SUSTAINALYTICS
a Morningstar company

SUSTAINALYTICS
SUSTAINABLE FINANCE SOLUTIONS

Second-Party Opinion on Sustainability-Linked Loans

Introduction to Sustainalytics' Corporate Solutions

Sustainalytics, a Morningstar Company, is a leading global ESG research, ratings, and data firm supporting corporations and their financial intermediaries to consider sustainability issues in their policies, practices, and capital projects. As the leading second-party opinion provider in the market, Sustainalytics offers issuers credible verification on the use of proceeds for sustainable finance products. Corporations also leverage Sustainalytics' ESG Risk Ratings to understand and promote their ESG performance with their internal and external stakeholders. The firm has received awards in recognition of its ESG solutions and opinion services, most recently from Climate Bonds Initiative, Environmental Finance and GlobalCapital. With 17 offices globally, Sustainalytics has more than 1,200 staff members, including more than 500 analysts with varied multidisciplinary expertise across more than 40 industry groups. For more information, visit www.sustainalytics.com

What Sustainability Linked Loans Are And How They Work

A Sustainability Linked Loan (SLL) is a loan instrument that links a borrower's performance on sustainability issues that are material and relevant to its business and sector with the terms of the loan. Accordingly, an SLL incentivizes the borrower to achieve their agreed upon performance objectives known as Sustainability Performance Targets (SPTs), such as an improved ESG rating, carbon emissions or other KPIs.

SLLs can be used for general corporate purposes as the terms are tied solely to the borrower's ESG- related performance and not the use of proceeds or the projects financed by the loan. The flexibility of this type of instrument, along with the benefits of improving a company's overall ESG performance, makes it an attractive option for borrowers across many sectors, including those that may not be considered "green".

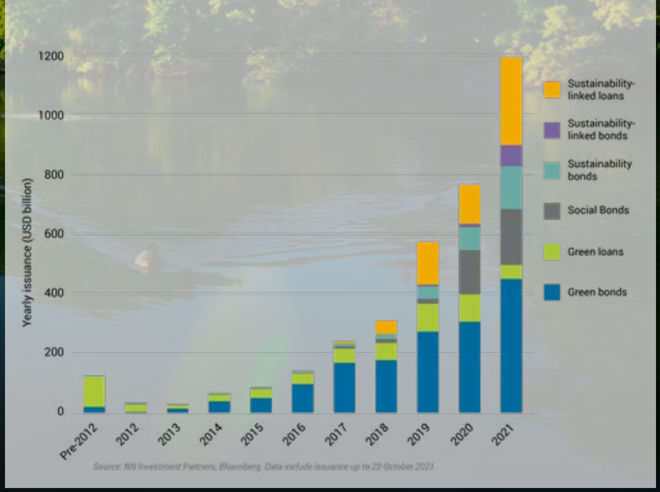
Sustainable Linked Loans' Evolution Trends

For nearly three decades, investors have increasingly focused on the impact of their investment decisions on the environment and key stakeholders. In recent years, forward-looking lenders have also put sustainability at the core of their allocation strategies, resulting in a growing demand for sustainable finance products. According to accenture Sustainable-linked lending skyrocketed from $5 billion in 2017 to $120 billion in 2020.

SLLs are an opportunity for lenders to manage ESG risks by incorporating sustainability considerations in their lending decisions and encouraging better reporting from issuers on sustainability issues that are material and relevant to the business and sector.

Source: https://www.accenture.com/gr-en/insights/banking/sustainable-lending

Sustainable Loans and Bonds Issued by Type



Sustainable Linked Loans—Key Benefits

Key Benefits for Banks

- Expand lending portfolios and meet firm-wide sustainability financing commitments
- Incentivize corporate clients to improve their sustainability performance
- Leverage credible third-party ratings and opinions to accelerate the lending process
- Support positioning as sustainable finance leader
- Assist to meet public commitments made for sustainable finance
- Deeper relationships and engagement with customers

Key Benefits for Companies

- Access to discounted loan rates
- Improve overall sustainability performance
- Demonstrate sustainability commitment to stakeholder
- Flexibility to use the funds for general corporate purposes
- Deepen relationship and interactions with banks
- Drive internal alignment across the business

The goal of the Sustainability Linked Loan Principles (SLLP) is to:

- Promote the development and preserve the integrity of sustainability linked loans.
- Provide guidelines which capture the fundamental characteristics of these loans.
- Promote sustainable development, aligning the ESG and financial performance of companies.
- Set out a framework, enabling all market participants to clearly understand the characteristics of a sustainability-linked loan.

Core Components of SLLPs:

1 Selection of Key Performance Indicators (KPIs)

The KPIs chosen should be relevant, material, follow a consistent methodology and able to be benchmarked.

2 Borrower's Sustainability Strategy

Borrower's sustainability strategy should be ambitious using benchmarks and should be consistent with the issuer's sustainability strategy.

3 Loan Characteristics

Disclose how the economic outcome is linked to whether the selected predefined SPT(s) are met.

4 Reporting

Transparently report on the KPI performance on an annual basis.

5 Verification

Performance level against each SPT for each KPI at least once a year.

Key Concepts

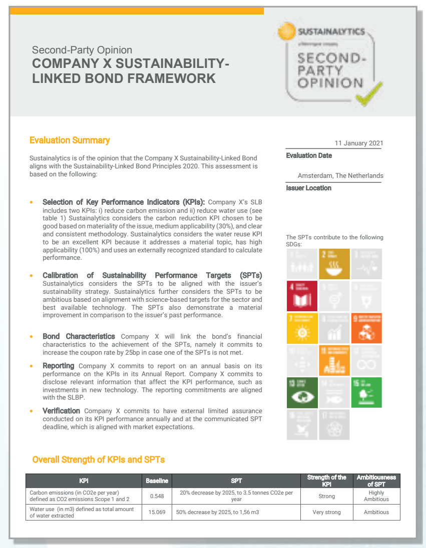
Materiality and Relevance

The SLLP require KPIs to address the borrower's relevant, core and material sustainability issues. Therefore, credible KPIs should address key areas of company impact related to environmental and social issues. Often companies have an impact on several sustainability issues, and thus may choose to focus on one or two key impact areas. To align with best practice in the selection of KPIs, issuers should focus on their most important areas of impact on environmental and/or social issues.

Ambitiousness

The SLLP recommend assessing the ambitiousness of the SPTs by using a combination of the following approaches:

1. Benchmarking against past performance, for which the issuer's performance on selected KPIs over the last three years is used to determine whether the SPTs are set beyond the company's historical performance trajectory.
2. Peer comparison, which includes a comparison of the issuer's SPTs against peer performance and targets set by other companies in the same sector and with similar business models.
3. Benchmarking against science includes a comparison against science-based targets. Science-based targets are set to align a company's pressure on global resources with the carrying capacity of global or local ecosystems. In case science-based targets are not available for a specific sector, best available technology can also be used as a proxy.


Second-Party Opinion
COMPANY X SUSTAINABILITY-LINKED BOND FRAMEWORK

SUSTAINALYTICS
SECOND-PARTY OPINION

Evaluation Summary

Sustainalytics is of the opinion that the Company X Sustainability-Linked Bond aligns with the Sustainability-Linked Bond Principles 2020. This assessment is based on the following:

- **Selection of Key Performance Indicators (KPIs):** Company X's SLB includes two KPIs: i) reduce carbon emission and ii) reduce water use (see table 1) Sustainalytics considers the carbon reduction KPI chosen to be good based on materiality of the issue, medium applicability (30%), and clear and consistent methodology. Sustainalytics considers the water reuse KPI to be an excellent KPI because it addresses a material topic, has high applicability (100%) and uses an externally recognized standard to calculate performance.
- **Calibration of Sustainability Performance Targets (SPTs)** Sustainalytics considers the SPTs to be aligned with the issuer's sustainability strategy. Sustainalytics further considers the SPTs to be ambitious based on alignment with science-based targets for the sector and best available technology. The SPTs also demonstrate a material improvement in comparison to the issuer's past performance.
- **Bond Characteristics** Company X will link the bond's financial characteristics to the achievement of the SPTs, namely it commits to increase the coupon rate by 25bp in case one of the SPTs is not met.
- **Reporting** Company X commits to report on an annual basis on its performance on the KPIs in its Annual Report. Company X commits to disclose relevant information that affect the KPI performance, such as investments in new technology. The reporting commitments are aligned with the SLBP.
- **Verification** Company X commits to have external limited assurance conducted on its KPI performance annually and at the communicated SPT deadline, which is aligned with market expectations.

11 January 2021
Evaluation Date

Amsterdam, The Netherlands
Issuer Location

The SPTs contribute to the following SDGs:

Overall Strength of KPIs and SPTs

KPI	Baseline	SPT	Strength of the KPI	Ambitiousness of SPT
Carbon emissions (in CO2e per year) defined as CO2 emissions Scope 1 and 2	0.548	20% decrease by 2025, to 3.5 tonnes CO2e per year	Strong	Highly Ambitious
Water use (in m3) defined as total amount of water extracted	15.069	50% decrease by 2025, to 1,56 m3	Very strong	Ambitious

These approaches help to assess ambitiousness from different angles. Sustainalytics' evaluation of the SPTs' ambitiousness will be built on one or several of the benchmarking approaches outlined above.

Our Offer

Second-Party Opinion

To support the credibility of the sustainability-linked loans market, Sustainalytics offers a Second-Party Opinion Service (SPO) on the SLL which covers the following:

1. Detailed evaluation on the alignment of the SLL with the five core components of the SLLP.
2. Assessment of the strength of the borrower's sustainability strategy.
3. Contribution of the loan to the Sustainable Development Goals.

Annual Review

The SLLP requires borrowers to receive a verification at least once a year. With Sustainalytics' SPO Annual Review you can provide additional assurance to your lenders and the market on the performance levels against your SPTs by demonstrating that you follow up on your sustainability commitments. With the SPO annual review, Sustainalytics will verify the KPI reporting practices, the methodology used for calculating the KPI performance, as well as the alignment with the SPTs.

Use of Proceed SPO

Sustainalytics' Opinion evaluate the alignment of the client's Green/ Social/Sustainability/ Transition Bond Framework with the respective International Capital Markets Association (ICMA) Bond Principles and market expectations. For transition use of proceeds bonds, Sustainalytics provides an external review of the alignment of the bond with the Sustainalytics' transition eligibility criteria or with internationally established decarbonization pathways.

Key benefits of Second-Party Opinion

Gain investors/ lenders confidence
A SPO from a leading ESG research, ratings and data firm, like Sustainalytics, provides provides additional assurance on the credibility of the issuer/ borrower.

Enhance Awareness of Environmental or Social Issues
Issuers/Borrowers can highlight their green assets or their work in addressing sustainability goals to investors and other stakeholders.

Meet Market Expectations
A SPO assesses the alignment of the bond/loan framework with recognized International Capital Market Association's (ICMA) Principles.

Use of Proceeds, Key Performance Indicators and Sustainability Performance Targets
A SPO assesses the impact of use of proceeds and relevance/ambitiousness of linked instruments.

Meet Growing Investor / Lenders Demand
As the importance of sustainability grows, an increasing number of investors / borrowers are making pledges on climate action and sustainable finance.

Diversify Issuer Investor / Lender Base
The demand for thematic bonds is high and green, social and sustainability bonds tend to be oversubscribed.

Second-Party Opinion Process

Sustainalytics will take a collaborative and time-efficient approach to engaging and coordinating with various teams within your organization. We will effectively identify key follow-up points and communicate with relevant teams/persons directly, thereby reducing coordination efforts.

Sustainalytics commonly holds two or three phone calls with relevant teams, followed by email communication to receive relevant documents and clarify any questions.

1 Kick off meeting
- Understand issuer's loan and sustainability objectives
- Understand KPIs and SPTs
- Understand reporting process and loan characteristics
- Identify relevant document for evaluation

2 Evaluation
- Evaluate selection of KPIs and calibration of SPTs
- Evaluate KPIs, reporting process and frequency
- Assess alignment of the loan with sustainability strategy
- Draft an option

3 Feedback
- Provide draft document to client
- Receive feedback
- Provide updated draft document to Sustainalytics' Internal Review Committee
- Receive feedback from client and the Committee

4 Final Document
- Finalize evaluation
- Update opinion
- Receive client sign-off

5 Marketing
- Provide marketing support as requested by the borrower

Post issuance (optional)

6 Annual Review
- Review KPI Performance and alignment with SPT
- Review methodology and reporting practices as aligned with commitments made to investors

Why Sustainalytics

25+ years
ESG experience and developing innovative solutions.

Largest Second-Party Opinion Provider
As recognized by Environmental Finance and the Climate Bonds Initiative.

Global presence
With offices in 17 locations.

Our analysts speak over **40 languages**.

End-to-End ESG Solutions
ESG Products and services that serve the entire value chain.

Single Market Standard
Connsistent approach to ESG assessments across investment spectrum.

Recent Awards

Are you interested in learning about how a Second-Party Opinion on your Sustainability-Linked Loan can support your borrowing or lending strategy?

Contact us today to connect with our team of experts.

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