

April 2018

HSBC Equity Linked Green Bond Report



Introduction

The past decade has seen the evolution of socially-responsible investing instruments turn from a niche pocket of the market into secure holdings for pension funds and institutional investors to now be a mandate for a whole range of assets. The Climate Bond Initiative estimates that the total amount of green bonds issued in 2017 reached \$156.7bn with projections up to \$250bn for 2018 – a substantial rise from the \$4bn logged in 2010¹. The huge growth in the green bond market has been fuelled in part by companies increasingly incorporating sustainability performance, and the rising popularity of the asset class has led to the development of the green equity linked bond market, which provides extra yield for investors whilst also putting funds towards sustainable causes.

HSBC aims to help the green bond market in all facets grow by facilitating market dialogue and helping clients find appropriate finance solutions to release their green potential. The Group has a quarterly Sustainable Financing Newsletter, providing comment and information on the latest developments in the market. The sixth edition of this newsletter is available at <http://www.gbm.hsbc.com/solutions/sustainable-financing> where you can also sign up to receive direct distribution.

In 2017 HSBC issued a new Equity Linked Green Bond; the basis of which is to use HSBC as the issuer of a Green Bond linked to a well-defined Environmental, Social and Governance (ESG) index. The Equity Linked Green Bond will be issued and governed by the process documented under the HSBC Green Bond Framework (available at <http://www.hsbc.com/investor-relations/fixed-income-investors/green-bonds>). The difference with a standard Green Bond is that the payoff (and capital redemption) will be linked to equity performance of a chosen ESG Index.

The HSBC issued Equity Linked Green Bond appeals to investors who are already active in standard equity-linked notes, as this would be a variant of the products they trade currently, helping them allocate funds to Green investing. Additionally, to those investors who are demonstrating appetite for green-focused products and want to see new products in this space.

These products play an increasingly fundamental role in helping to address environmental concerns as climate change mitigation and adaption have become major policy priorities for policymakers around the world. As the HSBC Green Bond survey revealed in September 2017, this drive has been led by Europe with other regions now beginning to catch up.

Market Opportunity

Green bonds have raised awareness across financial markets for the need for private sector financing to tackle climate challenge. Green bonds are rapidly shifting investor expectations in fixed income markets. They are also leading to rapid increase in investor demand for ESG investments, as well as for additional information to help shape their investment decisions.

Yet, much more progress is required. In meeting this growing investment need, the United Nations has estimated an annual funding gap of US \$2.5tn against what is needed to achieve the Sustainable Development Goals (SDGs) and within this US \$1tn is needed annually to fund investments in clean energy alone.³ In 2017 HSBC launched its inaugural SDG Bond in support of the UN SDG Goals. The bond was over subscribed and details of the framework are available on our website (<http://www.hsbc.com/investor-relations/fixed-income-investors/green-and-sustainability-bonds>).

Numerous institutional investors have already established ESG investment policies across asset classes. HSBC Institutional and Wealth Management Sales have been working to build ESG-orientated Equity products for investors. HSBC's opportunity arises from a new investment need, supporting client's sustainable business activities and understanding their changing investment criteria during this global transition.

Market Overview





2017 delivered another strong year for the Green, Social, Sustainability bond market, with market volume up 54% year-on-year. Total market volume of global green bonds hit a record \$121.9bn in 2017, totalling 87.1% of the sustainable finance market. Almost half (\$57.1bn) of issues were in Europe, and Asia-Pacific drew in \$43.4bn.⁴ As a frontrunner in the market, HSBC launched its inaugural Equity Linked Green Bond on 27 March 2017, which has since supported €40m of investment in energy efficiency projects in the UK and France.

In November 2017, HSBC pledged to provide \$100bn in sustainable financing and investing by 2025, cementing our wider commitment to supporting these developments. Our Equity Linked Green Bond will support these efforts for clean energy and lower-carbon technology, through securing investment from the private sector as the world transitions to a climate-friendly future.

Systemic support of sustainable finance initiatives are set to help further promote investments in carbon emission-reducing initiatives. In a bid to close the \$180bn funding gap needed to cut the European Union's greenhouse gas emissions by 40% by 2030⁵, the European Commission launched its Action Plan on sustainable finance. The Commission plans to create a unified classification system to identify areas where sustainable investment can make the biggest impact, and from this create EU labels for green financial products. The Action Plan's measures will identify to investors the investments that comply with green or low-carbon criteria, as well as requiring investment firms to advise clients on the basis of their preferences on sustainability, creating an environment where green products will be set to thrive.

HSBC Green Bond Framework Summary

Pillar

 <p>Use of proceeds</p>	<ul style="list-style-type: none"> • Renewable energy • Energy efficiency • Sustainable waste management • Sustainable land use • Efficient buildings • Clean transportation • Sustainable water management • Climate change adaptation
 <p>Evaluation</p>	<ul style="list-style-type: none"> • Agreed criteria for selecting Use of Proceeds and confirming eligibility • Relationship Managers propose the Use of Proceeds • Group Sustainability review for ESG factors and compliance with Green Bond Framework and form a recommendation • Green Bond Committee confirms eligibility
 <p>Funds tracking</p>	<ul style="list-style-type: none"> • Use of Proceeds tracked via register, ultimately will be tracked via internal loan management system
 <p>Reporting</p>	<ul style="list-style-type: none"> • The issuing entity will provide a Green Progress Report, annually until full allocation. Thereafter, the issuing entity will provide a Green Progress Report if there have been material updates made to the project allocation • The Green Bond Committee review and approve each Green Progress Report, which includes: <ul style="list-style-type: none"> – Aggregate amounts of funds allocated to each of the Eligible Sectors, followed by more detailed descriptions of the types of business and projects financed – The remaining balance of unallocated Green Bond proceeds at the reporting period end – Confirmation that the Use of Proceeds of the Green Bond(s) issued conform to the HSBC Green Bond Framework

Assurance obtained a second party opinion from CICERO on the HSBC Green Bond Framework and been certified as 'Dark Green'.

Summary

Overall, HSBC's Green Bond framework and environmental policies provide a progressive framework for climate-friendly investments. The Green Bond framework lists eligible businesses and projects that are mainly supportive of the objective of promoting a transition to low-carbon and climate-resilient growth and is supported by a strong governance structure.



Excluded Use of Proceeds

As stated in our framework:



Nuclear power



Weapons



Gambling



Alcohol

HSBC has engaged PwC as an independent assurance provider to provide assurance that selected information in this report has been prepared in line with the HSBC Green Bond Framework.

Furthermore no coal and Palm Oil related assets are or will be financed under this Green Bond Framework.

Reporting Evaluation and Selection Procedure

The cornerstone of every Green Bond is the verifiable use of its proceeds to support sustainable investment. To facilitate this, issuers need a robust and transparent framework detailing, among other aspects, a strong project evaluation and selection process.

HSBC's Green Bond Framework is overseen and governed by the Green Bond Committee (GBC). The GBC is chaired by Group Treasury and consists of sustainability specialists and senior directors from across the businesses, including input from the HSBC Centre of Sustainable Finance (<http://www.sustainablefinance.hsbc.com>) where appropriate.

The GBC has responsibility for the ratification of sustainable projects, which are initially proposed by local banking teams and evaluated by Group Sustainability via a highly-disciplined, multi-step process following clear and consistently applied guidelines, as defined below:

- ◆ A definition of green finance/lending has been developed and approved for the purposes of identifying, monitoring and reporting green finance activity across the bank
- ◆ Once a green project is identified by the local banker, if the finance/lending is considered to fit within the tighter green bond Eligible Sectors definitions of the Green Bond Framework, the bankers are prompted to complete a form that details the specifics of the client and the associated green finance/lending
- ◆ Once identified, green finance/lending is reviewed by Group Sustainability which considers conformity to HSBC's Green Bond Eligible Sectors. Sustainability risk including physical, transition and liability risk is also reviewed to ensure only those deemed acceptable are considered for HSBC Green Bond allocation recommendation
- ◆ Finally the project details, together with Group Sustainability recommendation are submitted to the GBC for their ratification of inclusion or exclusion as use of proceeds of the respective HSBC Green Bond.

The HSBC Green Bond is linked to an equity index that is compliant and aligned to high quality sustainability standards. HSBC has reviewed a variety of ESG aligned market indices and evaluated based on quality of ESG selection criteria, ESG performance, independence and client feedback. Our selection process has concluded in the nomination of the STOXX Europe ESG Leaders 30 as the base index. This index was chosen because it combines indexing expertise with 134 ESG KPI data from Sustainalytics to create a passive investment into the E, S and G leaders in Europe. Also, a further low volatility filter helps improve risk-adjusted returns.

Regional Bond Allocation Within EMEA

Projects are located in



Key Stats:

Amount Disbursed to Eligible Green Projects or Business



Reporting Criteria For this Green Structured Note

A summary of the selection process for these projects is noted below:

- ◆ HSBC finance/lending identified as green by Relationship Manager – noting whether the Use of Proceeds conform to HSBC Green Bond Framework
- ◆ Exchange rates are taken from HSBC internal conversion rates where project investments are made in alternative currencies
- ◆ Projects within the region of the issuing entity, in this case EMEA, are considered for potential inclusion
- ◆ For the purpose of this report new projects are those which were agreed and signed since the publication of the 2017 Green Bond report. All other projects are considered to be “existing” projects
- ◆ The HSBC Green Bond Register tracks all projects identified by Relationship Managers within the region of the issuing entity and records the review/approval process performed by Group Sustainability and the Green Bond Committee as noted below
- ◆ There is no direct financial link between the allocated assets and the green bond itself, i.e. this is an unsecured issuance
- ◆ All projects in the HSBC Green Bond Register are reviewed by Group Sustainability and if ‘approved’, they are ‘ratified’ for inclusion in the Green Bond by the Green Bond Committee
- ◆ The HSBC Green Bond Register forms the basis of the data in the table below:
- ◆ If ratified by the Green Bond Committee, the projects outstanding commitments as per HSBC’s financial reporting systems at 30 June 2017 (elected reporting date) are recorded within the HSBC Green Bond Progress Reported data

HSBC Green Progress Report

Green Bonds Details

Issuer	HSBC France SA
Issue Date	27 March 2017
Currency	EURO
Tenor	8 years
Issued Amount	38,000,000
ISIN	FR0013224334

Use of Proceeds

EUR (numbers are rounded to the nearest m)

(A) Amount Disbursed to Eligible Green Projects	38	100%
(A) Energy Efficiency (EE)	38	100%

HSBC business area	Type of Project, per HSBC Green Bond Framework Eligible Sector List	Project description	Geography	Loan committed as at 30/06/2017 EUR (numbers are rounded to the nearest m)	Number of assets supported Asset supported	Renewable Energy installed capacity – predictions/projections made by our clients in public sources for the full project
Project finance	Energy Efficiency	Boilers, radiators, water heaters, solar thermals, CHP units and renewable energy solutions	France and UK	38m EUR	Multiple / Boilers, radiators, water heaters, solar thermals and renewable energy solutions	Over 3 million tonnes of CO2 have been saved by their micro-CHP units over 20 years. (CO2 saved for end users)

HSBC Sustainable Financing Updates

HSBC has created various platforms to facilitate enhanced communications of its Sustainable Financing activities. These are listed below:

- ◆ Sustainable Financing Website:
<http://www.gbm.hsbc.com/solutions/sustainable-financing>
- ◆ HSBC Sustainable Financing Quarterly Newsletter (available on website above): <http://www.gbm.hsbc.com/solutions/sustainable-financing/edition6-newsletter-2017>
- ◆ HSBC Green Bonds Website:
<http://www.hsbc.com/investor-relations/fixed-income-securities/green-bond-reports>
- ◆ HSBC Centre of Sustainable Finance:
<http://www.sustainablefinance.hsbc.com/>



2015-2018 YTD HSBC Sustainable Financing Milestones

HSBC is a member of several industry bodies focused on climate change, such as:

- ◆ **The ICMA Green Bond Principles Executive Committee** – HSBC was one of the initial banks to support the Green Bond Principles (GBP), run by ICMA and has been a member of the Executive Committee since June 2014
- ◆ **Social Bond Guidance Steering Committee** – HSBC helped establish the Social Bond Guidance (released by ICMA GBP in June 2016), and have been members of the Steering Committee since it was formed in February 2016. In June 2017, HSBC signed ICMA's Social Bond Principles, committing the bank to promote market transparency and disclosure, as well as maintain the integrity of the Social Bond Market
- ◆ **Green Growth Platform Financial Advisory Council** – HSBC joined the Advisory Council in 2015 which brings together ministers from European governments, businesses and the European Parliament to discuss and debate the economic opportunities and challenges involved in the transition to a low-carbon economy
- ◆ **HSBC is partner to the Climate Bonds Initiative** – HSBC is the sole sponsor of the only jointly published CBI/HSBC State of the Market report each year to help raise awareness of climate financing
- ◆ **Institutional members of China's Green Finance Committee (GFC)** – HSBC joined in June 2015 having representatives from HSBC's UK and China offices. The GFC includes members of China's financial community. The purpose is to identify practical steps to achieve economic growth and environmental improvements through reform of China's financial system
- ◆ **Accredited member of the Green Climate Fund** – HSBC is one of a handful of International Commercial Banks to be accredited by the Green Climate Fund, gaining accreditation in March 2016, thus allowing it to arrange GCF funding for projects
- ◆ **The Catalytic Finance Initiative** – HSBC joined the enlarged CFI in 2016. As part of the Secretariat Group HSBC has helped expand CFI's interest beyond Clean Energy financing into other Sustainable Project Financing
- ◆ **The Equator Principles Association** – HSBC was one of the early signatories of the Equator Principles in 2003. Starting in 2004, HSBC published its own internal Sustainability Policies. We consulted with customers, industry experts, shareholders and non-governmental organisation (NGOs), focusing on sectors which may have high adverse impact on people or the environment and in which we have a significant number of customers. We keep our policies under constant review, updating them wherever necessary
- ◆ **HSBC Climate Change Centre of Excellence** – has again been voted by Extel as the Number 1 provider of climate change research, for the fifth year in a row, with specialist research teams in London and Hong Kong
- ◆ **Created the HSBC Centre of Sustainable Finance** - Appointed Global Head of Sustainable Finance and established sustainable finance hubs in Hong Kong, Paris, London, New York and Toronto

- ◆ **Adopted Task Force on Climate-related Financial Disclosures recommendations** - to improve transparency, HSBC's 2017 annual report was published in February 2018 according to TCFD governance, strategy and risk management recommendations. HSBC also published a standalone ESG update in April 2018
- ◆ **HSBC publish Sustainable Finance Commitments** – HSBC has committed to provide USD100bn of Sustainable Financing and Investment by 2025 to develop clean energy, lower-carbon technologies and projects that contribute to the delivery of the Paris Agreement and the UN Sustainable Development Goals (Nov 17)
- ◆ **HSBC issues world's first corporate sustainable development bond** – The bond is based on the United Nations Sustainable Development Goals (UNSDGs) and this is the first time a private sector entity has issued a benchmark-sized bond of this type. This reflects the Group's commitment to financing projects that benefit communities and the environment (Dec 17)

Conclusion



The Paris Climate Agreement aims to limit the risk of an increase in temperatures to 2°C above pre-industrial levels. An estimated \$100tn of investment is needed in new green infrastructure over the next 15 years to provide a 66% change of meeting this goal.

We recognise the critical role finance has to play and HSBC aspires to be a leading global partner in financing, managing and shaping the transition to a low carbon economy. Our shared challenge is to secure growth and diversification in what remains a market with huge untapped potential.

As our own sustainable finance survey reveals, demand for green financing is growing rapidly. Most large corporates are already on a journey towards a low-carbon economy. To achieve the goals of the Paris Climate Agreement, we must also encourage growth in the mid-cap market.

Diversifying the Green, Social, Sustainability bond market beyond project finance assets into corporate loans, and working more with mid-sized companies, forms a significant step towards realising that goal, one which is increasingly being reflected in HSBC's own Green Bond allocation and creation of the Equity Linked Green Bond. By working together with issuers and investors, of all sizes, HSBC is helping to make a low-carbon future a shared reality.

In support of our ongoing commitment to the robustness and transparency of the Green Bond and Equity Linked Green Bond market, we have appointed PwC as our independent third-party assurance provider of our Equity Linked Green Bond Progress Report and their full assurance statement is provided within this report.



1 Climate Bond Initiative website as of 28 March 2018

2 United Nations Conference on Trade and Development, World Investment Report 2017

3 Ceres, Investing in the Clean Trillion, January 2014 4 Dealogic website as of 4 October 2017

4 Dealogic website as at 3 April 2018

5 European Commission, Sustainable Finance Action Plan, 8 March 2018

6 renewable energy; energy efficiency; efficient buildings; sustainable waste management; sustainable land use; clean transportation; sustainable water management; and climate change adaptation

7 Mission 2020, 6 Milestones, as of 4 October 2017