

LMA

Loan
Market
Association



TREASURY
EXCELLENCE
AS STANDARD

Getting Started in Sustainable Finance

www.lma.eu.com

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Introduction

- This joint ACT and LMA Guide is aimed at newcomers to the sustainable finance loan market and seeks to provide an introduction to its origins and the products on offer to support borrowers' sustainable finance strategies.
- The Guide covers:
 - the background to the emergence of the sustainable lending market in the UK;
 - an overview of global sustainability commitments driving the sustainability agenda;
 - an introduction to the sustainable lending products set out in the Principles issued by the APLMA, LMA and LSTA; and
 - details of resources on hand to help.
- Companies of all sizes and in a cross-section of sectors risk being left behind if they do not get started on their sustainability journey. A base understanding of the key sustainability considerations is therefore vital moving forward.
- Sustainable finance can not only provide the finance needed for transition but can also help identify the expertise needed to support companies on this journey.

Background to the emergence of the sustainable finance market

- Sustainability is increasingly important for companies seeking access to capital globally.
- Drivers of sustainability include national and international sustainability commitments, stakeholder activism, media focus and public pressure.
- Increasingly financial institutions have been setting ambitious climate and broader sustainability goals, which will impact their lending behaviour.
- There is growing scrutiny of companies and their sustainability credentials, from both a regulatory and public perspective.
- Regulation is being developed nationally and globally to support and encourage sustainable finance and sustainable supply chains.

Sustainability matters: international initiatives

Set out below is a non-exhaustive list of initiatives that have shaped the global sustainability agenda.

Regulation/Treaty/ Initiative	Description
The Paris Agreement	<p>The Paris Agreement, adopted at COP21 in Paris in December 2015 and which entered into force in November 2016, was the first ever universal, global climate agreement. It includes agreement on a long-term goal to limit global temperature increases to well below 2°C above pre-industrial levels, and to pursue efforts to limit the increase to 1.5°C above pre-industrial levels.</p> <p>Significantly, the Paris Agreement (Article 4, paragraph 2) mandated that each party prepare, communicate and maintain successive nationally determined contributions that it intends to achieve (The Paris Agreement United Nations).</p>
UN Sustainable Development Goals (SDGs)	<p>The 17 SDGs were set in 2015 as part of UN General Assembly Resolution 70/1 outlining the 2030 Agenda for Sustainable Development, and came into effect in January 2016. The SDGs are intended to provide a blueprint to achieve a better and more sustainable future for all. They are aimed at addressing the global challenges faced by society, including those related to poverty, inequality, climate change, environmental degradation, peace and justice. The SDGs are intended to be achieved by 2030 (United Nations Sustainable Development).</p>
UN Race to Zero	<p>The UN's Race to Zero is an international campaign, part of the United Nations Framework Convention on Climate Change, otherwise known as UNFCCC, to mobilise action in the fight against climate change and to promote the potential benefits of sustainable growth. The Race is the largest alliance committed to achieving net zero carbon emissions by 2050. It includes non-State actors such as companies, financial institutions, cities and 52 states and regions.</p>

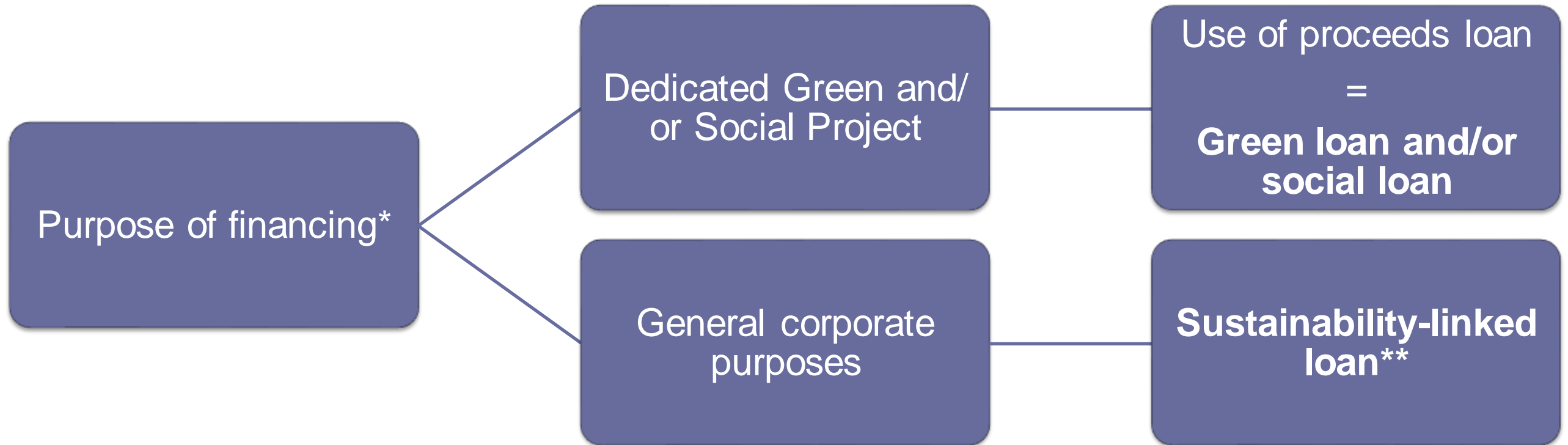
Sustainability matters: international initiatives

Regulation/Treaty/ Initiative	Description
UN Principles for Responsible Investing (PRI)	The PRI was established in 2006 by the UN to reflect the increasing relevance of ESG issues to investment practices. It has over 5,000 signatories representing over \$121trn of assets under management.
Kunming-Montreal Global Biodiversity Framework (GBF)	The GBF was adopted by the COP15 on 19 December 2022 and replaces the Aichi Biodiversity Targets. The GBF sets out an ambitious pathway to reach the global vision of a world living in harmony with nature by 2050. Among the GBF's key elements are 4 goals for 2050 and 23 targets for 2030. More information can be found at: https://www.cbd.int/gbf/
High Seas Treaty 2023	On 4 March 2023, countries meeting at the United Nations reached a significant milestone for the protection of the oceans and for efforts to stem global biodiversity decline when they agreed a new international treaty to safeguard marine life in areas that lie beyond national jurisdiction. The Treaty was formally adopted on 19 June 2023. The Treaty will take effect 120 days after it is ratified by at least 60 countries.
Net Zero Banking Alliance (NZBA)	Launched in April 2021, the NZBA is a group of 134 leading global banks committed to financing ambitious climate action to transition the real economy to net zero greenhouse gas emissions by 2050.
Race to Resilience	Sibling campaign to the Race to Zero campaign, the Race to Resilience is the UN-backed global campaign to catalyse a step-change in global ambition for climate resilience, putting people and nature first in pursuit of a resilient world where they don't just survive climate shocks and stresses, but thrive in spite of them.

Development of sustainable finance products

- In recent years, a number of specific sustainable finance products have emerged in the market.
- Broadly speaking, these fall into two categories, namely:
 - (i) green and/or social use of proceeds loans; and
 - (ii) sustainability-linked loans (**SLLs**).
- The LMA has, together with the APLMA and the LSTA, developed a set of high-level voluntary market standards¹ for the various types of sustainable lending (the **Principles**) which are recognised globally. Whilst the Principles do not have the force of law or regulation, labelling a loan as “green”, “social” or “sustainability-linked” when it does not comply with the relevant Principles has certain consequences. The Principles are available on the [LMA website](#).
- The International Capital Market Association (**ICMA**) has developed a similar set of principles for the sustainable bond market. The two sets of principles are closely aligned with a view to promoting consistency across financial markets. More information can be found on the [ICMA website](#).

Sustainable lending products – which to consider:



* Use of Proceeds Loans and Sustainability-Linked Loans can be used in conjunction, but that complexity is for another Guide.

**The LMA has produced Model Provisions for SLLs that look to provide a starting point for the negotiation of SLL provisions. These are available to members on the [LMA website](#). In addition, the [ACT](#) has published a [Borrower's Guide to Sustainability-Linked Loan Terms](#) which is freely available to members and non-members.

Green Loans

- The green loan market aims to facilitate and support the key role that credit markets can play in financing progress towards environmental sustainability.
- In 2018, the APLMA, LMA and LSTA published the first iteration of the Green Loan Principles (GLP) which seek to promote the development of the green loan product by providing a recommended high-level framework of market standards and guidelines for use across the green loan market.
- The GLP define green loans as “*any type of loan instrument and/or contingent facilities...made available exclusively to finance, re-finance or guarantee, in whole or in part, new and/or existing eligible Green Projects and which are aligned to the four core components of the GLP*”, the core components being:-
 1. Use of Proceeds
 2. Process for Project Evaluation and Selection
 3. Management of Proceeds
 4. Reporting
- The GLP include a non-exhaustive list of eligible Green Project categories that foster a net zero emissions economy, protect and restore the environment, facilitate adaptation to climate change, and/or provide other environmental benefits.

Social Loans

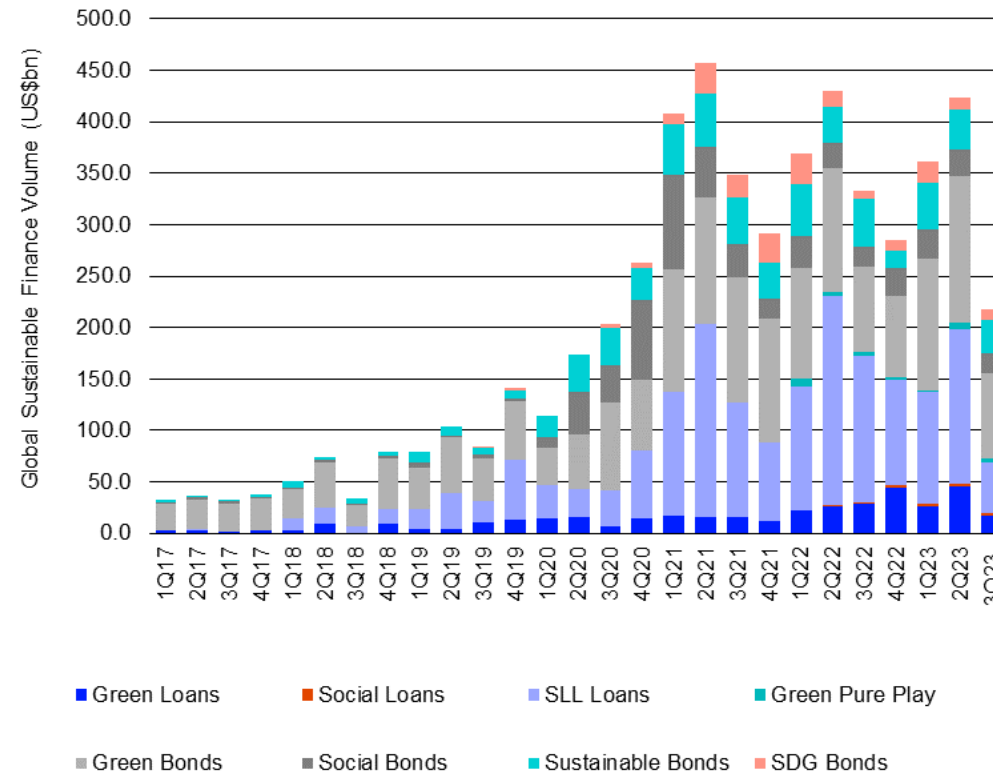
- The social loan market aims to facilitate and support the key role that credit markets can play in financing the mitigation of social issues and challenges, and/or the achievement of positive social outcomes.
- In 2021, the APLMA, LMA and LSTA published the first iteration of the Social Loan Principles (SLP), setting out a framework enabling all market participants to understand the characteristics of a social loan, and which is based around the same four core components as the GLP.
- *The SLP define social loans as “any type of loan instrument and/or contingent facilities...made available exclusively to finance, re-finance or guarantee, in whole or in part, new and/or existing eligible Social Projects, and which are aligned to the four core components of the SLP”, the core components being:-*
 1. Use of proceeds
 2. Process for project evaluation and selection
 3. Management of proceeds
 4. Reporting
- Social Projects should directly aim to address or mitigate a specific social issue and/or seek to achieve positive social outcomes including for, but not limited to, a target population (defined within the SLP).

Sustainability-Linked Loans

- SLLs are a transition tool, supporting the borrower as it seeks to improve its overall sustainability performance.
- In 2019, the APLMA, LMA and LSTA published the first iteration of the Sustainability-Linked Loan Principles (SLLP), setting out a framework to articulate the fundamental characteristics of SLLs, based around five core components being:-
 1. Selection of Key Performance Indicators (KPIs)
 2. Calibration of Sustainability Performance Targets (SPTs)
 3. Loan Characteristics
 4. Reporting
 5. Verification
- Under the SLLP, SLLs are defined as *“any types of loan instruments and/or contingent facilities... for which the economic characteristics can vary depending on whether the borrower achieves ambitious, material and quantifiable predetermined sustainability performance objectives.”*
- The aim is to support a borrower’s efforts in improving its sustainability profile over the life of the loan by aligning the borrower's sustainability performance with the loan terms.

How popular are sustainable lending products?

- The figure below illustrates the scale of the sustainable finance market by providing a breakdown of the global volume of sustainable finance (US\$bn).



Source: LSEG LPC, 2023

How to choose the right product



In selecting the right product for your business, some of the questions to ask include:

- Would you benefit from raising a loan that has ESG attributes?
 - Are there commercial, financial and/or operational benefits?
 - Is it a key part of your sustainability / ESG strategy?
 - Is it something that your stakeholders are expecting?

- Do you have a specific ESG project in mind that needs financing?

- Specifically for SLLs, can you identify suitable KPIs / SPTs relevant for your sector and your organisation?
 - Have you set short-, mid- and long- term targets for some of your objectives?
 - Do you have relevant targets that cover the tenor of the loan or part of it?
 - Is the data readily available?
 - Is historical data available?
 - Is the data reliable, robust and verifiable?
 - Do you have a set of KPIs that you have already been tracking?
 - Is the KPI/SPT aligned with your long-term ESG strategy?
 - Is the SPT beyond business as usual?
 - Is the data benchmarkable?

How to choose the right product



Green / social loans

- Provides investors with a transparent use of funds lent
- Easier to report on to stakeholders
- Transparent link of funds to specific projects

- Requires tracking of funds dispersed
- Funds unavailable for general use and to support working capital needs
- Requires frequent verification of use of proceeds
- Timing of disbursement may have to be linked to actual use of funds

Sustainability-linked loan

- Enables borrower to use funds for a wider range of purposes
- Can be used to fund projects not yet specifically identified
- Easier to fund projects which may fail key aspects of the Principles

- KPIs may not be considered appropriate
- Targets may need to be revised in the future

What are the potential benefits to corporates in using sustainable lending products?

Benefits for corporates may include, but are not limited to:

- building stronger, values-based relationships with stakeholders;
- reinforcing internal stakeholders' commitments towards the achievement of an organisation's ESG projects and/or sustainability objectives;
- communicating your sustainability strategy to a wider audience, enhancing transparency, reputation and credibility;
- aligning your sustainability strategy with your financing options, and showing commitment to achieving sustainability goals with a correlated economic impact;
- access to wider pool of prospective investors; and
- encourage, and provide a contractual structure around, monitoring and assessing the borrower's ESG performance on an ongoing basis, helping to reduce the risk of unexpected ESG liabilities materialising in the future.

LMA resources: available to members and non-members at <https://www.lma.eu.com/sustainable-lending/resources>

Green Loans

[Green Loan Principles](#)
[Guidance on Green Loan Principles](#)
[Guidance for Green, Social, and Sustainability-Linked Loans External Reviews](#)

Sustainable Real Estate Finance

[Guidance on the application of the Green Loan Principles in the real estate finance \(REF\) investment lending context – Green buildings](#)
[Guidance on the application of the Green Loan Principles in the real estate finance \(REF\) lending context – Retrofit projects](#)
[Guidance on the application of the Sustainability-Linked Loan Principles in real estate finance and real estate development finance](#)

Social Loans

[Social Loan Principles](#)
[Guidance on Social Loan Principles](#)
[Guidance for Green, Social, and Sustainability-Linked Loans External Reviews](#)

Sustainability-Linked Loans

[Sustainability-Linked Loan Principles](#)
[Guidance on SLLP](#)
[Model Provisions for SLLs and term sheet](#)
[Guidance for Green, Social, and Sustainability-Linked Loans External Reviews](#)
[Sustainability Co-ordinator Guidance](#)
[LMA and ELFA Best Practice Guide to Sustainability-Linked Leveraged Loans](#)
Articles on protecting the integrity of a sustainability-linked loan:-

- [KPI Selection: A Matter of Materiality](#)
- [Fear of Failure Frustrating Ambition](#)
- [A Matter of Time](#)

General resources

[Sustainable Lending Glossary of Terms](#)
[Guidance for Company Advisers to ESG Disclosure in Leveraged Finance Transactions](#)
[ESG Diligence Questionnaire - Asset Manager](#)
[Best Practice Guide for Term Sheet Completeness](#)
Article – [Financing a Sustainable Future for Aviation](#)
Article – [Financing Sustainability in Shipping](#)
Article – [Trade Finance: How to set up a Sustainability-Linked Loan](#)

ACT resources and initiatives

- [Borrower's Guide to Sustainability-Linked Loan Terms](#)
- [ACT webpage: ESG/Sustainable Finance](#)
- [Sustainability: An introduction to ESG - Online course - FutureLearn](#)
- [Sustainability: The role of Private Sector Finance - Online Course – FutureLearn](#)
- [Sustainability: The role of financial reporting – Online Course - FutureLearn](#)

Other helpful resources

- [UK Business Climate Hub](#)
- [Guidance on Use of Sectoral Pathways for Financial Institutions](#)
- [Towards a Global Baseline for Net-Zero Transition Planning](#)
- [Fact Sheet: Net Zero-aligned Financial Centre](#)
- [Task Force on Climate-related Financial Disclosures](#)
- [Greening Finance: A Roadmap to Sustainable Investing – UK GOV](#)
- [Transition Plan Taskforce – UK](#)
- [ICMA KPI registry](#)
- [ICMA Climate Transition Finance Handbook](#)

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