Evolving Bahrain's ESG Landscape & Capital Markets

بورصـــة البحـرين
BAHRAIN BOURSE

IN COLLABORATION WITH

HSBC

CONTENT

BAHRAIN BOURSE FOREWORD

Bahrain Bourse is pleased to announce its collaboration with HSBC in developing a guide to Sustainable Finance as part of our commitment the United Nations Sustainable Stock Exchanges Initiative to focus on the sustainable development agenda and green finance.

The increased focus on sustainable development, climate change, and the global transition to more sustainable and inclusive economies have led to a rapid increase in demand for transparent and comprehensive reporting on Environmental, Social and Governance (ESG) information.

We believe that ESG is an integral part of exchanges strategies and ethos, as evident by the initiatives undertaken by exchanges globally as well as in the GCC. As a licensed exchange and market operator, we are committed to creating a sustainable future within the capital markets ecosystem by promoting sustainable business practices and driving action on sustainable finance products.

Investor demand for ESG products continues to drive innovation. While green bonds are the most offered ESG products, offerings across all sustainability product categories have now increased, including Sustainability Linked Bonds (SLBs).

ESG factors represent opportunities that investors can capture as companies innovate to build a sustainable future. This guide focuses on capital markets in general and sustainable finance in particular.

It is worth noting that by 2030, Bahrain's private sector aspires to drive a sustainable economic growth, leveraging Bahrain vision's through three guiding principles: sustainability, fairness, and competitiveness. Economic growth can only be achieved through preserving the environment, the Kingdom's cultural heritage, and the long-term well-being of Bahraini citizens.

There is a greater need now, more than ever, to promote sustainability within the capital markets through intensifying our collective efforts in this direction, by increasing our positive footprint within the ESG landscape, and leveraging new ESG-driven capital raising opportunities and creating value for all stakeholders.

Sh. Khalifa Bin Ebrahim Al Khalifa
Chief Executive Officer
Bahrain Bourse

HSBC FOREWORD

HSBC Bahrain is honoured to partner with the Bahrain Bourse in developing a guide to Sustainable Finance.

At HSBC, we're committed to the transition to a global net zero economy, not just by playing our part, but by helping to lead it. Working with peers and industry bodies to develop globally relevant common standards to measure progress is one of the many ways in which we are doing so.

In October 2020, HSBC Group committed to aligning the financed emissions from our portfolio of customers to net zero by 2050 or sooner, in line with the Paris Agreement goals. To help get there, HSBC's ambition is to provide between USD750bn to USD1 trillion in finance and investment by 2030 to support our customers in their transition to net zero.

In the Middle East, we are leading the region's low-carbon transition by supporting customers to thrive through transition, being a catalyst for climate action in our communities and making our own operations and supply chains net zero.

We know that how we do business is as important as what we do and reporting on our environmental, social and governance (ESG) performance transparently is essential to building confidence and creating value for all our stakeholders.

We're mobilising finance and accelerating innovation to make this happen, working in partnership with our customers to build a more sustainable, resilient and prosperous future.

There's growing awareness in Bahrain of the importance of sustainability, with more corporates working towards improving their ESG ratings to align with Bahrain's Economic Vision 2030 of building an economy that is based on sustainability, fairness and competiveness.

We look forward to supporting businesses, our customers and communities in their journey towards a more sustainable future as we open up a world of opportunity.

Christopher Russell
Chief Executive
HSBC Bahrain

1. INTRODUCTION

ESG at a Glance

Since 2019, the awareness and the importance of the sustainability agenda has gained significant momentum in the Kingdom of Bahrain. Bahrain's capital market has seen an uptake in the rate of sustainability reporting from 7% to 33%[1] of total listed companies representing 78% of total market capitalisation, as well as a greater number of companies taking key strides towards improving their ESG performance and disclosure. The topic of ESG and Sustainability has also been heavily featured across boardroom agendas and discussions.

ESG reporting supports companies to align their strategy with Bahrain's Economic Vision 2030[2] – contributing to national priorities and fulfilling economic growth ambitions. The Bahrain Economic Vision 2030 focuses on reshaping the vision of the government, society, and the economy, based around three guiding principles: sustainability, fairness, and competitiveness.

1.1. ESG Investment Trends for Investors

a) Growth of ESG aligned Investing

The awareness and adoption of ESG considerations is continually growing exponentially among investors, regulators and corporates. Financial institutions and asset management companies have augmented a range of socially responsible investment funds to meet the market demands for ESG investing. Large corporate and financial institutions are demonstrating their commitments to sustainability and ESG issues by collaborating with investors, governments, non-governmental organisations and even other corporates and financial institutions to promote and support advocating and cultivating long-term investments in sustainable projects and initiatives. Investors are amplifying efforts in assessing ESG risks and opportunities in investment strategies and portfolio management as investment providers are broadening their offerings to meet the growing demand. The below graph showcases the YoY growth in ESG aligned investing:

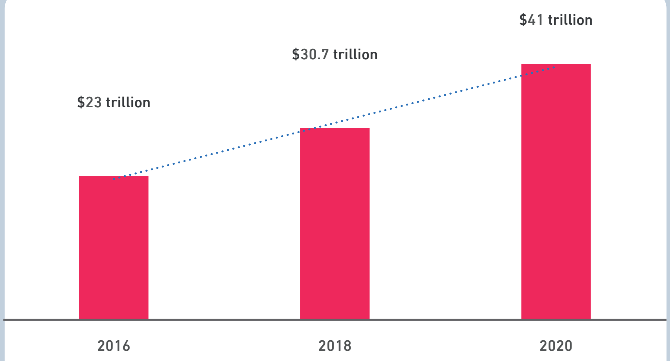


Figure 1: Snapshot of Global Sustainable Investing Assets [3&4]

b) Increasing emphasis on adoption of ESG disclosures

Investors will hold corporates to higher standards when it comes to the adoption of Sustainability/ESG metrics and addressing key ESG issues. Expectations are that ESG data disclosures are on a path of significant improvement as investors require more transparency and visibility on the activities of issuers and asset managers and their diligent compliance to ESG metrics.

Although disclosure of ESG information and data has enhanced globally, many jurisdictions are yet to mandate such disclosures requirements, though may have voluntary frameworks. US Regulators are expected to grow more inclined towards pursuing enhanced requirements for ESG disclosures under the new administration of president Joe Biden. This is evidenced in the president's recent appointment of Gary Gensler as the new Chair of the US Securities and Exchange Comission as of April 2021, who signalled his ambitions to address many issues including the boom of ESG investing and the lack and need for oversight on market players in that arena, in addition to other topics such as climate risk and diversity.

Addressing prominent and trending ESG issues In the year 2020, with COVID-19 rampant across the globe, sustainability became front and centre of every conversation as the pandemic escalated the need to address this long pending issue of our environment. How the public and private issuers will contribute to respond in addressing these issues will unlikely escape the attention of not just ESG investors who are keen on focusing in socially responsible and sustainable investments, but other investors, market players and even societies as a whole. Key areas of focus in 2021 and beyond will include:

Environmental Issues

Climate change is one of the most pressing issues of our time and probably the most debated in ESG and sustainability discussions. It will remain to be a key focus area around the world across different industries and sectors, particularly in the energy, utilities and industrials where energy efficiency and the call for transitioning to green, clean and renewable energy sources to reduce the carbon footprint and greenhouse gas emissions from these sectors are a hot topic and key investment focus. In recent years, climate change took centre stage following to the Paris Agreement[5] of 2016 which is currently ratified by 196 countries including Bahrain. There is a growing public and private sector interest in green investments even in the world's hydrocarbon hub (The Middle East):

- **Green Saudi Initiative[6]:** The Saudi Crown Prince launched an ambitious programme to reduce the carbon footprint of the region's largest oil exporter with the second biggest afforestation initiative in the region. The country is also aiming for renewable energy to supply c. 50% of the Kingdom's energy requirements by 2030.

- **Saudi Aramco[7]:** The world's largest oil company has established a USD 500 million fund for investing in clean and renewable energy.

- **Dubai Clean Energy Strategy[8]:** Since 2015, Dubai has ventured on a clean energy strategy targeting to produce c. 75% of its energy requirements from clean sources by 2050.

- **Sustainable Energy Authority[9]:** In 2014, Bahrain established the Sustainable Energy Authority as a joint venture between the Office of the Minister of Electricity and Water and the UNDP with the objective of developing a cohesive and sustainable energy policy and to promote renewable energy and energy efficiency in the Kingdom of Bahrain.

The technology sector[10] is also witnessing commitments from large players in 'Silicon Valley' namely Apple, Microsoft, Amazon, Google and Facebook to reduce emissions from facilities and achieve 'net-zero' targets by 2050 as well. And even in industries such as financials there are ambitious plans and commitments from large global financial institutions e.g. HSBC[11], Citi Bank, Standard Chartered and BNP Paribas just to name a few, to contribute in achieving 'net-zero' targets between 2030 and 2050 and double-down on ESG and sustainability aligned investments and initiatives in the coming years.

Investors will keep a close eye on the progress and milestones that corporations have pledged to achieve on this front, this shall also function as another catalyst for emphasizing the importance of enhanced and diligent ESG disclosures, reporting and oversight.

Social Issues

Since the outbreak of the COVID-19 pandemic the world has been experiencing numerous healthcare crises with countries facing challenges in mobilizing required medical supplies and resources coupled with the rising infected and critical cases. The pandemic has also challenged the strength and efficiency of healthcare systems of world's nations, and also shed the light on issues such as the healthcare quality, equality and access to medical supplies and vaccines by the less-fortunate which all became critical talking points in global, regional and local forums as the pandemic continues to persist. Additionally, on the back of the adverse economic impact due to the restrictions imposed to curtail the pandemic, job losses on the back of the sharp decline in economic activity intensified unemployment rates with the International Labour Organization (ILO)[12] estimating that 114 million people lost their jobs over 2020 mainly driven by the disruptive economic, supply and demand implications of the pandemic. Socially responsible investors are taking active interest in investments aimed at relief programmes and reforms to tackle these healthcare and employment crises and to address the ever-growing issues of income and wealth inequalities that have widened in recent times. The increasing emphasis on social issues from issuers and investors is also evidenced in the fact that social bond issuances shot up to USD 147 billion in 2020[13] from USD 18 billion in the previous year.

Governance Issues

Diversity and inclusion is another key focus area on the radar of investors and portfolio managers when it comes to asset allocation strategies and the selection of organizations for investment opportunities. Shareholders are increasingly pressurizing corporates for disclosure and reporting of diversity and inclusion metrics, goals and achievements. In 2020, following a spate of anti-racism and discrimination protests in the US, large corporates have made a slew of group-wide pledges on racial and ethnic enablement programmes to advance minorities into more leadership roles across organizational levels, also setting targets for diversity in the workplace.

1.2. ESG as a Regulatory Imperative

In the Kingdom of Bahrain, Bahrain Bourse considers environmental, social and governance issues of critical importance to our core business, and takes the ambition of the Bahrain Economic Vision to heart. The increased focus on sustainable development, climate change, and the global transition to more sustainable and inclusive economies have led to a rapid increase in demand for transparent and comprehensive reporting on Environmental, Social and Governance (ESG) information. We understand our critical role as a catalyst for sustainable capital markets and as a key driving force to promote ESG disclosure among listed companies.

As a Partner Exchange member of the Sustainable Stock Exchanges (SSE) initiative, and a member of the World Federation of Exchanges (WFE), Bahrain Bourse has made a formal commitment to drive sustainability in capital markets[14]. In June 2020, Bahrain Bourse launched its voluntary environmental, social and governance (ESG) reporting guideline[15] for listed companies and other stakeholders. The voluntary ESG guideline includes the latest reporting methodologies widely adopted by the industry and enables listed companies to navigating through the evolving standards on ESG data disclosure.

In the GCC, public joint stock companies listed on the Abu Dhabi Securities Exchange (ADX) and the Dubai Financial Market (DFM) in the United Arab Emirates (UAE) (Listed PJSCs) are now required to publish their sustainability report on a mandatory basis.

On 10 January 2021, the Securities and Commodities Authority (SCA)[16] in the UAE issued a general clarification to Article (76) of the Governance Code which sets out in more detail the required contents of sustainability reports and a confirmation that such report must be published annually.

Globally, there has been an increase in the regulatory requirements for reporting on ESG information. An example is the introduction of the European Directive on mandatory non-financial reporting which requires large companies to publish non-financial information. The directive, which was introduced in 2014 but adopted in 2016, dictates that non-financial statements should include ESG information to help investors, consumers, policy makers and other stakeholders to evaluate the non-financial performance of large companies and encourages them to develop a responsible approach towards conducting their business operation.

Due to its role in monitoring and assessing vulnerabilities that affect the global financial system, the Financial Stability Board, an international body that monitors the global financial system, established a Task Force, in December 2015, that aims to drive consistent climate-related financial risk disclosures. These voluntary disclosures guidelines are to be used by companies to provide information for investors, lenders, insurers and other stakeholders.

The 32-member Task Force is global; its members were selected by the Financial Stability Board and come from various organizations, including large banks, insurance companies, asset managers, pension funds, large non-financial companies, accounting and consulting firms, and credit rating agencies. The Task Force developed four widely adoptable recommendations on climate-related financial disclosures that are applicable to organizations across sectors and jurisdictions.

In 2021, some key regulators around the globe are due for updating the requirements for ESG disclosures. There is also potential for collaboration among regulators around the globe in order to harmonise efforts and reach consistent and uniform regulations and requirements for ESG disclosures that can span across different jurisdictions and markets. Some of developments in this space from around the world in 2021 include:

- **EU's regulations on sustainability-related disclosure in the finance services sector:** Regulation requiring financial market participant to implement policies and ensure disclosure on a comply-or-explain basis with regards to sustainability-related risks and factors relevant to their investment activities effective from March 2021.

- **EU's non-financial reporting directive[17]:** The European Commission will specify information that the applicable companies need to disclose on how and the extent to which activities align with the environmentally sustainable activities as defined in the taxonomy.

- **TCFD (Task Force on Climate-related Financial Disclosures) aligned disclosures in the UK:** Certain companies will be required to make TCFD aligned disclosures on a comply-or-explain basis in 2021. The scope will be increased to 100% in 2022 subject to market cap.

- **Business responsibility and sustainability report for Indian companies:** The Securities and Exchange Board of India (SEBI)[18] has proposed a new business responsibility report for the top 1000 listed entities by market cap on voluntary basis until 2021, after which it shall be mandatory.

1.3. ESG as an Investment Consideration

ESG information provides insights into the quality of management and the environmental and social impact that can affect financial performance; it also helps investors identify companies that are well positioned to sustain their performance over the long term and avoid those which are likely to underperform or fail. In 2020, the collective AUM represented by PRI signatories who have pledged to integrate ESG factors in investment decisions by becoming signatories to the UN backed Principles for Responsible Investment (PRI)[19], increased by 20% from USD86.3 trillion to USD103.4 trillion as of March 2020, representing 3,038 signatories. This is an astronomical growth of 392% since 2010 when signatories represented USD21 trillion in AUM. Concurrently, the number of investor signatories also rose by 29% to 2,701, of which 521 are asset owner signatories.

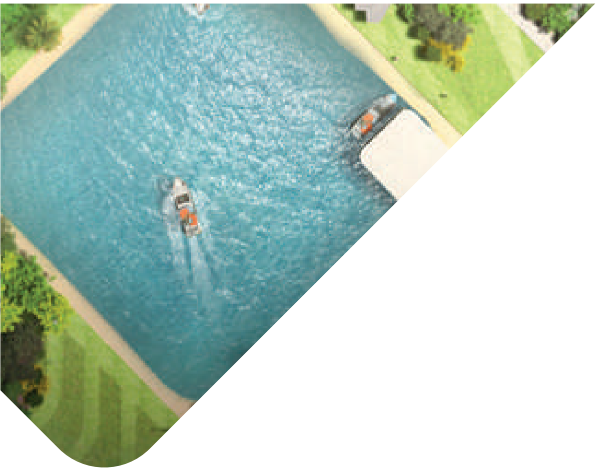
Large asset owners and asset managers are at the top of the investment chain and, therefore, have an important role to play in influencing the organizations in which they invest to provide better ESG disclosures. To name a few examples, in January 2020, BlackRock Chief Executive Officer, Larry Fink[20], issued a letter to companies declaring and reaffirming BlackRock's stance on sustainable investing. In support of this new commitment towards sustainability and climate integrated portfolios, Blackrock announced a number of initiatives to place sustainability at the centre of its investment approach. The asset management company also commits to vote against management and Board Directors if companies are not making sufficient progress towards sustainability-related disclosures and business practices. The large European asset management company Amundi, has also set out an ambitious action plan to be fully executed by end of 2021 aimed towards a deep and comprehensive integration of ESG criteria and mainstream this integration into its investment processes, voting policies and its strategic goals. These market trends speak greatly to the fact that asset managers and owners are cognizant that ESG-compliant organizations are better equipped for outperformance in the long-run.

1.4. Rise of ESG Rating

ESG rating agencies are increasingly influential in determining how capital is allocated as they help index providers and fund managers understand and quantify the ESG performance of companies.

ESG ratings agencies assess and quantify the ESG performance of companies. They also measure the level of exposure of a company against material industry risk and assess whether these risks are being adequately managed or mitigated. Ratings are usually industry-specific; key ESG issues are identified as those with most relevance to the industry. Through measuring risk exposure against these issues, a company's management system and performance indicators, ESG rating agencies determine how a company is managing ESG related risks.

ESG rating agencies have developed numerous ESG indices which are designed to help investors measure, benchmark and manage the stock performance of the world's leading companies in terms of economic, environmental and social criteria. MSCI Inc. has developed more than 600 equities and fixed income ESG indices, while S&P Dow Jones Indices has more than 75 ESG indices. FTSE Russell, a leading provider of data solutions, also has a number of sustainable investment indices which aim to integrate ESG and investment considerations into single index solutions, sustainable investment data models, ratings and analytics. These indices cover a range of industries and geographical areas. Criteria are industry-specific, and scores are weighted according to different materiality and risk exposure among different companies and industry sectors.



1.5. Importance of ESG Disclosure

a) Supporting the UN Sustainable Development Goals

Over the past decade, the Kingdom of Bahrain has reinforced its commitment to further enhance living standards for the Bahraini citizens, through emphasising sustainable development. The UN Development Goals (SDGs) are being implemented through the Government Plan of Action in collaboration with the private sector and civil society. The Government has not only made a commitment and progress to achieve these goals, but also mapped its key national priorities revolving around: people, planet, prosperity, peace and justice, against the SDGs 2030. Achieving the SDGs also requires involvement of the private sector. ESG reporting can support Bahraini companies align with the SDGs – contributing to global and national priorities.

b) Meeting requirements of investors, ESG rating agencies, and sustainability indices

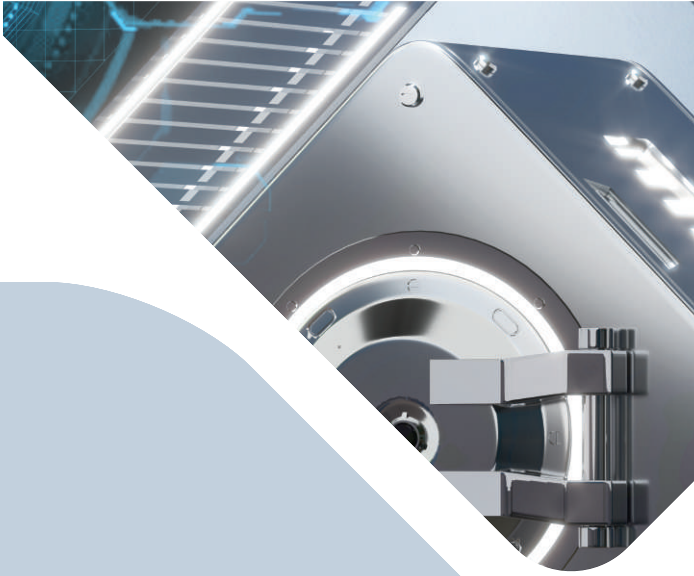
Institutional investors recognize ESG factors as key drivers of value, as such, they integrate these factors across the investment process to identify opportunities and hedge risks. As responsible investing is on the rise so is investors demand for ESG information. ESG rating agencies continually monitor companies' ESG disclosures and performance, selecting the top performing companies in the most important international sustainability indexes such as the Dow Jones Sustainability Index and the FTSE4Good. They are considered a strategic tool to support investors identify the ESG risks and opportunities of their investment portfolio, contributing to the development of active and passive investment strategies. ESG reporting can support companies to meet the requirements of institutional investors, rating agencies ESG information. Companies with low ESG scores are usually excluded from investment portfolios and indices leading to missed opportunity for additional capital inflows from qualified institutional investors that integrate ESG factors in their investment decisions.

c) Strengthening financial performance, enhancing reputation and global competitiveness

Investors are increasingly embracing the idea that integrating ESG into investment strategies translates into improved corporate profits and investment performance. A growing number of institutional investors are seeking to avoid financial risks associated with ESG factors and aiming to enhance returns by investing in companies that have strong ESG track records. Strong ESG risk awareness and management can contribute to improved long-term corporate financial and investment performance, particularly when material ESG factors are mitigated.

d) Meeting regulatory requirements

The aim of regulators is to enhance the availability and reliability of listed companies' information in relation to ESG factors. Companies that report on key ESG information not only can align with current local, regional and international regulations, but can also anticipate future regulations that may impact the company's operations.



1.6. Case Study: Benefits of being in Compliance in ESG – Issuers

In 2020, shariah-compliant bonds green (Sukuk) valued at USD 1.3 billion were issued by the Saudi Electricity Company (SEC)[21]. Among other milestones, the offering which was greatly oversubscribed was the first green sukuk to be issued by a Saudi Arabian corporation and by a utility company in the Middle East. SEC used the proceeds to finance a national programme to rollout 'Smart Meters' as part of SEC's digital transformation plans and sustainability agenda and also to facilitate the Kingdoms shift to a low-carbon nation in line with Saudi's 2030 vision.

SEC's unique Green Sukuk offering was able to gain quick momentum and strong demand attracting considerable interest from social responsible investors (SRI), green investors along with typical conventional fixed income investor, enabling SEC's transaction to build a high-quality and diversified order book that peaked at USD 5.3 billion. This transaction also represented SEC's return to the international debt capital markets for the first time since 2018 and supported SEC by diversifying its funding sources and broadening its investor base in the market and attracting high quality investors from across the globe to support its green projects portfolio.

2. SUSTAINABLE FINANCE OPTIONS

2.1. ESG and Banking

Banks and financial institutions have always been a key pillar for economic growth by providing opportunities to customers and communities to invest and expand. These institutions also help regulators and governments implement policies and governance on the global financial infrastructure. There is a critical role for financial institutions to play in supporting the global drive towards Net Zero. Financial institutions need to play a leading role to enable and support this transition by steering businesses and economies towards more sustainable activities.

As banking regulations evolve to incorporate Sustainability as a core part of the resilience requirement within the banking framework, banks and financial institutions have become increasingly committed to support their corporate and institutional clients on their low-carbon transition journeys, by leveraging their financing strength, international networks, extensive expertise and participating in ESG research and innovating solutions such as sustainable and green financing, investments, deposits, payments and supply chain.

These emerging sustainable solutions offered by banks can enable customers to evolve their business models and are positioned to:

- **Create Awareness**
  - Key information on disclosures and local/international regulations
  - Latest trends, developments and news in the sustainability arena
  - Industry and business insights
- **Conform with market trends (investor/consumer/regulatory)**
  - Importance of incorporating ESG considerations in business decisions
  - Understanding changes in consumer behaviour and preferences
  - Cooperate with organizations/regulators to promote adoption of ESG disclosures
- **Build resilience and sustainability within their supply chains**
  - Promoting/facilitating green trade through business incentives linked to ESG
  - Supporting clients to shift towards greener supply chain structures
- **Access to funding**
  - Project-level funding with green and sustainable accreditations
  - Flexible working capital solutions with green accreditations
  - Financing incentives based on customers' sustainability ambitions and ESG track-record

2.2. Sustainable Finance Options:

I. Green, Social and Sustainable (GSS) Bonds

In the fixed income space ESG/sustainable financing has become especially popular also owing to the changes in economic, political, social and environmental trends which is reflected in investors' behaviour and preferences that have become more inclined towards issuers with ESG/sustainability aspirations functioning as a key catalyst for conceiving new and innovative types of bond and debt instrument issuances. There are significant benefits that both bonds and sukuk issuers can reap from the adoption of such instruments to support capital budgeting decisions, including:

- Opportunity to showcase issuers' commitments to their ESG/sustainability ambitions and to the expectations of the market and investors
- Attracting a broader and more diversified investor base, with increasing green investment mandates with particular interest in such investments
- Potential for outperformance as the market for such bonds is still considered as 'undersupplied' as such issuances remain a rare commodity in many markets around the globe
- Enjoy positive media and press coverage including recognition and support from both public and private sector bodies domestically and internationally

a) Green Bonds

A fixed income debt instrument where the purpose of these issuances are for the channelling of proceeds towards financing projects addressing key environmental objectives, including to sector and project categories such as renewable energy, energy efficiency, pollution prevention and control, natural resources management, water and waste management, eco-friendly products, technologies and processes and green buildings.

The progress of the GSS bond market has been facilitated by the introduction of market standard principles. The Green Bond Principles (GBP)[22] were established in 2014 by a consortium of investment banks and since have moved to an independent secretariat hosted by the International Capital Market Association (ICMA).

b) Social Bonds

Social Bonds are aimed at financing projects that address social objectives and target positive socio-economic advancements and developments focusing on sectors and projects cantered around health, education, access to financial services, housing, vocational training, clean living, food security, empowering and promoting entrepreneurship and SME support initiatives.

In 2015, ICMA introduced the Social Bond Principles (SBP)[23] to promote the integrity in the social bond market with a standard set of principles promoting transparency, disclosure and reporting. These voluntary guidelines aim to address or mitigate specific social issues leading to positive social outcomes.

c) Sustainable Bonds

These bonds/sukuk are issued for the purpose of exclusively financing projects with a combination of green and social implications and objectives such as energy efficiency for social housing development projects, clean transport, clean waters and improving water quality of lakes, rivers and seawater.

In 2018, the ICMA has published guidelines for Sustainablility Bond Guidelines[24] to facilitate and provide guidance on the appropriate criteria and best practices of such instruments to ensure an optimal positive impact is achieved from such issuances.

II. Sustainability-linked Bonds (SLB)

SLBs are general corporate purpose bonds with no restrictions on use of proceeds, instead the use of the proceeds incorporates ESG/Sustainability metrics/KPIs from which Sustainability Performance Targets (SPTs) can be set, which are assessed and measured periodically over the life of the bonds. The coupon rate on these instruments is tied to key SPTs which may include dimensions such as emissions intensity, ESG ratings, etc.

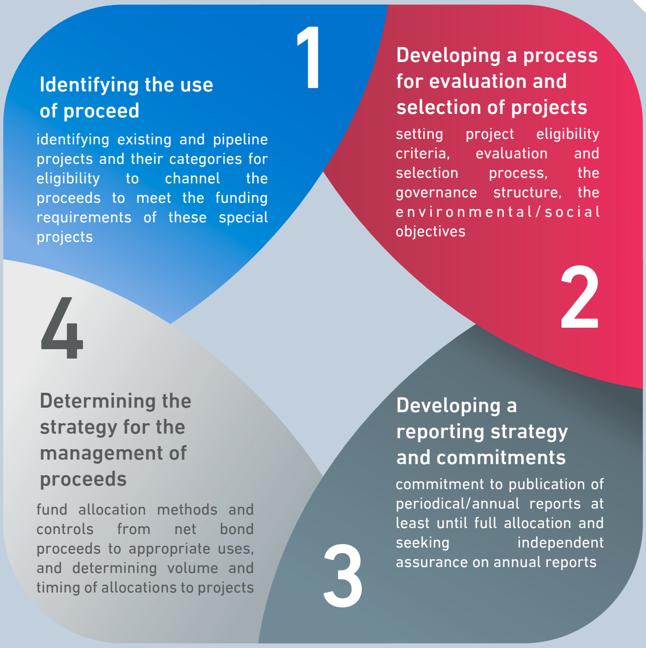


Figure 2: Four key steps that issuers should consider for GSS bonds issuances

In 2020, the ICMA has also introduced the Sustainability-linked Bond Principles[25] for optimal recommendations on structuring features, disclosures and reporting for SLBs and ensure the alignment of such issuances with SPTs.

These principles have five core components:

1- Selection of KPIs: issuer's performance is to be measured through these KPIs, which should be relevant, core and material to the issuer's overall business. They should also be measureable, externally verifiable and capable of being benchmarked

2- Calibration of SPTs: to be consistent with issuers' overall sustainability/ESG strategy with pre-defined timelines for execution and achievement

3- Bond Characteristics: The bond issues to include financial or structural impacts set to take effect from trigger events, e.g. coupon pricing

4- Reporting and verification: importance of issuers to publish regular or at least annual reports with:

- Updated information on the performance of the selected KPIs
- A verification assurance report from an independent external party
- Additional information on SPTs

III. Transition Bonds

These instruments have been introduced to support 'brown' companies with significant carbon dioxide emissions to gradually transform their business to become more green, efficient and clean and ultimately reduce their carbon footprint. Such issuances have become more common and popular with sectors operating in energy, mining, minerals, chemicals, utilities and transport.

In 2020, the ICMA issued a publication titled 'Climate Transition Finance Handbook'[26] specifically aimed at providing guidelines for issuers raising funds in debt capital markets to support their green transition. There are four key elements for issuers to consider in availing such financing to support their transition strategy:

1- Issuer's climate transition strategy and governance: A 'transition' label applied to such a debt financing instrument communicates the issuers strategy to transform the business model in ways addressing climate-related risks and in alignment with the goals of the Paris Agreement.

2- Business model environmental materiality: The transition strategy should be relevant to the environmentally material parts of the issuer's business model.

3-Climate transition strategy to have science-based targets and pathways: Issuer's strategy should reference scientific evidence and targets throughout the transition journey.

4- Implementation transparency: Issuer's transition journey and key milestones achieved should be (to the extent practicable) communicated and reported supplemented with external independent opinion on the veracity and alignment with the transition strategy.

IV. Green Social and Sustainable Loans

These are loans whereby the proceeds are directly targeted at environmentally-friendly or green projects and initiatives. Such transactions are subject to project evaluation and assessment process. Loan proceeds are used to fund 'green' activities by the borrower, while providing transparency and visibility to the lender in order to ensure and evidence the appropriate use of funds for the dedicated purposes. These projects include but are not limited to: Renewable energy, green buildings, pollution/waste prevention/reduction/treatment and recycling, clean transportation, energy efficiency, conservational projects for natural resources, waste-water management, eco-friendly technologies, etc.

Financial institutions have worked closely with the Loan Market Association (LMA)[27] to publish industry standard principles for Green Loans and Sustainability-linked Loans. Both sets of principles are voluntary for banks and aim at promoting behaviours and projects ultimately conducive and beneficial towards sustainable outcomes. The four key pillars to the Green Loan Principles are as follows:

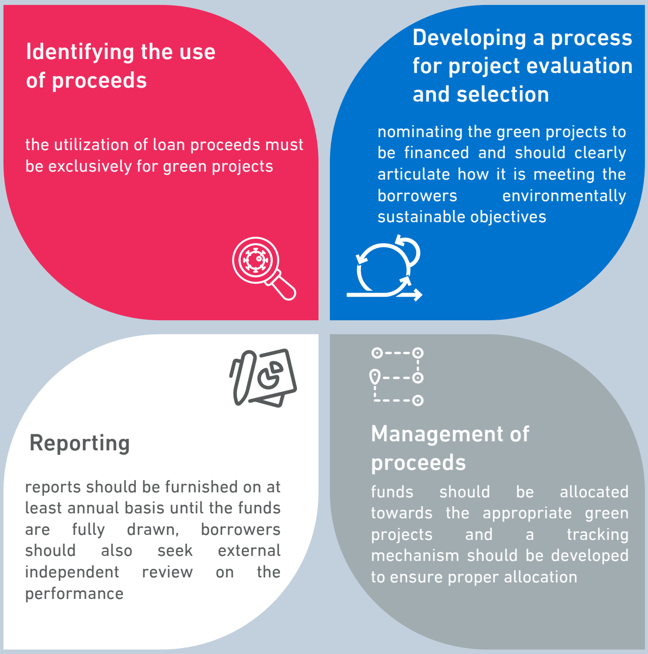


Figure 3: The four key pillars to the Green Loan Principles

Global issuance of green loans witnessed a strong increase since 2015. One of the key catalysts driving this growth is owed to the inception of the Green Loan Principles (GLPs) in March 2018 published by the LMA, as in the same year global green loan issuances experienced the biggest YoY growth to reach c. USD 60 billion, only to further show remarkable growth in the following year for total issuances to reach c. USD 93.4 billion by 2019. In 2020, issuances slightly decline to USD 80.3 billion as a result of the global outbreak of the Covid-19 pandemic disrupting the market, with expectations for improvement in the following year as the world economy is on a path to recovery.

Worth highlighting that the LMA has also issued a publication in April 2021, setting out guidelines and principles for social loans, a new financing option to fund eligible social projects which has been gaining accelerated prominence owing to the social impacts of the pandemic. These principals are outlined as following:

1- Use of proceeds: a fundamental principal is the utilization of loan proceeds towards social projects which should be properly delineated and described by borrowers.

2- Process for project evaluation and selection: borrowers should clearly communicate to lenders their:

- Social objectives
- Process by which they determine project eligibility
- Their eligibility criteria / exclusion criteria

3- Management of proceeds: the loan proceeds should be credited to a dedicated account or tracked by the borrower in the appropriate manner to ensure that they are channelled into the appropriate operations

4- Reporting: borrowers should maintain readily available up to date information on the use of proceed by establishing reports at least on an annual basis.

V. Sustainability-linked Loans (SLL)

SLLs aim to facilitate and promote environmentally and socially sustainable business activities and growth by way of linking uses of loan funds to ESG/Sustainability metrics/KPIs from which the Sustainability Performance Targets (SPTs) can be derived and determined for the borrower of such funds. There are no restrictions on the use of the proceeds from these loans, and the compliance and adherence to incorporated ESG/Sustainability metrics are benchmarked and measured periodically by external and independent third parties, with the lender encouraging borrowers to meet these pre-determined SPTs via pricing and loan structure incentives.

The LMA has also developed voluntary guidelines recommended for SLL[28] issuances in 2019 which have been revamped in May 2021. The framework has five key components to consider:

1- Selection of KPIs: borrowers should communicate to lenders their sustainability goals as set out in their ESG strategy and how they align with their proposed SPTs. Borrowers should select KPIs that are material to their sustainability and business strategy with the considerations (shown in figure 4) in mind for each KPI.

2- Calibration of SPTs: SPTs should be calibrated as per each KPI, and should be meaningful and ambitious to borrowers' businesses and tied to a sustainability improvement in relation to a predetermined performance target benchmark.

3- Loan characteristics: a key characteristic of SLLs is that an economic outcome is linked to whether selected SPTs are met. E.g. reduction in loan pricing margins if borrower satisfies pre-determined SPTs/KPIs.

4- Reporting: borrowers should furnish at least yearly reports with information on company performance against SPTs with third party opinion on the information to supplement these reports and gauge the materiality of SPTs

5- Verification: borrowers should seek independent external review on reports communicated to lenders for assurance on borrower's performance and commitment to SPTs

SLL issuances in 2019 saw astronomical growth to USD 140.1 billion from USD 46.8 billion in the preceding year[29]. Given the broad applicability of funds within SLL, we expect the growth to continue through 2021 and beyond.

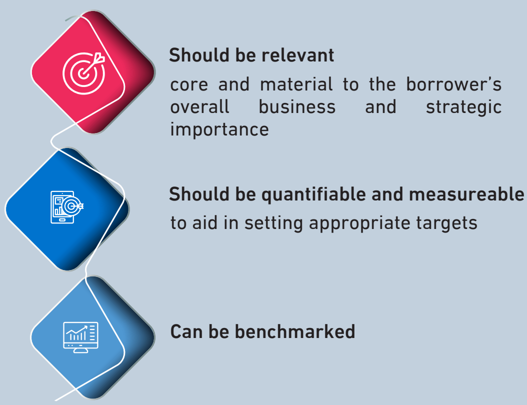


Figure 4: Considerations for Selection of KPIs

Sustainable Trade Finance

As the Bond and Loan market matures, financial institutions are also increasingly investing resources and efforts in innovating and introducing funded and non-funded working capital financial products and solutions that focus on 'green' and 'sustainable' dimensions to support and promote business and institutional clients to meet their ESG performance targets. Sustainable Trade Finance encompasses a range of trade finance products and instruments extended under special facility limits granted for customers to facilitate green and sustainable commercial transactions and activities.

a) Sustainable Trade Instruments

These products refer to trade finance instruments such as bank guarantees, letters of credit, or standby letters of credit issued under sustainable trade finance unfunded facility limits exclusively extended to the customers of a financial institution to facilitate environmentally and/or socially sustainable economic and business activities, including:

- Sourcing sustainably extracted/produced raw materials
- Procuring environmentally or socially sustainable machinery/goods/services Manufacturing or producing sustainable products
- Trading of sustainable commodities Supporting sustainable infrastructure projects

Due to the lack of availability of market principles for 'unfunded' instruments, financial institutions such as HSBC took the initiative to develop Sustainable Trade Instrument principles to address the specific needs of their clients and the market.

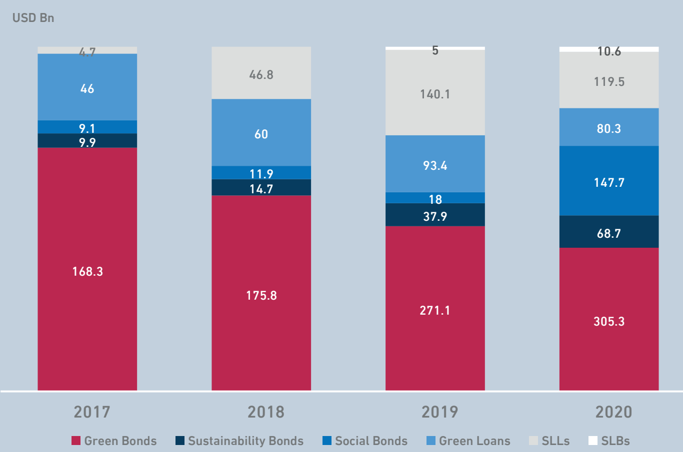


Figure 5: Persistent Overall Growth in the Sustainable Debt Market (USD Billion)

b) Green Trade Finance

The Green Trade Finance proposition incorporates funded trade finance products such as trade loans and receivables finance exclusively to fund environmentally sustainable/green trade activities involving purchase, supply or trading of goods which can be evidenced by underlying trade transaction documents, in adherence to the Green Loan Principles (GLP).

c) Sustainable Supply Chain Finance

A supply chain financing solution is a model of facilitating trade transactions where the suppliers can receive upfront payments financed by their buyers' banks, with the former bearing the cost of financing. Such solutions are ideal for suppliers who have a strong business relationship with buyers that enjoy better credit and pricing with their bankers. Under the sustainable proposition, banks can make early payments to their customers' suppliers on pricing terms that take into account the latter's sustainability performance.

2.3. Case Study: Existing Example in the Region

ماجد الفطيم
MAJID AL FUTTAIM

In 2019, the UAE-based Majid Al Futtaim Group (MAF), a leading shopping mall operator, retail and leisure pioneer across the Middle East issued two Green Sukuks valued at USD 600 million[30] each listed on Nasdaq Dubai. In addition to being MAF's debut green offering, these landmark issuances marked a number of key milestones for the group and in the market:

- It was the first green transaction from a non-financial institution in the MENA region
- It was the first benchmark-size green sukuk by a corporate globally

The order book on the offering gained great momentum following MAF's roadshow to investors, and quickly attracted interest and subscriptions from investors across MENA and Asia followed by Europe and US. The issuances were met with strong demand with the order book peaking at USD 3 billion. In addition to broadening its high quality investor base, the 4.7x ove rsubscription allowed MAF to price the bonds favourably.

MAF has developed a 'Green Finance Framework' [31] opting for the issuance of Green Bonds/Sukuk for capital budgeting activities aimed at sustainable and green projects. These issuances are aligned with the pillars of the Green Bond Principles (2018) developed by the ICMA, and the framework that MAF has developed is considered as exemplary work in compliance to these principles and meeting its standards with flying colours:

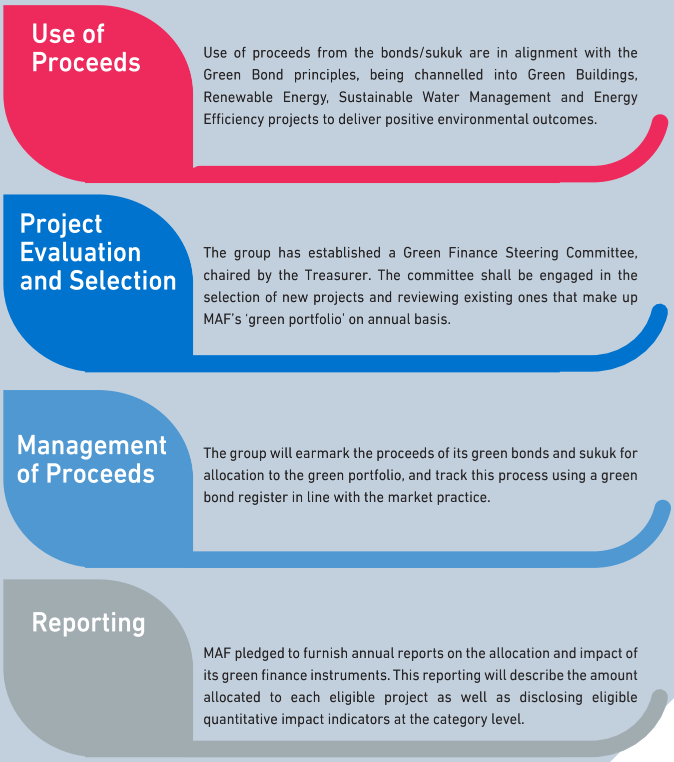


Figure 6: MAF Green Finance Framework

3. CONCLUSION

ESG and Sustainable Finance is a mega trend and is already seeing exponential growth. Over the coming years ESG investing is expected to continue to be the key topic taking center stage in Bahrain and the GCC. According to a Bloomberg report[32], analysts are projecting that the total market value of ESG investments to reach USD 53 trillion representing a third of the total global assets under management by 2025. The awareness and interest among regional Issuers, investors and regulators is noticeably growing in the direction of the global trends. Regional issuers are increasingly demonstrating active steps towards embracing sustainable and ESG aligned goals and objectives in developing long-term strategies, and are supported by the products and instruments developed by financial institutions to cater to these requirements and commitments with innovative solutions to support capital budgeting decisions. Investors in the region are driving a growing demand for ESG aligned issuances and investment options that address pressing issues, evaluating and upholding corporates and issuers on their ESG and sustainability commitments and on the delivery of their promised outcomes. Regulators understand their important role in facilitating a conducive and efficient regulatory environment in the marketplace to promote such issuances and investments to grow and thrive while ensuring the adherence of issuers to the best standards and frameworks with increasing emphasis on mandatory ESG disclosures and reporting. It is highly likely for the GCC countries to adopt similar disclosure requirements as those already being rolled out in Europe.

To get started, each organization should aim to develop an ESG or sustainability strategy with measurable targets. The targets should be focused on the most material ESG issues for each organisation, and this will vary based on the type of sector, or region and geographical reach. Common ESG issues include, for instance, greenhouse gas emissions, water use, waste generated, women in management positions, health and safety management, and many more. The GRI framework for sustainability reporting has one of the most comprehensive lists of ESG issues, including sector-level guidance on the most material ESG issues for each sector. Once a strategy is in place with defined targets and key milestones agreed, it is also important for organizations to consider a reporting framework, data collection, transparency, and embedding the business culture to represent the shift towards a sustainable business operation.

If you are interested to know more about Sustainable Finance and how to get started on your ESG journey, please contact representatives from Bahrain Bourse or HSBC on the below contacts:

Bahrain Bourse
P.O.Box 3203 Manama, Kingdom of Bahrain
Tel: +973 17 261260
Fax: +973 17 256362
Email: mbsd.info@bahrainbourse.com
Web: www.bahrainbourse.com

HSBC Bank Middle East Ltd. – Bahrain Branch
P.O Box 57, Manama
Kingdom of Bahrain
csc.bahrain@hsbc.com
www.business.hsbc.com.bh/en-gb/environment-social-governance-business-for-the-future

4. GLOSSARY

Sukuk

Fixed income debt instruments functioning as the Islamic shariah-compliant alternative to conventional bonds.

Net Zero

The balance between the amount of greenhouse gas produced and the amount removed from the atmosphere achieving carbon neutrality.

International Capital Market Association (ICMA)

A self-regulatory organization and trade association for participants in the capital markets. ICMA aims to promote high standards of market practice, appropriate regulation, trade support, education and communication.

Loan Market Association (LMA)

Formed in December 1996 and based in London, UK, its key objective is improving liquidity, efficiency and transparency in the primary and secondary syndicated loan markets in Europe, the Middle East and Africa (EMEA).

Sustainability Performance Targets (SPTs)

Are measurable improvements in key performance indicators to which issuers commit to a predefined timeline. SPTs should be ambitious, material and where possible benchmarked and consistent with an issuer's overall sustainability/ESG strategy.

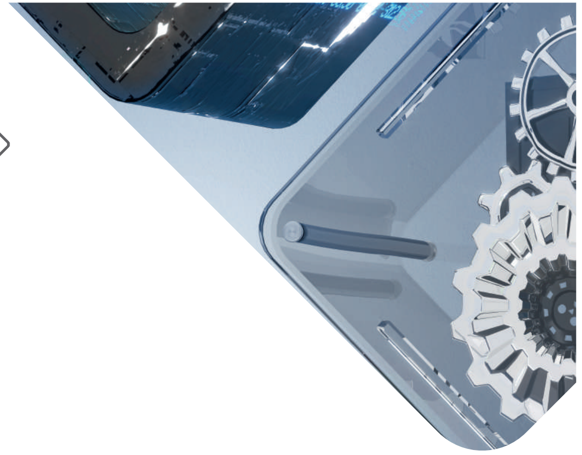
Bank Guarantees / Standby letters of Credit

A security undertaking by a licensed financial institution on behalf of obligors who are bonded to a certain performance or agreement towards their counterparties.

Letters of Credit

A security undertaking by a bank to reimburse the selling party on behalf of their buyer in a commercial transaction with amount due to them under the agreement upon their compliance to the terms set out in the letter of credit.

ABOUT BAHRAIN BOURSE



Who we are

Bahrain Bourse is a self-regulated multi-asset marketplace. Bahrain Bourse aims to offer to its investors, issuers, and intermediaries a comprehensive suite of exchange-related facilities including offering listing, trading, settlement, and depository services for various financial instruments.

We aim to offer our stakeholders with the best investment and trading solutions, and pair it with creative insights and problem-solving skills to provide our investors, issuers, and intermediaries with valuable resources to meet their every expectation. Our key growth pillars underpins our way of conducting business and how we interact with our stakeholders: Origination, Innovation, Collaboration, and Pioneering Spirit, and all of them working together is what enables us to offer you with an "Oasis of Investment Opportunities".

Our history extends back to 1987, which marked the establishment of "Bahrain Stock Exchange (BSE)", the predecessor of "Bahrain Bourse (BHB)". Since then, Bahrain Stock Exchange has achieved milestone successes, largely attributed to the support of the Government of Kingdom of Bahrain and the collaboration provided by its stakeholders. In 2010, Bahrain Bourse was established in accordance with Law No. 60 for the year 2010 as a shareholding company to replace its predecessor Bahrain Stock Exchange. Bahrain Bourse is the sole entity in the Kingdom of Bahrain licensed by the Central Bank of Bahrain to act as a licensed exchange.

Bahrain Clear, a fully-owned subsidiary of Bahrain Bourse, was established in June 2017 as a clearing house with a disclosed capital of BD5 million, and a paid up capital of BD1 million. Bahrain Clear is licensed by the Central Bank of Bahrain and offers pre and post trade services to investors as well as a range of services including transactions depository, clearing, settlement, central registry and registration. Since its establishment, BHB has joined several regional and international organizations such as Arab Federation of Exchanges “AFE”, International Organization of Securities Commissions “IOSCO”, World Federation of Exchanges "WFE", Africa & Middle East Depositories Association "AMEDA", and Association of National Numbering Agencies "ANNA", partner exchange member to the Sustainable Stock Exchanges “SSE” Initiative, and Middle East Investor Relations Association – Bahrain Chapter “MEIRA”, which enables Bahrain Bourse to bolster its position within the global capital markets.

What we do

Bahrain Bourse, as a Self-Regulated Organization (SRO) and a front-line regulator, plays a key role in shaping Bahrain’s capital markets. Bahrain Bourse provides a platform for the listing and trading of a various securities including Equities, Real Estate Investment Traded Funds (REITs), Government Bonds and Sukuks, T-Bills, Mutual Funds, and Bahrain Investment Market.

بورصـــــة البحـــرين
BAHRAIN BOURSE

P.O.Box 3203 Manama, Kingdom of Bahrain
Tel: +973 17 261260
Fax: +973 17 256362
Email: mbsd.info@bahrainbourse.com
Web: www.bahrainbourse.com
Follow us on:

ABOUT HSBC

About HSBC

Our purpose – Opening up a world of opportunity – explains why we exist. We're here to use our unique expertise, capabilities, breadth and perspectives to open up new kinds of opportunity for our customers. We're bringing together the people, ideas and capital that nurture progress and growth, helping to create a better world – for our customers, our people, our investors, our communities and the planet we all share.

HSBC is one of the world's largest banking and financial services organisations. Our global businesses serve more than 40 million customers worldwide through a network that covers 64 countries and territories.

Our customers range from individual savers and investors to some of the world's biggest companies, governments and international organisations. We aim to connect them to opportunities and help them to achieve their ambitions.

We have been present in Bahrain since 1944 and the products and services we offer vary widely according to customers' needs. We provide individuals and families with mortgages that help them buy their own home, as well as savings accounts and wealth management products that help them plan for the future.

We offer businesses loans to invest in growth, and products such as foreign exchange and trade financing that enable them to expand internationally. And for large companies and organisations operating across borders, we offer tailored advice on decisions such as financing major projects, issuing debt or making acquisitions.

Becoming a net zero bank

We are committed to reducing our footprint through our operations, supply chain and financing portfolio. Being net zero means reducing the emissions we add to the atmosphere while increasing the amount we remove, so we achieve a balance that protects the planet, while creating a thriving, resilient global economy.

At the heart of our climate plan is a goal to align financed emissions from our portfolio of customers to the Paris Agreement goal of net zero by 2050 or sooner.

Intensifying our support for customers in their transition to lower carbon emissions is key to achieving this goal. Our global ambition is to provide between USD750 billion and USD1 trillion in sustainable financing and investment by 2030 to support them as they switch to more sustainable ways of doing business. We will also provide expert, tailored advice through our dedicated ESG Solutions team.

We believe collaboration is the best way to protect the planet. We work with investors, governments, non-governmental organisations, other financial institutions and our suppliers to support long-term investment in environmentally sustainable projects.

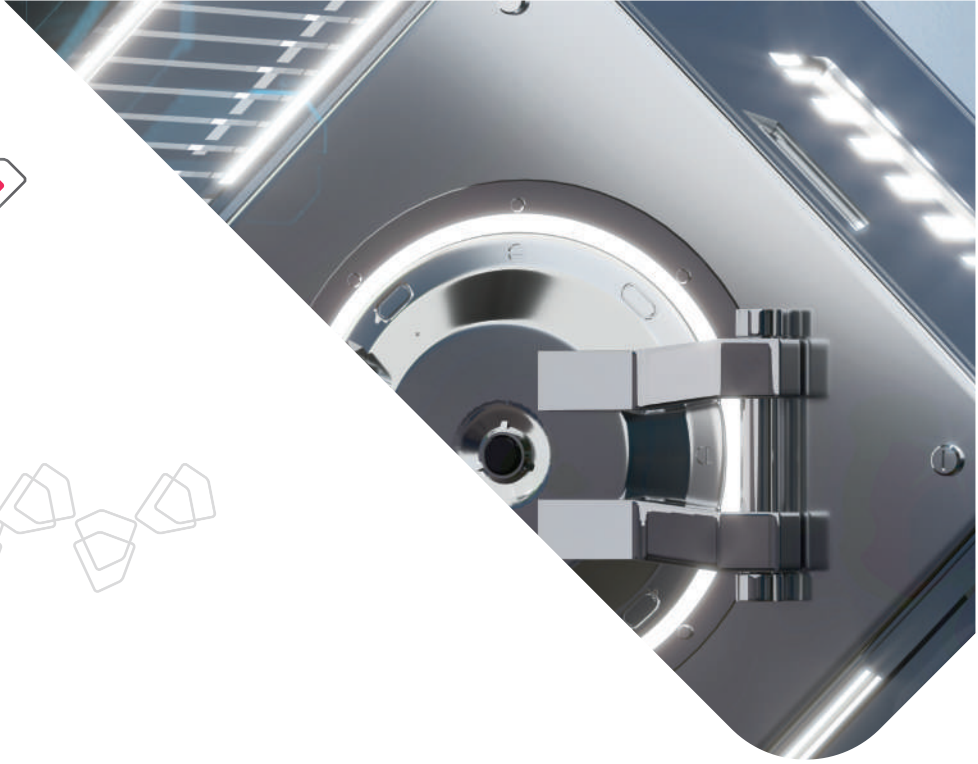
As we work to achieve net zero, we will build coalitions of public and private bodies to mobilise the financial system to develop globally consistent, future-proofed standards for measuring and tracking financed emissions.

HSBC

HSBC Bank Middle East Limited
P. O. Box: 57
Manama, Kingdom of Bahrain

www.business.hsbc.com.bh/en-gb/environment-social-governance-business-for-the-future

DISCLAIMER



This document has been jointly prepared by Bahrain Bourse BSC (c) (‘BHB’) and HSBC Bank Middle East (‘HSBC’) for information purposes only.

The information provided herein are made in good faith and based on sources belived to be reliable at the time. Neither BHB nor HSBC nor any of their directors or employees give any representation or warranty as to the reliability, accuracy, or completeness of the information, nor do they accept any responsibility arising in any way for errors or omissions from the information, nor shall be held responsible for any loss or damage arising out of the use of all or part of this document by the recipient. Bahrain Bourse and HSBC are not responsible for any unintentional errors or omissions.

Issued jointly by Bahrain Bourse BSC (c) licensed and regulated by the Central Bank of Bahrain, and HSBC Bank Middle East Limited Bahrain Branch, P.O. Box 57, Manama, Kingdom of Bahrain, licensed and regulated by the Central Bank of Bahrain as a Conventional Retail Bank in the Kingdom of Bahrain and lead regulated by the Dubai Financial Services Authority.

REFERENCES

1. Bahrain Bourse Sustainability Report 2020: https://bahrainbourse.com/resources/files/Sustainability/sus-tainability%20report_2020_en.pdf

2. Bahrain Economic Vision 2030: www.bahrain.bh

3. Global Sustainable Investment Review (2016, 2018): http://www.gsi-alliance.org/wp-content/uploads/2019/03/G-SIR_Review2018.3.28.pdf

4. ESG Data Integration by Asset Managers: Targetting Alpha, Fiduciary Duty & Portfolio Risk Analysis: http://www.opimas.com/re-search/570/detail/

5. The Paris Agreement - UNFCCC: https://unfccc.int/process-and-meetings/the-paris-agreement/the-paris-agreement

6. Saudi Green Initiative: https://saudigreeninitiative.org

7. Saudi Aramco Energy Ventures Plans New $500M Fund Targeting Renewable Energy: https://www.greentechmedia.com/arti-cles/read/saudi-aramco-energy-ventures-plans-launch-of-500-million-fund

8. Dubai Clean Energy Strategy - The Official Portal of the UAE Government: https://u.ae/en/about-the-uae/strategies-initia-tives-and-awards/local-governments-strategies-and-plans/dubai-clean-energy-strategy

9. Sustainable Energy Authority – Kingdom of Bahrain: https://www.sea.gov.bh/

10. Tech Firms Are Setting the Most Ambitious Net-Zero Goals: Green Insight - Bloomberg: https://www.bloomberg.com/news/arti-cles/2021-04-07/tech-firms-are-setting-the-most-ambitious-net-zero-goals-green-insight

11. Propositions- HSBC UAE: https://www.business.hsbc.ae/en-gb/environment-social-govern-ance-business-for-the-future/propositions

12. International Labour Organization: https://www.ilo.org/global/lang--en/index.htm

13. Social Bonds Propel ESG Issuance: https://www.bloomberg.com/news/articles/2021-01-11/so-cial-bonds-propel-esg-issuance-to-record-732-billion-in-2020

14. Bahrain Bourse Joins UN SUstianable Stock Exchanges Initiative: https://www.bahrainbourse.com/bahrain-bourse-joins-un-%E2%80%99s-sustainable-stock-exchanges-initiative

15. Bahrain Bourse ESG Reporting Guideline: https://www.bahrainbourse.com/resources/files/Sustainabili-ty/ESG_11-June-2020-V2.pdf

12. International Labour Organization: https://www.ilo.org/global/lang--en/index.htm

13. Social Bonds Propel ESG Issuance: https://www.bloomberg.com/news/articles/2021-01-11/so-cial-bonds-propel-esg-issuance-to-record-732-billion-in-2020

14. Bahrain Bourse Joins UN SUstianable Stock Exchanges Initiative: https://www.bahrainbourse.com/bahrain-bourse-joins-un-%E2%80%99s-sustainable-stock-exchanges-initiative

15. Bahrain Bourse ESG Reporting Guideline: https://www.bahrainbourse.com/resources/files/Sustainabili-ty/ESG_11-June-2020-V2.pdf

16. UAE Securities & Commodities Authority Mandates Sustainability Reporting: https://feeds.dfm.ae/documents/2021/Jan/31/2a177-bee-9cea-4343-a8b8-6bd3e0acc939/SCA_MDN.pdf

17. Corporate Sustainability Reporting - European Commission: https://ec.europa.eu/info/business-economy-euro/company-repor-ting-and-auditing/company-reporting/corporate-sustainability-reporting_en

18. Securities and Exchange Board of India: https://www.sebi.gov.in/

19. United Nations: Principles for Responsible Investing: https://www.unpri.org/

REFERENCES

20. Blackrock's 2020 Letter to Clients: https://www.blackrock.com/corporate/investor-relations/2020-blackrock-client-letter

21. Saudi Electricity Company: https://www.se.com.sa/

22. ICMA Green Bond Principles (GBP): https://www.icmagroup.org/sustainable-finance/the-principles-guidelines-and-handbooks/green-bond-principles-gbp/

23. ICMA Social Bond Principles (SBP): https://www.icmagroup.org/sustainable-finance/the-principles-guidelines-and-handbooks/social-bond-principles-sbp/

24. Sustainability Bond Guidelines (SBG): https://www.icmagroup.org/sustainable-finance/the-principles-guidelines-and-handbooks/sustainability-bond-guidelines-sbg/

25. Sustainability-Linked Bond Principles (SLBP): https://www.icmagroup.org/sustainable-finance/the-principles-guidelines-and-handbooks/sustainability-linked-bond-principles-slbp/

26. Climate Transition Finance Handbook: https://www.icmagroup.org/sustainable-finance/the-principles-guidelines-and-handbooks/climate-transition-finance-handbook/

27. Loan Market Association - the authoritative voice of the European market: https://www.lma.eu.com/

28. LMA Sustainability-linked Loan Principles: https://www.lma.eu.com/application/files/5115/8866/8901/Sustainability_Linked_Loan_Principles_V032.pdf

29. The Sustainable Debt Market Is All Grown Up - Bloomberg: https://www.bloomberg.com/news/articles/2021-01-14/the-sustainable-debt-market-is-all-grown-up

30. Majid Al Futtaim Lists Corporate Green Sukuk: https://www.majidalfuttaim.com/en/media-centre/press-releases/2019/05/majid-al-futtaim-lists-world-s-first-benchmark-corporate-green-sukuk--on-nasdaq-dubai

31. Majid Al Futtaim – Green Finance Framework (April 2019): https://www.majidalfuttaim.com/-/media/feature/mafcorporate/investor/downloads/bonds-and-credits/green-finance-framework.pdf

32. Expert insights into data and ESG in the Middle East | Bloomberg Professional Services: https://www.bloomberg.com/professional/blog/expert-insights-into-data-and-esg-in-the-middle-east/?tactic-page=438402