Updates in the Sustainability-Linked Bonds ("SLB") market

Continued issuances of SLBs in SGD: In February 2021, the SGD bond market saw the first SLB priced from Surbana Jurong Pte Ltd ("SRBJNG"), an unlisted global urban, infrastructure and managed services consulting firm which raised SGD250mn. Since then, there has been four more SLB issuances that came to market, raising ~SGD1.8bn. Two SLBs totalling SGD500mn was priced YTD, representing half of all green, social, sustainability, sustainability-linked ("GSSSL") instruments priced so far (excluding GSSSL from statutory boards).

Some recap: Unlike green bonds where the use of proceeds are catered for specific green projects, according to Bloomberg, SLBs can be viewed as behaviour-based debt, where the intent is to encourage issuers to modify their behaviour. Like sustainability-linked loans ("SLL") which has a longer history in Singapore, SLBs are structurally linked to the issuer's sustainability targets, expressed through key performance indicators which are measurable and trackable. These key performance indicators are termed as Sustainability Performance Targets ("SPTs") for SLB issuances. If structured appropriately, these should catalyse change across the issuer's entire business operations.

SLBs are instruments that can finance transitions: At OCBC Credit Research, we continue to hold the view that transition finance is an important part of the financing equation on the quest towards decarbonisation and that SLLs and SLBs are key instruments in meeting such transition needs. This is especially more so as transition-labelled bonds (a use of proceeds bond) is lacking traction. As at 10 June 2022, there are only ~SGD17.2bn of transition bonds outstanding globally per Bloomberg data (including self-reported ones), in contrast to ~SGD216bn of outstanding SLBs. This is in part due to lack of clarity on what constitutes transition activities. Lack of clarity over transition activities can also apply to SLBs, although unlike transition-labelled bonds, SLBs are explicitly linked to behavioural changes. While certain investors still prefer green bonds over SLBs, SLBs is becoming the main format for transitioning companies where growth in SLBs is being aided by International Capital Market Association ("ICMA") Sustainability-Linked Bond Principles 2020 (rolled out as voluntary guidelines since June 2020). It is perhaps no coincidence that the largest SLB issuer so far in the SGD corporate credit market with SGD975mn outstanding is Sembcorp Industries Ltd ("SCI") and where SCI is also a green bond issuer. Power generation is a key business for SCI. Whilst the company still generates power using fossil fuel, the company has invested in renewable power since 2012 and is in the midst of transitioning to becoming greener. For more details on SLBs please refer to our SGD Year 2022 Credit Outlook.

SGD SLBs more insulated from allegations of greenwashing? In the past 12 months, allegations of greenwashing have come to the fore, culminating in US and German regulators investigating certain asset management companies. As far as we are aware, there have been no significant concerns in the SGD GSSSL market thus far with regards to greenwashing allegations. While we cannot claim that greenwashing does not happen in Singapore, in our view it is less likely in the SGD GSSSL market, which only started to become more active in 2020. By 2021, greenwashing was already a prevalent concern which market participants and regulators in Singapore were well aware of, making it less likely for an issuer with unsubstantiated claims to successfully come to market. We note that all four companies who had issued SLBs had set up their sustainability-linked financing framework to be aligned with the ICMA Sustainability-Linked Bond Principles 2020. All four companies had subjected their frameworks and SPTs to external party commentary, although with different levels of surveillance in our view.

Figure 1: Overview of SGD-denominated SLBs

Issuer	Issuer's Key Industry Segment	Issue	UN Sustainability Development Goal Mapping	Nature of Sustainability Performance Targets ("SPT")[1]	External Opinion
Sembcorp Industries Ltd	Power generation and urban development	SCISP 2.66% '32s SCISP 3.735% '29s	Goal 7 and 13	• Reduction of greenhouse gas ("GHG") emissions intensity • Reduction of absolute GHG • Renewable energy capacity	Second Party Opinion by DNV
Ascott Residence Trust	Hospitality REIT; service apartments, hotels and other type of long stay property owner	ARTSP 3.63% '27s	Goal 7, 11 and 13	• Reduction of carbon emissions intensity • Reduction of energy intensity • Green buildings	Second Party Opinion by Vigeo Eiris
Nanyang Technological University ("NTU")	Education	NTUSP 2.185% '36s	Goal 3, 4, 7, 11 and 13	• Reduction of carbon emissions intensity • Carbon neutrality for NTU Yunnan Campus in Singapore	Report on certain agreed upon procedures by PwC
Surbana Jurong Pte Ltd	Urban, infrastructure and managed services consulting	SRBJNG 2.48% '31s	Goal 3, 7, 9 and 11	• GHG emissions intensity • Number of consultancy mandates relating to design of green buildings • Energy consumption levels of company's offices	Report on certain agreed upon procedures by PwC

Source: Bloomberg, Company, OCBC Credit Research
Note: (1) SPTs per the Sustainability-Linked Finance Framework of the issuers; each SLBs may be structured such that they are linked to one or more SPTs
(2) All four of the frameworks are aligned to ICMA Sustainability-Linked Bond Principles 2020

Longer list of potential SLB issuers: Whilst the SGD market only has five SLBs outstanding (from four issuers), a larger number of SGD corporate bond issuers are present in the sustainability-linked financing market through being SLL borrowers and/or have issued sustainability-linked derivatives. In our view, these companies are a pool of potential issuers of SLBs as the market develops further. Aside from those with specific experience in linking their financing to sustainability targets, we also see the SGD corporate credit issuers who are already issuers in the GSSSL market as possible future issuers of SLBs.

Figure 2: SGD Corporate Credit Issuers Present in the Sustainability- Linked Financing Market

Company	Key Industry Segment
ARA Asset Management Ltd	Property investment and management
Ascott Residence Trust	Hospitality REIT
Cagamas Berhad	National mortgage corporation
CapitaLand China Trust	Diversified REIT
Capitaland Group Pte Ltd	Property investment, management and development
CapitaLand Integrated Commercial Trust	Commercial REIT
City Development Ltd	Property development
China Construction Bank Corp	Financial Institution
CPI Property Group SA	Property development
Cromwell European REIT	Industrial REIT
ESR Cayman Ltd	Property investment, management and development
ESR LOGOS REIT	Industrial REIT
Ford Motor Company	Automaker
Frasers Centrepoint Trust	Retail REIT
Frasers Logistics & Commercial Trust	Diversified REIT
Frasers Property Group	Property investment, management and development
Indorama Ventures PCL	Property investment, management
Keppel Corporation Ltd	Property, infrastructure, sustainability solutions, telecommunications
Keppel Infrastructure Trust	Business trust focused on owning infrastructure assets
Lendlease Global Commercial REIT	Commercial REIT
Mapletree Industrial Trust	Industrial REIT
Mapletree Investments Pte Ltd	Property investment, management and development
Mapletree Logistics Trust	Industrial REIT
Nanyang Technological University	Education
Olam International Limited	Agri-business
OUE Commercial Trust	Diversified REIT
PSA Marine Pte Ltd	Port and harbour operator
Sembcorp Industries Ltd	Power generation and urban development
Sembcorp Marine Ltd	Marine and offshore engineering solutions
Singapore Telecommunications Ltd	Telecommunications
StarHub Ltd	Telecommunications
Suntec Real Estate Investment Trust	Commercial REIT
Surbana Jurong Pte Ltd	Urban, infrastructure and managed services consulting
UOL Group Ltd	Property investment, management and development

Source: Company, OCBC Credit Research
Note: (1) Non-exhaustive list
(2) Companies (or their subsidiaries) who has set up Sustainability Linked Financing Frameworks and/or who has issued sustainability linked financing instruments (eg: SLBs, SLLs, derivatives)

Stacking of Sustainability Credentials: Thus far in the SGD corporate credit market, green bonds and SLBs are two distinct instruments though globally, there has been issuances of green SLBs where the bond is linked to specific SPTs whilst at the same time the use of proceeds are for green purposes. Verbund AG, a leading Austrian-based power generation company priced the first green SLB in March 2021 (EUR500mn, 20-year maturity), which was well received by investors. According to the company, more than 90% of the bond deal was allocated to sustainability focused investors. Green SLBs are still a very niche market. We calculate ~SGD5.0bn of such bonds outstanding globally as at 10 June 2022 using Bloomberg's data. The largest green SLB is a RMB-denominated RMB10bn (~SGD2.1bn) 3-year bond priced in May 2022 from China Construction Bank Corp, a big four Chinese bank and one of the largest banks globally. In April 2022, Yunnan Energy Investment Overseas Finance Company Ltd (Guarantor: Yunnan Energy Investment Group Co Ltd, a China-based power generation company) became the first green SLB issuer in the Asiadollar space, pricing a USD230mn 3-year green SLB.

SLBs are still mainly corporate credit instruments: The first SLBs were issued in September 2019 and since then have managed to gain support from corporate credit issuers and investors alike but is little used by governments. According to data from the Climate Bonds Initiative ("CBI"), a not-for-profit funded by various foundations and multilateral organisations, ~88% of SLBs issued in 2021 by volume (in USD billions) were from non-financial corporates, ~5% were from financial corporates while government-backed entities (eg: utilities, airports and universities) comprise the remaining ~7%.

……although no longer just for corporates: However, in January 2022, the City of Helsingborg in Sweden (population of around 150,000) priced an SLB with SPTs linked to absolute GHG emissions, becoming the first public sector issuer to do so. The city has a target of becoming socially, environmentally and economically sustainable by 2035 while Sweden was the first country to legally bind the country to reach net-zero. Legislation was passed in 2017 for Sweden to reach net-zero by 2045. CBI reports that in February 2022, the Arizona Industrial Development Authority priced USD200mn of SLBs in two parts to finance forest restoration activities, becoming the first US municipal issuer of SLBs.

In the sovereign space, Chile priced a landmark USD2bn 20-year SLB in March 2022, becoming the first sovereign SLB issuer globally. The bond's orderbook reached more than USD8bn per S&P Global. Chile's SLB follows on from the country's established track record as a sovereign GSSSL bond issuer. This SLB is linked to absolute GHG emissions and share of non-conventional renewable energy generation in the national electric system. Whilst Singapore has unveiled the Singapore Green Bond Framework which would cater for the upcoming green bond issuance, it remains to be seen if the country will take the next leap into the SLB space. In our view, a sovereign SLB is more demanding vis-à-vis a green bond. If SPTs are selected appropriately, this puts a limelight on a sovereign's commitment to the Paris Agreement which is then tracked closely by the bond market, in contrast to the specific use of proceeds nature of a green bond.

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<u>**Explanation of Issuer Profile Rating / Issuer Profile Score**</u>

Positive ("Pos") – The issuer's credit profile is either strong on an absolute basis or expected to improve to a strong position over the next six months.

Neutral ("N") – The issuer's credit profile is fair on an absolute basis or expected to improve / deteriorate to a fair level over the next six months.

Negative ("Neg") – The issuer's credit profile is either weaker or highly geared on an absolute basis or expected to deteriorate to a weak or highly geared position over the next six months.

To better differentiate relative credit quality of the issuers under our coverage, we have further sub-divided our Issuer Profile Ratings into a 7-point Issuer Profile Score scale.

IPR	Positive		Neutral			Negative	
IPS	1	2	3	4	5	6	7

<u>**Explanation of Bond Recommendation**</u>

Overweight ("OW") – The bond represents **better relative value** compared to other bonds from the same issuer, or bonds of other issuers with similar tenor and comparable risk profile.

Neutral ("N") – The represents **fair relative value** compared to other bonds from the same issuer, or bonds of other issuers with similar tenor and comparable risk profile.

Underweight ("UW") – The represents **weaker relative value** compared to other bonds from the same issuer, or bonds of other issuers with similar tenor and comparable risk profile.

Please note that Bond Recommendations are dependent on a bond's price, underlying risk-free rates and an implied credit spread that reflects the strength of the issuer's credit profile. Bond Recommendations may not be relied upon if one or more of these factors change.

<u>**Other**</u>

Suspension – We may suspend our issuer rating and bond level recommendation on specific issuers from time to time when OCBC is engaged in other business activities with the issuer. Examples of such activities include acting as a joint lead manager or book runner in a new issue or as an agent in a consent solicitation exercise. We will resume our coverage once these activities are completed. We may also suspend our issuer rating and bond level recommendation in the ordinary course of business if (1) we believe the current issuer profile is incorrect and we have incomplete information to complete a review; or (2) where evolving circumstances and increasingly divergent outcomes for different investors results in less conviction on providing a bond level recommendation.

Withdrawal ("WD") – We may withdraw our issuer rating and bond level recommendation on specific issuers from time to time when corporate actions are announced but the outcome of these actions are highly uncertain. We will resume our coverage once there is sufficient clarity in our view on the impact of the proposed action.

Analyst Declaration

The analyst(s) who wrote this report and/or her or his respective connected persons held financial interests in the following above-mentioned issuers or companies as at the time of the publication of this report: Singapore Airlines Ltd, GuocoLand Ltd, Oxley Holdings Ltd, Frasers Centrepoint Trust, Suntec Real Estate Investment Trust, Mapletree Commercial Trust, Frasers Hospitality Trust, Lendlease Global Commercial REIT, Ascott Residence Trust.