

KUTXABANK S.A

SOCIAL BOND

FRAMEWORK OVERVIEW AND SECOND-PARTY REVIEW BY SUSTAINALYTICS

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- FRAMEWORK OVERVIEW AND SECOND-PARTY REVIEW BY SUSTAINALYTICS** **0**

- 1. PREFACE** **2**

- 2. FRAMEWORK OVERVIEW** **2**
 - 2.1 Introduction 2
 - 2.2 Kutxabank Social Bond 2
 - 2.2.1 Use of Proceeds 2
 - 2.2.1.1 Eligibility Criteria 2
 - 2.2.2 Management of Proceeds 3
 - 2.2.3 Reporting 4

- 3 SUSTAINALYTICS' OPINION** **5**
 - Conclusion 6

1. PREFACE

Kutxabank has engaged Sustainalytics to review and support its efforts to formulate a framework that can be used to issue a social bond. As part of this engagement, Sustainalytics held conversations with Kutxabank to understand its support for social housing and planned use of proceeds for its social bond; reviewed relevant public and internal documents, and provided its opinion.

This document contains two sections:

- Framework Overview – summary of Kutxabank’s social bond framework;
- Sustainalytics’ Opinion – an opinion on the framework.

2. FRAMEWORK OVERVIEW

2.1 Introduction

Kutxabank is a commercial bank that provides banking and financial services primarily in the Basque region of northern Spain. It offers a range of products and services, such as mortgage and consumer loans; financing for businesses and developers; demand and time savings products; guarantees; and debit and credit cards, and engages in insurance brokerage activities. Kutxabank was officially founded on 1 January 2012 out of the merger of three Basque financial institutions - Bilbao Bizkaia Kutxa (BBK), Gipuzkoa Donostia Kutxa (Kutxa), and Caja Vital Kutxa (Vital).

2.2 Kutxabank Social Bond

Kutxabank is planning to issue a social bond to finance lending activities that support low-income individuals and families with access to adequate accommodation. The bond is a covered bond that leverages Kutxabank’s participation in the Basque government’s Viviendas de Protección Oficial (VPO) programme. The VPO programme provides subsidized housing to low-income individuals in the Basque region. The housing units are dwellings, intended for rent or purchase, with regulated dimensions and prices. The economic benefits are only applicable to specific individuals, therefore requirements such as income, age, and family status of the priority groups are applied.

The following sections summarize Kutxabank’s social bond framework with regards to the use of proceeds, management of proceeds and reporting.

2.2.1 Use of Proceeds

The proceeds of the social bond will be allocated to:

- a. Kutxabank’s existing VPO loans
- b. New loans made under the VPO programme
- c. Construction finance for housing projects to be used for the VPO programme

2.2.1.1 Eligibility Criteria

To be eligible for the social bond proceeds, the mortgages under the use of proceeds (a) and (b) must be issued to individuals or families who meet the following criteria:

- a) Permanent residents of the Basque country; and
- b) Qualify as low income; or
- c) Individuals having special needs such as:
 - a. Reduced mobility and/or a mental handicap;
 - b. Separated or divorced;
 - c. 70 years of age or over; or
 - d. Female victims of gender-based violence.

Kutxabank adheres to the Basque government's VPO programme's definition of low-income, whereby individuals or families must

- a) Earn a weighted income between EUR 3,000 and EUR 39,000 (for applicants intending to rent), or
- b) Earn a weighted income between EUR 9,000 and 50,000 (for applicants intending to purchase)¹; and
- c) Not have owned property in the two years prior to the mortgage application.

Additional details about the Basque government's VPO programme requirements are available on its website [here](#)². Given that the VPO programme is contingent on the continued support of the local Basque government, it may be subject to expiry, or modified over the course of the bond's tenure. However, Kutxabank has a strong existing loan book of mortgages made under the programme which can support the bond's proceeds.

2.2.2 Management of Proceeds

The proceeds from the social bond will be placed in Kutxabank's treasury and managed by the treasury department. Kutxabank intends to allocate most of the proceeds from the social bond to existing loans made under the VPO programme, and at least one third of the proceeds to new loans made under the VPO programme and to construction finance for developers building new housing developments to be used in the VPO programme.

Kutxabank has an internal system to identify and track loans granted under the VPO programme, including identifying lending for construction finance of VPO housing to which the proceeds from Kutxabank's social bond will be allocated.

The eligibility for loans is determined by the eligibility criteria of VPO programme and an additional credit check based on Kutxabank's internal standards.

To verify the management of proceeds, on an annual basis, Kutxabank's external auditor will review the amount of bond funds allocated to mortgages and construction finance of houses under VPO programme and the balance of unallocated funds.

¹ Income requirements may vary within that range depending on the kind of social housing sought.

² http://www.etxebide.euskadi.eus/x39-contpest/es/contenidos/informacion/requisitos/es_etxecont/requisitos.html

2.2.3 Reporting

Kutxabank commits to provide the following reporting with regard to the social bond:

1. Kutxabank will disclose, on an annual basis, the total amount of loans provided under this program using the social bond proceeds, the number of loans granted, and the number of individuals and families to whom Kutxabank granted a mortgage under the VPO programme.
2. Kutxabank will disclose, on an annual basis, the number of housing units constructed using social bond proceeds.

3 SUSTAINALYTICS' OPINION

A socially-oriented institution:

Kutxabank's founding mission is to be a socially conscious financial institution. The company is rated in Sustainalytics' Global Platform as an outperformer in the social category, and demonstrates involvement in several activities to promote inclusive finance, including loans for young entrepreneurs and students, the financing of social impact activities for non-for-profit organisations, and the provision of micro-credit for under-served segments of population. In addition, Kutxabank is a signatory to UN Global Compact. Furthermore, Kutxabank has not been involved in any controversies or incidents relating to environmental, social or governance issues.

Given its mission, vision and programmes aimed at creating socially positive outcomes in Spain, and given its outperformance among its peers in the management of social issues, Sustainalytics is of the opinion that Kutxabank is socially-oriented and is well positioned to issue a social bond.

Supporting Social Housing: Kutxabank is an ardent supporter of social housing, both in the Basque region and across the rest of Spain. The company has been providing loans under state and regional VPO programmes for two decades. Since its inception in the 1980s, the Basque region's VPO programme has supported thousands of individuals and families in their pursuit of adequate permanent housing. The VPO programme is part of the local Basque government's strategy to reduce social inequality in the region.

In addition to providing mortgages to qualified individuals and families, Kutxabank is involved in various aspects of social housing from project financing the construction of the buildings for social housing, to the donation of apartments to be rented to vulnerable populations. As a result, even if the VPO programme is subject to legislative change over the course of the bond tenure, Kutxabank has a strong portfolio of activities to support social housing in the Basque region to which the bond's proceeds can be allocated.

Impact: Economically speaking, the Basque region of Spain is not underperforming. In fact, the region is currently the wealthiest in Spain, with a GDP per capita 30% higher than the European Union average.³ Nevertheless, the region has suffered along with the rest of Spain in recent years due to the economic crisis and has seen unemployment increase from 12.1% to 15.5%.⁴ Although the level of poverty is still relatively low at around 3% of the population⁵, there is a higher concentration of social inequality within more vulnerable groups, including the elderly and physically handicapped, leading to more difficulties for these groups to obtain adequate, affordable housing. The PES Group reports that access to decent housing is undoubtedly a key aspect of social inclusion, and lists disabilities (mental, physical, and age related) as risk factors to obtaining housing in the Basque Region.⁶ Furthermore, persons with disabilities in Spain have experienced negative impacts on their living conditions due to budgetary cuts in the country. In a recent report by the Commissioner for Human Rights of the Council of Europe, the Commissioner outlined concerns that the economic crisis and resulting financial restrictions have had a detrimental

³ <https://ec.europa.eu/growth/tools-databases/regional-innovation-monitor/base-profile/basque-country>

⁴ <https://ec.europa.eu/growth/tools-databases/regional-innovation-monitor/base-profile/basque-country>

⁵ <http://www.irekia.euskadi.eus/en/news/2424-the-basque-country-heads-europe-the-fight-against-poverty>

⁶ http://issuu.com/pes_cor/docs/a_european_agenda_for_social_housing?e=1480646/2076474#search

impact on most programmes and policies aimed at promoting the inclusion of persons with disabilities in Spain.⁷

Therefore, in Sustainalytics opinion, the special loan considerations included in VPO program for more vulnerable members of society, such as the elderly, or those with reduced mobility and mental handicaps, will have a significant positive impact in enabling these groups to obtain adequate housing.

Conclusion

By issuing the social bond and using the proceeds to provide mortgages under the VPO program in Basque Country, Spain, Kutxabank is enabling increased housing opportunities for low-income and vulnerable individuals that are at a higher risk of social exclusion. These disadvantaged groups would benefit significantly from access to affordable housing which has a positive effect on their living conditions. Kutxabank's social bond framework is aligned with market best practices and norms such as the Green Bond Principles. Furthermore, Kutxabank has committed to have an external auditor audit the allocations of the bond proceeds, which provide further transparency. Overall, Kutxabank's social bond is robust and credible.

⁷<https://wcd.coe.int/com.intranet.InstraServlet?command=com.intranet.CmdBlobGet&IntranetImage=2389885&SecMode=1&DocId=2077824&Usage=2>

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