

more
than
money



2016 EQUATOR PRINCIPLES *Report*

1 October 2015 – 30 September 2016



About NAB

National Australia Bank Limited (“NAB”) is a financial services organisation that provides a comprehensive and integrated range of banking and financial products and services including wealth management. NAB has operations based in Australia, New Zealand, the United Kingdom, North America and Asia.

NAB’s financial year

NAB’s financial year (FY) is the reporting period commencing 1 October and ending 30 September. All data in this report is as at 30 September 2016, ie. FY16.

About the Equator Principles

NAB has been a signatory to the Equator Principles¹ (“EP”) since October 2007 and we take EP requirements into consideration when lending for the purpose of financing specific projects.

NAB’s project finance portfolio

NAB’s global project finance portfolio helps large customers to invest in infrastructure, energy and resources projects.

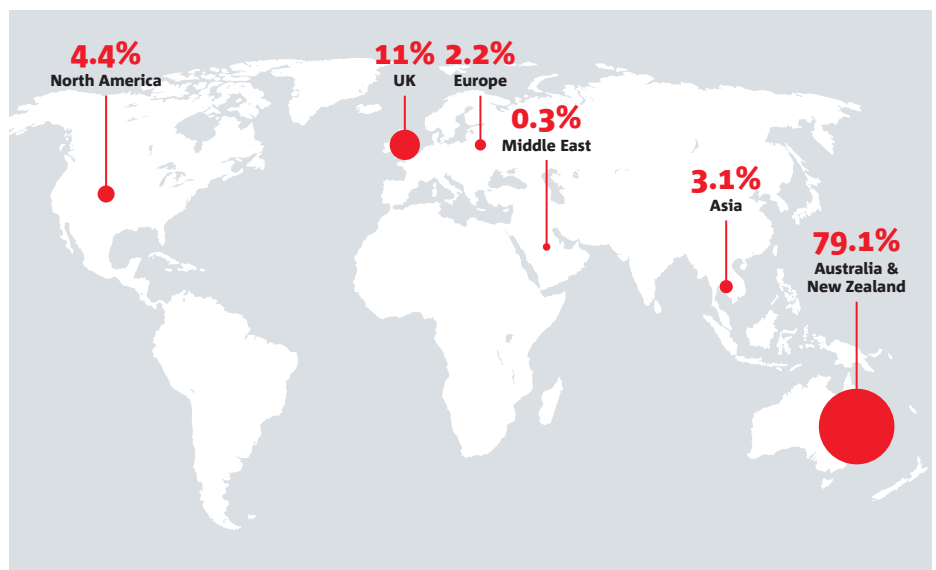
In FY16:

- Project finance represented 1.4% of total Group Exposure at Default (EAD)² at 30 September 2016. Of this lending, 96.6% of projects were in designated countries³ and 3.4% were in non-designated countries.
- We closed 16 new project finance transactions, refinanced 22 existing deals, and removed 13 deals from our loan book.
- Although transactions can be declined at any stage in negotiation or due diligence, none were declined during the 2016 reporting period specifically on the basis of environmental or social risk issues.

Table 1: Total project finance portfolio: Transactions by EP Categories

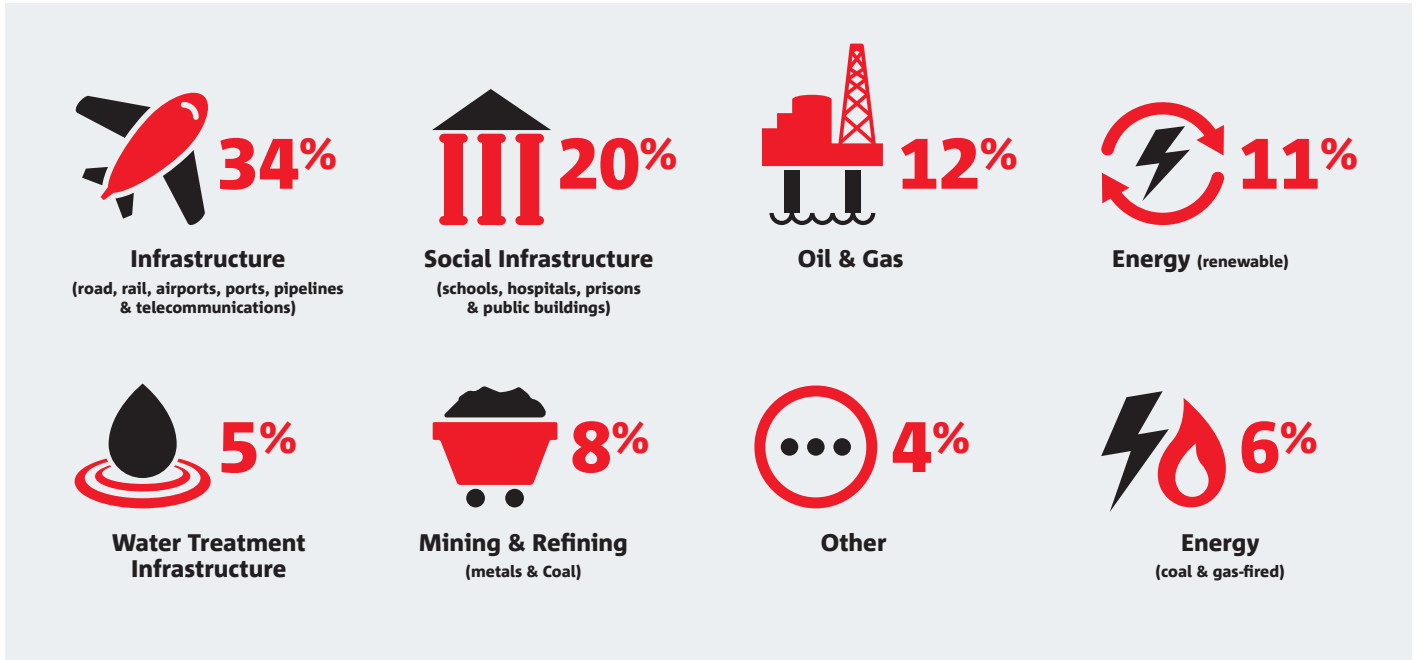
EP category	Number of projects	Projects as a % of total portfolio value
A	4	11
B	49	46
C	21	19
Pre-EP adoption (prior to October 2007)	17	10
Project finance post EPs III to which EPs do not apply	23	14
Total	114	100

Figure 1: Project finance portfolio by region as a % of total portfolio value, expressed as Exposure at Default (as at 30 September 2016)



1. See <http://www.equator-principles.com/> for more information, including the Equator Principles definition of project finance which is used by NAB Group.
 2. EAD is a parameter used in the calculation of economic capital or regulatory capital under Basel II for a banking institution. It is the gross exposure under a lending facility upon default of a customer.
 3. A [list of designated countries](#) is published by the Equator Principles Association. Non-designated countries are those countries not found on the list.

Figure 2: Project finance portfolio by sector as a % of total portfolio value, expressed as Exposure at Default (as at 30 September 2016)



Project finance for energy infrastructure

NAB has provided \$4.9 billion in project finance for renewable energy projects since 2003. We continue to be the leading arranger (by market share)⁴ of project finance to the Australian renewable energy sector.

In 2016, NAB provided \$739 million (measured as EAD at 30 September 2016) for renewable energy projects⁵. Our current global portfolio of renewable energy generation projects represents a total generation capacity of 2,594 megawatts (MW).

In 2012, NAB made a public commitment to continue to make a significant investment in renewable energy through project finance. To continue to build on this commitment, in FY15, NAB set a new commitment to finance \$18 billion over the next seven years (to 30 September 2022) to help our customers undertake climate change mitigation/adaptation activities, e.g. renewable energy generation, energy efficiency (including low carbon property development) and low emission transport.

In addition to providing information on the megawatts of renewable energy generation financed, in FY16 we also estimated⁶ our share of the total Scope 1 and 2 greenhouse gas (GHG) emissions from Australian designated⁷ power generation assets we finance in our PF portfolio. We estimate an amount of 2,655,650 tonnes of carbon dioxide equivalent (tCO₂-e) based on NAB’s participation in financing for each facility as a percentage of debt as at 30 September 2016.

4. Project Finance International 2006-2016 Asia Pacific Initial Mandated Lead Arrangers League Tables Midyear 2016 US\$ Project Allocation, NAB analysis ranking against four major Australian banks – cumulative volume as at 30 June 2016.

5. Amount includes new transactions and re-financing.

6. As these GHG emissions are not generated directly by NAB, we have relied on the public information disclosed by the Australian Clean Energy Regulator, which is information reported by designated generation facilities for the purpose of National Greenhouse and Energy Reporting. Our methodology involved identifying the reported Scope 1 and 2 GHG emissions associated with each generation facility we project finance in Australia. We then multiplied these emissions by NAB’s participation in financing for each facility as % of debt as at 30 September 2016. We then aggregated our share of Scope 1 and 2 GHG emissions to get the total tCO₂-e for the portfolio of power generation assets we project finance in Australia.

7. Designated generation facilities are facilities where the principal activity is electricity generation and where the facility is not part of a vertically-integrated production process. The emissions figure calculated for our project finance portfolio of Australian designated generation facilities covers 96.4% of the Australian power generation assets (measured as MW capacity of the power generation facilities) included in NAB’s project finance portfolio. Data for the remaining 3.6% of assets (measured as MW capacity of the power generation facilities) was not available.

Project finance case studies

NAB provides project finance across a range of sectors. This year's project finance case studies feature examples of finance for renewable energy and social infrastructure projects. These case studies illustrate our implementation of the Equator Principles.

Case study 1 – Renewable Energy Financing

Consistent with our goal to provide \$18 billion of environmental financing activities over the seven years to September 2022, we continue to provide corporate and project finance for renewable energy generation projects. This year our renewables financing included refinancing a portfolio of UK wind and solar farms with project finance and providing corporate finance for the construction of the White Rock Wind Farm.

The UK wind and solar portfolio owned by Cubico Sustainable Investments, was financed in three phases. This is a portfolio of 13 operational wind farms and solar parks principally located in the South West of England and including two solar parks in Scotland. The portfolio has a combined installed generation capacity of 138 MW.

White Rock Wind Farm will be located in northern New South Wales, Australia (500 km north of Sydney). The project received its environmental approvals from Government in July 2012.

The project will be constructed in phases, with phase 1 consisting of around 70 turbines. This is expected to have a generation capacity of around 175 MW. The finance provided by NAB for the White Rock Wind Farm is corporate finance. This triggered the criteria for a Project-Related Corporate Loan under the Equator Principles.

As part of NAB's due diligence and credit risk assessment process environmental and social risks were considered. Environmental issues considered included environmental management planning and systems, climate change mitigation, landscape and visual impact, noise, potential impacts on ecology and biodiversity and land management. Social issues considered included Indigenous and European heritage values, stakeholder engagement planning and processes and occupational health and safety.

The EP assessment resulted in a Category B project designation.

Case study 2 – WA Schools Public Private Partnership

NAB believes financing of social infrastructure is critically important to the standard of living and quality of life in local communities. Therefore, our project finance portfolio includes projects such as hospitals, schools, and social housing.

In 2016, NAB was one of three mandated lead arrangers that jointly arranged finance for a Public Private Partnership (PPP) to fund the design, construction and facilities management by EduWest⁸ of four primary schools to be completed by December 2016 and four Secondary Schools to be completed by December 2022. This is the first-ever WA Schools PPP.

The design of the schools is to be based on ecologically sustainable design principles, with a particular emphasis on reducing energy consumption. The project will have an environmental management plan and system to ensure it achieves required environmental performance standards and minimises the potential for environmental impacts during the construction period. There were no material social issues identified during the project's due diligence and credit risk assessment process.

Overall, this was a project with low environmental and social risk. In fact, this new PPP is considered to have a positive social impact as it will mean the principals and school staff do not have to manage and maintain school facilities, and they will then have more capacity to focus on student learning, support and wellbeing.

The EP assessment resulted in a Category C project designation.

8. EduWest is a consortium of the following organisations – Macquarie Corporate Holdings Limited, Sumitomo Mitsui Banking Corporation and Macquarie Capital (Australia) Limited, Badge Group, Perkins Group and Spotless.

NAB Group's FY16 Equator Principles Data

The total number of project finance transactions that reached Financial Close⁹ in FY16 was 35¹⁰. Of these transactions, 19 were refinancing existing project finance loans, 11 were for brownfield assets which did not trigger the Equator Principles and 5 were for projects which triggered EPs requirements.

In accordance with the reporting requirements of EP III, Table 2 provides a breakdown of our relevant project finance data with respect to the 5 transactions referred to above by sector, region, country type and whether an independent review has been carried out during FY16.

Table 2: Project Finance Data

	Breakdown by Category		
	A	B	C
EP transactions closed during the period 1 October 2015 to 30 September 2016	1	2	2
By Sector	A	B	C
Energy (coal and gas-fired)	0	1	0
Infrastructure (road, rail, airports, ports, pipelines and telecommunication)	0	1	0
Social Infrastructure (schools, hospitals, prisons, public buildings)	0	0	2
Mining and refining (metals and coal)	1	0	0
By Region	A	B	C
Australia & New Zealand	0	1	2
North America	0	1	0
Asia Pacific	1	0	0
By Country type	A	B	C
Designated	0	2	2
Non-designated	1	0	0
Independent Review ¹¹	A	B	C
Yes	1	2	2
No	0	0	0

In accordance with the reporting requirements of EP III, Table 3 provides project name reporting for transactions which reached financial close in FY16.

Table 3: Project Finance Project Name Reporting

Project Name	Calendar Year	Sector	Name of Host Country
Australian National University Student Accom.	2016	Social Infrastructure	Australia
Western Australia Schools PPP	2015	Social Infrastructure	Australia
Westconnex New M5	2015	Infrastructure	Australia
Oyu Tolgoi	2015	Mining and refining	Mongolia
Towantic Energy Center	2016	Energy (coal and gas-fired)	USA

9. Defined in the EPs as "the date on which all conditions precedent to initial drawing of the debt have been satisfied or waived".

10. This is the total for new and refinanced deals regardless of whether the EPs apply.

11. Conducted in accordance with Principle 7 – Independent Review.

There was one Project-Related Corporate Loan (as defined in the EP) that reached Financial Close during the period 1 October 2015 to 30 September 2016 to which EP applied. Data on this Project-Related Corporate Loan is provided in Table 4.

Table 4: Project-Related Corporate Loan Data

	Breakdown by Category		
	A	B	C
EP transactions closed during the period 1 October 2015 to 30 September 2016	0	1	0
By Sector	A	B	C
Energy (renewable)	0	1	0
By Region	A	B	C
Australia & New Zealand	0	1	0
By Country type	A	B	C
Designated	0	1	0
Independent Review	A	B	C
	0	0 ¹²	0

The number of Project Finance Advisory Services (as defined in the EP) mandated during the period from 1 October 2015 to 30 September 2016 was 11. A breakdown is shown in Table 5.

Table 5: Project Finance Advisory Services

By Sector	Number of Services mandated
Energy (renewable)	5
Water treatment infrastructure	3
Waste management	1
Other	2
By Region	Number of Services mandated
Australia & New Zealand	11

12. In accordance with EP Principle 7, NAB determined that an Independent Review was not required. Internal review of the project was deemed sufficient and undertaken by NAB.

Personnel involved in PF transactions

Project finance is managed through NAB's Specialised Finance team and supported by our in-house Technical Services Group (TSG) and Credit groups. From time to time, our Sustainability Governance & Risk (SG&R) team also provides support on specific Environmental, Social and Governance (ESG) risk issues.

EP implementation

NAB recognises that businesses today operate in an environment which includes many environmental and social challenges that affect our economy and society. These include issues such as human rights, climate change and natural capital loss and degradation. To assist in managing these issues, NAB has a set of **ESG Risk Principles** which provide an overarching framework for integrating ESG risk considerations into our day-to-day decision-making.

NAB considers exposure to ESG risk at both a lending portfolio and an individual client level. At the client level, ESG risk is assessed on a case-by-case basis as part of the credit risk assessment and due diligence process. This includes our assessment of ESG risks associated with particular sectors.

In addition to NAB's general credit risk policies and practices, NAB has a specific credit policy that addresses implementation of the EP. During the credit risk assessment process for corporate and institutional lending, it is our practice to identify potential corporate finance transactions where the EP could apply. NAB's 'Group Credit Policy Manual' (the database for Group credit risk policy) was reviewed and updated accordingly to reflect EP III.

Our TSG team is required to ensure the EP are applied as required for financing of projects. This includes categorisation (A, B or C) of projects.

For project finance transactions, a tailored due diligence is undertaken as required by our general credit policies. For all project finance transactions, a TSG member is allocated to the transaction prior to the commencement of due diligence. The frontline team, in conjunction with TSG will agree the technical, environmental and social scope of work, the requirements for site visits during the due diligence process, and the selection of independent experts/consultants.

Independent environmental and social experts are used to assist TSG, where applicable, and in accordance with the EP.

Where there are potentially controversial issues or significant ESG risks associated with a potential project finance transaction, the SG&R team may also review material relevant to a transaction after referral from either the frontline Specialised Finance team, Credit group or TSG.

As project-related lending usually involves a syndicate of banks, it is NAB's general experience that there is usually consensus reached amongst the bank group on the project category assignment, and in most cases, a conservative approach is taken.

When potential projects occur in **non-designated countries** (defined in EP III), this includes applying **IFC Performance Standards**¹³. Standards 5 (Land Acquisition and Involuntary Resettlement) and 7 (Indigenous Peoples) are particularly relevant, when we review how our clients are managing the issue of land rights and impacts on local communities.

Loan document covenants are reviewed by the Specialised Finance frontline team, NAB Legal, and where appropriate TSG. Standard facility agreements typically contain covenants sufficient to satisfy the EP covenant requirements – where necessary these are amended on a case-by-case basis.

TSG is tasked with tracking a project's compliance with the EP. This includes seeking client consent for Project Name reporting. Client consent requests are tracked, recorded and held in a central location.

Monitoring ongoing EP compliance

NAB undertakes an annual review of every PF transaction. This includes targeted site visits by our frontline team, TSG, and independent monitoring where necessary (generally during construction and operations for complex and/or Category A projects). We also require general construction, operational and compliance reporting from the client. The frequency and scope of this reporting is based on the risk associated with a project. A higher risk project typically requires more frequent reporting so we can check that it is being developed in accordance with project approvals, project documents and any additional requirements of NAB's banking team/TSG.

Reporting to management

NAB's executive committee and board of directors receive reports on NAB's lending book exposure to a list of industry sectors with potentially higher ESG risk sensitivities (as designated by NAB internally), such as mining and energy generation. This reporting includes PF lending. NAB also monitors the carbon intensity of its PF energy generation portfolio as part of internal management reporting.

Assurance over our PF data

On an annual basis, NAB has key PF data reviewed by an independent audit firm. In FY 16, this assurance was provided by KPMG. **KPMG provided assurance** over PF by sector as a proportion (%) of total PF portfolio value, expressed as EAD, for the year ended 30 September 2016.

Further information on the Equator Principles can be found at www.equator-principles.com

13. See http://www.ifc.org/wps/wcm/connect/topics_ext_content/ifc_external_corporate_site/ifc+sustainability/our+approach/risk+management/performance+standards/environmental+and+social+performance+standards+and+guidance+notes