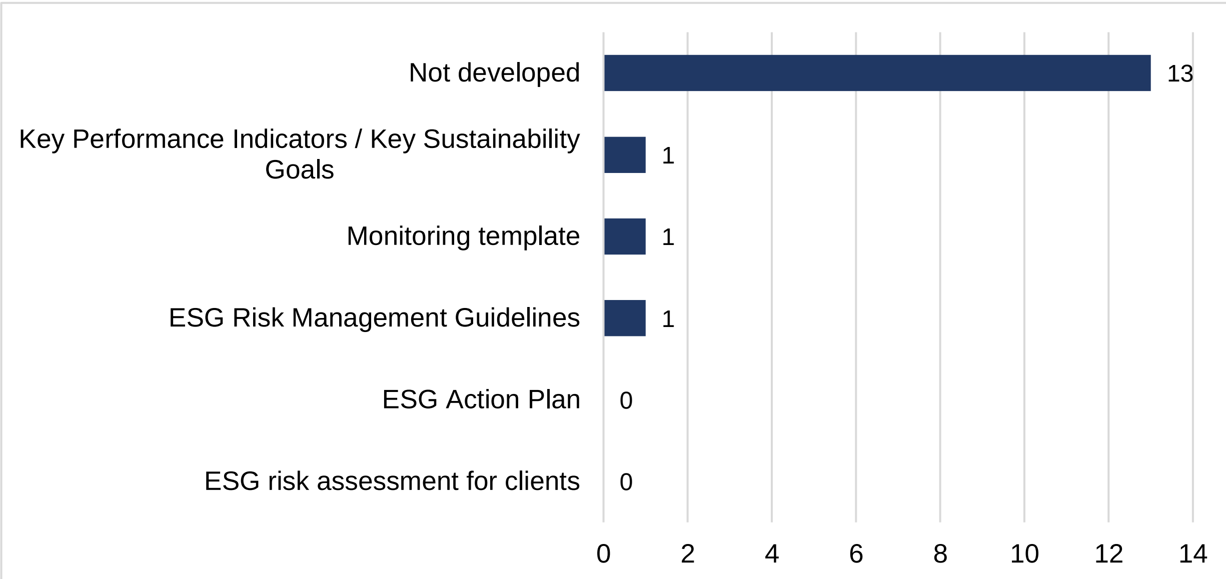
Chart 16. Assessment of ESG risks by insurance companies



In terms of the impact of the risks, 54% of the insurance sector consider the risks to have a low impact in the short term (1 year), while 46% believe they have a medium impact. In the long term (more than 3 years), the risks were perceived as more serious. For example, 46% of companies rated the impact as high.

The development of internal documents on ESG risk management in the insurance sector, setting risk appetite limits and integrating these risks into business decision-making processes and stress testing, as well as establishing internal reporting on ESG risks are at an early stage. Only 1 company reported having developed ESG risk management policies, a monitoring template and key sustainability objectives (Chart 17). 2 companies identified sectors at risk. These indicators show that the insurance sector has great potential for development in ESG risk management and structured approaches.

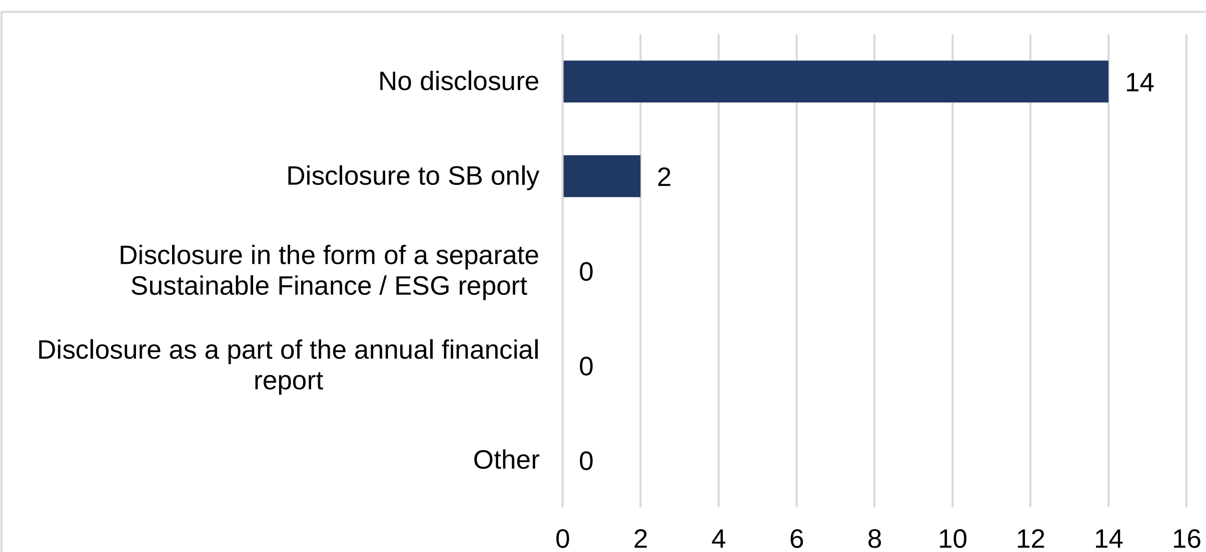
Chart 17. Development of appropriate trainings or tools to integrate ESG risks into business decision-making process



3.4 ESG Reporting

The insurance sector is limited in its disclosure of sustainability strategy, risks, opportunities and related information. 14 insurance companies reported that they do not disclose this information at all. Only 2 companies reported sharing this information with the SB on a limited basis. No information was disclosed in a separate publicly available sustainability financial/ESG report or integrated into the annual financial report (Chart 18).

Chart 18. Disclosure of strategy, risks, opportunities and other related ESG information



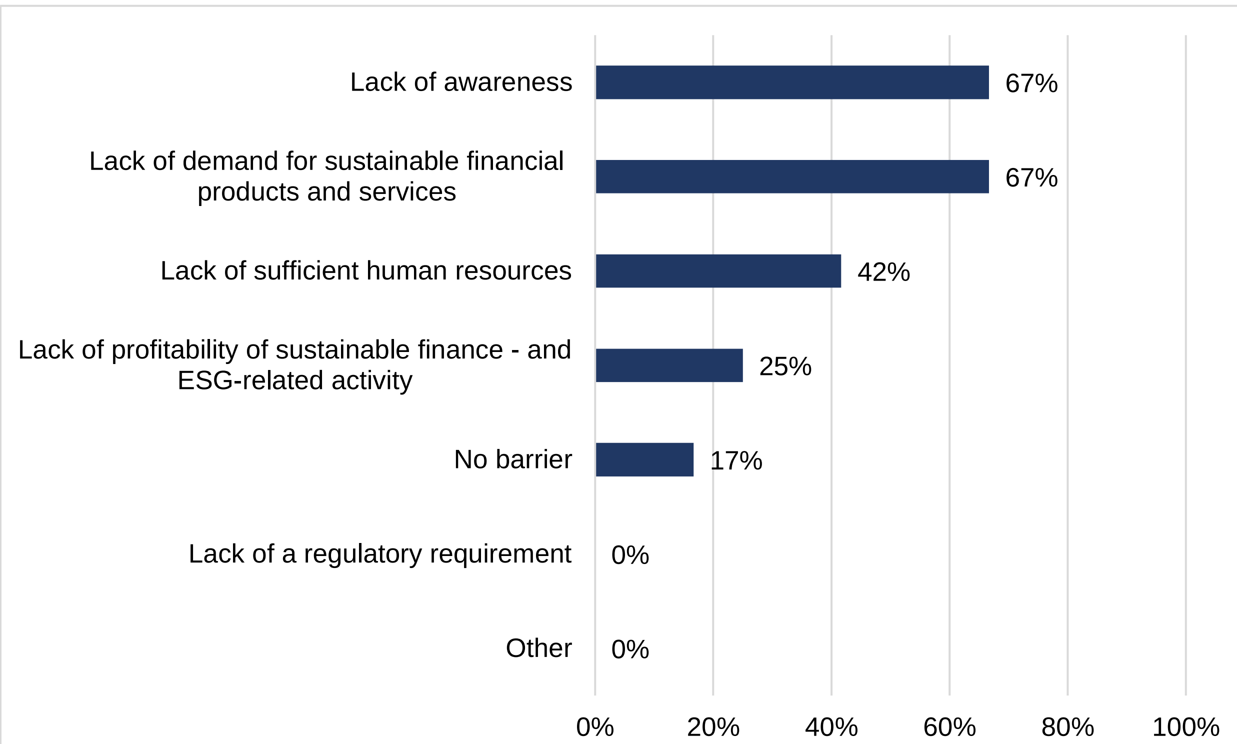
In terms of carbon disclosure, the vast majority of companies (15 companies) indicated that they do not measure this information. Only 1 company reported having such plans.

4. Capital market

4.1 Business strategy

The vast majority of investment companies have not yet integrated ESG factors into their long-term business strategies. Companies cited the lack of awareness, demand for sustainable financial products and services, and insufficient human capacity in this area as the key barriers to integrating sustainable finance and ESG principles into their operations (Chart 19).

Chart 19. Key barriers to sustainable finance implementation as reported by investment companies



More than half of the investment companies did not have ESG factors as part of their decision-making process. Most companies incorporating ESG principles have taken actions in the area of investment product development. At the same time, the analysis found that only one investment company offered a financial product aimed at reducing carbon emissions. It is also clear that during the period covered by the survey, the investment companies did not apply any kind of incentive differentiation for sustainable products.

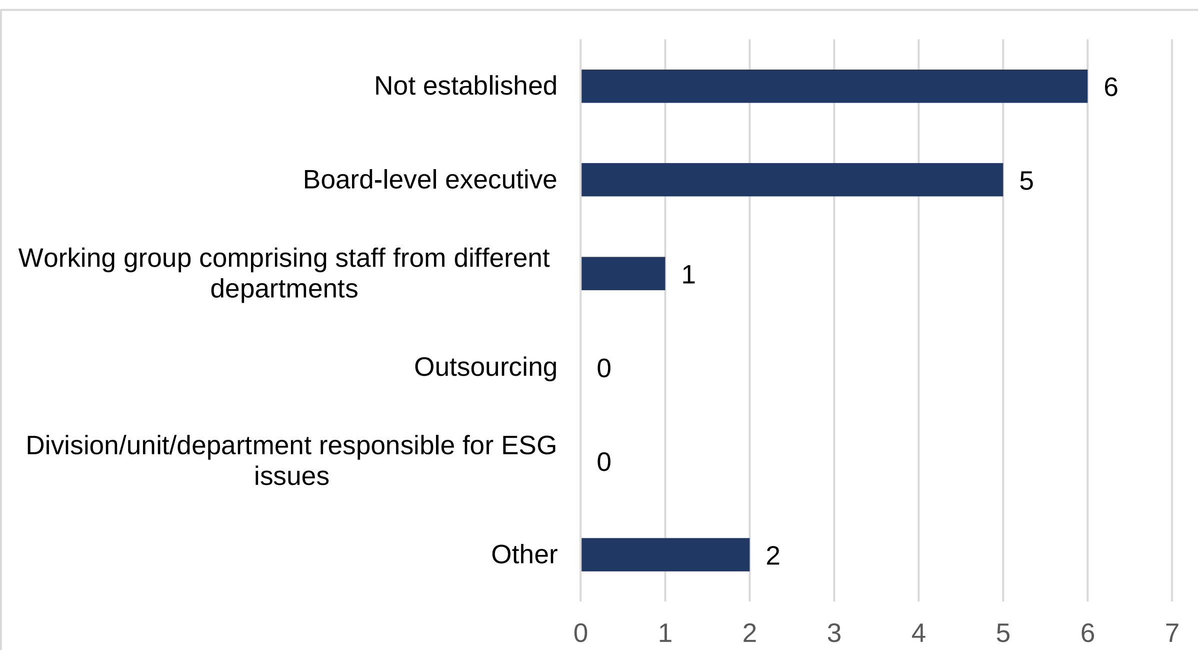
The results show that the cooperation of investment companies with international organizations is generally limited and that initiatives are needed in this area. Only 2 of the investment companies reported cooperation with international organizations in the areas of training and attracting funding.

Approximately half of the investment companies reported the implementation of resource saving measures in their operations. Companies that reported implementing resource efficiency measures indicated that their activities were primarily focused on reducing paper waste, but had limited activities in the areas of water and energy conservation.

4.2 Corporate governance

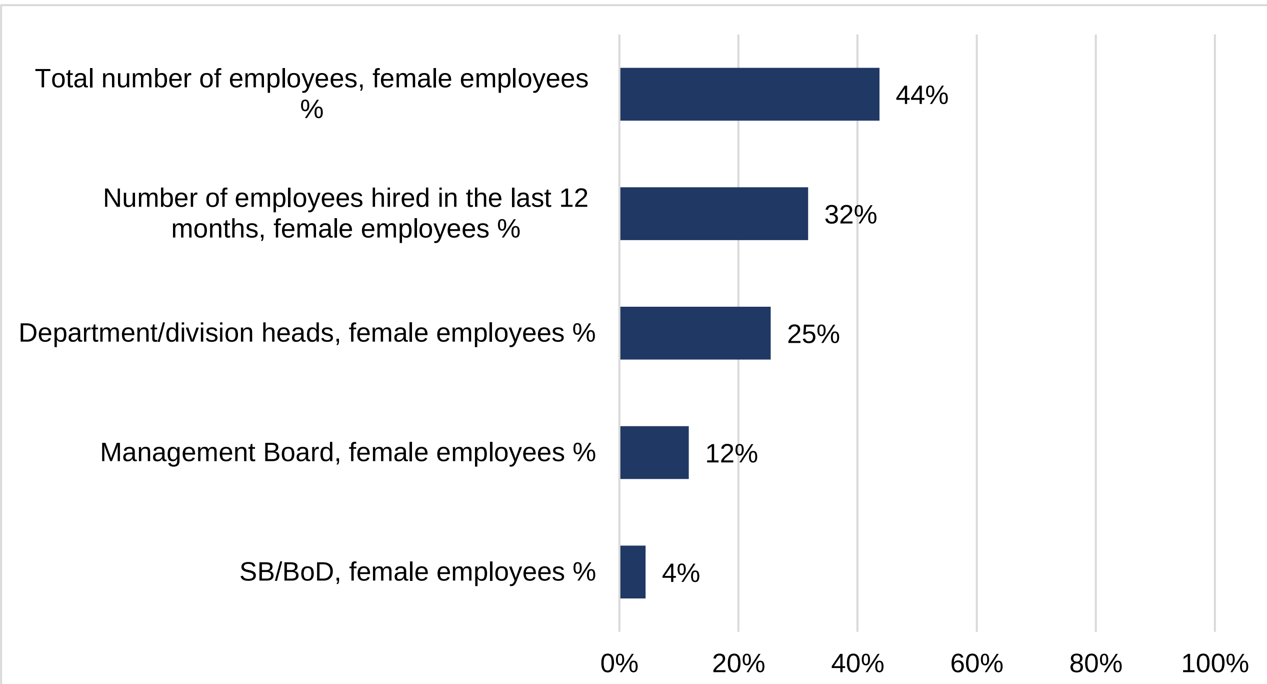
Investment companies are at a limited stage of development in terms of integrating ESG factors into corporate governance. Five companies have appointed a person responsible for ESG issues at HR level, and one company has set up a working group comprising employees from different departments (Chart 20). Only 1 company has defined the division of duties, authorities and responsibilities for the implementation of green, social and other sustainable financial investments at the SB level. These indicators suggest that the management mechanisms for sustainable financial investments are not yet fully established in the vast majority of companies. The lack of segregation of duties at the SB level also indicates that sustainability decisions are not being made systematically or that corporate governance in this area is weak.

Qrafik 20. Governance framework for sustainable finance in investment companies



The investment companies' gender diversity performance is close to the industry average. Women currently make up 44% of the workforce and 32% of new hires last year. However, women are less represented in senior management positions. While women hold 25% of positions such as department and division heads, the numbers are even lower at senior management levels. Women hold 4% of SB positions and 12% of MB positions (Chart 21).

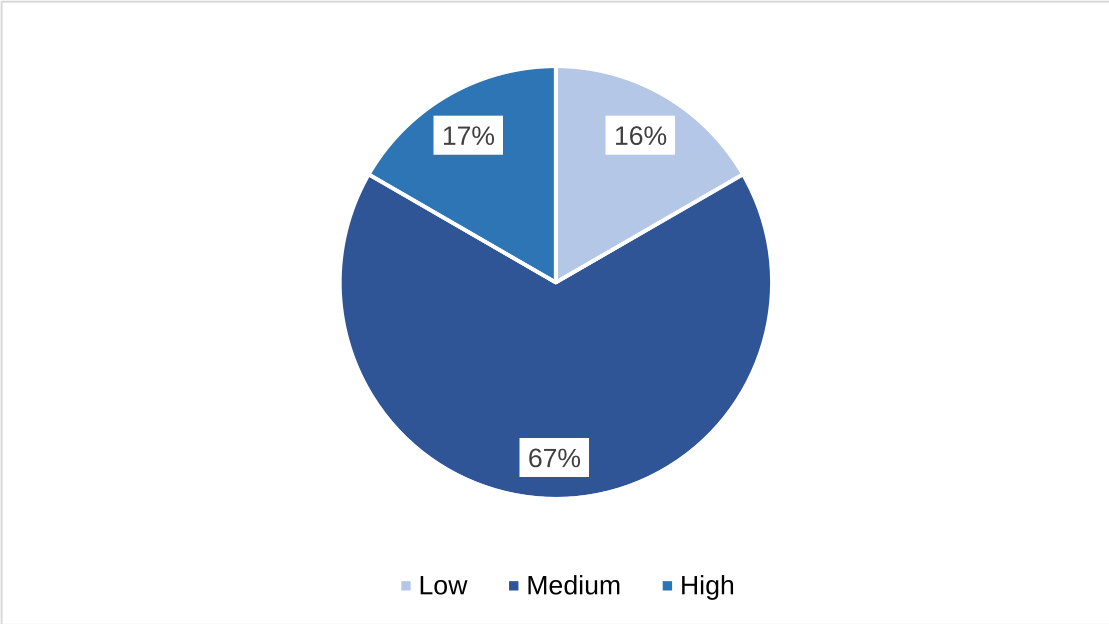
Chart 21. Share of female employees at various management levels in the investment sector



4.3 Risk management

67% of investment companies rate managing ESG risks as moderately important (Chart 22). Most capital market participants believe that the impact of climate change and ESG risks will be low in the short term, but moderate to high in the medium and long term.

Chart 22. The importance of managing climate-related and ESG risks

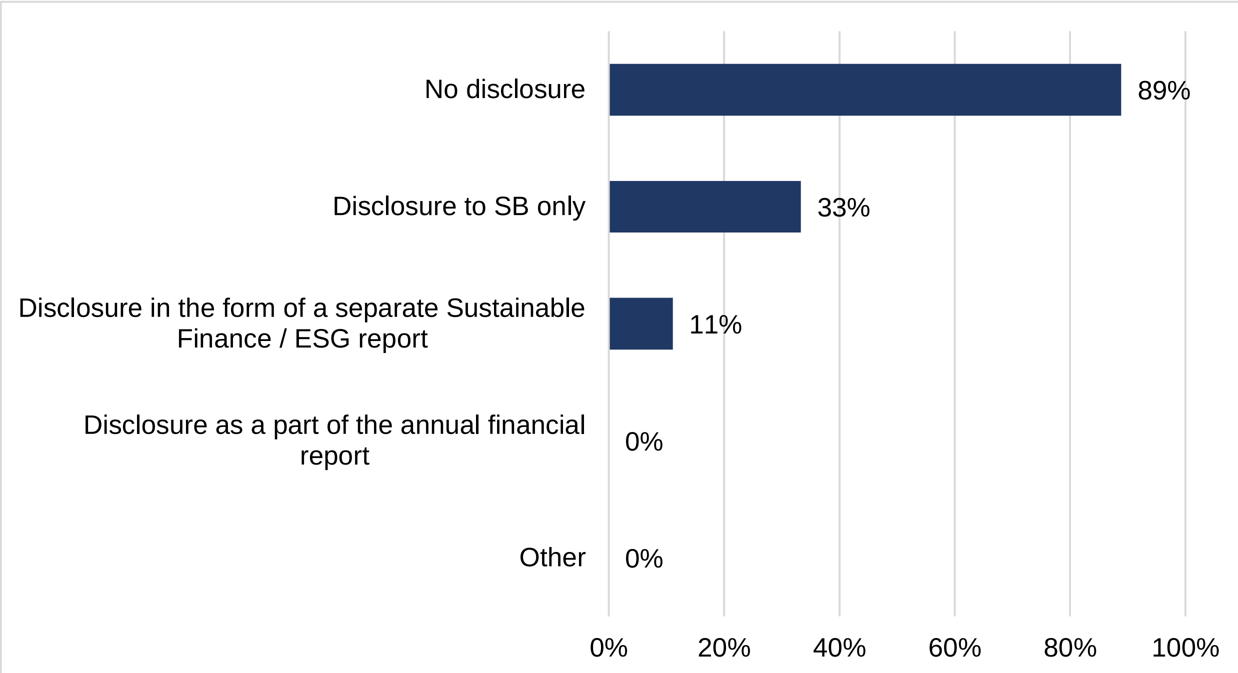


Overall, the level of climate-related risk identification in investment companies is low. More than 80% of investment compaies have not taken any action to identify climate-related risks. Only one company reported having developed a policy to integrate climate-related and ESG risks into business decision-making. These findings highlight the need for investment companies to improve their management of ESG risks.

4.4 ESG Reporting

According to the disclosure section of the Survey, investment company disclosure of sustainability strategies, risks, opportunities and related information is limited. For example, 8 companies reported that they do not provide this information in any form. 3 companies reported that they provided this information to the SB. Only 1 investment company disclosed the information in a separate, publicly available sustainable finance/ESG report or in an integrated form in the annual financial report (Chart 23).

Chart 23. Disclosure of strategy, risks, opportunities and other ESG-related information



Finally, with respect to disclosure of carbon emissions, only 3 companies indicated that they had plans to work in this direction in the near future.

These findings reiterate that investment companies have a lower level of application of ESG principles than other financial institutions, and that future years will require action to ensure development in these areas.

5. Conclusion and priorities

The Survey results indicate the need for broader initiatives to improve ESG and sustainability performance in financial institutions. Building on existing efforts, initiatives will be pursued in line with the Sustainable Finance Roadmap to achieve progress in the development of sustainable finance in the country. These initiatives will cover at least the following areas:

5.1 Business strategy:

- **Strengthening the ESG policy framework:** It is considered essential for financial institutions to develop formal internal policies to manage the risks of sustainable finance and ESG principles, and to develop and implement a plan in line with the Central Bank's Sustainable Finance Roadmap for 2023-2026.
- **Setting ESG targets:** Financial institutions should set targets for reducing GHG and becoming resource efficient.
- **Introducing innovative social impact mechanisms:** There is a need to expand sustainable and inclusive financial products, such as SME-focused loans and hybrid car loans.
- **Investing in employee development:** Providing internal and external training opportunities in ESG-related skills can foster innovations and increase staff readiness for sustainable finance. It is important for financial institutions to be part of the UN Sustainable Development Goals and other international sustainability initiatives.
- **Raising awareness:** Initiatives to promote understanding of ESG principles and their relevance to business operations can help embed sustainability into corporate culture.
- **Encouraging green finance products:** Expanding the supply of green credit, green insurance, and sustainability-related financial instruments can stimulate demand for green and sustainable projects.

5.2 Corporate governance:

- **Strengthening the governance capacity for ESG:** It is essential for financial institutions to integrate sustainability issues into the framework of their middle and senior management and to establish an internal structure that is responsible for ESG. In addition, clear governance frameworks should be promoted, including the representation of independent members on management bodies and gender equality policies.

- **Promoting gender equality:** Financial institutions should strengthen gender equality in leadership roles and expand the implementation of social programs to support staff well-being and general care.
- **Aligning incentive mechanisms with ESG goals:** In addition to financial rewards, including non-financial incentives such as recognition and career advancement opportunities can motivate employees to prioritize sustainability.

5.3 Risk management:

Incorporating climate risk management, scenario analysis and stress testing into the framework: There is a need to develop climate risk assessment methodologies and integrate them into the decision-making process.

5.4 ESG Reporting:

- **Expanding disclosure:** Financial institutions should ensure public disclosure of ESG strategies, Key Performance Indicators, and achievements, which is essential to strengthen trust in the sector, attract investors, and align with global sustainability standards.
- **Evaluating ESG performance:** The establishment of internal ESG performance evaluation systems is considered essential for financial institutions to monitor developments in the relevant area, effectively manage risks, and increase reporting.