

REVIEW OF FMO'S SUSTAINABILITY BOND PROJECTS

March 10th, 2017

Introduction

In April 2015, FMO has issued its second Sustainability Bond underlining FMO's strategic commitment to the Green and Sustainability Bond market. The proceeds of the Sustainability Bond support the financing of green and inclusive finance projects according to FMO's Sustainability Bond Framework¹, which is aligned with FMO's long term strategy of fostering inclusive and green growth.

Further, FMO states that all green projects should be value added, and go beyond complying with regulatory standards in order to initiate and/or enable a market shift.

Scope of work

In 2017, FMO has engaged Sustainalytics to review its current Sustainability Bond projects with the aim of assessing whether the new projects selected by FMO for the bond are compliant with the eligibility criteria (Appendix 2) defined in FMO's Sustainability Bond Framework. Sustainalytics reviewed these projects selected under the Climate Change Mitigation Criteria and the Inclusive Finance Criteria.

A similar compliance review for Sustainability Bond projects previously implemented has been performed by Sustainalytics in 2015 and 2016².

¹ FMO's Sustainability Bond Framework has been published in March 2015, and is available for download on FMO's website: <https://www.fmo.nl/sustainability-bonds>

² Sustainalytics' 2015 Bond Projects Review and 2016 Bond Projects Review are available for download on FMO's website: <https://www.fmo.nl/sustainability-bonds>

FMO provided Sustainalytics a full list of projects for review, including detailed descriptions of each project, their Environmental & Social Risk Assessment Profile, and the associated environmental benefits. In addition to reviewing the information received, the work undertaken as part of this review included conversations with relevant FMO's employees and review of relevant documentation to confirm the alignment with the Sustainability Bond Framework.

Sustainalytics made all efforts to ensure the highest quality and rigor during its assessment process and enlisted its Sustainability Bonds Review Committee to provide oversight over the review.

Assessment

In 2017, 17 new projects were assessed to verify compliance with the eligibility criteria defined in FMO's Sustainability Bond Framework.

The outcome of this assessment is as follows:

- All of the Climate Change Mitigation projects were assessed and all of them meet the eligibility criteria.
- All of the Inclusive Finance projects were assessed and all of them meet the eligibility criteria.
- It is reasonable to assume that all the projects meet the exclusionary criteria because FMO has detailed Appraisal and Approval, and Know Your Customer policies and procedures that ensure that exclusionary criteria is met before selecting its clients. An exclusionary criteria screening has also been performed by Sustainalytics in the scope of this review. No evidence of involvement with controversial activities has been detected for the projects reviewed.

Appendix 1 provides details of the assessment.

Conclusion

Based on the assessment of projects and review procedures, nothing has come to Sustainalytics' attention that causes us to believe that, in all material respects, the reviewed bond projects are not in alignment with the eligibility criteria defined in FMO's Sustainability Bond Framework.

Appendix 1: Assessment Details

Climate Change Mitigation

	Project Name	Country	Use of Proceeds	MDB Sector	MDB Sub-Sector	E & S Risk Assessment Completed?	Eligibility Criteria Compliant?
1	Access Uganda Solar Ltd	Uganda	Solar PV production	4. Renewable Energy	4.1. Electricity generation, greenfield projects - Solar Power	Yes	Yes
2	EMS Africa Nyamwamba Ltd	Uganda	Hydro Power Project	4. Renewable Energy	4.1. Electricity generation, greenfield projects - Hydro Power	Yes	Yes
3	Banco BAC San Jose S.A.	Costa Rica	Renewable Energy and Energy Efficiency Lending Program	9.4 Financing instruments	9.4.2 Renewable energy and energy efficiency financing through financial intermediaries or similar	Yes	Yes
4	Banco De La Produccion S.A.	Ecuador	Renewable Energy and Energy Efficiency Lending Program	9.4 Financing instruments	9.4.2 Renewable energy and energy efficiency financing through financial intermediaries or similar	Yes	Yes
5	Elz Saglik Yatirim A.S.	Turkey	Construction of green buildings	2. Demand-side, greenfield energy efficiency	2.1 Construction of new buildings	Yes	Yes
6	Heksagon Kati Atik S.A	Turkey	Waste management	7. Waste and wastewater	7.1.1 Solid waste management that reduce methane emissions (e.g. incineration of waste, landfill gas capture, and landfill gas combustion)	Yes	Yes
7	Lubilia Kawembe Hydro Limited	Uganda	Hydro Power Project	4. Renewable Energy	4.1. Electricity generation, greenfield projects - Hydro Power	Yes	Yes
8	Mabani Seven Company Ltd	Ghana	Construction of green buildings	2. Demand-side, greenfield energy efficiency	2.1 Construction of new buildings	Yes	Yes
9	Mecanismos de Energia Renovable S.A.	Honduras	Solar PV production	4. Renewable Energy	4.1. Electricity generation, greenfield projects - Solar Power	Yes	Yes
10	Mohammed Enterprises Tanzania Limited Group	Tanzania	Non-energy greenhouse gas reductions, cleaner production	6. Agriculture, forestry and land use 9. Cross sector activities	6.4.1 Agriculture projects that do not deplete and/or improve existing carbon pools 9.3 Supply chain	Yes	Yes

11	Odeabank A.S.	Turkey	Renewable Energy Lending Program	9.4 Financing instruments	9.4.2 Renewable energy and energy efficiency financing through financial intermediaries or similar	Yes	Yes
12	Tororo Solar North Limited	Uganda	Solar PV production	4. Renewable Energy	4.1. Electricity generation, greenfield projects - Solar Power	Yes	Yes
13	Usher Eco Power Ltd	India	Waste management	7. Waste and wastewater	7.1.3 Waste recycling projects that recover or reuse materials and waste as inputs into new products or as a resource	Yes	Yes
14	Yes Bank Limited	India	Solar and Wind Power Projects	4. Renewable Energy	4.1. Electricity generation, greenfield projects - Solar Power	Yes	Yes

*FMO has demonstrated net emission reduction for all hydro power projects

Inclusive Finance

	Project name	Country	Project Type	Year of Last MFI Review	Average Loan Size Disbursed by MFI (USD)	Eligibility Criteria Compliant?
1	CJSC Finca Bank	Kyrgyzstan	MFI	Dec-17	777	Yes
2	Financiera Confianza S.A.A.	Peru	MFI	Dec-14	1,633	Yes
3	Kompanion Bank CJSC	Kyrgyzstan	MFI	Jul-16	635	Yes

APPENDIX 2: Eligible activities

2a: Eligible activities under climate change mitigation

Energy efficiency

Commercial and residential buildings	<ul style="list-style-type: none"> • Energy-efficiency improvement in lighting, appliances and equipment • Substitution of existing heating/cooling systems for buildings by cogeneration plants that generate electricity in addition to providing heating/cooling • Retrofit of existing buildings: Architectural or building changes that enable reducing energy consumption • Waste heat recovery improvements
Public services	<ul style="list-style-type: none"> • Energy-efficiency improvement in utilities and public services through the installation of more efficient lighting or equipment • 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.
Agriculture	<ul style="list-style-type: none"> • Reduction in energy use in traction (e.g. efficient tillage), irrigation, and other agriculture processes
Industry	<ul style="list-style-type: none"> • Industrial energy-efficiency improvements through the installation of more efficient equipment, changes in processes, reduction of heat losses and/or increased waste heat recovery • Installation of cogeneration plants • More efficient facility replacement of an older facility (old facility retired)
Transmission and distribution systems	<ul style="list-style-type: none"> • Retrofit of transmission lines or substations to reduce energy use and/or technical losses, excluding capacity expansion • Retrofit of distribution systems to reduce energy use and/or technical losses, excluding capacity expansion • Improving existing systems to facilitate the integration of renewable energy sources into the grid
Power plants	<ul style="list-style-type: none"> • Renewable energy power plant retrofits • Energy-efficiency improvement in existing thermal power plant • Thermal power plant retrofit to fuel switch from a more GHG-intensive fuel to a different, less GHG-intensive fuel type • Waste heat recovery improvements
Construction of new buildings	<ul style="list-style-type: none"> • Use of highly efficient architectural designs or building techniques that enable reducing energy consumption for heating and air conditioning, exceeding available standards and complying with high energy efficiency certification or rating schemes

Renewable Energy

Electricity generation	<ul style="list-style-type: none"> • Wind power • Geothermal power, if net emission can be demonstrated • Solar power (concentrated solar power, photovoltaic power) • Biomass or biogas power that does not decrease biomass and soil carbon pools • Ocean power (wave, tidal, ocean currents, salt gradient, etc.) • Hydropower plants only if net emission reduction can be demonstrated
Transmission systems, greenfield	<ul style="list-style-type: none"> • New transmission systems (lines, substations) or new systems (e.g., new information and communication technology, storage facility, etc.) to facilitate the integration of renewable energy sources into the grid
Heat production or greenfield	<ul style="list-style-type: none"> • Solar water heating and other thermal applications of solar power in all sectors • Thermal applications of geothermal power in all sectors • Thermal applications of sustainably-produced bioenergy in all sectors, including

Transport

Vehicle energy efficiency fleet retrofit	<ul style="list-style-type: none"> • Existing vehicles, rail or boat fleet retrofit or replacement (including the use of lower-carbon fuels, electric or hydrogen technologies, etc.)
Urban transport modal change	<ul style="list-style-type: none"> • Urban mass transit • Non-motorized transport (bicycles and pedestrian mobility)
Urban development	<ul style="list-style-type: none"> • 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 • Transport demand management measures to reduce GHG emissions (e.g., speed limits, high-occupancy vehicle lanes, congestion charging/road pricing, parking management, restriction or auctioning of license plates, car-free city areas, low-emission zones)
Inter-urban transport and freight transport	<ul style="list-style-type: none"> • Improvement of general transport logistics to increase energy efficiency of infrastructure and transport, e.g. reduction of empty running • 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) • 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)

Agriculture, forestry and land use

Afforestation (plantations) on non-forested land	<ul style="list-style-type: none"> • Afforestation (plantations) on non-forested land • Reforestation on previously forested land
Reducing emissions from the deforestation or	<ul style="list-style-type: none"> • Biosphere conservation projects (including payments for ecosystem services)

degradation of ecosystems	
Sustainable forest management	<ul style="list-style-type: none"> • Forest management activities that increase carbon stocks or reduce the impact of forestry activities
Agriculture	<ul style="list-style-type: none"> • 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.)
Livestock	<ul style="list-style-type: none"> • Livestock projects that reduce methane or other GHG emissions (manure management with biodigestors, etc.)

Waste and wastewater

Waste and wastewater	<ul style="list-style-type: none"> • Solid waste management that reduce methane emissions (e.g. incineration of waste, landfill gas capture, and landfill gas combustion) • Treatment of wastewater if not a compliance requirement (e.g. performance standard or safeguard) as part of a larger project • Waste recycling projects that recover or reuse materials and waste as inputs into new products or as a resource
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Non-energy GHG reductions

Industrial processes	<ul style="list-style-type: none"> • Reduction in GHG emissions resulting from industrial process improvements and cleaner production (e.g. cement, chemical)
Air conditioning and cooling	<ul style="list-style-type: none"> • Retrofit of existing industrial, commercial and residential infrastructure to switch to cooling agent with lower global warming potential
Fugitive emissions and carbon capture	<ul style="list-style-type: none"> • Carbon capture and storage projects (including enhanced oil recovery) • Reduction of gas flaring or methane fugitive emissions in the oil and gas industry • Coal mine methane capture

Cross-sector activities

Policy and regulation	<ul style="list-style-type: none"> • National mitigation policy/planning/institutions • Energy sector policies and regulations (energy efficiency standards or certification schemes; energy efficiency procurement schemes; renewable energy policies) • Systems for monitoring the emissions of greenhouse gases • Efficient pricing of fuels and electricity (subsidy rationalization, efficient end-user tariffs, and efficient regulations on electricity generation, transmission, or distribution)
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	<ul style="list-style-type: none"> • Education, training, capacity building and awareness raising on climate change mitigation/sustainable energy/sustainable transport; mitigation research
Energy audits	<ul style="list-style-type: none"> • Energy audits to energy end-users, including industries, buildings, and transport systems
Supply chain	<ul style="list-style-type: none"> • Improvements in energy efficiency and GHG reductions in existing product supply chains
Financing instruments	<ul style="list-style-type: none"> • Carbon markets and finance (purchase, sale, trading, financing, guarantee and other technical assistance). Includes all activities related to compliance-grade carbon assets and mechanisms, such as Clean Development Mechanism (CDM), Joint Implementation (JI), Assigned Amount Units (AAUs), as well as well-established voluntary carbon standards like the Verified Carbon Standard (VCS) or the Gold Standard. • Renewable energy and energy efficiency financing through financial intermediaries or similar (e.g. earmarked lines of credit; lines for microfinance institutions, cooperatives, etc.)
Low-carbon technologies	<ul style="list-style-type: none"> • Research and development of renewable energy or energy efficiency technologies • Manufacture of renewable energy and energy efficiency technologies and products
Activities with greenhouse gas accounting	<ul style="list-style-type: none"> • 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 that are higher than a commonly agreed threshold

2b: Eligible activities under inclusive finance

FMO provides funds to microfinance institutions (MFIs) to provide loans to micro-enterprises. FMO plans to use the Sustainability Bond proceeds to fund such MFIs. FMO undertakes a detailed due diligence exercise, including an assessment of ESG related risks, before selecting a MFI to receive funding from FMO. Projects are classified as microfinance if they meet the following criteria:

- a) The end-client should meet two of three criteria to be eligible for the Sustainability Bond: 1) number of employees <10; 2) turnover <USD 100,000; 3) total assets <USD 100,000; or
- b) If data mentioned in point 'a' is not available, then the loan size should be < USD 10,000.

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

2c: Exclusionary Criteria

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

1. Forced labour³ or child labour⁴.
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
 - 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. Destruction⁵ of High Conservation Value areas⁶.
5. Radioactive materials⁷ 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 activities⁸:
 - a) Alcoholic Beverages (except beer and wine);
 - b) Tobacco;
 - c) Weapons and munitions;
 - d) Gambling, casinos and equivalent enterprises; or
 - e) Nuclear energy.

³ Forced labour means all work or service, not voluntarily performed, that is extracted from an individual under threat of force of penalty as defined by ILO conventions.

⁴ Persons may only be employed if they are at least 14 years old, as defined in the ILO Fundamental Human Rights Conventions (Minimum Age Convention C138, Art. 2), unless local legislation specifies compulsory school attendance or the minimum age for working. In such cases the higher age shall apply.

⁵ Destruction means the (1) elimination or severe diminution of the integrity of an area caused by a major, long-term change in land or water use or (2) modification of a habitat in such a way that the area's ability to maintain its role is lost.

⁶ High Conservation Value (HCV) areas are defined as natural habitats where these values are considered to be of outstanding significance or critical importance

⁷ This does not apply to the purchase of medical equipment, quality control (measurement) equipment or any other equipment where the radioactive source is understood to be trivial and/or adequately shielded.

⁸ For companies, 'substantial' means more than 10% of their consolidated balance sheets or earnings. For financial institutions and investment funds, 'substantial' means more than 10% of their underlying portfolio volumes.

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