

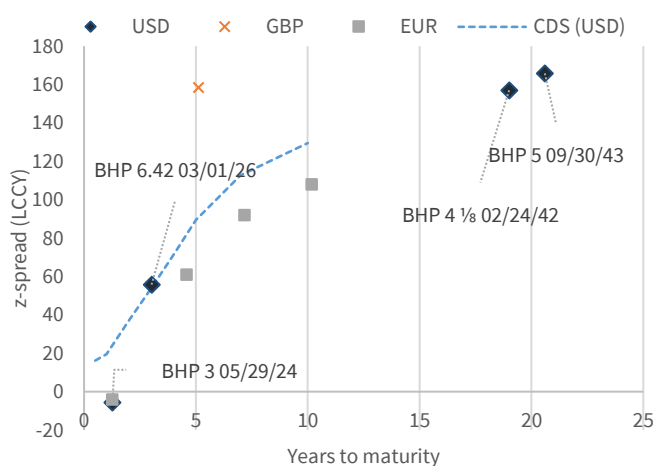
# BHP: Think big with an SLB

Stéphanie Mielnik, CFA<sup>(\*)</sup>, Josephine Richardson, Ulf Erlandsson

Mining giant BHP is looking to tap the USD bond market for the first time in ten years with three tranches (3, 5 and 10 years). The bonds are expected to price today (23 Feb 2023).<sup>1</sup> Barclays, BofA Securities, BNP, MUFG and Santander will act as joint bookrunners. The bonds have an expected rating of A2/A- (Moody's/S&P).

BHP is one of the largest coal miners in the world. In 2021 they made some successful coal divestments.<sup>2</sup> More recently its strategy has shifted, reportedly both due to surging coal prices and reduced investor concerns.<sup>3</sup> Retaining Mt Arthur coal mine seems to be alongside an extension of its operating life from 2026 to 2030, which is still shorter than attempts to offer it for sale with an operating life to 2045. While divestment can clean up a company for its investors, the bigger picture can be that the problem is pushed elsewhere, often with less oversight and transparency.<sup>4</sup>

Figure 1. BHP bond spreads (USD, EUR, GBP) and CDS curve (USD).  
Source: AFII, Bloomberg, accessed 23 Feb 2023.



**Below, we propose an alternative Sustainability-Linked Bond (SLB) structure that would involve targets on Scope 1, 2 and 3 emissions as well as a 100% reduction in thermal coal reduction, in line with the company's earlier commitments. In our view, this would open up the potential for more investors to invest in the name as part of a credible transition story.**

**We also discuss how stronger documentation can be added, with language allowing investors to 'put-back' their debt, if specific decommissioning objectives are not achieved. Such a structure would likely lead to lower funding costs for the company as well as a higher probability of better environmental outcomes.**

<sup>1</sup> We are cognizant that this deal might have priced by the time of publication, however, we believe the key ideas could be translated to other and future issuances.

<sup>2</sup> BHP sold its stakes in BHP Mistui Coal to Stanmore Resources and in the Colombian Cerrejón mine to Glencore in 2021. See "[BHP reaps up to \\$1.35bn from Australia coal mines in fossil fuels retreat](#)", Financial Times, 8 Nov 2021.

<sup>3</sup> "[BHP Abandons Thermal Coal Exit as Investors and Prices Shift](#)", Bloomberg, 16 June 2022.

<sup>4</sup> For an example of this please see "[Sembcorp: Carbon footprint arbitrage of a lifetime](#)", AFII, 6 Nov 2022.

Not investment advice. This version 23 Feb 2023. Important disclaimers at end of the document.

(\*) Anthropocene Fixed Income Institute ([www.anthropocenefii.org](http://www.anthropocenefii.org)), Author for contacts: [sbm@anthropocenefii.org](mailto:sbm@anthropocenefii.org)

## Existing debt

Table 1 shows the outstanding bonds from BHP, and Figure 1 shows recent market pricing. What is notable is how long it has been since the company came to market; most recently in 2015 for a EUR deal. It last raised USD debt nearly ten years ago in September 2013.

Table 1. BHP outstanding bonds. Source: Bloomberg, accessed 23 Feb 2023.

Description	ISIN	Issue Date	Maturity	Currency	Amount	
						Outstanding
BHP \$4.125 42s	US055451AR98	24-Feb-12	24-Feb-42	USD	1,000,000,000	
BHP €3 24s	XS0787786440	29-May-12	29-May-24	EUR	560,134,000	
BHP €3.25 27s	XS0834385923	25-Sep-12	24-Sep-27	EUR	750,000,000	
BHP £4.3 42s	XS0834399981	25-Sep-12	25-Sep-42	GBP	1,000,000,000	
BHP £3.25 24s	XS0834399635	25-Sep-12	25-Sep-24	GBP	463,043,000	
BHP €3.125 33s	XS0924998809	30-Apr-13	29-Apr-33	EUR	750,000,000	
BHP CAD3.2 23s	CA05545FAA53	14-May-13	15-May-23	CAD	750,000,000	
BHP \$5 43s	US055451AV01	30-Sep-13	30-Sep-43	USD	2,500,000,000	
BHP \$3.8 23s	US055451AU28	30-Sep-13	30-Sep-23	USD	734,413,000	
BHP €1.5 30s	XS1224955408	28-Apr-15	29-Apr-30	EUR	750,000,000	

A lot has changed in that time with regards to investor attitude to environmental impact, and it will be interesting to see appetite for an infrequent issuer in an emissions-intensive sector.

## Coal divestment history

In 2020, BHP put its open-pit Mt Arthur Coal mine up for sale.<sup>5</sup> Companies such as Yancoal and Adani Enterprises expressed interest, but BHP failed to attract a viable offer and announced in June 2022 its intention to retain Mt Arthur Coal mine in its portfolio.<sup>6</sup> BHP's initial mining consent allows the company to operate the mine until June 2026. In 2021, BHP presented to its stakeholders a plan to seek an approval to extend Mt Arthur Coal operations to 2045.<sup>7</sup> After scrapping the mine's sale plan, the company announced it will seek to extend operation to 2030 instead of 2045, after which it will close the mine.<sup>8</sup> According to BHP's annual report,<sup>9</sup> the Mt Arthur coal mine produced 14Mt of thermal coal in 2022. In 2020, the mine was listed amongst the then biggest operating coal mines in the world, based on recoverable coal reserves.<sup>10</sup>

## SLB structure

Although the company has clearly stated emissions reduction targets, there are concerns regarding how it plans to effectively align its capital expenditures with its decarbonization plan.<sup>11</sup> An ambitious SLB can alleviate such concerns by aligning the company's capital with specific targets, thereby providing bond investors with a hedge against potential shifts in the company's strategy. There is precedent for SLBs in the mining sector. In September 2022, Anglo American issued a €745mm SLB with three KPIs; one linked to direct emissions, one to water usage, and one to local job creation.<sup>12</sup>

<sup>5</sup> ["BHP puts Australian thermal coal mine up for sale: sources"](#), Reuters, 23 June 2020.

<sup>6</sup> ["BHP Abandons Thermal Coal Exit as Investors and Prices Shift"](#), Bloomberg, 16 June 2022.

<sup>7</sup> ["Mt Arthur Coal – Continuation project"](#), BHP, March 2021.

<sup>8</sup> ["Coal divestment review update - BHP to retain New South Wales Energy Coal"](#), BHP, 15 June 2022.

<sup>9</sup> ["BHP - 2022 annual report"](#).

<sup>10</sup> ["The ten biggest coal mines in the world"](#), Mining Technology, 3 Jan 2002.

<sup>11</sup> ["BHP Group Limited - Final Company Assessment"](#), Climate Action 100+, 9 Sept 2022.

<sup>12</sup> ["Anglo-American launches €745 million sustainability-linked bond"](#), 14 Sep 2022.

Table 2. An example of KPIs and targets that could be used in an SLB issued by BHP Group. Source: AFII.

KPI	Baseline date	Baseline value	SPT	Target Date
<b>Operational emissions (Scope 1+2) - Absolute(MtCO2-e)</b>	2020	16.2	-30%	2030
<b>Scope 3 emissions - Absolute (MtCO2-e)</b>	2020	415.7	-23%	2030
<b>Thermal coal output (Mt)</b>	2022	18	0	2030

BHP sustainability goals target a 30% reduction in operational (Scope 1 & 2) GHG emissions by 2030, and net zero Scope 1, 2 & 3 by 2050.<sup>13</sup> The company’s 2030 Scope 3 target focuses on supporting technologies and pathways to reduce emissions in the steelmaking industry (that account for a large portion of Scope 3 emissions) and shipping of BHP products. Its Scope 3 2050 target addresses the whole supply chain value without explicitly mentioning energy suppliers – the prime customers for thermal coal.

BHP concedes itself that achievement of its Scope 3 net zero target is uncertain. For an SLB to be effective in this space, and to depend on decommissioning of coal mines, Scope 3 emissions must be included, and interim targets prior to 2050 must be set and validated. Applying a linear interpolation between 2020 and 2050, we estimate the company could set a 2030 Scope 3 reduction target of -23%. Such an estimation is highly indicative and subject to a further scientifically approved target.

In addition to emissions, and to focus on coal decommissioning, absolute thermal coal output could be used. This would be a clearer metric on which to set future targets, transitioning towards zero production in 2030. The focus is on clearly defined numerical metrics, which are scientifically validated, with near-term targets.

We summarize in Table 2 a set of proposed KPIs and associated targets. We believe that these targets could be calibrated such that an actual pricing of the SLB could come inside the pricing of traditional bond tranches.<sup>14</sup>

We have also heard talk of stronger covenants, perhaps involving a put-back option for investors in the event of missing certain environmental objectives. This approach could be used here, with investors able to put-back the debt if the Mt Arthur Coal mine were not decommissioned by a specific date. We believe such a clause would give investors comfort that it is a true transition instrument, and they would effectively be withdrawing funding should the decommissioning objective not be achieved.

<sup>13</sup> “[Sustainability](#)” & “[Climate Change](#)”, BHP, accessed 23 Feb 2023.

<sup>14</sup> For full details please see “[An option pricing approach for sustainability-linked bonds](#)”, AFII, 8 Nov 2022. We would be happy to discuss how to achieve this, please contact the authors.

**IMPORTANT DISCLAIMER:**

*This report is for information and educational purposes only. The Anthropocene Fixed Income Institute ('AFII') does not provide tax, legal, investment or accounting advice. This report is not intended to provide, and should not be relied on for, tax, legal, investment or accounting advice. Nothing in this report is intended as investment advice, as an offer or solicitation of an offer to buy or sell, or as a recommendation, endorsement, or sponsorship of any security, company, or fund. AFII is not responsible for any investment decision made by you. You are responsible for your own investment research and investment decisions. This report is not meant as a general guide to investing, nor as a source of any specific investment recommendation. Unless attributed to others, any opinions expressed are our current opinions only. Certain information presented may have been provided by third parties. AFII believes that such third-party information is reliable, and has checked public records to verify it wherever possible, but does not guarantee its accuracy, timeliness or completeness; and it is subject to change without notice.*

*Any reference to a company's creditworthiness or likelihood of positive or negative performance in the current or future market is purely observational and should not be taken as a recommendation or endorsement or critique of such company or security.*

*The Anthropocene Fixed Income Institute is a non-profit organization "to monitor, advocate for and influence the impact of the fixed income and bond markets in the age of human induced climate change." For more information about the Institute, please visit [www.anthropocenefii.org](http://www.anthropocenefii.org) or follow us using the hashtag #anthropocenefii.*

*AFII is not in any way associated with, nor are any of its directors, employees or advisors, any of the companies it references in its materials or reports and is not receiving compensation or consideration of any nature for its observations and/or insights.*

