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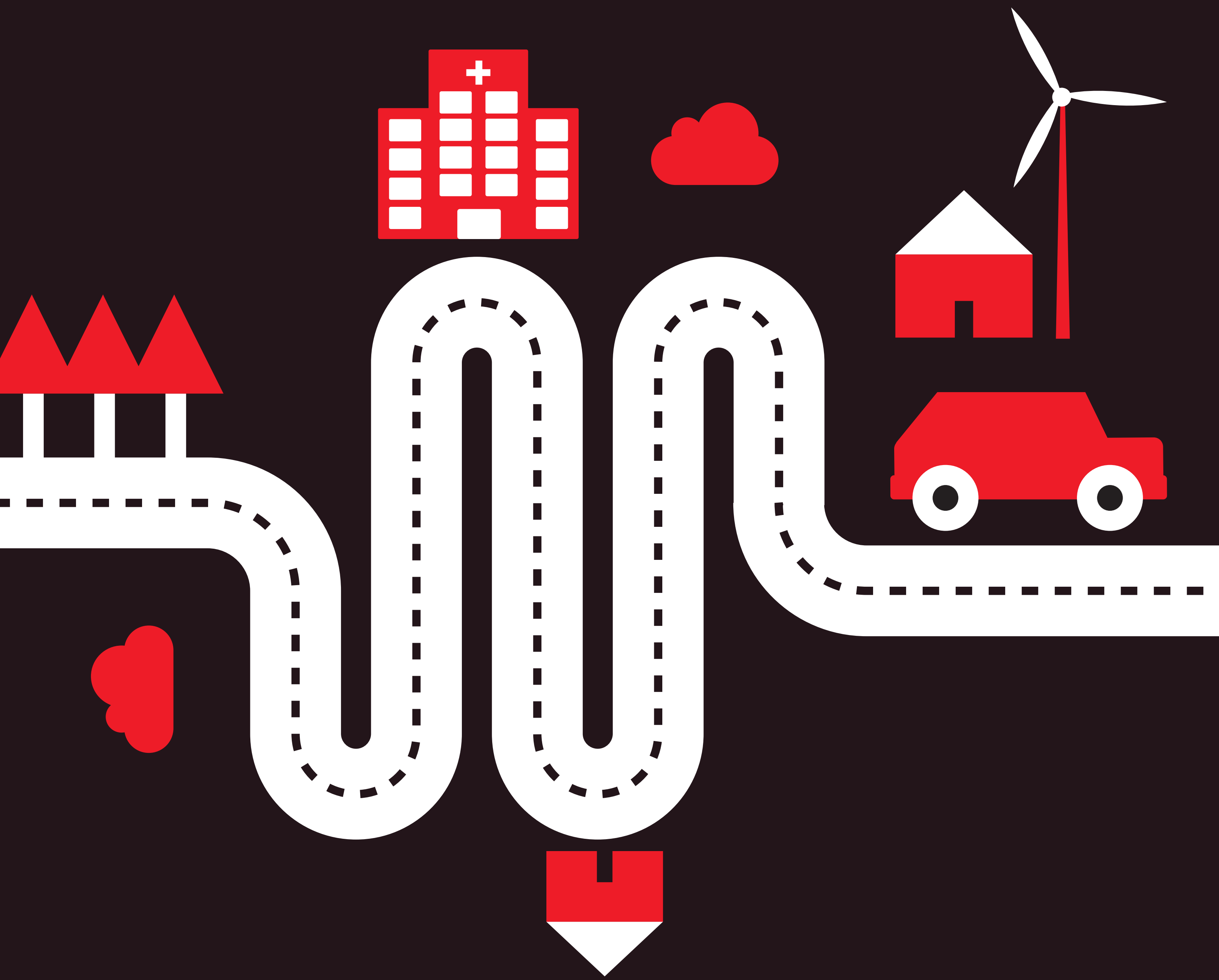
nab

2018
EQUATOR PRINCIPLES
Report

1 October 2017 – 30 September 2018



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 2018 and for the 2018 FY ("FY18").

About the Equator Principles

NAB became a signatory to the Equator Principles[1] ("EP") in October 2007. NAB considers EP requirements when lending for specific projects.

NAB's project finance portfolio

As part of its global project finance portfolio, NAB helps its customers invest in infrastructure, energy and resources projects.

In FY18:

- Project finance represented 1.85% of total Group Exposure at Default ("EaD")[2] at 30 September 2018. Of this lending, 97.6% of projects were in designated countries[3] and 2.4% were in non-designated countries.
- NAB closed 39 new project finance transactions, refinanced 21 existing deals, and removed 13 deals from its loan book.
- Transactions can be declined at any stage in negotiation or due diligence. In 2018, only one transaction was declined primarily 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	9
B	83	48
C	24	15
Pre-EP adoption (prior to October 2007)	11	5
Project finance post EP III to which EP do not apply	45	23
Total	**167**	**100**

Figure 1: Project finance portfolio by region as a % of total portfolio value, expressed as EaD (as at 30 September 2018)

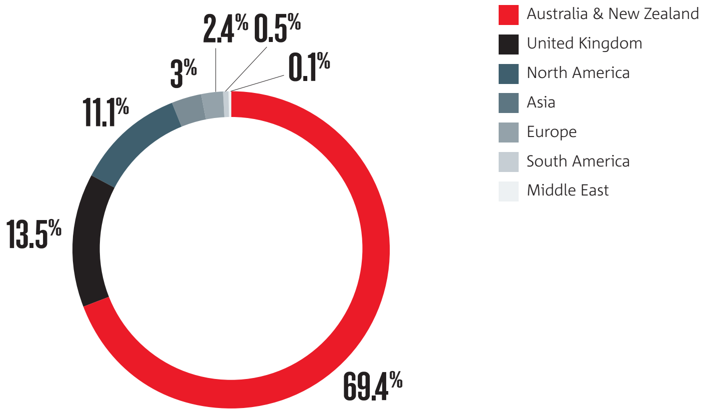
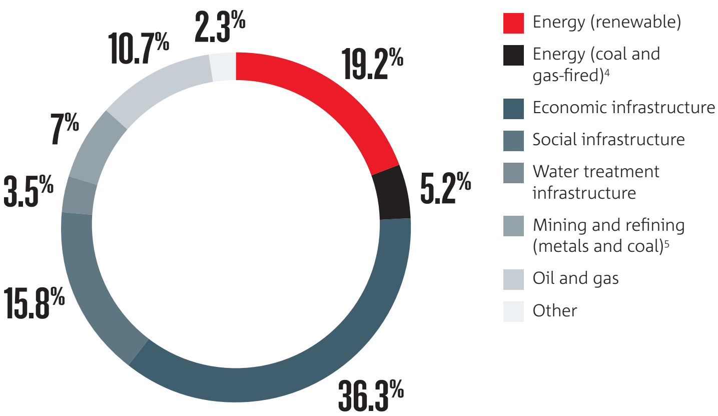


Figure 2: Project finance portfolio by sector as a % of total portfolio value, expressed as EaD (as at 30 September 2018)



1 See http://www.equator-principles.com/ for more information, including the Equator Principles definition of project finance which is used by NAB and its subsidiaries (together, the "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.
4 Coal fired power represented 0.3% of PF exposures as EaD at 30 September 2018.
5 Lending to existing coal projects represents 1.2%, the remaining exposure in this category is to mining of metals.

Project finance for energy infrastructure

NAB has provided $7.7 billion[6] in project finance for renewable energy projects since 2003. NAB continues to be the leading arranger (by market share)[7] of project finance to the Australian renewable energy sector.

In 2018, NAB provided $1.5 billion (measured as committed debt at 30 September 2018) for renewable energy projects. NAB's current global portfolio of renewable energy generation projects represents a total generation capacity of 9,570 megawatts ("MW").

In late 2016, a Climate Change Working Group ("CCWG") was formed with management representatives from across the NAB Group to review the key risks and opportunities facing NAB's business and customers arising from the Paris Agreement to limit global warming to less than two degrees above pre-industrial levels. During FY17, the CCWG refreshed the NAB Group's climate change strategy, which included increasing NAB's current environmental financing commitment from $18 billion by 2022, to $55 billion by 2025[8] to assist the low carbon transition. This includes:

- $20 billion to support green infrastructure, capital markets and asset finance; and
- $35 billion in new mortgage lending flow for 6 Star residential housing in Australia (new dwellings and significant renovations).

NAB's project finance lending contributes significantly to achieving NAB's environmental financing commitment. Further detail on NAB's progress against its environmental financing commitment can be found on page 38 of our Sustainability Report 2018.

In FY18, NAB also estimated[9] the share of the total Scope 1 and 2 greenhouse gas ("GHG") emissions from Australian designated[10] power generation assets which NAB financed, being an estimated 262,591 tonnes of carbon dioxide equivalent ("tCO2-e"). This estimate is based on NAB's participation in financing for each facility as a percentage of debt as at 30 September 2018 (1,726,175 tCO2-e in 2017).

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 power generation and social infrastructure projects. These case studies illustrate NAB's implementation of the Equator Principles.

CASE STUDY 1 – BUILDING RENEWABLE ENERGY IN THE US

The United States' 2015 Wind Vision sets a goal to achieve 20% wind energy by 2030 and 35% wind energy by 2050. NAB's environmental financing commitment is aligned with achieving this goal. As part of our support for a low carbon transition, NAB has participated in a number of US renewable energy transactions including wind power projects, such as the Canadian Breaks wind farm.

Canadian Breaks is an 87 wind turbine project located 28 miles west of Amarillo in the Texas Panhandle - an area mainly used as ranch and agricultural land. The wind farm will have a peak generation design capability of 210 MW and will connect into the Electric Reliability Council of Texas electricity grid.

As part of NAB's due diligence and credit risk assessment, we undertook an ESG risk assessment which included consideration of a range of environmental aspects related to wind farm development. These include status of landholder agreements, stakeholder engagement and grievances processes, cultural and archaeological heritage, environmental management policies, process and approvals and other relevant permitting requirements, impacts on land and biodiversity, and climate change impacts. This project is rated as an EP category B project.

6 Amount includes new transactions and re-financing.
7 Project Finance International 2006-2018 Asia Pacific Initial Mandated Lead Arrangers League Tables Midyear, 2018 US$ Project Allocation, NAB analysis ranking against four major Australian banks – cumulative volume as at 30 June 2018.
8 Represents total cumulative new flow environmental financing from 1 October 2015.
9 As these GHG emissions are not generated directly by NAB, NAB has relied on 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. The methodology involved identifying the reported Scope 1 and 2 GHG emissions associated with each generation facility NAB project financed in Australia. These were then multiplied by NAB's participation in financing for each facility as % of debt as at 30 September 2018. NAB's share of Scope 1 and 2 GHG emissions were then aggregated to get the total tCO_2-e for the portfolio of power generation assets NAB project financed in Australia.
10 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 NAB's project finance portfolio of Australian designated generation facilities covers 97.9% 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 2.1% of assets (measured as MW capacity of the power generation facilities) was not available.

CASE STUDY 2 – CONNECTING MELBOURNE

Melbourne's Metro Tunnel Project will build twin nine-kilometre tunnels and five new underground stations. It will untangle the city loop so that more trains can run more often across Melbourne. As a result, room will be created on the network to enable more than half a million passengers per week across Melbourne's train network during the peak periods. The Metro Tunnel is expected to increase Victoria's Gross State Product by at least $7 billion, with a range of community benefits. These include creating over 7,000 jobs during construction, including positions for almost 800 apprentices, trainees and cadets. Local suppliers will also provide 88% of materials.

The project has established community reference groups in precincts along the new tunnel route to consult, share information and resolve community concerns, where they arise. Meeting minutes and presentations are publicly available. The project also has a clear complaints process. The project's Environmental Effects Statement had an integrated assessment of environmental, economic, social and planning impacts. It also included technical studies that identified and assessed potential effects and provided guidance on mitigation measures.

We considered a range of social, environmental, economic and financial (including credit risk) aspects of the project as part of NAB's due diligence and credit risk assessment process. The social and environmental considerations included heritage values, community and indigenous engagement, environmental management policies, processes and approvals, environmental impacts on ecology, biodiversity and contribution to climate change mitigation and the requirements of the EP. This project has been rated as an EP category B project.

CASE STUDY 3 – WATER TREATMENT AND RECYCLING TO PROTECT THE ENVIRONMENT

The Springvale Water Treatment Facility (WTF) is a greenfield water treatment facility located near Lithgow in NSW. Once constructed, it will be able to treat 42 mega litres of water a day from Centennial Coal's Springvale Colliery. The water will be treated via clarification, filtration and reverse osmosis. It will be used as cooling water at the Mount Piper Power Station[11] (MPPS) which provides approximately 15% of NSW's electricity needs.

NAB supported Veolia in their bid to build, own, operate and transfer the Springvale WTF project. The key project requirements include: transferring mine water from the Springvale Colliery to the MPPS via a 16km pipeline; the treatment and reuse of mine water at the newly built WTF; ensuring excess water discharge complies with relevant environmental obligations; and implementing brine extraction.

This project is important as it will minimise saline mine water from being discharged into the Coxs River Catchment in NSW. This addresses community and environmental concerns about mine water being released into Sydney's drinking water catchment.

NAB's due diligence and credit risk assessment for this project considered a range of social and environmental aspects alongside economic, financial, and credit considerations. Key considerations were environmental management policies, processes and approvals, environmental impacts on ecology and biodiversity, aboriginal cultural heritage, community engagement, consultation and complaints processes, and the requirements of the EP. This project has been rated as an EP Category B project.

11 MPPS is owned by Energy Australia

NAB Group's FY18 Equator Principles Data

The total number of project finance transactions that reached Financial Close[12] in FY18 was 60[13]. Of these transactions, 21 were refinancing existing project finance loans, 19 were for operational assets which did not trigger the Equator Principles and 20 were for projects which triggered EP requirements.

In accordance with the reporting requirements of Equator Principles Version III ("EP III"), Table 2 provides a breakdown of NAB's relevant project finance data with respect to the 20 transactions referred to above by sector, region, country type and whether an independent review has been carried out during FY18.

Table 2: Project Finance Data

	Breakdown by Category		
	A	**B**	**C**
EP transactions closed during the period 1 October 2017 to 30 September 2018	0	20	0
By Sector	**A**	**B**	**C**
Energy (gas-fired)	0	1	0
Energy (renewable)	0	12	0
Oil & Gas	0	2	0
Infrastructure (road, rail, airports, ports, pipelines and telecommunication)	0	1	0
Water infrastructure	0	2	0
Mining and refining	0	2	0
By Region	**A**	**B**	**C**
Australia & New Zealand	0	10	0
North America	0	8	0
United Kingdom	0	1	0
Latin America	0	1	0
By Country Type	**A**	**B**	**C**
Designated	0	20	0
Non-designated	0	0	0
Independent Review[14]	**A**	**B**	**C**
Yes	0	20	0
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 FY18.

Table 3: Project Finance Project Name Reporting

Project Name	Calendar Year	Sector	Name of Host Country
Blyth Holdings Limited	2018	Energy (renewable)	UK
Tahoka Wind Farm	2018	Energy (renewable)	USA
Kawailoa Solar Project	2018	Energy (renewable)	USA
NRG Oahu Solar Project	2018	Energy (renewable)	USA
Rio Bravo Wind Farm	2018	Energy (renewable)	USA
Caitan S.p.A. (Spence)	2018	Water Infrastructure	USA
Corpus Christi	2018	Oil and Gas	USA
Canadian Breaks Wind Farm	2018	Energy (renewable)	USA
South Field Energy	2018	Energy (gas-fired)	USA
Phoebe Solar	2018	Energy (renewable)	USA
Emerald Solar Farm	2017	Energy (renewable)	Australia
Springvale Mount Piper Water Treatment Project	2017	Water Infrastructure	Australia
Dalgaranga Gold Project	2017	Mining and Refining	Australia
Melbourne's Metro Tunnel Project	2018	Infrastructure	Australia
Stockyard Hill Wind Farm	2018	Energy (renewable)	Australia
Cooper Energy Ltd	2018	Oil and Gas	Australia
Gruyere Gold Project	2018	Mining and Refining	Australia
Crowlands Wind Farm	2018	Energy (renewable)	Australia
Lal Lal Wind Farms	2018	Energy (renewable)	Australia
Haughton Solar Farm	2018	Energy (renewable)	Australia

There were no Project-Related Corporate Loans (as defined in the EP) that reached Financial Close during the period 1 October 2017 to 30 September 2018 to which EP applied.

There was a Project Finance Advisory Service (as defined in the EP) mandated during the period from 1 October 2017 to 30 September 2018. Data on this Project Finance Advisory Service is provided in Table 5.

Table 5: Project Finance Advisory Services

By Sector	Number of Services mandated
Other (Organics processing facility)	1
By Region	**Number of Services mandated**
Australia & New Zealand	1

12 Defined in the EP as "the date on which all conditions precedent to initial drawing of the debt have been satisfied or waived".
13 This is the total for new and refinanced deals regardless of whether the EP apply.
14 Conducted in accordance with Principle 7 - Independent review

Personnel involved in PF transactions

Project finance is managed through NAB's Specialised Finance team and supported by its 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") risks.

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 NAB's 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 an 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 NAB's practice to identify potential corporate finance transactions where the EP could apply. NAB's Group credit risk policy reflects EP III requirements.

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

For project finance transactions, tailored due diligence is undertaken as required by NAB's 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 frontline Specialised Finance team, Credit team 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[15]. Standards 5 (Land Acquisition and Involuntary Resettlement) and 7 (Indigenous Peoples) are particularly relevant as part of reviewing how NAB's clients are managing 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 project finance transaction. This includes targeted site visits by TSG and independent monitoring where necessary (generally during construction and operations for complex and/or Category A projects). NAB also requires 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 NAB can monitor 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 project finance lending. NAB also monitors the carbon intensity of its project finance energy generation portfolio as part of internal management reporting.

Assurance over PF data

On an annual basis, NAB has key project finance data reviewed by an independent audit firm. In FY18, this assurance was provided by KPMG. KPMG provided assurance over project finance by sector as a proportion (%) of total project finance portfolio value, expressed as EAD, for the year ended 30 September 2018.

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

15 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.