

# SLBs: a summary of 2023 targets

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The Sustainability-Linked Bond (SLB) market, which began in 2019, is reaching adolescence, in that the early vintage bonds are reaching the observation dates of their Sustainability Performance Targets (SPT). Only a handful of bonds have so far been through this test, and the market dynamics of both the period of uncertain sustainability performance, but also once a target is missed, have not yet been well observed.

To our knowledge so far two SLBs have missed their targets. The first was Polish refiner Orlen with an SLB linked to its ESG rating, and so was continually observed.<sup>1</sup> The second was Greek utility company PPC that missed an absolute Scope 1 emissions KPI at the end of 2021.<sup>2</sup> Both saw limited market reaction to the events.

Despite current market volatility, **the financial relevance of sustainability performance should not be ignored**. Twenty benchmark SLBs will observe their SPTs in 2023; we have analysed the KPI performance and potential market impact to support the perspicacious investor.

**The most material SLB observation at the end of 2023 is for Enel**, the largest issuer of SLBs. Our analysis concludes that the target is likely to be missed and, if so, \$10.8bn of bonds will pay a step-up coupon.<sup>3</sup> Recent market pricing implies a 35% likelihood of the target being missed.<sup>4</sup>

**PPC, a Greek utility that already missed a target at the end of 2022, is likely to miss again**. Despite a muted market reaction last year, the bond in question this time has a longer maturity, and a lower starting coupon, and although the broader market is less supportive for sub-investment grade issuers, there could be more value to this step-up option.

**We also highlight a BB-rated Mexican packaging issuer, San Miguel Industrias, that has given very limited recent reporting on progress, and so has risk of volatility**. This highlights the benefits for issuers of clear and ongoing disclosure, giving investors comfort in sustainability trajectories.

It is also interesting to look back on the early vintage of SLBs, to compare with recent structures, to observe market progress. In this population no bonds include Scope 3 emissions, and two SPTs were just to get an emissions reduction plan approved by SBTi. **We believe SLB investors now demand a higher standard of materiality and ambition, as evidenced by some of the stronger structures currently being issued.**<sup>5</sup>

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<sup>1</sup> We covered the bond in “[One small step for Orlen, one giant leap for the SLB market](#)”, AFII, 29 Nov 2022.

<sup>2</sup> “[Impact of PPC’s Failure to Meet Sustainability-Linked Bond Targets Limited](#)”, FitchRatings, 16 Mar 2023.

<sup>3</sup> For full analysis please see “[Enel SLBs: update on 2023 observation date](#)”, AFII, 20 Oct 2023.

<sup>4</sup> The SLBs in question have been outperforming, as presented in “[Enel SLBs: market update](#)”, AFII, 8 Nov 2023. Latest pricing on the EUR 2027 bond switch is -7bp (data from Bloomberg as of 10 Nov 2023), which when compared with our calculated 20.5bp value of the full step-up, implies around a 35% probability of missing the target.

<sup>5</sup> For some examples please see “[Sustainability-Linked Bond Bumper Week](#)”, AFII, 11 Sep 2023.

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## Summary of bonds

Our analysis has focused on USD and EUR denominated bonds, as we view these as most interesting for the international investor community.<sup>6</sup> Table 1 shows the population of bonds that we have identified, alongside our analysis of the status.

Table 1. SLBs with KPI observation date in 2023. Source: AFII, Bloomberg.

Issuer	ISIN	Issue Date	Maturity	Observation Date	Currency	Amount		Status
						Outstanding		
CHINA CONSTRUCT BANK/HK	XS2331713102	22-Apr-21	22-Apr-26	31-Dec-23	USD	0.55		Currently MET
ENEL FINANCE INTL NV	XS2353182020	17-Jun-21	17-Jun-27	31-Dec-23	EUR	1.00		Likely MISS
ENEL FINANCE INTL NV	XS2353182293	17-Jun-21	17-Jun-30	31-Dec-23	EUR	1.25		Likely MISS
ENEL FINANCE INTL NV	US29278GAN88	12-Jul-21	12-Jul-28	31-Dec-23	USD	1.00		Likely MISS
ENEL FINANCE INTL NV	US29278GAP37	12-Jul-21	12-Jul-31	31-Dec-23	USD	1.00		Likely MISS
ENEL FINANCE INTL NV	US29278GAM06	12-Jul-21	12-Jul-26	31-Dec-23	USD	1.25		Likely MISS
ENEL FINANCE INTL NV	XS2390400633	28-Sep-21	28-May-26	31-Dec-23	EUR	1.25		Likely MISS
ENEL FINANCE INTL NV	XS2390400716	28-Sep-21	28-May-29	31-Dec-23	EUR	1.00		Likely MISS
ENEL FINANCE INTL NV	XS2432293673	17-Jan-22	17-Nov-25	31-Dec-23	EUR	1.25		Likely MISS
ENEL FINANCE INTL NV	US29278GAV05	15-Jun-22	15-Jun-25	31-Dec-23	USD	0.75		Likely MISS
ENEL FINANCE INTL NV	US29278GAZ19	14-Oct-22	14-Oct-25	31-Dec-23	USD	0.75		Likely MISS
EQT AB	XS2338570331	14-May-21	14-May-31	31-Dec-23/31-Dec-26	EUR	0.50		MET 2023 target
FORVIA SE	XS2553825949	15-Nov-22	15-Jun-26	31-Dec-23	EUR	0.95		Currently MET
KNORR-BREMSE AG	XS2534891978	21-Sep-22	21-Sep-27	31-Aug-23	EUR	0.70		MET
ORBIA ADVANCE CORP SAB	US68560EAA64	11-May-21	11-May-26	31-Dec-23	USD	0.60		Likely MEET
PUBLIC POWER CORP	XS2359929812	21-Jul-21	31-Jul-28	31-Dec-23	EUR	0.50		Likely MISS
REXEL SA	XS2332306344	05-May-21	15-Jun-28	31-Dec-23	EUR	0.40		Currently MET
REXEL SA	XS2403428472	10-Nov-21	15-Dec-28	31-Dec-23	EUR	0.60		Currently MET
SAN MIGUEL INDUSTRIAS	US79911QAA22	02-Aug-21	02-Aug-28	31-Dec-23	USD	0.38		50:50
YUNNAN ENERGY INST OVR	XS2445143329	21-Apr-22	21-Apr-25	31-Dec-23	USD	0.23		Likely MEET

### 1) Targets met

When analysing the reporting for these issuers, we note that two issuers have already met their targets. Knorr-Bremse had observation dates earlier in the year, and has successfully achieved its KPI. One other, EQT, has achieved its 2023 target before the deadline. EQT has two additional SPTs which will be observed in 2026 and so may pay a step-up linked to those KPIs.

We note that both these targets were digital: to have an SBTi approved emissions plan. Once the targets have been achieved, they cannot subsequently no longer be achieved. While having a target in plan may seem weaker than ensuring emissions reductions are in line with the pathway, we do recognise that having an approved plan is a necessary first step, and therefore can be suitable for a near-term SPT.

<sup>6</sup> Our population starts with a Bloomberg search for bonds identified as sustainability-linked. We exclude schuldschein and have focused on EUR and USD SLBs for now.

## EQT AB

EQT AB (ticker EQT), a Swedish private equity firm, issued an SLB (ISIN XS2338570331) linked to three KPIs. The first depended on setting an SBTi-approved emissions reduction plan by 2023. This was reported as achieved in Oct 2021,<sup>7</sup> only a few months after the bond issuance. The later two are linked to gender diversity within EQT and within portfolio companies, with targets in 2026.

## Knorr-Bremse AG

Knorr-Bremse (ticker KNOGR) is a German manufacturing company, supplying items to the global rail industry. It issued an SLB (ISIN XS2534891978) in Sep 2022 with a target to set an SBTi approved emissions target for Scope 3 by Aug 2023. The target was achieved a few weeks before the deadline, in Jul 2023.<sup>8</sup>

## 2) Targets currently met

For three issuers, the China Construction Bank, Forvia and Rexel, the latest reporting shows that the KPIs are currently meeting the targets. The KPIs are numeric, and so can continue to change. While one might feel comfortable that emissions intensity will always be decreasing, two of these targets are for absolute emissions, which could depend on how the overall size of the business changes.

Therefore, these targets cannot be guaranteed to be met; however, there is a high chance that they will be.

### China Construction Bank (CCB)

China Construction Bank (Ticker CCB) was originally state owned, but is now listed on the Hong Kong stock exchange. It has issued green bonds, as well as two SLBs. The SLBs use a single KPI, the ratio of green loans to adjusted gross loans and advances to customers. Its first SLB targets above 9.5% at 31 Dec 2022, and the SLB in Table 1 (ISIN XS2331713102) targets above 10% at 31 Dec 2023. In CCB's 2022 report on labelled bonds, this figure was 13.51% as of 31 Dec 2022.<sup>9</sup>

This means the SPT was met on the earlier bond, and the current level is also above the 2023 target. While it is possible to reduce this KPI if a large portion of non-green loans was originated, the KPI is sufficiently high above the target that we view this as unlikely.

### Forvia SE

Forvia (ticker EOFP), a French automotive technology group, issued its SLB (ISIN XS2553825949) late last year with one KPI linked to Scope 1 + 2 emissions reductions. The target was a 20% reduction compared to a 2019 baseline by the end of 2023. Forvia's 2022 sustainability report gives a reduction of 31.4% from the 2019 baseline,<sup>10</sup> which is below the 2023 SPT. Given this is an

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<sup>7</sup> ["EQT becomes the first private markets firm to set science based targets"](#), EQT, 15 Oct 2021.

<sup>8</sup> ["Knorr-Bremse gains SBTi validation for 2030 climate targets"](#), Knorr-Bremse, 13 Jul 2023.

<sup>9</sup> ["2022 Green, Social, Sustainability and Sustainability-Linked Bonds Annual Report"](#), CCB, accessed 10 Nov 2023.

<sup>10</sup> Please see p25 on ["Sustainability Report 2022"](#), Forvia, accessed 10 Nov 2023.

absolute target, we do not consider this target to be definitively achieved, as the size of Forvia’s business may adjust, but we certainly believe it will likely be met.

## Rexel SA

Rexel (ticker RXLFP), a French electrical manufacturer, issued two SLBs one in 2021 and a further in Sep 2023. The 2021 SLBs (ISIN XS2332306344 and XS2403428472) have two KPIs. They target the reduction of Scope 1 + 2 emissions by -23.7% and the reduction by -23% of Scope 3 emissions intensity related to consumption of products sold.

Table 2. Rexel emissions and SLB target. Source: Rexel.

	Scope 1 + 2 emissions	Scope 3 intensity
2021	-24.8%	-29.5%
2022	-25.0%	-35.6%
2023 Target	-23.7%	-23.0%

Sustainability reporting from 2021 and 2022 confirms that the KPIs are below the 2023 targets (see Table 2).<sup>11</sup> While we consider that the emissions intensity is unlikely to increase, the fact that one KPI is on absolute emissions means we acknowledge that a growing business could increase this above the target, and so we classify these SPTs as very likely to be met.

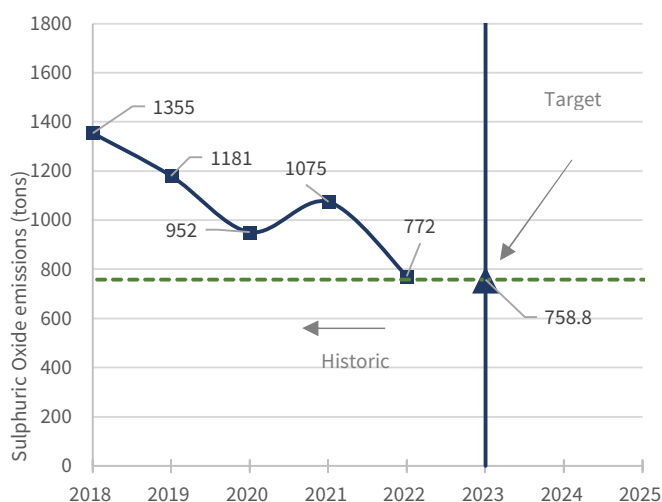
### 3) Targets likely to be met

There are two further issuers, Orbia Advance Corp & Yunnan Energy, whose targets our analysis suggests are likely to be achieved.

## Orbia Advance Corp

Orbia (ticker ORBIA) is a Mexican chemical company with four SLBs outstanding.<sup>12</sup> The \$600mm bond (ISIN US68560EAA64), which has its SPT observation at the end of 2023, has one KPI, to reduce sulphuric oxide (SOx) emissions by 44% compared to a 2018 baseline. Orbia’s 2022 sustainability reporting noted a reduction of 43% compared to 2018, and so this target is very nearly achieved.<sup>13</sup>

Figure 1. Historic Sulphuric Oxide emissions for Orbia. Source: Orbia.



Historical figures have been volatile (as shown in Figure 1), but the trend has been of meaningful reductions, hence we expect this target will likely be met.

<sup>11</sup> Documents sourced from “[Sustainability](#)”, Rexel, accessed 10 Nov 2023.

<sup>12</sup> We cover the sector in more detail in “[Chemicals sector: synthesising impact with SLBs](#)”, AFII, 13 Jul 2023.

<sup>13</sup> “[2022 Sustainability Report](#)”, Orbia, accessed 13 Nov 2023.

# Yunnan Energy Investment Overseas

Yunnan Energy Investment Overseas is a wholly owned subsidiary of Yunnan Provincial Energy Investment Group (ticker YNPOWE), a Chinese state-owned enterprise engaged in regional energy management. YNPOWE has issued several CNY-denominated bonds, and issued two USD-denominated bonds from Yunnan Energy Investment Overseas which are guaranteed by the parent company. The SLB in question (ISIN XS2445143329) was issued in Apr 2022 at a size of \$230mm.

The bond has two SPTs related to its renewables capacity. The first SPT is to increase the total installed capacity of wind power by 173% from a 2021 baseline of 432.6 MW. The second SPT is to increase the Solar Power Generating Capacity by 43% from a 2021 base line of 1,112.7 MW. Failure to meet the SPT 1/2 will result in coupon steps of 15/10bps respectively.<sup>14</sup>

These SPTs are linked to installed capacity, and not a blend of actual power generation, so it can be achieved by aggressive CAPEX strategies.

In wind, the required additional capacity is 747 MW over two years. Fitch reports that 430 MW was added in H1 2023,<sup>15</sup> which would suggest the target is achievable over a two-year period. A Chinese energy blog reports that 750 MW was added in a single project in 2023.<sup>16</sup>

In solar, the required capacity to be added is 478 MW. Fitch projects that 345 MW will be added in 2023 alone.<sup>15</sup> There are further online reports that 4GW of solar will be added within 2023, as part of a 10GW overall investment.<sup>17</sup>

Precise details are hard to get but, on the basis of the Fitch reports, we extrapolate that the chance of these targets being met is high.

## 4) Targets 50:50

One further issuer, San Miguel Industrias, we classify as 50:50. This is primarily due to a lack of data.

### San Miguel Industrias

San Miguel (ticker SMIPET), a Latin American plastic company, issued its only bond, an SLB (ISIN US79911QAA22), in Jul 2021. The bond set out two KPIs, the percentage of rPET content in preform and thermoforming products and total tons of collected waste. The target on KPI1, rPET usage, was to use 20% at least by 31 Dec 2023. The target on KPI2, total collected waste, was to divert from landfill at least 34,000 tons per annum for the year ending 31 Dec 2023.

Baseline information varies between the documents. The bond prospectus gives a baseline for KPI1 as 10.1% in 2020,

Table 3. SMIPET historic KPI data. Source: SMPIET Sustainability-Linked Bond Framework, accessed 13 Nov 2023.

	rPET usage	collected waste (tons)
2018	9.9%	24,010
2019	10.8%	29,982
2020	9.8%	21,020
2023 Target	20.0%	34,000

<sup>14</sup> Yunnan’s Sustainable Finance Framework sourced from Bloomberg.  
<sup>15</sup> “[Fitch Revises Outlook on Yunnan Energy to Stable; Affirms at ‘BBB-’](#)”, FitchRatings, 9 Aug 2023.  
<sup>16</sup> “[China’s Yunnan adds 750-MW wind power project](#)”, Xinhua, 17 May 2023.  
<sup>17</sup> “[China’s Yunnan province will build 10GW of new solar PV projects](#)”, Enerdata, 1 Mar 2023.

whereas the financing framework uses 10.8% in 2019. For KPI2, the prospectus gives 18.161 in 2020 as a baseline, whereas the financing framework uses 24.010 in 2018. Table 3 gives historical data from the Sustainability-Linked Bond Framework.<sup>18</sup>

According to the data from the financing framework, both KPIs have moved in the wrong direction since the baseline was set. We see no updated data since 2020. The trend might suggest the targets are unlikely to be achieved, but given so much time has passed since the last data, we assign a 50:50 classification to this step-up.

The bond pays a 25bp step-up from Aug 24 to Aug 28, which using the AFII option pricing framework and a probability of 50%, gives a running value of 11.8bp,<sup>19</sup> which will go to 0 or 23.6bp when the results are announced. The lack of data creating such uncertainty on the step-up should drive volatility in the bond pricing, which could be reduced with more ongoing transparency from the issuer.

5) Targets likely to be missed

According to our analysis, two issuers are likely to miss their 2023 targets, Enel and PPC.

Enel, the largest SLB issuer has ten bonds with an observation step-up at the end of 2023. We have analysed these bonds extensively in other papers.<sup>3,4</sup>

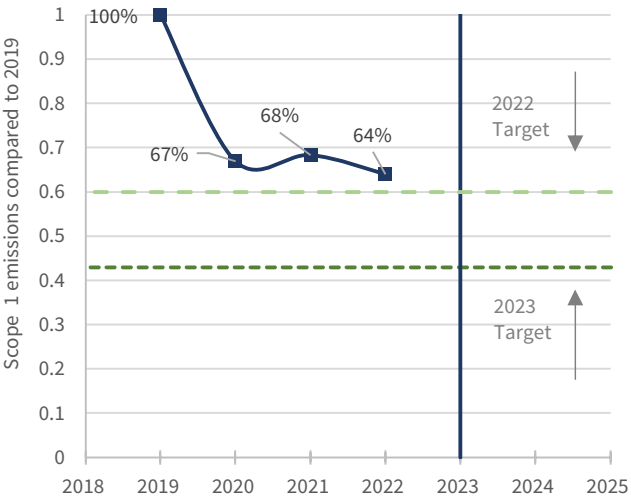
Public Power Corporation

KPI Details

Public Power Corporation, (PPC, ticker PPCGA), rated BB/Stable, is the largest electricity utility in Greece. In 2021 it issued the first SLB from a sub-investment grade issuer in Europe,<sup>20</sup> following up with a second in the same year.<sup>21</sup>

Its first SLB (ISIN XS2314265237) was a 3.875% coupon 5-year bond issued in Mar 2021. Its SPT was observed in Dec 2022, with a targeted 40% reduction in Scope 1 CO<sub>2</sub> emissions compared to the 2019 level. The failure to meet this target was confirmed by the company in Mar

Figure 2. PPC Scope 1 emissions. Source: PPC.



2023, when reporting a figure of 36%.<sup>22</sup> “The 4 percentage points divergence compared to the

<sup>18</sup> “Sustainability-Linked Bond Framework”, SMI, Jul 2021.  
<sup>19</sup> For full details of the option pricing framework please see “An option pricing approach for sustainability-linked bonds”, AFII, 8 Nov 2022.  
<sup>20</sup> “Europe’s first sustainable junk bond draws scrutiny over green impact”, FT, 12 Mar 2021.  
<sup>21</sup> “Public Power Corp raises 500 mln euros from sustainability-linked bond”, Reuters, 14 Jul 2021.  
<sup>22</sup> “Performance Report for the Sustainability-Linked Senior Notes due in 2026”, PPC, 20 Mar 2023.

target is attributed to increased lignite-fired generation in order to safeguard security of supply in the electricity system of Greece due to the energy crisis”.<sup>22</sup> This led to a step-up in the coupon of the bonds by 50bp from 30 Mar 2023.

Its second SLB (ISIN XS2359929812) has a notional of €500mm and matures in 2028, and targets a reduction of 57% in Scope 1 CO<sub>2</sub> emissions from the 2019 baseline by Dec 2023.

Figure 2 shows the trajectory of this KPI. In 2021 there was a small increase in emissions,<sup>23</sup> followed by a decrease in 2022 which was not sufficient to reach the target. A further 21% reduction is needed to achieve the 2023 target.

PPC’s lignite plants, which had been due to close in 2023, have received an extension to the end of 2025.<sup>24</sup> We see no other route to such a significant reduction in Scope 1 emissions, and so anticipate that PPC is likely to miss the 2023 target.

### Bond performance post an SPT miss

PPC 26s was the first index-eligible SLB to miss a target, and be eligible to pay a step-up coupon. It was reported at the time that the miss “[would] not lead to any meaningful changes in [...] its pricing in the secondary market, even though the proportion of ESG-labelled funds owning the bond is about 60%”.<sup>25</sup> Our analysis suggested a lower holding among ESG funds, and therefore a limited price reaction.<sup>26</sup> It has also been reported that the EBRD’s holdings of the bond have supported the security.<sup>27</sup>

Figure 3. PPCGA bond spreads. Source: Bloomberg, accessed 13 Nov 2023.

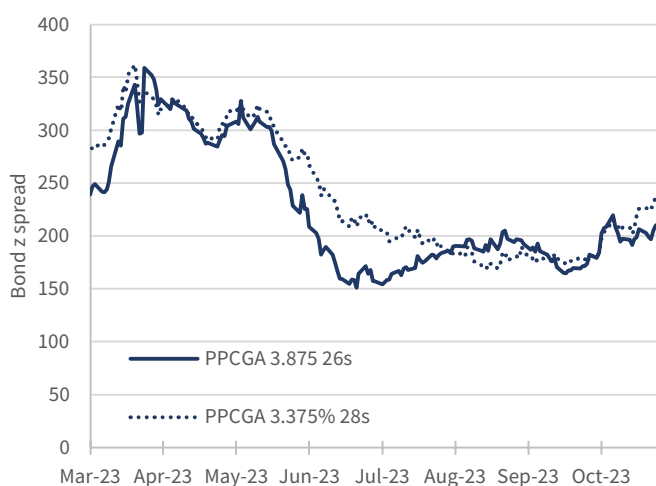


Figure 3 shows historical spreads for PPC bonds after the miss. We note that both are SLBs; when the 26s were confirmed to have missed their target, we would expect the 28s also to be commensurately more likely to miss.

Nevertheless, there was some outperformance of the 26s in Q2, as the step-up was being digested by the market. It seems to have been given back since.

We note a few differing bond characteristics that could create more volatility this time around. The bond in question has a longer maturity, with five years outstanding compared to four the first time around. We calculate in fact an extra 1.5 years of step-up coupon, due to the exact coupon dates. We also note, the starting coupon is lower at 3.375% compared to 3.875%, and so the step-up could be more material.

<sup>23</sup> “[2021 Sustainability Report](#)”, PPC, accessed 13 Nov 2023.

<sup>24</sup> “[Greece delays closure of three coal plant units to 2025](#)”, Balkan Green Energy News, 16 Dec 2022.

<sup>25</sup> “[Impact of PPC’s Failure to Meet Sustainability-Linked Bond Targets Limited](#)”, FitchRatings, 16 Mar 2023.

<sup>26</sup> “[SLB triggers: What next if Nobian or PPC miss their targets?](#)”, AFII, 28 Feb 2023.

<sup>27</sup> “[Limited fallout forecast for bondholders as first index-eligible SLB misses target](#)”, Responsible Investor, 22 Mar 2023.

Alongside the press coverage of the value coming from the Enel step-up,<sup>28</sup> this could drive investors to provide more value to the hedge coming from an increased coupon.

## Conclusions

The SLB market is still sufficiently nascent that SPT observations need careful analysis. Twenty bonds, from ten issuers, have target dates in 2023, making this the most significant observation so far.

Enel, the flagship issuer of SLBs, will likely miss a target on ten bonds. Recent market movements encouragingly suggest investors are valuing the option of the SLB step-up.

PPC, the issuer of the first index-eligible SLB which missed a target in 2022, has a second SLB that will likely miss its target at the end of 2023. The bond in question has a longer maturity, and a lower coupon, which could make the step-up more significant. Despite a reported muted market reaction to the last miss, as the SLB market matures, we watch for signs that investors see value in this step-up coupon as with Enel.

San Miguel Industrias has given investors very little ongoing data to understand its KPI progress. This leaves a high degree of uncertainty around whether its target will be met or not, which may drive price volatility. Providing more transparency for investors around sustainability performance could reduce this.

This has also been an interesting exercise in analysing an older vintage of SLBs. In general, we do think the standard of KPI and SPT selection has improved even in such a short time.

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<sup>28</sup> [“Top Issuer in \\$250 Billion ESG Bond Market Risks Trigger Event”](#), Bloomberg, 20 Oct 2023.



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