Baker McKenzie.

Top ten tips for ESG Debt Financing

Fact

Environmental, social and governance ("ESG")-Finance is here to stay.

Reality

This rapidly-growing market needs immediate attention, but the voluminous protocols and evolving products can be daunting and confusing.

Solution

Our top ten tips will give you the headstart you need to navigate the challenges and opportunities that ESG debt financing presents.

1. Select your shade of green

Whilst the terms often connected to ESG finance, such as "green", "social" and "sustainable", have different meanings across markets and products, and are subject to widely varying guidelines and implementations, there is cause for hope, since:

- Procedures for compliance are now becoming more streamlined, with greater flexibility built in; and
- The development of a broader spectrum of products is providing a more diverse range of options to issuers and investors alike.

2. Choose the right ESG product

The scope of categories of ESG financings is constantly evolving, providing issuers with wide-ranging options to choose from to best suit their business model and needs, including:

Green	Social	Sustainability
Transition	Sustainability-linked or KPI-linked	Blue

3. Any industry can play

ESG-related initiatives are not limited to wind farms and recycling plants. Corporates in ANY industry can identify green or CSR targets to address in their business.

The next step is to link the company's financial objectives with these ESG milestones and determine a path to effectively promote the ESG aspects of the financing to potential investors.

4. Pick your poison (remedies for missing objectives)

Though investors have to date relied on the good faith efforts of the borrower or issuer to ensure that their investment is or will remain ESG-compliant, we believe one or more mechanics will soon emerge, as the market evolves, to provide investors with greater comfort on this front.

Options include: interest-rate ratchets; investor puts; issuer calls; default clauses; contractual representations and warranties, and indemnification.

Baker McKenzie can advise on the right combination of these options to best suit your business and maximize appeal to investors.

5. Maximize the benefit to you

Besides the reputational benefit to aligning your ESG objectives with the global ESG agenda, sustainability-linked and KPI-linked loans or bonds can also confer economic benefits. They can reward issuers that meet performance targets, e.g. with a decrease in interest rate and/or commitment fee.

Don't forget - investor demand for ESG debt finance products is growing!

TRANSACTIONAL POWERHOUSE

Leading and closing complex deals - every day

6. Consider ongoing disclosure and reporting

While the market expects some form of ongoing ESG reporting from borrowers and issuers, the content and preparation of those reports can vary significantly.

Notably, investors are increasingly demanding more standardized ESG disclosure and greater transparency with respect to market participants' ESG impact, which companies looking to raise ESG debt should take into account.

7. Adopt a jurisdiction-specific financing strategy

With no central regulator or authority yet overseeing ESG financings, market practice is somewhat divergent across jurisdictions. Similarly, market participants have varying degrees of familiarity with the respective ESG finance products, depending on where they are based.

Careful thought should therefore be given at the outset of the process as to (a) the specific regulations, principles and guidelines to which a particular ESG financing will or ought to be subject, and (b) to the target market.

8. Understanding the ratings process

- Engaging with the rating agencies early on and obtaining a credit rating is key.
- ESG considerations will play an increasingly important role in credit quality determinations as the financial impact of ESG issues becomes clearer.
- There are two key ESG-specific aspects to the ratings workstream to keep in mind:
  - ✓ ESG considerations are given substantial weight in the primary credit ratings process, and
  - ✓ Bespoke ESG ratings can be obtained from dedicated ESG data providers.

9. Know your investor base (and develop an effective marketing strategy)

Understanding at the outset of a transaction where investor demand lies for particular ESG finance products, what the key ESG drivers are from the investors' perspective, and what onward disclosures those investors will have to make, will allow the borrower or issuer and its advisors to structure a deal that is best set up for success.

10. Engage experienced advisors

To facilitate best execution, borrowers and issuers should look to engage:

- Transactional advisors able to assist in the development of applicable ESG targets and advise on other ESG-specific aspects of the transaction, and
- Legal advisors with robust ESG-specific experience.
  Baker McKenzie's leading, multi-disciplinary sustainable finance practice group is comprised of lawyers with transactional and advisory experience in ESG financings across a wide range of finance products—please visit our website for more information.

Tier 1
Risk Advisory: Corporate Governance
Legal 500 2019

Band 1
Climate Change
Chambers 2008-2020

Contacts:

Rob Mathews
Partner, London
rob.mathews@bakermckenzie.com

Adam Farlow
Partner, London
adam.farlow@bakermckenzie.com

Caitlin McErlane
Partner, London
caitlin.mcerlane@bakermckenzie.com

Samantha Greer
Senior Associate, London
samantha.greer@bakermckenzie.com

Maxim Khrapov
Senior Associate, London
maxim.khrapov@bakermckenzie.com

For more information on ESG Debt Financing tips, click here.

www.bakermckenzie.com