International Journal of Law and Society
2024; 7(1): 30-38
http://www.sciencepublishinggroup.com/j/ijls
doi: 10.11648/ijls.20240701.15
ISSN: 2640-1894 (Print); ISSN: 2640-1908 (Online)

Analyzing Ethiopia Banking Sector Credit Policy Against Environmentally Sustainable Lending

Jemere Fufa

Legal Services, Commercial Bank of Ethiopia, Finfinne, Ethiopia

Email address:
jemerefufa780@gmail.com

To cite this article:
Jemere Fufa. (2024). Analyzing Ethiopia Banking Sector Credit Policy Against Environmentally Sustainable Lending. *International Journal of Law and Society*, *7*(1), 30-38. https://doi.org/10.11648/ijls.20240701.15

Received: December 12, 2023; **Accepted**: January 16, 2024; **Published**: February 1, 2024

Abstract: The very essence of this study is investigating Ethiopia Banks lending policy and regulations against environmental sustainability. The motivation behind this analysis is that environmental sustainability regulated under Ethiopia EIA proclamation, Ethiopia Investment proclamation and other national directives lacks adequacy to protect environmental sustainability. On top of this Ethiopia is signatory to many different global environmental treating and protocols, from Rio 1992 Earth Summit to COP 15 Paris climate change agreement. The question mainly addressed by the writer is that whether Ethiopian banks lending policy accommodate environmental sustainability in providing loan and the existence of policy at the national level that requires the financial sector of the country to promote environmental sustainable lending. This article will be significant in many ways. For instance, the currently available research works in the field of environmental protection integration in Ethiopia are not adequate. Thus, this article will fill the gap in the existing literature in the field and also it will be informative to the public and the government about the impacts of not integrating environmental protection in the credit activities of Ethiopia banks and what needs to be done in the future to make the integration more effective. This article revealed that there is no any visible policy law that mandate Ethiopia banks to integrate environmental sustainability in banks credit operations. Finally the writer recommended the Ethiopia Minister of Finance (MoF), National Bank of Ethiopia and Ethiopia Commercial Banks to enact Ethiopia environmental sustainable finance principle, environmental sustainable banking guideline, self regulatory environmental sustainable credit guideline respectively.

Keywords: Commercial Banks of Ethiopia, Environmental Sustainability, Credit policy, National Bank of Ethiopia, Climate Resilience Green Economy, Environmental Impact Assessment

1. Introduction

Environmental protection integrated banking sector, as a practice and policy concept, is growing globally. The driving force for this new banking business model is the increased demand from beneficiaries, as policy signals to achieve global sustainability agendas. [1] To date, the focus of these initiatives has largely been on the role of institutional investors and asset owners [1]. Growing global debt, diminishing quality, and competitive pressures can have important implications for promoting environmental protection in corporate finance. [2] On the one hand, environmental protection integration into lending (credit) activities may contribute to resilience in the financial sector. [2]

Global leaders have regularly underscored that private finance will be needed to achieve many global goals. [3] However, such goals do not appear to be fully reflected in many commercial and investment banking practices. For example, research by the European Central Bank has found that corporate lending is less likely to promote lower CO2 emissions.. [4] Until very recently, no widely recognised environmental and social standards existed for general corporate lending, although they represent the vast majority of banking finance activities. This changed in 2019 with the publication of the OECD Due Diligence for Responsible Corporate Lending and Securities Underwriting [5] and, separately, the UNEP FI Principles for Responsible Banking.. [6] Both standards provide frameworks for environmental sustainability risk management for lending transactions beyond project finance. However, as they have only recently been introduced, awareness and implementation of these standards are in their initial stages and many banks have only recently began incorporating Environmental, Social and Goverence (ESG) considerations into general corporate lending transactions. [6]

The African Development Bank Group has undertaken to promote economic development of its Regional Member Countries (RMCs) by financing development projects and programmes. [7] Traditionally, viability of its funded projects was mainly based on technical and economic criteria. Environmental soundness was considered as implicit in the technical and economic viability of these investment projects. [7] However, growing concerns about the environmental related financial risks and continued degradation of Africa's natural resources and the appearance of environmental issues at the top of the international political agenda, driven the Bank to adopt a more proactive stance in environmental management. [7] The Bank has indeed made considerable progress, over the years, in integrating environmental concerns into country programming and lending operations. [7] Since the publication of its environmental policy in 1990, the bank has produced a number of environmentally-orientated policy documents and guidelines, which give practical advice on implementation of the policies. These are considered important documents which guide staff, RMCs and the public on environmental issues within project design in order to achieve environmental sustainability. [7]

Unilateral implementation of environmental protection integration in financial sector regulations is a fast growing phenomena in recent years. For example, Mongolia launched its sustainable finance policy in December 2014. [7] As more countries adopt similar regulations, the list will keep expanding. Some notable countries which integrated environmental protection in their banking credit services are Bangladesh, Brazil, China, Colombia, Indonesia, Mongolia and Nigeria. [7] It should be noted that there are other countries in the process of developing their own banking environmental protection integration regulatory policies. Examples of these are Kenya, India, Turkey, the United Kingdom and South Africa.. [7] Given the scale and significance of this part of the sector, strengthening environmental protection integration in corporate lending practice will be necessary to meet global sustainability goals as well as enhance resiliency in the financial sector.

Ethiopia is signatory to many different global environmental treaties and protocols, from Rio 1992 Earth Summit to COP 15 Paris climate change agreement. But the Ethiopia banks still did not incorporated environmental protection in its credit business activity. Without integrating environmental sustainability in all sectors of developments it would be difficult to achieve environmental sustainability at the national. Thus, it is time regulating the banking sectors of the country to implement these international treaties and conventions as a bench mark to endorse and implement its credit activities. Furthermore, it needs banks to consider national legislatives in connection with environmental and social agendas in its business activities especially lending operation. It required the banking sector of the country to collaborate with other stakeholders to implement the sustainable development agenda and Climate Resilience Green Economy (CRGE) strategy of the country.

Ethiopia has signed many international agreements, from the Rio 1992 Earth Summit to COP 15 on the Paris climate change agreement. At the national level, it has been more than ten years since Ethiopia government launched the green Legacy. Ethiopia also implementing Sustainable Development Agenda and the Green Strategy for Green Economy (CRGE). [8] There is no strong and coherent functionality within the banking system that can effectively manage environmental sustainable lending policies. For example the National Bank of Ethiopia establishment proclamation [9] or national bank credit directive and other commercial banks credit policy and regulations did not set any environmental protection requirements in provisions of loans. [10]

In many jurisdictions, including Ethiopia, environmental consultants will prepare an EIA for the proponent (project owners). Because they are hired and paid by the proponent, consultants may be biased in favour of approving the project, believing that approval will lead to future work or other benefits.

Ethiopian environmental law requires projects likely to have negative impacts to undergo environmental assessment. [11] There are no objective criteria to determine the nature and degree of such impacts. On the other hand, projects that are not likely to have negative impacts do not require EIA. [11] The EIA Proclamation, issued in 2002, authorized the Environmental Protection Authority to issue a directive stating which projects might have negative impacts and thus require EIA. But there is no still directive issued by the Authority. Rather the Authority issued working manual which has no any authoritative power on the banking sector.. [12] Even the manual does not include any criteria for determining which projects require EIA, but instead simply lists twenty two types of projects that should be subject to EIA.

Ethiopia's Investment Proclamation does not make EIA arequirement for obtaining an investment permit, and in practice the Ethiopian Investment Authority grants investment permits without EIA as a requirement. [13] Investors who comes to banks for credit service, are not required to provide EIA. However, the EIA Proclamation imposes a duty on any licensing agency to ensure that the relevant environmental agency has authorized implementation of a project before issuing an investment permit. [11] The investment proclamation, on the other hand, only grants investment permits following the fulfillment of the requirements outlined from Art 10 up to art 13 of the proclamation and does not consider conducting an EIA as a requirement to obtain an investment license. [14] Aside from this, the investment application form does not expressly require the submission of an EIA or any other data pertaining to the prospective investment project's environmental impact.[15] We can see from a critical examination of the aforementioned debates that the investment proclamation and environmental regulations are incompatible with one another.

Having this problem, analyzing the adequacy of Ethiopian banks lending (credit) policies or regulations to promote environmental sustainable investment is imperative problem to be analyzed.

2. Concept of Environmentally Sustainable Banking

In order to ensure long-term corporate success, businesses must also support social and economic progress, a healthy environment, and a stable society. [7] The provision of financial resources and risk management tools to initiatives and businesses that advance or do not impair social justice, environmental protection, and economic development is known as sustainable finance. [7]

The phrase environmentally sustainable banking refers to banking methods that support environmentally friend internal procedures and environmentally friend external financing practices. [7] Sustainable banking is defined as the decision made by banks to only offer goods and services to clients who consider the social and environmental effects of their activities, with the goal of enhancing customer satisfaction and the economy as a whole without having a negative effect on people or the environment. [7] Environmentally sustainable banking is a type of banking activity in which banks take the initiative to carry out their everyday operations as diligent members of society by taking internal and external environmental sustainability into consideration. [7] The banks that engage in such initiatives are known as social responsible, environmental friend or ethical banks. [7] It means supporting eco-friendly methods and lowering the carbon impact of banking operations.. [16] Green banking (environmentally sustainable banking) is about going above and above to maintain the earth livable without causing any serious harm. [16] Ethical banking is another name for green banking, which takes into account all social and environmental factors. [16] Environmentally sustainable banking refers to environmentally friend or eco-friend banking to stop environmental damage and improve the habitability of this world.

Thus, environmentally sustainable banking entails a two-fold strategy. [16] First, Green transformation of all banks' internal processes is the emphasis of environmental sustainable banking. [16] This means that in order to reduce the carbon footprint, all banks should adopt proper strategies by implementing renewable energy and other measures. Second, all banks should use environmentally conscious finance, taking into account the environmental risks of projects before making financing decisions, and supporting and encouraging the expansion of new green initiative projects in particular. [17]

The banking industry is currently under intense pressure from many shareholders to conduct its credit business in a manner that is environmentally sustainable. The foundation of the United Nations Environment Programme Finance Initiatives (UNEPFI) in 1990 was one of many initiatives to carry out sustainable banking credit activity around the world. According to the United Nations Environment Programme - Finance Initiative's definition of sustainable banking is (UNEP-FI, 2007), the process by which the banks consider the impact of their various business activities and their products and services for meeting the needs of the current as well as the future generations. [17]

3. The Driving Forces to Integrate Environmental Sustainability in Bank Lending

For banks to integrate environmental sustainability in its banking operation there is driving factors. First, banks started to manage risks and to capitalize on opportunities. These factors were the main drivers for the integration of sustainable banking and E&S practices in the banking sector as they tended to strengthen banks' capacity to rely on long-term benefits rather than focus on short to medium-term gains. The conventional financial sector takes sustainability considerations into account because it is demanded business, because regulators prescribe it, because of personal attitudes of leaders or because of the demand of clients. [18] Global governments and organizations have not been the only ones to respond to sustainability challenges. In banks, reactions are now occurring. They have also reportedly started to support the shift to a more sustainable economy by incorporating sustainability factors into their risk management models and governance frameworks. [18] Secondly, Social pressure and expectations from civil society are growing rapidly on the banking sector to take environmental and social concerns into account. For instance, as part of protests against the construction of the Dakota access Line (DL) in the United States, several campaigns targeting banks that provided financial support to the project were launched, asking their clients to close their accounts. [19] International instruments, such as the UN Guiding Principles, Guidelines for Multinational Enterprises Principles for Business and Human Rights also recognize that businesses, including banks, should prevent and minimize any negative effects on society and the environment that may result from their operations. [20]

Bearing this in mind, it can be safely said that it was the contribution of all these factors that motivated regulators to integrate sustainability issues into financial regulations. [19] The development of new business opportunities was considered by financial institutions in Brazil, Colombia, and Peru as one of the most significant drivers for incorporating sustainability considerations into financial regulations. [20] Access to capital from investors or foreign financial organizations was deemed to be of the paramount importance in Nigeria. The main sources of funding for Nigerian banks are financial capital injections from foreign financial institutions like the FMO (Dutch Entrepreneurial Development Bank), the IFC (International Financial

Corporation), or other organizations [20] However, external financial institutions want to make sure that their investments are made in accordance with certain sustainability concepts and have established sustainability criteria. [20] As a result; Nigerian banks endeavored to create procedures and policies that satisfy these requirements. [20]

In Bangladesh, in addition to the impact of the IFC, the relative absence of environmental regulations for polluting industries and their enforcement was a reason to focus on the financial sector as an environmental regulator, and to create incentives to support environmental-friendly practices. [20] The situation was similar in China, where environmental pollution has a significant impact on the environment and health. Consequently, financial mechanisms were applied to support non-polluting industries and penalize polluting industries. [20] Thus, based on this analysis, the following drivers help to explain integrating sustainability aspects into financial regulations that overlap in some countries.

In China, Brazil and Bangladesh the main driver to integrate, environmental issues are social pressure and environmental pollution which is considered as internal pressure. [20] The policy makers in emerging economies have a different view toward the financial sector than developed countries. Specifically, developed countries may view the financial sector as an intermediary in determining efficient allocations of capital, whereas developing countries may view the sector as a source of governance that justifies a more activist-policy approach with regard to sustainable development. [20] It was external pressure from financial aid institutions such as the FMO and the IFC for countries like Nigeria, Bangladesh, Mongolia and Indonesia. [20] No such pressure exists for developed economies, which already have established robust environmental regulatory systems. Political and economic pressure from regional neighbors is considered as another driver for banks to consider environmental sustainability for countries like Colombia and Peru. [20] Since Brazil, the most powerful economy in South America, has adopted sustainable finance regulations, other neighboring countries may feel pressure or see the opportunity to go a similar route. [20] This may support economic relations with the neighboring country that has implemented guidelines, as well as foster a more sustainable financial industry. [20] The regulators contend that addressing sustainability issues boosts the banking sector's positive influence on sustainable development and that integration boosts the sector's financial stability and financial performance.

4. Analysis of Relevant Ethiopia Laws Against Environmental Sustainability in Bank Lending

4.1. Analysis of Ethiopia Environmental Impact Assessment Law in Promoting Environmental Sustainability in Ethiopia Bank Lending Activities

Firstly, despite the EIA Proclamation's inclusion of specific provisions pertaining to EIA, a careful study of these provisions demonstrates that they are insufficient to support Ethiopia's EIA system's performance. On the other hand, the EIA Proclamation's inadequacy is brought on by some of its significant gaps and its generality. In other words; some of the Proclamation's provisions are too broad to be applied without the aid of other legal documents. Similar to this, for the Proclamation to be properly executed, there are gaps that must be filled by issuing subsidiary documents. First the Proclamation does not explicitly state which actions are subject to EIA, rather it states that these actions should be determined by the directives to be issued by FEPA. This demonstrates that, in the absence of these directives, no one will be legally required to conduct an EIA because a proponent cannot know which action is subject to EIA and which is not. [21]

The aforementioned instances highlight how insufficient the EIA Proclamation's provisions are by itself to ensure the effectiveness of the EIA system. The EIA Proclamation is in fact more like a skeleton than a fleshy document. As a result, other, more particular subsidiary instruments must be issued in order for it to be implemented effectively. On the other hand, the FDRE Parliament has given the Council of Ministers power to adopt rules required for the Proclamation's successful execution because it is aware of both the generality of its provisions and the gaps they include. But though the EIA Proclamation's shortcomings (generality and gaps) are obvious and it is plain that regulations are necessary for the Proclamation to be implemented effectively. This indicates that no proponent can now be legally obligated to do an EIA because the EIA Proclamation requires proponents to conduct EIA in line with FEPA directives even if those directives have not yet been issued.

The analysis demonstrates unequivocally that there is a significant disconnect between theory and actual EIA process implementation and application in Ethiopia. Therefore, it is imperative for Ethiopia banking sector to have strong policy and regulations that promote environmental sustainability of banks lending.

4.2. Analysis of Environmental Sustainability Under Ethiopia Investment Law

Before engaging in investment operations, investors must comply with a number of conditions set forth by environmental legislation. Investors cannot begin implementing investment activities without first obtaining approval from the relevant federal or regional environmental authorities. [22] As a result, the investor or proponents must complete EIA and afterwards present an environmental clearance certificate (ECC). [22] In addition to this, if an unanticipated fact with significant implications is discovered after the filing of an environmental impact study report, the proponent of the investment is required to update or do the EIA. [22] In addition to this, the proclamation imposes penalties on investors who started their investing activity without first conducting an EIA. Any person who, without authorization from the Authority or the relevant regional environmental agency, or makes false presentations in an environmental impact assessment study report commits an offense and shall be subject to a fine of not less than fifty thousand birr and not more than one hundred thousand birr. [22] The clause also required the licensing authority to wait until the Authority or the appropriate regional environmental agency has approved the project's implementation before issuing an investment permit or a trade or operating license for any project. [22]

Conversely, the investment permit is covered under Part 4 of Investment Proclamation No. 1180/2020. The proclamation's article 10 deals with the granting of licenses or permits for investments. The investor will therefore receive an investment license following the completion of the requirements outlined in this section of the proclamation. Additionally, the appropriate investment body must consider the anticipated investment activity in light of the investment proclamation, regulations, and directives before granting permission. A completed application form must be submitted to the investment authorities in accordance with the Investment Proclamation (Proclamation No. 1180/2020) in order to get an investment permit. The application form requests information about the applicant's status, the type of intended investment activity, the amount of investment capital, the investment area (restricted to a region), the nature and scope of the intended production or service, and the anticipated number of jobs the investment will support. [23] Aside from this, the application form does not call for the submission of an EIA or any other data pertaining to the prospective investment project's environmental impact.

The grounds for suspending and revoking investment licenses are laid out in the Investment Proclamation. If an investor obtained their investment permit dishonestly or by providing false information, transferred it to a third party without permission from the investment authority, neglected to renew their permit on time, misappropriated or illegally transferred incentives to third parties, or engaged in commercial activity without obtaining a business license, their investment license may be suspended or revoked. [24] The Investment Proclamation makes it clear that starting a project involving investments without first getting EIA approval is not a reason for license suspension or revocation.

Aside from this, the investment application form does not expressly require the submission of an EIA or any other data pertaining to the prospective investment project's environmental impact. We can see from a critical examination of the aforementioned debates that the investment proclamation and environmental regulations are incompatible with one another. Because the countries environmental laws, on the one hand, mandate conducting an EIA before beginning any investment activity and obtaining permission from the relevant federal and environmental institution.

The investment proclamation, on the other hand, only grants investment permits following the fulfillment of the requirements outlined in this section of the proclamation and does not consider conducting an EIA as a requirement to obtain an investment license. [24] Thus, it is crucial to harmonize these two rules. Even by applying the rule of interpretation, we are unable to reconcile them. Therefore, amendment may be the best solution to bring them together. As a result, the lawmaker should include the need for an EIA as a prerequisite in the investment proclamation in order to obtain an investment license.

The proclamation instructs the licensing agencies, as it is indicated in the preceding sentence, to withhold issuing licenses to anyone for any project that is subject to an EIA until an ECC (environmental clearance certificate) has been generated from the appropriate environmental organs. While some licensing authorities do demand ECC, there are also licensing bodies that do not or just rarely require it. Some licensing organizations that do not require ECC contend that subsequent laws, particularly the Investment Proclamation No. 1180/2020, relieve them of their obligation to comply with the EIA Proclamation. [24] It is accurate to say that an ECC is not a requirement for obtaining an investment permit under the Investment Proclamation No. 1180/2020. Even though they are aware of the region(s) they will invest in, some investors may not be aware of the locations of their investments when they apply for permits. So, requiring them to conduct an EIA before they choose their investment sites won't be suitable. [24]

In such gaps in the Ethiopia investment law regarding EIA it is better to have environmental sustainability policy and regulations in the banking industry to achieve all round environmental sustainable development.

4.3. Analysis of Environmental Sustainability Under Ethiopia BITs

Environment-related provisions found in bilateral investment agreements are not monotonic and inserted either in the treaty's preamble or substantive provisions. Accordingly, the treaty's preambular part may recognize environmental protection and conservation as one of the treaty’s objectives. [25] BIT’s may also contain environmental references under its substantive provisions placing States under a continuing obligation to uphold environmental standards and not to worse environmental standards and regulations to attract foreign investments. Investment treaties may also incorporate under its substantive provision environmental exception clauses-that seeks to reserve policy space to regulate environmental matters. From other countries’ practices, there is evidence suggesting that BITs can and do contain provisions aimed at facilitating environmental damage caused by FDI projects, both in the preamble and the substantive provision.

However, with few exceptions, most BITs to which Ethiopia is a party has significant drawbacks concerning the environmental concern and portray features of old-generation investment treaties. It is because the treaties did not have environmental clauses and failed to grant contracting states with regulatory power for environmental protection. Accordingly, investment treaties signed with countries sending investment to Ethiopia such as Ethiopia-China, Italy-Ethiopia, UK-Ethiopia, Turkey-Ethiopia, Ethiopia-

Netherlands, Ethiopia Sudan BITs didn't incorporate environmental provisions. [26] Technically speaking, failures to incorporate environmental clauses have a negative effect on both contracting states.

However, pragmatically, Ethiopia will be most affected by this treaty since investment inflow to Ethiopia prevails the investment outflow to other contracting states. So, this leads Ethiopia to expensive international arbitrations claiming compensation than other contracting states. So, fearing this arbitration, an environmental measure that might be taken may be minimal, and this will, in turn, finally pose a risk of environmental pollution. Even among those BITs that incorporate environmental clause except the 2006 Ethiopia-Finland BIT [26], the remaining treaties have not yet entered into force. All this indicates they are contrary to the country's goal and policy of achieving sustainable investment.

Further, it is an infringement of the Constitution of FDRE, which imposes the duty on the government to make sure that the international treaties that Ethiopia signs guarantee sustainable development. [27] One of the reasons for having such weak BITs in terms of environmental protection is the absence of a model investment treaty. Having such weak environmental clause in BITs of ethiopia, it is sound reason Ethiopia required to integrate environmental sustainability in its lending policy and regulation.

4.4. Analysis of Environmental Sustainability Under Ethiopia Banks' Lending Policy

There is no strong and coherent function inside the banking sector Ethiopia that can effectively manage environmental and social policies with a good track record of regular banks. For instance, the national bank of Ethiopia's establishment proclamation, [28] the national bank's credit directive, and other commercial banks' credit policies and regulations did not impose any environmental protection standards in loan provisions. [28] This new business model is not integrated into Ethiopia banking system that ensures the bank to makes a profit by promoting responsible social and environmental behavior by working closely with individuals or companies who borrow money from the bank and invest or expand the existing businesses.

But there is an attempt in development banks of Ethiopia in integrating environmental sustainability and social policy in its credit policy. Based on the responsibilities and powers granted to it by Public Enterprises Proclamation No. 25 of 1992 and the Public Financial Enterprises Agency Council of Ministers Regulation No. 98/2004, the Development Bank of Ethiopia's board of management issued the credit policy. [29] The Bank is offering investment loans to borrowers and projects that have undergone a comprehensive evaluation and been determined to be socially, economically, and fiscally viable. [29] This means that for a project to be funded by the Development Bank of Ethiopia, it must not jeopardize societal interests. The bank is responsible for determining whether the project would be beneficial to society. Even if is not well organized fully implemented in terms environmental expert with in the bank, it is a good beginning for the country's banking sector to incorporate environmental sustainability in the credit operations of the banks. Even if the Ethiopia development bank incorporated environmental sustainability in its credit policy there is no a policy for Ethiopia development bank to reviews and strengthens post-loan management.

Apart from DBE, there is no any visible policy in the national banks of Ethiopia or others commercial banks regarding environmental sustainability in banks credit operations. If we look at the Ethiopia National Bank risk management guideline in relation to its credit operation it is the integrity, reputation, and legal ability to assume the liability is taking into account before entering into any new credit relationship with debtors. [30] As a result, before beginning any new credit connection, a bank needs to become familiar with the borrower or counterparty and be certain that it is doing business with someone or something of good standing and creditworthiness. [30] This guideline seriously avoids affiliation with anyone engaged in illegal activity. [30] Depending on the type of credit exposure and the nature of the credit relationship with the counterparty, the factors to be considered and documented in credit granting include, purpose of the credit and sources of repayment, borrower's repayment history and current capacity to repay, based on historical financial trends and future cash flow projections under various scenarios, terms and conditions of the credit including covenants designed to limit changes in the future risk profile of the borrower, adequacy and enforceability of collateral or guarantees under various scenarios, current risk profile of the counterparty (including the nature and aggregate amounts of risk), and sensitivity to economic and market developments, especially for major exposures; and borrower's business expertise and management capability. [30] Thus, this guideline gives only attention for borrower's repayment history and current capacity to repay the current debt and adequacy and enforceability of the collateral to repay back the loan if the borrower in default without giving any environmental sustainability consideration of the project or business financed by the bank.

In addition to this, looking through the check list of credit request document of certain commercial banks of Ethiopia like CBE, Abssiniya Bank, Awash Bank, Dashen Bank, Oromica cooperative bank, Wegagen Bank and Oromia International Bank practically shows that there is no a requirement that demand the borrower to come up with EIA certificate to be granted loan from the bank. [1] Simply they are implementing the National Banks of Ethiopia bank risk management guideline which has no place EIA as criteria for loan provision.

Due to the absence of green economic development regulations in the present credit-granting legislation in Ethiopia, credit institutions are free to reject business investment projects that adhere to the green economic development standards. Besides, business investment projects on demand of green growth require significant investment capital, slow

1 *See credit request check list of governmet and private commercial banks.*

capital recovery time, higher content of science and technology in green financial products. Therefore, credit institutions still focus on finding business investment projects with fast capital turnover and guaranteed capital recovery.

The banking sector in Ethiopia as a policy needs to have a comprehensive environmental sustainability covenants that urges its clients to improve social and environmental risk management. Even to have a comparable environmental sustainable policy, there must be policy that requires clients who pose significant environmental and social risks, to submit environmental and social risk reports and pledging their willingness to be under the lender's supervision. The writer urges Ethiopian banking institutions to have a policy or regulations that reviews and strengthens post-loan management, similar to what other nations like China and Bangladesh are doing. Actions for post-loan management that are pertinent and appropriate must be established and put into place for clients who pose potential major environmental and social hazards. They must set up and enhance an internal reporting and accountability system for the key social and environmental risks that their client's face. The Ethiopia Banking institutions should have periodically plan and conduct internal auditing on green credit as well as include the implementation of green credit in the scope of internal compliance evaluation.

5. Why Ethiopia Should Integrate Environmental Sustainability in Its Banking Credit Business Activity

Firstly, Ethiopia banks provided loans despite their actual knowledge or constructive knowledge that borrowers are financing for polluting projects. Actual knowledge refers to the existence of direct evidence that banks are aware that a specific act pollutes the environment. Constructive knowledge is a presumption that banks should be aware of environmental pollution caused by companies according to the universal cognitive abilities of average people. [30]

Secondly, by their new business model which is recently introduced in Ethiopia which is named Interst free Banking. [31] Under interst free banking activities in Ethiopia there is a possibilities of banks invests with client to establish and developes the company to share profit or loss if any. For example Musharak Finance. The word Musharaka literally means sharing. According to Islamic law, a musharaka is a joint partnership in which two or more people pool their resources, such as money or labor, to start a business. The profit is divided among the partners in accordance with a predetermined ratio, while the loss is distributed in accordance with the contribution ratio. [32] With an influence so significant as to dominate an investment project that has caused environmental pollution, banks are highly accountable for such pollution and shall assume environmental legal liabilities.

Thirdly, Ethiopia is signatory to many different global environmental treating and protocols, from Rio 1992 Earth Summit to COP 15 Paris climate change agreement. To achieve such national commitment all stakeholders including the banking sector should integrate environmental sustainability in their business activities.

Fourthly, there is no law and regulation in Ethiopia to protect the environment without the involvements of banks. Environmental impact assessments (EIA) must be carried out on investment projects in order to determine any potential effects to the environment. In cases where the EIA shows potential impacts to the environment, appropriate steps should be made to prevent or mitigate that harm. But when we see the effectiveness Ethiopia environmental impact assessment proclamation there is a gap. Mainly the Proclamation does not explicitly state which actions are subject to EIA; rather, it states that these actions should be determined by the directives to be issued by FEPA. This demonstrates that, in the absence of these directives, no one will be legally required to conduct an EIA because a proponent cannot know which action is subject to EIA and which is not. [21]

Fifthly, International lending institutions like banks and bilateral aid organizations now demand environmental impact assessments before making loans. [33] Borrowing countries must abide by this EIA Directive because it was made a condition for all of the World Bank's investment projects by an operational directive it published in 1989. In June 1985, the European Community Council also passed Directive 85/337, requiring EIA for projects that are being considered. Due to the demands of the World Bank and other development banks and donors, as well as capacity building initiatives started after the Rio Declaration, developing countries began to adopt environmental impact assessments.

6. Conclusion

Apart from Development Bank of Ethiopia, there is no any visible policy in the national banks of Ethiopia or others commercial banks regarding environmental sustainability in banks credit operations. Carefully examining Ethiopia's banking business proclamation show that there is no a single phrase that encourages banks to incorporate environmental sustainability into their banking lending business activities. This proclamation's preamble states that banks play a significant role in economic development through the mobilization of funds from inside and outside the country and the channeling of those funds to various sectors of the economy. We can infer from this preamble that the bank finances nearly every economic sector in order to highlight the economic development of the nation without paying adequate attention to the environmental sustainability of the projects funded. It can be a full meaning of the proclamation that environmental protection is not the banks' line of business, as long as the creditor's business activities are profitable enough to pay back the loan. The national bank of Ethiopia's credit directive is more concerned with the loan repayment and loan classification than with the inclusion of environmental protection in loan provisions. The Ethiopia

National Bank Risk Management Guideline, gives only attention for borrower's repayment history and current capacity to repay the current debt and adequacy and enforceability of the collateral to repay back the loan if the borrower in default without giving any environmental sustainability consideration of the project or business financed by the bank.

7. Recommendations

Based on the analysis and the conclusions drawn above, the author recommends the following points that he deems will contribute in directing Ethiopia banks to integrate environmental sustainability in their credit business activities.

1) The Ethiopia Minister of Finance (MoF) should establish the Ethiopia Sustainable Finance Principles and Sector Guidelines, which provide a framework to help local banks to integrate environmental considerations into lending decisions.
2) The National Banks of Ethiopia should establish environmental sustainable credit guidelines as a policy that urge lending institutions to integrate Environmental Sustainability (green credit) in order to serve the real economy.
3) The boards of directors of each commercial banks should develop a broad environmental policy which has details of auditing procedures, reporting formats, and checklists including post loan periods.
4) Commercial banks should establish a separate Green Banking department that lead by senior executive who will be in charge of planning, analyzing, and managing the bank's associated green banking concerns.
5) The Ethiopia Bankers Association should enact self-regulatory a guideline that promote environmental sustainable bank credit activity and should committed to the guideline to enhance the environmental policy of the country.

ORCID

0009-0002-3959-9155

Conflicts of Interest

The Author declares no conflicts of interest.

References

[1] OECD, *ESG practices and policy for institutional investors,* (2019) available from https://www.oecd-ilibrary.org/sites/d5c54bd6-en/index.html?itemId=/content/component/d5c54bd6-en#chapter-d1e8145 [Accessed 12 June 2022]

[2] OECD, *Promoting responsible lending in the banking sector: -The next frontier for sustainable finance (2019*) available from https://www.oecd-ilibrary.org/sites/d5c54bd6-en/index.html?itemId=/content/component/d5c54bd6-en [Accessed 12 June 2022].

[3] United Nations, Paris Agreement, (2015) available from https://unfccc.int/sites/default/files/english_paris_agreement.pdf [Accessed 16 May 2022].

[4] Ralph De Haas, Alexander Popov, Finance and Carbon Emission, working paper series number 2318/2019 European Centeral Bank, at, 9 (2019) available from https://www.ecb.europa.eu/pub/pdf/scpwps/ecb.wp2318~44719344e8.en.pdf

[5] OECD, Due diligence for Responsible corporate lending and under writing:-Key considerations for banks implementing the OECD guidelines for multinational enterprises (2019) available from https://www.oecd.org/investment/due-diligence-for-responsible-corporate-lending-and-securities-underwriting.htm [Accessed 12 June 2022].

[6] UNEP-FI, Principle for responsible banking, (2019), available from https://wedocs.unep.org/20.500.11822/32227 [Accessed 4 May 2022].

[7] Africa Development Bank Goup's, Environmental policy, (2004) p 8 available from https://www.afdb.org/fileadmin/uploads/afdb/Documents/Policy-Documents/10000027-EN-BANK-GROUP-POLICY-ON-THE-ENVIRONMENT.PDF

[8] FDRE, *Climate resilencegreen economy strategy* (2011) https://www.preventionweb.net/files/61504_ethiopiacrge.pdf [Accessed 12 June 2022].

[9] *Ethiopia banking business proclamation, Number 592/2008.*

[10] *Ethiopia National Bank Directive Number SBB/69/2018.*

[11] Environmental Impact Assessment Proclamation number 299/2002.

[12] Ethiopia environmental impact assessment guideline (2000).

[13] Investment Proc. No. 1180/2020, FEDERAL NEGARIT GAZETA.

[14] Investment Proc. No. 1180/2020.

[15] EIC Application Form for New Investment Permit http://admin.theiguides.org/Media/Documents/Investment%20Permit%20Application%20Form.pdf [Accessed 19 July 2022].

[16] Md. Shafiqul Islam, Prahallad Chandra Da, *Green Banking practices in Bangladesh*, 8 IOSR Journal of Business and Management (IOSR-JBM) 39-44, Bangladesh, Kazi Nazru Islam University (2013) pp 39 available from http://iosrjournals.org/iosr-jbm/papers/Vol8-issue3/G0833944.pdf

[17] Kanak Tara, Saumya Singh and Ritesh Kumar, *Green Banking for Environmental Management: A ParadigmShift, 10(3) Current World Environment, 1029-1038, India* (2015) pp, 1030 available from https://www.researchgate.net/publication/288857355_Green_Banking_for_Environmental_Management_A_Paradigm_Shift

[18] Adeboye Oyegunle and Olaf Webber, *Developmenet of sustainability and green banking regulations — Existing codes and practices CIGI papers no. 65* Waterloo, Otario (2015), pp 8 available from https://www.cigionline.org/publications/development-sustainability-and-green-banking-regulations-existing-codes-and-practices

[19] Carla F. Frederick, Mark Meaney, Nicholas Pelosi and Kate R. Finn, Social cost and material loss: The Dakota acess pipeline (2018) available from https://www.colorado.edu/program/fpw/content/social-costs-and-material-loss [Accessed 12 June 2022].

[20] OECD Guidelenes for multinational enterprises 2011 edition, -34(2011 edition) available from https://www.oecd.org/daf/inv/mne/oecdguidelinesformultinationalenterprises.htm [Accessed 12 June 2022].

[21] Dejene Girma, *Environmental impact Assessment in Ethiopia: law and practice*, un published (2012) available from https://www.academia.edu/10278336/ENVIRONMENTAL_IMPACT_ASSESSMENT_IN_ETHIOPIA_LAWS_AND_PRACTICES [Accessed 16 May 2022].

[22] Ethiopia Environmental Impact Assessment, proclamation No. 299/2002.

[23] Ethiopia Investment Commission Application Form for New Investment Permit available from http://admin.theiguides.org/Media/Documents/Investment%20Permit%20Application%20Form.pdf [Accessed 19 July 2022].

[24] Ethiopia investment proclamation number 1180/20220.

[25] Hailu Abebe Endale, *The Implications of Bilateral Investment Treaties on Environmental Protection in Ethiopia: The Law and the Practice* un published Addis Abeba University, school of law, (2020) p 48-49 available at https://www.degruyter.com/document/doi/10.1515/gj-2020-0067/html?lang=en

[26] https://investmentpolicy.unctad.org/international-investment-agreements/countries/67/ethiopia

[27] FDRE constitution, (1995).

[28] National Bank of Ethiopia, *Bank Risk Management Guidelines* (Revised), 2010 available at https://nbebank.com/wp-content/uploads/2019/04/Rm-Guideline-revised-1.pdf

[29] Development Bank of Ethiopia, Credit Policy, September, 29, 2009.

[30] UNEP, *Establishing China's Green Financial System: Establishing the Legal Liabilities of Financial Institutions*: Detail recommendations 13, (2014) available at https://www.cbd.int/financial/privatesector/china-ecgfs-13Lender%20Liability.pdf [Accessed 17 June 2022].

[31] Ethiopia Banking amendment proclamation number 1159/2019.

[32] Hussain G. Rammal, Financing Through Musharaka: Principles and Application, p 3(2004) avaliable at https://www.researchgate.net/publication/256002438_Financing_Through_Musharaka_Principles_and_Application [Accessed 16 Aug 2022].

[33] Pacifica F. Achieng Ogola, Environmental impact assassement general procedures p, 3 (2007) available at https://orkustofnun.is/gogn/unu-gtp-sc/UNU-GTP-SC-05-28.pdf