Introduction of EU SURE Social Bond

The temporary **S**upport to mitigate **U**nemployment **R**isks in an **E**mergency (SURE) is a transient measure approved by the European Committee on October 7, 2020. The SURE instrument provides financial assistance up to EUR100 billion in the form of loans from the EU to the affected EU Member States to fight and mitigate the severe negative social-economic consequences due to the COVID-19 outbreak on their territory. Under the EU SURE Social Bond Framework, structured well aligned with the ICMA Social Bond Principles (ICMA SBP), the European Commission is empowered to issue social bonds under the SURE instrument on behalf of the EU. The framework is also meant to allow the investor community to allocate their funds towards social needs of EU Member States.

The European Commission issued the very first EU SURE Social Bond on October 27, 2020. The EUR 17 billion social bond issuance consisting of two tranches: a EUR 10 billion tranche with a 10-year maturity, and a EUR 7 billion tranche with a 20-year maturity. The bond received unprecedented investor response with 13 times oversubscribed and was the ever record-high Use of Proceeds Bond[1] issuance among the green, social or sustainability bonds. The European Commission issued another EU SURE Social Bond on November 17, 2020. It also consisted of two tranches with an aggregate amount of EUR 8 billion and EUR 6 billion. The detail of these EU SURE Social Bonds including the basics of the bonds, the features of the bonds, the transactions, and the information disclosure requirements, will be introduced in the following paragraphs.

[1] The Use of Proceeds Bond is a standard recourse-to-the-issuer debt obligation for which the proceeds shall be credited to a sub-account, moved to a sub-portfolio, or otherwise tracked by the issuer and attested to by a formal internal process that will be linked to the issuer's lending and investment operations for eligible projects such as green bond, social bonds, and sustainability bonds.

1. Descriptions of the EU SURE Social Bond

(1) Summary of terms and conditions

Issuer	The European Commission			
Issue Date	2020/10/27	2020/10/27	2020/11/17	2020/11/17
Maturity Date	2030/10/4	2040/10/4	2025/11/4	2050/11/4
Tenor	10 年	20 年	5 年	30 年
Issued Amount	EUR 10 billion	EUR 7 billion	EUR 8 billion	EUR 6 billion
Coupon	0%	0.1%	0%	0.3%
Issue Price	102.396	99.39	102.566	99.515
Listing	Luxembourg Green Exchange			

(2) Use of proceeds

The EU SURE Social Bond is designed to raise funds by the European Commission to facilitate the Member States to fulfill their funding demands for the sudden and severe increase of their public expenditure due to the COVID-19 pandemic. The European Commission will use the proceeds from the EU SURE Social Bonds to disburse back-to-back loans on favorable terms to the Member States to finance or refinance health-related measures and short-time work schemes. The EU SURE Social Bond issuance is the very first time that the European Commission raising funds solely for social projects. As a financial assistance under the EU loan programmes[2], the

[2] The EU loan programmes include 3 programmes:

(1) European Financial Stabilisation Mechanism (EFSM): According to the Council Regulation (EU) 407/2010 of May 2010, EU financial assistance may be granted in the form of a loan or a credit line to a Member State in difficulties to maintain the financial stabilities in the EU. Under the mechanism, the European Commission had injected up to EUR 46.8 billion funds in the form of loans to Ireland and Spain between 2011 and 2014.

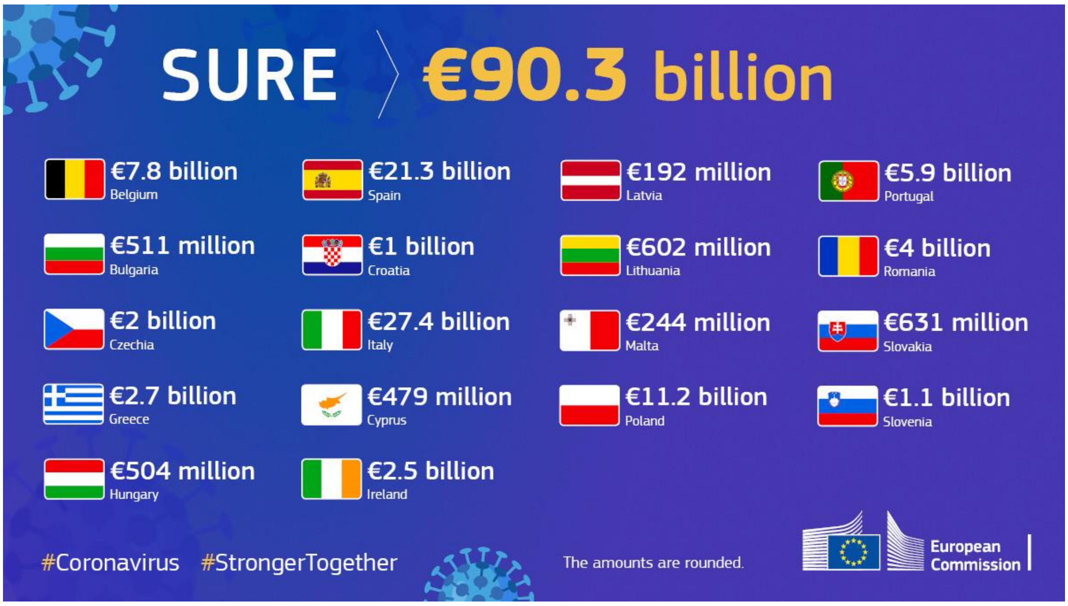
(2) Balance of Payments Programme (BoP): According to the Council Regulation (EU) 332/2002 of 18 February 2020, the EU may provide financial assistance to Member States outside the euro area. The financial support, up to EUR 13.4 billion, was funded to Hungary, Latvia, and Romania between 2008 to 2010.

(3) Macro-Financial Assistance (MFA): The EU may assist countries that are receiving financial

current outstanding amount of the EU SURE Social Bond reached EUR 52 billion.

From 1 February 2020, the financial support under the SURE programme is providing to the Member State on an upon-request basis. So far, 17 Member States have received the financial support totaling EUR 87.9 billion to protect jobs and reduce the risk of unemployment and loss of income, and hopefully restore the economic growth, eventually. In addition, the European Commission submitted a EUR 2.5 billion fiscal support plan for Ireland on 16 November 2020. If approved, the total financial support will reach EUR 90.3 billion as Graph 1 displayed below. Up to the present, the EU SURE bonds have been injecting up to EUR 31 billion in the form of loans to Italy, Spain, Poland, Greece, Croatia, Lithuania, Cyprus, Slovenia, Malta, and Latvia.

Graph 1: Member States fiscally supported by the SURE Programme



Source: The official website of the European Union

support from IMF with grants and/or loans based on individual decisions of the European Parliament and of the Council. The outstanding loan have reached EUR 4.8 billion.

2. Key features of the EU SURE Social Bond Framework

(1) Aligned with the ICMA Social Bond Principles and acquired external certification

The EU, enjoying a AAA credit rating with stable outlook by Moody's and Fitch, empowered the European Commission to establish the EU SURE Social Bond Framework. The SURE Social Bond Framework, like other social bond frameworks, is structured around and be compliment with the ICMA Social Bond Principles and is also contributing to some of the United Nations' Sustainable Development Goals (SDGs). This framework, received a favorable second-party opinion from Sustainalytics, provides credibility for investors to assure that the net proceeds will be fully allocated to eligible projects.

(2) The core components of the Framework

The EU SURE Social Bond Framework is aligned with the four core components of ICMA SBP, and according to the EU, green, social, and sustainability bonds will be integrated within the same framework, and this framework will be consistent with the EU Taxonomy. The four core elements of the framework are briefly introduced as below.

I. Use of proceeds

ICMA Social Project Categories	Eligible Social Projects	UN Sustainable Development Goals
Employment generation, and programs designed to prevent and/or alleviate unemployment stemming from socioeconomic	Eligible social expenditures: providing financial assistance to Member States experiencing a sudden and severe increase in public expenditure on the	SDG 3: Good health and Well-Being

ICMA Social Project Categories	Eligible Social Projects	UN Sustainable Development Goals
crises.	preservation of employment, to tackle the economic disturbance caused by the COVID-19 outbreak.	SDG 8: Decent Work and Economic Growth
	Eligible social financing or refinancing (in whole or in part): measures designed by the Member States to reduce the risk of unemployment and loss of income for employees and self-employed.	
Access to essential services	Eligible social financing or refinancing: health-related measures, particularly in the workplace.	

II. Process for project evaluation and selection

The Member State must submit to the European Commission a detailed and substantiated request for financial assistance in accordance with the SURE Regulation. The European Commission will assess whether the beneficiary Member States' actual and planned expenditure are eligible social expenditures. In addition, the European Commission will assess the costs of the requested measures to facilitate its evaluation of the terms of the loan.

III. Management of proceeds

The European Commission will use the funds raised by the

EU SURE Social Bonds to disburse the loans to Member States requesting for financial assistance. The beneficiary Member States must open an account with its national central bank for the management of the use of the proceeds; meanwhile, in accordance with the loan agreement, the Member State should also transfer the principal and the interest due to an account with the European System of Central Bank.

The European Commission will track and monitor whether the Member State allocated the SURE Social Bond proceeds to finance or refinance the eligible social expenditures as they committed.

IV. Reporting

The European Commission will report both the allocation report and impact report on its website. The first report will be published within 6 months after the first issuance under the SURE Social Bond Framework, and every 6 months thereafter. The allocation reporting will present in aggregated terms the breakdown of the proceeds by beneficiary Member State and will present by the major categories of eligible social expenditures. According to the SURE Regulation, the beneficiary Member States must inform the European Commission about its implementation of planned public expenditure. The impact reporting will depend on the quality and granularity of the information reported by the Member States.

3. An overview of the secondary market transactions

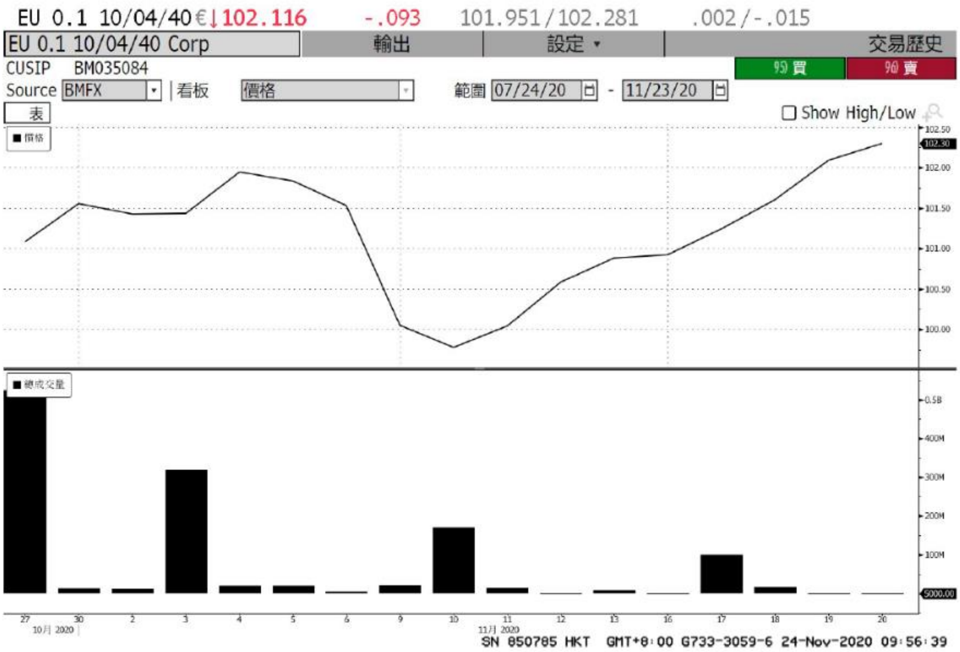
According to the pricing supplements, the 4 tranches of EU SURE Social Bonds are listing and trading on Luxembourg Green

Exchange. The average daily trading volume is around EUR 70 million to EUR 100 million as the graph below displayed.

Graph 2: the trading volume and price of the 10-year EU SURE Social Bond

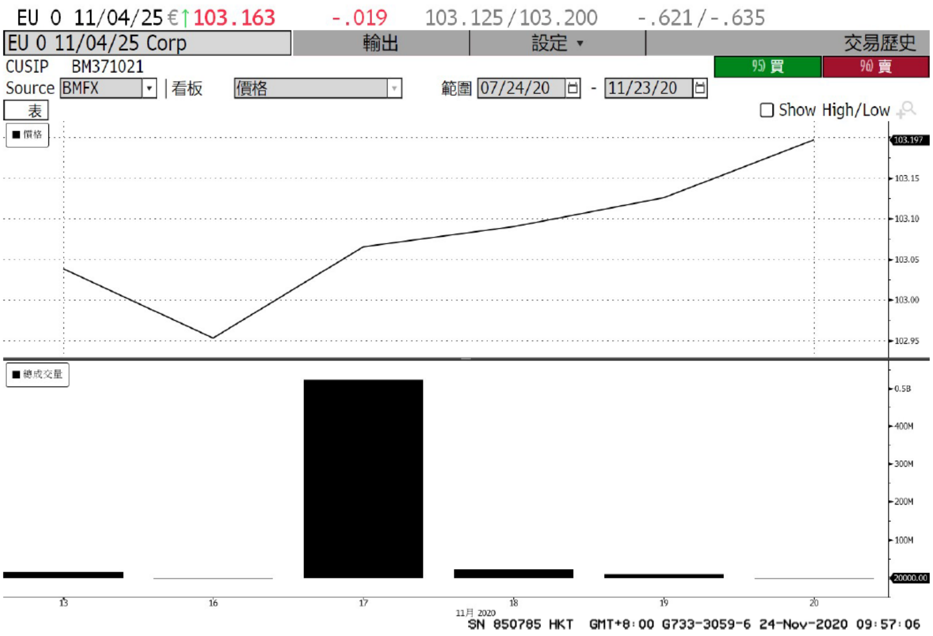
Source: Bloomberg database

Graph 3: the trading volume and price of the 20-year EU SURE Social Bond



Source: Bloomberg database

Graph 4: the trading volume and price of the 5-year EU SURE Social Bond



Source: Bloomberg database

Graph 5: the trading volume and price of the 30-year EU SURE Social Bond

Source: Bloomberg database

4. The information disclosure requirements

(1) Pre-issuance information disclosures

Before the SURE Social Bond issuance, the EU SURE Social Bond Framework and its external certification are made available to the investors. Besides, the relevant information disclosures are included in its base prospectus and pricing supplement.

(2) Post-issuance information disclosures

According to the EU SURE Social Bond Framework, the European Commission will report on the tracking and monitoring of the proceeds within 6 months of the first EU Social Bond issuance, and every 6 months thereafter. The European Commission will report on the allocation and impact of the proceeds and publish the reports on its webpage.

The allocation reporting will present in aggregated terms the breakdown of the proceeds by beneficiary Member State and will present by the major categories of eligible social expenditures. According to the SURE Regulation, the beneficiary Member

States must inform the European Commission about its implementation of planned public expenditure. The impact reporting will depend on the quality and granularity of the information reported by the Member States.

Appendix. An introduction about the definition of a social bond and its international standard[3]

A Social Bond is any type of bond instrument where the proceeds will be exclusively allocated to finance or refinance in whole or in part to new and/or existing eligible Social Projects. Except for the restrictions on the use of proceeds, the social bonds are as the same as the ordinary bonds. ICMA introduced a series of principles to enhance the information transparency and to provide a standardized reference for the specific market sector throughout the past 5 years. ICMA published the ‘Social Bonds- Guidance for Issuers in 2016 and then replaced it by the Social Bond Principles (SBP) in 2017. This principle is a reference meant to facilitate the development of the social bond market.

SBP is a set of voluntary guidelines providing issuers with guidance on the key components involved in issuing a credible social bond. The key components include: Use of Proceeds, Process for Project Evaluation and Selection, Management of Proceeds, and Reporting. In addition, an external review is recommended in connection with the issuance of a social bond or a programme to confirm the alignment of their bonds with the four components of the SBP. So far, the SBP has been considered as an international practice when issuing social bonds. The main idea of the SBP four core components is summarized in the chart on next page.

[3] The content of this Appendix is based on the Social Bond Principles published by ICMA. The original document is available at https://www.icmagroup.org/assets/documents/Regulatory/Green-Bonds/June-2020/Social-Bond-PrinciplesJune-2020-090620.pdf

ICMA SBP Four Core Components			
Use of Proceeds	Process for Project Evaluation and Selection	Management of Proceeds	Reporting
To identify the eligible social investment projects for the social bonds.	The process by which the issuer evaluates and determines how the projects fit within the eligible social project categories.	The process and mechanism by which the issuer set up to manage the proceeds and to assure that the proceeds will be allocated to eligible projects.	Periodically report to the investors the status of the use of the proceeds and the expected impact.

According to the ICMA SBP, Social Project categories include, but are not limited to, providing and/or promoting:

1. Affordable basic infrastructure (e.g., clean drinking water, sewers, sanitation, transport, energy)
2. Access to essential services (e.g., health, education and vocational training, healthcare, financing, and financial services)
3. Affordable housing
4. Employment generation, and programs designed to prevent and/or alleviate unemployment stemming from socioeconomic crises, including through the potential effect of SME financing and microfinance
5. Food security and sustainable food systems (e.g., physical, social, and economic access to safe, nutritious, and sufficient food that meets dietary needs and requirements; resilient agricultural practices; reduction of food loss and waste; and improved productivity of small-scale producers)
6. Socioeconomic advancement and empowerment (e.g., equitable access to and control over assets, services, resources, and

opportunities; equitable participation and integration into the market and society, including reduction of income inequality)

Examples of SBP target populations include, but are not limited to, those that are:

1. Living below the poverty line
2. Excluded and/or marginalised populations and /or communities
3. People with disabilities
4. Migrants and /or displaced persons
5. Undereducated
6. . Underserved, owing to a lack of quality access to essential goods and services
7. Unemployed
8. Women and/or sexual and gender minorities
9. Aging populations and vulnerable youth
10. Other vulnerable groups, including as a result of natural disasters