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CHAPTER 7

The Growing Importance of ESG in Restructurings

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Introduction

The number of assets allocated to socially responsible investment products continues to increase, and environmental, social and governance (ESG) criteria continue to gain ground, with many institutional investors investing only in those companies that provide ESG performance reporting.

Socially responsible investment (SRI) began years ago, although the term 'ESG investment' emerged from the Principles for Responsible Investment (PRI) published by the United Nations (UN) in 2006. In 2005, Kofi Annan, the then General Secretary of the UN, brought together the world's leading institutional investors to participate in the development of six fundamental principles of responsible investing, which became a set of investment principles offering an array of possible actions for incorporating ESG criteria into investment practices. Although these ambitious principles are voluntary, their adoption by senior management of investment institutions represents a commitment to endorse them. Originally, the PRI focused on the fundamentals of large investors, with long investment horizons and highly diversified portfolios. However, they apply to all types of institutional investors, investment managers and their professional services providers. In the last quarter of 2022, PRI added 140 global organisations as new PRI signatories,[2] including 14 asset owners; PRI now has

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2 As of 30 March 2023, there are 38 Mexican signatories of the PRI programme, representing diverse sectors, such as pension funds, real estate and infrastructure developers, and

5,319 signatories, representing US$121 trillion assets under management.[3] New signatories include ZENKYOREN (National Mutual Insurance Federation of Agricultural Cooperatives) in Japan, Korea Investment Corporation and Netherlands-based Aegon NV.[4]

The aim of the PRI programme is to encourage investors to consider and implement responsible ESG factors in their investment decisions (stock, fixed income, private equity, hedge funds and real estate assets) and to assist them with their responsible investment approaches. PRI was present at COP27 in Sharm El-Sheikh in November 2022, where its work focused on convening government leaders and investors on actionable targets in line with the Paris Agreement and published its Sustainability Outcomes report on signatory practices. In its early days, SRI emerged as a market niche focused on allocating capital to companies seeking social and environmental change. It has evolved into ESG investment, the aim of which is to gather under the same umbrella the fundamentals of ESG (i.e., environment, social and governance topics) and to seek profitability.

There is no universal categorisation for ESG topics and so they can be defined in different ways depending on the industry, company characteristics or business model. For the preparation of sustainability reports, there are different standards or methodologies, ranging from self-declaration, following a particular structure defined by each organisation, or even an alternative model for sustainability, to adhering to an internationally known standard methodology.

In the midst of the proliferation of ESG frameworks and metrics, there are a number of already well-developed and recognised harmonisation efforts. For instance, the Global Reporting Initiative (GRI) is an international, independent body that sets and periodically reviews standards, bringing a common language for organisations to report on effects on sustainability in a way that is both uniform and reliable. The latest review of the GRI standards, approved in July 2021 by the Global Sustainability Standards Board (GSSB), entered into force on 1 January 2023, although earlier adoption was encouraged.[5] However, it is important to clarify that the GRI standards are not binding in any jurisdiction, and so reporting may vary significantly if other stratagems are applied.

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private equity. See https://dwtyzx6upklss.cloudfront.net/Uploads/j/w/a/pri_signatory_directory_march_2023_2.0_979851.xlsx (last accessed 12 June 2023).

3 See https://www.unpri.org/download?ac=18057 (last accessed 12 June 2023).

4 See https://www.unpri.org/download?ac=18057 (last accessed 12 June 2023).

5 See https://www.globalreporting.org/standards/standards-development/universal-standards/ (last accessed 12 June 2023).

Although ESG investment continues to develop, there are a number of challenges that need to be addressed to help nurture and promote this growth, such as clarifying the definitions and use of the terms associated with ESG, to prevent their interchangeability and the confusion and misunderstanding created by this lack of uniformity. In that sense, and as an example, in February 2023, members of the International Sustainability Standards Board (ISSB) signed off on its first two disclosure standards for companies, including one that references the GRI and the EU sustainability reporting standards (ESRS)[6] so that investors can use comparable information about sustainability-related risks and opportunities in their investment decisions without delay.[7]

ESG goes beyond mere compliance and checklists. It includes the pursuit of meaningful impact, both for businesses and the planet, by generating sustainable outcomes that drive value and foster growth, while simultaneously enhancing our environment and societies. Businesses must adapt to a changing world where the measure of success is no longer solely financial metrics but encompasses goals ranging from achieving net-zero emissions to embracing the circular economy.

In recent years, the scope of ESG reporting obligations, especially in Europe, has broadened, coinciding with a rising inclination among investors to distance themselves from companies that do not meet ESG criteria. Following these examples, Mexican institutions, such as the Mexican Stock Exchange (BMV) and the Institutional Stock Exchange (BIVA), National Banking and Securities Commission (CNBV), and the Ministry of Finance, have begun to introduce regulatory requirements for issuers and investors, which provide heightened ESG standards and disclosure obligations. For example, Mexican pension funds (AFOREs) must now consider ESG criteria investment factors and, in February 2023, BIVA introduced BIVASG, a platform designed to consolidate all ESG-related information pertaining to issuers in Mexico, offering comprehensive information on the initiatives and ESG criteria adopted by the listed issuers on BIVA and other stock exchanges. The platform includes a technical dossier containing key details and documents such as the reference framework, allocation of resources, offering notices, and prospectuses related to these issuances, aiming to provide the most up-to-date and relevant global information on methodologies, regulatory advancements and issues aligned with ESG principles.[8]

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6 See https://www.responsible-investor.com/issb-board-approves-first-sustainability-standards-including-reference-to-gri-and-esrs/ (last accessed 12 June 2023).

7 See https://abmagazine.accaglobal.com/global/articles/2023/feb/practice/issb-approves-first-sustainability-standards.html (last accessed 12 June 2023).

8 See https://www.biva.mx/biva-sostenible/introduccion (last accessed 12 June 2023).

For its part, BMV encourages companies to create ESG reports to measure and disclose their efforts in sustainability. In this regard, the sustainability maturity self-assessment serves as an annual questionnaire that enables issuers to identify their progress in ESG criteria, which can be accessed on the BMV's website and in 2022, a total of 30 issuers responded to the sustainability maturity self-assessment. Also, through the BMV system (Emisnet), issuers can publish their Sustainability Reports to make their information public and accessible to their stakeholders. It is worth noting that 85 per cent of BMV listed companies (119 out of 139) disclosed ESG information in 2022, either through an integrated annual report, sustainability report or on their websites.[9] As part of the BMV's efforts to further promote this market, the company launched the Sustainable Accompaniment Program (PAS) in 2021, a workshop aimed at companies that require training in the adoption of ESG criteria, which has already been joined by more than 500 participants from over 350 companies. The BMV also developed the Sustainability Guide to facilitate the path for issuers in the design of their sustainability strategies.[10]

ESG as a new way to invest

What is ESG?

The term 'ESG' is often used interchangeably with 'corporate social responsibility' or 'corporate sustainability' but ESG encompasses much more. There is no universal agreement on definitions for the various styles of investment that seek a positive social or environmental outcome. For example, John Hill states[11] that ESG may be summarised as an innovative way of investing that seeks a positive social or environmental impact as an outcome of the development of business without sacrificing the earning of the stakeholders. In fact, it is stakeholders who have been pushing ESG, partly with the support of governments and organisations such as the UN, when an investor or fund manager invests in public debt or equity, often via mutual funds or exchange-traded funds.

To date, there is no general consensus on what is encompassed by ESG; however, the following descriptions are generally accepted:

9 See https://www.bmv.com.mx/docs-pub/sustenta/sustenta_1274583_2022_1.pdf (last accessed 12 June 2023).

10 See https://expansion.mx/mercados/2023/05/11/bonos-asg-bolsa-mexicana-superan-200000-mdp (last accessed 12 June 2023).

11 John Hill, Environmental Social and Governance (ESG) Investing (Academic Press, 2020, London, UK).

- the E factor (environmental) refers to decision-making based on how a company's activities affect the environment;
- the S factor (social) takes into account the impact of a company's activities on the community, for example, in terms of diversity, human rights or healthcare; and
- the G factor (governance) studies the impact of shareholders and a company's administration and is based on issues such as the structure of the board of directors, the rights of shareholders, transparency and compliance with applicable laws, among other things.

ESG rating agencies and scores

Although ESG is a trend that is likely to become the norm for many stakeholders in company restructuring – mainly because of the long-term exposure to ESG risks – there is yet no consensus on the metrics and standards used to evaluate compliance with ESG matters, and therefore scores can often be contradictory and misleading. To date, there are no standards to evaluate ESG compliance by companies, as no jurisdiction has yet addressed this. ESG scores are typically based on two factors: exposure to risk and opportunity, and performance. As such, criteria for creating scores have been established by private rating agencies, of which there are approximately 125,[12] some of the most notable being MSCI,[13] ISS, RobecoSAM, Sustainalytics, RepRisk, ISS and Refinitiv. Each rating agency uses its own scoring method, resulting in different non-financial metrics being evaluated and disagreement about the components of ESG. These methods also have different indicators, which are not always clear or transparent. This is in contrast with credit ratings, for which agencies use consistent financial information, besides the three major credit rating agencies that now incorporate ESG criteria in their analyses. Furthermore, ESG disclosures are not audited. Finally, to date, ESG ratings have not identified the potential risks of non-compliance, notably including the *Wells Fargo* and *Volkswagen* cases.[14] According to an analysis

12 Bergman, Curran, Deckelbaum, Karp, Martos, et al., 'ESG Ratings and Data: How to Make Sense of Disagreement' (January 2021), at https://www.paulweiss.com/insights/esg-thought-leadership/publications/esg-ratings-and-data-how-to-make-sense-of-disagreement?id=39303 (last accessed 12 June 2023).

13 MSCI is responsible for evaluating 8,500 companies and more than 680,000 fixed income and equity securities globally, making it the most notable of the agencies. See 'What Is an ESG rating?', The Motley Fool. See: https://www.fool.com/investing/stock-market/types-of-stocks/esg-investing/esg-rating/ (last accessed 12 June 2023).

14 Timothy M Doyle, 'Ratings That Don't Rate: The Subjective World of ESG Ratings Agencies', American Council for Capital Formation. See: https://accfcorpgov.org/wp-content/

carried out by CSRHub,[15] this lack of consistency has led to different evaluations about the same entity; consequently, critics of these agencies have questioned the validity of the ratings.

Nevertheless, these agencies are becoming an increasingly important part of the market, and a growing number of public companies are taking their scoring more seriously. Furthermore, investment funds and other key players are requiring certain companies to improve their scores as a condition for providing investment, but this remains a complicated task as long as these companies do not implement more consistent parameters.

Moreover, companies in Latin America, as in other parts of the world, can comply with all applicable domestic laws while not necessarily meeting the criteria measured by these rating agencies, including intangible matters that are sometimes difficult to identify. This can result in a low score, which can affect the financing of a company that is not otherwise regulated, even when the company – as is most often the case – is not negligent.

This can be an important factor in a restructuring and could become increasingly important. Companies may be denied access to financial support from firms that are now often required to invest or restructure based on ESG standards, and depending on which rating agency has evaluated it. When eventually uniform standards are agreed, the consistent evaluation of rating agencies will be a key component in restructuring calculations.

Stakeholders in restructuring proceedings

Companies undergoing a restructuring proceeding are normally in need of new money to support the process; this funding is traditionally available through either debt (loans, bonds or other financial instruments) or equity, by the introduction of new investors.

In recent years, ESG has affected the manner in which banks, investment funds and other key stakeholders approach the introduction of new capital in distressed companies and, therefore, in restructuring proceedings.

ESG can affect companies that are seeking funding to restructure through debt or equity, or a combination of both, as further described below. ESG can also affect the ability of companies to perform contractual obligations and compromise their financial results and viability. Breaching ESG standards can certainly imply

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uploads/2018/07/ACCF_RatingsESGReport.pdf (last accessed 12 June 2023).

15 See https://content.csrhub.com/files/How+CSRHub+Generates+Consensus+ESG+Ratings_2020_04_27.pdf (last accessed 12 June 2023).

a deterioration in a company's financial position and solvency, thus becoming a critical aspect in triggering a company's restructuring. Take, for instance, the recent cases of *Credito Real*, *AlphaCredit* and *Interjet* in Mexico, whose insolvency and restructuring proceedings have been complicated by allegations of fraud, mismanagement, lack of transparency, reporting issues and shareholders disputes. All of these circumstances reflect the lack of proper G-focused ESG policies which indirectly contributed to the financial viability of these companies and will certainly pose a challenge to the feasibility of their potential reorganisation in a new order where stakeholders will show major concerns with ESG topics surrounding such companies.

Debt

ESG has rapidly gained a strong presence and is now a factor in a growing number of transactions and in the analysis of the viability of a number of projects in the financial sector. The banking industry has a central role as an important catalyst in reorienting financial flows towards sustainable activities and in supporting industries and governments in meeting ESG requirements.

Commercial banks are already adding ESG to the agenda of credit and restructure committees. This is not only prudent in terms of a holistic, long-term analysis of the viability of projects to be financed or refinanced, but also relevant from a reputational perspective on the type of project a bank is willing to support. In recent months, there has been a dramatic increase in ESG-linked loans. The aim of this kind of loan is to encourage a commitment to sustainability by the borrower, through the setting of certain performance targets relating to ESG.

As we already know, distressed companies can initiate a restructuring process by increasing their liquid assets through loans from financial institutions. There is currently no requirement for ESG compliance for a bank or financial institution to agree to lend money; however, many of the key players in the financial markets have set up special budgets for sustainable finance for the coming years.

Furthermore, international organisations are increasing their efforts to promote and establish measures and including on their agenda ESG-related initiatives that will make the implementation of ESG principles appealing for both private and public agencies that manage debt.

For example, the International Finance Corporation has launched its own social bond programme, which combines an investment proposition with the bonus of making a positive impact where it may be applied. Between its creation in 2017 and 31 December 2022, 76 social bonds were issued in several different currencies, amounting to US$5.17 billion.[16]

Another practice that has become relevant to international organisations is the issuance of sustainable and social bonds for the advancement of gender equality. On 25 May 2022, UN Women entered into an MOU with BlackRock for cooperation in promoting the growth of strategies to mobilise capital in support of economic opportunities for women.

In respect of sovereign debtors, ESG factors are already important and will continue to be. The restructuring of debt earmarked for the construction of an international airport in Mexico City (for approximately US$1.8 billion) is one example. An analysis by a global wealth and asset manager estimated the price of ESG risks (including 'instances of corruption, independence of the central bank, access to employment and benefits in place for workers, social security, and the funding of pensions') at 30 base points of its spread, which represented approximately 9 per cent of the total spread.[17]

Equity

Distressed companies can also seek financing to comply with their obligations by including new shareholders in their corporate structure. Key players here include funds, asset managers, private equity companies and family businesses.

Larger market players continue to highlight the importance of meeting ESG requirements to be able to invest in a company and to play a relevant role as a key player. In his annual letter to CEOs in 2022, BlackRock's chair and CEO Larry Fink highlighted the importance of companies having a clear sense of purpose, to have consistent values and to recognise the importance of engaging with and delivering for their stakeholders (not only as an ideological or 'woke' matter but as mere capitalism). These features are the foundation through which capital is efficiently allocated, durable profitability is achieved, and value is created and sustained over the long term.

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16 See https://www.ifc.org/wps/wcm/connect/corp_ext_content/ifc_external_corporate_site/about+ifc_new/investor+relations/ir-products/socialbonds (last accessed 12 June 2023).

17 Jose Saracut and Vincent Zheng, Manulife Investment Management, 'Case Study: ESG Integration' in A Practical Guide to ESG Integration in Sovereign Debt, PRI, pp. 51–53.

Mr Fink expressed his belief that the decarbonisation of the global economy will create the investment opportunity of a lifetime and that companies must evolve as the world changes or risk being replaced by new competitors. Further, he stressed the importance for companies to issue their reports consistently with the Task Force on Climate-related Financial Disclosures (TCFD) and is adamant that BlackRock will focus on sustainable investments.

In his letter, Mr Fink stated:

> *Putting your company's purpose at the foundation of your relationships with your stakeholders is critical to long-term success. Employees need to understand and connect with your purpose; and when they do, they can be your staunchest advocates. Customers want to see and hear what you stand for as they increasingly look to do business with companies that share their values. And shareholders need to understand the guiding principle driving your vision and mission. They will be more likely to support you in difficult moments if they have a clear understanding of your strategy and what is behind it.*
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> . . .
>
> *Most stakeholders – from shareholders, to employees, to customers, to communities, and regulators – now expect companies to play a role in decarbonizing the global economy. Few things will impact capital allocation decisions – and thereby the long-term value of your company – more than how effectively you navigate the global energy transition in the years ahead.*
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> . . .
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> *We focus on sustainability not because we're environmentalists, but because we are capitalists and fiduciaries to our clients. That requires understanding how companies are adjusting their businesses for the massive changes the economy is undergoing. As part of that focus, we are asking companies to set short-, medium-, and long-term targets for greenhouse gas reductions. These targets, and the quality of plans to meet them, are critical to the long-term economic interests of your shareholders. It's also why we ask you to issue reports consistent with the [TCFD]: because we believe these are essential tools for understanding a company's ability to adapt for the future.*[18]

18 See https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter (last accessed 12 June 2023). However, in his 2023 annual letter to investors, Mr Fink expressed his belief that the responsibility for making policy and enacting legislation related to environmental matters rested with governments, rather than with companies, including asset managers like BlackRock, who should not be expected to serve as 'environmental police'. See https://www.blackrock.com/corporate/investor-relations/larry-fink-annual-chairmansletter (last accessed 12 June 2023).

The growing importance of ESG in restructurings

BlackRock and other big players continue to stress how important it is for companies to prioritise the application, compliance and continued monitoring of ESG targets. Other funds, such as Fidelity and PIMCO, family businesses, such as The Rockefeller Foundation, and public and sovereign funds also stand firm on the importance of ESG.

ESG will be key to success in future restructuring proceedings, even if the underlying restructuring is governed by the domestic laws of emerging economies where ESG has not yet had any significant influence on the local environment. Apollo Global Management, Aeroméxico's debtor-in-possession lender in Apollo's Chapter 11 procedure (which concluded satisfactorily during the first quarter of 2022), has declared the importance of ESG for future investments and includes the following in its responsible investing mission statement:

> *Responsible investment considers how environmental, social and governance issues impact the firm, the companies in which Apollo-managed funds invest, the communities in which they operate, and the world at large. At Apollo Global Management and its subsidiaries, we have a long-term practice of using ESG factors in our investment management strategy and believe that careful attention to such factors makes good business sense.*[19]

ESG and the bond market

Mexico's market for ESG bonds is still emerging. ESG bonds, also known as green bonds, social bonds or sustainability bonds, are fixed-income instruments issued by companies, municipalities or governments to raise capital for projects with specific ESG objectives and allow investors to support initiatives that align with their sustainability goals while generating financial returns.

Mexico has shown an increasing interest in sustainable finance and ESG-related initiatives. In recent years, some Mexican companies, financial institutions, and government entities have started to explore and issue ESG bonds.

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19 Apollo, '2018 ESG Summary Annual Report'. See https://www.apollo.com/~/media/Files/A/Apollo-V2/documents/apollo-2018-esg-summary-annual-report.pdf at [2] (last accessed 12 June 2023).

Institutional investors, including AFOREs are showing interest in directing resources towards these types of bonds. According to BIVA, approximately 35 percent (totaling 51 billion pesos) of all long-term corporate debt placements in 2022 comprised bonds with green, social, sustainable, and sustainability-linked criteria, and a similar percentage of 35 percent is anticipated for 2023.[20]

Since the issuance of the first ESG bonds by BMV in 2016, the financing through these instruments has exceeded 200 billion pesos, as reported by CNBV data. Notably for the BMV, the year 2022 marked a significant milestone in sustainable financing, with ESG bonds constituting 44 percent of the total long-term debt through 22 separate issuances,[21] amounting to 88 billion pesos. These encompassed the pioneering blue bond,[22] green bonds, social bonds, sustainable bonds, and sustainability-linked bonds, all of which played a pivotal role in achieving this record-breaking year.[23]

The growth of ESG financing has been exponential, both in terms of amount and number of issuances. In total, 70 thematic bonds have been listed: 29 sustainable, 17 linked to sustainability, 16 green, 7 social and 1 blue. During 2022, the financing of these ESG bonds accounted for 44 per cent of the total debt market amount, while so far this year, it represents 32 per cent as of May 2023. Among the most active issuers of these types of instruments in the BMV are the financial sector (20.16 per cent), followed by the development banking sector (16.54 per cent), consumer staples (15.48 per cent) and infrastructure (13.60 per cent).[24]

According to Bloomberg, the appeal of ESG instruments continues to increase. This year, it is expected that 50 per cent of the debt issuances in Mexico will have some connection to these three elements. The growing interest in these types of instruments is driving the increase in the number of issuances, according to the specialist Luisa Adame from HR Ratings Sustainable Impact. The ESG market is experiencing accelerated growth. According to data from the BMV, in the last three years, the amount and number of thematic bond issuances have

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20 See https://www.eleconomista.com.mx/mercados/Bonos-ASG-seran-el-35-de-todas-la-emisiones-de-deuda-en-Biva-en-2023-20230214-0095.html (last accessed 12 June 2023).

21 Issuers included Femsa, Orbia, Grupo Aeroportuario Centro Norte, Grupo Hérdez, Cocal Cola Femsa, Fonacot, CFE, Banco Compartamos, América Móvil, BBVA, Estado de México and Desarrollos Hidráulicos de Cancún.

22 Blue bonds are issued with the objective of financing projects that contribute to UN Sustainable Development Goal 6, Clean Water and Sanitation.

23 See https://www.bmv.com.mx/docs-pub/sustenta/sustenta_1274583_2022_1.pdf (last accessed 12 June 2023).

24 See https://expansion.mx/mercados/2023/05/11/bonos-asg-bolsa-mexicana-superan-200000-mdp (last accessed 12 June 2023).

grown by more than 400 per cent and at the end of 2022, thematic issuances accounted for 40 per cent of the total debt market on the stock exchange. An example of the increase in issuing thematic instruments was the introduction of sustainability-linked bonds, which showed flexibility in the use of resources. In these debt instruments, companies commit to reducing emissions or environmental impacts within a defined timeframe and percentage. If they fail to meet the targets, the interest rate on the debt instrument will increase as a penalty. [25]

One example of an ESG instrument is the successful bond issuance by BBVA Mexico on the BMV in early 2023, raising approximately 15 billion pesos. This marked their second green bond issuance in the local market and is aligned with their updated Sustainable Debt Financing Framework. The bonds received top credit ratings from Fitch Ratings and Standard & Poor's. The market response was positive, with demand exceeding 18.7 billion pesos, indicating an oversubscription of 1.26 times. Institutional investors, including insurers, pension funds, and investment funds, participated in the issuance. The proceeds will be directed towards financing sustainable transportation and renewable energy projects. In 2022, BBVA Mexico facilitated 65 billion pesos as an intermediary bond underwriter for sustainable bonds in the areas of climate change and social action.[26]

On 5 May 2023, Mexico's Ministry of Finance was awarded by *The Banker* for introducing a sustainable bond in US dollars within the 'Bonds: Sovereign, Supranational and Agency' category. In addition, this year, the bond received recognition from Climate Bonds as the Largest Sovereign Social and Sustainability Bond of 2022. *The Banker* extensively highlighted the bond's distinguishing features, classifying it as an ESG compliant instrument, with a total value of US$1.8 billion and an additional US$486 million available for swaps. It is worth emphasising the substantial demand for this issuance, which reached US$6.5 billion. Notably, 60 per cent of the bond allocation was directed towards ESG investors.[27]

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25 See https://www.bloomberglinea.com/2023/02/22/emisiones-asg-en-mexico-seran-la-mitad-de-la-colocacion-de-deuda-en-el-2023-hr-ratings/ (last accessed 12 June 2023).

26 See https://www.bbva.com/es/mx/sostenibilidad/bbva-mexico-realiza-emision-de-bonos-por-cerca-de-15-mil-millones-de-pesos-en-la-bolsa-mexicana-de-valores/ (last accessed 12 June 2023).

27 See https://www.gob.mx/shcp/prensa/comunicado-no-32-mexico-recibe-premio-por-emision-de-bono-sustentable-en-dolares?idiom=es#:~:text=M%C3%A9xico%20fue%20premiado%20por%20la,%2C%20Supranacionales%20y%20de%20Agencias%E2%80%9D (last accessed 12 June 2023).

Also, in April 2023, Mexico's Ministry of Finance conducted its fourth offering of Sustainable Local Government Bonds (BONDESG) in the domestic financial market under the Reference Framework for Sovereign Bonds linked to the Sustainable Development Goals (SDGs) as part of Mexico's Sustainable Financing Strategy. This is the highest demand recorded for this type of bond, confirming the interest of the investing public in the development of the local sustainable market. The aim of the issuance is to continue promoting the development of the sustainable debt market in the country and strengthen the government's benchmark yield curve so that corporations, state-owned enterprises, and subnational governments can issue thematic financial instruments. Bonds were issued with maturities of two years for an amount of 2.03 billion pesos, three years for an amount of 9.4 billion pesos, and five years for an amount of 3.57 billion pesos, with spreads of 0.15 per cent, 0.1872 per cent, and 0.2395 per cent, respectively. Around 32 domestic investors participated, and the total demand reached 92.1 billion pesos, equivalent to 6.1 times the amount placed. An amount equivalent to the total issued will be allocated to sustainable projects, following the guidelines of the Sustainable Bonds published by the International Capital Market Association (ICMA), and in accordance with the Reference Framework for Sovereign Bonds linked to the SDGs. In this way, the Government of Mexico strengthens its commitment to promoting sustainable financing and the development of bond markets with ESG criteria.[28]

The outlook in Mexico

On 22 June 2020, S&P Dow Jones Indices (S&P DJI) and BMV announced the S&P/BMV Total Mexico ESG Index, which was updated in June 2023.[29] This index provides the local and international investment community with an indicator based on global principles of ESG characteristics. This indicator replaced the S&P/BMV IPC Sustainable Index. The new index uses company selection criteria based on ESG principles. It encompasses a broad set of industries[30]

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28 See https://www.gob.mx/shcp/prensa/comunicado-no-28-hacienda-fortalece-el-mercado-de-deuda-local-sostenible?idiom=es (last accessed 12 June 2023).

29 As of 31 May 2023, there are 28 constituents with a total market cap of 5,442,504.61 Mexican pesos. See: https://www.spglobal.com/spdji/en/idsenhancedfactsheet/file.pdf?calcFrequency=M&force_download=true&hostIdentifier=48190c8c-42c4-46af-8d1a-0cd5db894797&indexId=92393717

30 As at 31 May 2023, the S&P/BMV Total Mexico ESG Index displayed the following sector breakdown: consumer staples accounted for 27.4 per cent of the index, followed by financials at 17.7 per cent, materials at 14.7 per cent, real estate at 13.3 per cent, communication services at 8.1 per cent, industrials at 7.4 per cent consumer discretionary

listed on BMV, but excludes companies involved in the conventional arms and tobacco industries, as well as those that do not meet the requirements of the UN Global Compact.

The aim of creating this new index was to provide greater exposure to the Mexican equity market and, over time, significantly boost ESG performance.

Reid Steadman, managing director and global head of ESG indices at S&P DJI, noted: 'ESG criteria have become a dominant trend in investing as market participants increasingly understand the importance and relevance of the indices that incorporate data and principles of sustainability.' The ESG indices established by S&P DJI add a further element to be considered by investors looking for projects that offer an appealing financial return in a sustainable manner. In recent years, Mexican investors have shown their interest in sustainable financing and responsible investment by supporting new responsible investment opportunities in Mexico, such as the issuance of bonds labelled either 'green', 'social' or 'sustainable' (known as thematic bonds). This has required investors to be aligned with the MX Green Bond Principles, published by Mexico's Consejo Consultivo de Finanzas Verdes (Advisory Council on Green Finance or CCFV) which in turn are allied with the Green Bond Principles published by the International Capital Markets Association.

In Mexico, thematic bonds can be offered as debt instruments, as subordinated debt or as capital instruments or preferred capital for both new and existing projects, as well as for refinancing processes. These bonds will be backed by one of the two authorised stock exchanges in Mexico and have a certification or attestation that the resources will be allocated to sectors considered as eligible (renewable energy, sustainable construction, energy efficiency, clean transportation, water adaptation, waste management, agriculture, bioenergy, forestry and food supply chain).

What comes next?

Companies with strong environmental and social strategies are expected to be the first to issue a new class of assets aimed at reducing carbon dioxide emissions and transitioning to a net-zero carbon future. Mexico is seeking to adopt energy transition bonds to support this market development and help companies achieve

at 7.4 per cent, and healthcare at 4 per cent. These percentages represent the weightings of each sector within the index, highlighting the relative importance of these sectors in terms of their ESG performance in Mexico. See: https://www.spglobal.com/spdji/en/indices/esg/sp-bmv-total-mexico-esg-index/#data (last accessed 12 June 2023).

their decarbonisation goals by 2050. The country has seen significant participation in sustainable bonds, social bonds, and bonds linked to sustainability, but the issuance of transition bonds is still pending. The introduction of a Sustainable Taxonomy in Mexico is considered a crucial step towards promoting energy transition and providing clarity to investors regarding companies' sustainability efforts. The taxonomy will serve as a foundation for potential regulations and incentives in financing, ensuring transparency and alignment of bonds and credits in Mexico. The growing importance of thematic bonds is evident, with their issuance representing a significant portion of the debt capital markets.

Sustainability is thus taking on an increasingly important function, with sustainable finance guiding the destination of investment funds in order to be able to develop projects whose social and environmental purposes play a relevant role. Sustainable financing will be key, to allow the evolution to a new economic paradigm, which encourages new investments based, among other criteria, on parameters that are environmentally friendly and focused on achieving sustainable development.

A new business environment requires new thinking and new elements to be considered. Sustainability, diversity and compliance must be aligned to create a new policy and business environment that redefines policies, objectives and recipients of projects, starting from an integral perspective of environmental care and social inclusion.

Loosely defined, ESG framing, guidance and oversight comes from an array of institutions that influence and help broadly define forward-looking, non-financial reporting. They do so by determining what is material to the long-term sustainability goals of the business, and the interaction of such goals with broader issues of sustainability aligned with the global economy and financial system, the environment, and society, including social values such as human rights. These institutions include a range of issuer information disclosure regulating bodies at national and international levels; exchanges and other self-regulating organisations, and related industry associations, oversight authorities, such as market regulators, and bank and pension fund supervisors; and international organisations that set standards and guidelines regarding responsible investing and sustainability goals. While the many institutions that engage in the ecosystem beyond issuers and investors can help bring relevance, substance and different perspectives, the current state of development merits further attention to ensure these potential benefits are achieved in practice.[31]

31 Boffo, R, and R Patalano (2020), 'ESG Investing: Practices, Progress and Challenges', OECD Paris. See: www.oecd.org/finance/ESG-Investing-Practices-Progress-and-Challenges.pdf (last accessed 12 June 2023).