ÓBUDA UNIVERSITY

Keleti Károly Faculty of Economics
Institute of Management and Organisation

# DEGREE PROJECT

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**2023** Student's registration number: **T007619/FI12904/G**

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## THESIS ASSIGNMENT

**Student's surname, forename (s):** Aizhan Nassir
**Thesis number:** [redacted]
**Registration number:** T007609/FI12904/G **Neptun code:** [redacted]

**Branch of study:** Technical Management
**Specialization:** Corporate Strategy
Electrical Engineering

**Thesis title:** Investigating the sustainability of Kazakhstan's economy
**Task description:**
1. Introduce the Kazakh economy!
2. What does the literature say about the sustainability of investigation? Describe!
3. State your research questions!
4. Analyse your results!
5. Draw your conclusions!

**Institutional consultant's name:** Dr. Gábor Géza Gyarmati

**The limitation period of the theme issued:** 15.05.2024.
**Deadline for submission of Thesis:** 15.12.2023.

The thesis is: Not secreted.

Issued: Budapest, 12.12.2023.

Óbudai Egyetem Keleti Károly Gazdasági Kar Vállalkozásfejlesztés és Infokommunikációs Intézet 1. Budapest

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Director of Institute

The Thesis is suitable for submission:

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Institutional consultant

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External consultant

# STUDENT'S DECLARATION

I the undersigned student named Aizhan Nassir (Neptun code: [redacted]) hereby declare that the degree project is the result of my own work; I referred to the special literature and the means used inan identifiable manner. The results included in the degree projectcompleted are allowed to be used by the university and the institution announcing the task for their own purposes free of charge, subject to any restrictions on classification as confidential.

Budapest, 15 December 2023

student's signature

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## 1. INTRODUCTION

When we talk about programs, projects, and activities that are meant to preserve a certain resource, we're talking about sustainability. As the four pillars of sustainability, it truly refers to four different domains :human, social, economic, and environmental.(Lorek, 2014)

The ability of the state's economic system to withstand, adjust to, and recover from adverse external effects determines the stability of the country's economy. In the context of the temporal and geographical volatility of the contemporary global economy, the issue of enhancing the stability of the domestic economy has taken on particular scientific and practical importance. The state's ability to guarantee steady economic growth and social development is weakened by the low degree of stability of the national economy.

In 2019, Kazakhstan submitted it’s first Voluntary National Review (VNR), reaffirming it’s commitment to the SDG (Sustainable Development Goals) model for progress and identifying key areas for improvement, especially in logistics and budgeting. More importantly, Kazakhstan has been a part of Global ESG(Environmental, Social, Governance)-transformation, as well as supporting 17 Goals of Sustainability.

The substantial lending to environmentally unfriendly sectors in Kazakhstan highlights the urgent need to address additional credit risks linked to achieving net zero emissions. Effectively managing these risks and incorporating them into credit pricing is crucial. Presently, commercial banks often overlook environmental risks in their loan cost calculations, even though their magnitude could be assessed based on current trends in greenhouse gas emissions across various sectors of the national economy.

Integrating mandatory climate change considerations into risk assessment models for commercial banks, conducting climate stress tests to enhance capital adequacy, and reducing borrowing costs for environmentally conscious "green" companies through differentiated interest rates to support green investments will enhance the resilience of the National Bank of the Republic of Kazakhstan, contributing to a more robust national economy and financial system.

In conjunction with the development of "green" banking, the efficient allocation and mobilization of capital within the national financial system pose significant challenges. (Barua,2020) In this context, national regulators should focus on creating conditions that prevent "greenwashing"—the unjustified portrayal of a company, product, or service as environmentally friendly in the market. Measures should also be taken to avoid the formation of "green bubbles," arising from excessive investments in renewable energy sources that are inconsistent with the debt capacities of companies involved in clean technologies.

Modern foreign economic science has significant developments regarding the criteria, subsystems and factors of national sustainability, including the sustainability of the national economy. Such developments are reflected in the publications of experts from the World Economic Forum (Global Risks, 2013),the Organization for Economic Cooperation and Development (OECD,2016), the Institute for Public Policy Research (IPPR NORS,2014).

Despite the significant theoretical groundwork of domestic and foreign scientists, the problem of increasing the level of stability of the national economy to ensure the economic security of the state in the context of the permanent occurrence of crises at the global and local levels, the rapid transmission of negative external impulses to the national economy needs further scientific research.

The purpose of the thesis work is to study the features and specifics of sustainability in terms of a country at the current stage of development, as well as to develop recommendations for implementation. In addition, an important part will be the systematization and deepening of theoretical and practical knowledge in the field of implementing ESG principles and their application in solving specific problems, as well as evaluating efficiency. The study of the Kazakhstan market of ESG-banking is also crucial. To achieve the goals of the thesis work, it is necessary to solve a number of tasks:

- To study and systematize knowledge and practical experience in the implementation of ESG principles at enterprises in Kazakhstan;
- To study the most common problems in the development and implementation of ESG principles in Kazakhstan enterprises and determine ways to effectively solve them;
- To study the sustainability reports of MFB Zrt. and Halyk Bank;
- To create recommendations for the implementation of ESG-banking in Kazakhstan and Hungary on the example of MFB Zrt. and Halyk Bank.

Currently, more and more banks in Kazakhstan are interested in implementing ESG rankings. For such enterprises, the systematic review and conclusions based on the research in this final thesis will be of great help. The object of study of the thesis work is an enterprise evaluation of an implementation ESG in different countries, by that improving the given system in Kazakhstan .The subject of research of the final qualifying work is comparative qualitative analysis of the implementation process.

The entire theoretical part of the work is based on the materials of professional practitioners and scientists in the field of ESG. A significant number of authoritative sources were used to justify the use of any of the models or the presentation of any thesis. The work is complemented by thoughtful and structured conclusions. When developing the final qualifying work, the following were used:

– In-depth investigation (specialist interview);
– Financial documentation, Internal reporting (balance sheet, income statements);
– Results of internal corporate reporting (sustainability reports);
– Statistics data and so on.

The final qualifying work consists of an introduction, three chapters and a conclusion. The first chapter describes the theoretical background necessary to understand the principles and foundations of sustainability. The second one provides an overview of the Kazakhstan market and observations of the ESG-banking and identification of problems of the investment process. The third chapter directly evaluates the effectiveness, develops implementation measures and recommendations. In summary, the main conclusions for all three chapters of the work are given. The purpose of the study is to further study the implementation of ESG in financial institutions in order to respectively boost the country’s economic sustainability.

## 2. SUSTAINABILITY: CONCEPTS, METHODOLOGY, IMPLEMENTATION

### 2.1. Ways of evaluating sustainability

In general, it should be noted that the more stable the ratio of production and financial and banking capital in the country, the more stable the national economy, based on OECD (2020). Consequently, the assessment of its safety will be quite high. Violation of proportions and connections between various elements of the economic system leads to its destabilization and acts as a signal of the transition of the economy from a safe state to a dangerous one. The generalization of scientific approaches disclosed in the economic literature makes it possible to single out the following characteristics of a sustainable economy:

- diversity and diversification of industries and spheres of the national economy, the economic system resistant to negative external influences includes a large number of entities that occupy various market niches and use different development strategies;
- the interdependence of financial institutions and organizations in the economic system, which determines the pace and extent of the spread of crises.

The stability of the national economy is ensured by the presence of macroeconomic, regulatory, legal, organizational and institutional conditions as necessary circumstances that determine the ability of the national economic system to withstand internal and external "loads", adapt to them and recover from them. With another article for example Briguglio (2016) said that to counteract negative external impacts on the economy and reduce their consequences, the following goals and objectives of state policy in the field of ensuring the sustainability of the national economy are distinguished: macroeconomic stability, efficiency of the domestic market and public administration, social development .(Bagley,2012)

Macroeconomic stability should be considered from the standpoint of the Keynesian theory of macroeconomic equilibrium. If the total spending in the economy, that is, the planned spending of macroeconomic entities, changes evenly with the actual spending of the business sector, then in accordance with the Keynesian input-output model, the economy will be characterized by an internal balance, low inflation and unemployment close to natural, as well as positive balance of payments.

Efficiency of the internal market. Economics studies markets and their functioning through the price mechanism as an efficient way of allocating resources in an economy. In the book Bagley (2012) it is stated that in conditions of effective market self-regulation, the consequences of negative external influences on the economy are absorbed by the appropriate adjustment. If market imbalances are characterized by a tendency to persist, then resources are not distributed efficiently in the economy and there is an outflow of financial and human capital, there is a shortage in commodity markets.

Social development, as a qualitative change in society, which leads to the emergence of new social relations and institutions (norms and rules of conduct) is another of the key conditions for ensuring the stability of the state's economic system. Developed social relations contribute to the growth of the efficiency of the functioning of the economic mechanism without the threat of social upheavals. Social cohesion reflects the level of development of social dialogue in society, as well as general approaches to determining public policy measures in the field of ensuring the sustainability of the national economy to negative external influences (Briguglio, 2006).

According to international practice, the conditions for ensuring the sustainability of the national economy are formed by measures of foreign trade, financial, tax, competitive and social policies, which are carried out by a system of state institutions to support the sustainable state of the economy. The subject of ensuring the stability of the national economy is the state, which performs the main functions of increasing the level of stability of the economic system of the country through the legislative, executive and judicial authorities.

In addition, the conditions for the stability of the national economy also include, firstly, the integrity and unity of the economic space of the state, the uniformity of its socio-economic development. Secondly, the state regional policy should stimulate the innovative activity of the regions on the basis of a developed system of appropriate financing. Thirdly, the country's dependence on external sources of raw materials, food, fuel and energy resources means a low level of resistance of the national economy to negative external influences.

**Role of ESG in a modern world**

Environmental, Social, and Governance (ESG) factors play a crucial role in evaluating the sustainability of a country. These factors provide a comprehensive framework for assessing the impact of a nation's policies, practices, and overall performance on the environment, society, and governance structures. Here's an overview of how ESG factors contribute to the evaluation of a country's sustainability:

Environmental Factors (E):

Climate Change Policies: Evaluation of a country's commitment to addressing climate change, implementing renewable energy sources, and mitigating environmental risks.

Natural Resource Management: Assessment of how a nation manages and preserves its natural resources, including water, land, and biodiversity.

Emissions and Pollution Control: Examination of efforts to control emissions, manage waste, and reduce pollution to promote a cleaner environment.

Social Factors (S):

Social Equity: Analysis of social inclusivity, income distribution, and poverty alleviation measures to ensure fair economic opportunities for all citizens.

Labor Practices: Evaluation of labor standards, workplace safety, and overall treatment of workers to promote fair employment practices.

Healthcare and Education: Assessment of healthcare and education systems to gauge the well-being and development of the population.

Governance Factors (G):

Political Stability: Evaluation of the political climate, government effectiveness, and overall stability to ensure a conducive environment for economic and social development.

Corruption Prevention: Assessment of anti-corruption measures and the effectiveness of governance structures to maintain transparency and accountability.

Legal Framework: Examination of the legal system, rule of law, and protection of property rights to ensure a stable and secure business environment.

By considering these ESG factors, investors, policymakers, and analysts can gain insights into the long-term sustainability and resilience of a country. Sustainable practices contribute not only to environmental preservation but also to social well-being and stable governance. Integrating ESG considerations into the evaluation process encourages responsible and ethical decision-making, fostering a holistic approach to national development. As global awareness of sustainability grows, countries that prioritize ESG factors are likely to attract investments, build resilient economies, and contribute positively to the well-being of their citizens and the planet.(Yakovlev,2010)

Companies aiming to meet ESG requirements commit to principles of social responsibility and environmental consciousness. For instance, they are expected to:

- Reduce air, water, and soil pollution;
- Sort and recycle waste;
- Rely on renewable resources and alternative energy sources;
- Abandon the use of natural fur in their products and cease animal testing;

They are also expected to:

- Create favorable working conditions for employees
- Enhance benefits for customers
- Support various charitable, educational, sports, and public organizations
- Initiate their own public initiatives

Furthermore, they should:

- Employ ethical business practices
- Ensure transparency in operations and gender diversity in the workforce
- Enhance the quality of corporate governance

It's worth noting that some experts differentiate between "ESG investments" and "Impact investments." ESG is considered anything that does not harm the planet, while "impact" encompasses actions that contribute to increased societal benefits. However, this is a nuanced distinction, and one company can simultaneously adhere to both ESG and Impact principles.


Figure 1. The fundamental pillars of ESG

There is a growing demand for investments in such companies. According to Reuters, from January to November 2021, ESG-focused funds worldwide attracted a record $649 billion. For comparison, in 2020, investors invested $542 billion, and in 2019, only $285 billion. According to Refinitiv Lipper, ESG now accounts for about 10% of all assets in global investment funds, amounting to an estimated $35 trillion to $46 trillion.

### 2.2. ESG-banking as a connecting tool to sustainability of a country's economy

ESG (Environmental, Social, Governance) companies are commonly considered less risky, with lower reputational, political, and regulatory risks. They are less prone to fines, corporate scandals, and environmental disasters.

Additionally, companies practicing responsibility by disclosing their environmental, social, and governance initiatives can enhance their reputation among shareholders, customers, employees, and partners. This, in turn, can attract increased investments and revenues.

Regarding the returns on ESG investments, opinions differ. A 2021 survey by Morning Consult of 2,200 Americans revealed that the majority of respondents believe investing in ESG is profitable. Among active investors, 69% claimed that ESG investing yields profits. Active investors, defined as those frequently buying various financial instruments, prioritized profit for 54%, while only 35% emphasized the environmental and social responsibility of companies as their primary consideration when investing. In essence, the evaluation of ESG investment profitability in this instance came from financially motivated individuals rather than those exclusively focused on ecological concerns.

Conversely, there are research findings that point to lackluster or unfavorable results in transactions involving ESG assets. A study conducted by the University of Chicago scrutinized the sustainability ratings provided by Morningstar, examining data from 20,000 mutual funds overseeing a total of $8 trillion in investor assets. The outcome revealed that funds boasting high sustainability ratings attracted more capital; however, none of these funds surpassed the returns of regular funds with low ESG ratings.

In essence, while sustainable development initiatives are commendable, the current landscape of this realm presents significant contradictions.

ESG ratings have grown in importance in recent years. They serve as one of the metrics used to track how much the business considers managerial, social, and environmental aspects of its operations, as well as the risks involved. Since environmental, social, and governance factors are included in ESG, these elements are related to the operations of every economic sector and ought to be taken into consideration when evaluating the success of their initiatives and the outcomes of their policies.

Many people wrongly assume that businesses in many economic sectors involved in resource utilization and production are the only ones affected by ESG considerations and their application. In actuality, though, these standards ought to be applied to all economic entities—including financial institutions—in order to promote sustainable growth, first of all, banks. Banks may utilize ESG ratings as an extra assessment of a borrower client's creditworthiness. (Gasperini, 2019)

Banks are supporting stronger company environmental protection as a result of these ratings. It will be more challenging for the business to obtain a bank loan if it actively pollutes the air or generates trash, violates social and corporate rules, and has a low ESG rating. In a similar vein, banks that support the operations of businesses with low ESG ratings run the danger of receiving a bad ESG rating themselves. This might damage the bank's brand and image, cause depositors to leave, and raise the likelihood of bankruptcy. The analysis of the ESG rating using a variety of techniques revealed that it is necessary to standardize ESG rating indicators and universalize ESG rating indicators.

Understanding ESG risks and opportunities is essential for making informed investment decisions that align with both financial goals and broader sustainability objectives in long term.

Responsible investing (PRI) means that the acceptance of investment decisions by investors are justified taking into account ESG factors and aligns with sustainability goals.

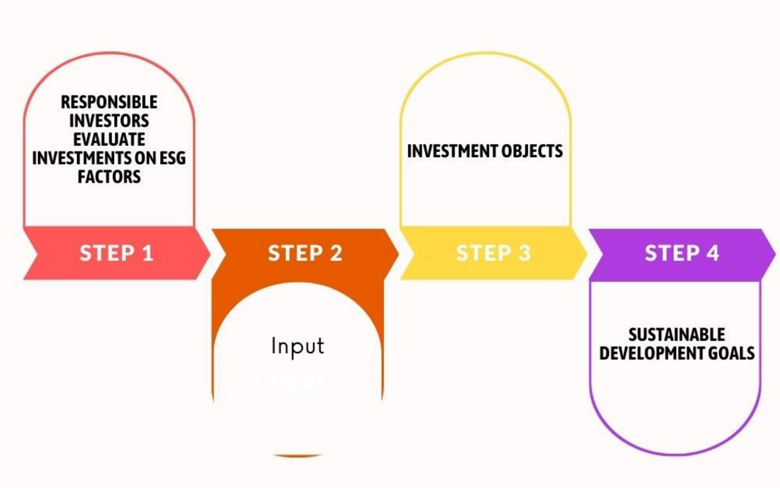



Figure 2. Visualization of the way ESG affects SDG: further sustainable growth of the economy

Source: own investigation

In the context of preserving and developing global value chains, compliance with ESG practices are, on the one hand, a condition for attracting responsible investors and, on the other hand, a mandatory requirement for businesses of all industries, ownership and size.

On the other hand, it is a mandatory requirement for businesses of all industries, forms of ownership and sizes based on the experience of Friede, G., Busch, T., & Bassen, A. (2015).

Otherwise:

- Enterprises unwilling to play by "green" rules will lose value;

- Rejection of ESG principles by lenders and investors may result in the emergence of systemic risks in the economy;

- Concentration of lending activity in real economy sectors with high CO2 emissions will increase risks in the financial sector. CO2 emissions will increase risks in the financial sector.

Simultaneously, ESG specialists actively seek investment opportunities to improve performance indicators. Some investors analyze data related to automotive companies to understand how their operations align with the trend toward the electrification of vehicles, incorporating the results of this analysis into revenue forecasts for their investment portfolios. Others invest in companies where management specifically focuses on ESG issues, anticipating that such companies are likely to outperform their competitors in the long run.

# 3. AN ANALYSIS OF IMPLEMENTING ESG PRINCIPLES IN KAZAKHSTAN

## 3.1. Overview of the Kazakhstan’s investment climate

Market surveys conducted by the Republic of Kazakhstan's Bureau of National Statistics reveal that 87.7% of the nation's examined enterprises are not aware with the ESG standards.

Following ESG guidelines now frequently has a direct impact on an organization's asset value and investment appeal. The Republic of Kazakhstan should also take note of this, particularly in light of its commitments under the UN Sustainable Development Goals (SDGs).

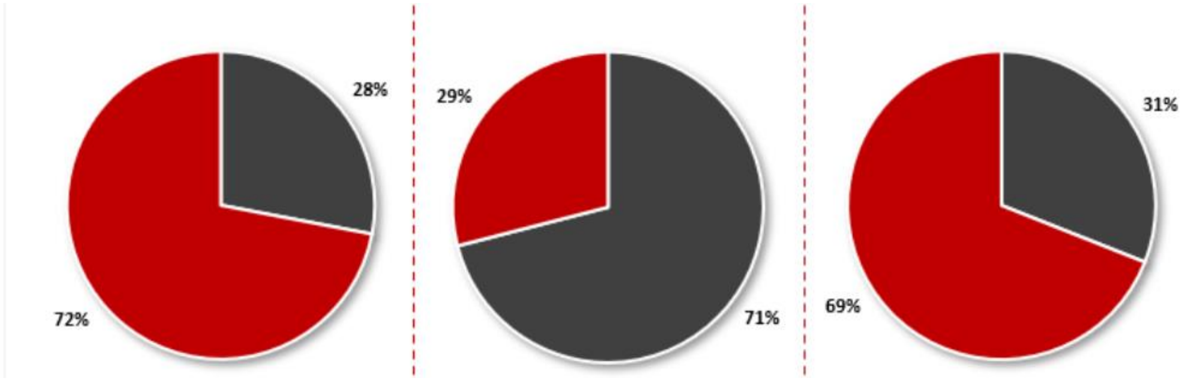
Regrettably, the little progress of Kazakhstan's entrepreneurship in this regard is demonstrated by the fact that only 12.3% of the enterprises questioned are aware of the standards and tenets of ESG.

The areas of Zhetysu (25.5%), Ulytau (23.1%), Pavlodar (21.7%), Atyrau (21.1%), and West Kazakhstan (18.5%) had the highest percentage of businesses familiar with ESG concepts. The areas of Turkestan, Almaty, and North Kazakhstan exhibit the lowest indices.

72% of the assessed firms do not meet the environmental requirements of sustainable development, and 69% do not meet the standards of corporate governance, according to a review of their degree of compliance with the ESG criteria. Simultaneously, just 29% of businesses do not meet the social standards for sustainable development, despite 71% being fully accountable for this aspect of ESG.

Figure 3. Ratio of implementation of ESG standards in enterprises, Kazakhstan

Source:Republic of Kazakhstan's Bureau of National Statistics




Ecological criteria Social criteria Governance criteria

Meet criteria Do not meet criteria

Kazakhstan ranked 53rd out of 183 nations in the ESG area for 2022, according to the worldwide evaluation, with a score of 38.68.

In the area, the nation rose to prominence at the same time as the EAEU(Eurasian Economic Union) and CA(Central Asia). The Republic of Kazakhstan is clearly leading the other nations; for instance, Armenia came in just 65th position overall, followed by Kyrgyzstan (67th), Belarus (79th), Russia (92nd), Turkmenistan (94th), Uzbekistan (100th), and Tajikistan (115th).

As a result, Kazakhstan has made significant progress in this area, and the Republic of Kazakhstan's business community actively participates in the realization of the SDGs and ESG.

## 3.2. Problems faced by the ESG-banking integration: ESG-risks

**Rating agency S&P Global Ratings has prepared a report "Banking Industry Country Risk Assessment (BICRA)."**

Analysts of the agency noted that as a result of the assessment, the banking sector of the Republic of Kazakhstan (BBB-/Negative/A-3) was assigned to the "9" group in terms of industry and country risks. This group includes, for example, the banking systems of Vietnam, Cambodia, Azerbaijan, Egypt, Kenya and Turkey. As a comparison, the banking systems of Cyprus, Jordan, Uzbekistan and Georgia belonging to the "8" group are also given .

Commercial banks that exclusively conduct business in Kazakhstan have a basic grade of "b +."

Financial institutions that draw deposits, provide loans, or do business in these categories are taken into account as part of the BICRA analysis, whether or not they have S&P Global Ratings. Based on the BICRA classification, banking systems are categorized into 10 categories based on the level of risk they face. Group "1" comprises the nations with the lowest risk, while group "10" comprises the countries with the highest risk. The industrial risk evaluation is a "9," and the economic risk assessment for Kazakhstan's banking sector is a "8," according to the experts.

Over the next three years, it is expected that the economy will grow at a rate of little less than 4% annually. According to the analysis, the expansion of the Tengiz oil field will be the primary driver of this growth and will result in a notable rise in oil output.

The experts of the agency state that Kazakhstan's economic risks are still considerable, as evidenced by the evaluation of economic risk at the "8" level.

Pressure on economic indicators has increased, which has been made worse by increased geopolitical threats related to the crisis in Ukraine, a dramatic rise in global inflation rates, and changes in interest rate dynamics. Even if the amount of bad loans in Kazakhstan's banking industry has dropped dramatically over the last two years, the industry's average indicator—roughly 9% of all loan portfolios—remains high. In particular, given the potential identification of new loans as problematic and the increasing trend of banks to expand their loan portfolios, it is anticipated that Kazakh banks' expenses related to the establishment of reserves for potential loan losses will stay at the level of up to 2% over the next 18 months. The research states that there is a consistent trend in the growth of economic risk.

**Moderating effect of the Russian-Ukrainian war on Kazakhstan's economic development and banking sector.**

Although, Russia is Kazakhstan's largest trading partner and the main supplier of goods and services to the country. With Statistical data from article on communications of Russia and Kazakhstan, made by Kenzheali (2022), Russian imports accounted for about 35% of Kazakhstan's total imports in the first quarter of 2022, and exports to Russia account for about 9% of total exports. Bans on sugar and grain exports imposed by Russia and a depreciation of the Kazakhstan tenge against the Russian ruble led to a sharp increase in food prices in Kazakhstan, which led to inflation at 15% as of July (on an annualized basis). The secondary impact of the sanctions imposed on Russia can also create difficulties for local trading companies operating in certain sectors, although we understand that in reality the volume of trade probably increased, given the free movement of goods, services and labor between countries.

Also, minimal market diversification could be one of the reasons of challenges in banking sector: the portion held by the country's largest 5 banks in terms of customer deposits rose from 67% as of January 1, 2022, to 72% by June 1;

a decline in the capability to manage debt for certain corporate borrowers, SMEs, and individuals: the percentage of problematic loans for this year is projected to reach 9%.

If we talk about ESG and Sustainable Finance, I would cite the book Gaganis et al. (2023), as the theoretical knowledge I have gained from there on this topic. The success of business operations and the management of various policies, such as how ESG disclosures are made, how a company's board is organized, how diversity is encouraged, how executive compensation is distributed, how corruption and fraud are avoided, and general communication strategies meant to increase transparency, are all aided by Governance risks.

Businesses looking to enhance the governance part of their ESG risk management plan should stay informed about new environmental laws and the board's drive to keep an eye on and control ESG risks.

The process of investment encompasses a series of actions undertaken by various participants involved in investment activities. These actions are oriented towards addressing the developmental tasks of the country's production potential, its industries, individual enterprises, regions, and the enhancement of socio-cultural aspects, along with the preservation of environmental objects. It is noteworthy that the influence of the investment process on the economic condition holds considerable significance. The extent and pace of scientific and technological progress are contingent on the activity within this process, consequently improving labor productivity at the national, sectoral, and regional levels, as well as at the enterprise level .

Over the years of independence, Kazakhstan has undergone significant changes in the realm of investments. During its formative years, Kazakhstan sought external financing for systematic economic development. Approximately $330 billion in foreign investments were attracted from around 120 countries over the years of independence. Kazakhstan's economy is gradually evolving, becoming more competitive and appealing to investors. In this context, the structure of attracting foreign investments may undergo changes, with a shift from predominance in extractive industries to other sectors that attract investor interest, based on the data given in Heim (2020).

The investment climate in Kazakhstan demonstrates positive dynamics. However, there are negative factors that could impede the influx of investments into the country. For the economic modernization of the nation, the role of attracting investments is pivotal. While the investment climate in Kazakhstan holds promise, instability exists, and challenges hindering further development include financial risk, currency control, Kazakhstan's tax and financial regime, undeveloped transport and communication infrastructure, a shortage of qualified labor, a weak securities market, and limited and inactive IPOs of Kazakhstani companies. (Varavin&Kozlova,2018)

The investment attraction process undergoes structural transformation each year. A three-level investment attraction system has been established, featuring investment programs designed for all foreign institutions with a five-year duration. These programs specify sectors and the number of companies Kazakhstan aims to collaborate with, allowing embassies to work with approximately 150-200 interested investors. After evaluating proposals, a preliminary list of around fifteen interested companies is considered, and these are further reviewed by regional authorities and industry government agencies. (Heim ,2020)

In response to changing circumstances, an Investment Agreement for strategic investors has been introduced to facilitate the effective implementation of major projects in strategically vital economic sectors. The role of the petrochemical industry is predominant in the country's economy, having developed successfully in recent years, with promising potential for agribusiness development. Other sectors involving international companies, such as mining and metallurgy, position Kazakhstan as a leading producer of copper, tungsten, gold, uranium, chrome, and more. These opportunities signify potential for further economic development.

Based on 2019 data, the inflow of foreign direct investments in Kazakhstan across sectors remains stable, with significant portions directed towards the mining sector (56.3%), followed by manufacturing industries (14.3%), trade (12.3%), transportation (4.6%), construction (2.7%), and other sectors (5.4%).

Table 1.The inflow of FDI in Kazakhstan

| Indicator | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|---|---|---|---|---|---|---|---|
| Environmental expenditure as a percentage of GDP | 0,36 | 0,35 | 0,43 | 0,32 | 0,32 | 0,31 | 0,32 |
| Growth in Environmental Costs | 18,0 | 8,9 | 24,2 | -12,9 | 15,3 | 8,9 | 16,0 |
| Investments, tenge, millions | 77500,4 | 103492,2 | 82883,2 | 43936,9 | 86962,0 | 111161,4 | 198721,6 |
| Investment Growth Rate,% | | 33,54 | -19,91 | -46,99 | 97,92 | 27,83 | 78,77 |
| Share of investments aimed at environmental protection in the total volume of investments,% | | 1,6 | 1,2 | 0,6 | 1,0 | 1,0 | 1,6 |

Source: Republic of Kazakhstan's Bureau of National Statistics

Let us assess the Republic of Kazakhstan's policy for "green" investments in order to identify both the advantages and disadvantages of its execution. The amount of money Kazakhstan continues to spend on environmental protection is a crucial indicator of its investment strategy in environmental preservation. Official data from Kazakhstan's Agency for Strategic Planning and Reforms' National Statistics Bureau indicates that spending on environmental protection is very variable, growing at a pace between -12.9% and 24.2%.

We look at the measure of the amount spent on environmental protection as a percentage of GDP in order to lessen the effect of inflation on the trend of current spending (Table 1). This measure of GDP varied between 0.31% and 0.43% during the course of the study period. These numbers strongly imply that Kazakhstan's environmental protection programs are not receiving enough financing. In contrast, 27 member states of the European Union allotted 1.7% of their GDP and 0.8% of their overall government spending to environmental preservation in 2018. Since 2017, Kazakhstan's investments in environmental preservation have been on the rise.

At the moment, 81.7% of all investments made in Kazakhstan go toward renewable energy sources. Aside from air protection (5.5%), other noteworthy investment areas are waste management (4.6%), soil, subterranean, and surface water conservation and rehabilitation (4.4%), and biodiversity and habitat preservation (2.1%). By contrast, investments in energy-efficient technology and measures to reduce greenhouse gas emissions account for a meager 0.0005% of the overall investment volume, or about 0.3% of the total. In conclusion, 1.6% of investments are disproportionately little when considering the larger picture of capital investment that goes toward environmental preservation.

By sector, the Republic of Kazakhstan invested 86.8% of total funds for environmental protection in 2019. Of them, 58.3% went toward gas and electricity delivery, steam and air conditioning, energy supply, and manufacturing, while 21.6% went into manufacturing. 6.6% of investments went to the mining and quarrying sector, which is almost equivalent to what was allocated to the building sector.

Even though Kazakhstan has a thriving responsible investment market, there are still informational, legal, and structural barriers that must be taken into consideration. With its heavy reliance on banks and government finance, the domestic financial system adheres to a non-continental model, which is one of its biggest drawbacks. This makes it much more difficult for leading techniques to be adopted, but it does not negate the benefits of catching up in development.Falcone (2020)

The development of responsible investing in Kazakhstan is hindered by low transparency of Kazakh companies, corporate governance deficiencies, weak attention of businesses to environmental issues, high concentration of the financial market on raw material companies, and a population mindset that shows limited interest in ESG principles.

**Key Findings (Conclusions):**

Currently, Kazakhstan's economy is developing under a "brown" scenario and remains heavily oriented towards the extraction of natural resources at the expense of "green" technologies. The state should act as a driver for the priority promotion of "green" projects, making the transition to a "green track" financially attractive for businesses.

## 3.3.EXISTING MISCONCEPTIONS REGARDING ESG INTEGRATION

There are common misconceptions about ESG investing, integration, as it is a new field of study, based on the experience, and theoretical and practical, that were described in the book of Matos, P. (2020). ESG and Responsible Institutional Investing Around the World: A Critical Review. CFA Institute Research Foundation.

Adhering to ESG integration practices does not imply:

- Prohibition of investments in specific companies, industries, or countries;
- The need to sacrifice portfolio returns;
- The need to consider insignificant ESG factors at the expense of traditional financial factors; or
- The need for substantial changes to the investment process.

Prohibition of investments in specific companies, industries, or countries

Some investors believe that the ESG integration method and the screening/ESG filter method (rejecting investments that do not meet established ESG criteria) are synonymous. However, these two approaches have two fundamental differences:

a. One approach (screening/ESG filter method) may potentially limit an investor's investment universe, while the other (ESG integration) does not.
b. One approach is based on the concept of "values" (screening/ESG filter method), while the other (ESG integration) is based on the concept of "value."

The screening method is practiced within a policy that sets ESG filters applied to investments and, as a result, may reduce an investor's investment universe. (Houston & Shan, 2021) Such a policy typically operates at the company or fund level and is characterized by:

- A list of prohibited actions, products, and/or services; and
- Rules specifying which countries, industries, and companies are prohibited for investments.

| Approach | Definition |
|---|---|
| **Negative screening** | The exclusion of certain sectors, companies, or practices |
| **Positive selection** | Investment in sectors, companies or projects selected for positive performance |
| Norm-based screening | Screening of investments against minimum standards of business practice based on international norms e.g. United Nations Global Compact |
| Environmental, social and governance (ESG) integration | The systematic and explicit inclusion of ESG factors into analysis |
| Sustainability themed investing | Investment in themes or assets specifically related to sustainability |
| Impact/community investing | Targeted investments aimed at solving social or environmental problems, where capital is directed to underserved communities and businesses with a social or environmental purpose |
| Corporate engagement and shareholder action | The use of engagement or shareholder power to influence corporate behaviour |

Table 2. Investment selection strategies

Source: Global Sustainable Investment Alliance, '2018 Global Sustainable Investment Review', pg.7

The screening process is often carried out before the investment analysis. This runs counter to the ESG integration technique, which does not place any limits on investments in certain businesses, sectors of the economy, or nations. Instead, it considers that the analysis of financial and ESG information is an essential component of the securities selection and portfolio creation process.

The requirement to forgo portfolio returns

The mitigation of risks and/or optimization of returns is a key component of ESG evaluation in the investing process. Using ESG integration techniques, investors might uncover hidden hazards that could otherwise go undetected through an examination of ESG data and current developments in the ESG space. (Houston & Shan, 2021)

ESG experts regularly look for investment possibilities to raise performance metrics at the same time. Some investors use automotive company data research to see how their operations fit into the trend of electrification of cars. They then use the investigation's findings to project revenue for their investment portfolios. Others put money into businesses whose management places a special emphasis on environmental, social, and governance (ESG) concerns, believing that these businesses would eventually beat their rivals.

### 3.4. Research on banks

#### 3.4.1. Research objective and research questions

Research Objective:

To conduct a comparative ESG (Environmental, Social, and Governance) analysis of two banks operating in different countries, with the aim of evaluating their sustainability practices and identifying key differences or similarities in their ESG performance.

Research Questions:

ESG Framework and Policies:

How do the ESG frameworks and policies of Bank A (in Country X) and Bank B (in Country Y) differ or align with international best practices?

What specific ESG criteria and indicators do each bank prioritize in their operations?

*Environmental Practices:*

What are the environmental initiatives and practices adopted by each bank to minimize their ecological footprint?

How do the banks address climate-related risks and opportunities in their lending and investment activities?

*Social Impact:*

How do Bank A and Bank B contribute to social development in their respective countries, including aspects such as community engagement, financial inclusion, and support for social welfare programs?

What measures do the banks take to ensure fair labor practices, diversity, and employee well-being?

Governance Structure:

How are the governance structures of the two banks designed, and how do they ensure transparency, accountability, and ethical conduct?

What mechanisms are in place to prevent corruption and ensure compliance with regulatory standards?

Risk Management and Integration:

How do Bank A and Bank B integrate ESG factors into their risk management processes?

Are there specific ESG-related risk mitigation strategies in place, and how do they align with industry benchmarks?

Stakeholder Engagement:

How do the banks engage with stakeholders, including customers, investors, and the local communities, regarding ESG matters?

What communication and reporting mechanisms are used to disclose ESG-related information to stakeholders?

Performance Metrics:

What key performance indicators (KPIs) or metrics do the banks use to measure their ESG performance?

How have these indicators evolved over time, and what trends or patterns can be identified?

Regulatory Compliance:

How well do Bank A and Bank B comply with local and international ESG regulations and standards?

Are there notable differences in regulatory expectations and enforcement in the two countries?

By addressing these research questions, the comparative ESG analysis can provide valuable insights into the sustainability practices of the selected banks, contribute to the existing knowledge in the field, and offer recommendations for improving ESG performance in the banking sector.

### 3.4.2. Research methodology

In essence, this research methodology employs a mixed-methods approach, combining qualitative and quantitative research elements. This approach allows for a comprehensive understanding of the banks' ESG practices, considering both the qualitative context and the quantitative measures that contribute to a robust comparative analysis. The research methodology described above incorporates elements of both qualitative and quantitative research. Here's how:

Qualitative Aspects:

Literature Review: Qualitative research is involved in reviewing existing literature, understanding the theoretical frameworks, and gaining insights into key ESG indicators and practices.

Case Selection: The process of selecting two banks based on specific criteria involves qualitative judgment and reasoning.

Data Collection: Qualitative data, such as information from reports, statements, and official documents, is gathered to provide context and depth to the analysis.

ESG Framework Analysis: Qualitative analysis is employed to understand and compare the ESG frameworks, policies, and guidelines of each bank.

Quantitative Aspects:

Data Collection: Quantitative data, such as ESG scores, performance metrics, and financial data, is collected to provide numerical measures for analysis.

Environmental Analysis: Quantitative indicators related to the banks' carbon footprint, energy efficiency, and compliance with environmental regulations can be assessed.

Social Impact Assessment: Quantitative data on community development initiatives, financial inclusion efforts, and employee welfare programs can be analyzed.

Governance Structure Examination: Governance metrics and quantitative aspects of board composition, transparency, and compliance can be included in the analysis.

Risk Management and Integration Analysis: Quantitative measures related to how banks integrate ESG factors into their risk management processes can be assessed.

Performance Metrics Assessment: Analysis of key performance indicators involves quantitative evaluation and comparison.

Regulatory Compliance Review: The assessment of regulatory compliance can involve both qualitative understanding and quantitative measures of adherence.

Data Analysis and Interpretation:

Both qualitative and quantitative data analysis techniques are employed to interpret the findings and draw conclusions.

### 3.4.3. Research finding

1. ESG Framework and Policies:

When it came to ESG and sustainable development frameworks and policies, both banks aimed for the most distinct vision. However, if we consider the variations and parallels with global best practices, we can conclude that MFB is a relatively new player in the integration of ESG factors. As a fully governmental organization, it is working towards the Central Bank of Hungary's (MNB) Green Recommendation of MNB Compliance.

The MNB aims to enhance the preparedness of the Hungarian financial system in terms of sustainability, climate change, and environmental risk management prior to the implementation of relevant EU and national laws. Regarding the development of business strategies, corporate governance, risk management, and disclosures, the MNB set forth expectations. The Central Bank of Hungary revised and updated its previous recommendation 5/2021 (IV.15) with Recommendation No. 10/2022 (VIII.2) on climate-related and environmental risks and the integration of environmental sustainability considerations into the operations of credit institutions in response to modifications in EU regulations, surveys, and market consultations. By establishing priority targets, the new suggestion pushes banks to operate more sustainably and lays out more precise expectations than the previous one.

The Green Recommendation action plan's execution was deemed a priority project by MFB Zrt. in 2022. The management of the Bank arranged the efforts of the Sustainability Working Group into a project-like framework with the express purpose of coordinating the MNB's Green Recommendation's implementation. Both the action plan and the Green Recommendation's general framework address practically every aspect of banking operations. It has already produced outcomes in terms of a financial institution's biodiversity and inclusion. By implementation of this project, MFB in 2022 prepared its first ESG Report for 2021 according to the GRI Global Reporting Initiative’s international sustainability reporting framework Core (basic) and SASB materiality criteria, where determination of MFB’s Carbon

Footprint measurement has started with the involvement of the KÖVET Association. After the measurement for year 2021, the necessary data for 2022 has been collected.

Halyk Bank used innovative methods to evaluate their own ESG sustainability. We talk about a tool, that can measure the amount of carbon footprint of an organization in their loan portfolio. They divided portfolio into selections based on the industry, and maintained the goal of identifying the most pollutant companies in order to decrease their own footprint. It also can be  an indicator of Risk Management inclusion, because to take an action on concerning issue in terms of institution as huge, as Halyk Bank, you have to identify the main concerns and take steps ahead. This clearly shows the commitment to ESG values and factors, that they follow.

Both of the Banks have new plans, with vision for a long-term, MFB mostly focused on Governance factor, while Halyk was more detailed on Environmental and Governance factors.

2) Environmental Practices

**Waste generation of MFB Zrt.**

| | 2020 | 2021 | 2022 |
|---|---|---|---|
| **Total waste (kg)** [45] | **23 708** | **23 865** | **23 970** |
| Separately collected non-hazardous waste (kg) | 4 440 | 4 430 | 4 540 |
| Paper | 3 500 | 3 495 | 3 500 |
| Of which: office paper | 3 873 | 2 678 | 1950 |
| Of which: packaging waste | - | 817 | 1550 |
| Plastic | 940 | 935 | 940 |
| Separately collected hazardous waste (kg) | 68 | 235 | 230 |
| Of which: batteries | 68 | 31 | 0 |
| Of which: toner cartridge | 0 | 204 | 230 |
| Other municipal waste (kg) | 19 200 | 19 200 | 19 200 |

[45] Scrap metal is removed with municipal waste. For municipal waste collection, an estimate has been used based on the total capacity of the waste bins placed on site.

Table 3. Waste generation of MFB

It is the responsibility of outside contractors to handle, transport, and dispose of materials used during maintenance work at MFB Zrt. headquarters.

The way materials are utilized will be governed by the Bank's fire safety policy. The following ecologically hazardous products, whether or not they are created on the bank's property, need to be gathered, transported, and disposed of by the bank: light sources (operational personnel is required to store and remove goods); batteries, including those from cell phones, must be kept in a designated location close to the registration desk.

To recycle commodities, the Bank autonomously collects waste plastic (mostly PET bottles and Tetra Pak) and paper (paper grinds). MFB Zrt employs specialized companies to move, get rid of, and recycle these products. In 2022, a total of 4540 kg of waste were sorted and processed. There are two types of paper waste produced by the Bank. There are two types of paper waste: packaging trash from bank purchases and office paper consumption. Every year, less papers are utilized in offices. In 2022, paper use will continue to decrease on the same trend as in prior years. Reducing the amount of paper used in workplaces is the aim of the bank's digitalization initiatives. In comparison to the base year 2019, recent measures have resulted in an additional 7% drop in the overall quantity of office paper use, for a total reduction of 77%. Similarly, each employee's paper usage has decreased by more than 80% as compared to 2019. Beginning in 2021, employees will have access to green-labeled office supplies and recycled paper through internal procurement.

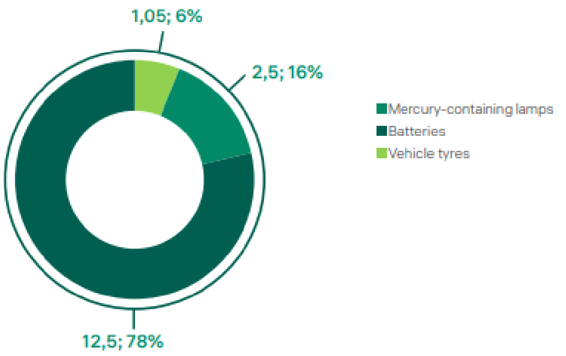



Figure 5. Ratio of MFB

7,280.5 tonnes of garbage were produced overall by the Bank's operations in 2022, of which 12.5 tonnes were hazardous trash and 7,268.0 tonnes were non-hazardous. The Bank has a range of hazardous waste products on hand, such as mercury-containing lights, automobile tires, and batteries. Among the non-hazardous trash are household garbage and solid waste paper (SDW).

The Bank disposes of and recycles all of its waste by sending it to approved suppliers. For example, wastepaper is sent to specialized organizations for recycling, non-ferrous metals are recovered before disposal, fluorescent lamps have their mercury vapour extracted (a process known as demercurization), batteries have their acidic electrolyte neutralized, and non-hazardous SDW is disposed of in landfills.

2. Environmental Initiatives

If we start with Halyk Bank, it has been taking into consideration and implementing ESG factors on diverse set of environmental issues, in order to minimize their ecological footprint. The most importantly, it was the decarbonization initiative, set along with governmental goals on carbon neutrality by 2060. The document envisages the large-scale decarbonization of almost all sectors of the economy and the renovation of production chains. From their side Bank initiated climate targets with the capabilities of:

- Finance innovative technologies that contribute to technological development and

the decarbonization of carbon-intensive industries in accordance with Kazakhstan's

net zero strategy;

- Special financing conditions for customers who have approved carbon neutrality

goals;

- Financing activities that contribute to a reduction and absorption of carbon.

Another unity of targets in reducing carbon emissions and supporting governmental initiative can be seen on Kazakhstan's Target of NDC14 : Reduce GHG emissions by 15% versus the 1990 level by 2030, which was supported by initiatives by Halyk Bank accordingly:

- Increase the share of project financing whose objectives are consistent with the

green taxonomy of Kazakhstan;

- Support the corporate customers who have publicly approved the decarbonization

Goals;

- Increase the share of the portfolio associated with high-tech and low-carbon

activities, including industries with a low carbon footprint.

Followed by the results of reducing the carbon emissions:

| | 2020 | 2021 | 2022 |
|---|---|---|---|
| **Direct GHG emissions (Scope 1), $TCO_2e$, including:** | 4 756,9 | 4 474,9 | 4 095,2 |
| $CO_2$ emissions | 4 744,4 | 4 463,2 | 4 084,4 |
| $CH_4$ emissions | 0,128 | 0,125 | 0,114 |
| $N_2O$ emissions | 0,0317 | 0,0312 | 0,0287 |
| **Indirect GHG emissions (Scope 2), $TCO_2e$, including** | 65 252 | 64 033 | 64 224 |
| Electricity | 49 257 | 47 310 | 46 290 |
| Heating | 19 283,3 | 17 942 | 17 935 |

* - The methodology for calculating GHG emissions is presented in the Annexes

Table 3. The carbon emissions data by Halyk Bank

Halyk has big plans concerning their environmental, carbon footprint reduction, as the results on their usage is not perfect enough. So, they created a 4 years plan on how to reduce the amount of pollutions. Mainly it consists of the benchmark on cutting carbon emissions by 4% over the course of 4 years. Nevertheless the waste management also has to be taken under control, as there are hazardous garbage that needs to be disposed, let along non-hazardous garbage that can be recycled and used in other sustainable ways. Exciting, how even small changes can make a difference, if you choose the way of staying eco-friendly, there will be a major decision from the Bank in reducing municipal waste by changing from fluorescent bulbs to LED ones in all headquarters.

3) Social Impact:

Halyk Bank contributes to socio economic development of Kazakhstan heavily, for example by participating in the "Lending Mechanism for Priority Projects– Economy of Simple Things" (EST) Program, which provides subsidies and guarantees for projects in priority sectors of the manufacturing industry, as well as production and processing by agribusinesses. The size of the subsidy under the program is up to 13.5% of the commission rate, and funding is issued for a period of up to five years or seven years as part of priority sectors of the economy. From the start of the program in December 2018 to 31 December 2022, the Bank received applications from entrepreneurs total KZT620.7 billion, while the Bank approved overall funding of KZT576.2 billion.

As well as participating in projects in education and healthcare, as funding multiple kindergartens and medical clinics, showing interest in development of female entrepreneurship, as it would be expected because of the prevalence of women in the whole organization in ratio of 73% to 27%. Halyk Bank began initiative to encourage female entrepreneurship in 2021, which resulted in KZT1.9 billion in funding at the end of 2022, supporting more than 200 women by developing neat and efficient terms on lending for specifically this group of society.

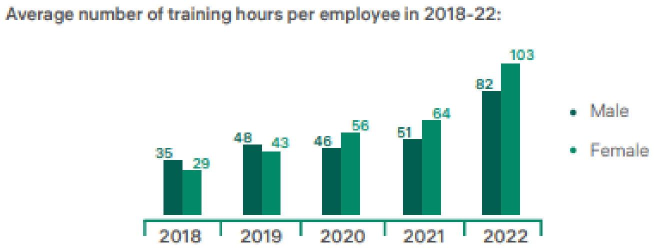



Figure 6 .Average number of training hours per employee in Halyk Bank

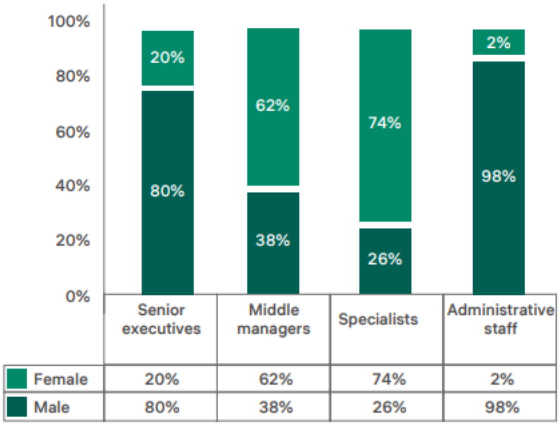



Figure 7. Ratio of gender equality in Halyk Bank

If we talk about MFB, and it's ways to maintain proper social development, it also has strong employer branding strategies, such as great rate of retention and employee satisfaction surveys with high (91%) results. Also, they have prepared new onboarding process description, in which we added additional tools to those already in place, such as a face-to-face CEO meeting and an onboarding video, which is less possible to do in Halyk Bank, regarding the size of the institution, but is a sufficient way to integrate newcomers.

The employer branding initiatives also encompassed the establishment and management of the MFB Workplace Nursery, along with the creation of the Maternity Compass—a daycare facility located within the bank's headquarters. This strategic move aims to provide support for working parents returning from maternity leaves. Given the nature of the bank's operations, MFB employees are engaged in tasks primarily evaluated through the Hay job assessment system methodology, emphasizing intellectual activities. As part of the HR digitalization efforts, the new HR-E-Admin system has been implemented, offering all employees a transparent and user-friendly platform for defining, modifying, and monitoring job descriptions. Notably, this system now integrates job competences, further enhancing the efficiency of HR operations.

Both organizations implement benefits including staff salaries after a fixed period of employment, access to holiday and sports facilities, the provision of equipment needed for work, financial support adapted to specific life situations, and opportunities for professional development (e.g. language teaching, participation in professional events and external professional training). As well as the MFB has it’s own training for ESG awareness among employees, and created choice on cash or non-cash allowances. The main purpose of non-cash family allowances is to ensure that employees starting a family do not have to choose between family and career. All this is supported by the Bank with a wide range of benefit tools.

Halyk, in contrast, views personnel assessment as one of the tools, that can help the company to be informed enough about the personal development and career prospectives of their employees. In this assessments it is crucial to cover all of the categories of employees, Management Board and even higher. The assessment process makes use of a number of instruments, including the balanced scorecard (BSC), which allows for the connection between executive compensation and the goals for each KPI of the Bank's business divisions. Another way to use the Assessment of Job Performance and Competencies (AJPC) technique is by using the corporate portal's automated form. An additional crucial instrument for making management decisions is the performance evaluation, such as creating a talent pool, creating programs for staff development, paying incentives, identifying the Bank's top workers, and determining the yearly bonus.

3. Governance impact

Transparent and responsible governance is a top priority for MFB Zrt., a state-owned financial institution. The Minister in charge of overseeing state assets appoints the Chief Executive Officer, the five-member Supervisory Board, and the five-member Board of Directors that make up the governance structure. The MFB Act governs the combined appointment of the CEO and Chairman of the Board, who are chosen by the members. The Rules of Procedures for Decision-Making's explicit decision-making processes are guaranteed by the framework.

MFB Zrt. adheres to the moral guidelines and strict standards specified in the Code of Conduct and Ethics, placing a strong emphasis on responsible corporate governance. Promoting an anti-fraud culture, developing internal control systems, and increasing ethical awareness are the three primary ethical goals. The Ethics Committee, which is made up of delegates from Internal Audit, Compliance, and

Internal Audit, and Human Resources, investigates violations and discloses ethical or legal breaches.

Ethical training, including anti-corruption modules, is provided to all employees. The code of conduct prohibits corruption and sets guidelines for receiving business gifts. Ethical expectations, including anti-corruption, must be acknowledged by employees, and MFB Zrt. communicates its anti-corruption policies to business partners. The Bank ensures that partners have their own ethical code of conduct before entering into a business relationship.

In the fight against money laundering and the funding of terrorism, MFB Zrt. scrupulously complies with national, international, and EU legal obligations. Group-level policies are developed, and each member firm creates customized internal policies. The rule directs banking activities, including monitoring, reporting, screening, and screening of suspected activity. Fund payments are subject to due diligence, which is backed by a special compliance application. Employees get thematic training, and procurement procedures are handled in accordance with public procurement regulations with a focus on competitive circumstances.

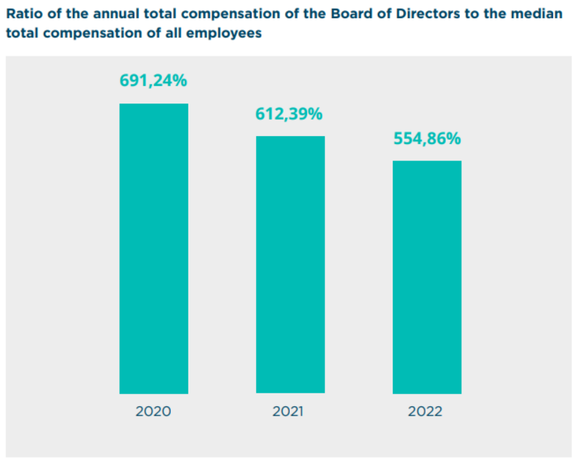



Figure 8. Ratio of the MFB compensation

In terms of its impact on governance, the ratio of the annual total compensation of the Board of Directors to the median annual total compensation of all employees—as established by statutory regulations—gives a clear picture of the Board's pay scale. The income of the highest-paid employee has not increased recently, but attempts to enhance pay have progressively lifted the median compensation for other employees. By 2022, there will likely be a notable increase of 20%. Consequently, there is now less of a pay difference between CEOs and employees. Apart from the basic salary that is applied to the wages of managers and staff, the Remuneration Policy outlines the specifics of compensation linked to performance.

The approval of the financial statements is concurrent with the evaluation of pay related to performance. In addition, the Benefit Policy describes additional types of monetary and non-cash benefits, such as pension fund contributions and fringe benefits.

Significant legal non-compliance, according to MFB Zrt., is any deviation found following an inquiry process carried out by organizations using their statutory control authorities. Whether or whether penalties are listed as a penalty in the judgment or audit report, this term still holds true. There were eight cases of non-compliance in 2022, however none of them were penalized financially. One case involved inspections of a designated critical system element as part of a comprehensive regulatory audit on critical infrastructure protection carried out by the National Directorate; the other seven non-compliance cases involved investigations by bodies that monitor the use of grants from specific EU funds.

**Significant non-compliances**

| Number of significant non-compliances | 2020 | 2021 | 2022 |
|---|---|---|---|
| **Total number of cases of non-compliance** | **3** | **5** | **8** |
| Number of cases of non-compliance resulting in financial fines (case) | 1 | 1 | 0 |
| Number of cases of non-compliance resulting in non-financial penalties (case) | 2 | 4 | 8 |

Table 5. Significant non-compliances

In 2021, Halyk Bank proposed and approved a revised version of the rules governing the preparation and conduct of papers related to board of directors meetings. The Board of Directors got 68% less printed documents than the previous year because to this initiative, which also considerably reduced the quantity of paper items supplied to board members.

It is imperative to adhere to the Corporate Governance Code of the Bank. The General Shareholders Meeting of December 2006 approved the present Code, which outlines the fundamental principles and directives that govern the management of the Bank. These include the relationships between the shareholders and employees, the management board and the board of directors, and the internal operations and protocols of the bank. The Code offers a comprehensive framework for the administration of the Bank. It was drafted in accordance with Kazakh legislation and integrates both national and international best practices for corporate governance.

By introducing an automated system for decision-making in some mortgage lending programs in 2021, the Bank made significant progress toward modernizing its operations.

PricewaterhouseCoopers LLP confirmed the Bank’s internal audit compliance with international standards in 2022.

In accordance with global standards, the Board of Directors completed a self-evaluation, which was presented to shareholders during the General Shareholders Meeting. The growth plan of Halyk Group for the years 2022–24 is centered on building a dependable, technologically advanced ecosystem with a focus on sustainability and ESG. 2020 saw the approval of a policy against corruption as well as guidelines for evaluating board activity. In 2019, the Bank established a policy on corporate social responsibility.

The Bank upholds openness through a corporate governance component on its website and frequently covers the liabilities of its executives and directors. As part of the annual report, yearly corporate governance reports are posted online, showcasing the bank's dedication to openness and responsibility.

One of the cornerstones of Halyk Bank's corporate social responsibility is the prevention of corruption. The bank adheres strictly to its internal rules, international standards, and anti-corruption legislation in Kazakhstan. Halyk Bank implemented a thorough anti-corruption policy in 2020, which is accessible on their ESG platform.

The policy states that the primary objectives of the anti-corruption system are to integrate anti-corruption ideas into every aspect of the bank's operations. The bank is aware of the potential for corruption from employees who could abuse their positions of power to take advantage of them or other people for financial gain. To fix this, the bank has updated its records as necessary.

11,023 workers from Halyk Bank's head office and branch offices received anti-corruption policies and techniques training in 2022. Employees were given knowledge tests after the course, and the bank intends to repeat this training every year. Based on a report from 2020, a residual corruption risk assessment method was carried out in the first quarter of 2022.

Notably, no corruption violations were found during the reporting period, emphasizing the effectiveness of the measures implemented, both for newly hired and current employees.

Risk Management and Integration:

The MFB bank follows the MNB's Green Recommendation by incorporating ESG considerations into its risk management. In 2021 and 2022, they finished organizational procedures, identified hazards associated with climate change, and revised policies. The bank addresses ESG responsibilities, sets sectoral restrictions, and integrates environmental risk management into its structure. They set up a methodical framework for risk management, complete with stress tests and portfolio review procedures. A risk-oriented questionnaire spanning several factors is being prepared, and ESG customer assessment includes an ESG Index score and IT development. By taking part in the creation of a standard ESG questionnaire, the bank actively supports the integration of ESG principles across the banking industry.

By embracing responsible finance, preparing to assess the carbon footprint of its portfolio's indirect emissions, and putting in place ESG segmentation of the corporate loan portfolio, Halyk Bank incorporates ESG concepts into its risk management system. The bank integrates sustainable development goals into its regulatory framework and highlights the role of fintech in moving toward sustainable development models. The bank also actively participates in environmental projects, trains employees in ethical behavior, and encourages ecologically conscious conduct.

MFB began incorporating ESG risks into its risk management framework in accordance with the Central Bank of Hungary's (MNB) Green Recommendations, and it is getting ready to include ESG risk assessments into risk management procedures.

Stakeholder Engagement:

For the commitment to ESG factors Halyk Bank was nominated as The Best Bank and Best Bank for Diversity in 2022 in Kazakhstan. Although it has branches in 6 Eurasian countries, they are looking for the ways to strive, expand and grow in all dimensions. The comparative analysis based on the banks' sustainability reports showed, that linear correlation between country's sustainability as well as banking system's benchmark on development to more conscious decisions.

Thus, this study showed that by comparative analysis of two banks in the Kazakhstan and Hungary, we still need a common, universal tool to measure ESG factors in integration. Nevertheless, the openness of the data on all impact spheres. First of all, it is necessary to help analysts on predicting the future in market, also gives clear perspective on integration of the financial mechanisms.

In summary, while MFB and Halyk Bank differ in their specific approaches, both are committed to integrating ESG principles, promoting sustainability, and contributing positively to their respective social and environmental landscapes. Their efforts in governance, risk management, and stakeholder engagement demonstrate a holistic approach to sustainable banking practices.

Some international challenges include, for example, the absence of internationally recognized definition of ESG banking, as well as the lack of a standard interpretation of ESG risks and methodologies for ESG risk management. In the banking sector, there is no unified taxonomy adapted to it. There is no clear correlation between financial and non-financial reporting, on which one could rely when assessing the impact of ESG initiatives on the bank's financial performance. Different approaches to ESG assessment used in the financial market and the absence of a unified platform for sharing experiences and knowledge in the field of ESG also hinder implementation.

Among the local barriers is the high dependence on raw materials, which creates difficulties for a quick and cost-effective transition to a sustainable economy. Various levels of financial and human resources allocated by banks for the development of ESG practices play a role. It is also possible to highlight the lack of individual approaches to ESG banking suitable for the Kazakh economy and common standards for issuing green loans. Low awareness of banks and borrowers about the benefits of ESG integration also has a negative impact.

**4. ESG-banking: opportunities and threats**

Opportunities of ESG Banking based on the experience of Smiles, (2023), and the investigation I have made on Sustainability reports of MFB and Halyk Bank:

1. Market Growth and Differentiation:

ESG banking presents an opportunity for market growth by catering to the increasing demand for sustainable and responsible financial services. It allows banks to differentiate themselves and attract a growing segment of environmentally and socially conscious investors and customers.

2. Access to Capital:

Banks embracing ESG principles gain access to a broader pool of capital, including sustainable investment funds and ESG-focused investors. This expanded access to capital can provide financial institutions with a competitive advantage and support the funding of ESG-related projects.

3. Risk Mitigation:

Integrating ESG factors into risk management practices enhances a bank's ability to identify and mitigate long-term environmental, social, and governance risks. This approach contributes to overall financial stability by proactively addressing issues that may impact the bank's performance in the future.

4. Innovation and Product Development:

ESG considerations drive innovation in financial products and services. Banks can seize the opportunity to develop new offerings, such as green finance solutions, sustainable investment instruments, and ESG-aligned financial products that meet the evolving needs of environmentally conscious consumers and investors.

5. Regulatory Alignment:

Aligning with ESG principles positions banks favorably in the evolving regulatory landscape. Governments and regulatory bodies worldwide are increasingly emphasizing sustainability, and banks that proactively incorporate ESG criteria into their operations can adapt more easily to changing regulatory requirements.

6. Enhanced Brand Image and Reputation:

Demonstrating a strong commitment to ESG values enhances a bank's brand image and reputation. This not only fosters trust and loyalty among customers but also attracts top talent. A positive reputation for ethical and sustainable practices can lead to long-term relationships with customers and stakeholders.

7. Long-Term Financial Performance:

Banks that integrate ESG principles may experience better long-term financial performance. By aligning with sustainable business practices, financial institutions can address the evolving expectations of investors and society, contributing to enhanced financial resilience and performance over time.

Threats of ESG Banking:

- Regulatory and Compliance Risks:

Evolving and complex ESG regulations pose challenges for banks to ensure compliance. Failure to meet regulatory standards can result in legal and reputational risks, impacting the bank's standing in the market.

- Greenwashing Concerns:

There is a risk of greenwashing, where banks falsely represent their ESG initiatives. Such misrepresentation can lead to reputational damage and loss of trust if stakeholders perceive inconsistencies between the bank's claims and actual practices.

Transition and Implementation Costs:

The initial costs associated with transitioning to ESG practices, including implementing new technologies, conducting staff training, and adapting existing processes, can pose financial challenges for banks, especially smaller institutions with limited resources.

- Market Volatility:

Rapid changes in ESG-related market sentiments and priorities can result in market volatility. This can impact the valuation of ESG-focused financial instruments and investments, creating uncertainties for banks operating in this space.

- Lack of Standardization:

The absence of standardized ESG reporting frameworks and metrics creates challenges in comparing and benchmarking the performance of banks. This lack of standardization affects transparency and accountability, hindering the ability of stakeholders to assess and compare banks' ESG initiatives.

- Customer Education and Awareness:

Low awareness among customers about ESG principles and their impact on financial products may limit the adoption of ESG banking services. Banks must invest in educational efforts to increase customer awareness and understanding of the benefits of ESG-aligned products and services.

- Transitioning Economies:

Banks operating in economies heavily dependent on traditional industries may face challenges in transitioning to ESG banking. Economic structures and dependencies on non-sustainable practices can create obstacles for banks in aligning their operations with ESG principles.

Navigating these opportunities and threats requires a strategic and well-informed approach, as banks strive to integrate ESG principles into their core business operations.

## 5. SUMMARY

In this study, an analysis of the ESG market was carried out, the main trends, problems and prospects of this market, the advantages and disadvantages of implementing an ESG system in an enterprise were identified. Recommendations for the implementation of ESG systems were developed. The practical part of this study focused on the implementation of the ESG-banking system at MFB and Halyk Bank. The following conclusions were made during the study:

- The market is witnessing a process of expanding the interaction of domestic enterprises with leading foreign companies. At the same time, Kazakhstan companies are intensifying the use of advanced evaluation methods used by their foreign partners. The consequence of this interaction is the appearance on the domestic market of ESG-bankings. This process has a pronounced progressive and irreversible character.

- The implementation of ESG-systems is an important step with previous research to be done properly. In this regard, studies of mechanisms for reducing these costs are relevant. However, the current practice of implementing such systems shows that each project is implemented at domestic enterprises as individual and unique, which, in fact, is an additional source of high costs. Typification of the process of implementing ESG- systems will reduce the negative factors listed above.

- The market for the use of ESG factors at enterprises abroad is just as developed as in Kazakhstan. But there might be some issues in terms of specific economic sustainability. We need to increase the level of awareness about ESG factors in broader way of communicating with enterprises in Kazakhstan.

In conclusion, the sustainability efforts of MFB and Halyk Bank not only enhance the resilience and stability of the financial sector but also play a crucial role in contributing to the overall sustainability of Kazakhstan's economy. These banks serve as exemplars for integrating responsible and sustainable practices that align with the nation's economic development goals. Their initiatives lay the groundwork for a more resilient, inclusive, and environmentally conscious economic future for Kazakhstan.

- The main recommendations for the implementation of ESG systems include: paying a lot of attention to already existing information, experience in the same field. It will boost whole process, if you will try to do the implementation by given methodologies. In the banking system it will require clarity of finance and annual reports, which might be the reason of challenge for most of the interprises. Attention to detail to the Social factor might increase the level of productivity of employees, if right tools were used. In general, implementation of ESG factors will create appropriate brand image and long-term road map of development. Also, the growth of the numbers of companies following benchmark of ESG will assist on governmental progress. As we could see from the report, that it directly affects the economic sustainability in every side.

Based on the analysis, here are some recommendations for both MFB and Halyk Bank to further enhance their sustainability initiatives:

1. ESG Framework and Policies:

MFB: Given that MFB is a newcomer in ESG integration, continue to prioritize the implementation of the Green Recommendation action plan. Consider establishing clear targets and key performance indicators (KPIs) aligned with international best practices to monitor and measure progress in sustainability initiatives. Regularly update and communicate the action plan to stakeholders.

Halyk Bank: Continue efforts to integrate ESG principles into the risk management system. Explore opportunities for collaboration with international organizations and industry partners to stay informed about evolving ESG standards and best practices. Enhance transparency by providing detailed disclosures in alignment with international reporting frameworks.

2. Environmental Practices:

MFB: Expand waste reduction initiatives beyond office paper consumption. Consider adopting more sustainable practices, such as reducing single-use plastics and increasing the use of recycled materials. Set specific targets for waste reduction and regularly report progress to stakeholders. Explore partnerships with local organizations for effective waste management.

Halyk Bank: Strengthen the commitment to decarbonization by setting quantifiable targets for reducing direct and indirect carbon emissions. Consider leveraging innovative technologies to further reduce the environmental impact. Increase the transparency of environmental practices by regularly publishing comprehensive reports on carbon emissions and waste management.

3. Social Impact:

MFB: Continue fostering a diverse and inclusive workplace. Enhance initiatives for employee well-being and professional development. Consider expanding programs that support female entrepreneurship and family-friendly policies. Regularly assess and report on the social impact of lending activities, particularly in priority sectors.

Halyk Bank: Build on the success of programs supporting female entrepreneurship. Consider expanding social impact initiatives in education and healthcare, aligning them with the Sustainable Development Goals (SDGs). Collaborate with local communities and NGOs to address specific social challenges and needs.

4. Governance Impact:

MFB: Strengthen efforts to ensure transparent and accountable governance. Regularly review and update the Code of Conduct and Ethics to address emerging ethical challenges. Consider conducting periodic external audits to validate governance practices and enhance stakeholder trust.

Halyk Bank: Continue modernizing governance processes, such as the automation of decision-making. Explore opportunities to further reduce paper consumption in governance-related activities. Enhance transparency by regularly updating the Code of Corporate Governance and ensuring alignment with evolving national and international standards.

5. Risk Management and Integration:

MFB and Halyk Bank: Collaborate on industry-wide efforts to develop a uniform ESG questionnaire. Enhance communication and collaboration with regulators to stay informed about evolving ESG regulations. Regularly update risk management frameworks to incorporate emerging ESG risks. Consider engaging with industry associations to share best practices in ESG risk assessment.

6. Stakeholder Engagement:

MFB and Halyk Bank: Continue engaging with stakeholders through regular workshops and feedback sessions. Consider expanding stakeholder engagement efforts to include a wider range of perspectives, including those of environmental and social advocacy groups. Ensure that stakeholder feedback is systematically incorporated into decision-making processes.

These recommendations aim to build on the existing sustainability initiatives of both MFB and Halyk Bank, helping them further integrate ESG principles, reduce environmental impact, enhance social impact, strengthen governance practices, and effectively manage risks associated with sustainability. Regularly monitoring and reporting progress on these recommendations will contribute to the long-term success of their sustainability efforts.

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