Deutsche Bank
Corporate Bank

Integrating ESG into corporate financing for sustainable transformations

#PositiveImpact

DIRK

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Contents

Why is ESG important?

1

Why is Sustainability important to so many businesses?

The focus on sustainability accumulates across different stakeholders

Considerations:

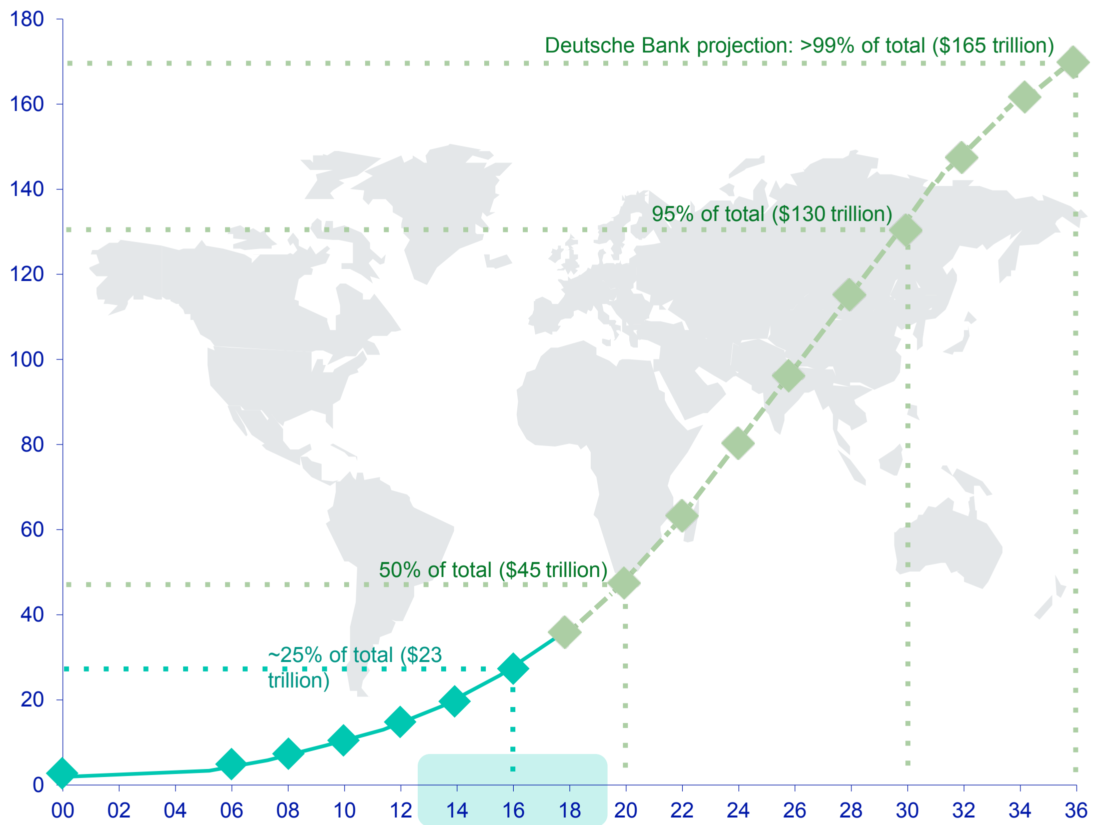
1. Business models often either profit or harm from the trend of sustainability – many need to transform
2. Expectations of suppliers and customers around sustainability and climate change are increasing
3. ESG factors especially climate change are included in investment and financing decisions
3. Demand for sustainable assets and responsibly run business is high
4. Increasing regulatory forces around the topic of sustainability such as the "Lieferkettengesetz" emerge
5. Positioning as responsible, open-minded and future orientated company
6. Disclosure and Reporting requirements will increase in the future

Overview of financial landscape & rising importance of ESG

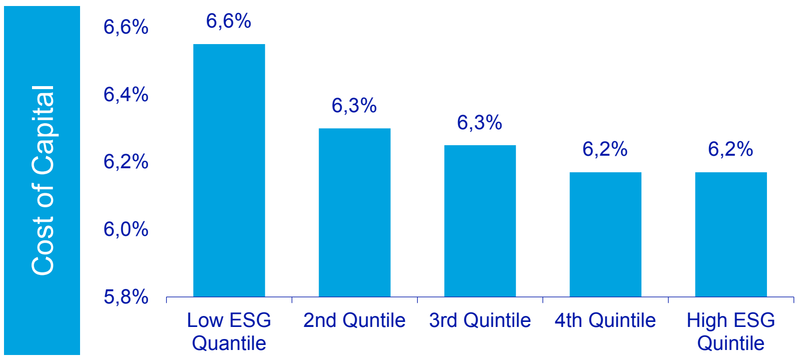
ESG is influencing the flow and cost of capital

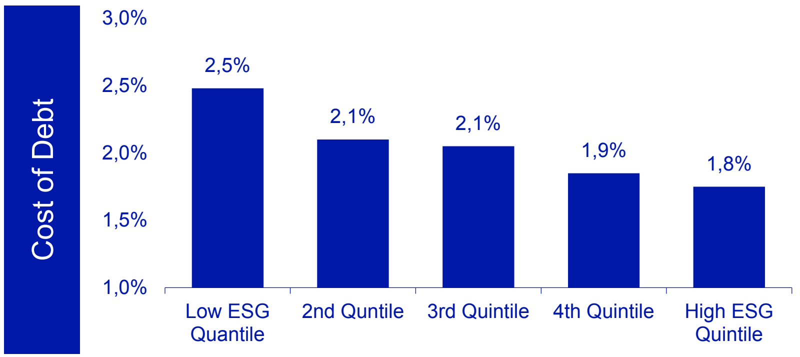
Global assets under management with an ESG mandate (in USD trillion)

Country/ Region	Growth (2014-2016)	Growth (2016-2018)	CAGR (2014-2018)
Europe	12%	17%	7%
U.S.	33%	38%	16%



ESG is also having a real impact on cost of capital





Global initiatives most relied on by investors

PARIS2015 UN CLIMATE CHANGE CONFERENCE COP21·CMP11

SUSTAINABLE DEVELOPMENT GOALS

United Nations Global Compact

Note: Monthly averages were reported over the period from 31 December 2015, to 29 November 2019. The average number of companies in the MSCI World Index and MSCI Emerging Markets Index over the analysis period was 1,552 and 960, respectively.
Source: DB Global Markets Research "Konzept: big data shakes up ESG investing. October 2018. MSCI, February 25, 2020 "http://www.gsi-alliance.org/wp-content/uploads/2019/06/GSIR_Review2018F.pdf

Determine key content

What topics are most important to address with investors?

To the right, we identify 6 key topics to address when engaging with fixed-income investors on ESG

While each category is important in it's own right, the first topic, 'overview of the Company's Sustainability / ESG strategy' is arguably most important

Investors have increasingly valued how ESG is integrated into a Company's business rather than it being approached as an independent item

Key Topics	Key Content
Overview of the Company's Sustainability / ESG Strategy	– Clearly communicate company wide ESG / sustainability strategy including commitment, efforts and actions taken to improve environmental footprint – Overview of Company's internal sustainability structure and management accountability
Key Sector-Specific Material Risks	– Each company and sector has unique top material risks that – Explain what these are, how you have mitigated and commitment to mitigation going forward – Investors often rely on SASB, Sustainalytics, MSCI and other similar 3rd party agencies to identify these risks
Sustainable Performance Targets (i.e. KPIs)	– Meaningful, measurable and time based ESG goals (i.e. KPIs) – How is your ESG strategy yielding real results and contributing to a lower carbon environment
Track record of performance on KPIs or Material ESG Issues	– E.g. Overview of existing asset base and investments made to de-carbonize the business – Other ESG initiatives undertaken that correspond to material ESG issues
ESG Ratings	– Include in content particularly if 2nd party ratings are strong, otherwise, be prepared to address questions on why rating is lagging – Investors primary focus on Sustainalytics and MSCI
Framework (for ESG bond)	– For deal related marketing (for use-of-proceeds or sustainability-linked bond issuance) – In addition to the above, detail the bond framework in alignment with ICMA's green bond principles including use-of-proceeds, reporting, verification

Alignment with Global Alliances

Industry Specific Alliances

DB Sustainable Finance Strategy & Offering

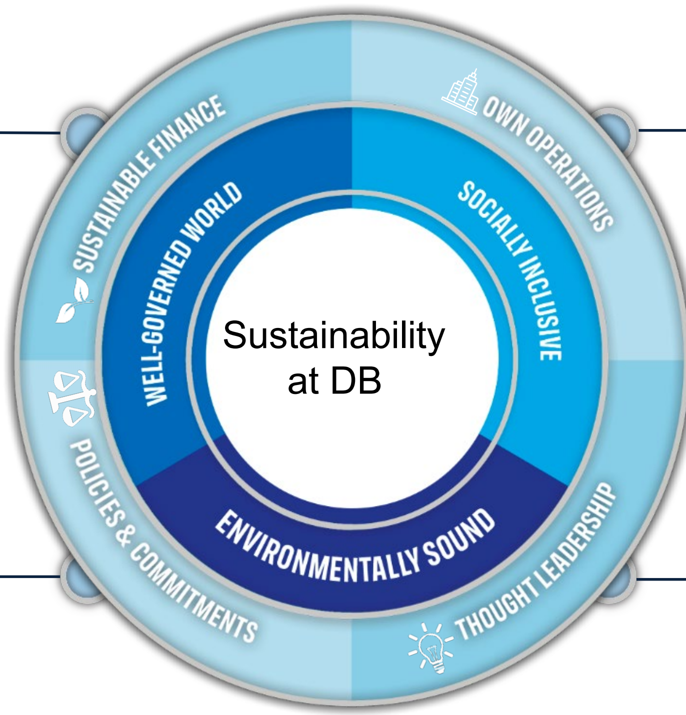
2

Deutsche Bank's sustainability strategy at a glance

Our mission: "We aspire to contribute to an environmentally sound, socially inclusive and well-governed world. We strive to support our clients in their transformation.
Our advice as well as our products and solutions shall be built on this commitment."

Support clients in their transformation by advising and financing
- Accelerating the speed of our sustainable finance target of EUR 200bn from 2025 to 2023
- Deutsche Bank Taxonomy training offered to 50% of client facing staff by year end 2021; 100% by year end 2022

Manage the impact of our business on the environment and society
- Disclosure of CO2 footprint of our loan portfolio till year end 2022
- Announcement of future Green Asset Ratio target by mid-2022
- Transition dialogue with clients in the ESG focus initiated until year end 2021



Embed sustainability into all operations and ensure good governance
- Source 100% renewable electricity by 2025
- 35% women on Managing Director, Director and Vice President level by 2025
- Reducing DB car fleet gasoline consumption by 30% by 2025 and carbon zero by 2030 in Germany

Advocate transformation and be a leader on sustainability in the industry
- Embed ESG considerations within small and mid-cap ('SMID cap') research reports
- Engagement with Ocean Risk and Resilience Action Alliances first banking member

UNITED NATIONS · PARIS2015 COP21·CMP11 · IFC International Finance Corporation WORLD BANK GROUP · GRI · TCFD TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES · ILO

Sustainable Finance Offering to support your strategy

How banks look at the ESG profile of companies...

Corporate

... and how they support companies in the development of sustainability strategies.

1) ESG Integration

2) Sustainable Finance Solutions

3) Incentives from the regulator?

Sustainable use of proceeds (e.g. "green / social loans") and/ or pricing linked to the achievement of ESG KPIs		Incentivizing suppliers to become more sustainable	Diverse strategies from ESG integration to impact investing	Dedicated ESG Services / Advisory
Financing	**Trade & Risk Management**	**Supplier Finance**	**Cash, Liquidity & Pension Management**	**Sustainability Transformation**
Green/ Social or Sustainability-linked… – Loans – Bonds – Project Finance – Structured Trade and Export Finance – Natural Resource Finance – Trade Flow Facilities	*Green/ Social or Sustainability-linked…* – Trade Flow Facilities – FX – Rates	– Sustainable Supply Chain Finance – Private Equity impact fund, e.g. investing in renewable energy project	– Structured Notes of Impact Funds – Green Deposits AM Solutions: – Money market funds – Investment solutions for Equities, Fixed Income, Multi Asset and Alternatives	– ESG updates & advisory (trends, rating, regulation, investor access, etc.) – ESG reporting services for sustainable debt and loan agencies

Globally integrated, product-agnostic approach to accompany clients in their sustainability transformation incl. tailor-made ESG client workshops

How can Sustainable Finance support you?

Benefits and the two common concepts applicable to all financial products

Benefits		
	1	Anchor: Sustainability aspects become further integrated within your organization and people mobilized
	2	Signal: Aligning your financing with your sustainability strategy signals your ESG commitment to various stakeholders (customers, suppliers, investors, etc)
	3	Innovation: Allows the Treasury team to play an innovative role by operationalizing the company's ESG strategy
	4	Feedback: Receive external feedback regarding materiality and ambition level of KPIs and ESG strategy
	5	Pricing: If targets are achieved, a more competitive pricing is possible
	6	Applicability – only for sustainability-linked structures: independent from project and can be used for multiple products/ deals as a corporate level framework

… We are determined to reach our ultimate target of becoming fully carbon neutral by 2050, and this agreement serves as another enabler for us to deliver on that ambition …

– CEO Maersk

… By combining sustainability improvements with our new credit line, we have found an innovative way in corporate finance to further advance our sustainability strategy …

– Head of Treasury Continental AG

	Use of proceeds concept	Sustainability-Linked concept
Sector and specific asset required	– A specific asset is required, some sectors are better suited for asset-based solutions	– No specific asset or financing purpose is required, eligible for general corporate purposes
Clear sustainability strategy	– Recommended due to changing external environment	– Recommended, transparency on targets is key
Reporting	– Allocation (projects financed) and impact reporting	– Pre-agreed KPIs (publicly disclosed or undisclosed)
Marketing strategy	– Message to stakeholders about major investments in sustainable activities	– Showing commitment to Sustainability strategy by linking financial products
Advantages	– Ideal for pre-defined purposes, no dedicated sustainability strategy required	– Available to any company due to linkage to different KPIs, no asset/investment or sustainably orientated business model needed

Deep Dive Sustainability-Linked Loans

3

Process overview

A

Three steps: Defining and including KPIs into the loan documentation

Different parties involved

- In line with the market standards an ESG-linked loan should always build upon an existing ESG Strategy and respective reporting
- In case a company cannot yet rely upon an ESG Strategy and reporting, this can be set up either by company or with the help of a 3rd party consultant
- Depending on the existing data, the integration of an ESG-link takes 6-12 weeks
- DB's role in any case is to ensure a market facing transaction structure

Without external consultant:

Step	To-Do	Responsibility
1) Initial ESG DD	a) Perform detailed ESG DD b) Derive first KPIs to discuss with client c) Define the range of margin step ups/downs	DB
2) Structuring phase	a) Structure and fix the KPIs with the client in line with the LMA standards b) Draft the legal language for the contract c) Define Post-closure reporting requirements on KPIs	DB & client
3) Post-closure monitoring	a) Verify annual ESG compliance b) Initiate respective margin adjustment	DB

With external consultant:

Step	To-Do	Responsibility
1) Initial ESG DD	a) Perform detailed ESG DD b) Derive first KPIs to discuss with client c) Define the range of margin step ups/downs	DB
2) Structuring phase	a) Mandating consultant (letter incl. role description) b) Perform detailed ESG DD, develop KPI structure proposal with client and make recommendations c) Fix KPIs & Targets d) Ensure compatibility with LMA standards e) Draft the legal language for the contract f) Define Post-closure reporting requirements on KPIs	a) Client b) Client & 3rd party consultant c) Client, DB & 3rd party consultant d) – f) DB f) 3rd party consultant
3) Post-closure monitoring	a) Verify annual ESG compliance b) Initiate respective margin adjustment	DB

DB involvement

Design of an ESG-linked structure

B

Sustainability-Linked Loans
Operating principle & client benefits

Sustainability-Linked Loans (SLL) as a strategic solution

- Sustainability-linked loans (SLLs) complement the existing sustainability strategy and can be adapted to companies specifics
- SLLs can be used for general corporate financing
- The loan margin is adjusted depending on the achievement of predefined sustainability KPIs. The range here is [2.5-5] basis points

- Design in line with the sustainability strategy
- Ideally, SLLs operationalize existing goals & reporting structures

Benefits of Sustainability-Linked Loans

- Intensify cooperation with relevant stakeholders around shared values
- Additional external feedback regarding the sustainability strategy
- Profitability and sustainability aspects are combined and incentivised through margin adjustment
- Promoting sustainable long-term growth
- Investment in employee recruitment or additional differentiating factor when recruiting qualified employees

Selected potential KPIs for Sustainability Linked Transactions

Additional KPIs can be structured around the reported data to show details of the sustainability efforts undertaken by our clients

According to current market standards, the focus is on environmental KPIs. This is also reflected in the EU taxonomy

A further development towards the dimensions "social" & "governance" is increasingly emerging

Environment	Social	Governance
Climate Change Mitigation: – Total **Carbon Footprint** or **Emission Intensity** as gross carbon emissions in tons CO2 equivalent per EUR million revenues – Increase share of **renewable energy usage** Circular Economy: – **Increase share of recycled waste** – **Decrease of total fresh water usage**	– **Diversity and Inclusion** (diverse hiring and retention) – **Average training time per employee per year** – **Lost Time Injury Frequency Rate** (accidents at work per million hours worked, LTIFR)	– **Supply Chain engagement** (Supplier assessment and engagement based on procurement spend) – **Share of employees** having received dedicated ▪ Code of Conduct and/or ▪ anti-trust and/ or ▪ anti-corruption and bribery training

In accordance with LMA Sustainability-Linked Loan Principles[1]:

- KPIs should be ambitious, meaningful and linked to substantial improvements
- Transparent connection between sustainability KPIs and sustainability strategy
- Borrowers must obtain external verification of the performance level for each KPI
- Borrowers shall report at least once a year on the achievement of targets

Source: (1) Loan Market Association – Sustainability Linked Loan Principles May 2021

Sustainability linked concept

Various options to design a Sustainability-linked Structure

We suggest [3-5] KPIs with a focus on environmental ones as they are the most important ones given current political and societal dynamics

With regards to pricing, an ESG matrix helps to transparently communicate the progress under the selected KPIs

A potential malus within this context could be donated to a charity in line with the overall ESG strategy

1) Area of focus (General vs. Specific)

General

KPI(s) that try to capture overall ESG performance of the company

External ESG Score(s)

Specific

KPI(s) that focus on specific E, S and/or G areas important to the company

E.g. E: Scope 1-3 GHG emissions; S: Employee training opportunities

2) KPI development tracking

Cumulative

Assessing the target achievement on a cumulative basis over the entire period

5% reduction till Y1, 10% reduction till Y2,…

Year on Year Improvement

Assessing the target achievement each year independently

5% reduction each year

Achievement Yes/No

Assessing the target based on a rolling average

On average 5% reduction in the last 3 years

3) Target type

Constant

The target to be set achieved stays constant over the lifetime of the loan

E.g. ESG score > 85

Progressive

The target to be achieved gets progressively harder

E.g. 80 in Y1, 82 in Y2,…

4) Margin calculation multiple targets

Achievement Yes/No

For the margin to be reduced each and every target has to be achieved

Bonus: -2.5, -2.0 bps.
Malus: +2.5, +2.0 bps

	1st Test	2nd Test	3rd Test	4th Test
KPI A	✓	✓	✓	✓
KPI B	0	✓	✓	✓
KPI C	✓	✓	✓	×
Margin Reduction?	×	✓	✓	×

Matrix

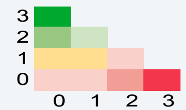
Margin reduction is calculated based on a pre-defined margin grid

+2.5; +1.5, 0; -1.5; -2.5 bps

	1st Test	2nd Test	3rd Test	4th Test
KPI A	✓	✓	✓	✓
KPI B	0	✓	✓	✓
KPI C	✓	✓	✓	×

Margin Reduction matrix:

Targets achieved



Targets failed

5) Add-on Opportunity

Donation-Option

Instead of a malus payment to DB (in case of „fail“): Donation to a charity

E.g. leveraging community engagement activities

DB recommendations – to be discussed

Monitoring

C

Ensuring credibility through solid post-closure monitoring

Reporting and monitoring considerations

- In order to ensure a robust SLL transaction, there is a need for transparency in determining whether KPIs have been met or not
- This has to be ensured via reporting obligations and an external review or audit to verify clients performance against the KPIs
- As of today, there is no single globally accepted methodology for reporting on KPIs; this has to be discussed and decided in close collaboration with the company and DB
- DB suggests to verify the ESG compliance annually based on an ESG compliance certificate where upon receipt the margin adjustment is triggered
- The below lines out the most important structural elements when structuring the post-closure monitoring aspect

Reporting frequency

- Agree on binding reporting schedule (periodic reports)
- Usually, client should be required to report on their KPIs at least once a year

Methodology

- Chosen methodology will depend on client and KPIs
- Client to provide details of any underlying methodology and assumptions (and an analysis of how the methodology differs from any previous years, if any)

Independent review

- An external review of the KPI performance is necessary
- External reviewer are usually the auditor, environmental consultant or an independent rating agency

Disclosure

- Public reporting vs. private with preference for public
- In case of public reporting the reporting should ideally sit with the audited financial statements

Q&A

4

Disclaimer

Disclaimer