Case Study:

Success of East Africa's Debut Green Bond Issue: The Case of Acorn Holdings

Abstract

On October 3, 2019, Acorn Holding Limited made history when it issued the first Green Bond in Kenya and by extension, the East African region. In the process, the vertically integrated real estate company, operating out of Nairobi, raised KSh4.3 billion for the development of environmentally friendly student accommodation in the city.

The security, a five-year project bond, was to fund the construction of six purpose-built, student accommodation properties in Nairobi. The projects were benchmarked against International Finance Corporation EDGE Platform (Excellence in Design for Greater Efficiencies) for water use, energy efficiency and low embodied energy in building materials, with the aim of achieving low operational utility costs and low carbon impact to the environment in the long term.

According to Acorn, the choice of a Green Bond to finance the projects was a "natural progression", an affirmation of the firm's sustainability agenda. The firm also says it was keen to attain the highest levels of transparency to aid in the execution of due diligence by investors.

The Acorn Green Bond was also the first deal to evidence the success of the Green Bonds Program-Kenya (GBPK), a private sector-led initiative. The Green Bond Programme - Kenya, which aims to promote financial sector innovation by developing a domestic green bond market, is brought together by the Kenya Bankers Association (KBA), Nairobi Securities Exchange (NSE), Climate Bonds Initiative, Financial Sector Deepening (FSD) Africa and FMO - Dutch Development Bank. The program has also benefited from technical support and guidance from the International Finance Corporation (IFC), the World Bank private sector wing and World Wildlife Fund (WWF)-Kenya.

This Case Study seeks to document the evolution of the Acorn Green Bond as Kenya's pioneer issuance in that category. It seeks to document how Acorn was able to ride on the momentum of an active Green Bonds advocacy program, while borrowing from international best practice and a fairly well developed, albeit untested, local regulatory framework.

Background

Acorn describes itself as a leading integrated real estate business, with its core business currently being the provision of purpose-built rental housing for young people.

Established in 2001, Acorn started with project management, before it developed capacity to develop and manage its own assets. This would grow into an inventory of over 50 projects developed and managed by the firm. With a value topping $550 million, the firm's portfolio includes some iconic real estate in Nairobi, including the former regional headquarters of beverage transnational Coca-Cola and that of consulting giant Deloitte.

In 2015, Acorn Holding Limited was formed, following a partnership with private equity (PE) firm Helios Investment Partners, which has a long history of activity in Africa. The new firm trained its sights on developing and managing "quality, affordable rental accommodation, starting with purpose-built student accommodation (PBSA)," targeted at university and college students.

Acorn's choice of a Green Bond to finance its student accommodation assets was informed by its sustainability antecedents. "Social, environmental, economic and financial considerations are central to the long-term commercial success of our business. In terms of environmental considerations in our building designs, Acorn has made commitment that all its projects will be green resource efficient with climate resilient building design for sustainable urban development, and that these projects would be certified by a third party (IFC Edge).

The firm was also keen to cultivate a transparent framework within which would-be investors would be able to conduct credible due diligence.

"Credible, science-based, widely supported guidelines about what should and should not be considered a qualifying investment helps investors make informed decisions about the environmental credentials of a bond. The Climate Bonds Standard provides clear, sector specific eligibility criteria for assets and projects that can be financed through Climate and Green Bonds," says a company spokesperson.

The Acorn Green Bond

The approval and subsequent issuance of Kenya's first Green Bond was done under the framework of the *Policy Guidance Note on Green Bonds*, which had earlier been issued by the Capital Markets Authority (CMA) in February 2019. It was the first time the policy was being applied and tested.

The Green Bond, issued by Acorn Project (Two) Limited Liability Partnership, was a fixed rate, five-year variant. It was a senior, secured, rated and guaranteed issue. The funding structure was hinged on an upfront commitment with deferred drawdown schedule. Priced at a fixed rate of 12.25 percent per annum, the Acorn Green Bond has a five-year tenure, with an early redemption clause at the issuer's option, with land and developments thereon being the principal security.

The Acorn Green Bond was certified as a green bond by Climate Bonds Initiative (CBI). One special feature of the issuance was the fact that it was a *restricted public offer*. This meant that the issuer was to raise funds from targeted, sophisticated investors only.

GuarantCo, a Private Infrastructure Development Group (PIDG) company, played a key role in the issuance, by providing investors with a partial credit guarantee on 50 percent of the principal and interest due under the KSh5 billion note program. The issuance also benefited from a B1 Stable rating by credit rating agency Moody's, while monitoring and evaluation expertise was provided by MaceYMR, an independent technical advisor.

Outcomes

The Acorn Green Bond issue was successful, raising KSh4.3 billion, against a minimum target threshold of KSh2 billion. The bond's structure incorporated an upfront commitment from investors at financial close, with drawdowns from the said commitments required to be made out periodically, in line with the cashflow needs of the projects being financed. While this structuring was a first in the Kenyan capital market, it was positively received by investors.

By June 30, 2019, Acorn had successfully drawn down KSh1.7 billion of the commitment made by investors, in two tranches. The issue was also successfully listed on the Nairobi Securities Exchange and the London Stock Exchange in January 2020, capping a successful program.

The entire process from conceptualization to issuance took 12 months. Among the key actions on the roadmap were preparation of commercial heads of terms; preparation of legal documentation and IM (Information Memorandum) and submission of the application to CMA. Other actions before the bond issuance were submission of green bond certification; financial model audit by EY; credit rating by Moody's; investor engagement through site visits and road shows and the Opening of the Offer.

The Acorn Green Bond attracted significant interest from the elite, sophisticated investors it was targeted at. Among the key takers were local pension schemes, commercial banks, insurance and reinsurance companies and a DFI. A key investor in the green bond was the Emerging Africa Infrastructure Fund (EAIF), a PIDG company like GuarantCo, which chalked up KSh1.297 billion worth of bonds and is currently the largest single investor in the program.

Being a trailblazer in the Kenyan and East African green bond markets and having stress-tested the country's regulatory regime and extant human resource capacity, and found them adequate, it is hoped that the Acorn Green Bond will trigger an active pipeline of similar issues, going forward.

The then CMA Chief Executive Paul Muthaura, said on approving the Acorn Green Bond issuance on August 15, 2019: "This issuance is a critical step in advancing the development of an effective ecosystem to support the establishment of green capital markets in Kenya, in line with the Marrakech Pledge of 2016, now that the necessary legal instruments are in place to facilitate such issuances."

According to *Africa Green Finance*, a blog that tracks green finance developments on the continent, the Acorn bond was the fifth in Africa in 2019, taking the overall inventory way past the $2 billion milestone, to a cumulative total of over $2.114 billion.

Enabling factors and Lessons

Being Kenya's and indeed the region's first green bond, Acorn was launching into uncharted territory when it thought of such an instrument to finance its real estate investments. There was no precedent to benchmark within East Africa, with most out of Africa's inventory of 17 green bonds mostly domiciled in the south, west and north of the continent. Market awareness of what a green bond is, and its benefits were limited. It did not help that the issuance was done against the backdrop of a jittery market, whose confidence had just been pricked by a series of corporate bond defaults.

Still, a number of unique factors underwrote the issuance's overall success:

- **Facilitative regulatory regime:** Earlier in the year, in February, the regulator Capital Markets Authority had issued its *Policy Guidance Note on Green Bonds.* This seminal work was to be the regulatory playbook for the issuance.
- **Strong advocacy and green finance movement:** Despite a paucity of green bond issuances in Kenya, a strong and active pro-green finance lobby and movement had already taken root in the country through the GBPK. The GBPK had done landmark work in quantifying and documenting the green finance opportunity in Kenya through a series of surveys. Besides GBPK, the issuer also worked with Guarantco and the PIDG Group. These organizations have a mandate to develop and deepen the capital markets by promoting sustainable financial instruments.
- **Government support:** The GBPK has had direct government support. Besides having been endorsed by the National Treasury, Central Bank of Kenya Governor, Dr. Patrick Njoroge is the patron.
- **Existing pipeline of assets:** Acorn Holdings already had an active conveyor belt of assets with ESG (Environmental, Social and Governance) credentials. This means that it was relatively easy to identify and certify qualifying assets.
- **Narrowcasting:** Being a *restricted public offer*, the book-building process was targeted at sophisticated investors only. This ensured significant uptake in a market where most fund managers do not have explicit ESG mandates.

1. **Pricing:** Priced at a fixed rate of 12.25 percent per annum, the return on the Acorn Green Bond was over 200 basis points above the Government Bond of the same tenor at the time of issue. Investors tend to compare the yield on any issuance with that of a Government bond of an equivalent tenure, while making investment decisions.

2. **Guarantee:** The provision to investors of a partial guarantee to cover 50 percent of the principal and interest due under the KSh5 billion note program by GuarantCo, was a major enabler, materially improving the risk profile and ultimately, the attractiveness of the bond.
3. **Commercial viability:** A growing youth population and rapid urbanization have created growing demand for accommodation targeted at this demographic. This realization is behind the inclusion of Affordable Housing as one of the pillars of the Big 4 Agenda, the government's latest blueprint for economic takeoff. The nexus between the demand for clean, safe, conducive, amenable and yet affordable housing and Acorn's own accent on sustainability impact has spawned a viable, bankable proposition.
4. **Outsourced Expertise:** Acorn worked with credible partners to ensure that the bond was structured in the highest standards. These partners included Climate Bonds Initiative (green bond certification); Moody's (credit rating); MaceYMR (Bond holders' technical advisor); IFC Edge (green certification of the projects) and GuarantCo (guarantee). The financial model for the green bond was audited by EY.

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