EASIER CAPITAL RAISING WITH GREEN AND SUSTAINABLE LABELING

Green, Blue, and Sustainable Bonds: Key Definitions and the Labeling Process
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AsianBondsOnline Green Bond
Environment-Social-Governance

• Risk focus
• Looks at how ESG aspects flow through to financial risk
• Used to screen out investments with high ESG risks

Sustainable Finance

• Impact focus
• Looks at the positive impacts / credentials of investments in terms of sustainability
• Used to identify investments which are ready for the future
THE MANY FLAVORS OF SUSTAINABLE FINANCE: GREEN, SOCIAL, SUSTAINABLE, BLUE, GENDER, PANDEMIC, TRANSITION…

**Environmental Focus**
- Green
- Climate
- Blue
- Transition

**Social Focus**
- Pandemic
- Education
- Essential services
- Employment

**Sustainability Focus**
- Green + Social = Sustainable
- Sustainable Development Goals (SDGs)

**Instruments**
- Bonds
- Loans
- Sukuk
- ABS
- RMBS
- Funds
- ETFs
- Indices
LABELLING OF TRANSACTIONS IS A SUBSTANTIAL PROCESS

Outline of the Labelling Process

Overview → Identifying Green Projects and Assets → Developing a Green Bond or Sustainable Finance Framework → Confirming Internal Processes and Controls → Reporting on Allocations and Green Credentials → Setting Up for Impact Reporting

Engaging the External Reviewer → Managing the External Review Process → Seeking Certification or Recognition → Media, Stakeholders, Indices, and Listings → Post-Issue Reporting and Disclosure → Further Issuance of Labelled Instruments

ADB has created a Green Bonds section on the Asian Bonds Online website. This includes 12 factsheets which step through the labelling process in detail. https://asianbondsonline.adb.org/green-bonds/index.html
THE FIRST THREE STEPS ARE FOCUSED ON INTERNAL WORK

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</tbody>
</table>
IDENTIFYING GREEN PROJECTS AND ASSETS

Projects, Assets, and Expenditures Eligible for Inclusion in a Green Bond

**Owned Projects and Assets**
- **Physical assets**: Existing and operational equipment, machinery, infrastructure, buildings, or land
- **Projects**: Equipment, machinery, infrastructure and/or buildings in construction, redevelopment, (e.g., upgrades, expansion); and similar asset-value creation or enhancement activity

**Financing Arrangements for Projects and Assets**
- Capital expenditure undertaken to increase the value and/or lifetime of the physical assets or projects
- Acquisition costs or purchase price for an entity (e.g., company, division or similar)
- Long leaseholds on land, buildings, and infrastructure; or leasing structures resulting in right-of-use assets and liabilities
- Loans and mortgages
- Subsidies, taxes and other incentives, credit schemes and grants, and other similar arrangements provided by public entities or agencies, including local and national governments

**Related and Supporting Expenditures**
- Relevant installation and routine maintenance expenditure and upgrades undertaken to maintain the value and/or lifetime of the asset
- Relevant performance monitoring costs with respect to tracking climate credentials (e.g. GHG emissions) and climate information services
- Relevant research and development, training, and program implementation costs and expenditures
# SELECTING AN APPROPRIATE SET OF GREEN DEFINITIONS

## Current Options for Green Definitions

### Green Bond Principles
**High Level List**
- Very broad range of high level categories for green projects & assets
- Seen as the minimum level of green ambition
- Further explanation of green credentials is usually included by issuers

### ASEAN Green Bond Standard
- Adopted in 2017 and updated in 2018 by the ASEAN Capital Markets Forum
- Uses high-level list from Green Bond Principles
- Additional condition that fossil fuel power generation projects must be excluded
- Issuers must have a geographic or economic connection to ASEAN

### National or Regional Taxonomies or Guidelines (e.g., the PRC, Japan, Indonesia)
- The PRC has a Green Project Catalogue (updated in 2020).
- Japan has Green Bond Guidelines (updated in 2020).
- Other ASEAN countries are looking to develop locally relevant taxonomies.

### Climate Bonds Initiative Taxonomy
- Most commonly used international set of definitions with a focus on climate
- Used by most green bond index providers and adopted by some external reviewers
- Also has sector-specific criteria that are used for certification under the Climate Bonds Standard

### European Union’s Sustainable Finance Taxonomy
- Very complex approach with additional checks beyond just green credentials
- Will be expanded beyond climate issues to deal with other sustainability topics
- May be necessary for green bond issuers to clarify alignment if they are looking to issue their bond in an EU jurisdiction or attract investors from the EU

## Key Considerations for Choosing a Set of Green Definitions

### Labelling Requirements in the Jurisdiction Where the Issuance Will Occur
- Some jurisdictions require issuers of labeled bonds to follow very specific regulations and approval pathways (e.g., the PRC).
- Other jurisdictions have voluntary guidelines that add to investor confidence.

### Markets and Investors Being Targeted for the Bond Issuance
- If the issue is targeting local investors, then local definitions are usually enough.
- For international investors, it may be necessary to use international definitions.

### Locations of the Green Projects & Assets
- The relevant jurisdictions may have specific green definitions that need to be used.
- Definitions used in advanced economies may not be relevant for other markets, especially emerging markets in Asia.

### Types of Green Projects & Assets Available to the Green Bond Issuer
- Green projects and assets can use definitions with more green ambition.
- Some sectors or subsectors are not covered by existing taxonomies.

### Investor and Market Perspectives on the Level of Ambition of Green Definitions
- Some investors are concerned that definitions with low ambition are riskier from a greenwashing perspective.
- Most investors are comfortable with the Green Bond Principles’ high-level list with extra exclusions for fossil fuel sectors.
SELECTING AN APPROPRIATE SET OF GREEN DEFINITIONS

CREATING THE LIST

The issuer needs to prepare documents and internal procedures to do the following:

- Identify the green projects and assets that are proposed to be associated with the green bond and that have been assessed as likely to be eligible;

- Establish a list of green projects and assets that can be kept up-to-date during the full term of the green bond;

- Establish, document, and maintain a decision-making process to determine the eligibility of the green projects and assets in the list; and

- Establish, document, and maintain a process to identify and manage potentially material social and environmental risks associated with the projects.
# DEVELOPING GREEN BOND OR SUSTAINABLE FINANCE FRAMEWORK

## GREEN BOND FRAMEWORK

| A | A statement on the green objectives of the green bond; |
| B | How the green objectives of the green bond are positioned within the context of the issuer’s overarching objectives, strategy, policy and/or processes relating to environmental sustainability; |
| C | Confirmation that the bonds that will be issued under the green bond framework are aligned with one or more established approaches to labelling. This may include statements of alignment with applicable standards such as the Green Bond Principles, the Association of Southeast Asian Nations Green Bond Standards, the Climate Bonds Standard, or local or regional regulations or guidelines; |
| D | A summary of the green projects and assets that will be associated with the green bond such as sectors covered or geographic distribution; |
| E | The list of proposed green projects and assets associated with the green bond (if this is available and/or can be disclosed prior to issuance of the green bond); |
| F | A description of the decision-making process that has been used to select the green projects and assets; |
| G | A summary of the approach to the management of unallocated proceeds from the green bond and the expected timeline for green bond proceeds to be fully allocated; |
| H | An estimate of the share of the green bond proceeds that will be used for financing new green projects and assets and the share used for refinancing existing green projects and assets, including the relevant green projects and assets or investment areas that may be refinanced and how long since those green projects and assets were originally financed; and |
| I | The intended approach to providing update reports while the green bond remains outstanding. |
**DOCUMENTATION OF PROCEDURES**

**Selection of green projects and assets**

The selection process determines whether the green projects and assets meet the relevant eligibility requirements of the chosen set of green definitions or taxonomy. This should include any green standards or certifications referenced in the selection criteria. It can also refer to exclusion criteria or any other process applied to identify and manage potentially material environmental, social, or governance risks associated with the projects and assets.

**Management of the green bond proceeds**

These need to cover three key aspects with respect to management of proceeds:

- **Tracking of proceeds**
  The proceeds of the green bond can be credited to a subaccount, moved to a sub-portfolio (often called “ring-fencing” of proceeds), or otherwise tracked by the issuer in an appropriate manner and documented (often called “earmarking” of proceeds).

- **Earmarking funds to green projects and assets**
  An earmarking process can be used to manage and account for funding to the green projects and assets and enables estimation of the share of the green bond proceeds being used for financing and refinancing.

- **Managing unallocated proceeds**
  The balance of the green bond proceeds that have not yet been allocated to green projects and assets can be managed so that the proceeds are not being used for nongreen projects and assets. This usually involves holding cash or cash-equivalent instruments as part of a broader Treasury function.

**Reporting on allocations, eligibility, and impact**

This refers to processes to bring together all of the relevant information and provide robust reports for internal and external audiences. See further details on reporting in Factsheet 11.
REPORTING IS A KEY FOCUS FOR POTENTIAL INVESTORS AND OTHER STAKEHOLDERS

Reporting on Allocations and Green Credentials
• Two approaches to allocation of proceeds
• Satisfying Green Eligibility Requirements
• Investor and Market Expectations
• Reporting Formats and Channels

Setting Up for Impact Reporting
• Output–Outcome–Impact Frameworks
• Examples of Impact Indicators
• Ex-Post versus Ex-Ante Reporting
• Data and Systems
Approaches to Allocation of Proceeds

**Ringfencing.** This occurs when the issuer decides to separate the proceeds from its business-as-usual operations by putting the proceeds into a specific subaccount or sub-portfolio. For instance, ring-fencing could happen when a portfolio of solar farms is being financed and the proceeds are held in a special purpose vehicle for each of the wind farms.

**Earmarking.** The proceeds enter the balance sheet of the issuer and are matched up, or “allocated,” to the issuer’s list of green projects and assets so that the proceeds are “tracked by the issuer in an appropriate manner”. There is no segregation of proceeds in separate subaccounts. This is common practice among issuers of green bonds (including sovereign issuers) and is widely used to finance future capital investment or to refinance investments in longer-term projects.
**Example 1.** Commercial buildings under Climate Bonds Taxonomy are defined as being in the top 15% of the buildings in that city in terms of greenhouse gas performance per square meter of net lettable area. The Green Bond Principles’ high-level categories have no thresholds for green buildings, so the issuer can choose any approach to eligibility, such as “better than building code” or “20% better than average.”

**Example 2.** Hydropower is a source of renewable energy, but is also controversial for many investors based on the social and environmental impacts of hydropower development. Under the ASEAN Green Bond Standard, all renewable energy is eligible; while under the Climate Bonds Standard, there are substantial requirements for hydropower assets. Furthermore, under the Climate Bonds Standard, any hydropower asset must meet a threshold based on its greenhouse gas emissions footprint as well as undergo a site-specific assessment using the Environmental, Social, and Governance Gap Analysis Tool.
EXAMPLES OF IMPACT INDICATORS

Examples of the impact indicators for green projects and assets include the following:

**Renewable energy**
- energy capacity installed
- electricity generated
- greenhouse gas emissions reduced or avoided
- number of households provided with access to clean power

**Green buildings**
- greenhouse gas emissions performance of buildings
- certifications under recognized building rating systems

**Clean transportation**
- number of passengers carried by public transport
- number of electric vehicles manufactured
- reduction in number of cars required due to public transport options being available

**Sustainable water infrastructure**
- volume of wastewater treated
- number of new access points for clean water
- decrease in water use from investments in better water management assets
EXTERNAL REVIEW IS A KEY STEP IN THE LABELLING PROCESS

Engaging the External Reviewer
- Scoping Out What You Need
- Engagement Contracts
- Pre-Issuance and Post-Issuance Assessments
- Pricing and Timing Expectations

Managing the External Review Process
- Sharing Information with the External Reviewer
- External Review Procedures
- Draft Reports and Close-Out Processes
- Form and Use of Final Reports

Seeking Certification or Recognition
- Investor and Market Expectations
- International versus Regional versus National Approaches
- Pathways for Recognition
- Key Decision Points
## SCOPING OUT WHAT YOU NEED

### THE FOUR TYPES OF EXTERNAL REVIEW

<table>
<thead>
<tr>
<th>Type</th>
<th>What is it:</th>
<th>Who does it:</th>
<th>Pros</th>
<th>Cons</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Second Party Opinion (SPO)</strong></td>
<td>Report from a specialized consultant which provides an opinion on the framework, the bond’s label and the issuer’s sustainability/green narrative.</td>
<td>CICERO, Sustainalytics, Vigeo Eiris, ISS-oekom, DNV GL, etc.</td>
<td>- Most commonly used approach in the market.</td>
<td>- Only provides a check prior to the bond issuances.</td>
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<td></td>
<td>- Confirm alignment with the GBPs.</td>
<td>- No follow up after issuance and allocations have occurred.</td>
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<td>- Well accepted across the spectrum of investors.</td>
<td>- Many different approaches used by firms, including proprietary</td>
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<td>methods and assessment frameworks.</td>
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<td><strong>Certification:</strong></td>
<td>Formal endorsement of the bond’s credentials and consistency with national/regional regulations or an accepted standard. Requirements are clearly stated in the standard or relevant regulations.</td>
<td>Approved verifiers, such as under Chinese regulations, EU structures, or CB’s list.</td>
<td>- Includes a formal independent check prior to and after the issuance and allocation of proceeds.</td>
<td>- Less flexible due to clear and specific requirements, rather than guiding principles.</td>
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<td>- Confirms alignment with a transparent standard.</td>
<td>- May not cover all green assets due to limited set of detailed criteria which are currently available.</td>
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<tr>
<td><strong>Verification / Assurance:</strong></td>
<td>Report from an assurance provider which provides a formalised assurance statement on the labelled bonds alignment with the issuer’s stated approach, which may include external criteria.</td>
<td>Audit firms, EY, Deloitte, KPMG, etc. Often linked with other audit services for the issuer.</td>
<td>- More formalised approach to assessing the situation and providing an opinion than SPO.</td>
<td>- The criteria used for the assessment are defined by the issuer, rather than an external standard.</td>
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<td>- Often confirms alignment with the GBPs.</td>
<td>- Reports often provide very little detail.</td>
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<td>- Leverages existing audit relationships.</td>
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<tr>
<td><strong>Scoring/Rating:</strong></td>
<td>Report from a ratings agency or specialised firm which scores the issuer’s framework or bond against an established range. Usually involves proprietary methods and datasets for the assessment.</td>
<td>S&amp;P Ratings, Moody’s Sustainalytics</td>
<td>- Often confirms alignment with the GBPs.</td>
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<td>- Leverages existing credit rating or ESG scoring relationships.</td>
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<td>- Provides a score within a range, rather than binary.</td>
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<td></td>
<td>- The criteria used and the scoring methods are proprietary</td>
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<td>- Service is often expensive compared to other external review options.</td>
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<td></td>
<td></td>
<td>- Usually just pre-issuance, with no follow up.</td>
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Maturity of the issuer’s green bond framework and internal processes
- If this is the issuer’s first green bond, then the framework and processes may need further refinement prior to finalization. This takes more time and consumes billable hours for the external reviewers.
- A more mature situation is likely to have all of the supporting information and evidence that the external reviewer needs to work quickly.

Complexity of the portfolio of green projects & assets, including eligibility assessments according to thresholds or criteria
- A simple situation with one or two types of green projects and assets where the eligibility is very obvious will minimize costs and timelines.
- A very complex portfolio with a large number of different projects and assets, where eligibility must be demonstrated via ongoing performance or expert analysis, will result in much higher costs and longer timelines.

Hourly rate of the external reviewers undertaking the work
- Some external reviewers have very reasonable hourly rates for the work they do, particularly when local providers are being used by local issuers.
- Some external reviewers have high hourly rates, even for very junior staff, which creates much higher total costs for the services provided.
MANAGING AN EXTERNAL REVIEW PROCESS

EIGHT STEPS FOR AN EXTERNAL REVIEW, FROM THE ISSUER’S PERSPECTIVE

1. The issuer provides its package of key documents and access to relevant people for interviews, usually based on an information request from the external reviewer.

2. The external reviewer assesses the readiness of the issuer and the proposed bond to meet all of the nominated requirements (e.g., Green Bond Principles, Association of Southeast Asian Nations Green Bond Standards, or Climate Bonds Standard, among others).

3. The external reviewer conducts desk-based review of documents, interviews with relevant people from the issuer, confirmation of assertions based on external sources (e.g., government approvals, satellite imagery), follow-up questions, and clarification on specific topics. Procedures can also include site visits to specific projects and assets, but this is not very common.

4. The external reviewer prepares a checklist or template that the external reviewer uses to document its findings.

5. The external reviewer provides a draft report to the issuer, who then provides feedback on the preliminary findings and any further information or clarification required.

6. The issuer and external reviewer have a close-out call (see further details below).

7. The external reviewer finalizes the report and provides it to the issuer.

8. The issuer provides the external reviewer’s report to the potential investors and other stakeholders, such as regulators or certification systems, prior to issuance of the green bond.
APPROACHES TO RECOGNITION OR CERTIFICATION OF A GREEN BOND

VARIOUS APPROACHES AROUND THE WORLD AND AT DIFFERENT LEVELS OF COVERAGE.

GLOBAL APPROACHES:
Green Bond Principles, Climate Bonds Initiative

REGIONAL APPROACHES:
ASEAN Green Bond Standard, EU Green Bond Standard

NATIONAL APPROACHES:
People’s Republic of China, Japan, India, Indonesia, Mexico, South Africa, etc
**PATHWAYS FOR RECOGNITION**

**CASE STUDIES FOR SELECTING PATHWAYS FOR RECOGNITION**

**SITUATION**
- Solar company with portfolio of solar assets in India issues a USD-denominated bond for refinancing
- Municipality in an Association of Southeast Asian Nations (ASEAN) member country issues a Sukuk (Islamic bond) in the local currency to finance flood defenses
- Property development company with green buildings in a multiple ASEAN cities issues a bond in the local currency
- Bank based in the People’s Republic of China (PRC) with a wide-ranging green loan portfolio in multiple countries issues a benchmark bond in euros and United States dollars
- Australian food producer adopting sustainable practices across its operations issues a bond in Japanese yen

**KEY CONSIDERATION**
- USD-denominated issuance will attract international investors; simple and obviously green assets make it easier to use best practices
- Currency and structure likely to focus on local investors; Projects are aligned with the ASEAN requirements (i.e., location, no fossil fuels)
- Local currency issuance will attract mostly local investors; projects are aligned with ASEAN requirements (i.e., location, no fossil fuels)
- All PRC-based issuers need approvals from domestic regulators to use the green label; scale and currency will attract mainstream international investors
- Japanese yen issuance will attract international investors; complex mix of green projects means that detailed criteria and thresholds do not yet exist

**RECOGNITION PATHWAY**
- Certification under the Climate Bonds Standard
- Conformance with ASEAN Green Bond Standard
- Conformance with ASEAN Green Bond Standard
- PRC regulatory requirements, plus certification under the Climate Bonds Standard
- Alignment with Green Bond Principles
AFTER ISSUANCE THE FOCUS IS ON HARVESTING THE ONGOING BENEFITS

Media, Stakeholders, Indices, and Listings

• Building Momentum
• Media Formats and Channels
• Index Inclusion
• Listing Platforms

Post-Issuance Reporting and Disclosure

• Allocations Reporting
• Eligibility Reporting
• Impact Reporting
• Reporting Formats and Channels

Further Issuance of Labelled Instruments

• Strong Investor Appetite
• Green, Social, and Sustainable Portfolios
• Tracking the Stacks
• Efficiencies and Transaction Costs
**UNITED NATIONS SUSTAINABLE STOCK EXCHANGE INITIATIVE MEMBERS AMONG ASEAN+3 STOCK EXCHANGES**

<table>
<thead>
<tr>
<th>Stock Exchange</th>
<th>Economy</th>
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<tbody>
<tr>
<td>Hong Kong Exchanges and Clearing Limited</td>
<td>People’s Republic of China</td>
</tr>
<tr>
<td>Shanghai Stock Exchange</td>
<td>People’s Republic of China</td>
</tr>
<tr>
<td>Shenzhen Stock Exchange</td>
<td>People’s Republic of China</td>
</tr>
<tr>
<td>Indonesia Stock Exchange</td>
<td>Indonesia</td>
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<tr>
<td>Japan Exchange Group</td>
<td>Japan</td>
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<tr>
<td>Korea Exchange</td>
<td>Korea, Republic of</td>
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<tr>
<td>Bursa Malaysia</td>
<td>Malaysia</td>
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<tr>
<td>Philippine Stock Exchange</td>
<td>Philippines</td>
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<td>Singapore Exchange</td>
<td>Singapore</td>
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<td>Stock Exchange of Thailand</td>
<td>Thailand</td>
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<tr>
<td>Hanoi Stock Exchange</td>
<td>Viet Nam</td>
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<tr>
<td>Ho Chi Minh Stock Exchange</td>
<td>Viet Nam</td>
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</tbody>
</table>
POST-ISSUANCE REPORTING REQUIREMENTS

ALLOCATION REPORTING

The allocation reporting part of the update report should include the following:

- confirmation that the green bond is aligned with one or more established approaches to labeling, including statements of alignment with other applicable standards such as the Green Bond Principles, the ASEAN Green Bond Standard, the Climate Bonds Standard, domestic regulations in the People's Republic of China, Japanese Green Bond Guidelines, or other approaches;
- a statement on the objectives of the green bond;
- the list of green projects and assets to which proceeds have been allocated (or reallocated);
- the amounts allocated to the green projects and assets;
- an estimate of the share of the green bond proceeds used for financing and refinancing, which green projects and assets have been refinanced, and the look-back period for refinanced projects and assets; and
- the geographical distribution of the green projects and assets.

ELIGIBILITY REPORTING

The eligibility reporting part of the update report should include the following:

- confirmation that the green projects and assets continue to meet the relevant eligibility requirements that are described in the green bond framework; and
- information on the environmental characteristics or performance of green projects and assets that is relevant to the eligibility requirements.
The impact reporting part of the update report (if it covers impact reporting) should include the following:

- expected or actual outcomes or impacts of the green projects and assets with respect to the objectives of the green bond;
- qualitative performance indicators and, where feasible, quantitative performance measures of the outcomes or impacts of the green projects and assets; and
- methods and the key underlying assumptions used in preparation of the performance indicators and metrics.
Different Approaches to Tracking Green Bonds and Green Projects

**Individual Green Bonds are aligned with specific Green Projects**

**All Green Bonds are aligned with the entire portfolio of Green Projects**

- **Legend:**
  - Bond 1
  - Bond 2
  - Bond 3
  - Project 1
  - Project 2
  - Project 3
  - Project 4
  - Project 5
  - All Projects
THERE HAVE BEEN THOUSANDS OF ISSUANCES FROM MANY COUNTRIES SO THERE IS INCREASING UNDERSTANDING OF HOW TO DO IT WELL

**Key lessons from labelling experience to date**

1. Labelling a bond / loan / sukuk / etc is essentially a marketing tool so it should be aligned with other branding and messaging to have maximum effect.

2. Transparency is what investors want and expect from sustainable finance products, both before the transaction and from the ongoing reporting.

3. This green / sustainable / ESG trend is not going away.

4. Pricing benefit is possible but other benefits dominate for issuers and borrowers.

5. Almost all treasurers who label a transaction want to figure out how to do another.
FREQUENTLY ASKED QUESTIONS FROM ISSUERS

- How much does it cost?
- What are the benefits in terms of cost of capital?

- How much time will it take to prepare everything?
- Will it distract the deal team from the core objective of capital raising?

- Will I get my name in the newspaper / industry news?
- Will my kids think I am awesome for trying to save the planet?

- What are the risks?
- What happens if it goes badly?

- Is this new focus on green and sustainable really going to last?
THANK YOU

FOR FURTHER INFORMATION:

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