

SECOND PARTY OPINION (SPO)

Sustainability Quality of the Issuer and Green Bond Asset Pool

AFRICA FINANCE CORPORATION
14 September 2020

VERIFICATION PARAMETERS

Type(s) of instruments contemplated	<ul style="list-style-type: none">• Green Bond
Relevant standards	<ul style="list-style-type: none">• ICMA Green Bond Principles
Scope of verification	<ul style="list-style-type: none">• Africa Finance Corporation's Green Bond Framework (as of 09.2020)• Africa Finance Corporation's Green Bond Portfolio (as of 26.08.2020)
Lifecycle	<ul style="list-style-type: none">• Pre-issuance verification
Validity	<ul style="list-style-type: none">• For a single issuance after SPO publication

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Overall Evaluation of the Green Bond

Africa Finance Corporation (AFC) commissioned ISS ESG to assist with its Green Bond by assessing three core elements to determine the sustainability quality of the Bond:

1. AFC's Green Bond framework – benchmarked against the International Capital Market Association's (ICMA) Green Bond Principles (GBPs).
2. The asset pool – whether the projects aligned with ISS ESG's issue-specific key performance indicators (KPIs) (See Annex 2).

ISS ESG ASSESSMENT SUMMARY

SPO SECTION	SUMMARY	EVALUATION ¹
Part 1: Performance against GBPs	The issuer has defined a formal concept for its Green Bond regarding use of proceeds, processes for project evaluation and selection, management of proceeds and reporting. This concept is in line with the ICMA GBPs.	Positive
Part 2: Sustainability quality of the asset pool	The overall sustainability quality of the asset pool in terms of sustainability benefits, risk avoidance and minimisation is good based on the ISS ESG Green Bond KPIs. The Green Bond KPIs contain a clear description of eligible asset categories which include: wind energy and hydroelectric energy. All assets of the asset pool are located in developing countries (Ivory Coast, Cape Verde, Djibouti). Risks potentially relate to adverse social, environmental and governance impacts in financed activities despite these being actively mitigated by the issuer.	Positive
Part 3: Issuer indicative sustainability performance	The issuer intends to secure a full ESG Corporate Rating in the near term. The Corporate Rating will be communicated by the issuer	Not applicable

¹ ISS ESG's present evaluation will remain valid until any modification of the Green Bond Framework or addition of new assets into the asset pool by the issuer. The controversy check of the underlying assets has been conducted on the 03.09.2020





Contribution of the Green Bond to the UN SDGs

Based on the assessment of the sustainability quality of the green bond asset pool and using a proprietary methodology, ISS ESG assessed the contribution of AFC's green bond to the Sustainable Development Goals defined by the United Nations (UN SDGs).

This assessment is displayed on a 5-point scale (see Annex 2 for methodology):

Significant Obstruction	Limited Obstruction	No Net Impact	Limited Contribution	Significant Contribution
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Each of the bond's Use of Proceeds categories has been assessed for its contribution to, or obstruction of, the SDGs:

USE OF PROCEEDS	CONTRIBUTION OR OBSTRUCTION	SUSTAINABLE DEVELOPMENT GOALS
Wind Power	Significant Contribution	 
Hydroelectric Power	Limited Contribution	 

ISS ESG SPO ASSESSMENT

PART I: GREEN BOND PRINCIPLES

1. Use of Proceeds

The net proceeds raised from the AFC Green Bonds will be allocated to finance (or refinance) eligible projects as outlined below. Eligible projects will contribute to one or more of the high-level objectives of the Green Bond Principles.

Selected eligible green projects are shown below:

AFC Sector	ICMA GBP	Example projects
Power	Renewable Energy	Installation of wind farms to support energy independence, displacing liquid fuel plants.
		Hydroelectric power plants to increase power capacity and reduce generation costs.
		Solar power projects encompassing production, transmission and maintenance.
Transport & Logistics	Clean transportation	Clean transportation such as electrification of public transport and railways as well as transportation such as toll roads that decongest urban cities and reduce commuting time.

Opinion: ISS ESG considers the Use of Proceeds description provided by AFC's Green Bond Framework as complete and aligned with the GBPs. Environmental benefits associated with the use of proceeds category are described.

2. Process for Project Evaluation and Selection

AFC's definition of a Green Project

AFC defines green projects as any mitigation or adaptation project that focuses on reducing carbon emissions or increasing resilience. Examples of the types of projects AFC considers eligible include the following:

- Energy Generation and Access through renewable energy sources (solar, hydro and wind);
- New transport technologies, including the use of alternative fuels, more efficient engines, and electric and hybrid technologies. More sustainable approaches to urban transport and infrastructure planning can have a huge impact on future emissions trajectories;
- Reducing emissions from deforestation and forest degradation;
- Energy efficiency and the adoption of lower emission sources of energy for industries;
- Efforts to reduce emissions from energy, transport, and cities and the creation of resilient infrastructure systems such as integrated water supply systems.

Selection Process

All projects under consideration for green bond financing undergo an assessment process on the basis of the AFC Investment Policy which includes consideration with regards to a) Efficiency and effectiveness: this reflects economic potential / bankability of the project b) Impact potential: this reflects the level of impact with regards to reducing emissions or increasing resilience; and c) Sustainable development potential: this reflects the wider long-term development impact as it relates to E&S, gender etc.

Examples of some of the SDGs that may be addressed include SDG 7 (Affordable and Clean Energy), SDG 13 (Climate Action), SDG 8 (Decent Work and Economic Growth) and SDG 9 (Industry, Innovation and Infrastructure).

Phase 1: A project is identified as being green (in accordance with the definition above) at the origination stage

Phase 2: Green projects are appraised in accordance with AFC's internal investment process

Phase 3: Approved projects will become eligible for inclusion in the Green Bond program

Phase 4: If there is a need to replace any project on the list of potential projects, AFC may change it and find a substitute project that meets the eligibility criteria.

Opinion: *ISS ESG considers the Process for Project Evaluation and Selection description provided by AFC's Green Bond Framework as complete and aligned with the Green Bond Framework. Moreover, the issuer has established a structured process to determine that projects fit within defined categories, reflecting good market practices.*

3. Management of Proceeds

Every project under the Green Bond Program is subject to AFC's portfolio monitoring under AFC's Investment Policy. AFC's portfolio management approach includes control and monitoring of disbursements, operation status and contractual compliance, client and operation credit risk. In addition, disbursements for projects under the Green Bond Program are monitored by the Assets and Liability Committee (ALCO) in order to ensure the proper use of the Green Bond proceeds.

AFC intends to allocate the proceeds from green debt financing instruments to a portfolio of Eligible Projects, selected in accordance with the use of proceeds criteria and project evaluation and selection process presented above. AFC intends to allocate the proceeds within a year.

AFC will endeavor to achieve a level of allocation for the eligible green project portfolio which matches the balance of net proceeds from its outstanding green debt financing instruments. Additional eligible green projects will be added to the issuer's eligible green project portfolio to the extent required to ensure that the net proceeds from outstanding green debt financing instruments will be allocated to eligible green projects.

Any unallocated proceeds will be earmarked and held as cash or in AFC's Treasury Liquidity Portfolio pending investment in Eligible Projects in accordance with ICMA's Green Bond Principles.

Green Bond Program Proceeds Monitoring

The net proceeds from any AFC Green Bond issuances will be managed within AFC's treasury liquidity portfolio ahead of distribution to the eligible projects selected. For the duration of the Green Bond's life, AFC will track the outstanding balance of the net proceeds and reconcile against allocations made to eligible green projects

over the time horizon. AFC will manage any unallocated proceeds from green bond issuances in accordance with the Green Bond Principles. A selected project can be in one of the following three stages:

- i) New projects that have been approved and meet all the requirements in order to start the disbursement period;
- ii) Projects that are already in the disbursement period;
- iii) Projects that have finished receiving disbursements and are either in their grace period or have begun to amortize, but still have a relevant amount in AFC's portfolio pending amortization.

Given that every individual project selected for the program has different characteristics including tenor, disbursement period, grace period and amortization schedule, cashflow mismatches when compared to the characteristics of the bonds are common.

Opinion: *ISS ESG finds that Management of Proceeds proposed by AFC is well aligned with the GBPs as the green bond proceeds will be tracked in an appropriate manner by the issuer. Additionally, AFC has established a procedure in case of divestment or postponement, reflecting best market practices.*

4. Reporting

AFC will provide investors with reporting on the allocation of proceeds until proceeds have been fully allocated and the impact of eligible green projects on an annual basis for the duration of the Green Bonds. Data will be collected and reported at the project level using a data collection tool developed by the AFC and facility documents will include contractual clauses for annual ESG and Development Impact reporting to AFC.

Allocation Reporting

The allocation report provides:

- The total amount of investments in the Eligible Green Projects Portfolio
- The amounts of new and existing projects
- The balance of unallocated proceeds

Impact Reporting

AFC will report on the environmental impact of the projects funded with the Green Bonds proceeds or refer to existing sustainability reporting (within or outside of the Annual Report). Listed below are potential environmental impact indicators.

Potential Impact Indicators:

- Annual additional energy capacity (kW)
- Annual GHG emissions avoided (tons of CO₂e)
- Capacity of renewable energy plant(s) built or rehabilitated (MW)
- Passenger-kilometres (i.e. the transport of one passenger over one kilometre) and/or passengers; or tonne kilometres (i.e. the transport of one tonne over one kilometre) and/or tonnes
- Annual GHG emissions reduced/avoided in tCO₂-e p.a.
- Annual Greenhouse Gas (GHG) emissions reduced or avoided (tCO₂e). Depending on the type of project, a relevant GHG emission factor will be applied to activity data, such as: annual energy savings (MWh) or annual renewable energy produced (MWh)
- Minimum energy efficiency improvement achieved (%)

Each report will be prepared and reviewed by the Investments and E&S teams and approved by the Chief Investment Officer and the Chief Risk Officer (or their designates). The reports will be able to view on our website www.africafc.org.

Opinion: *ISS ESG finds that the reporting proposed by AFC is in line with industry best practices. AFC has established a detailed allocation and impact reporting, and selected detailed impact indicators, reflecting best market practices.*

External review

AFC has appointed ISS ESG as an independent assurance provider to provide a second party opinion on this green finance framework pre-issuance and to annually assure the process used in financing of Eligible Projects in accordance with this framework.

This second party opinion will be made publicly available on [AFC website](#).

PART II: SUSTAINABILITY QUALITY OF THE ASSET POOL

Wind Energy (Onshore)

As a Use of Proceeds category, wind energy has a significant contribution to SDG 7 “Affordable and clean energy” and SDG 13 “Climate action”.

The table below presents the findings of an ISS ESG assessment of the assets (re-) financed against KPIs.

ASSESSMENT AGAINST ISS ESG KPI'S

Site selection

- ✓ 100% of assets are not located in key biodiversity areas (Ramsar sites; IUCN protected areas I-IV).
- ✓ 100% of assets underwent an environmental impact assessment at the planning stage.
- ✓ 100% of assets feature community dialogue as an integral part of the planning process (e.g. sound information of communities, community advisory panels and committees, surveys and dialogue platforms, grievance mechanisms and compensation schemes).

Environmental aspects of construction and operation

- ✓ 100% of assets meet high environmental standards during the construction phase (e.g. noise mitigation, minimisation of environmental impact during construction work).
- ✓ 100% of assets provide for measures to protect habitat and wildlife during operation of the power plant (e.g. measures to protect birds and bats).
- ✓ 100% of assets are based in countries that provide for high labour and health and safety standards for construction and maintenance work (e.g. ILO core conventions).

Controversy assessment

ISS ESG conducted a controversy assessment, and no controversy erupted that could be attributed to the issuer.

Hydro Power

As a Use of Proceeds category, hydro power has a limited contribution to SDG 7 “Affordable and clean energy” and SDG 11 “Climate action”.

The table below presents the findings of an ISS ESG assessment of the assets (re-) financed against ISS ESG KPIs.

ASSESSMENT AGAINST ISS ESG KPI

Site selection

- ✓ The asset is not located in key biodiversity areas (Ramsar sites). However, 30 species in the area of the project have a special status on the IUCN and Aké-Assi lists.
- ✓ The asset underwent an environmental impact assessment at the planning stage.
- ✓ The asset featured community dialogue as an integral part of the planning process (e.g. sound information of communities, community advisory panels and committees, surveys and dialogue platforms, grievance mechanisms and compensation schemes).

Environmental aspects of construction and operation

- ✓ 100% of assets meet high environmental standards during the construction phase (e.g. noise mitigation, minimisation of environmental impact during construction work).
- ✓ Compensation for disturbed economical activities are put in place.
- ✓ The asset provides some measures to protect habitat and wildlife during operation of the power plant (e.g. management of erosion risks, sediment management, environmental flow management).

Working conditions during construction and maintenance work and dam safety

- The asset does not provide for high labour and health and safety standards for construction and maintenance work (e.g. ILO Core Conventions).
- ✓ 100% of assets provide for high dam security (management of dam security, monitoring, inspections, emergency plans, etc).

Controversy assessment

A controversy assessment was conducted on the asset and revealed no controversy that could be attributed to the issuer.

PART III: ASSESSMENT OF AFC'S ESG PERFORMANCE

The issuer intends to secure a full ESG Corporate Rating in the near term. The Corporate Rating will be communicated by the Africa Finance Corporation

DISCLAIMER

1. Validity of the SPO: For AFC's first issuance following the SPO release date.
2. ISS ESG uses a scientifically based rating concept to analyse and evaluate the environmental and social performance of companies and countries. In doing so, we adhere to the highest quality standards which are customary in responsibility research worldwide. In addition, we create a Second Party Opinion (SPO) on bonds based on data from the issuer.
3. We would, however, point out that we do not warrant that the information presented in this SPO is complete, accurate or up to date. Any liability on the part of ISS ESG in connection with the use of these SPO, the information provided in them and the use thereof shall be excluded. In particular, we point out that the verification of the compliance with the selection criteria is based solely on random samples and documents submitted by the issuer.
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ANNEX 1: Methodology

ISS ESG Green KPIs

The ISS ESG Green Bond KPIs serves as a structure for evaluating the sustainability quality – i.e. the social and environmental added value – of the use of proceeds of AFC’s Green Bond.

It comprises firstly the definition of the use of proceeds category offering added social and/or environmental value, and secondly the specific sustainability criteria by means of which this added value and therefore the sustainability performance of the assets can be clearly identified and described.

The sustainability criteria are complemented by specific indicators, which enable quantitative measurement of the sustainability performance of the assets and which can also be used for reporting. Those indicators may be tailor-made to capture the context-specific environmental and social risks.

To review the KPIs used in this SPO, please contact Federico Pezzolato (details below) who will send them directly to you.

Asset evaluation methodology

ISS ESG evaluates whether the assets included in the asset pool match the eligible project category and criteria listed in the Green Bond KPIs.

All percentages refer to the amount of assets within one category (e.g. wind power). Additionally, the assessment “no or limited information is available” either indicates that no information was made available to ISS ESG or that the information provided did not fulfil the requirements of the ISS ESG Green Bond KPIs.

The evaluation was carried out using information and documents provided to ISS ESG on a confidential basis by AFC (e.g. Due Diligence Reports). Further, national legislation and standards, depending on the asset location, were drawn on to complement the information provided by the issuer.

Assessment of the contribution and association to the SDG

The 17 Sustainable Development Goals (SDGs) were endorsed in September 2015 by the United Nations and provide a benchmark for key opportunities and challenges toward a more sustainable future. Using a proprietary method, ISS ESG identifies the extent to which AFC’s Green Bond contributes to related SDGs.

ANNEX 2: Quality management processes

SCOPE

AFC commissioned ISS ESG to compile a Green Bond SPO. The Second Party Opinion process includes verifying whether the Green Finance Framework aligns with the ICMA GBPs and to assess the sustainability credentials of its Green Bond as well as the issuer's sustainability strategy.

CRITERIA

Relevant Standards for this Second Party Opinion

- ICMA GBPs
- ISS ESG KPI set: Wind Energy and Hydro Energy

ISSUER'S RESPONSIBILITY

AFC's responsibility was to provide information and documentation on:

- FW
- Asset pool
- Documentation of ESG risks management at the asset level

ISS ESG'S VERIFICATION PROCESS

ISS ESG is one of the world's leading independent environmental, social and governance (ESG) research, analysis and rating houses. The company has been actively involved in the sustainable capital markets for over 25 years. Since 2014, ISS ESG has built up a reputation as a highly-reputed thought leader in the green and social bond market and has become one of the first CBI approved verifiers.

ISS ESG has conducted this independent Second Party Opinion of the Green Bond to be issued by AFC based on ISS ESG methodology and in line with the ICMA GBPs.

The engagement with AFC took place in September 2020.

ISS ESG'S BUSINESS PRACTICES

ISS has conducted this verification in strict compliance with the ISS Code of Ethics, which lays out detailed requirements in integrity, transparency, professional competence and due care, professional behaviour and objectivity for the ISS business and team members. It is designed to ensure that the verification is conducted independently and without any conflicts of interest with other parts of the ISS Group.

About ISS ESG SPO

ISS ESG is one of the world's leading rating agencies in the field of sustainable investment. The agency analyses companies and countries regarding their environmental and social performance.

As part of our Sustainable (Green & Social) Bond Services, we provide support for companies and institutions issuing sustainable bonds, advise them on the selection of categories of projects to be financed and help them to define ambitious criteria.

We assess alignment with external principles (e.g. the ICMA Green / Social Bond Principles), analyse the sustainability quality of the assets and review the sustainability performance of the issuer themselves. Following these three steps, we draw up an independent SPO so that investors are as well informed as possible about the quality of the bond / loan from a sustainability perspective.

Learn more: <https://www.isscorporatesolutions.com/solutions/esg-solutions/green-bond-services/>

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