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Second Party Opinion

Banco ABC Brasil S.A.'s Sustainable Finance Framework

Aug. 28, 2023

Editor's note: This SPO report is based on S&P Global Ratings' "[Analytical Approach: Second Party Opinions and Transaction Evaluations](#)" dated Dec. 7, 2022, which was partly superseded by S&P Global Ratings' "[Analytical Approach: Second Party Opinions: Use of Proceeds](#)," dated Jul. 27, 2023, following the launch of our integrated use-of-proceeds SPOs. For more information on how we are managing the post-launch grace period, please see [S&P Global Ratings To Launch Integrated SPOs Soon](#).

Banco ABC Brasil S.A. (ABC Brasil) is a Brazilian bank founded in 1989, controlled by the Arab Banking Corp. and representing a material share of the group's assets (26%). ABC Brasil specializes in providing commercial loans, treasury services, and international lines of credit to large companies. Recently, the bank has been diversifying its services by expanding them to midsize companies and developing new business lines such as investment banking and energy commercialization.

In our view, ABC Brasil's sustainable finance framework, published on Aug. 28, is aligned with:

- ✓ Social Bond Principles, ICMA, 2023
- ✓ Social Loan Principles, LMA/LSTA/APLMA, 2023
- ✓ Green Bond Principles, ICMA, 2021 (with June 2022 Appendix 1)
- ✓ Green Loan Principles, LMA/LSTA/APLMA, 2023
- ✓ Sustainability Bond Guidelines ICMA, 2021

Issuer's Sustainability Objectives

Since 2020, ABC Brasil has been formally integrating ESG-related topics into its strategic planning. For this purpose, the entity has updated its internal policies to incorporate social, environmental, and climate factors, and restructured its governance to oversee the implementation of its newly created sustainability strategy based on four pillars: institutional, impacts, social responsibility, and sustainable businesses.

In our view, ABC Brasil's framework specifically aligns with the sustainable businesses pillar under which the bank aims to identify opportunities in the sustainable finance market to unlock positive impacts across different sectors, enabling clients to access resources to contribute to the transition toward a sustainable future. Therefore, the bank seeks financing to boost its low-carbon portfolio and reduce the environmental footprint of financed activities, while also enhancing social benefits to low-income, disadvantaged, and minority groups and increasing access to financing for micro, small, and midsize enterprises (MSMEs).

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Second Party Opinion Summary

Use of proceeds

Alignment  ABC Brasil's sustainable finance framework is aligned with this component of the applicable Principles.

Score Not aligned **Aligned** Strong Advanced

ABC Brasil commits to allocating an amount equivalent to the net proceeds of instruments issued under its framework to finance and/or refinance eligible green and social projects. These contribute to at least one sustainability objective and support targeted U.N. sustainable development goals (SDGs). The entity will disclose the share of financing versus refinancing, with a maximum look-back period of 24 months for refinanced projects.


Process for project evaluation and selection

Alignment  ABC Brasil's sustainable finance framework is aligned with this component of the applicable Principles.

Score Not aligned **Aligned** Strong Advanced


The framework outlines that the bank's environmental and social risk and sustainability teams will select projects to fit eligible categories based on solid criteria. A multidisciplinary team will oversee allocation and deliberate on matters related to the proceeds. ABC Brasil incorporates clear eligibility criteria by setting quantitative thresholds or referencing market-based certifications for most of the eligible project categories.

Management of proceeds

Alignment  ABC Brasil's sustainable finance framework is aligned with this component of the applicable Principles.

ABC Brasil states that all financing issued under the framework will be allocated within a two-year period after each issuance. Monitoring of allocation will be conducted on a semiannual basis. Until redemption, unallocated proceeds will be temporarily invested in cash or highly liquid instruments.

Reporting

Alignment  ABC Brasil's sustainable finance framework is aligned with this component of the applicable Principles.

Score Not aligned **Aligned** Strong Advanced

ABC Brasil commits to annually reporting the allocation of net proceeds and impact of financed projects until redemption of the instruments issued under the framework. This information will be available on the entity's website.

Framework Assessment

Use of proceeds

The Principles make optional recommendations for stronger structuring practices, which inform our alignment opinion as aligned, strong, or advanced. For use of proceeds, we consider the commitments and clarity on how the proceeds are used.

 ABC Brasil's sustainable finance framework is aligned with this component of the applicable Principles.

Commitments score

Not aligned

Aligned

Strong

Advanced

We consider ABC Brasil's overall use of proceeds commitments to be aligned.

ABC Brasil commits to allocating an amount equivalent to the net proceeds from any financial instrument issued under its framework to finance/refinance eligible green and social projects, in line with the bank's sustainability strategy aimed at expanding financing to sustainable businesses in Brazil.

The framework has seven green categories: environmentally sustainable management of living natural resources and land use, renewable energy, energy efficiency, green buildings, clean transportation, sustainable water and wastewater management, and pollution prevention and control. Projects relating to renewable energy, energy efficiency, clean transportation, and green buildings contribute to climate change mitigation by minimizing dependence on fossil fuel-based products and activities.

In each category, ABC Brasil provides a clear description of the eligible financed activities. For example, it considers as eligible waste biomass power plants if projects meet an 80% energy efficiency threshold and a 16.0 grams of carbon dioxide equivalent per megajoule of energy (gCO₂e/MJ) emissions threshold, which is in line with the Climate Bonds Standard Bioenergy criteria. For forestry activities, the framework adopts two layers of screening: market-based certifications such as the Forest Stewardship Council (FSC), and for noncertified projects, it requires following the national regulator's guidelines to have a sustainable management plan and address chemical use.

The framework also includes projects that deliver environmental benefits while requiring intensive land use, which constrain our assessment at aligned. For example, although animal waste treatment projects promote a circular economy and energy efficiency, they could rely on manure from cattle, which is land-use-intensive. For biofuels, particularly important in Brazil, net environmental benefits for very carbon-intensive baselines may be significant, but scaling up also creates additional environmental risks, such as increased land use competition and degraded soil quality.

For such cases, we view positively that ABC Brasil requires thresholds for greenhouse gas emissions aligned with the E.U. Renewable Energy Directive (RED II), requires BONSUCRO certification for large sugarcane producers, and excludes projects that could drain carbon reserves in soil or compete with food production. However, the framework doesn't exclude competition with feed production areas, which could potentially allow for exposure to indirect risks of land-use change.

The framework's five social project categories are affordable basic infrastructure, affordable housing, employment generation, socioeconomic advancement and empowerment, and access to essential services for both education and health care. Funding projects in this category aim to achieve social benefits such as improving access to financing for MSMEs that meet gender, racial, and people with disabilities criteria and enhancing affordability and access to education and health services at free or subsidized rates. The target population is described for each social category following international indexes and governmental definitions.

We see financing to affordable housing projects as especially relevant considering the housing deficit of about six million homes in the country, according to the [latest official data](#). In addition, projects that provide public school transport help to address a significant social gap in the country: more than 2 million children and adolescents from ages 11 to 19 are not attending school

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in Brazil and 18% of them say the lack of transportation is the reason for dropping out, according to [Unicef](#). We view positively that although classified as social, the project also includes market-based clean transportation thresholds for greenhouse gas emissions.

ABC Brasil communicates its sustainability objectives by outlining specific SDG targets that each eligible project category aims to meet. Moreover, the bank will disclose the share of proceeds used to finance and refinance eligible projects, which we see as favorable.

Process for project evaluation and selection

The Principles make optional recommendations for stronger structuring practices, which inform our alignment opinion as aligned, strong, or advanced. For our process for project selection and evaluation, we consider the commitments and clarity on the process used to evaluate and select eligible projects to fund with the proceeds of the sustainable finance instrument.



ABC Brasil's sustainable finance framework is aligned with this component of the applicable Principles.

Commitments score

Not aligned

Aligned

Strong

Advanced

We consider ABC Brasil's overall process for project selection and evaluation commitments to be aligned.

The framework outlines the process that the bank will use to determine how projects fit within the eligible categories. The environmental and social risk and the sustainability units will identify whether the operations fall under any of the eligible green or social categories based on specific criteria, such as the alignment of the client's activity with the Brazilian Federation of Banks' Green Taxonomy, the client's size and location, the financed items, and the diversity of the client's leadership or entrepreneurship. Additionally, other strategic units of the bank--such as the treasury, risk management, and human resources teams--will be involved in monitoring the financial allocation and reviewing the projects' environmental and social benefits and how they align with the entity's policies and exclusion list.

Moreover, the bank will rely on its environmental and social risk management system (ESMS) to identify, measure, mitigate, and monitor direct and indirect risks associated with financed projects. The ESMS applies the IFC Performance Standards and national regulation, which is in line with industry practices. All credit operations funded by the proceeds issued under the framework will be categorized into low, medium, or high E&S risk, with the latter submitted to the credit committee and requiring additional corrective measures.

In addition to connecting all eligible green and social projects to specific targets under U.N. SDGs, ABC Brasil incorporates clear eligibility criteria by setting quantitative thresholds or referencing market-based certifications for several project categories. For example, various green projects have their thresholds aligned with the Climate Bonds Initiative or require solid market certifications such as LEED (gold or higher) and Forest Stewardship Council and Programme for the Endorsement of Forest Certification. The bank also includes a specific exclusion list covering items such as deforestation operations, non-RSPO (Roundtable on Sustainable Palm Oil) certified palm oil, and thermal coal mining. For social projects, target population definitions mainly follow official definitions, referencing organizations such as the U.N. or IFC in the absence of governmental definitions.

In the bank's extensive list, not all applicable project categories include clearly defined thresholds and/or incorporate market-based taxonomies, which is in line with the global banking industry's practices, but constrains our assessment.

Management of proceeds

The Principles require disclosure of the issuer's management of proceeds from sustainable finance over the life of the funding. The alignment opinion focuses on how clear in the documentation is the issuer's commitment to ensure that the funds raised will remain dedicated to eligible sustainability projects throughout the life of the sustainable finance funding.

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 ABC Brasil's sustainable finance framework is aligned with this component of the applicable Principles.

ABC Brasil commits to monitoring net proceeds from instruments issued under the framework semiannually and fully allocating them within two years after each issuance. The net proceeds will be deposited in a general account and the bank will ensure that an equivalent amount is used to finance qualifying projects, complying with the bank's lending policies and applicable exclusions, such as refraining from investing in carbon-intensive assets.

In case loans take the form of one or more tranches of loan facilities, the bank will ensure that only green tranches can be labeled as green. The issuer will de-label the securities that fail to use proceeds as planned and hold unallocated proceeds in the bank's liquidity reserve, in cash and other highly liquid market securities, which is in line with market practice. Moreover, the entity commits to reallocating proceeds to eligible projects within 12 months and disclosing changes to the portfolio in its annual reports, which we view as in line with best market practices.

Reporting

The Principles make optional recommendations for stronger disclosure practices, which inform our disclosure opinion as aligned, strong, or advanced. We consider commitments for reporting on the allocation of proceeds to eligible projects and the expected or actual impact of the projects financed, as well as the frequency of reporting.

 ABC Brasil's sustainable finance framework is aligned with this component of the applicable Principles.

Disclosure score

Not aligned

Aligned

Strong

Advanced

We consider ABC Brasil's overall reporting practices to be aligned.

ABC Brasil commits to annually reporting on the allocation of the proceeds issued under the framework until the instruments' redemption. The report will be available on the entity's public website and will contain relevant information, such as the amount of unallocated proceeds and the proportion of funds used for refinancing as well as additional descriptive information, such as the amount allocated per region of the country and the disbursement for each green and social category. An external verifier will validate the amounts disclosed in the allocation report.

The bank will also be transparent about the impacts for each category until redemption on an annual basis. Moreover, ABC Brasil commits to disclosing output and outcome indicators for all project categories as well as the methodologies selected for their calculation, which we view positively. For green projects, the list would include a comprehensive set of indicators, ranging from more basic metrics such as the number of beneficiaries and the production under sustainable practices to more consolidated KPIs such as avoided greenhouse gas emissions and financial losses. In contrast, social indicators selected are limited to inputs and outputs, such as the number of financed projects and beneficiaries, which reflects common limitations faced by the sector when tracking social impact.




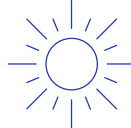
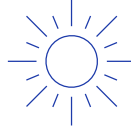


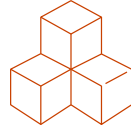

However, ABC Brasil does not commit to measuring expected impacts before the financing, which constrains our assessment.

Mapping To The U.N.'s Sustainable Development Goals

The Sustainable Development Goals (SDGs), which the United Nations (U.N.) set up in 2015, form an agenda for achieving sustainable development by 2030.

We use the International Capital Market Association's (ICMA's) SDG mapping for this part of the report. We acknowledge that ICMA's mapping does not provide an exhaustive list of SDGs and that ICMA recommends each project category be reviewed individually to map it to the relevant SDGs.

ABC Brasil's sustainable finance framework intends to contribute to the following SDGs:

Use of proceeds	SDGs
Environmentally sustainable management of living natural resources and land use	<div style="display: flex; justify-content: space-around; align-items: center;"> <div style="text-align: center;">  <p>2. Zero hunger*</p> </div> <div style="text-align: center;">  <p>13. Climate action*</p> </div> <div style="text-align: center;">  <p>15. Life on land*</p> </div> </div>
Renewable energy	<div style="text-align: center;">  <p>7. Affordable and clean energy*</p> </div>
Energy efficiency	<div style="text-align: center;">  <p>7. Affordable and clean energy*</p> </div>
Green buildings	<div style="display: flex; justify-content: space-around; align-items: center;"> <div style="text-align: center;">  <p>12. Responsible consumption and production</p> </div> <div style="text-align: center;">  <p>13. Climate action*</p> </div> </div>
Clean transportation	<div style="display: flex; justify-content: space-around; align-items: center;"> <div style="text-align: center;">  <p>9. Industry, innovation and infrastructure</p> </div> <div style="text-align: center;">  <p>11. Sustainable cities and communities*</p> </div> </div>

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Sustainable water and wastewater management



6. Clean water and sanitation*

Pollution prevention and control



9. Industry, innovation and infrastructure



12. Responsible consumption and production*

Access to essential services



3. Good health and well-being*

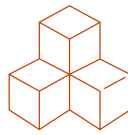


4. Quality education*

Affordable basic infrastructure



6. Clean water and sanitation*



9. Industry, innovation and infrastructure*



11. Sustainable cities and communities*

Affordable housing



11. Sustainable cities and communities*

Financing for SMEs (employment generation)



8. Decent work and economic growth*



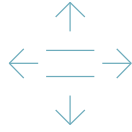
9. Industry, innovation and infrastructure*

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Socioeconomic advancement and empowerment



5. Gender equality*



10. Reduced inequalities*

*The eligible project categories link to these SDGs in the ICMA mapping.

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