FINANCING FRAMEWORK

Green, Social and Sustainability Linked Projects

Punjab National Bank

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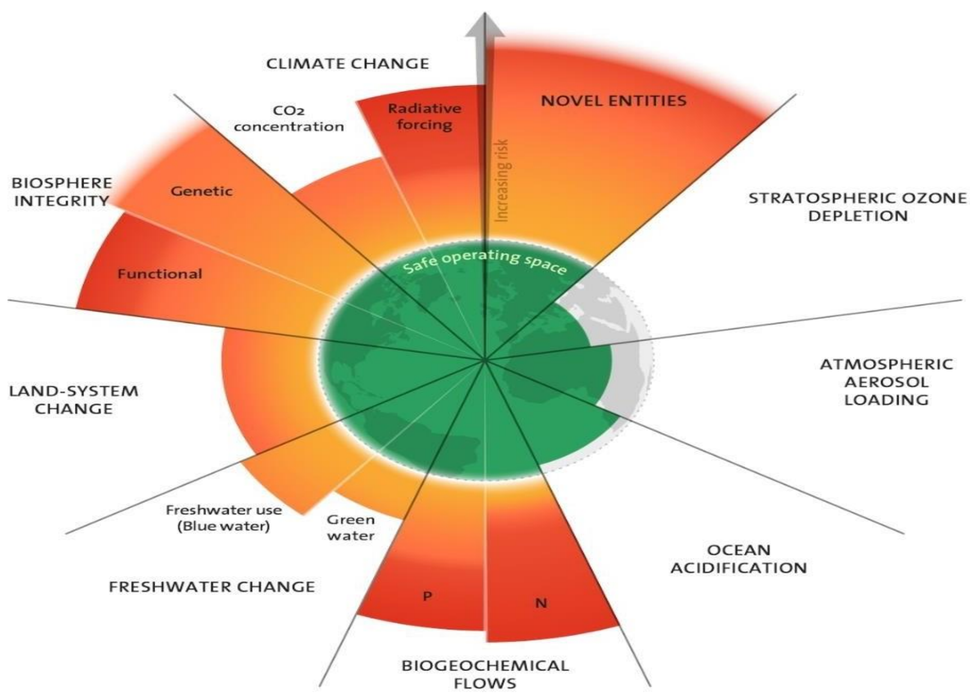
INTRODUCTION

"What we are doing to the forests of the world is but a mirror reflection of what we are doing to ourselves and to one another"

~Mahatma Gandhi

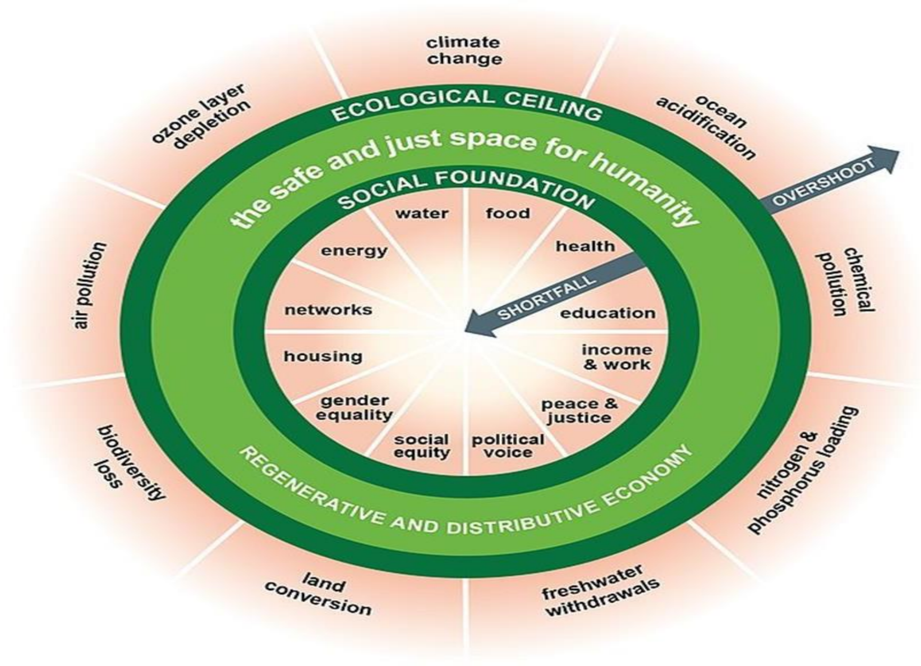
A Case for Sustainability

Financial Stability Board (FSB) has identified that the occurrence of extreme climate events, as well as a disorderly transition to a low-carbon economy, could have destabilising effects on the financial system [1]. Further, the economic implications of environmental issues (such as climate change, resource scarcity, biodiversity loss, and deforestation) and social challenges (such as poverty, income inequality, and human rights) are increasingly being recognized. Many scientific and economic models that capture the sustainability concerns have been developed. One such model by the Stockholm Resilience Centre identifies nine "planetary boundaries" within which humanity can continue to thrive for generations and in 2015, it found that four of them, namely climate change, loss of biosphere integrity, land-system change, and altered biogeochemical cycles (phosphorous and nitrogen) have exceeded their safe limits. The latest update in September 2023 not only quantified all boundaries, but also concludes that six of the nine boundaries have been transgressed. [2]



Doughnut Economics

A popular socio-economic framework, namely doughnut economics, is developed by economist Kate Raworth that combines planetary boundaries with the complementary concept of social boundaries. The Doughnut consists of two concentric rings: a social foundation, to ensure that no one is left falling short on life's essentials, and an ecological ceiling, to ensure that humanity does not collectively overshoot the planetary boundaries that protect Earth's life-supporting systems. Between these two sets of boundaries lies a doughnut-shaped space that is both ecologically safe and socially just: a space in which humanity can thrive. [3]



The Doughnut of social and planetary boundaries

In a similar vein, UNEP claims that an Inclusive Green Economy is an alternative to today's dominant economic model, which generates widespread environmental and health risks, encourages wasteful consumption and production, drives ecological and resource scarcities and results in inequality. An Inclusive Green Economy on the other hand, is an economy which is not only low carbon, efficient and clean in production, but also inclusive in consumption and outcomes, based on sharing, circularity, collaboration, solidarity, resilience, opportunity, and interdependence. [4]

Sustainability at Punjab National Bank: Legacy and Mission

Our legacy of 128 years is testament to our commitment to social and environment cause. The Bank has played a significant role in financial inclusion as well as delivering on number of social welfare schemes by the Government of India and priority sector lending requirements by RBI. Today, the extensive network of the Bank is serving citizens and businesses of India and helping build a more resilient economy.

We promote sustainable practices at every level and processes of our Organization. We promote renewable energy adoption, water conservation, and encourage minimum waste in our operations. We are an equal opportunity employer. The well-being of our employees and customers are central to our strategy. We believe in just and equal society and strive to facilitate the same.

We are aware of the increasing relevance of sustainability safeguards in our business strategy. We understand that sustainability concerns vary from industry to industry, and our policies should be framed accordingly. We also commit to engage with our customers to educate them with the best practices in sustainable operations and promote sustainable finance.

Sustainable Finance

Raising Funds

Green Deposits and Green Bonds are the instruments by which Bank will raise funds which will be earmarked for being allocated towards green finance/ refinance. Such kinds of funds will be used towards achievement of identified environmental outcomes.

Similarly, Social Deposits and Social Bonds will be used towards achievement of identified social outcomes.

Further, these special funds will be deployed for their specific usage within an identified timeline. Moreover, general deposits can also be used for sustainable finance.

<u>Deploying Funds</u>

Financing Instruments (Loan/ Bond) could be categorized into three categories depending on their respective sustainability ambitions:

GREEN (ENVIRONMENTAL)	SOCIAL	SUSTAINABILITY LINKED
Projects with identified benefits to climate and/or environment through Energy, buildings, transport, urban and industrial energy efficiency, waste, water, land use, pollution, infrastructure, and biodiversity.	Projects with identified benefits to affordable basic Infrastructure, access to essential services, employment generation, affordable housing, and socioeconomic advancement and empowerment.	Projects where Issuers/ Borrowers commit to specific improvements in sustainability outcomes, which may be environmental, social, and/or governance related.

These general categories of instruments are further segmented into various other labels, viz. Climate (use of proceeds related to climate change mitigation and adaptation projects), Transition (to help brown sectors to transition towards greener practices), Blue (Sustainable practices related to marine and ocean based activities), SDG-linked (specific commitment to advance Sustainable Development Goal (SDG) related targets), etc. Further, there could be an instrument which caters to requirements of more than one categories, such as sustainability loans/ bonds which has both environmental and social outcomes embedded. However, for the purpose of this framework, we will limit ourselves to the three categories presented in Table above. Identification of sustainability activities and reporting thereof shall also be segmented into these three categories.

Approach adopted for Sustainable Finance

Identification

For Green and Social Finance

Positive Screening based approach is adopted, wherein identified activities have been listed for consideration as sustainable instruments to encourage flow of fund to them. Some exclusions within those activities have also been laid out.

For Sustainability Linked Finance

Though use of proceeds are not defined for this category of instruments, the approach to identify them is similar to positive screening approach wherein targets are set to improve sustainability profile of the borrower over time.

Appraisal

After identification step, the projects will be processed as per extant guidelines.

Reporting/ Monitoring

To facilitate reporting of sustainable portfolio, Flag/ Identifier will be developed in Core Banking Solution (CBS)/ Lending Solution (LeNS)/ Electronic Data Warehouse (EDW)/ Other System. The identification will be developed in two Layers: (i) Type of Instrument, (ii) Use of Proceeds.

The portfolio of green, social, sustainability linked finance will be monitored quarterly.

<u>Assurance Requirements</u>

External Review Opinion

An independent External Review (Second Party) opinion on Financing Framework will be sought, wherever required. The report will be made available on Bank's website.

Internal Checks and Balances

Bank's internal control processes will be leveraged to determine end use of funds in case of Green/ Social financing.

Third Party Verification/ Assurance

An independent third party verification/ assurance of allocation of funds in case of funds raised through Green/ Social instruments will be carried out at designated intervals, wherever required. The report will be made available on Bank's website.

Impact Assessment

International Capital Market Association's harmonized framework [5] for impact investing will be leveraged to conduct impact assessment of sustainable portfolio on social and environmental problems. The report will be made available on Bank's website.

<u>Reporting/ Disclosures</u>

Apart from regular assurance related updates on Bank's website, a sustainability report containing initiatives and outcomes related to sustainability will also be prepared. The report will be made available on Bank's website. Further, a portfolio level disclosure regarding the use of the green deposit funds will also be made part of annual financial statement.

Framework Management

The financing framework along-with Second Party Opinion will be made available on Bank's website. The framework will be reviewed as and when required. For any changes other than mandated by Financial Regulators, the External Review/ SPO will be obtained for the revised framework.

References:

[1] "The implications of climate change for financial stability" publication by Financial Stability Board

[2] "Planetary Boundaries" research by Stockholm Resilience Centre

[3] "Doughnut Economics" by Doughnut Economics Action Lab

[4] "Inclusive Green Economy explained in why does green economy matter" by United Nations Environment Programme (UNEP)

[5] "Harmonised Framework for Impact Reporting" handbook by International Capital Market Association (ICMA)

GREEN FINANCING

"Climate change is the tragedy of the horizon. . . The horizon for monetary policy extends out to two to three years. For financial stability it is a bit longer, but typically only to the outer boundaries of the credit cycle—about a decade. In other words, once climate change becomes a defining issue for financial stability, it may already be too late."

~Mike Carney

Principles and Standards

The green financing framework will be the guiding document for financing eligible green activities as well as for raising green deposits and/ or green bonds. The framework derives its content from following principles and regulations:

- *RBI's Notification on Framework for acceptance of Green Deposits, issued on 11th April 2023 [1]*
- *International Capital Market Association's Green Bond Principles (2021) [2]*
- *Loan Market Association's Green Loan Principles (2023) [3]*

Based on these guidelines, green financing process will have following components:

Use of proceeds

The eligible green finance categories are as below:

Categories
1. Renewable Energy
Description given by RBI • Solar/wind/biomass/hydropower energy projects that integrate energy generation and storage. • Incentivizing adoption of renewable energy. Some Applications Loans or investments in projects or assets related to renewable energy projects that integrate energy generation and storage, including, but not limited to: • Solar Power - photovoltaic/concentrated solar power (with ≥85% of electricity generated to be derived from solar energy), infrastructure and manufacturing, transmission. • Wind Energy - offshore and onshore wind farms (at least 85% of electricity generated from wind energy), infrastructure, manufacturing, generation and transmission.

• Small-scale Hydropower Energy Projects (Producing power not more than 25 MW) or run-of-river projects without artificial reservoir with life-cycle emissions threshold of 100 g CO2e/kWh and facilities with a power density for electricity generation above 5W/m2 • Renewable energy projects generating energy from biomass (Not using feedstock originated from protected areas) • Electricity production from geothermal energy with life-cycle emissions threshold of 100 g CO2e/kWh. • Energy storage (e.g. fuel cells). • Green Hydrogen - production facilities partly or fully dedicated to the production of green hydrogen. • Financing Green Energy Corridors.
2. Energy Efficiency
Description given by RBI • Design and construction of energy-efficient and energy-saving systems and installations in buildings and properties. • Supporting lighting improvements (e.g. replacement with LEDs). • Supporting construction of new low-carbon buildings as well as energy-efficiency retrofits to existing buildings. • Projects to reduce electricity grid losses. Some Applications Loans or investments in projects or assets related to the development and implementation of products or technology that uses energy with higher efficiency. Examples include, but are not limited to: • Energy efficient lighting (e.g. installation/ replacement of LEDs). • Projects to reduce electricity grid losses. (e.g. smart grid meters). • Supporting construction of new low-carbon buildings as well as energy-efficiency retrofits to existing buildings along with design and construction of energy-efficient and energy-saving systems and installations.
3. Clean Transportation
Description given by RBI • Projects promoting electrification of transportation. • Adoption of clean fuels like electric vehicles including building charging infrastructure.

Some Applications

Loans or investments in projects or assets related to the development, manufacture, acquisition, financing, leasing, renting, and operation of means of clean transportation. Examples include, but are not limited to:

- Projects promoting electrification of transportation including charging Infrastructure.
- Projects related to manufacturing/ recycling of batteries used in electric vehicles.

4. Climate Change Adaptation

Description given by RBI

- Projects aimed at making infrastructure more resilient to impacts of climate change.

Some Applications

Loans or investments in projects or assets related to avoid/ reduce weather related disruptions. Examples include, but are not limited to:

- Infrastructure to increase resilience against extreme weather events.
- Information support systems which would monitor/ forecast flood, cyclone, drought or any other climate related hazards.
- Emergency response system in case of climate related disasters.
- Climate induced hygiene emergency and epidemic disaster.

5. Sustainable Water and Waste Management

Description given by RBI

- Promoting water efficient irrigation systems.
- Installation/upgradation of wastewater infrastructure including transport, treatment and disposal systems.
- Water resources conservation.
- Flood defence systems.

Some Applications

Loans or investments in projects or assets related to improve water use efficiency and processing waste water. Examples include, but are not limited to:

- Projects or product that reduce, reuse, or recycle water like water harvesting efficient irrigation systems, etc.
- Projects related to drip and sprinkler irrigation production/ installation.
- Sustainable infrastructure for clean and/or drinking water like water purification plants.
- Waste-water treatment facilities.
- Flood defence systems.

6. Pollution Prevention and Control

Description given by RBI

- Projects targeting reduction of air emissions, greenhouse gas control, soil remediation, waste management, waste prevention, waste recycling, waste reduction and energy/emission-efficient waste-to-energy.

Some Applications

Loans or investments in projects or assets related to pollution prevention and control including waste management. Examples include, but are not limited to:

- Projects targeting reduction of air emissions
- Projects related to greenhouse gas control or soil remediation
- Projects and processes related to waste management which includes waste prevention, reduction and recycling. The projects may also include Municipal solid waste management, industrial solid waste, exhaust gas and effluent.
- Energy efficient production and transmission of electricity, heating or both based on combustion of organic substances contained in waste materials.

7. Green Buildings

Description given by RBI

- Projects related to buildings that meet regional, national or internationally recognized standards or certifications for environmental performance.

Some Applications

Loans or investments in projects or assets related to buildings (new as well as existing) that meet regional, national or internationally recognized standards or certifications for environmental performance. Examples include, but are not limited to:

• Leadership in Energy and Environmental Design (LEED) rating – Gold or higher. • Green Rating for Integrated Habitat Assessment (GRIHA) Council rating 3 or above. • Indian Green Building Council (IGBC) rating - Gold or higher. • Very *good BREEAM rating*
8. Sustainable Management of Living Natural Resources and Land Use
Description given by RBI • Environmentally sustainable management of agriculture, animal husbandry, fishery and aquaculture. • Sustainable forestry management including afforestation/ reforestation. • Support to certified organic farming. • Research on living resources and biodiversity protection. Some Applications Loans or investments in projects or assets related to environmentally sustainable management of Living Natural Resources and land use. Examples include, but are not limited to: • Forest conservation projects, afforestation (plantations) on non-forested land or reforestation on previously forested land. • Environmentally sustainable fishery and aquaculture projects. • Environmentally sustainable agriculture activities like development of agriculture projects that do not deplete or that improve existing carbon pools, precision farming, etc. • Integrated Pest Management • Agricultural technique that decreases amount of soil erosion such as no till farming. • Environmentally sustainable management of agriculture, animal husbandry, fishery and aquaculture. • Conservation of designated wetland/ peatland.
9. Terrestrial and Aquatic Biodiversity Conservation
Description given by RBI • Projects relating to coastal and marine environments. • Projects related to biodiversity preservation, including conservation of endangered species, habitats and ecosystems.

Some Applications Loans or investments in projects or assets related to biodiversity conservation. Examples include, but are not limited to: • Terrestrial and aquatic biodiversity conservation including the protection of forests, coastal, marine, lake or river. • Regenerative agriculture farming practices like zero-carbon farms that helps to improve productivity and enhance biodiversity by reducing the carbon footprint. • Projects related to biodiversity preservation, including conservation of endangered species, habitats and ecosystems.
10. Bank's existing schemes with environmental benefits Bank already has a number of retail and other schemes wherein the use of funds aligns with the above 9 use of proceeds. For Example PNB Green Car Scheme, PNB SATAT (Bio gas) Scheme, PNB Saur Urja Yojana, etc. Such schemes will be periodically reviewed and a catalog of the same along with outstanding will be maintained within Bank's green finance portfolio.

RBI mandated Exclusions:

Following activities will not be considered as a part of Sustainable Finance by the Bank.

- *Projects involving new or existing extraction, production and distribution of fossil fuels, including improvements and upgrades; or where the core energy source is fossil-fuel based.*
- *New or existing Nuclear power generation projects.*
- *Projects involving new or existing Direct waste incineration.*
- *New or existing projects involving Alcohol, weapons, tobacco, gaming, or palm oil related activities.*
- *Renewable energy projects generating energy from biomass using feedstock originating from protected areas.*
- *Landfill projects.*
- *Hydropower Projects generating more than 25 MW.*

Process for Project Evaluation and Selection

Projects with environmental outcomes from the list of Use of Proceeds above, will be eligible for green financing. Such projects will be identified and labelled as Green Projects by a specific and uniform process for credit/ investment sanctions. Once identified as green finance, the project will be processed as per extant guidelines.

Management of Proceeds

Projects selected and financed will become part of the Bank's Green Asset Pool. The projects will be classified under activities mentioned above. At any point in time, Bank will try to maintain higher Green asset in terms of total outstanding in Green Project portfolio than the total net proceeds of all Green Financing Instrument's outstanding. Bank on a best-efforts basis will aspire to maintain a buffer of Eligible Green assets over net proceeds of Green Financing Instruments at all time, Bank will try to substitute maturing proceeds from Green Financing with an appropriate alternative fresh green funds. The Green Assets and Green Liabilities will be monitored on daily basis to detect potential mismatch. In case of a negative mismatch where green liabilities are more than green assets, the Bank's Treasury Unit will direct the mismatch amount to be allocated towards liquid instruments up to a maximum original tenure of one year.

Impact Assessment

International Capital Market Association's harmonized framework for impact investing will be leveraged to conduct impact assessment of green portfolio on environmental problems. Bank will assess the impact associated with the funds lent for or invested in green finance activities/ projects through an Impact Assessment Report with the assistance of external firms by FY 2024-25 and upload Impact Assessment Report on website.

Reporting

The SARC committee shall convene at least at quarterly intervals. Monitoring division shall place a review report through SARC to the Board on annual basis, within three months of the end of the financial year. The review report shall cover the following details:

- Amount raised under Green deposits during the previous financial year.
- List of Green activities/projects to which proceeds have been allocated, along with a brief description of the projects.
- The total amount of outstanding Green Finance proceeds in the respective categories (i.e. bonds, deposits, etc.) and the share of proceeds used for financing purposes.
- Amount of unallocated proceeds and particulars of its temporary allocation.
- A copy of the Third-Party Verification/Assurance Report and the Impact Assessment Report.

Bank shall make appropriate disclosures in their Annual Financial Statements on the portfolio-level information regarding the use of the Green funds raised during current and previous financial year.

External review

Bank will appoint/ empanel external reviewers to seek second party opinion on Framework. Moreover, the allocation of funds raised through green loan or deposit by the Bank during a financial year shall be verified by an independent Third-Party Verifier. The Third-Party Verification shall be done on annual basis. The Third-Party Verification/Assurance Report shall, at the minimum, cover the following aspects:

- Use of the proceeds to be in accordance with the eligible green activities/projects as described. The Bank will monitor the end-use of funds allocated against the deposits raised.
- Policies and Internal Controls including, inter-alia, project evaluation and selection, management of proceeds, and validation of the sustainability information provided by the borrower to the Bank and Reporting and Disclosures.

References:

[1] "Framework for acceptance of Green Deposits" by RBI

[2] "Green Bond Principles" by International Capital Market Association (ICMA)

[3] "Green Loan Principles" by Loan Market Association (LMA)

SOCIAL FINANCING

"May all be happy, all be free from disease, be witness to all auspicious events and no one has to be a part of sorrow"

~Brihadaranyaka Upanishad

Principles and Standards

The social financing framework will be the guiding document for financing eligible social activities as well as for raising social deposits and/ or social bonds. The framework derives its content from following principles and regulations:

- *International Capital Market Association's Social Bond Principles (2023) [1]*
- *Loan Market Association's Social Loan Principles (2023) [2]*

The life cycle of social finance process will have following components:

Use of proceeds

The eligible social finance categories are as below:

<table>
<tr><th>Categories</th></tr>
<tr><td>1. Affordable basic infrastructure</td></tr>
<tr><td>Some Applications

Loans or investments in projects or assets related to basic infrastructure related activities, including, but not limited to
Building social infrastructure facilities clean drinking water, sanitation and sewers in rural and semi-urban areas along with Tier-2 to Tier-4 cities
Construction of roads, basic telecommunication and other infrastructure in rural, semi-urban areas or hilly terrains.</td></tr>
<tr><td>2. Access to essential services</td></tr>
<tr><td>Some Applications

Loans or investments in projects or assets related to essential services and related activities, including, but not limited to
Building schools, hospitals, diagnostic centers and other social infrastructure related activities.
Projects related to Research and Development related activities in Pharmaceuticals and Healthcare industry.
Education loans to individuals.</td></tr>
</table>

3. Affordable housing
Some Applications Loans or investments in projects or assets related to affordable housing segment, including, but not limited to • Affordable housing Projects • Housing loans to individuals for purchase/ construction of affordable/ low-cost house. • Housing loans to individuals for renovation of an existing house.
4. Food security and sustainable food systems
Some Applications Loans or investments in projects or assets related to food security and sustainable food systems, including, but not limited to: • Projects related to new/ improved method/ techniques which helps in efficient farming practices and reduce carbon footprint.
5. Socioeconomic advancement and empowerment
Some Applications Loans or investments in projects or assets related to empowering social advancement, including, but not limited to: • Advances to target populations including, but are not limited to, those who are: 1. Living below the poverty line (as per local guideline); 2. Excluded and/or marginalized populations and/or communities; 3. People with disabilities; 4. Migrants and/or displaced persons; 5. Undereducated (including illiteracy/digital illiteracy); 6. Underserved, owing to a lack of quality access to essential goods and services (as per local guideline); 7. Unemployed; 8. Women and/or sexual and gender minorities; 9. Aging populations and/or vulnerable youths; and; 10. Other vulnerable groups, including as a result of natural disasters. • Advances to Micro, Small and Medium Enterprises (MSME) Sector.

6. Employment Generation
Some Applications Loans or investments in projects or assets related to employment generation, including, but not limited to: • Advances to SMEs and/or microenterprises to prevent and/or alleviate unemployment stemming from socioeconomic crisis, climate transition projects and/or other considerations for a "just transition".
7. Priority Sector Lending
Reserve Bank of India has identified various activities as Priority Sector. Those activities within Priority Sector which aligns with social outcomes listed above will be considered in Bank's social portfolio along with being treated under Priority Sector Lending.

Exclusions:

- *Agriculture activity carried out on land allotted/ classified as forest land, legally preserved areas or any other such protected area.*
- *Units/ borrowers engaging in unfair practices which impacts social or environmental fabric.*

Process for Project Evaluation and Selection

Projects with social outcomes from the list of Use of Proceeds above, will be eligible for social financing. Such projects will be identified and labelled as Social Projects by a specific and uniform process for credit/ investment sanctions. Once identified as social finance, the project will be processed as per extant guidelines.

Management of Proceeds

Projects selected and financed will become part of the Bank's Social Asset Pool. The projects will be classified under activities mentioned above. At any point in time, Bank will try to maintain higher Social asset in terms of total outstanding in Social Project portfolio than the total net proceeds of all Social Financing Instrument outstanding. Bank on a best-efforts basis will aspire to maintain a buffer of Eligible Social assets over net proceeds of Social Financing Instruments at all time, Bank will try to substitute maturing proceeds from Social Financing with an appropriate alternative fresh social funds. The Social Assets and Social Liabilities will be monitored by Credit Review and Monitoring Division on daily basis to detect potential mismatch. In case of a negative mismatch where social liabilities are more than social assets, the Bank's Treasury Unit will direct the mismatch amount to be allocated towards liquid instruments up to a maximum original tenure of one year.

Reporting

The SARC committee shall convene at least at quarterly intervals. The committee shall place a review report to the Board on annual basis within three months of the end of the financial year. The review report shall cover the following details:

- Amount raised under Social deposits during the previous financial year.
- List of Social activities/projects to which proceeds have been allocated, along with a brief description of the projects.
- The total amount of outstanding Social Finance proceeds in the respective categories (i.e. bonds, deposits, etc.) and the share of proceeds used for financing purposes.
- Amount of unallocated proceeds and particulars of its temporary allocation.
- A copy of the Third-Party Verification/Assurance Report and the Impact Assessment Report.

Bank shall make appropriate disclosures in their Annual Financial Statements on the portfolio-level information regarding the use of the Social funds raised during current and previous financial year.

External review

Bank will appoint/ empanel external reviewers to seek second party opinion on the Framework. Moreover, the allocation of funds raised through social loan or deposit by the Bank during a financial year shall be verified by an independent Third-Party Verifier. The Third-Party

Verification shall be done on annual basis. The Third-Party Verification/Assurance Report shall, at the minimum, cover the following aspects:

- Use of the proceeds to be in accordance with the eligible social activities/projects. The Bank will monitor the end-use of funds allocated against the deposits raised.
- Policies and Internal Controls including, inter-alia, project evaluation and selection, management of proceeds, and validation of the sustainability information provided by the borrower to the Bank and Reporting and Disclosures.

References:

[1] "Social Bond Principles" by International Capital Market Association (ICMA)

[2] "Social Loan Principles" by Loan Market Association (LMA)

SUSTAINABILITY LINKED FINANCING

“We have not inherited the world from our forefathers, we have borrowed it from our children.”

~Lester Brown

Principles and Standards

This sustainability linked financing framework is applicable on Sustainability Linked Loans (SLL). The framework derives its content from following principles and regulations:

- *Sustainability Linked Loan Principles jointly developed by Asia Pacific Loan Market Association, LMA and Loan Syndications and Trading Association [1]*
- *IFSCA Notification on Guidance Framework on Sustainable and Sustainability linked lending by Financial Institutions on 26th April 2022. [2]*

Sustainability linked loans are any types of loan instruments and/or contingent facilities (such as bonding lines, guarantee lines or letters of credit) which incentivise the borrower's achievement of ambitious, predetermined sustainability performance objectives. The borrower's sustainability performance is measured using SPTs, which include key performance indicators, external ratings and/or equivalent metrics and which measure improvements in the borrower's sustainability profile.

Sustainability linked loans look to improve the borrower's sustainability profile by aligning loan terms to the borrower's performance against the relevant predetermined sustainability performance targets (SPTs).

Sustainability linked loans characteristics are based around the following five core components which are:

1. *Selection of Key Performance Indicators (KPIs)*
2. *Calibration of Sustainability Performance Targets (SPTs)*
3. *Loan Characteristics*
4. *Reporting*
5. *Verification*

Following process flow to be adopted for Sustainability Linked Financing.

A. Borrower Assessment

Borrower assessment can be done based on the activities undertaken. As Sustainability-Linked Loan (SLL) Principles guidelines clearly mentions that the use of proceeds in relation to a SLL is not a determinant in its categorisation and, in most instances, SLLs will be used for general corporate purposes.

B. Manner of Selection of Key Performance Indicators (KPI)

- Borrower to select relevant KPIs as per overall Business.
- The KPIs must be material to the borrower's core sustainability and business strategy, and address relevant ESG challenges of its industry sector. Proliferation of KPIs that are not credible to be avoided.
- The KPIs should be of high strategic significance to the borrower's current and/ or future operations.
- The KPIs should be measurable or quantifiable on a consistent methodological basis.
- The selected KPIs to be such that they are able to be benchmarked ((i.e. as much as possible using an external reference or definitions to facilitate the assessment of the SPT's level of ambition)
- Borrower to communicate these KPIs to the bank and provide a rationale for the selection of chosen specific KPIs to the Bank which should include:
    - i. A clear definition of the selected KPIs.
    - ii. Applicable scope or parameters, as well as the calculation methodology.
    - iii. Definition of a baseline and be benchmarked against an industry standard and/or industry peers where feasible.

Relationship to Borrower's Overall CSR Strategy

The borrower of a sustainability linked loan should clearly communicate to its lenders its sustainability objectives, as set out in its CSR/ ESG / Sustainability Strategy / Net-zero strategy or disclosures made in regulatory reports like BRSR or non-regulatory disclosures like Sustainability Report, and how these align with its proposed SPTs.

C. Calibration of Sustainability Performance Targets (SPT), to be set in mutual agreement between borrower and lender

The process for calibration of the SPT(s) per KPI is key to the structuring of SLLs, since it will be the expression of the level of ambition the borrower is ready to commit to.

- While setting the SPT(s), following considerations should be taken into account:
  - I. SPTs must be set in good faith and remain relevant (so long as they apply) and ambitious throughout the life of the loan.
  - II. An annual SPT should be set per KPI for each year of the loan term. (In instances where strong rationale is provided as to why this is not appropriate, exceptions to the annual frequency of SPTs can be agreed between the borrowers and lenders).
  - III. The borrower should, where possible and taking competition and confidentiality considerations into account, also highlight any strategic information that may decisively impact the achievement of the SPTs.

- The SPTs should be ambitious, and take into consideration the following factors*:*
  - i. Should represent a material improvement in the respective

KPIs and be beyond both a "business as usual" trajectory and regulatory required targets.

ii. Where possible be compared to a benchmark or an external reference;

iii. Be consistent with the borrower's overall sustainability strategy; and

iv. Be determined on a predefined timeline, set before or concurrently with origination of the loan.

Borrower to communicate following information to bank with respect to target setting;

i. The timelines for the target achievement, including the target observation date(s)/period(s), the trigger event(s) and the frequency of review of the SPTs.
ii. Where relevant, the verified baseline or science-based reference point selected for improvement of KPIs as well as the rationale for that baseline or reference point to be used (including date/period);
iii. Where relevant, in what situations pro-forma adjustments or recalculations of baselines and/or recalculation of KPIs and subsequent SPTs will take place;
iv. Where possible and taking competition and confidentiality considerations into account, how the borrower intends to reach such SPTs, e.g. by describing its ESG strategy, supporting ESG governance and investments, and its operating strategy, i.e. through highlighting the key levers/ type of actions that are expected to drive the performance towards the SPTs as well as their expected respective contribution, in quantitative terms wherever possible; and
v. Any other key factors beyond the borrower's direct control that may affect the achievement of the SPTs.
vi. Taking pre-signing Second Party Opinion (SPO)/ External Review or KPI/ SPT assessment by borrower where relevant and required. Post-signing by, in case of any

material changes to parameters/ KPI methodology/ SPT(s) calibration.

D. Financial and/or structural characteristics to incentivize the achievement of the SPTs and /or involve a penalty if the SPTs are not met

This to be decided and implemented and should also be communicated to the borrower in Terms and Conditions of Sanction.

Eg: the margin under the relevant loan agreement will often be reduced where the borrower satisfies a pre-determined SPT as measured by the pre-determined KPIs and vice versa

E. Reporting

Borrowers should, at least once per annum, provide the bank with the following details:

i. Up-to-date information sufficient to allow bank to monitor the performance of the SPTs and to determine that the SPTs remain ambitious and relevant to the borrower's business.
ii. A sustainability confirmation statement with verification report attached, outlining the performance against the SPTs for the relevant year and the related impact, and timing of such impact, on the loan's economic characteristics.

F. Mechanism for verification of performance

Borrower should provide the bank with the following documents for the verification purpose:

The borrower should provide bank with an independent and external verification of the borrower's performance done by a qualified external reviewer with relevant expertise.

G. Review

For publicly traded companies, Bank will use borrower's public disclosures to verify its performance against its SPTs. However, for unlisted companies where information relating to SPTs is not made publicly available or otherwise accompanied by an audit/ assurance statement, external review of borrowers' performance against its SPTs will be mandatory. Once reporting has been completed and external review (if any) has taken place, the Bank will evaluate the borrower's performance against the SPTs based on the information provided.

Indicative List of KPI that can be used for reference:

Environmental	Social	Governance
Air quality	Access & affordability (incl. Access to Medicine)	Business ethics
Biodiversity (incl. soil/land use)	Community and Human Rights	Consumers (incl. relation and welfare, responsible marketing and product labelling)
Climate change (GHG emissions and energy)	Diversity, Equity, and Inclusion	Data protection & security (incl. cybersecurity)
Raw material sourcing and recycling (circular economy)	Just transition	Product governance (safety & quality)

Indicative List of SPTs that can be used for reference:

Category	Example
Energy efficiency	Improvements in the energy efficiency rating of buildings and/or machinery owned or leased by the borrower
Greenhouse gas emissions	Reductions in greenhouse gas emissions in relation to products manufactured or sold by the borrower or to the production or manufacturing cycle
Renewable energy	Increases in the amount of renewable energy generated or used by the borrower.
Water consumption	Water savings made by the borrower.
Affordable housing	Increases in the number of affordable housing units developed by the borrower
Sustainable sourcing	Increases in the use of verified sustainable raw materials/supplies
Circular economy	Increases in recycling rates or use of recycled raw materials/supplies
Sustainable farming and food	Improvements in sourcing/producing sustainable products and/or quality products (using appropriate labels or certifications)
Biodiversity	Improvements in conservation and protection of biodiversity
Global ESG assessment	Improvements in the borrower's ESG rating and/or achievement of a recognised ESG certification

References:

[1] "Sustainability Linked Loan Principles" by Loan Market Association (LMA)

[2] "Guidance Framework on Sustainable and Sustainability linked lending by Financial Institutions" by International Financial Services Centres Authority (IFSCA)