Why Banks Issue Sustainability-Linked Loans: Evidence on Motives and Consequences

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Abstract

Sustainability-linked loans (SLLs), the innovative sustainable finance product, have raised considerable interests among lenders and borrowers. In this study, we include 1103 deals of SLLs worldwide from 2017 to 2022. We first examine the incentives of SLLs issuers and find that banks with higher credit risk and lower profitability are more likely to issue SLLs. Next, by using the non-sustainability loans as control group, we find that banks charge higher loan margins on SLLs than other loans, implying the bank's incentive to achieve higher loan margins. Further, we examine the subsequent impact of SLLs issuance on banks' risk profiles and borrowers' performance. Our findings reveal that increases in the volume of SLLs issuance are positively associated with a higher proportion of Stage-1 loan classifications under IFRS 9, as well as with the change in borrowers' profitability. These results suggest that SLLs contribute to enhanced banks' loan quality and borrowers' performance. Overall, the study provides early evidence on SLLs, a booming area experiencing rapid growth in response to the global move toward sustainability.

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