DENTONS

How are sustainable finance instruments being used to finance sustainability or impact?

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As part of our ESG global webinar series, which is focused on bringing General Counsel and in-house legal teams practical insights on some of the biggest ESG topics, over 40 senior legal attendees joined us recently for a discussion on financing sustainability or impact. Here are the key takeaways.

Navigating ESG policies and regulations to drive opportunities and reach sustainable outcomes

Vivien Teu, Partner, outlined that we are seeing a significant increase in government and central bank policies on climate and sustainability, regulations on green disclosures of corporates and financial institutions, and regulations and international standards on specific ESG issues. This presents both risk (climate-related, ESG/sustainability performance and greenwashing) and opportunity (transition, development finance etc.) for organizations looking to meet stakeholder and societal expectations. Sustainable finance addresses sustainability risks through finance to create long-term value (financial and non-financial impacts) and should be the starting point for investment and financing decisions. We are now seeing the current landscape start to shape products with this objective in mind. Let us now take a look at some of these products.

Impact investing innovation and fund manager selection criteria

Owen McLennan, Partner, highlighted an excellent example of an innovative structure focused on positive impact. Owen recently advised on the UK Foreign Commonwealth and Development Office (FCDO) investment in the Green Guarantee Company (GCC), the world's first Green Guarantee Company. The purpose of this investment is to use guarantees to help borrowers and developing countries improve their credit ratings to enable them to access global capital markets, with the potential to attract and mobilize institutional and private investors for green transition. This will lead to prioritizing green infrastructure, renewable resources, alternative energy, and clean transportation. It will also help issuers build their capacity and the quality of reporting on the climate impact of guaranteed green bonds and loans.

In this context of the broader impact investing landscape, what should investors look for when choosing an Impact Investing fund manager? Due to the high degree of scrutiny from public bodies and the general public, the regulatory profile and track record of the fund manager are critical. Impact Investing is novel

and therefore it is also important the investment manager understands the needs and interests of the investor. When considering a strategy with an investment manager, it is essential to have transparency on costs. Impact Investors should continue to manage usual risks around limited liability, the intended investment exposure and expected risk-return objectives, and ensure they are aligned with their investment objective and strategy for allocating the fund.

Global momentum grows for blended finance

Since COP28, we have seen Multilateral Development Banks (MDBs) committing to sustainable finance and using climate and nature-linked financial instruments. Ruben Eduardo Lujan, Partner, explained that a global task force led by the Inter-American Development Bank (IDB) and the U.S. International Development Finance Corporation (DFC) has been established to scale climate and nature-linked financing and credit enhancement instruments. Our recent work on the Ecuador debt-for-nature swap transaction will serve as a model for the development of these types of products at the public and private sector level.

The goal of this transaction was to create a financial mechanism that would allow Ecuador to dedicate significant funds to the conservation and protection of the Galápagos Islands and the ecosystems located in the marine reserves. This transaction was the largest debt-for-nature swap transaction to date in the world, releasing $450 million for the preservation and conservation of the Galápagos Islands. It involved exchanging sovereign debt for new debt with a longer maturity and a lower interest rate. This method differs from exchanging sovereign bonds or linked bonds because it involves real commitments overseen by independently recognized organization. This model is suitable for situations where organizations are keen to refinance or re-structure their current debt (without incurring additional debt), while also achieving their ESG goals.

A need for organizations and funders to get ahead of opportunities

There is a growing momentum for using innovative structures and instruments to achieve sustainability goals. The area of sustainable finance and impact investing is broad and collaborative, with tremendous interest and opportunities for blended finance. As such, organizations and funders should work strategically to get ahead of these opportunities. The panel also advised that it is worth reviewing the organization’s investment committee procedures and protocols to make sure the sustainability of transactions and impact have been considered.