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Reliance Rail states its ESG ambition by combining green loan with SLL

Reliance Rail says the addition of sustainability-linked features to its green loan will help it achieve environmental goals beyond its existing asset pool, such as energy consumption targets and emissions reduction. Any margin savings will be directed to sustainability improvements rather than reducing funding costs, which the borrowers says is a distinguishing feature of its facility.

Reliance Rail announced the A$1.8 billion (US$1.3 billion), 21-year green sustainability-linked loan (SLL) on 1 March – a first for an Australian private public partnership (PPP).

Climate Bonds Initiative (CBI) certifies the transaction as a green loan under its low-carbon transport criteria, and the structure adds a sustainability-linked structure to the use of proceeds (UOP) facility. BNP Paribas, Commonwealth Bank of Australia (CBA) and National Australia Bank acted as joint sustainability coordinators, while DNV provides verification and second-party opinions.

The SLL has four sustainability performance targets (SPTs), which includes the cornerstone target of Infrastructure Sustainability Council (ISC) operations rating score. The other three SPTs relate to the energy intensity of Reliance Rail's maintenance centre and trains, solar PV installation and operational water consumption.

Louise Iida, chief financial officer at Reliance Rail in Sydney, says the ISC score is the SPT with the greatest potential for margin benefit. The company believes it will drive sustainability improvement across the business.

Borrower and lenders are not disclosing further details of the SPTs or the loan's pricing incentives. Iida says the SPTs are structured to become progressively more ambitious over the first 10 years of the loan and to incentivise the company to meet targets as early as possible.

She adds that a structure like this demonstrates that mature public-private partnerships (PPPs) can still drive sustainability enhancements through innovative financing. "Older PPPs such as ours may not have been structured with sustainability improvement in mind. But our partners have welcomed this proactivity as they were also looking for opportunities to collaborate," Iida says.

Reliance Rail is a PPP with the New South Wales government, established in 2006 to design, manufacture and maintain passenger trains. Its core assets are its 78 Waratah trains – which account for about a third of Sydney Trains' suburban passenger sets – and the Auburn Maintenance Centre (AMC). This is a purpose-built facility that maintains more than 60 per cent of Sydney Trains' passenger fleet. Having procured the trains and built AMC, Reliance Rail is in the maintenance phase of its contract in collaboration with Downer EDI Rail.

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LOUISE IIDA RELIANCE RAIL

Borrower ambition

The green SLL refinances all Reliance Rail's existing bank debt until the rolling stock PPP project expires in 2044. The borrower has been considering the use of a green label for this financing for some time, Iida reveals.

"We really liked the idea of issuing green debt but had to consider what the label alone would accomplish if the margin benefit could not be quantified," she says. "Our assets already qualify as green and we could label the debt as such, but we wanted to find a way for it to contribute to future improvement."

The deal potentially paves the way for corporate borrowers to issue UOP debt instruments that incorporate sustainability-linked features, Madeleine Harmer, Sydney-based senior associate, sustainable finance at CBA, suggests.

"We have had a number of conversations with clients about creating holistic sustainability frameworks that are not just green or sustainability-linked but cover a broad universe of green, social and sustainability factors and give them the option to go down multiple sustainable financing pathways," Harmer says.

James Waddell, director, corporate finance at NAB in Sydney, says there is a pipeline of borrowers preparing to execute SLLs. He adds the key factor for entities to take up sustainability-linked products is what data they have available, from which the SPTs are based off.

"Entities need to consider what their key material risks are, what baseline data they have and what they are prepared to commit to in terms of targets to address those risks."

KangaNews understands this is the second green SLL in the Asia-Pacific region following a deal from Brookfield in December last year. There have also been several green, social and sustainability UOP loans for Australian PPPs, including Canberra Metro, Qtectic and Royal Adelaide Hospital.

Iida says Reliance Rail turned its attention turned to the SLL option as the product gathered momentum with other Australian borrowers. "We have a significant portfolio of debt and wanted to leverage it to help achieve our sustainability objectives," she adds. "If we could achieve margin savings by refinancing with a SLL, we could then direct those benefits to funding sustainability initiatives."

Waratah trains have energy-efficient components in place but improvements are still possible over their remaining 30-year operational life, according to Chad Smithies, Sydney-based chief executive officer at Reliance Rail. "The stretch targets and margin savings that follow allow us to apply technology improvements to our assets," he says.

The green SLL fits into the company's sustainability strategy, complementing Sydney Trains' ambitions. "Sydney Trains has a wide portfolio, so having our own sustainability strategy in place – in line with the UN's Sustainable Development Goals – to focus on material issues specific to our assets was imperative," Smithies says.

Chris Ruffa, head of capital markets group at BNP Paribas Australia in Sydney, highlights the ambition behind the decision to add SLL KPIs to a green loan. He tells *KangaNews*: "The SLL was particularly innovative also because it gave effect to ambitious and relevant sustainability objectives beyond Reliance Rail's direct control, which is quite often the biggest challenge for PPP borrowers."

Given the company operates within a contractually regulated environment, Ruffa says the sustainability coordinators concentrated on areas of its ESG [environmental, social and governance] ambition within these confines.

Waddell adds, despite being constrained by its contractual obligations to its government partner, Reliance Rail has gone "above and beyond in making significant reductions in energy and water usage."

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CHRIS RUFFA BNP PARIBAS AUSTRALIA

Identifying SPTs

Understanding the information and data Reliance Rail could obtain from Downer was crucial to determine what was possible in setting targets, Harmer says.

She adds the sustainability coordinators undertook extensive due diligence with ISC and DNV to ensure the cornerstone target was material and ambitious. "Using a rating as an SPT can sometimes be challenging as it can be difficult to determine the true improvement in an asset or company's operations," she explains. "However, in this case, the transparency associated with the ISC rating and its 14 ESG metrics allowed for a credible target."

Reliance Rail's direct emissions profile derives from trains and their maintenance. Harmer says the deal group determined that energy and water intensity metrics per service were the most appropriate to measure the success of the borrower's reduction commitments.

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MADELEINE HARMER COMMONWEALTH BANK OF AUSTRALIA