PRIVATE CAPITAL

Investing in Sustainable Private Credit

Roundtable Discussion

February 8, 2022

Guy Haselmann, head of thought leadership at MetLife Investment Management, recently sat down with Aurelie Hariton-Fardad, vice president of private credit ESG and corporate private placements, Annette Bannister, head of European infrastructure and Poorvi Dholakia, head of private structured credit to discuss sustainable private assets place in a multi-asset portfolio. A few of the key topics discussed are the role and significance that sustainable investing plays in MIM's origination as well as deal sourcing across geographies and inputs to qualify sustainable metrics. Also discussed was transparency, regulation, and reporting as it relates to a sustainable private asset portfolio.

MetLife Investment Management

***Guy:* When hearing terms like sustainable and private credit are there certain definitions that we should know about?**

Aurelie: Sustainable investing means different things to different people. For MetLife Investment Management we include in sustainable private credit:

- investments that specifically target green or social projects (called green or social private placements);
- financings that include sustainability covenants, which are labeled ESG-linked private placements; as well as;
- industries that we consider as being sustainable, which include infrastructure supporting the transportation, distribution and storage of electricity and water, broadband and mobile infrastructure, renewable energy, low-carbon transport assets, energy efficiency projects, green buildings, and infrastructure for essential services such as healthcare and education, and social housing.

We believe these sectors are essential to a sustainable future and that they will remain resilient in the long term. Our definition of sustainable investment will undoubtedly evolve over time, and it is something that we review continuously to ensure that it remains appropriate.

***Guy:* Are you able to find sustainable deals across most sectors and is there much variability in performance?**

Aurelie: The largest sectors within our sustainable private placements investment portfolio relate to renewable energy and electricity infrastructure, water, and essential services such as healthcare and education, as well as social housing.

As far as the second part of your question, performance is fairly uniform across our portfolio other than maybe a lower correlation to the economic cycle and events such as the Covid-19 pandemic which was reflective of the bias towards infrastructure and essential services. We believe one advantage is that, given the nature of the assets, you can generally achieve longer duration than for a typical private credit portfolio.

***Guy:* How significant is sustainable investing in terms of the role it plays within the whole of MetLife Investment Management's private capital team?**

Aurelie: MetLife Investment Management has been investing in sustainable private credit for many years. As of December 31, 2021, we had $18.3 billion in assets under management in Private Infrastructure, Corporate and Structured Finance Debt. In the last 12 months alone, we originated $4.3 billion in such debt across a range of sectors and geographies.

Annette: We have seen a number of opportunities for sustainable investing in infrastructure, most notably in sectors such as social housing and renewables, but also in some transportation and energy deals. We have seen the emergence of more deals where if specific, measurable KPIs have been met or not, the coupon rate either decreases or increases respectively, further incentivizing the issuer to ensure sustainability is at the forefront of their operations.

Poorvi: Private structured credit market offers several opportunities for investors to further their ESG-focused investment goals while potentially generating incremental yield. MIM's Private Structured Credit team's ESG-focused investments span across several asset classes including residential solar, Property Assessed Clean Energy (PACE), and low-income housing. During 2021 we initiated investments in commercial-PACE with the goal of generating incremental yield and furthering the sustainability goals for some of our clients. We believe that the commercial PACE sector is well-positioned for continued growth as more states adopt this assessment financing to incentivize commercial property owners and developers to make energy-efficient investments in their properties. During the year, we also originated a debt bond backed by a large, diversified pool of low-income housing assets.

Aurelie: In the corporate space, green and ESG issuance represented approximately two-thirds of sustainable origination in 2021 with the bulk of that being issues that support green projects. These are typically issued under a green bond framework, with external oversight to help ensure that the projects that are being financed with our debt meet sustainability standards. By way of examples, we did a few deals with property funds to finance green projects, usually centered around greater energy efficiency of their buildings. We also did a couple of deals for European rail lessors that were green bonds and where the proceeds go towards electric railcars.

Guy: **Where do you expect to see the bulk of new sustainable issuance in 2022? Has the landscape significantly changed in recent years given global governmental efforts on climate change?**

Annette: We expect the number of sustainability-linked deals to increase as issuers seek to attract capital that is focused in this area, whilst giving them an economic benefit for meeting stated goals. Renewable energy deals will likely continue to be highly sought after in the investment community and we believe discipline will be required to ensure financing structures remain robust in an environment where demand for assets is high. Other sectors such as transportation and utilities will also likely seek to issue green or sustainability-linked bonds by carving out specific projects for financing which demonstrate strong ESG characteristics.

Aurelie: We expect green and ESG-linked financings will likely represent a bigger share of the market over time as companies and sponsors articulate their ESG objectives and targets and explicitly link new financings to those objectives. Essential services, especially healthcare, are also expected to see further issuance as is the energy sector, where transition should support financing needs.

Poorvi: Within Private Structured Credit we expect ESG-friendly transactions to grow in volume amid increased investor focus. Residential solar loan and lease transactions have received strong investor support especially after demonstrating solid credit performance during the COVID-crisis. We feel the performance reflects the credit quality of the receivables and robust transaction structures. We believe Solar ABS issuance volume will continue to grow in 2022. In addition, while C-PACE is a relatively new asset class, it is garnering a significant amount of investor interest. We expect accelerated issuance volume in 2022 which will be met by strong investor demand.

Guy: **Are you concerned about greenwashing?**

Aurelie: Absolutely. Green and ESG labels have sometimes been used in circumstances where companies were focused on activities that, in our view, were not that sustainable. Our approach has been to focus on how our financing is used as well as the overall ESG strategy of the company or project we are financing. There should not be significant disparities at that level. We would usually expect meaningful improvements being targeted and facilitated by our financing. We find that communicating that early in the process helps ensure alignment and that minimum standards are met.

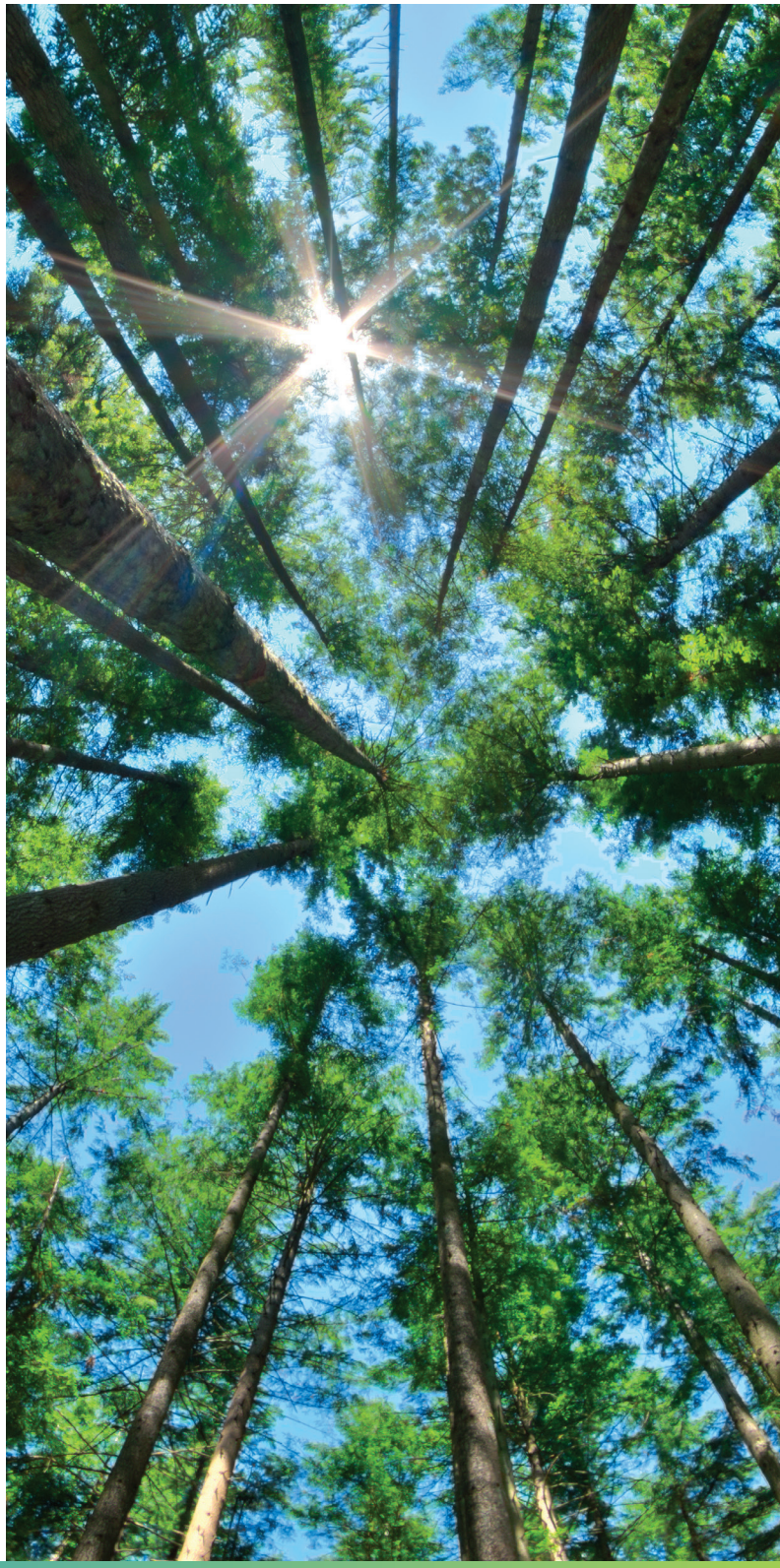
Annette: Greenwashing is a concern, and as an investment community we need to ensure that sustainably linked financings have real, measurable, stretch targets for improvement from the current position.

Guy: **What are the implications of regulatory changes in relation to sustainability?**

Aurelie: New regulations will require the disclosure of a specific set of ESG data on an investor's portfolio. For investors based in the European Union, there is the Sustainable Finance Disclosure Regulation (SFDR), which requires disclosure on more than 15 data points across environmental, governance and social factors. A few other countries, including the UK and Switzerland, are aligning themselves with the recommendations of the Task Force on Climate-Related Finance Disclosures (TCFD), which focuses on environmental factors. The main difficulty for private lenders is the availability of data. Whereas public investors can source most of the data from vendors, we've found coverage to be very low for private companies and projects. Working with companies and sponsors is one way to increase coverage, as is using estimates.

Annette: From the conversations that we have had with our sponsors, it's clear that the commitment to ESG and the desire to report on KPIs is there. However, as we stand here today there is no clear benchmark or consistent reporting standards required across the industry. Therefore, we believe the introduction of regulation requiring reporting on a standard set of data will even the playing field and make the data easier to collect, publish and follow, and allow investors the ability to compare information across their entire portfolios. Over time we expect reporting on ESG data will become a standard requirement and sponsors will be keen to provide this information, knowing that it is important for their underlying investors as well as the financing community.

Guy: **Thank you for sharing your thoughts on this topic.**



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We are institutional, but far from typical.

For more information, visit: investments.metlife.com/private-placement-debt

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