



04.

TRANSITION FINANCE TOOLKIT



KEY TAKEAWAYS Chapter 4

Green Finance is now a core component of Climate Action and benefits from a strong impetus and legislative plans from policy-makers. The global Green/Sustainable/Social debt market reached \$1.192 trillion threshold as of December 2020.

Brown industries are still largely absent from the Green Bond market, which still focuses on green activities and players

- Investors are relatively less confident in predominantly and/or historically brown companies as they assess company's profile & strategy in addition to the Use-of-Proceeds.
- There is a lack of standards for activities in "grey areas" (whose "greenness" depends on observed performances like efficiency gains).

The EU Taxonomy tries to address the lack of standards for activities in grey areas

- Stringent thresholds can be fairly understood from the climate neutrality objective but could lead to a niche of eligible companies or assets.
- The level of stringency, combined with its binary nature (i.e., without shades) makes the acceleration of brown industries' transition difficult.

There is increasing investors' appetite for transition KPI-linked products that could include brown industries

The General Corporate Purpose model tied to a key performance indicator on which different financial mechanism could be built allows a more holistic and forward-looking approach of climate finance. UoP & General Corporate Purpose should not be opposed and can be complementary.

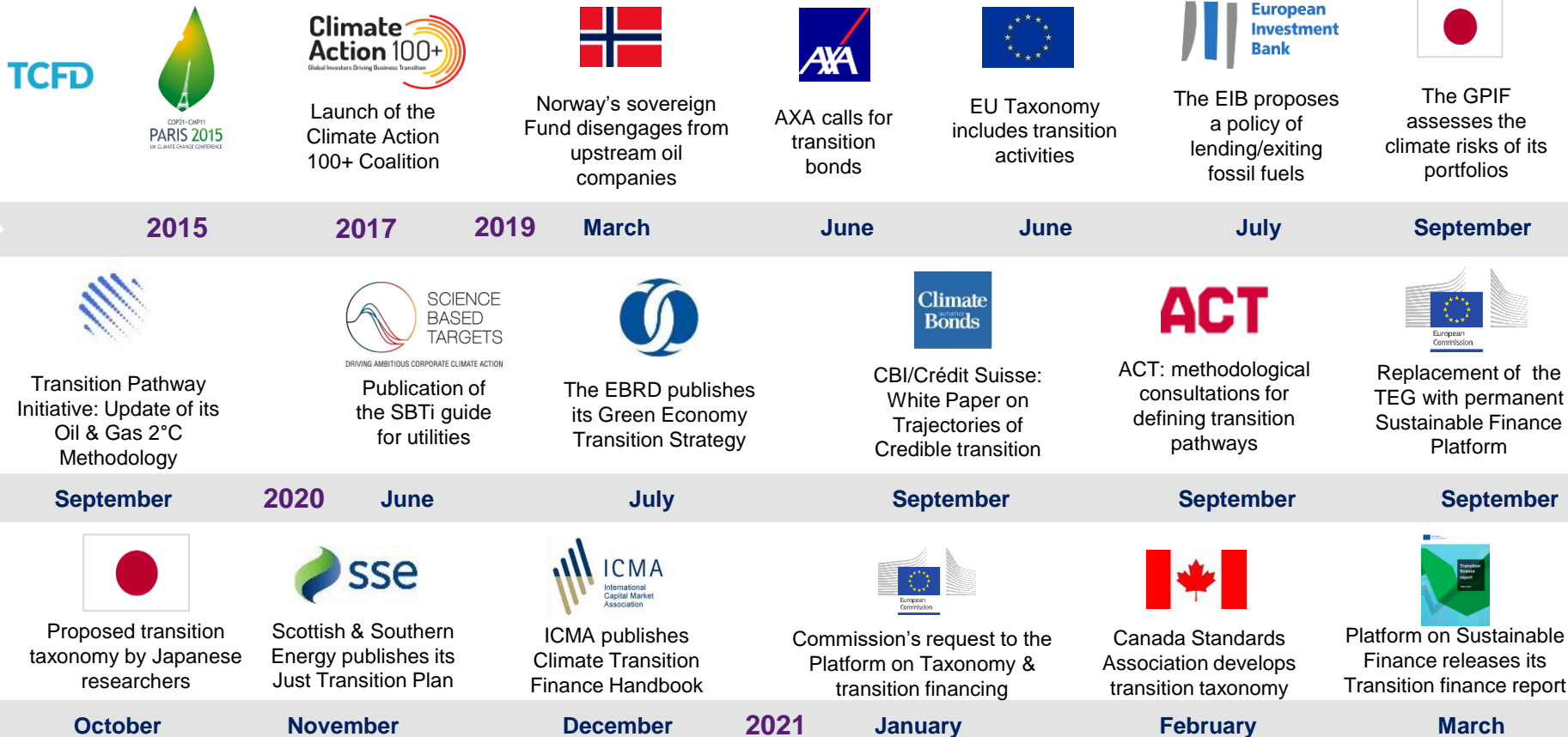
There is a new standard around Sustainability-Linked Bonds

The ICMA has launched guidelines on the disclosures that should be made by issuers when raising funds in debt capital markets (the "**Climate Transition Finance Handbook**").

Investors have willingness / appetite to invest in brown companies' transition, but without leniency and are open to new instruments (KPI-linked instrument), as shown in our Investors survey.

Source: Green & Sustainable Hub, Natixis

Strong momentum for transition finance



Self-labelled transition bond issuances

青山發電有限公司
Castle Peak Power Co. Ltd.

Castle Peak Power Energy Transition Bond
\$ 350M 10Y Energy Transition Senior
Unsecured Bond

Issue Date

25 July 2017
22 June 2020



SNAM Transition Bond
€ 500M 10Y Transition Senior Unsecured Bond

Issue Date

17 June 2020



EBRD Green Transition Bond
€ 625M 5Y Green Transition
Senior Unsecured Bond

Issue Date

17 October 2019



GRUPE
BPCE

BPCE Transition Bond
€ 100M 10Y Transition Senior Non-Preferred
Bond

Issue Date

9 December 2020



Marfrig Sustainable Transition Bond
€ 500M 10Y Sustainable Transition
Senior Unsecured Bond

Issue Date

6 August 2019



Your Gas Network

Cadent Transition Bond
€ 500M 12Y Transition
Senior Unsecured Bond

Issue Date

11 March 2020



中國銀行
BANK OF CHINA

Bank of China ICMA Handbook-Linked Dual
Tranche Transition Bond
\$ 500M 3Y Transition Senior Unsecured Bond
¥ 1.8B 2Y Transition Senior Unsecured Bond

Issue Date

7 January 2021

4.1 | THE EU TAXONOMY OF SUSTAINABLE ACTIVITIES

A decisive boost in reshaping mainstream finance & exiting the sustainable finance niche

A “**science-based dictionary**” defining what is unambiguously green setting disclosure requirements for **various actors** covering a **broad scope of activities** with 90 activities assessed for climate change mitigation, and 98 for adaptation (Draft Delegated Acts, Nov. 2020).

COVERAGE

- **Welcome coverage of high emitting sectors but criteria’s stringency** makes it only practicable for forerunner “brown companies”
- Need for an **intermediary level of green & a definition of criteria defining brown or “harm”**

USE & PURPOSE

- **Numerous uses** (*design of sustainable products, funds, financing programs or supervisors and central banks interventions*)
- **Purposes beyond financing or investing activities** (*public procurement requirements, industrial policies, etc.*)

CRITERIA

- **Demanding data collection** for activities’ conformity assessment
- Companies’ processes and information systems **reshuffle** needed to feed the metrics and produce compliance data/KPIs

FURTHER DEVELOPMENT

- Adaptation & mitigation criteria will be extended, **adjusted** and **refined** regularly.
- Criteria for contribution to other environmental objectives are to be **developed** by the future Sustainable Finance Platform

An evolving scheme with **interim periods** during which some actors – verifiers, auditing firms, banks – will play a key jurisprudential role until full completion of technical screening criteria.



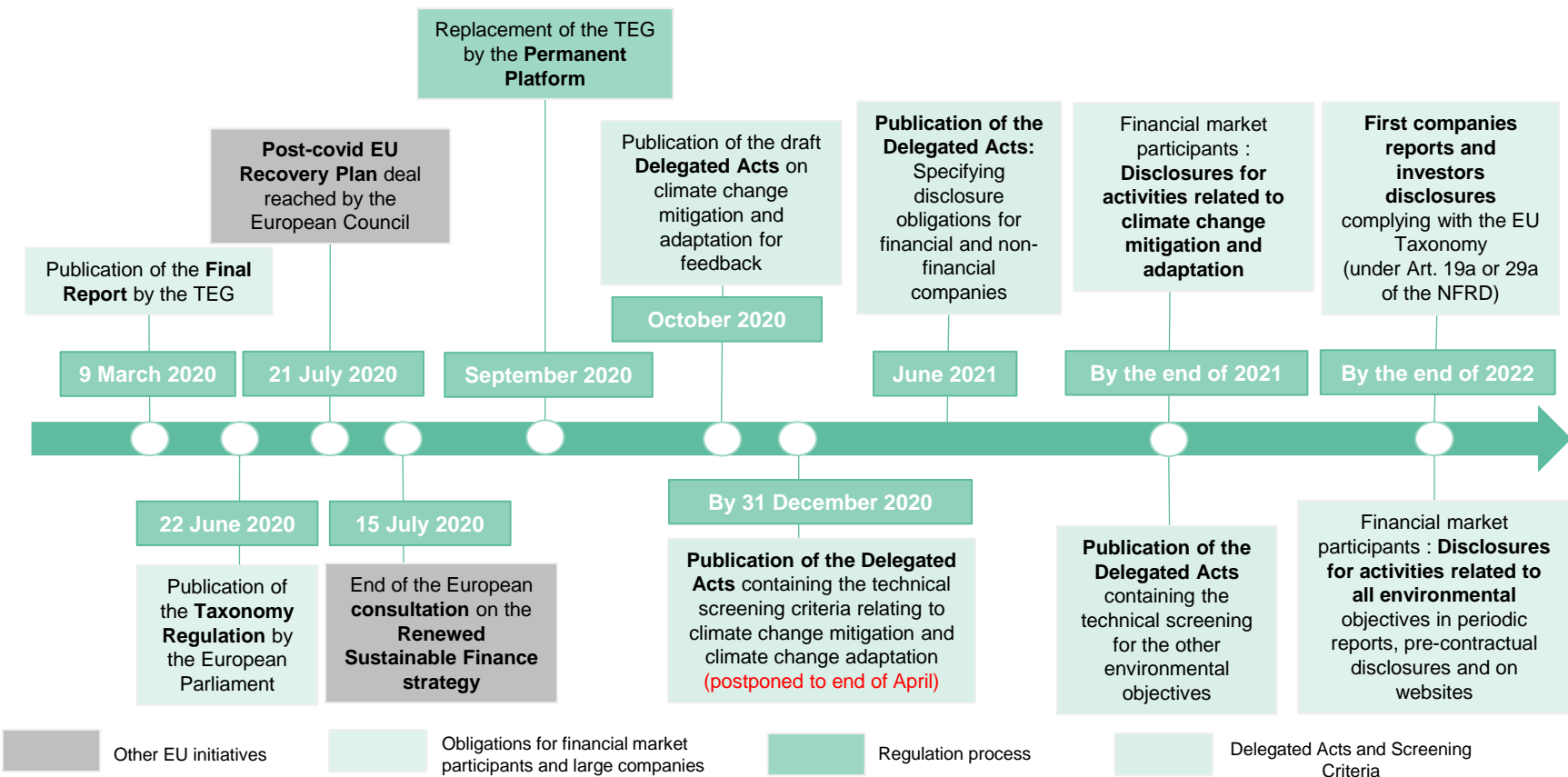
Entry into force in a very short lapse of time
First set of Taxonomy disclosures required by the end of 2021

- We invite actors **to seize the opportunities offered by the Taxonomy** and not to see it as a burdensome additional transparency requirement.
- A strategic use of the Taxonomy is possible for companies aiming at making their business models resilient to a carbon-constraint economy. Taxonomy KPI dashboards on revenues, CAPEX and R&D can be a compass in their transition journeys.
- In return, the policy-makers must closely monitor the (unintended) effects of the Taxonomy Regulation, be able to adjust, and feed their decisions with active feedback from market participants. Until now, transparency and dialogue have been remarkable.

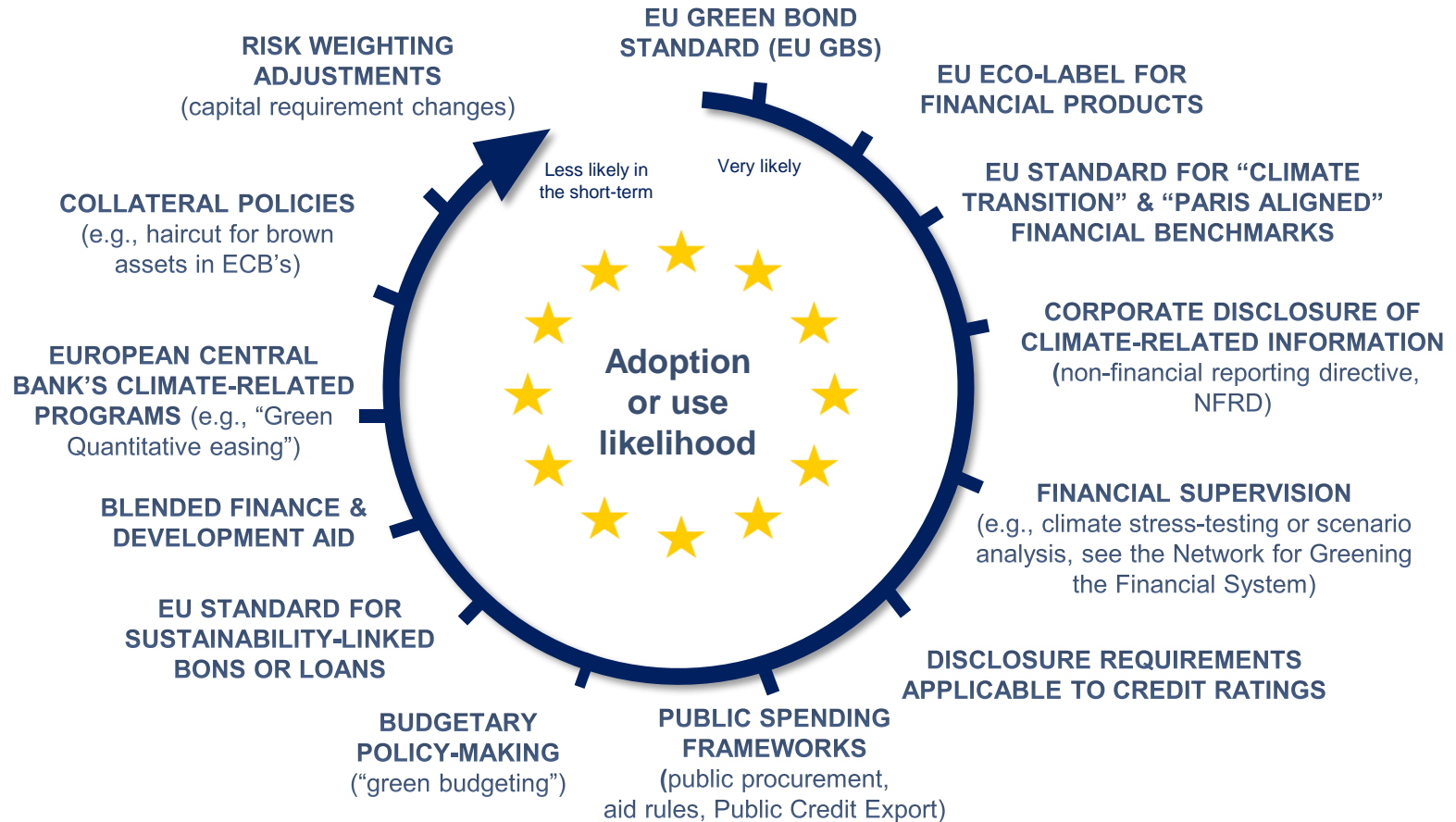


[Click here to see our dedicated report](#)

The EU Taxonomy Timeline: legislative process and entry into force



Overview of the potential and various uses of the Taxonomy



EU Sustainable Finance Platform's views on “transition finance”

The Taxonomy **entered into force in July 2020** and sets out different means by which economic activities can substantially contribute to that objective.

With regard to the objective of climate change mitigation, the Regulation explicitly defines “**transitional activities**” as those making a substantial contribution to environmental objectives within sectors where low-carbon alternatives are not yet available and thus caters in some respects for the need to support the transition. Transitional activities are considered sustainable to the extent that they meet clear requirements and support the transition to climate neutrality in line with EU climate objectives.

By June 1st, 2021, the Commission will adopt delegated acts setting out the content, presentation, and methodologies for complying with the disclosure requirements under Article 8 of the Taxonomy Regulation.

The Aim of the EU Platform on Sustainable Finance

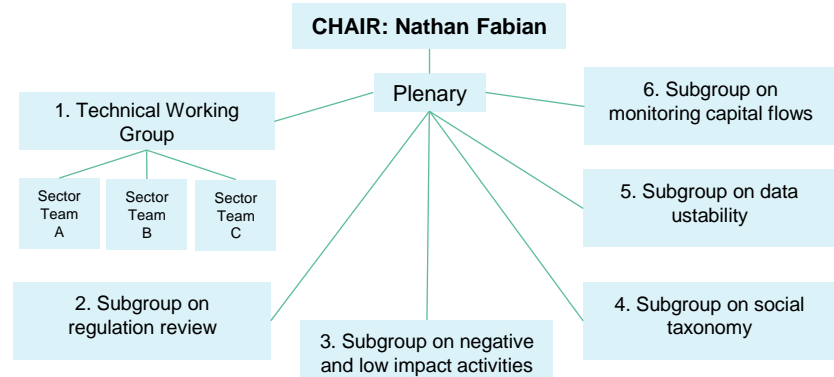
The platform is an **advisory body** subject to the Commission's **horizontal rules for expert groups**. Its main purpose is to **advise the European Commission on several tasks and topics related to further developing the EU Taxonomy** and support the Commission in the technical preparation of delegated acts, in order to implement the EU taxonomy.

Based on the mandate of the Platform in Article 20 Taxonomy Regulation, the members and observers started work on **four main tasks** to deliver key deliverables:

1. Advising the Commission on the **technical screening criteria** for the EU Taxonomy, including on the usability of the criteria
2. Advising the Commission on the review of the Taxonomy Regulation and on covering other sustainability objectives, **including social objectives and activities that significantly harm the environment**
3. **Monitoring and reporting** on capital flows towards sustainable investments
4. Advising the Commission on **sustainable finance policy** more broadly

The Platform's Organization

The Platform has, in principle, an unlimited duration, taking into account the different tasks provided for in the Taxonomy Regulation and the need to amend the technical screening criteria of the EU taxonomy over time, in order to reflect, for instance, changing EU environmental legislation or technological developments.



EU Sustainable Finance Platform's views on transition finance

The Request & Need for Advisory

In accordance with Article 20 of the Taxonomy Regulation, a platform is mandated to advise the European Commission in the evaluation and development of sustainable finance policies.

As part of their deliverables, the subgroups on negative and low-impact activities and on data and usability are each considering the applicability and use of the taxonomy to guide and incentivize the transition to a sustainable economy from different angles.

The expertise and preliminary findings of the Platform would therefore provide valuable input at this stage and could feed into the Commission's work on finalizing the delegated act on climate change objectives, the future Article 8 delegated act and the Renewed Sustainable Finance Strategy.

The Commission asked the platform on Sustainable Finance to provide advice on the existing and potential use of the EU taxonomy framework for enabling the financing of the transition towards a sustainable economy.

Given the fact that this matter is highly time sensitive, the request entails that the Platform provides its advice by mid-March 2021.

Members and observers in the platform

50 members selected from more than 500 applications

E.g.

- BNP Paribas
- Bloomberg
- Airbus
- Allianz
- ICMA
- Climate Bonds Initiative
- Global Reporting Initiative

7 members of public entities appointed through Article 20

- EEA
- EIB
- EIF
- EBA
- EIOPA
- ESMA
- FRA

10 invited observers

- EBRD
- ECB
- EFRAG
- EPA
- ESM
- NGFS
- OECD
- UNEP FI
- Cdp SpA

The Required Scope of Advice

The Platform was asked to provide answers to the following questions:

- Can the current EU taxonomy framework be used to provide **greater support for attracting capital for the transition of companies towards “sustainable” activities**, including in ways not yet proposed by the Commission and if so in which ways?
- Can the EU taxonomy framework **support finance for companies undertaking activities that do not yet meet**, or may be unable to meet, the substantial contribution criteria? And how can this be done?
- Can the current EU Taxonomy framework support **finance for companies active in sectors that are not covered in the Taxonomy Regulation's Delegated Act**?
- How does the use of key **terminology such as “sustainable”, “green” and “harmful” compare across the taxonomy framework** and other relevant sustainable finance frameworks and how can it be clarified and harmonized?
- What **further avenues** could be explored to enable financing the transition through **development of the taxonomy framework** and beyond?
- Can we clearly address the **concerns that the taxonomy will be used to prevent financing of transitional activities**, while at the same time ensuring that we are **not facilitating “green-washing”**?

The EU Sustainable Finance Platform's views on transition finance

Takeaways from the March 2021 report



[Click here to access the report](#)



Recommendations are divided into three groups:

1. Use other policies and tools | 2. Maximize the current Taxonomy | 3. Develop the future Taxonomy

Reminders:

- The Taxonomy in its current form describes which activities are green, without specifying those that are at risk of causing significant harm. It focuses on individual economic activities and is, therefore, more granular than “transition”.
- Taxonomy-reporting is mandatory for financial products that claim to either have an environmental objective or environmentally beneficial characteristics. The Taxonomy is useful for targeting, tracking and communicating progress.
- The EU Taxonomy contains criteria pertaining to specific activities carried out by companies. It is, therefore, not a classification of companies as such nor of their overall transition pathways.

Key proposals

- **Entity-level disclosure:** companies are encouraged to disclose their transition strategies and specify the role of the EU Taxonomy therein. Voluntary, forward-looking disclosures relating to taxonomy alignment can help to provide that longer-term vision.
- **Launch of a feedback loop:** stakeholders are given the opportunity to provide suggestions to the Platform on **what activities should be considered next** for inclusion in the Taxonomy and **whether criteria for existing activities should be revised**
- **Developing additional categories / criteria for activities with “no significant impact”** (little or no impact) and **“causing significant harm”** (identifying activities & performance levels that companies and financiers must move away from)
- **Going downstream in value chains:** currently, the technical screening criteria relate to either the final product (e.g., vehicles produced) or the production process (metals, cement) but it could include the downstream activities of the value chain (recognizing the contribution of the entire supply chain around taxonomy-aligned activities by financing, distributing, and selling of taxonomy-aligned products or services, or by providing critical materials to taxonomy-aligned activities)
- **Include activities that enable companies to stop performing significantly harmful activities** (through for instance decommissioning or closure)
- **Interim period & significant harm:** introduction of a phase-out trajectory from “Significant Harm” (SH) to progress towards the alignment with a “Substantial Contribution” (SC) over transition timeframes. Possibility to support significant improvements in performance of activities towards (but not reaching) the substantial contribution criteria)
- **Forward-looking activity-specific investment plan:** recognize activities that are part of an activity-specific investment plan to meet the Taxonomy criteria, through CapEx, OpEx and related finance (allowing companies to consider their investments as taxonomy-aligned)
- **Sustainability-linked Bonds:** the Taxonomy will also be attached to entity-level forward looking and holistic financial instruments, offering a comprehensive picture of companies' carbon neutrality strategies (taxonomy-related KPIs & SPTs).

INTERVIEW

BROWN INDUSTRIES' ROLE IN THE SUSTAINABLE FINANCE LANDSCAPE



CHRISTA CLAPP
Research Director, Cicero

°CICERO
Climate Finance

- “ If sustainable finance is limited to pure play green actors, we are not encouraging an economy-wide transition that is necessary to achieve the climate targets set out in the Paris Agreement. Traditional brown industries need to also be encouraged to play a role in the transition to low carbon, by making efficiency improvements and fuel-shifts that avoid locking-in fossil-based infrastructure.**
- “ Trillions of dollars are needed for infrastructure investments in the next decade, and if we ensure low-carbon climate resilient infrastructure decisions, we could save in damage costs from climate-related disasters. We need financing for all Shades of Green to solve the climate challenge.**
- “ Green bonds from oil companies are the most obvious controversial example. Key concerns include if the company is really planning a transition to a low-carbon future, and how they will avoid locking-in fossil fuel dependency.**
- “ Strong corporate governance is necessary to ensure that project selection and management are aligned with their ambitions for a green transition. Climate targets and procedures to support the achievement of those objectives within a corporation are important, in addition to environmental expertise and criteria being included in project selection and evaluation.**

The full interview is available here



INTERVIEW

BROWN INDUSTRIES' ROLE IN THE SUSTAINABLE FINANCE LANDSCAPE



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Research Director, Cicero

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Climate Finance

CICERO Shades of Green



Dark green is allocated to projects and solutions that correspond to the long-term vision of a low carbon and climate resilient future. Fossil-fueled technologies that lock in long-term emissions do not qualify for financing. Ideally, exposure to transitional and physical climate risk is considered or mitigated.



Medium green is allocated to projects and solutions that represent steps towards the long-term vision, but are not quite there yet. Fossil-fueled technologies that lock in long-term emissions do not qualify for financing. Physical and transition climate risks might be considered.



Light green is allocated to projects and solutions that are climate friendly but do not represent or contribute to the long-term vision. These represent necessary and potentially significant short-term GHG emission reductions, but need to be managed to avoid extension of equipment lifetime that can lock-in fossil fuel elements. Projects may be exposed to the physical and transitional climate risk without appropriate strategies in place to protect them.



Brown is allocated to projects and solutions that are in opposition to the long-term vision of a low carbon and climate resilient future.

Examples



Wind energy projects with a strong governance structure that integrates environmental concerns



Bridging technologies such as plug-in hybrid buses



Efficiency investments for fossil fuel technologies where clean alternatives are not available



New infrastructure for coal

Source: Cicero (2019)

[The full interview is available here](#)



INTERVIEW

“BROWN INDUSTRIES” ROLE IN THE SUSTAINABLE FINANCE LANDSCAPE



MANUEL ADAMINI
Head of Investor Engagement,
Climate Bonds Initiative



*The green bond market has grown from zero to around \$750 billion outstanding in about a decade. This is a global phenomenon. But it doesn't change the equation yet. [...] We face a climate finance gap of around \$2.5trillion per year, add SDG goals with their critical contribution to climate resilience, then we're looking at \$5-7trillion. **Achieving the milestone of \$1 trillion in annual green investment early in the 2020s will help change global perception of these numbers from headline style goals to achievable, investment reality.***

*While per-sector contributions can vary significantly across countries and regions and are sensitive to sector boundary definitions, the big five tend to be: energy, buildings, transport, energy-intensive manufacturing and materials, and agriculture/land-use (change). [...] **We need to activate [...] segments of the market that have remained absent [from the Green Bonds market] but offer huge emissions reductions potential as well as nice yield. [...] we're talking cement and concrete, metals and mining, and private transport.** This doesn't sound particularly green – yet we can't achieve our green targets without reductions in these sectors, and that's exactly the point.*

*We can spend every dollar only once. **We have to carefully set gatekeepers and markers when admitting brownish sectors to the green game.** [...] I want to see issuers committed to strategic change: green intentions turning into tangible and verifiably climate-relevant measures.*

***To the extent that KPI-linked products help the market better price [climate] risk, it is surely worth the try.** This market is young and still learning, and all innovation hence welcome.*

[The full interview is available here](#)



4.2 | OUR INVESTOR SURVEY ON TRANSITION

Brown industries' transition: a conditional appetite

In a nutshell



75 individual responses collected in 2019

(investors companies totaling ~\$9trn AuM)

Vivid willingness to invest in brown companies' transition among surveyed investors but **without leniency**.

As long as it is not properly defined with criteria, thresholds, or reference to scenario, **43%** are not in favor of transition bonds or loans.

Investors are open to new instruments (e.g., KPI-linked instruments).

Although it is a very nascent market, provided that **trust** is established regarding KPIs selection and calibration.

56% believe such instruments could be a driver of change and are willing to invest in it.

"Top picks" for transition products

Decarbonization of energy supply

Changes in business models towards circularity

Expenditures in breakthrough technologies

High expectations in terms of disclosure and credibility of the transition pathways.

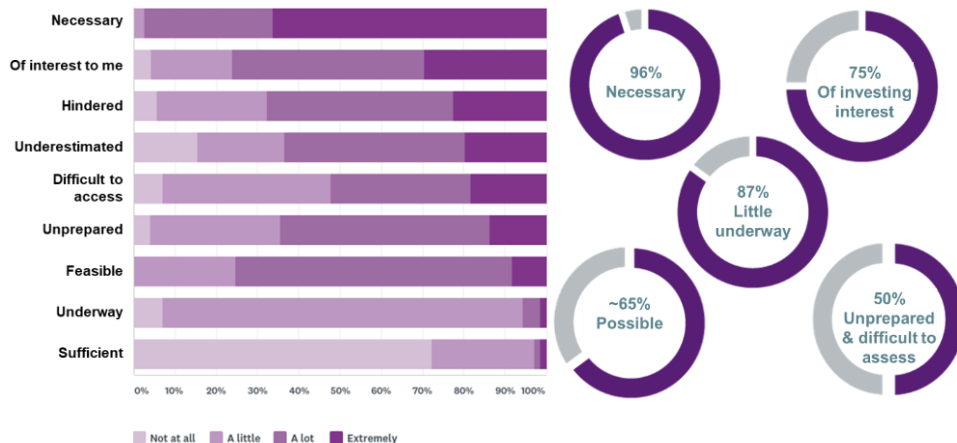
Ability to assess their ambition level against standards such as the EU Taxonomy or the Science-based Target Initiative will unarguably be a plus.

The full survey is available here



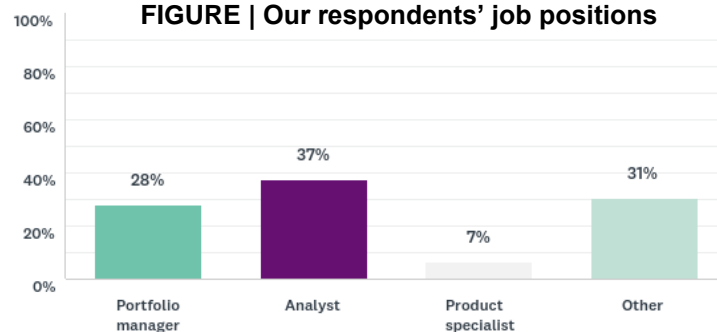
Brown Industries' transition in investors' view

How would you qualify brown industries' transition?



This survey was held online between March 2019 and Nov. 2019. We collected **75 individual answers** from people working in investment companies totaling **~\$9trn of assets under management**.

FIGURE | Our respondents' job positions



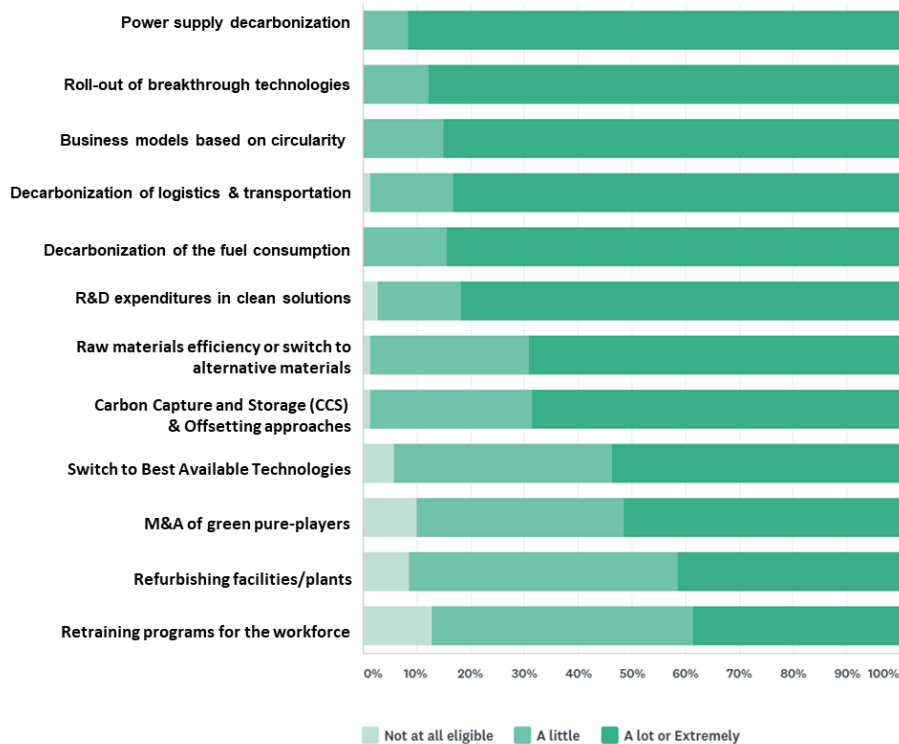
Sample of investors that have accepted to disclose their participation to our survey



Investors' preferred project categories



FIGURE | What technologies or expenditures would you consider as eligible proceeds for a green financing?



TOP PICKS

- Decarbonization of the power supply (renewable energy PPAs, i.e., OPEX, or direct investment in clean power supply)
- Roll-out of transformative technologies (45% consider it as “a lot” eligible and almost 43% as “extremely”)
- Business models based on circularity (waste or byproducts valorization, recycled scrap/“urban mining”)
- R&D expenditures in clean solutions

RELUCTANCIES

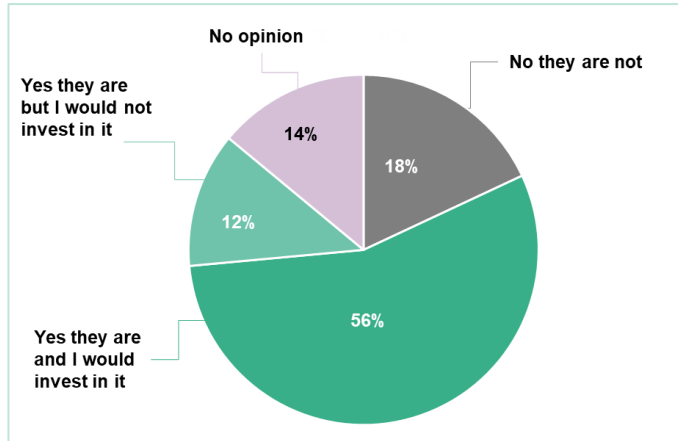
- CCS and other offsetting approaches do not convince investors (6% consider them as “not all eligible”, and almost 40% as “a little “eligible”).
- Refurbishing facilities/plans is not attractive for investors (50% answered “a little”).

“FAIR TRANSITION”

Sadly, in our view because the “just transition” and the management of its social cost is important, almost 50% of the respondents consider retraining programs for the workforce as “a little” eligible.

Transition KPI-linked instruments: appetite is clearly there provided that trust is established

Do you believe sustainability-linked financial instruments tied to KPIs can be a driver of change for brown companies?
If yes, would you invest in such financial instruments?



ANONYMIZED RESPONDENTS' QUOTES

*"We would invest in such instruments after a **case by case analysis**"
[...] "I think any initiative is welcome, but it is a **case by case approach to decide if we invest or not.**"*

*"Only if linked to a **meaningful decarbonization strategy** with a visible time horizon for switch to completely green assets, and with a discount compared to "pure" green loans."*

*"Yes, we would invest, provided the **measurement of such KPIs are checked by independent third party. Trust would be essential here...**"*



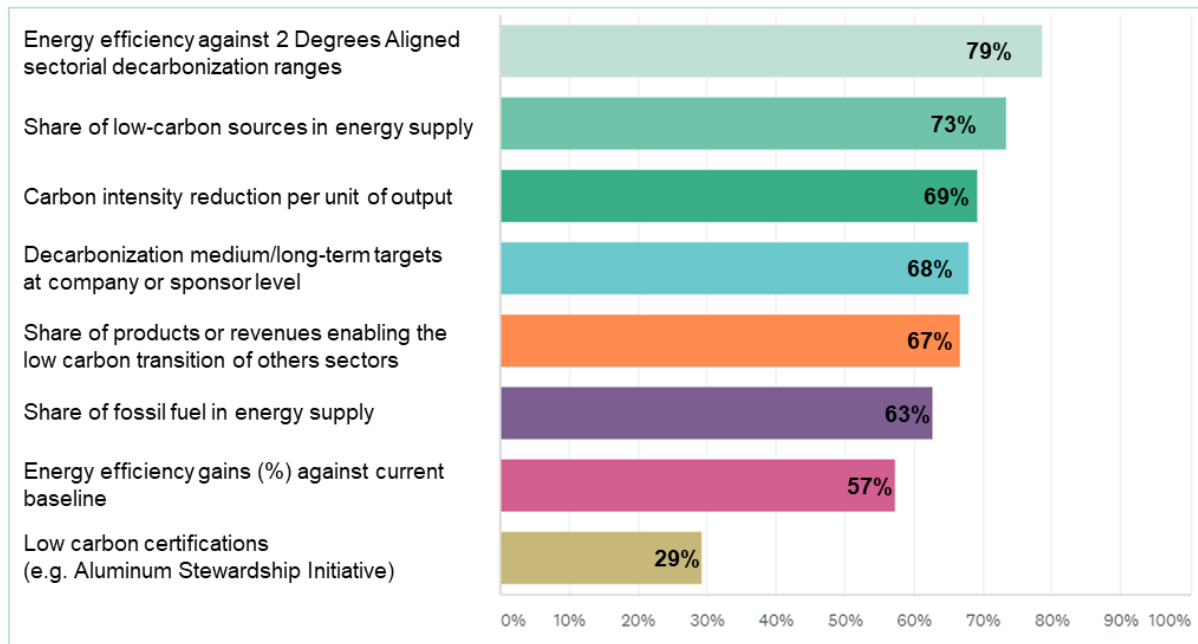
[Click here to access our SLB survey](#)



Nota bene: since 2019, we launched other investor survey, including one on Sustainability-Linked Bonds published in February 2021

Transition KPI-linked instruments: appetite is clearly there provided that trust is established

Which of the following indicators are relevant for assessing the transition ambition (tick if applicable)?



ANONYMIZED RESPONDENTS' QUOTES

*“Unlike a green factor, these indicators can be tailored to the specifics of each company to **make sure the effort is real and backed by a long term strategy**”*

*“They are questionable, as the decision criteria is missing in my opinion for **deciding whether the “sustainability improvement” is in line with Paris agreement (or the like)**. Inclusion of Science based Targets in the sustainability assessment and/or reference to EU Taxonomy would be a requirement”.*

*“Only if **KPIs are clearly defined without any possible distortion in their assessment.**”*

4.3 | INVESTORS' INITIATIVES ON TRANSITION

An extensive range of investment strategies can be used and combined when it comes to supporting energy & ecological Transition. Public institutions can also carry additional constraints (“lead by example”). Main investment strategies and practices on the O&G industry are presented below.

<p>Negative screening / Exclusion and/or Divestment (in full or part, always sequenced)</p>	<ul style="list-style-type: none"> • Case-by-case or rules-based divestment: <ul style="list-style-type: none"> – EIB's new lending policy (ban on fossil fuels with a few exceptions by end-2021) – BlackRock : exclusion of firms that derive >25% of their revenue from thermal coal production from its actively-managed portfolios – Newton IM: exclusion if an internalized cost of carbon at \$140/CO₂ ton produces a negative net income • “Fossil Free” movement (total or partial divestment, e.g., colleges/ universities/ foundations/ charities, especially in the US/UK; but also public entities, e.g. Republic of Ireland, Norwegian GPF). In 2019, >1,110 institutions, with > USD 11tn in AUM had committed to divest from fossil fuels. (1) • Sustainability & thematic funds (specific exclusion guidelines) • Sub-segments exclusion: Arctic exploration, non-conventional fossil-fuels exploration, Deep Offshore drilling, LNG • EU Climate Benchmarks (revenues threshold 10% from oil exploration or processing activities) • Future EU Eco Label for financial Products
<p>ESG integration & best-in-class investing</p>	<ul style="list-style-type: none"> • Integrated ESG risk Management & ESG Scoring (from external providers, and/or internal in-house methodology) • GHG footprint assessment and optimizing • Constituents weighting according to “climate scores”, e.g., based on Transition Pathway Initiative (TPI) assessment
<p>Investor engagement (stewardship activities)</p>	<ul style="list-style-type: none"> • Governance-related investor dialogue (Climate Change AGM Resolutions) • Coalitions-based shareholder dialogue (e.g. Climate Action 100+, Institutional Investors Group on Climate Change, IIGCC)
<p>Green Bonds Purchasing</p>	<ul style="list-style-type: none"> • Green Bond Principles (ICMA) • Climate Bonds Initiative (CBI) Taxonomy • EU GBS (but limited pool of Use-of-Proceeds because of aspirational thresholds from the EU Taxonomy) • Reputational backlash (consistency critics addressed to O&G companies, e.g. high capex in green assets in absolute terms but modest relative share)
<p>Transition KPI-linked instruments</p>	<ul style="list-style-type: none"> • Transition performance priced-in (coupon step-up/down) structures and attached dialogue • Financial Accountability “skin in the game” and forward-looking dimension

(1) USD 11tn and counting: new goals for a fossil-free world. 350.org

Asset owners' strategies regarding the O&G industry

Because of the volume of investment they make, and their long-term horizons, sovereign & pensions funds and insurers are key players for initiating change. If actions have until now concerned mainly the coal industry, asset owners are increasingly paying attention to other fossil fuels.

Sovereign Funds & Pension Funds

Impulse change through the mandates they give to asset managers.

Nordics have multiplied divestment announcements

- **Norway's Government Pension Fund Global (GPFG)**, the world's largest sovereign wealth fund and one of the six founding members of the One planet Sovereign Wealth Fund Working Group, has since 2017 reduced its investments in oil and gas as part of a strategic decision to reduce Norway's overall country exposure to the sector.
- In October 2019, **KLP** – Norway's largest pension fund – divested of its oil sands exposures.
- **PenSam** – a ~USD 20bn Danish pension fund – blacklisted in 2019 26 global oil firms, selling off shares with a total value of EUR 17mm.
- **AP2** - a ~USD 43bn Swedish pension fund - announced in December 2020 it will no longer invest in companies that derive more than 10% of their revenue from oil, or 50% revenue from gas.

Divestment commitments come also from other geographies

- **New York City** said in January 2018 that over five years it would remove fossil fuel investments from its public pension funds, which then had USD 189bn in AUM.
- **The EIB** announced in November 2019 it will stop funding oil, gas and coal projects at the end of 2021, cutting EUR 2bn of yearly investments.

Insurers

Have two main levers for actions:

Progressively retreating from underwriting fossil fuel

- In 2017, **Axa** committed to no longer underwrite new bituminous sands.
- **Generali** has committed not to ensure clients producing fossil fuels from bituminous sands.
- **Swiss Re** is committed to gradually cut business support in underwriting to the world's 10% most carbon-intensive oil and gas production by 2023.

Divesting fully or partially from fossil fuel related assets

- Since 2019, **Generali** is committed not to make new investments in bituminous sands projects, and to divest its residual bond exposure to this sector.
- **Talanx Group** will not make any new investments in companies that generate at least 25% of their revenues from fossil fuel sources.
- **Swiss Re** is committed to gradually cut support in asset management to the 10% most carbon-intensive oil and gas producers by 2023.

Banks

In addition to exclude funding the thermal coal, and sometimes non-conventional O&G activities:

- In September 2020, **BBVA, BNP Paribas, ING, Société Générale and Standard Chartered** published a report on the application of the Paris Agreement Capital Transition Assessment (PACTA) methodology, designed to **steer their credit portfolios towards the objective of the Paris Climate Agreement**.
- **Barclays, Morgan Stanley, JP Morgan and HSBC** have committed to **net-zero financed emission by 2050**.

Investment managers' strategies regarding the O&G industry

Beyond divestment, assets managers are adopting diverse strategies and calendars regarding O&G.

Investors	Oil & Gas Divestment Strategy
Full divestment	
OFI AM	<p>Sep. 2020 - The Ofi Group has announced it will divest from O&G extraction companies by 2050 in a three-stage plan.</p> <ul style="list-style-type: none"> Firstly, Ofi AM will exclude firms making more than 10% of their turnover from oil, shale gas, and tar sands extraction, removing those making more than 5% of turnover from the sectors by 2030. In the second phase from 2030, it will exclude firms starting new exploration projects in the Arctic, gradually removing all companies that extract oil and gas from the region by 2040. In the final stage, Ofi plans to exit the sector fully by 2050 at the latest.
Handelsbanken	Handelsbanken excludes investments companies involved in fossil fuels.
Partial divestment	
Thematic divestment (Arctic drilling, bituminous sands)	
Robeco	Sep. 2020 - Companies that derive >25% of their revenue from thermal coal or oil sands, or >10% from Arctic drilling , will be barred from investment portfolios. The exclusion applies to all of Robeco's mutual funds, excluding client-specific funds and mandates but including sub-advised funds.
Groupama AM	Groupama AM is no longer investing in companies for which oil sands represents more than 15% of their reserves.
Fossil free funds/strategies	
OP AM	Aug. 2020 - OP AM will make OP-Low-carbon World and OP-Sustainable World entirely fossil-free funds. This means that these funds will not invest in producers of fossil fuel or electricity companies that use fossil fuels.
Amundi	Amundi's Green Technology Equity Socially Responsible (SRI) Strategy excludes companies that produce fossil fuels.

NEW STRATEGIES REGARDING O&G

As part of their strategy to decarbonize their portfolios, asset managers are engaging with the O&G sector, but also contemplating investing in new type of sustainable debt instruments:

Investors engagement

At BP's 2019 annual general meeting, shareholders voted overwhelmingly in favor of a motion that will push BP to set out a business strategy aligned with the Paris Agreement's goals. Aviva Investors co-sponsored the resolution with Hermes IM and L&G IM.

As a result of engagement through the Climate Action 100+ in 2019:

- RD Shell released a joint statement committing to a range of industry leading climate commitments, including emissions reduction targets that include scope 3 emissions.
- PetroChina developed a climate change strategy and signaled the company's intention to align its climate policy to the goals of the Paris Agreement.

Transition & KPI-linked instruments

Past months have seen a growing interest of investors for sustainability-linked products...

...Sustainability-linked bonds & loans (coupon or margin tied to sustainable KPIs) could further encourage O&G companies to align their activities with the Paris Agreement, and thus make progressively their business model evolving.

INTERVIEW

TRANSITION ASSESSMENT METHODS IN THEIR INFANCY BUT ALREADY CRUCIAL



JULIEN BRAS
Green Bond Portfolio Manager,
AllianzGI



- “ We have three pillars for green bonds screening: i) alignment of the Framework with the Green Bond Principles; ii) the content and features of the underlying projects or assets (on the basis of an internal taxonomy, largely derived from CBI with slight adjustments) and iii) **the ambition and credibility of the issuer’s climate-change and decarbonization strategy.** ”
- “ ... the concept of transition is thoroughly considered and is at the core of the investment decision. ... **And we are not keen to invest in green bonds if we are not presented a clear transition strategy with ambitious targets.** ”
- “ **We have the willingness not to focus only on the best players but to encourage progress approach** and we even think that it is the best way to really generate an impact in the context of this investment solution. ”
- “ **It is necessary for us that the company has a medium-term transition plan.** We cannot require Science Based Targets (see SBTi) because for the moment, it would reduce too drastically the universe. That being said, we pay much attention to this question of credibility and ambition. To do so, we scrutinize if the management is supportive and involved in such a green bond program and whether it is likely to be a “one-off”. We have a strong preference for repeat issuers. ”
- “ **The main hurdle [for KPI-linked instruments] is the sound selection of indicators and how transparent and robustly calibrated indicators would be.** ”

The full interview is available here



INTERVIEW

PRINCIPLES-BASED RED LINES FOR AN IN-DEPTH TRANSITIONING INVESTOR DIALOGUE



VICTORIA BARRON
Former Responsible Investment
Analyst, Newton Investment
Management



- “ **[For the red line related to climate change], we felt that a principles-based approach better captures the nuances of business operations.** For example, through excluding gas producers you could also end up excluding utilities who are making big strides in renewable energy.
- “ **In our strategy, companies that are heavy emitters, which would be unprofitable under a certain carbon pricing** [$\$140/\text{CO}_2$ ton based on IEA World Energy Outlook 450 ppm scenario], and which have no current intention of transitioning, **are not investable.**
- “ **The preparedness of an actor can also be very hard to assess from a hard/data metric approach,** so when we do our ESG analysis, we also go through a company's reports and take a view on how active they are being.
- “ **Under this red line, around 9% of companies from the MSCI AC World Index are currently excluded, including various energy and mining companies, as well as certain airlines and utilities.**
- “ **We analyze many data points, including a company's scope 1 and 2 emissions on an absolute and intensity-level basis, and how a business compares to its peers.** Data analyzed will include: TPI, CDP, SBT, Bloomberg data, a company's own data, and that of our ESG service providers. [... the proprietary overall ESG] score takes a view on whether we think the company is going to improve in the future, based on current efforts.

CHART | Climate Change Red Lines



Illustration of Newton Investment Management's climate change red line process
Source: Newton Investment Management.

The full interview is available here



4.4 | TRANSITION & SUSTAINABILITY-LINKED BONDS

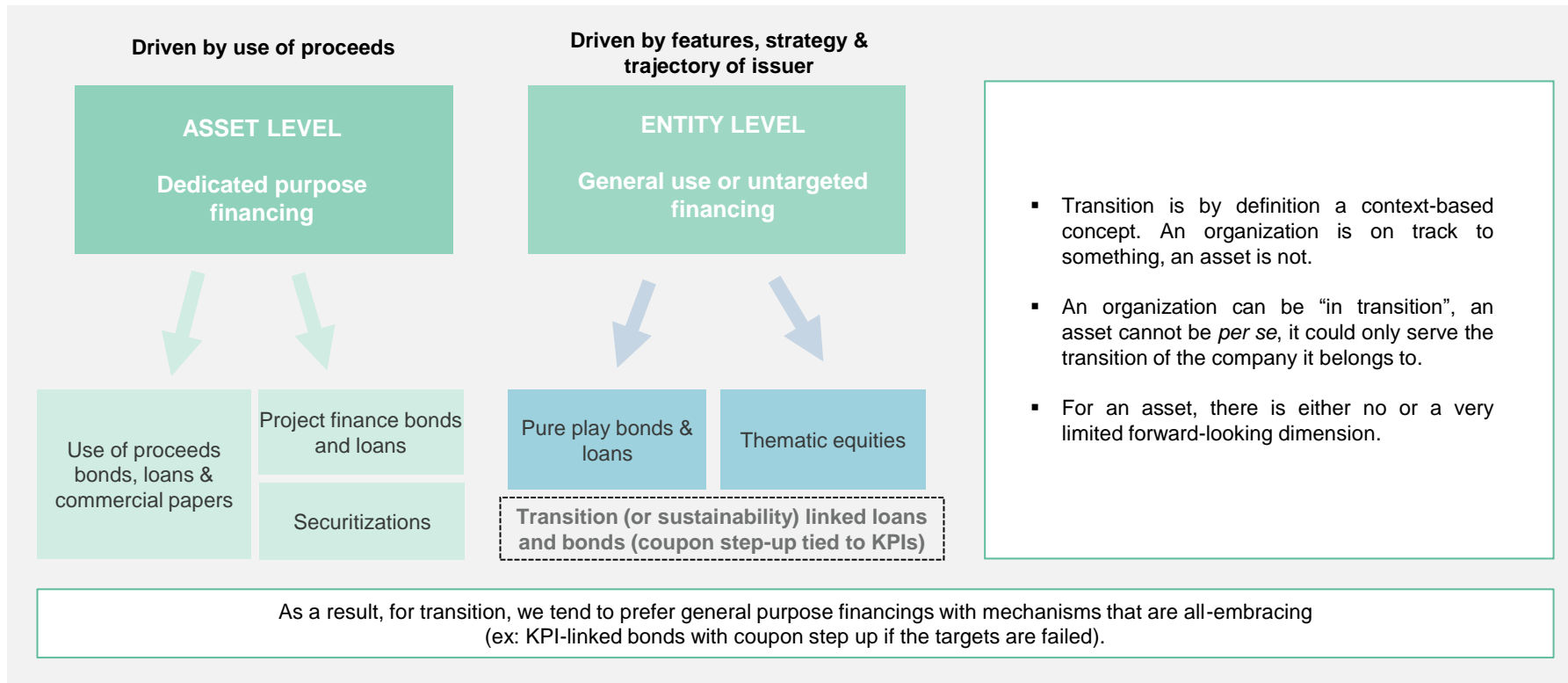
Why consider Green & Sustainable Financing ?

When funding meets sustainability: breakdown between **constraints & opportunities**

Pressure on business models	Regulatory environment	Market development
<p>Cost & risk management</p> <ul style="list-style-type: none"> Consequences for the top line: obsolescence of certain technologies / emergence of a low-carbon economy / changing consumer habits Emerging risks related to resource management, stranded assets, energy costs A matter of transparency & reporting 	<p>New sustainability related policies</p> <ul style="list-style-type: none"> Alignment with national & international agendas related to climate change and environment Acceleration of market regulation (E.U. Sustainable finance action plan, Sustainability disclosure requirements, 2030 Agenda – SDGs roadmaps disclosure) 	<p>Growing standardization & expectations</p> <ul style="list-style-type: none"> Acceleration of market standardization (ICMA, LMA, sustainable finance products development) Pressure from investors Peers' differentiation less relevant
Communication & image	Investors & lenders appetite	Internal engagement
<p>Support Sustainability Strategy</p> <ul style="list-style-type: none"> Set foot in the sustainable finance market Secure funding allocated to projects and activities with recognized environmental/social added value Positive impact on reputation and credibility (ESG evaluation) 	<p>Address new expectations & diversify</p> <ul style="list-style-type: none"> Investors strategic shifts towards sustainable finance (quantified commitments) Increasing demand for green assets & investment opportunities leading to diversification and attraction for issuers Investors with own reporting expectations on their investment portfolios 	<p>Virtuous circles and continuous improvement</p> <ul style="list-style-type: none"> Set-up/improve internal environmental management systems such as environment & climate accounting and reporting Support evolution of company practices, procurement... Increase sustainability performance & identify internal levers

Transition finance compass

Use-of-proceeds or general corporate purpose financing?



Definition of Sustainability-Linked Bond Principles

Introduction

- Sustainability-Linked Bonds **incentivize the issuers' achievement** of material, quantitative, pre-determined, ambitious, regularly monitored and externally verified **sustainability (ESG) objectives**
- The Sustainability-Linked Bond Principles ("SLBP") provide guidelines that recommend structuring features, disclosure and reporting and position integrity protection at the heart of the guidance.
- **Natixis was co-chairing the SLBP working group** under ICMA secretary.

Definition – Sustainability-Linked Bonds

Sustainability-Linked Bonds ("SLBs") are any type of bond instrument for which the financial and/or structural characteristics can vary depending on whether the issuers achieve predefined Sustainability/ ESG objectives.

In that sense issuers are committing to future improvements in sustainability outcome(s) within a predefined timeline. It is a forward-looking performance-based instrument.

Those objectives are measured through predefined Key Performance Indicators (KPIs) and assessed against predefined Sustainability Performance Targets (SPTs)

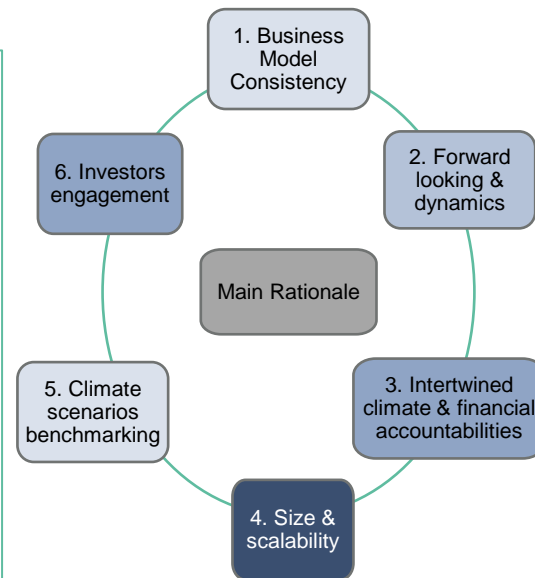
SLBs are intended to be used for general corporate purposes, hence the use of proceeds is not a determinant in its categorisation.

The SLBP have five core components :

- **Selection of Key Performance Indicators (KPIs)**
- **Calibration of Sustainability Performance Targets (SPTs)**
- **Bond characteristics**
- **Reporting**
- **Verification**

SLBP recommend that the issuers publicly communicate, about the selection KPI(s) (i.e. relevance, materiality), the SPT(s) (i.e. ambition level and consistency with overall strategic planning), trigger events for change of bond characteristics, intended post issuance reporting and external review format, as well as overall issuers' representation of the alignment with the SLBP.

Such disclosure may take place in the bond documentation and/or on the issuers' webpage, a dedicated framework, external reviews, or investor presentation, etc.



Core components of ICMA's Sustainability-Linked Bond Principles

1 Selection of KPI(s)

- **Relevant, core and material** to the issuer's **overall business**, and of **high strategic significance** to the issuer's **current and/or future operations**
- **Measurable or quantifiable** on a **consistent methodological basis**
- **Externally verifiable**
- Able to be **benchmarked** (i.e., as much as possible using an external reference or definitions making the ambition assessment of SPTs possible)

2 Calibration of SPTs

- The SPTs should be **ambitious**:
- Represent a **material improvement** in the respective KPIs and be beyond a "Business as Usual" trajectory
 - Where possible be compared to a **benchmark** or an **external reference**
 - Be consistent with the issuers' overall **strategic Sustainability / ESG planning**
 - Be determined on a **predefined timeline** set before (or concurrently with) the issuance of the bond

The target setting exercise should be based on a combination of benchmarking approaches:

- **The issuer's own performance over time** : track-record of 3 years is recommended and forward-looking guidance on the KPI when possible; and
- **The issuers' peers** i.e., the SPT's relative positioning versus its peers' where available (average performance, best-in-class performance) and comparable, or versus current industry or sector standards; and/or
- **Reference to the science**, i.e. science-based scenarios, or absolute levels or to official country/regional/international targets (Paris Agreement on Climate Change and net zero goals, Sustainable Development Goals (SDGs), etc.) or to recognized Best-Available-Technologies or other proxies to determine relevant targets across environmental and social themes.

3 Bond characteristics

- Bond **financial and/or structural characteristics** should vary **depending on whether (or not) the selected KPI(s) would reach the predefined SPT(s)** i.e., the SLB needs to include a financial and/or structural impact involving trigger event(s).
- Potential variation of the coupon is the most common example, but it is also possible to consider other variations
- Variation of the bond financial and/or structural characteristics should be **commensurate and meaningful** relative to the issuers' original bond financial characteristics.
- **Necessary element of the bond documentation**: The KPI(s) and SPT(s) definition (including calculation methodologies) and the potential variation of the SLB's financial and/or structural characteristics.
- **Any fallback mechanisms in case the SPTs cannot be calculated or observed in a satisfactory manner, should be explained.**
- Issuers may consider including language in the **bond documentation** to take into consideration potential exceptional events or extreme events, including drastic changes in the regulatory environment that could substantially impact the calculation of the KPI, the restatement of the SPT, and/or proforma adjustments of baselines or KPI scope.

4 Reporting

To be kept readily available & **regularly published**, at least annually and in case for any date/period relevant for assessing the SPT performance:

- Up-to-date information on the performance of the selected KPI(s), including baselines where relevant
- A verification assurance report relative to the SPTs outlining the performance against the SPTs and the related impact, and timing of such impact, on the bond characteristics
- Any information enabling investors to monitor the level of ambition of SPTs

5 Verification

- **Independent and external verification** of performance level against each SPT for each KPI by a **qualified external reviewer** with relevant expertise (an auditor or an environmental consultant)
- **At least once a year** and in any case for any date/period relevant for assessing SPT performance leading to a potential adjustment of SLB financial and/or structural characteristic
- Verification of the performance against the SPTs should be made **publicly available**

External review : SPO: recommended

Recommendation to appoint (an) **external review provider(s)** to confirm the **alignment of their bond with the five core components** of the SLBP (such as a SPO)

Suggested mandate includes the assessment of :

- the relevance, robustness and reliability of selected KPIs,
- the rationale and level of ambition of the proposed SPTs, the relevance and reliability of selected benchmarks and baselines,
- the credibility of the strategy outlined to achieve them, based on scenario analyses, where relevant.

Post issuance, in case of any material change to perimeter / KPI methodology / SPT(s) calibration, issuers are encouraged to ask external reviewers to assess any of these changes.

In cases where no SPO sought, it is recommended that issuers demonstrate (and document) or develop the internal expertise & processes to verify their methodologies..

Topics left to market innovation and/or Q&A

- Nature of financial and/or structural characteristics
- Examples of KPIs, benchmarks, references
- Documentation & structuring of changes in KPI & SPTs
- Exclusions / Do No harm approaches / Minimum ESG performance for issuers
- Programmatic or bond specific approach
- Detail on what "meaningful" and "commensurate" can mean?
- ECB eligibility discussion
- Articulation with GBP/SBP or transition bond.

A need for disruption – Breakthrough Use-of-Proceeds

Net carbon neutrality requires tackling “hard-to-abate” emissions via technologies that are not yet commercially available. Some “infant technologies” need to be considered as eligible due to their tremendous potential though they are riskier.

Use-of-Proceeds-based financing has limits in terms of “**transition spillover or impact**” since individual assets or projects hardly inflect the overall position of the company (especially to energy efficiency related projects, which are also fraught with carbon lock-in risks).

Andreas Schroeder, Tiffany Vass, Laura Cozzi from the International Energy Agency (see their interview “[The instrumental role of industry decarbonization in IEA’s Sustainable Development Scenario](#)”) identify some of the frontier technologies to watch:

Electro-technologies for process heat, such as infrared and ultraviolet heating

(with applications in drying and curing processes), induction melting and electric boilers for electrification across a range of industrial activities.

The electrification of clinker production

using induction or microwave heat for the cement sector’s most energy-consuming step (still at the laboratory stage).

An attractive option to indirectly electrify industrial high-temperature heat

either *via* direct combustion or blending with natural gas.

Mechanical vapor recompression

providing higher temperature heat than what is practicable using heat pumps. Such technology could be beneficial in pulp and paper and certain chemical production processes, though to be economically viable it requires low electricity prices (relative to natural gas).

Hydrogen-based direct iron reduction for primary steel production

to substitute coal or natural gas. Experts suggest that 100% electrolytic hydrogen-based steel production is not sufficiently advanced to be exploited before 2030. Partial injection of hydrogen is possible up to about a quarter without major process transformations but is highly dependent on economics

Example with the Steel industry: navigating Use-of-Proceeds and Sustainability-Linked Bonds

Technologies or **processes** can be used either as Use-of-Proceeds or as to determine KPIs (for example, the share of the total production delivered or derived given technology, or the share of CAPEX dedicated to such technology).

Another indicator is the mix between **a technology and its outcomes** (e.g., the amount of CO₂ captured through CCS over a given period).

Technology	Description	Use-of-Proceeds	KPIs usable for SLBs	Impact indicators related to the technology
Hydrogen as a reducing agent	Avoiding carbon and using hydrogen to reduce iron ore thereby averting the creation of CO ₂ and producing H ₂ O (water) instead.	Investment in facilities to enable the use of H ₂ as reducing agent (replace blast furnace sites with large sponge iron production site (by direct reduced iron with hydrogen produced using the hydropower)	Share of new manufacturing capacities that can use hydrogen as reducing agent (hydrogen powered production)	Carbon intensity reduction achieved through the use of hydrogen as reducing agent
Carbon Capture and Storage (CCS)	Generating a clean and concentrated CO ₂ stream that can be captured and stored.	Retrofitting expenditures to equip steel plants with capture technologies, build transportation networks, access to storage sites, etc.	Share of facilities equipped with CCS technologies or number of facilities equipped with CCS	Tons of CO ₂ sequestered over a period of time
Carbon Capture and Utilisation (CCU)	Using the components of the co-product gases from existing processes to produce fuels or input material for the chemical industry.	Investment in facilities to enable CCU	Share of steel plant equipped with CCU technologies	Tons of CO ₂ captured and converted into fuels or chemical industry inputs
Electrolysis	Reducing iron ore using electricity	Investment in electrolyzers	Number of electrolyzers installed/deployed	Steel carbon intensity improvement due to electrolysis

Transition & Sustainability-Linked Bonds: Who is eligible ?

Features to display for “alleged transitioner”

We propose criteria formalizing transition patterns that are illustrative of desirable transition features

1

Historically or predominantly belong to a **high emitting sector**



2

Disclose **scope 1 to 3 emissions** with consistency & accuracy



3

Diversifying range of products & services with a focus on decarbonization solutions (“*greening by*”) and increasing green revenues



4

Have at least 3 years track-record self-decarbonization above 5% per annum but **without all abatement potential exhausted**



5

Being able to share **documented emission reduction forecasts** over the next 5, 10, 15, 20 years.



6

Have **set evidence-based decarbonization targets** (based upon scenario analysis and sectorial decarbonization pathways)



Our 4-question radar

Is it ambitious?

Is it consistent?

Is it game-changing?

Is it enough?

Four criteria can be evaluated:

Assessing transition profile, pathways and claims of companies

- What is the big picture of the sector the company belongs to?
- Where does the company come from?
- Where does it stand now? Where is it going, at what speed?

#1

WILLINGNESS

#2

PREPAREDNESS

#3

AMBITION

#4

ACTION

#1

WILLINGNESS

It is a bedrock for analysis & engagement and demonstrates the goodwill of the company which provides enough transparency to evaluate its transformation. It enables understanding the situation from which the transition must begin or be continued, and against which progress must be monitored.

Disclosure

Scope 1 & 2 emissions not disclosed

No explicit climate policy nor process to manage climate risks

GHG emissions verification under ISO 14064-1 Standard

Reporting on verified Scope 3 emissions

Adhesion & implementation of TCFD recommendations

Scenario analysis & planning based upon 2°C compatible scenario & key assumptions disclosure

Transition *laggards*

#2

Our 4-question radar

PREPAREDNESS

It is mostly a backward & present looking analysis to take stock of what has been achieved, what is necessary next (completion level of the transition), and how credible ambitions are. It also touches upon adaptive capacities & ability to accelerate.

Performances & capacities

Steady growth of absolute GHG emissions and carbon intensity

Exit from dark brown activities (e.g., coal, tar sands) not completed nor imminently scheduled

Diversification (e.g., M&A) operations towards low-carbon or enabling activities successfully completed

Alignment with sectorial decarbonization intensity Benchmarks

GHG absolute emissions peak achieved

GHG absolute emission trends reversal (degrowth)

Transition *laggards*

#3

AMBITION

It is about the way the vision or strategy is translated into goals publicly endorsed. It enables assessing whether it is enough with regards to climate science and whether it is demanding and game-changing for the company and the sector .

Targets

Absence, vague, or only long-term targets (2040, 2050)

Scope 1 –2 reduction targets above sectorial average

Short & medium-term (~2025-2030) Scope 3 reduction target if Scope 3 emissions account for ≥ 40% of total emissions

Science-based Target (SBTi) validation

Carbon net neutrality targets

Transition *laggards*

Our 4-question radar

#4

ACTION

It is about how the company actually acts, the investment made, the managerial mechanisms in place and stakeholders' engagements. It touches upon the consistency of the different measures to assess whether they all head in the same direction.

Efforts							Share of low-carbon energy in total CAPEX (e.g., ≥ 10-15% for O&G companies until 2025, 20-25% from 2025 to 2030, etc.)
Investments in high breakeven price fossil fuels related activities	Zero or little diversification towards low-carbon energy (as a producer or for power supply)	Quantitative & time-frame bottom-up transition plan	Large-scale investments in carbon natural sinks or CCS	Workers retraining programs or pre-retirement schemes	Share of R&D dedicated to decarbonization ≥ 40%		

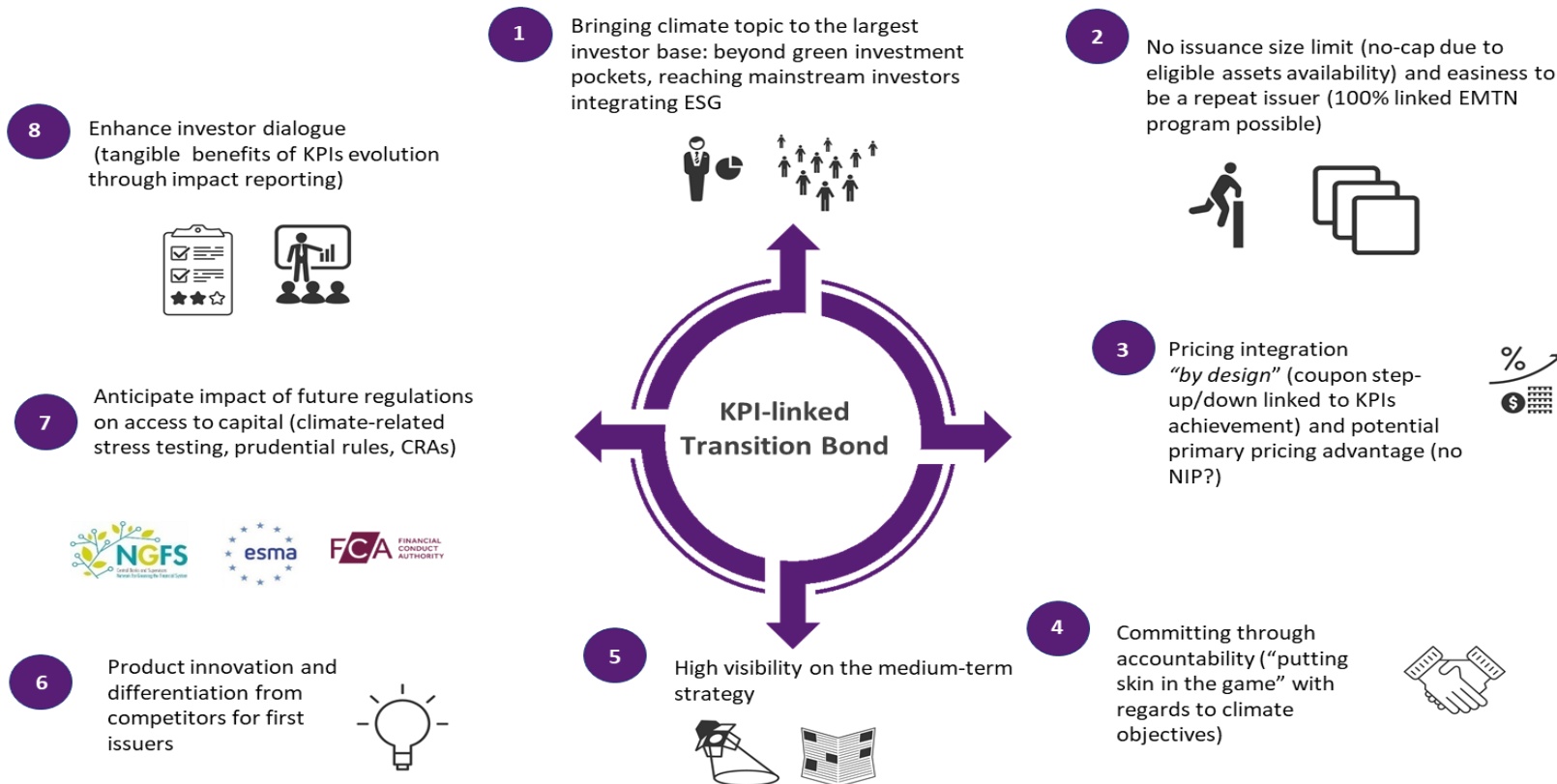
Transition laggards

Governance/decision-making processes

Lobbying against climate change action (trade associations)	Climate targets annual or biannual basis review	Variable remuneration of executives linked to climate-change & other targets accountability mechanisms	Internal Carbon Pricing & climate stress testing
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Transition laggards

Eight arguments in favor of sustainability-linked bonds for high-emitting companies



Transition & Sustainability-Linked Bonds: Three main steps

1

Choice of the Key Performance Indicator(s)

EXAMPLES

- Carbon intensity of sold products
- Share of low-carbon electricity and natural gas in sales mix in 2040
- Total renewable installed capacities

2

Calibration of the end target (or range) and potential intermediary milestones

EXAMPLES

- 20% by 2020 versus 2015 baseline
- Between 20% and 25% by 2020 *versus* 2015 baseline
- 13% by 2017, - 15% by 2018, - 18% by 2020 versus 2015 baseline

3

Basis Points (BPS) adjustment calibration

EXAMPLES

- Coupon step-up of 10/15 bps in case of target(s) failure
- NB: From an IFRS perspective, KPI-linked bonds should be accounted at amortized cost, meaning that the step up would be capped at the double of the investors initial rate of return (IFRS 9.B4.3.8a).

Resources for KPIs Selection & Calibration

Natixis' methodology uses those resources to structure robust sustainability-linked instruments

KEY FEATURES

Guidance on extra financial information disclosure (including metrics & indicators)



WHAT KPIs TO CHOOSE

Guidance in the identification of relevant KPIs

Corporates



77 industry standards



Carbon Transition Assessment for ~ 15 sectors



Industry-led initiatives

SSAs



2030 Agenda relevant to relate but not usable as such for corporates (by contrast, UN 169 targets and 232 indicators usable as they stand for countries, regions, or municipalities issuers), or assessment providers (alignment, efforts, etc.)

Is it enough?



Guidance in the identification & calibration of relevant sectorial KPIs



Technical screening criteria (threshold for 67 economic activities)

Is it credible?

Guidance in the feasibility evaluation of the KPIs (is the company on track, are actions set at the right level & timescale?)

ACT

ACT Retail methodology

ACT Electric Utility methodology

ACT Auto manufacturing methodology

Resources for KPIs Selection & Calibration

Natixis' methodology uses those resources to structure robust sustainability-linked instruments

When regulation is absent or piecemeal for some sectors regarding sustainability topics, and guidelines or classifications such as the EU Taxonomy of Sustainable Activities **do not exist either, industry-led initiatives might provide useful tools to benchmark performances within sectors, identify KPIs and calibrate targets.** The table below identifies some of the industry associations and provides examples of resources.

Those must be considered carefully as they are by nature **biased**, are prone to green washing and might be inclined to preserve the *status quo*. However, “self-regulation” has often proven in some cases to be useful and laying the foundations for hard law. For instance, the Green Bond Principles (GBP), forged through the International Capital Market Association (ICMA), revealed to be **an effective and transformative tool**. As evidence of that, the future EU Green Bond Standard mimics the GBP. On other topics, the OECD, which only produces **guidelines and soft law standards, has been able to unleash substantial transformations**, for instance on tax topics (Base Erosion Profit Shifting, BEPS), where international organizations and usual governance have failed to deliver.

Lastly, there are international, regional, and domestic associations. Some are general industry associations, some are focused on environment and sustainability, and some appear to be “traditional” lobbies. Many of them work with ISO on industry standardization.

SECTOR	INDUSTRY ASSOCIATIONS	EXAMPLES OF INITIATIVES/RESOURCES
Car	<ul style="list-style-type: none"> European Automobile Manufacturers Associations (ACEA) Japan Automobile Manufacturers Association (JAMA) 	<ul style="list-style-type: none"> Position paper (e.g. plan to help implement the European Green Deal) Factsheet (data, guidance, best practices, benchmark)
Shipping	<ul style="list-style-type: none"> International Maritime Organization (+ISO) Sustainable Shipping Initiative International Chamber of Shipping (+ISO) World Shipping Council (+ISO) 	<ul style="list-style-type: none"> Energy Efficiency Design Index (EEDI) for new ships (index that estimates g of CO₂ per ton-mile).
Oil & Gas	<ul style="list-style-type: none"> International Petroleum Industry Environmental Conservation Association International Association of Oil & Gas Producers Oil and Gas Climate Initiative (OGCI) 	
Petrochemicals	<ul style="list-style-type: none"> International Council of Chemical Association (including Solvay, BASF, Dow Chemicals, Sasol, DuPont...) Gulf Petrochemicals and Chemicals Association European Petrochemical Association 	<ul style="list-style-type: none"> ICCA's Building Technology Roadmap

Resources for KPIs Selection & Calibration

Natixis' methodology uses those resources to structure robust sustainability-linked instruments

SECTOR	INDUSTRY ASSOCIATIONS	EXAMPLES OF INITIATIVES/RESOURCES
Meat industry	<ul style="list-style-type: none"> Sustainable Agriculture Initiative Platform International Meat Secretariat (but does not necessarily have resources on sustainability) Livestock and Meat Commission (Northern Ireland) Meat & Livestock Australia Meat Industry Association of New Zealand 	For example, Meat & Livestock Australia invests (up to \$5.7m per year) in environmental and sustainability R&D , and create reports.
Iron & steel	<ul style="list-style-type: none"> World Steel Association (+ ISO) The European Steel Association (EUROFER) China Iron and Steel Association (CISA) 	<ul style="list-style-type: none"> Sustainable Development Charter Position papers that identifies technologies Low Carbon Roadmap Energy efficiency and pollution reduction resources (available only in Chinese), annual industry meetings and events, including one on environmental protection
Cement	<ul style="list-style-type: none"> Global Cement and Concrete Association The European Cement Association (Cembureau) + ISO China Cement Association 	<ul style="list-style-type: none"> GCCA Sustainability Guidelines, Sustainability Charter
Aluminum	<ul style="list-style-type: none"> World Aluminum (International Aluminum Institute) – organization in cooperation with ISO The Aluminum Association 	<ul style="list-style-type: none"> Sustainability materials

Fair transition Use-of-Proceeds

Overview of possible categories of just transition-related expenses

- Several suggested eligible proceeds below are not CAPEX but we believe that OPEX would be eligible and accepted by the market in the light of a fair transition and employee's considerations.
- The EU Green Bond Standard opens the door to green OPEX and some examples of Sustainable Bonds including retraining expenditures can be seen in the market (see for instance [CDC's sustainability framework](#))

	Transition : Exit from highly emitting fossil-fuel facilities	Fair transition : mitigating social impacts of transition	
		Active / retraining measures	Compensatory measures
Use-of-Proceeds	<p>Decommissioning</p> <ul style="list-style-type: none"> • Electrical generating units shut down • Removal of coal, electrical generating equipment & hazardous material from the generation process and buildings (e.g. asbestos) <p>Remediation & rehabilitation</p> <ul style="list-style-type: none"> • Investigation and cleanup of hazardous materials <p>Redevelopment & Repurposing</p> <ul style="list-style-type: none"> • Including compliance to potential legal requirements but also covering redevelopments and repurposing 	<ul style="list-style-type: none"> • Training and re-training programs ahead of exit plans and concomitantly • Career advice • Help employees with job search • Mentoring and coaching • Entrepreneurship and business creation 	<ul style="list-style-type: none"> • To maintain a level of income • Financial allowances • Geographical Mobility/relocation allowances • Pre-retirement schemes
Output & Impact indicators	<ul style="list-style-type: none"> • Total fossil fuel capacities decommissioned (in MW) • Absolute GHG emission reduction (yearly basis) • Impact on a company's carbon intensity • Air pollution reduction (dust, asbestos) • Water & soil pollution reduction (in % vs. legal thresholds) • Land rehabilitation and natural capital (fauna biodiversity) 	<ul style="list-style-type: none"> • Number of beneficiaries (breakdown by age, gender, diploma) • Numbers of jobs preserved on site • Number of hours of (re) training • Number of trained/graduated employees • Internal mobility allowed • Number of employees who found a job either elsewhere in the company or outside it within XX months of closure (of which, in low-carbon sectors, recycling, repair, rent activities) • Local economy metrics 	

INTERVIEW

TRANSITION BOND MARKET: REGARDLESS OF FINANCING FORMATS, THE MAIN QUESTION IS WHETHER THE ISSUER IS ON THE PATH TO A CREDIBLE CLIMATE TRANSITION



YO TAKATSUKI

Former Head of ESG Research and
Active Ownership, AXA IM



*We are very active buyers of Green Bonds and currently hold investments worth **around 5.5 billion Euros in this rapidly growing sector.***

We have found no major equity or bond benchmark that has a current alignment close to the +1.5°C limit sought by COP21. We need to switch our focus to the middle part of the portfolio – the section which is neither the most nor the least carbon intensive.

*Fortunately, there are many ways we can make genuine progress in decarbonizing the world economy. They include challenging carbon-intensive companies **in one-to-one engagements and participating in collaborative initiatives** such as Climate Action 100+ or the Powering Past Coal Alliance.*

*So last June, we published a call-to-action which sought the establishment of a new fixed income asset class called **Transition Bonds**. We believe **it is important that companies which are committed to meaningful decarbonisation at the corporate-level and which can adequately evidence progress should be able to secure stable and long-term through the Transition Bond market.***

*We all talk about companies having an over-arching multi-decade climate policy but **the truth is that senior executives and board directors of many of the companies we engage with are only starting to understand and acknowledge the scale of the changes required to mitigate global warming.***

*The most important aspect of both these financing approaches (Use-of-Proceeds and KPI-linked Bonds) is that they are first and foremost looking at what is happening at the issuer-level. **The big question being posed as a condition of financing in both is whether the issuer is on the path to a credible climate transition or not. So, I am encouraged that both these approaches are focusing on that part.***

The Use-of-Proceeds [approach] is about corporate expenditure as evidence – and that transparency is important to investors”. The other [KPI-linked] is about tracking key performance indicators over the maturity of the bond. I see a lot of synergies because ultimately, they want to achieve the same goal.

*With regards to KPI linked formats – **the challenge will be to convince investors that the KPI selected by corporates is the most appropriate measure** and that the targets in place are ambitious/stretching or not. We also will need to know the likelihood of the targets being achieved. This will determine whether the outcome of a KPI target being achieved – such as the coupon stepping up or down has any value to it.*

[The full interview is available here](#)



“Financing Credible Transition” report



In September 2020, Climate Bonds Initiatives & Credit Suisse published the “Financing Credible Transition” paper, presenting a framework defining an economy-wide credible transition pathways.

It is **inclusive** (traditionally “green” and “brown” actors), **flexible** by addressing whole entity transitions, broad enough to encompass both tied (use-of-proceeds) & general-purpose finance, and sets a high bar, requiring operating performance to be aligned with Paris Agreement targets.

A Transition Framework with 5 categories of economic activities based on the nature of their role in a global, economy-wide transition to the Paris Agreement targets is provided (see infographic below). **Enabling Activities** are considered to cut across all of the categories.

A broader scope than the EU’s definition of “transition”

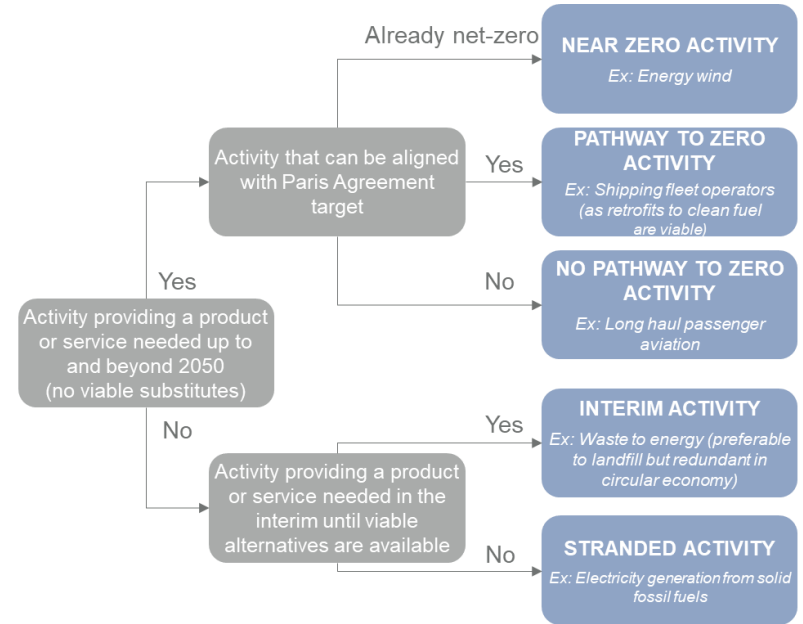
Inclusion of activities needed for an **interim period** (see activity typology below).

- **Consideration of measures reducing emissions/ increasing sequestration** (only addressed in the EU Taxonomy for a limited number of activities).
- Distinction between “**pathway to zero**” & “**no pathway to zero**” (both categories defined under “transitional activities” defined as activities which are not currently close to a net-zero carbon emissions level and therefore must significantly enhance their performance, without lock-in to carbon-intensive assets or processes).

Examples of credible transition measures

Type of activity	Towards a credible transition actions
Pathway to Zero	Decarbonize as fast as possible along appropriate transition pathways.
No pathway to zero	Reduce emissions as much as possible without locking-in technologies that might prevent future rapid decarbonization.
“Interim” activities	Phase out in line with their future sunset date, but in the meantime decarbonize them as fast as possible along appropriate transition pathways.
Stranded’ activities	Phase out, but at the same time take measures that can deliver substantial emissions reductions without locking in those stranded assets & technologies.
Enabling activities	The objective is that the activity makes a substantial contribution to facilitating another activity to follow an appropriate transition pathway. Their own decarbonization is a secondary priority.

CHART | 5 transition categories



“Financing Credible Transition” report

The report set five “Transition Principles” defining the characteristics of credible transition pathways in order to avoid greenwashing. Credible transitioning entities & economic activities are those that are **already following and will continue to follow such pathways** - not setting targets for future alignment.

Summary table of the Transition Principles for activity and entity level transitions

Principle	Details
Credible transition goals & pathways align with 1.5°C global warming limits	<ul style="list-style-type: none"> Transition goals & pathways need to be aligned with global targets for net zero emissions by 2050 and a nearly halving of emissions by 2030. Compatibility with Nationally Determined Contributions [...] is not automatically sufficient. Neither are pathways that are exclusively defined as best-in-class benchmarks (ex: best available technologies).
Credible transition goals & pathways are established by the climate science community and are not entity specific	<ul style="list-style-type: none"> The expertise of the climate science community & technical experts is needed [...]. Using science as a common base for transition pathways, maximizing the action of global emissions reductions & ensuring comparability between transitioning activities & entities in the same industry.
Credible transition goals & pathways do not count offsets, but should count upstream scope 3 emissions	<ul style="list-style-type: none"> Pathways should not account for emissions reductions generated through separate activities, including purchased offsets, but should address scope 1 and 2 and upstream scope 3 emissions as far as this is practically possible.
Credible transition goals & pathways consider technological viability, but not economic competitiveness	<ul style="list-style-type: none"> Development of transition pathways must include an assessment of current & expected technologies. Where a viable technology exists, even if relatively expensive compared to business-as-usual technology, it should be used to determine the appropriate decarbonization pathway for that economic activity.
Credible transition means following the transition pathway – pledges, policies and strategies alone are not sufficient	<ul style="list-style-type: none"> Actual operating metrics are the key indicators of performance, not simply pledges or the implementation of policies and procedures that may or may not deliver operational outcomes. Activities/ entities must be able to credibly demonstrate how they will follow the transition pathway over the financing term, and regular assessment is required to demonstrate that transition is continuing at the necessary scale and pace. In some situations, this will require activity/ entity level decarbonization plans and targets matched to the financing term

Transition action needs to be deployed at 3 levels



Credible measures to reduce emissions/ increase sequestration within activities/entities should:

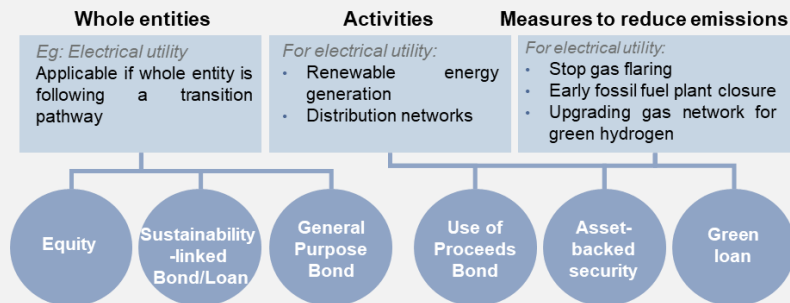
- ✓ Be part of a program to bring the performance of the activity/entity in line with a credible transition pathway
- OR
- ✓ Be recognized individually as making a substantial contribution to climate mitigation
- AND
- ✓ The measures should not lead to a lock-in of GHG intensive assets activities or entities

Source: Climate Bonds Initiatives, “Financing credible transitions” (Sept. 2020)

“Financing Credible Transition” report

Transition creates opportunities for investors, given the range of economy-wide transition actions & the diversity of associated financial instruments.

Application to entity, activity & measures



A need for green and transition labels ?

A distinction between activities that do not have a long-term role to play in a low-carbon economy (due to their high emissions) & those that do (despite their high emissions), providing the foundation of a “transition” label is suggested:

- **Green label** continues to be used for eligible investments in activities/entities that have a long-term role to play and are either already near zero or are following decarbonization pathways in line with halving global emissions by 2030 and reaching net zero by 2050
- **Transition label** for eligible investments that:
 - Either make a substantial contribution to halving global emissions levels by 2030 & reaching net zero by 2050 but will not have a long-term role to play
 - Or will have a long-term role to play, but at present the long-term alignment to net zero goals is not certain.

Source: Climate Bonds Initiatives, “Financing credible transitions” (Sept. 2020)

CBI Survey: summary of stakeholders’ views

The CBI developed a questionnaire for 27 stakeholders interested in the concept of transition bonds, including organizations that had issued labelled bonds.

- There is a broad agreement the concept of ‘transition’ referred to activities that **significantly reduce GHG emissions relative to current practice**, but not enough to comply with the EU taxonomy’s definitions of green.
- Few people appreciated that the EU taxonomy includes thresholds for “pathway to zero” activities.
- The transition label was considered applicable to **hard-to-abate sectors**.
- A minority of stakeholders thought that definitions of transition might vary between **emerging & developed markets** or in regions where renewable energy was not feasible.
- The term ‘sustainability’ should be used for environmental issues extending beyond climate, like circular economy or social issues.
- There were different views about whether the transition label was needed. Opponents were concerned that transition would be used to excuse weak or insufficiently demanding strategies to decarbonize, supporting greenwashing. **Deciding who and how these standards should be set was controversial**.
- There was strong support for any use-of-proceeds transition bond issuance to be accompanied by an enterprise level carbon reduction strategy. To be credible, such a strategy needed short-term KPIs linked to material reductions in emissions and support from (carbon pricing).

Stakeholders	Numbers of interviews
Banks	6
Investors	7
Issuers	7
Policy marker/MDB	2
Think tank	5
Total	27

More details of the survey can be found in the report.

To support the growth of climate transition finance, market practitioners through the ICMA has launched guidelines on the disclosures that should be made by issuers on their climate change strategy when raising funds in debt capital markets.

The concept of “climate transition” focuses principally on the credibility of an issuer’s climate change-related commitments and practices.

To meet the global objectives enshrined within the Paris Agreement on Climate Change to keep global temperature rise this century well below 2 degrees Celsius above pre-industrial levels and to pursue efforts to limit the temperature increase even further to 1.5 degrees Celsius, **significant financing is needed.**

To help facilitate these flows, **clear guidance and common expectations to capital markets participants on the practices, actions and disclosures to be made available when raising funds in debt markets for climate transition-related purposes must be provided for two formats of financial instruments (see on the right):**

Two main fixed-income financing formats

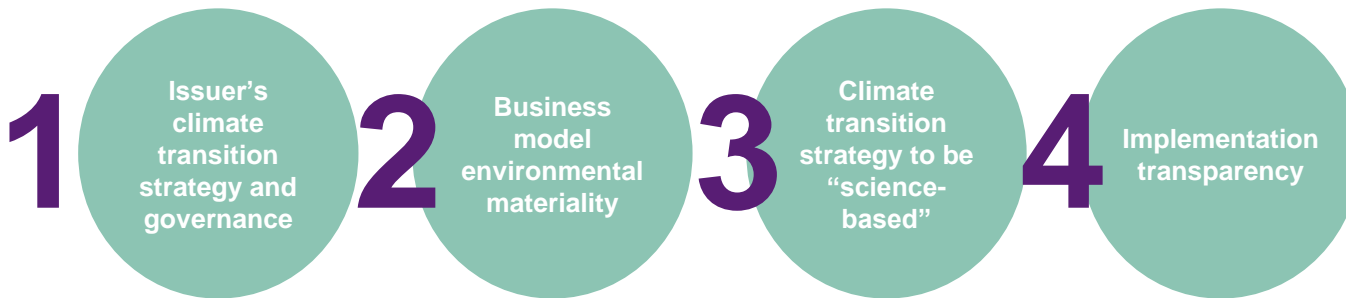
1

Use of Proceeds instruments, defined as those aligned to the Green and Social Bond Principles or Sustainability Bond Guidelines

2

General Corporate Purpose instruments aligned to the Sustainability-Linked Bond Principles

Four key recommendations



Source: ICMA (Dec 2020), Climate Transition Finance Handbook Guidance for Issuers

1. Issuer's climate transition strategy and governance

1

Issuer's climate transition strategy and governance

A "transition" label applied to a debt financing instrument should serve to communicate the implementation of an issuer's corporate strategy **to transform the business model** in a way which effectively addresses climate-related risks and contributes to the alignment with the goals of the Paris Agreement.

Disclosure

Disclosures regarding corporate strategies may be aligned with recognized reporting frameworks such as the recommendations of the Task Force on Climate-Related Financial Disclosures (TCFD), or similar frameworks. Suggested information and indicators:

- **A long-term target to align with the goals of the Paris Agreement**
- **Relevant interim targets** on the trajectory towards the long-term goal
- Disclosure on the issuer's levers towards decarbonization, and strategic planning towards a long-term target to align with the goals of the Paris Agreement
- **Clear oversight and governance of transition strategy**
- Evidence of a broader sustainability strategy to mitigate relevant environmental and social externalities and contribute to the UN Sustainable Development Goals

Rationale

- Corporate climate change strategies should respond to stakeholder expectations by **purposefully and explicitly seeking to play a positive role in achieving the Paris Agreement**. A range of climate change scenario providers exist in the market today to inform strategy design.
- The choice of the relevant provider, or the decision to design an in-house scenario are up to the issuer. However, regardless of the source, **an issuer's strategy should be guided by the objective of limiting global temperature increases ideally to 1.5°C and, at the very least, to well below 2°C**.

Independent review, assurance and verification

Such a review should include:

- Alignment of both the long-term and short-term targets with the overall scenario
- The credibility of the issuers' strategy to reach the targets

Source: ICMA (Dec 2020), Climate Transition Finance Handbook Guidance for Issuers

2. Business model environmental materiality

2

Business model environmental materiality

The planned climate transition trajectory should be relevant to the **environmentally material parts of the issuer's business model**, taking into account potential future scenarios which may impact on current determinations concerning materiality.

Disclosure

Discussion of the materiality of the planned transition trajectory may be included in the disclosures referenced for Element 1 above.

Rationale

Climate transition financing should be sought by the issuer for **the funding needed in the strategic change over time to its 'core' business activities**.

We note that the climate transition is not the only change faced by companies and that many are involved in various transformations across other business functions. The climate transition trajectory as far as it relates to financing should also be **a material factor to the future success of the business model, as opposed to being an incidental aspect**. The trajectory should also consider the salience of an issuer's climate impacts on the environment and society and seek to mitigate negative externalities.

Independent review, assurance and verification

Externally-provided comfort around materiality considerations may not be appropriate in all cases, however the accounting profession may provide guidance as required.

Source: ICMA (Dec 2020), Climate Transition Finance Handbook Guidance for Issuers

3. Climate transition strategy to be “science-based”

3

Climate transition strategy to be “science-based”

The planned transition trajectory should:

- Be quantitatively measurable (based on a measurement methodology which is consistent over time);
- Be aligned with, benchmarked or otherwise referenced to recognized, science-based trajectories where such trajectories exist;
- Be publicly-disclosed (ideally in mainstream financing filings), include interim milestones, and;
- Be supported by independent assurance or verification.

Rationale

With regards to climate change, authoritative scientific analysis has determined the rate of decarbonization (the ‘decarbonization trajectory’) required in the global economy in order to align the various economic activities with those scenarios which imply a Paris Agreement-aligned level of warming.

Science-based targets are targets that are in line with the scale of reductions required to keep the global temperature increase below 2°C above pre-industrial temperatures.

Disclosure

A number of pre-existing disclosure frameworks exist which issuers may find helpful in preparing to disclose their climate transition plans. It is acknowledged that other similar frameworks may be relevant, and that additional guidance may emerge over time.

Suggested information and indicators:

- Short, medium, and long-term greenhouse gas reduction targets aligned with the Paris Agreement;
- Scenario utilized, and methodology applied (e.g. ACT, SBTi, etc.)
- Greenhouse Gas objectives covering all scopes (Scope 1, 2 and 3)
- Targets formulated both in intensity and absolute terms

Independent review, assurance and verification

A variety of service providers are currently offering independent review services which set out to review a particular issuer’s proposed quantified “decarbonization trajectory” and offer an opinion on the extent to which this is aligned with reference trajectories noted in Element 1 above. Such independent, expert reviews provide prospective investors with an assessment of whether the proposed trajectory is aligned with the science-based trajectories deemed necessary to limit climate change to safe levels

4. Implementation transparency

4

Implementation transparency

Market communication in connection with the offer of a financing instrument which has the aim of funding the issuer's climate transition strategy should also **provide transparency to the extent practicable, of the underlying investment program including capital and operational expenditure.**

Disclosure

Disclosure of capital expenditure (CAPEX) and operational expenditure (OPEX) plans and other relevant financial metrics to the extent they relate to a transition strategy may be made via a company's annual report, website, or sustainability report. Disclosure of anticipated CAPEX and OPEX line items may take the form of a simple table providing detail on specific elements and their connection to the announced strategy, with estimated amounts involved.

Suggested information and indicators:

- Disclosure on the percentage of assets/revenues/expenditures/divestments aligned to the issuer's transition strategy
- Capex roll-out plan consistent with the overall strategy and climate science

Rationale

- It is **the internal allocation of capital by the company in order to implement the strategy** which will be most important, alongside the governance that supports such re-allocation. It is recommended to provide transparency with regards to the **planned capital and operational expenditure decisions** which will deliver the proposed transition strategy.
- Where a transition may have **negative impacts for workers and communities**, issuers should outline how they have incorporated consideration of a **'just transition' into their climate transition strategy** and may also detail any 'social' expenditures that are considered relevant within the context of transition finance.

Independent review, assurance and verification

- Specific assurance or verification of CAPEX and OPEX plans is unlikely to be appropriate given the difficulty in accurately predicting these forward-looking types of expenditures.
- The company may wish to consider providing an analysis of the extent to which outcomes have aligned with original plans, i.e. whether spending took place as anticipated, and in the event it did not, providing explanations as to why.

Source: ICMA (Dec 2020), Climate Transition Finance Handbook Guidance for Issuers

The Sustainable Bond Market (SBM) is a market component within the Debt Capital Market (“Bonds”) segment of the London Stock Exchange Group (LSEG) exclusively listing sustainable finance debt securities. The SBM offers more than 250 bonds, of which many are the world’s first in terms of currency, geography, or structure. It currently lists bonds from 23 countries worth more than £56bn.

The Rationale for Transition Bonds

- **The Transition Bond Segment is a sub-segment within the SBM** alongside the Use-of-Proceeds and General Corporate Purpose segments.
- Highly emitting companies have historically not been able to tap into dedicated / delineated sustainable finance opportunities (i.e., beyond ESG integration or some Indexes).

Emphasizing the transition efforts of high emitting companies through *sui generis/ad hoc* filters, segments or approaches, could help such companies tap into sustainable finance flows for their decarbonization strategies.

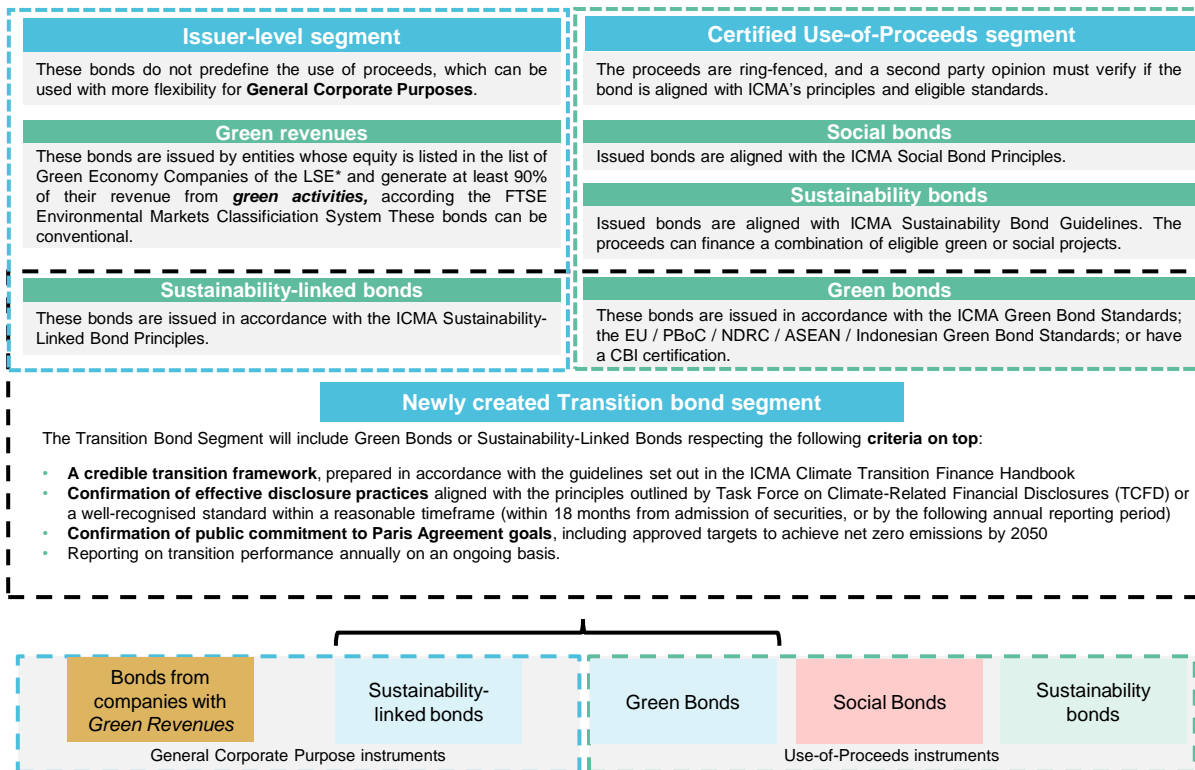
Momentum for these products builds up in the context of:

- A growing interest and appetite of investors towards portfolio transition strategies and transition-labelled products (defensive approach)
- Attracting additional capital from investors poised to be very activist from a climate change mitigation standpoint (offensive approach).

An Overlay for Existing Market Segments

- The bonds issued on **the SBM’s transition bond segment can take two forms**, as Issuers will be able to include both:
 - Use of Proceeds instruments, mainly Green Bonds issued by high emitting companies when these Bonds serve decarbonization purposes
 - General Corporate Purpose instruments aligned with the ICMA’s Sustainability-Linked Bond Principles.
- **The “transition” label of the LSEG can be characterized as an overlay to existing products or a distinctive feature rather than a financial product in itself.**
- An investor can distinguish between the different sustainable debt instruments listed on the LSE and efficiently **single out transition bonds to facilitate the financing of transition efforts of companies in higher-emitting sectors.**

A focus on the LSEG's Transition Bond Segment



4.6 | NATIXIS' GREEN WEIGHTING FACTOR

Steering transition at balance sheet level



What it is:

The Green Weighting Factor is an **internal mechanism** that **links analytical capital allocation to the degree of climate and environmental performance** of each financing.

- It is a tool that **incentivizes the origination of environmentally friendly loans** by weighting on the risk weighted assets linked to the loans
- RWAs being linked to their business profitability, the **originators are encouraged to account for the environmental aspect of each deals**
- In the end, the numbers of **environmentally friendly deals in the bank's balance sheet is bound to increase.**



Its Purpose:

The Green Weighting Factor was designed to **actively manage and steer Natixis CIB origination & balance sheet's transition.**

- **Accelerate the CIB's transition** to Sustainable finance i.e. incentivizing our green business origination (including in carbon intensive sectors)
- **Integrate Climate Transition risk** in the overall assessment of lending transactions , i.e., penalizing deals with negative impact on climate,
- **Monitor the CIB's climate strategy** towards the UN & Paris Agreement goals
- **Be prepared to upcoming regulations** regarding bank's response to climate risk.



Why it matters:

It is a **unique innovation**, fully integrated into the bank's processes and IT system representing an **unprecedented management tool and an asset to further enhance our strategic dialogue with clients.**

The tool is already proving its use cases:

- In our **credit process & lending decision making**
- In our **strategic dialog with clients** and the quality of our sustainable finance products structuring
- In our **commercial strategic planning** : client tiering, priority setting & green / transition opportunity screening
- In our **active balance sheet portfolio management** : distribution, securitization

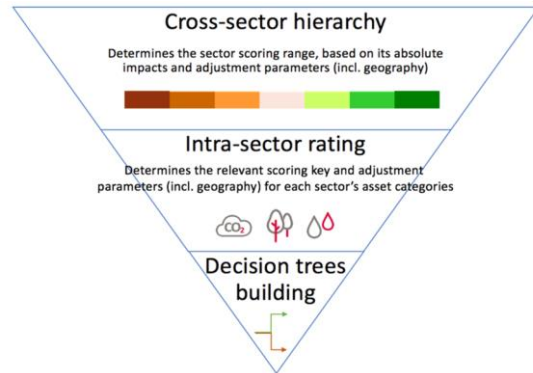
Steering transition at balance sheet level

- Rating methodology using **7-level scale**
- **Climate change centric**, adjusted by **most material environmental externalities**: biodiversity, water, pollution, waste
- **Simple tool**, with no room for interpretation: limited number of criteria, retrievable information, thresholds
- Using a **life-cycle analysis approach** along with established market practices
- **Sectorial approach**: cross-sector hierarchy and cross-asset hierarchy within each sector

DEDICATED PURPOSE FINANCING

Objective: determine the “color” (rating) of each loan **depending on the environmental impact of the object being financed**

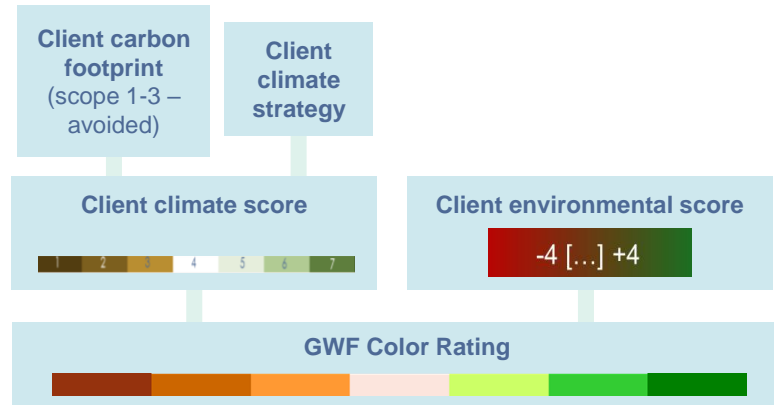
Tool: development **46 different decision trees** for each activity within 8 macro-sectors



GENERAL PURPOSE FINANCING

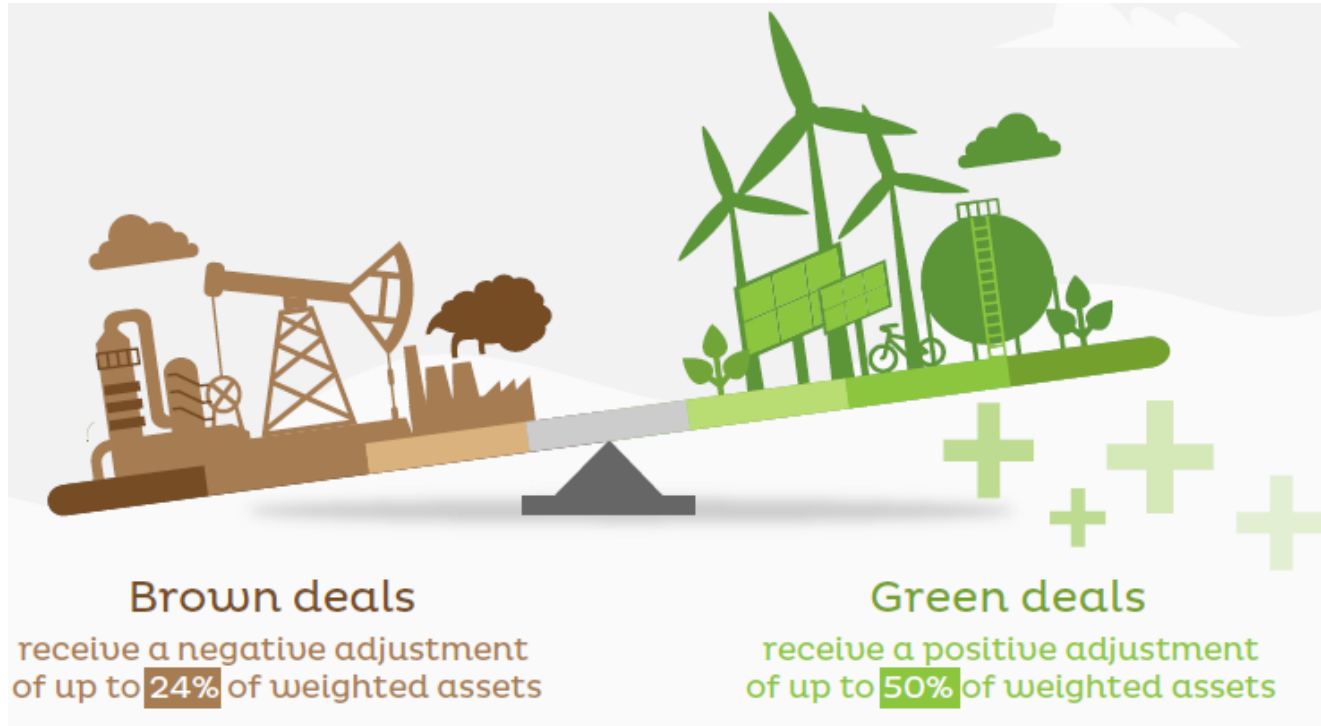
Objective: determine the “color” (rating) of each corporate and public client depending on its **carbon footprint, strategy to decarbonize and impact on most material environmental issue**

- Rating of clients representing 80% corporate exposure



Steering transition at balance sheet level

Scale of risk weighted assets adjustment



Steering transition at balance sheet level

Long term target: align Natixis' balance sheet with the objectives of the Paris Agreement on climate (below +2°C trajectory)

- **Set targets** (short, medium, long term)
 - For Natixis Corporate Investment Bank (CIB)
 - For each business line
- **Actively manage balance sheet's climate impact**

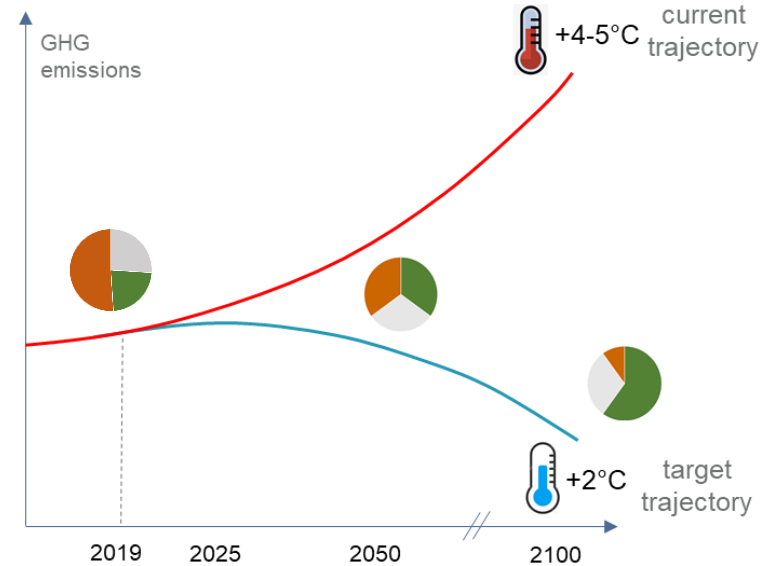
Internal indicators to monitor progress:

- **Green/brown mix of nominal exposure and RWA**
(monitors shift of financing portfolio)
- **Green/brown mix of underwritings**
(monitors shift of financing new origination)
- **EVA indicator**
(used to objectivize origination teams)

Expected frequency of monitoring: quarterly starting Q4 2019

- Transparency: regular disclosure of progress (at least annual)
Indicator expected to be used for external communication:
balance sheet's green/brown mix (nominal exposure & RWA)

FIGURE | Temperature scenarios trajectories



Methodology to translate balance sheet's green/brown mix into climate trajectory is still work in progress

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