Sustainable deals methodology 2024

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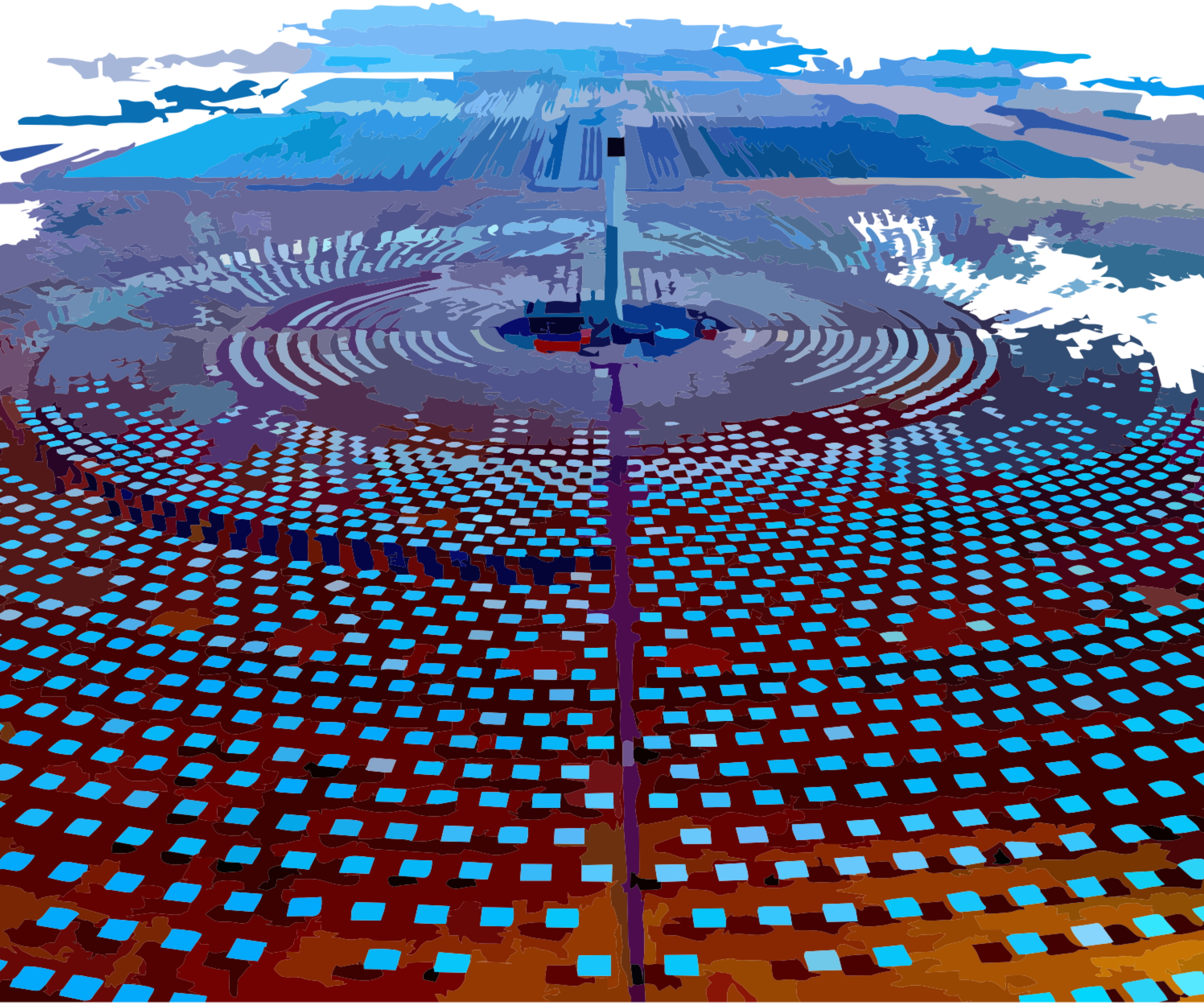

Part of Exile Group

Deal types and sustainability tiers

TXF and its parent the Exile Group are committed to conducting business in as responsible and sustainable a manner as possible. We also try wherever possible to highlight responsible, ethical and sustainable best practice in the markets that we cover.

In 2018 we began tracking sustainable deals. Several initiatives are underway in both the markets we cover and the wider financial community to develop standardised methodologies for classifying sustainable financings. However, since there is as yet no single standardised methodology, TXF and Exile have endeavoured to put together a classification system that is simple, transparent, and meets the needs both of our users and the individuals and institutions that contribute to our data.

At the heart of this system lies the distinction between core sustainable deals, and deals with a sustainable element

1. Core sustainable deals

The top tier of sustainable deals comprises green and social deals, and for which our methodology has not undergone any substantial changes. This allows us to keep our dataset consistent over the period since we started tracking these deals, allowing us to track market trends accurately. These will use our existing taxonomy, which is outlined on the next page.

2. Sustainability-linked deals

In addition to core green and social deals, where the asset being financed has demonstrable positive social and environmental impacts, transactions that help reduce negative impacts are becoming more popular, both in the export finance market and wider financial markets. These deals will not necessarily meet green or social criteria, but should have a positive impact and can deserve recognition. These are deals where the borrower agrees to meet specified green or social targets even if the borrower will not own or be building or buying green or social assets.

3. Impact mitigation deals

Deals where the proceeds will allow the borrower to achieve a significant improvement in its environmental or social performance even if its assets are not of themselves environmentally or socially friendly and the borrower has not set itself KPIs for improvement.

How we classify core sustainable deals

Our methodology for recognising core sustainable deals draws on the green and social loan principles that have been developed by the Loan Market Asocciation. We will look for deals with the following characteristics:

- a deal that has a positive impact on the environment (green), or
- has a positive impact on the community to improve their quality of life (social)

Although green and social bonds usually feature some sort of third-party verification or certification, we will not initially require evidence of that certification. We will, however, need a detailed explanation from a deal participant if it is not evident that the deal qualifies as green or social. We do this by offering market participants an opportunity to verify deals after they have received a preliminary classification. Participants can simply confirm they are happy with the classification or request that it is changed., but this change needs to be verified from someone in charge of the sustainability function within the submitter’s company (typically the sustainable debt desk). We follow the LMA green and social principles taxonomy for this.

Green eligibility

Eligible green deals

We follow the LMA classification for green deals, which covers the following uses of proceeds:

- Renewable energy (including production, transmission, appliances and products)
- Energy efficiency (such as in new and refurbished buildings, energy storage, district heating, smart grids, appliances and products)
- Pollution prevention and control (including reduction of air emissions, greenhouse gas control, soil remediation, waste prevention, waste reduction, waste recycling and energy/emission-efficient waste to energy)
- Environmentally sustainable management of living natural resources and land use (including environmentally sustainable agriculture; environmentally sustainable animal husbandry
- Climate smart farm inputs such as biological crop protection or drip-irrigation; environmentally sustainable fishery and aquaculture; environmentally-sustainable forestry, including afforestation or reforestation, and preservation or restoration of natural landscapes)
- Clean transportation (such as electric, hybrid, public, rail, non-motorised, multi-modal transportation, infrastructure for clean energy vehicles and reduction of harmful emissions)
- Terrestrial and aquatic biodiversity conservation (including the protection of coastal, marine and watershed environments)
- Sustainable water and wastewater management (including sustainable infrastructure for clean and/or drinking water, wastewater treatment, sustainable urban drainage systems and river training and other forms of flooding mitigation);
- Climate change adaptation (including information support systems, such as climate observation and early warning systems)
- Eco-efficient and/or circular economy adapted products, production technologies and processes (such as development and introduction of environmentally sustainable products, with an eco-label or environmental certification resource-efficient packaging and distribution)
- Green buildings which meet regional, national or internationally recognised standards or certifications

The table below provides an alternative means of classifying green deals with broader categories.

Green categories	
Category code	**Category name**
GL1	Renewable energy
GL2	Energy efficiency
GL3	pollution prevention and control
GL4	Natural resources & land sustainable management
GL5	Biodiversity conservation
GL6	Clean transportation
GL7	Sustainable water and wastewater
GL8	Climate change adaptation
GL9	Eco-efficient and/or circular economy adapted products
GL10	green buildings

Social eligibility

Eligible social deals

Social project categories also follow the classification used by the LMA. These include, but are not limited to, providing and/or promoting:

- Affordable basic infrastructure (e.g. clean drinking water, sewers, sanitation, transport, energy)
- Access to essential services (e.g. health, education and vocational training, healthcare, financing and financial services)
- Affordable housing
- Employment generation, and programs designed to prevent and/or alleviate unemployment stemming from socioeconomic crises, including through the potential effect of SME financing and microfinance
- Food security and sustainable food systems (e.g. physical, social, and economic access to safe, nutritious, and sufficient food that meets dietary needs and requirements; resilient agricultural practices; reduction of food loss and waste; and improved productivity of small-scale producers)
- Socioeconomic advancement and empowerment (e.g. equitable access to and control over assets, services, resources, and opportunities; equitable participation and integration into the market and society, including reduction of income inequality) Examples of target populations include, but are not limited to, those that are:

    1. Living below the poverty line
    2. Excluded and/or marginalised populations and /or communities
    3. People with disabilities
    4. Migrants and /or displaced persons
    5. People with disabilities
    6. Migrants and /or displaced persons
    7. Undereducated
    8. Underserved, owing to a lack of quality access to essential goods and services
    9. Unemployed
    10. Women and/or sexual and gender minorities
    11. Aging populations and vulnerable youth
    12. Other vulnerable groups, including as a result of natural disasters

Several of the objectives classed as social, including employment generation and affordable infrastructure, are very broad, and we are likely to look at more specific social objectives when classifying a deal as social.

The table below provides the broad categories for classifying social deals.

Social categories	
Category code	**Category name**
SL1	Affordable basic infrastructure
SL2	Access to essential services (health, education…)
SL3	Affordable housing
SL4	Employment generation & SME support
SL5	Food security & sustainable food systems
SL6	Socioeconomic advancement to vulnerable groups

Sustainability-linked deals

Eligible sustainability-linked deals

A sustainability-linked deal typically involves a borrower agreeing to take specified actions that will lead to green or social improvements. According to the LMA methodology, eligible deals should use the following process:

- Selection of key performance indicators (KPIs)
- Calibration of sustainability performance targets (SPTs)
- Deal characteristics
- Reporting
- Verification

Reporting and verification cannot be covered by a database of closed deals, though we will assume that lenders, trustees or agents are doing it over the life of the loan. But we will review KPIs, SPTs and deal characteristics.

Selection of KPIs

The ICMA considers that KPIs should be:

1. relevant, core and material to the issuer's overall business, and of high strategic significance to the issuer's current and/ or future operations;
2. measurable or quantifiable on a consistent methodological basis;
3. externally verifiable; and
4. able to be benchmarked, i.e. as much as possible using an external reference or definitions to facilitate the assessment of the SPT's level of ambition.

Calibration of Sustainability Performance Targets (SPTs)

Every KPI should have at least one SPT attached to it, and according to the IMCA The SPTs should be ambitious, i.e.:

1. represent a material improvement in the respective KPIs and be beyond a "Business as Usual" trajectory;
2. where possible be compared to a benchmark or an external reference;
3. be consistent with the issuers' overall strategic sustainability / ESG strategy; and
4. be determined on a predefined timeline, set before (or concurrently with) the deal closure.

Deal characteristics

Sustainability-linked deals must have financial or structural impact if a borrower misses its targets. This can be achieved by adjustments to the tenor, interest rate, distribution tests, etc. that disadvantage the borrower and should be substantial enough to discourage borrowers from deliberately missing them.

Impact mitigation deals

How we identify impact mitigation financings

There will be examples of transactions that do not qualify for green or social labelling, and whose impact cannot be captured using sustainably-linked KPIs, but which can have a beneficial environmental or social impact. These may include transactions for borrowers with high existing direct or indirect carbon footprints, or borrowers in a business whose social or environmental impacts are still a matter of debate.

Examples of such transactions might include deals where the borrower's business or the project involve:

- Developing the capability of using more sustainable fuel sources (e.g. Dual fuel ships)
- Substantially improving emissions from particular asset types (for instance by installing scrubbing technology on power plants or ships, or carbon capture and storage)
- Building facilities that will allow for the production or transportation of clean energy, but which may not be used exclusively for clean energy (Natural gas/hydrogen pipelines for example)
- Do not contribute to CO2 emissions but may feature additional environmental or social risks, whether by producing unwelcome waste products, or by having potential undesirable impacts on indigenous peoples or biodiversity (e.g. Nuclear, large hydro)

Eligible deals should be for assets that undergo significant improvements compared to the existing technologies that they use. But those improvements should not be carried out to meet mandatory targets from governments or regulators.

All deals classified as impact mitigation will be submitted by a participant, analysed on a case by case basis and eligibility will be discretionary, and always aligned with the technical standards of the EU taxonomy where applicable.

Submission and classification process

Depending on the category (green, social, sustainability-linked and climate impact mitigation) the information that we will require may be different. The tables at the bottom of pages 3 and 4 provide further detail on which industries and countries will be considered for eligibility as green or social if they meet the remaining requirements.

The process comprises the following steps:

1. Deal identification. In some cases, deals are automatically eligible (eg. renewables will almost always be classified as green) and no further details are needed. However, if the deal falls into the social, sustainability-linked or climate impact mitigation categories, it is recommended that submitters provide some evidence for their eligibility.

2. Deal review. We have access to outside experts in sustainability who can give us an opinion for deals that may not on first inspection fit into an eligible category, but where the information provided is sufficient to allow us to review them. In some cases, deals do not qualify for a certain category, while in others we may require additional information to help us make a decision. In those cases, we will request additional information from the submitter/s. We aim to be conservative and avoid accusations of greenwashing, so any deal that we cannot classify with confidence will be left out.

3. Provisional classification. Every submitter will receive a report with deal's provisional classification and we will give them the chance to make final representations about any deal before a set deadline.

4. Final classification and reporting: Once all classifications are resolved, the sustainable deals dataset will form the basis for a detailed report on the sustainable finance market.