ACADEMY SECURITIES MISSION DRIVEN

Academy ESG

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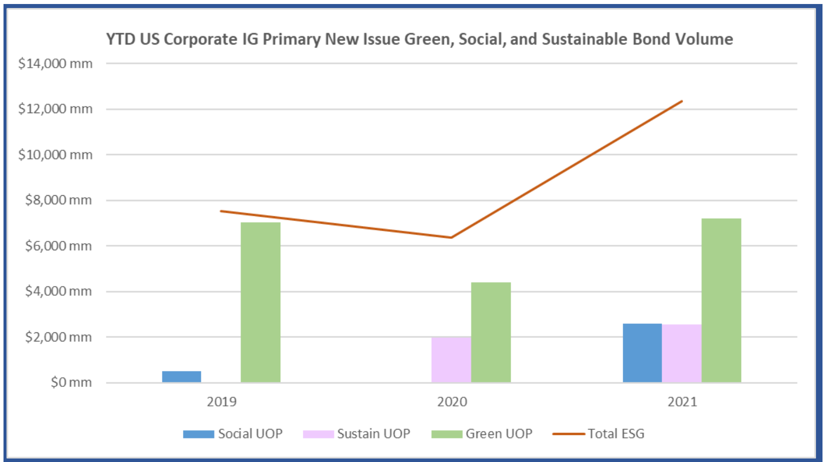
As the focus on ESG and its value proposition increases, regulators from around the world (including from countries like India, Chile, United States, UK, EU, and the IFRS) are looking to integrate climate risk and ESG into their oversight. In this month's report, we look at the impact of last year's US Q1 IG corporate ESG bonds including use of proceeds, allocation, the challenges associated with determining ESG impact, and where regulators and stakeholders can look to help improve the process.



2021 US ESG IG volume, after a slow start to the year, is beginning to outpace 2019 and 2020. Boston Properties (BXP), Northern States Power (XEL), and Citigroup (C) all came to market this March with green UOP bonds totaling $2.75bn. Both Mastercard (MA), and Aflac (AFL)—for which Academy served as joint bookrunner—printed a total $1bn in sustainable UOP this past month. Gross ESG themed US IG corporate issuance for the month of March was $3.75bn.

ESG Bond Reporting & Reports

One of the key principles that must be met for the ICMA's green/social/sustainable bonds is reporting, which according to the ICMA should include a list of projects for which green bond proceeds have been allocated and the expected impact (an area in need of improvement).

Of last year's eight Q1 US IG corporate issuers, seven have released reports or audits documenting the allocation of proceeds related to raising debt for either green or sustainable related projects. While there is a fair amount of discrepancy between the reports (part of the broader critique in ESG), the reports/audits in general provide information on the use of proceeds and sums of proceeds allocated. It's noteworthy that nearly all Q1 2020 issuers allocated 100% of funds or amounts equal to the funds raised in their respective ESG offerings, to projects within the first year of the issuance. This is because many issuers dedicate these funds to green/sustainable related acquisitions that have at times occurred 24-36 months prior to the issuer's ESG capital raise!

In addition to sums allocated, a green/sustainable bond report/audit should also include information on projects financed. The granularity of this will vary significantly between issuers. For instance, in its report, Prologis provides case studies on investments, like its properties, while others might just have a line-item description such as "Energy Efficiency Program Spend". As far as themes in Use of Proceeds (UOP), acquisitions related to clean transport (hybrid/EV), LEED properties, and renewable energy generation were among the broader line items. Other projects like recycled materials and sustainably managed sourcing were also funded.

Challenges with ESG Bond Reporting & Impact

Even though reporting is included as part of the ICMA's 4 core principles, the ICMA does not provide much guidance on what is to be included in a report. This lack of guidance quickly becomes noticeable and poses two obvious challenges.

The first of these challenges is the consistency of the data and information provided. If you are an investor concerned about ESG impact, then these reports and audits might not be of much help. Only half of Q1 2020 green/sustainable bond issuers provided information on GHG emissions (avoided or sequestered) and only one reported on water management/stress. This raises serious questions regarding how "green" or "social" an investment claims to be, and the metrics of assessing performance/impact. For example, two large utility companies mention energy efficiency as acquisition metrics, but do not indicate how many Kwh or Mwh are saved. Despite the ICMA mentioning impact reporting in their reporting section, few seem to comply with it.

Another, challenge is the accessibility of this information. There is often no convenient place for this type of information. Instead, one must go through the process of sifting through either a corporate sustainability website, IR page, or web search. Unlike investor relations pages, which tend to be straight forward and data driven, many corporate sustainability sites are laden with extraneous marketing and PR, making it difficult to determine what is the most recent and relevant. In some instances, one might have to go through both the bond audit and corporate sustainability report to get the complete picture of allocation.

Both of these (fixable) challenges speak to the critique of ESG laid out earlier this March in a USA Today oped by Tariq Fancy, Blackrock's former Chief Investment Officer of Sustainable Investing. Organizations like the IFRS can set guidance for impact reporting in line with financial materiality, helping to make it more consistent, while regulators can look to set guidance on access to information, how it is marketed to investors, and how it is disclosed.

Further Resources

Tariq Fancy OpEd: https://www.usatoday.com/story/opinion/2021/03/16/wall-street-esg-sustainable-investing-greenwashing-column/6948923002/