

# Sustainability Bonds Framework

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## FMO Sustainability Bonds framework 2018

This document (the “Sustainability Bond Framework” or “SBF”) contains information on Nederlandse Financieringsmaatschappij voor Ontwikkelingslanden NV (“FMO”) issuance of interest-bearing notes with added environmental criteria. The SBF<sup>1</sup> addresses 4 key pillars of the Green Bond Principles (GBP): definition and use of proceeds criteria (GBP1), process for selection and evaluation of projects (GBP2), management of proceeds (GBP3), reporting on eligible projects (GBP4).

## FMO is the Dutch Development Bank

Since 1970, FMO has been the driving force behind investments empowering entrepreneurs in emerging markets. We invest with the aim of enhancing local prosperity in places where this is needed most. We focus on underserved markets in key sectors for development, taking risks that few others are willing to take. Our role extends beyond financing, as we challenge businesses to meet high international standards regarding the welfare of people, corporate governance and the environment. These businesses in turn create jobs and tax income and contribute to a healthy private sector improving people’s prospects for a better life.

Last year, we launched our renewed strategy as part of our endeavours to contribute to a world in which, in 2050, nine billion people will live well and within the means of the planet’s resources. Our strategy calls on us to create a higher impact portfolio, deepen our relationships and increase productivity. Through our financing and investments, we enhance our and others’ impact and can contribute to a sustainable society on a liveable planet. We support the 17 United Nations Sustainable Development Goals (SDGs) and aim to contribute to their achievement through our mission and activities. In doing so, we focus on three prime SDGs:

- SDG 8: creating decent work and economic growth
- SDG 10: reducing inequalities
- SDG 13: climate action

To steer on impact supported with our investments, FMO has developed two steering metrics:

1. The Green Label, which steers our impact related to green investments associated with SDG 13: Climate Action, which translates into each department having its annual Green target for new production
2. The Reduced Inequality (RI) Label to steer impact related to reduced inequality projects associated with SDG 10: reduce inequality within and among countries. Two tracks underline the RI label: investments in the poorest countries (*reducing inequality among countries*) and

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<sup>1</sup> Please note that the framework does not include ring-fencing of projects and using separate accounts, as this will lead to inefficiencies in terms of liquidity management and operation

investments in inclusive business (*reducing inequality within countries*). Reducing inequalities is also connected to gender and equality for women and men (SDG5).



Our strategy aligns well with the recently published Investing in Global Prospects policy of the Dutch Ministry of Foreign Affairs, one of our key stakeholders. This policy aims to tackle the root causes of poverty, migration, terrorism and climate change, while enhancing the Netherlands' international earning capacity.

## 2018 Sustainability Bond Framework Update

The SBF is updated as per December 2018 in order (i) to include new categories for green and social projects, with corresponding eligibility criteria in the use of proceeds, and (ii) to allow FMO to issue Green Bonds, Social Bonds or Sustainability Bonds (Figure 1 on the next page presents FMOs SBF).

New categories, as per the 2018 Sustainability Bond Framework, as indicated in *italic*.

- I. Green projects
  - a. Climate Change Mitigation
  - b. Climate Change Adaptation
  - c. *Other Footprint (e.g., water and waste management, biodiversity) [NEW]*
- II. Social projects, aiming at reducing inequalities
  1. *Investments in the poorest countries (LDCs, Least Developed Countries)*
  2. Investments in inclusive business
    - a. Microfinance
    - b. WSME
    - c. Gender
    - d. *Agricultural SMEs [NEW]*
    - e. *Smallholder finance [NEW]*
    - f. *Agribusiness with smallholders [NEW]*
    - g. *Off-grid power [NEW]*
    - h. *Innovative solutions for the base of the pyramid [NEW]*
    - i. *Youth finance [NEW]*

The added Green and Social categories and eligibility criteria do not apply retroactively to FMOs Sustainability Bonds issued under the previous framework, but is applicable to future bonds, and hence only future investments.

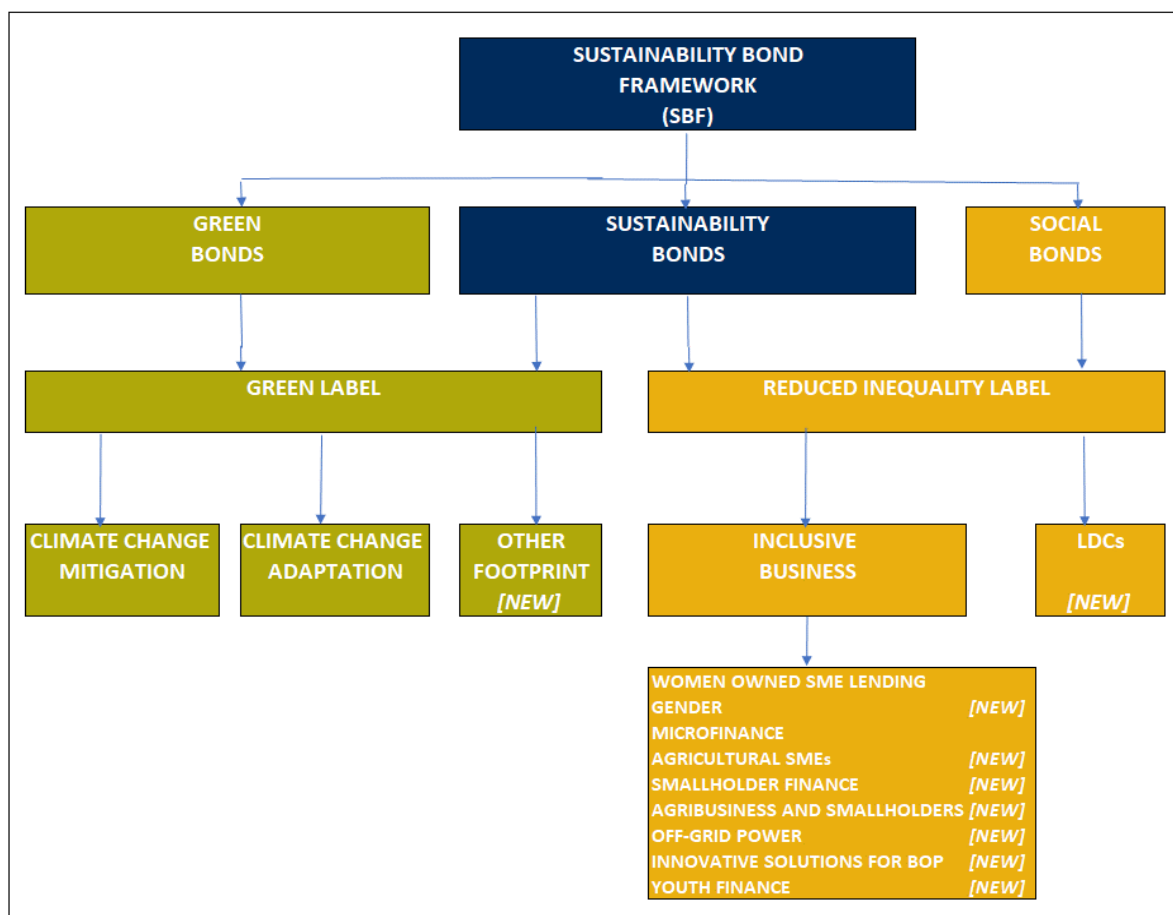
The use of proceeds will be included in the associated bond documentation (final terms) and specify whether the issued notes are either Green Bonds, Social Bonds or Sustainability Bonds. The final terms of the relevant public Green Bonds, Social Bonds or Sustainability Bond issued, will be published on FMOs website: <https://www.fmo.nl/funding-programs>

*Specifying bonds use of proceeds under the Sustainability Bond Framework*

Green Bonds are senior unsecured bonds, ranking pari-passu with bonds issued under FMO's Debt Issuance Program aimed at financing green projects. Social Bonds are senior unsecured bonds, ranking pari-passu with bonds issued under FMO's Debt Issuance Program aimed at financing reduced inequality projects. Sustainability Bonds are senior unsecured bonds, ranking pari-passu with bonds issued under FMO's Debt Issuance Program aimed at financing green and reduced inequality projects.

FMO applies strict investment criteria and follows a thorough due diligence process and integrated environmental, social and governance (ESG) approach. Eligible projects may be financed directly or indirectly, including through financial intermediaries.

Figure 1: SBF overview



## 1. Defining Investment Categories and Use of Proceeds criteria

This section defines green projects and social projects aiming at reduce inequalities, and provides eligibility criteria. FMO plans to use proceeds of bonds issued under this SBF to finance green and social projects to support its mission.

### 1.1 Green Projects Definition

All green investments should meet FMOs green principles described below.

#### FMOs Green Principles

1. Principle 1: Green investments contribute to a genuine improvement.
  - There should be a genuine improvement resulting from FMO's investment that is beyond the local regulatory requirements.
    - Example: If the local/regional market share of CNG (compressed natural gas) vehicles is saturated or approved by the local government as the only fuel type



that can be imported then replacing them with new CNG vehicles does not contribute to a genuine improvement and is not Green.

- Green investments should also be unrelated to local resources stress.
  - Example: Water efficiency is seen as Green provided it is more than 20% more efficient than what it was before, regardless of whether it is in a high rainfall area or a desert.
- 2. Principle 2: Green investments should not contribute to a long-term lock-in of high carbon infrastructure

FMO's definition of green projects focuses on climate-related projects that should be value-adding and go beyond compliance with local regulatory standards in order to initiate and/or enable a market shift. FMO defines three sub categories under green: climate change mitigation, climate change adaptation and other footprint.

#### Definition of Green Projects Categories

**Table 1 Definition Green Projects categories**

Category	Definition
<b>Climate Change Mitigation</b>	An activity is considered to be mitigating climate change if it contributes to either, reducing greenhouse gas (GHG) emissions into the atmosphere, or sequestering GHG emissions from the atmosphere. If the project or activity relates to Energy efficiency, it should achieve at least 20% reduction in energy consumptions or GHG emissions
<b>Climate Change Adaptation</b>	An activity is considered as climate change adaptation if the intention of the activity or project design is to reduce the vulnerability of human or natural systems to the impacts of climate change and climate-related risks, by maintaining or increasing adaptive capacity and resilience
<b>Other Footprint</b>	This category includes those activities that do not directly target climate change mitigation or adaptation yet have a positive impact on the environment including water, waste and biodiversity

## 1.2 Green Projects Eligibility Criteria

### Climate Change Mitigation Eligibility Criteria

For Climate Change Mitigation, FMO aligns with the existing common principles of Climate Mitigation as defined in the Multilateral Development Banks (MDBs) report for Climate Finance Tracking.

To be eligible for Green or Sustainability Bond proceeds, FMO states that a mitigation activity:

- Should contribute to the mitigation of climate change by reducing or avoiding GHG, or contribute to the protection and/or enhancement of GHG sinks and reservoirs that absorb GHGs;
- Can be a project or project component;
- Should be disaggregated from non-mitigation activities through a reasonable level of data granularity. For example, a project with a total cost of EUR 100 million may have a EUR 10 million component for energy efficiency improvements – only the EUR10 million should be allocated.



For a full list of eligible climate mitigation activities is referred to Annex 1a Eligible green activities under climate change mitigation. Broadly, they can be categorised as:

- Energy efficiency in industrial equipment/machinery, in buildings
- Renewable Energy;
- Transport;
- Agriculture, forestry and land use;
- Waste and wastewater;
- Cross-sector activities.

#### Climate Change Adaptation Eligibility Criteria

FMO defines this category along the lines of the Joint Report on MDB Climate Finance and states that to be eligible for Green or Sustainability Bond proceeds an adaptation-related activity needs to demonstrate that it potentially contributes to reducing the vulnerability to climate change identified in the project area, and that the following should be provided to substantiate this:

- A description of the context of climate vulnerability of the project based on an investigation of the vulnerabilities to climate change of the project's geographical area;
- An explicit statement of intent to address climate vulnerability as part of the project. This should be supported by an analysis of the project's planned activities to decipher a positive list of actions that can contribute to reducing vulnerability, or strengthening the resilience of communities, goods, or ecosystems to climate change;
- The articulation of a clear and direct link between the climate vulnerability context and the specific project activities; and
- Evidences that the project does not have negative impacts in terms of climate change mitigation (e.g., enhancing carbon intensive infrastructures).

For a full list of eligible climate adaptation mitigation activities is referred to Annex 1b Eligible green activities under climate change adaptation.

A few examples of climate change adaptation activities:

- Climate Smart Agriculture
- Increasing biological diversity
- Fisheries co-management and controlling overfishing
- Adaptive land use management

#### Eligibility Criteria for Green Projects with Other Footprint

This category includes those activities that do not directly target climate change mitigation or adaptation yet have a positive impact on the environment including water quality, waste treatment and biodiversity protection.

Water-related companies: Investment in a water supply activity is only eligible as 'Green' if:

- The process is either 20% more water- or energy- efficient than the most likely alternative or causes a shift to a less stressed water resource, and;
- The source of water is not contributing to depletion of a stressed water resource.

Remark : for Recycling companies:

- Recycling or waste water treatment as core business activity is considered a 'Green Client'.
- Recycling as part of business model is considered potentially (and partially) eligible for Green depending on certain case-specific factors like the measure(s) used and the context

For a full list of eligible other footprint activities is referred to Annex 1c Eligible green activities under other footprint. A few examples of other footprint activities:

- Waste water cleaning and full recycling
- Rainwater harvesting and storage
- Nutrient capture from waste water sewage
- Upgrading to best available techniques for recycling
- New process/technology to accommodate the use of recycled input
- Sanitation facilities with proper waste treatment if it replaces open defecation

### 1.3 Definition of Social Projects aiming at reduced inequalities

FMO defines two sub categories in social projects aiming at reduced inequalities: investments in the poorest countries (*reducing inequality among countries*) and investments in inclusive business (*reducing inequality within countries*).

Table 2 outlines FMO's definition of reduced inequality categories.

Table 2 Reduced Inequality investment categories

Category	Definition
<b>Investment in LDCs</b>	These are countries identified by the United Nations as "low-income countries" which are confronted with severe structural impediments
<b>Investment in inclusive business</b>	An inclusive business " <i>expands access</i> " to goods, services and livelihood opportunities on a commercially viable basis, either at scale or scalable, to people at the Base of the Pyramid (BOP) by making them part of the value chain of companies' core business of suppliers, distributors, retailers or customers

Note that, as part of the inclusive business definition, "*expands access*" refers to a first time or improved access to goods or services which strengthen the livelihoods of the end-beneficiaries by being verifiably of higher quality than the goods or services which they replace *or* an access that is more cost effective or efficient. Investments that expand access should lead to clear improvements in the lives of the BOP populations. BOP population is defined as the portion of the global population that lives on less than \$8 per day in purchasing power parity (PPP) terms or lacks access to basic goods, services, and income. Reaching the BOP populations is in line with FMO's commitment to reducing poverty and inequality (SDG 1 and 10). In practice, because of lack of data, it is not feasible

to measure the income of the end-beneficiaries of a business. FMO defined a number of proxies for the BOP/people lacking access to basic goods and services:

- The un(der)banked
- The unconnected / poorly connected
- Smallholder farmers and rural populations
- Youth
- Women

#### 1.4 Eligibility Criteria for Social Projects aiming at Reduced Inequality

FMO is committed to provide funds generated through the issuance of its Sustainability Bonds to microfinance institutions (MFIs) as well as directly to small- and medium-sized enterprises (SMEs) in developing and emerging markets. FMO undertakes a detailed due diligence exercise, including an assessment of ESG related risks, before selecting a MFI or and SMEs which receive funding from FMO.

FMO is committed through the issuance of its Social Bonds to invest in reduced inequality projects:

1. In LDCs: LDC's are highly vulnerable to economic and environmental shocks and have low levels of human assets. Currently there are 47 LDCs, see the full list in Annex 2. The list is updated every three years by the UN. To keep target setting and steering manageable, FMO will use the June 2017 list until 2025. A list of eligible activities is disclosed in Table 3.
2. In Inclusive business

Based on the inclusive business definition and proxies and considering FMO's investment focus, a number of classes of inclusive business deals were defined, as illustrated by Table 4.

The categories in the list are similar to the inclusive business/gender categories of IFC, the leading DFI in the inclusive business space. The exception is agricultural SME lending – which is not considered inclusive per se by IFC. The eligibility criteria and thresholds (second column in the table) are FMO-specific as other DFIs (including IFC) have not developed similar eligibility criteria.

Table 3: Activities financed in least developed countries

Category	Eligibility	Definition
<b>Agribusiness, food &amp; water</b>	<ul style="list-style-type: none"> <li>• Inputs: Seeds, Animal feed, Fertilized</li> <li>• Primary production: Crops, Livestock, Production, Fishing</li> <li>• Processing: Crushing, Storage, Handling, Packaging</li> <li>• Trade: Trading, Exporting</li> <li>• Distribution: Logistics, to Retail</li> </ul> <p>Excluding activities that do not align with Good Agricultural Practices or which contribute to deforestation.</p>	Investing across the agribusiness value chain – enhancing food security, supporting sustainability, efficient water usage, and promoting inclusive development

<b>Energy</b>	<ul style="list-style-type: none"> <li>• Wind</li> <li>• Solar</li> <li>• Hydro (Run-of-river)</li> <li>• Off-grid solutions</li> <li>• Resource efficiency &amp; refurbishment</li> </ul> <p>Excluding investments in fossil fuel based technologies</p>	Investing in long-term projects in the areas of generation and distribution – promoting the transition to a low-carbon system and safeguarding energy security.
<b>Financial Institutions</b>	<ul style="list-style-type: none"> <li>• SME Banks</li> <li>• Microfinance</li> <li>• Leasing companies (excluding leasing for fossil fuel technologies)</li> <li>• Insurance companies</li> <li>• FinTech</li> </ul>	Investing in long-term financing solutions, increasing access to finance and supporting financial inclusion

Table 4: Inclusive business definition and categories

Category	Eligibility	Definition
<b>Microfinance</b>	FMO's financing is earmarked for on lending to micro-enterprises	Micro-enterprise loans are defined as loans to businesses with an original loan amount < EUR 10,000
<b>Agricultural SME lending</b>	FMO's financing is earmarked for on- lending to agricultural SMEs.	Agricultural SMEs are defined as SMEs active in primary production or the agricultural value chain. Proxy for SME: loan size between EUR 10,000 and EUR 1,000,000.
<b>Smallholder Finance</b>	FMO's financing is earmarked for on-lending to smallholders.	Smallholder farmers are defined as marginal and sub-marginal farm households that own and/or cultivate relatively small plots of land, have low access to technology, limited resources in terms of capital, skills, and risk management, and depend on family labor for most activities. (FAO)
<b>Agribusinesses working with smallholders</b>	The agribusiness client: i. sources at least 30% of its inputs from smallholders AND ii. provides technical and/or financial support to its smallholder suppliers. Financing is earmarked to investments for inputs from smallholder farmers or technical and/or financial support to smallholder suppliers	Smallholder farmers are defined as marginal and sub-marginal farm households that own and/or cultivate relatively small plots of land, have low access to technology, limited resources in terms of capital, skills, and risk management, and depend on family labor for most activities. (FAO)
<b>Youth Finance</b>	FMO's financing is earmarked for young entrepreneurs or for youth-specific financial products/services (e.g. education loans) .Youth is defined as people under 35.	Youth finance is defined as people under 35

<b>Off-grid power</b>	FMO's financing is earmarked for off- grid power	Off grid in energy means stand- alone power systems or mini-grids that provide energy to e.g. households, communities, businesses and agriculture in remote and/or peri-urban areas. It includes businesses active in a range of products and solutions, such as pico and solar home systems, as well as (improved) cook stoves, agricultural appliances and mini-grids
<b>Innovative solutions for the BOP</b>	Investments in businesses that use innovative models (including Fintech) to bring essential goods, services and livelihood opportunities to the BOP. At least 30% of the revenue of the business comes (or is expected to come) from the BOP activity. Financing is earmarked to BOP activity.	The general FMO definition of inclusive business applies.
<b>Gender: Women-owned SME</b>	FMO's financing is earmarked for women-owned MSME lending.	A women-owned business is an enterprise which is: (a) at least for 51% owned by a woman or by women, or (b) (i) at least for 20% owned by a woman or by women, (ii). with a woman as CEO, COO, President or Vice President and (iii). if such enterprise has a board of directors, with at least 30% of such board of directors comprised of women. (IFC)
<b>Gender: Other</b>	The investment qualifies otherwise as an inclusive business investment AND at least 2/3 of the end-beneficiaries are women	As an example, an investment in a microfinance institution would qualify for the gender label if at least 2/3 of the clients of the MFI are women.
<b>Inclusive business funds (equity or debt)</b>	Investments in funds with at least 50% of their investments expected to be in inclusive businesses. Financing is earmarked to inclusive businesses.	Inclusive businesses are any of the categories of businesses defined above.

Note that the above categories are not exclusive – so multiple categories might apply. As an example, an investment in a microfinance institution with mostly female clients would fall into both the “Microfinance” and “Gender: Other” categories.

#### Financing microfinance institutions (MFIs)

FMO carries out an annual review of each MFI and their lending to evaluate if MFIs are meeting the conditions set by FMO.

#### Financing small- and medium-sized enterprises (SMEs)

FMO commits to finance SMEs in developing and emerging markets, typically through financial intermediaries, such as SME (focused) Banks, non-bank financial institutions and corporates<sup>2</sup>. FMO is

<sup>2</sup> FMO Investment Criteria, February 2017

committed<sup>3,4</sup> to invest in some of the poorest countries in the world. To be eligible for the use of proceeds, financial institutions should:

specifically target one or more of the following populations: females; rural populations who are focusing on agricultural production and agricultural value chains; economically excluded individuals; and low-income populations who earn less than USD 8 per day;

For Micro, small and medium sized enterprises the following definition applies throughout the framework

Table 5. IFC's definition for Micro-, Small- and Medium-size Enterprises

Indicator/Size of enterprise	Micro-size enterprise	Small-size enterprise	Medium-size enterprise
Number of employees	< 10	10 < 50	50 – 300
Total assets	< USD 100,000	USD 100,000 < USD 3 million	USD 3 million < USD 15 million
Annual sales	< USD 100,000	USD 100,000 < USD 3 million	USD 3 million < USD 15 million

If data in accordance with above definition is not available, the end-client average loan size should be:

less than USD 10,000 (micro-loan)

between USD 10,000 or more, but less than USD 1,000,000

#### Exclusion criteria

In addition to eligibility criteria, FMO specifies the following exclusion criteria with regard to use of proceeds. FMO will not finance any business or trade involved in:

1. Forced labour or child labour .
2. Activities or materials deemed illegal under host country laws or regulations or international conventions and agreements, or subject to international phase-outs or bans, such as:
  - a) Ozone depleting substances, PCB's (Polychlorinated Biphenyls) and other specific, hazardous pharmaceuticals, pesticides/herbicides or chemicals;
  - b) Wildlife or products regulated under the Convention on International Trade in Endangered Species or Wild Fauna and Flora (CITES); or

<sup>3</sup> <https://www.fmo.nl/l/library/download/urn:uuid:638188d0-5def-49f4-bf5a-7db9c94ddb52/2016+fmo+annual+report.pdf>

<sup>4</sup> [https://www.fmo.nl/l/library/download/urn:uuid:9978eafe-864f-4b3a-bed1-5e0563df0c85/fmo+sustainability+policy.pdf?format=save\\_to\\_disk&ext=.pdf](https://www.fmo.nl/l/library/download/urn:uuid:9978eafe-864f-4b3a-bed1-5e0563df0c85/fmo+sustainability+policy.pdf?format=save_to_disk&ext=.pdf)

- c) Unsustainable fishing methods (e.g., blast fishing and drift net fishing in the marine environment using nets in excess of 2.5 km in length).
- 3. Cross-border trade in waste and waste products, unless compliant with the Basel Convention and the underlying regulations.
- 4. Destruction of High Conservation Value areas .
- 5. Radioactive materials and unbounded asbestos fibres.
- 6. Pornography and/or prostitution.
- 7. Racist and/or anti-democratic media.
- 8. The following products forming a substantial part of a project's primary financed business activities :
  - a) Alcoholic Beverages (except beer and wine);
  - b) Tobacco;
  - c) Weapons and munitions;
  - d) Gambling, casinos and equivalent enterprises; or
  - e) Nuclear energy
- 9. Exclusion criteria for Green projects: investments in fossil fuels, biofuel from sources that deplete carbon pools and compete with food sources, large hydros, transport dedicated to fossil fuel

## 2. Process to select and evaluate eligible projects

FMO follows a two-stage process for the selection of green and reduced inequality projects under the SBF:

- 1. approved projects having received the Green or Reduced Inequality label
- 2. allocate bond funds to approved projects

Requests for the Green and RI labels are made through the Green and RI Labels tab via the internal "Impact Card" approach described hereunder.

### 2a. Green label process

Stage 1 Green deals:

- a) The deal team initially assesses the respective project against FMOs Green definition and Principles and identify the eligible green elements of the transaction. Deal Team should support the Green Label Request with adequate substantiation for the green eligibility of the financed activities. The 'GHG and Green Screen<sup>5</sup>' presents guidance per activity to the level of eligibility ("Green" or "Grey"), and to the type of substantiation that is expected.
- b) In case the activity may be eligible for a Green Label but it is not included in the 'GHG and Green Screen', the deal team needs to contact "DISUS" (FMO "Development Impact

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<sup>5</sup> See Annex 1: GHG Screen represented by eligible green activities



Sustainability team”) to discuss eligibility and next steps. FMO’s development impact consists of 10 team members, of which 2 Sustainability Officers and 8 Evaluation Analysts reporting to the manager DI-SUS.

- c) All deals expected to be eligible for a Green Label need to be reviewed by DISUS. Therefore, all Green label Requests identified as either “Green” or “Grey” in the GHG and Green Screen should be submitted via an internal system, Impact Card
- d) DISUS reviews the Green Label Request and the underlying substantiation of Green eligibility
- e) DISUS validates or requests additional information
- f) The Deal Team will be notified via email regarding the decision and/or if DISUS requires more information
- g) Outcome: Green label request is approved or rejected: These labels can range from 0% to 100%. Deals that have a 0% green label are not eligible for the Green label and deals that have a specified % (>0%) are found eligible for Green based on the specified %
- h) The formal decision on the Green Label request is recorded in an internal system (impact card)

For Project Finance and Financial Institutions (FIs), the Green Label may be assigned fully or partially to a transaction, based on the finance flowing towards underlying eligible elements. Green Label percentages are based on the share of the total FMO investment, which is ex-ante agreed (use of funds), going towards the predefined 'Green activity' or 'Green client'.

For Corporate Finance (general purpose loans), the Green Label percentage is proportionate to the share of company's revenues that are generated with eligible activities.

Figure 2: Green label process

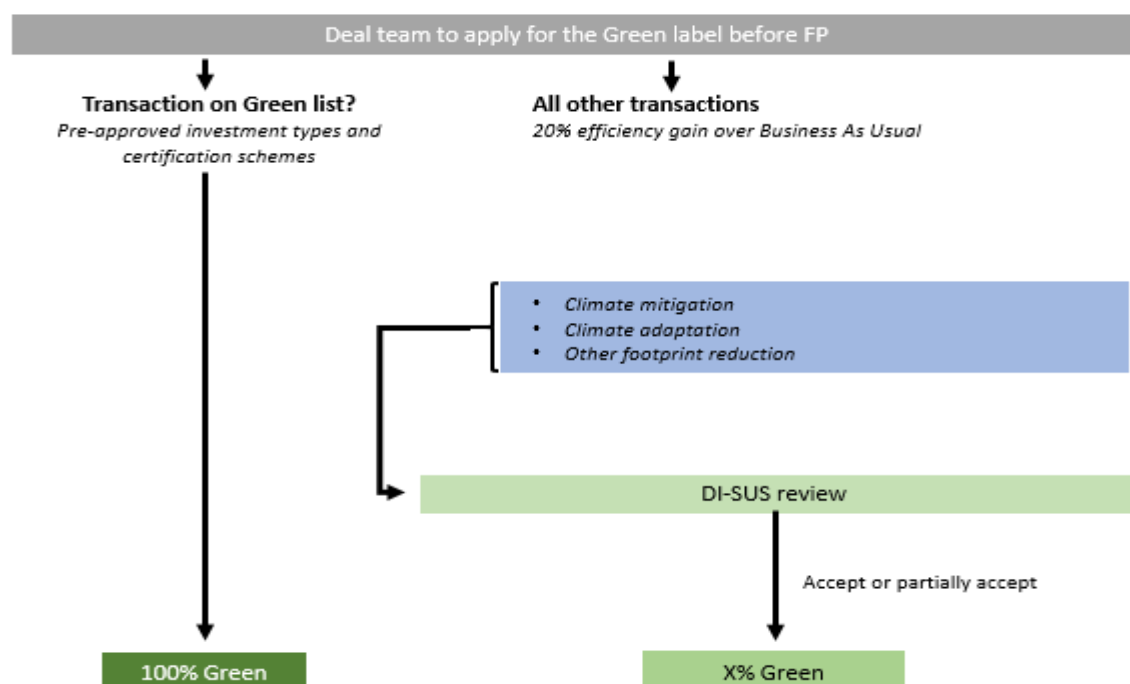
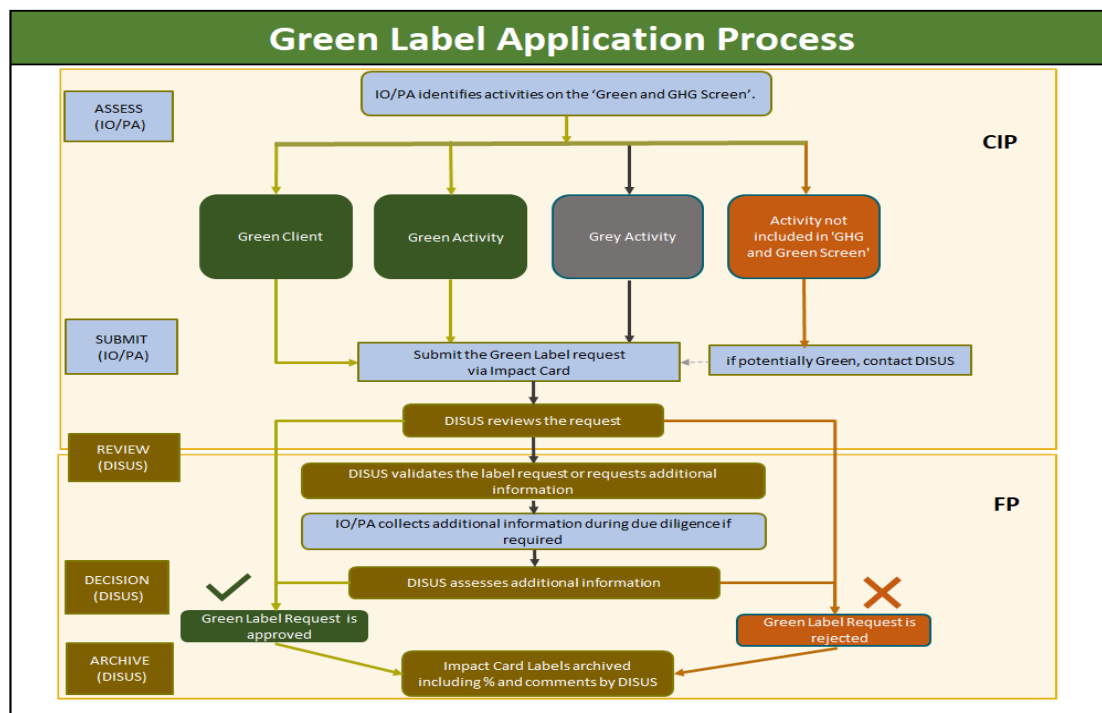


Figure 3: Green label application process



## 2b. Reduced Inequality Process

For the LDC sublabel, a request is not needed if the investment is single-country and the country of impact is the same as the Country of Risk Exposure.

A request for the LDC sublabel is needed if:

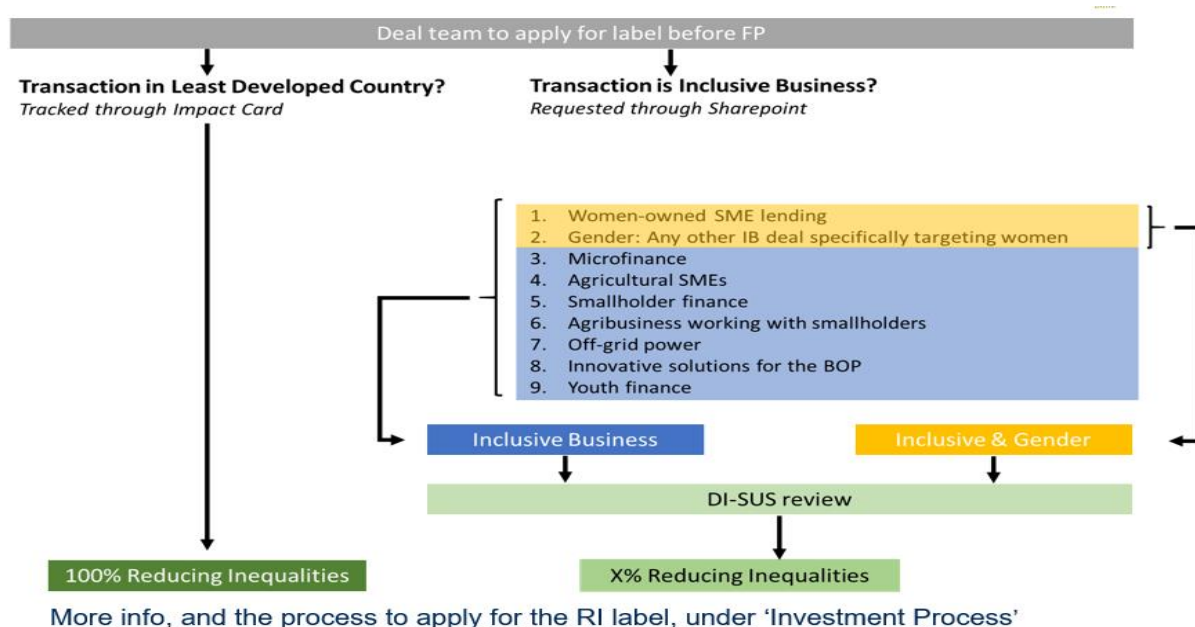
- the investment is multi-country with at least 50% of the investment expected to benefit LDC countries;
- the country of impact is a LDC and is different from the Country of Risk Exposure.
- If a loan provided to an inclusive investment is not fully dedicated to the eligible categories, FMO will use the bonds' proceeds only for the part of loan dedicated to eligible activities.

Stage 1 Reduced Inequality:

- a) The deal team initially assesses the respective project against FMOs Inclusive business categories and definition
- b) Deal Team should support the RI Label Request with adequate substantiation for the inclusive eligibility of the financed activities. Relevant source documents need to be listed
- c) All deals expected to be eligible for an Inclusive Label need to be reviewed by DISUS. Therefore, all Inclusive label Requests should be submitted via an internal system, Impact Card

- d) DISUS reviews the Inclusive Label Request and the underlying substantiation of inclusive eligibility
- e) DISUS validates or requests additional information
- f) The Deal Team will be notified via email regarding the decision and/or if DISUS requires more information
- g) Outcome: Inclusive label request is approved or rejected: These labels can range from 0% to 100%
- h) The formal decision on the RI Label request is recorded in an internal system (impact card)

Figure 4 Reduced Inequality label process



Assessing whether a transaction is in a LDC is obviously straightforward for single-country deals. For deals that have a multi-country coverage, a deal will qualify as an LDC investment if at least half of the funds are expected to flow to LDC countries. For investment in funds, the assessment is based on the investment strategy and the fund's pipeline. The definitions and concepts proposed here are aligned as much as possible with existing international frameworks and definitions such as G20, IFC and FAO.

Stage 2: Allocate bond funds to approved projects.

FMO reviews annually, all the approved and recorded projects under green or reduced inequality category, and selects only those projects for the bond proceeds allocation, that meet the eligibility criteria as defined in section 1. The bond proceeds are then allocated to these eligible projects and reported.

The steps in Appendix 3 highlight the process to select green and reduced inequality projects.

### 3. Management of Proceeds

The net proceeds of any issue under the SBF are held within FMO's Treasury in a sub-portfolio that is linked to FMO's lending operations in the fields of green finance and inclusive finance. As long as the notes issued under the SBF are outstanding, the balance of the sub-portfolio will be reduced by amounts corresponding to the financing or refinancing of eligible projects, or to repay a note issued under the SBF.

Pending allocations, the net proceeds of the notes will be held in FMO's liquidity portfolio and may temporarily be used for different purposes in case of liquidity stress situations. FMO expects the bond proceeds to be fully allocated within 2 years from the issue date.

Projects eligible to be financed with the proceeds of FMO's Green \ Social \ Sustainability Bonds include projects that meet the eligibility criteria described above and are:

- Projects committed after the issuance of the Green \ Social \ Sustainability Bond; or
- Projects committed before the issuance of the Green \ Social \ Sustainability Bond but funded (disbursed) after the issuance of the Bond;

### 4. Impact Measurement & Reporting

#### Reporting

FMO will report to stakeholders on an annual basis in line with the Green Bond and Social Bond reporting templates published during the Green Bond Principles (GBP) 2018 Annual General Shareholder Meeting. FMO is a member of the GBP.

FMO provides investors with an annual newsletter highlighting the following:

#### Allocation reporting

- The progress on allocation of use of proceeds for new and existing projects on a portfolio basis
- The bond allocations are based on outstanding portfolio and 85% of the committed non-disbursed project portfolio, per region, MDB category and subcategory
  - For Green: renewable energy → wind, solar, hydro
  - For Social: microfinance, smallholder finance etc
- A few case studies;

#### Impact reporting

- An estimation of annual GHG emission reduction from direct green investments on a portfolio level
- An estimation of the number of (in)direct jobs supported with our investments on per target group

In addition, FMO has moved towards a fully integrated annual report with financial and non-financial information including GHG emissions. FMO has the integrated report audited by its auditors providing (limited) assurance. FMO has published nine Sustainability Bond newsletters to date on its website: <https://www.fmo.nl/sustainability-bonds>

Additionally, the website provides detailed project information such as client info, the funding objective, and the rationale for funding.

### Impact Measurement

Within FMO, green transactions can either be direct (i.e. FMO finances a project or company directly), or indirect (i.e. FMO participates in a private equity fund targeting green investments, or provides a so-called green credit line to a bank or other financial intermediary). For all direct green investments, FMO calculates, accounts and reports the greenhouse gas (GHG) emission reductions that these investments are estimated to realize, by calculating the difference between the emissions caused by the project and the emissions 'without the project' or 'most likely alternative' scenario. The methodology FMO applies aligns with guidance provided by the following broadly accepted bodies and initiatives: (i) the GHG Protocol (accounting basics on scope 1,2,3 emissions and direct and indirect emission reductions), (ii) the UNFCCC, (iii) the IFI Framework on the Accounting of GHG Reductions. FMO accepts the following source data for its calculations, in order of preference:

- First preference: project-specific data from the Validation Report (or, if not yet available, from the most recent Project Design Document), issued as part of the project registration under the Clean Development Mechanism (CDM).
- Second preference: project-specific validated data from the Gold Standard or voluntary carbon credit scheme (VCS), or another voluntary carbon scheme or standard with an equal assurance level.
- Third preference: for electricity producing projects, compare the project's estimated power production and the project's estimated GHG emission with the emission from the same power production, using a grid emission factor endorsed by the UNFCCC or the IFI Harmonization Initiative on GHG Accounting, or published by the IEA. For other projects, use dedicated methodologies or independent consultant studies.

FMO calculates estimated annual GHG emission reduction based on the sum of the ex-ante estimate of each project financed through direct green investments, in proportion to the Green \ Sustainability Bond allocation. For example, for a EUR 100 million project with project savings of 100,000 tons of CO<sub>2</sub>eq per year, if, total FMO financing is EUR 20 million and total Green \ Sustainability Bond allocation is EUR 10 million (i.e., 10% of total project size), then total attribution to the Green \ Sustainability bond would be 10,000 tons of CO<sub>2</sub>eq per year (i.e., 10% of total GHG savings).

In addition, FMO has developed metrics to measure and capture positive outcomes from inclusive finance funding: the number of (in)direct jobs supported with its investments.

## Compliance Review

Each year, FMO will engage Sustainalytics to review projects funded by the Green \ Social \ Sustainability Bond in order to assess the compliance of projects with the use of proceeds criteria of the bond. Sustainalytics will review a broad sample of projects from the total allocated projects in order to determine whether or not they meet the use of proceeds criteria defined in the framework. Sustainalytics will provide a report of the evaluation, which FMO may plan to disclose publicly. In an unlikely event that a project did not meet the use of proceed criteria, FMO would reallocate the bond funds to a different project that is aligned with the criteria.

## Annex 1 Eligible green activities

### 1a climate change mitigation

1. Renewable Energy	
<b>1.1 Electricity Generation</b>	• Wind power
	• Realization of geothermal power generation - no net positive impact established yet
	• Realization of geothermal power generation (<100g CO <sub>2</sub> /kWh) - net positive impact needs to be established
	• Solar power (concentrated solar power, photovoltaic power)
	• Biomass or biogas power that does not decrease biomass and soil carbon pools (only if net emission reductions can be demonstrated)
	• Realization of 2nd generation waste biomass or biogas power generation (ie. From agri waste or landfills) because it does not decrease biomass and soil carbon pools (preferably with demonstrated expected annual GHG avoidance)
	• Ocean power (wave, tidal, ocean currents, salt gradient, etc.)
<b>1.2 Heat Production or other renewable energy application</b>	• Run-off river hydro power generation without storage
	• Solar water heating and other thermal applications of solar power in all sectors
	• Thermal applications of geothermal power in all sectors (<100g CO <sub>2</sub> /kWh)
	• Wind-driven pumping systems or similar
<b>1.3 Transmission systems, greenfield</b>	• Thermal applications of sustainably produced bioenergy in all sectors, incl. efficient, improved biomass stoves (excluding bioenergy derived from sources that deplete terrestrial carbon pools or compete with food sources)
	• New transmission systems (lines, substations) or new systems (e.g., new information and communication technology, storage facility, etc.) and mini-grid to facilitate the integration of renewable energy sources into the grid,.
	• Renewable energy power plant retrofits
	• Improving existing systems to facilitate the integration of renewable energy sources into grid

## 2. Lower-carbon and efficient energy generation

### 2.1 Transmission and distribution systems

- Retrofit of transmission lines or substations and/or distribution systems to reduce energy use and/or technical losses, excluding capacity expansion

### 2.2 Power Plants

- Waste heat recovery improvements.
- Energy-efficiency improvement in existing bioenergy plants

## 3. Energy efficiency

### 3.1 Brownfield energy efficiency in industry

- Industrial energy-efficiency improvements through the installation of more efficient equipment, changes in processes, reduction of heat losses and/or increased waste heat recovery (excluding investments in fossil fuel technology)
- Installation of co-generation plants that generate electricity in addition to providing heating/cooling (excluding investments in fossil fuel technology)
- More efficient facility replacement of an older facility (old facility retired) (excluding investments in fossil fuel technology)

### 3.2 Brownfield energy efficiency in commercial, public and residential sectors (buildings)

- Energy-efficiency improvement in lighting, appliances and equipment
- Substitution of existing heating/cooling systems for buildings by co/generation plants that generate electricity in addition to providing heating/cooling (excluding investments in fossil fuel technology)
- Retrofit of existing buildings: Architectural or building changes that enable reduction of energy consumption

### 3.3 Brownfield energy efficiency in public services

- Energy-efficiency improvement in utilities and public services through the installation of more efficient lighting or equipment (excluding investments in fossil fuel technology)
- Rehabilitation of district heating systems
- Utility heat loss reduction and/or increased waste heat recovery
- Improvement in utility scale energy efficiency through efficient energy use, and loss reduction (excluding investments in fossil fuel technology)

### 3.4 Vehicle energy efficiency fleet retrofit

- Existing vehicles, rail or boat fleet retrofit or replacement (including the use of electric or hydrogen technologies, etc.)

### 3.5 Greenfield energy efficiency in commercial and residential sectors (buildings)

- Use of highly efficient architectural designs, energy efficiency appliances and equipment, and building techniques that reduce building energy consumption, exceeding available standards and complying with high energy efficiency certification or rating schemes
- Use of highly efficient architectural designs, energy efficiency appliances and equipment, and building techniques that reduce building energy consumption, exceeding available standards and complying with high energy efficiency certification or rating schemes

### 3.6 Green Buildings

- Green Buildings certified by LEED (only LEED Gold or Platinum certification qualifies) or IFCs EDGE Tool
- Green Buildings, not yet certified or certified under other scheme

### 3.7 Energy Audits

- Energy audits to energy end-users, including industries, buildings, and transport systems

## 4. Agriculture, forestry and landuse

### 4.1 Agriculture

- Reduction in energy use in traction (e.g. efficient tillage), irrigation, and other agriculture processes



	<ul style="list-style-type: none"> <li>• Agriculture projects that do not deplete and/or improve existing carbon pools (Reduction in fertilizer use, rangeland management, collection and use of bagasse, rice husks, or other agricultural waste, low tillage techniques that increase carbon contents of soil, rehabilitation of degraded lands, etc.)</li> <li>• Projects or companies that lead to expanded sustainable/green output in line with one of the following certification schemes (company or project needs to be or become certified): UTZ Certified, Roundtable on Sustainable Biomaterials (RSB), The Intercultural Federation of Organic Agriculture Movements (IFOAM), Proterra, Soil Association or Bonsucro.</li> </ul>
<b>4.2 Afforestation and reforestation, and biosphere conservation</b>	<ul style="list-style-type: none"> <li>• Sustainable forest management activities that increase carbon stocks or reduce the impact of forestry activities</li> <li>• Biosphere conservation projects (including payments for ecosystem services) targeting reducing emissions from the deforestation or degradation of ecosystems</li> <li>• FSC and/or PEFC Certification</li> <li>• Rainforest Alliance Certification</li> </ul>
<b>4.3 Livestock</b>	<ul style="list-style-type: none"> <li>• Livestock projects that reduce methane or other GHG emissions (manure management with biodigestors, etc.)</li> </ul>
<b>4.4 Biofuels</b>	<ul style="list-style-type: none"> <li>• Production of biofuels (including biodiesel and bioethanol) (excluding from sources that deplete carbon pools or that compete with food sources)</li> </ul>
<b>5. Non-energy GHG reductions</b>	
<b>5.3 Air conditioning and refrigeration</b>	<ul style="list-style-type: none"> <li>• Retrofit of existing industrial, commercial and residential infrastructure to switch to cooling agent with lower global warming potential</li> </ul>
<b>5.4 Industrial processes</b>	<ul style="list-style-type: none"> <li>• Reduction in GHG emissions resulting from industrial process improvements and cleaner production (e.g. cement, chemical), excluding carbon capture and storage (excluding investments in fossil fuel technology)</li> <li>• Reduction in GHG emissions resulting from industrial process improvements and cleaner production (e.g. cement, chemical) demonstrated by &gt;20% GHG efficiency or resource efficiency improvement (excluding investments in fossil fuel technology)</li> </ul>
<b>6. Waste and wastewater</b>	
<b>6.1 Wastewater</b>	<ul style="list-style-type: none"> <li>• Treatment of wastewater if not a compliance requirement as part of an industrial process (only if net emission reductions can be demonstrated).</li> <li>• Waste management and waste-to-energy projects that reduce methane emissions and generate energy (e.g. incineration of waste, landfill gas capture, and landfill gas combustion)</li> </ul>
<b>6.2 Waste</b>	<ul style="list-style-type: none"> <li>• Waste-recycling projects that recover or reuse materials and waste as inputs into new products or as a resource (only if net emission reductions can be demonstrated).</li> <li>• Sanitation projects with proper waste treatment if it replaces open defecation.</li> </ul>
<b>7. Transport</b>	
<b>7.1 Urban transport modal change</b>	<ul style="list-style-type: none"> <li>• Urban mass transit</li> <li>• Non-motorized transport (bicycles and pedestrian mobility)</li> </ul>

<b>7.2 Transport oriented urban development</b>	<ul style="list-style-type: none"> <li>Integration of transport and urban development planning (dense development, multiple land-use, walking communities, transit connectivity, etc.), leading to a reduction in the use of passenger cars</li> </ul>
<b>7.3 Inter-urban transport</b>	<ul style="list-style-type: none"> <li>Railway transport ensuring a modal shift of freight and/or passenger transport from road to rail (improvement of existing lines or construction of new lines) - no GHG avoidance estimate available (excluding transport)</li> <li>Waterways transport ensuring a modal shift of freight and/or passenger transport from road to waterways (improvement of existing infrastructure or construction of new infrastructure) - no GHG avoidance estimate available</li> <li>Railway or Waterways transport ensuring a modal shift of freight and/or passenger transport from road to rail or water (improvement of existing lines or construction of new lines) if 3rd party verified GHG avoidance estimated aligning with the IFI harmonized GHG accounting approach for Transport Modal Shift</li> </ul>
<b>8. Low-carbon technologies</b>	
<b>8.1 Products or equipment</b>	<ul style="list-style-type: none"> <li>Projects producing and/or distributing components, equipment or infrastructure dedicated for the renewable and energy efficiency sectors</li> </ul>
<b>8.2 R&amp;D</b>	<ul style="list-style-type: none"> <li>Research and development of renewable energy or energy efficiency technologies</li> </ul>
<b>9. Cross-cutting issues</b>	
<b>9.1 Support to national, regional or local policy, fully or partially dedicated to climate change policy or action</b>	<ul style="list-style-type: none"> <li>Mitigation national, sectorial or territorial policies/planning/action plan policy/planning/institutions</li> <li>Energy sector policies and regulations (energy efficiency standards or certification schemes; energy efficiency procurement schemes; renewable energy policies)</li> <li>Systems for monitoring the emissions of greenhouse gases</li> <li>Education, training, capacity building and awareness raising on climate change mitigation/sustainable energy/sustainable transport; mitigation research</li> <li>Other policy and regulatory activities, including those in non-energy sectors, leading to climate change mitigation or mainstreaming of climate action</li> </ul>
<b>9.2 Other activities with net greenhouse gas reduction</b>	<ul style="list-style-type: none"> <li>Any other activity not included in this list for which the results of an ex-ante greenhouse gas accounting (undertaken according to commonly agreed methodologies) show emission reductions</li> </ul>
<b>9.3 Financing instruments</b>	<ul style="list-style-type: none"> <li>Carbon Markets and finance (purchase, sale, trading, financing and other technical assistance. Includes all activities related to compliance-grade carbon assets and mechanisms, such as CDM, JI, AAUs, as well as well-established voluntary carbon standards like the VCS or the Gold Standard.</li> <li>Greenline financing for purely renewable energy and/or water/material/pollution/energy efficiency &gt;20% improvement (re)-financed through a financial intermediary (earmarked with use-of-funds clause)</li> <li>Greenline financing for <b>non-renewable</b> energy and <b>non-energy</b> efficiency financing through new financial intermediaries or similar (e.g. earmarked lines of credit; lines for microfinance institutions, cooperatives, etc.) (earmarked with use-of-funds clause)</li> <li>Greenline (co)-financing for renewable energy and energy efficiency (re)-financing through financial intermediaries that are existing Green Partners (Green for Growth Fund (GfGF) and Climate Global Partnership Fund (CGPF)) (earmarked with use-of-funds clause)</li> </ul>

## 1b Eligible activities under climate change adaptation

### 10. Climate Change Adaptation

#### 10.1 Activities Addressing Climate Vulnerability

- Activity or technology that addresses the local climate vulnerability by strengthening the resilience of communities, goods, or ecosystems to climate change (see the 'Adaptation Examples' tab or the MDB Climate Finance Report for examples)

## 1c Eligible activities under Other Footprint

#### 11.1 Biodiversity

- Financed activity is either contributing to conserving/increasing biodiversity, or the core business/aim of the project is to conserve or increase biodiversity
- The transition to, or maintenance of, silvo-pastoral systems, if no conversion of natural land is involved.

#### 11.2 Pollution mitigation

- Financed activity is either contributing to pollution mitigation (beyond regulatory compliance) or the core business/aim of the project is to mitigate pollution (beyond regulatory compliance)
- Waste water treatment as the core business of the project (not part of specific industrial process)
- Company's core business is cleaning up hazardous waste sites (ie. soil remediation and mine rehabilitation)

#### 11.3 Conservation of natural resources

- Financed activity is contributing to or the core aim of the project is to conserve natural resources (ie land, water, forests, materials)
- Recycling /solid waste collection and treatment as the core business of the project
- Company's core business is the remanufacture of products (or extend their lifecycle in other ways), servitisation or complete circular economy business models

## Annex 2 Least Developed Countries (LDCs) list 2017



**United Nations**  
**Committee for Development Policy**  
Development Policy and Analysis Division  
Department of Economic and Social Affairs

### List of Least Developed Countries (as of June 2017)\*, \*\*

Afghanistan (1971)	Malawi (1971)
Angola <sup>1</sup> (1994)	Mali (1971)
Bangladesh (1975)	Mauritania (1986)
Benin (1971)	Mozambique (1988)
Bhutan (1971)	Myanmar (1987)
Burkina Faso (1971)	Nepal (1971)
Burundi (1971)	Niger (1971)
Cambodia (1991)	Rwanda (1971)
Central African Republic (1975)	Sao Tome and Principe (1982)
Chad (1971)	Senegal (2000)
Comoros (1977)	Sierra Leone (1982)
Democratic Republic of the Congo (1991)	Solomon Islands (1991)
Djibouti (1982)	Somalia (1971)
Eritrea (1994)	South Sudan (2012)
Ethiopia (1971)	Sudan (1971)
Gambia (1975)	Timor-Leste (2003)
Guinea (1971)	Togo (1982)
Guinea-Bissau (1981)	Tuvalu (1986)
Haiti (1971)	Uganda (1971)
Kiribati (1986)	United Republic of Tanzania (1971)
Lao People's Democratic Republic (1971)	Vanuatu <sup>2</sup> (1985)
Lesotho (1971)	Yemen (1971)
Liberia (1990)	Zambia (1991)
Madagascar (1991)	

\* The list will be updated when new decisions become available.

\*\* Year of inclusion on the list in brackets.

<sup>1</sup> General Assembly resolution A/RES/70/253 adopted on 12 February 2016, decided that Angola will graduate five years after the adoption of the resolution, i.e. on 12 February 2021.

<sup>2</sup> General Assembly resolution A/RES/68/18 adopted on 4 December 2013, decided that Vanuatu will graduate four years after the adoption of the resolution on 4 December 2017. General Assembly resolution A/RES/70/78 adopted on 9 December 2015, decided to extend the preparatory period before graduation for Vanuatu by three years, until 4 December 2020, due to the unique disruption caused to the economic and social progress of Vanuatu by Cyclone Pam.

[https://www.un.org/development/desa/dpad/wp-content/uploads/sites/45/publication/ldc\\_list.pdf](https://www.un.org/development/desa/dpad/wp-content/uploads/sites/45/publication/ldc_list.pdf)

### Annex 3 Earmarking green and reduced inequality projects

Treasury officer	Green and inclusive label overview\report prepared by DISUS to identify potential eligible projects. Provides Director TR, Director RM and Manager SUS with the report	<b>Frequency</b> Semi-annually  <b>Output</b> Report on eligible green and social projects
Director Treasury	Organizes a meeting together with DISUS, Director RM (and relevant Front-Office Directors, representatives). Determines based on report which green and social projects are eligible for earmarking for the respective bonds to be issued under the SBF	<b>Input</b> · Report on eligible green and inclusive disbursements  <b>Output</b> · List of facility id's to be 'earmarked' for the bonds issued under the SBF
Treasury Officer	Sends list of facility id's to be 'earmarked' together with the related SDG identifier \ ISIN code to Mid-Office	<b>Input</b> · List of facility id's to be 'earmarked' for the respective Bond  <b>Output</b> · Identification of eligible assets in ACBS and FIA
MO Officer	Enters the ISIN code in ACBS and FIA? for the disbursements to eligible clients/projects (tag isin code sus bond or green\social to facility id).	
Treasury officer	Provides report with 'earmarked' disbursements in ACBS to ALCO for information; 1073 report_sus bond portfolio Prepares newsletter with 'earmarked' projects for investors together with Corporate Communications on a annual basis. Sends annual newsletter to investors.	<b>Output</b> · Report for ALCO on 'earmarked' projects  · Semi-annual newsletter for investors
CC Officer	Ensures project disclosure for 'earmarked' projects is published on the external website in line with FMO's disclosure policy. Prepares a planning with actions for Treasury with regards to the drafting the newsletter. Publishes the newsletter on the external website: <a href="https://www.fmo.nl/susbonds">https://www.fmo.nl/susbonds</a>	