20-D-0989

December 14, 2020

JCR's view on Climate Transition Finance

Japan Credit Rating Agency Ltd. started to revise its Green Finance Evaluation Methodology to reflect "Climate Transition Finance Handbook" published by International Capital Market Association (ICMA) on December 10, 2020. JCR also provide a third party opinion on Sustainability Linked Loan and Sustainability Linked Bonds for the entities which have long-term climate transition strategies in accordance with the four elements shown in the Handbook.

The Climate Transition Finance aims to support in a form of Sustainable Finance to "Hard to Abate" sectors which try to reduce GHG emissions in accordance with its long-term climate transition strategies. These sectors are currently facing difficulties in reaching sustainable finance. According to the environment inventory office, CO_2 emissions amounted to 1.1 billion ton in 2018, which has quite serious impacts on global warming.

Prime Minister Suga declared to realize net zero GHG emission by 2050 on October 26, 2020. Reflecting this, various stakeholders started to discuss how to realize the zero carbon society. Huge investment is inevitable to achieve Paris Agreement goals. In Asia, total accumulated investment needs for coping with global warming amounted to about 13trillion JPY in 2020 to 2030. Under such situations, it is difficult to cover all the investment needs with green finance which can be financed to clean technologies such as renewable energy and it is urgent issues to be resolved to accelerate the R&D, realization and spread of low emission technologies on the way of net zero carbon world.

Capital market plays an important roles to enable climate transition by providing efficient finance from investors to issuers who cope with climate change risk. Reflecting such important roles, ICMA launched Climate Transition Finance Working Group on February 2020, where more than 80 stakeholders such as financial institutions, investors and external reviewers joined and finalized the Handbook.

JCR joined this working group and input Japan's stance on transition finance. With such efforts, the Handbook dedicated to deflect various nations efforts on this theme.

Please see the details of Climate Transition Finance related evaluation provided by JCR as follows:

Types and methodologies for Climate Transition Finance

Product Type	Use of Proceeds Type	Sustainability Linked Bonds Type
Evaluation type provided by JCR	Rating and evaluation reports	Third party opinion
Methodology	JCR Green Finance Evaluation Methodology	N.A.
Referred Principles	LMA/APLMA/LSTA Green Loan Principles ICMA Green Bond Principles (2018) ICMA Climate Transition Finance Handbook (2020)	LMA/APLMA/LSTA Sustainability Linked Loan Principle, ICMA Sustainability Linked Bond Principles ICMA Climate Transition Finance Handbook (2020)

Four Key Elements for Climate Transition Finance

1. Issuer's climate transition strategy and governance
Financing Purpose should be for enabling an issuer's climate change strategy. A 'transition' label applied to a debt financing instrument should serve to communicate the implementation of an issuer's corporate strategy to transform the business model in a way which effectively addresses climate-related risks and contributions to alignment with the goals of the Paris Agreement.
2. Business model environmental materiality
The planned climate transition trajectory should be relevant to the environmentally-material parts of the issuer's business model, taking into account potential future scenarios which may impact on current determinations concerning materiality.
3. Climate Transition strategy to be "science-based": including targets and pathways
Issuer's climate strategy should reference science-based targets and transition pathways. The planned transition trajectory should: ・ be quantitatively measurable (based on a measurement methodology which is consistent over time.; ・ be aligned with, benchmarked or otherwise referenced to recognized, science-based trajectories where such trajectories exist; ・ be publicly-disclosed (ideally in mainstream financing filings) include interim milestones, and; ・ be supported by independent assurance or verification.
4. Implementation transparency
Market communication in connection with the offer of a financing instrument which has the aim of funding the issuer's climate transition strategy should also provide transparency to the extent practicable, of the underlying investment program including capital and operational expenditure. This may include R&D-related expenditure where relevant, and details of where any such operating expenditure is deemed to 'non-Business as Usual', as well as other relevant information indicating how this program supports implementation of the transition strategy, including details of any divestments, governance and process changes.

(Source: ICMA Climate Transition Finance Handbook 2020)

JCR is currently revising its JCR Green Finance Evaluation Methodology to incorporate Climate Transition Finance. The revised methodology is expected to be released in January 2020.

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SUSTAINABLE DEVELOPMENT GOALS