Sustainalytics’ Opinion

Downer Group Sustainability Linked Loan

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Location of Borrower: Australia
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Introduction

Downer Group (Downer, the “company”, or the “borrower”) is an integrated service company active primarily in Australia and New Zealand, but also in the Asia-Pacific region, South America and Southern Africa. With more than 52,000 people employed across more than 300 sites, Downer designs, builds, and sustains assets, infrastructure and facilities.

Downer is negotiating a Sustainability Linked Loan (SLL) where the interest rate of the loan is tied to Sustainability Performance Targets (SPTs) that include four Key Performance Indicators (KPIs) associated with the company’s material sustainability-related issues.

The company has engaged Sustainalytics to review the SLL and provide an opinion on the alignment of the loan with the Sustainability Linked Loan Principles (SLLP).

As part of this engagement, Sustainalytics held conversations with various members of the company’s management team to understand the SPTs and associated KPIs, the company’s sustainability strategy, as well as the processes that it has in place to verify its performance in relation to the SPTs. Sustainalytics also reviewed relevant public documents.

This document contains Sustainalytics’ opinion of Downer’s SLL, reviewed against the SLLP.

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Alignment with the Sustainability Linked Loan Principles 2019

The four core components of the Sustainability Linked Loan Principles are:

1. Relationship to Borrower’s Overall Corporate Social Responsibility (CSR) Strategy
2. Target Setting – Measuring the Sustainability of the Borrower
3. Reporting
4. Review

Sustainalytics is of the opinion that the Downer SLL aligns to the four core components of the Sustainability Linked Loan Principles 2019.

Section 1: Relationship to Downer’s overall sustainability strategy

Downer has demonstrated its commitment to its sustainability strategy through the following efforts, as reported in its Sustainability Report 2020:

- Downer identified 11 material issue and 7 important issues during its materiality assessment undertaking. The issues identified are those that are most material to their business and stakeholders
and have the potential to affect the future success of Downer. The material issues that relate to the Downer SLL include:

- Climate change
- Health, safety & wellbeing of their employees
- Diverse and inclusive workplace

- The material issues were chosen by first developing a universe of potential material issues. Using this list as a base, a materiality survey was sent to a representative sample of stakeholders to gauge stakeholder importance of these issues. Stakeholder interviews were also conducted to provide qualitative input. Results of this process were presented to Downer’s Zero Harm Board Committee for validation and approval.

- Downer’s selected KPIs are linked to the material topics identified above. Downer has established an FY2020 baseline for its four SLL SPTs as follows:
  - Related to Climate change, Downer sets Scope 1 and Scope 2 emissions reduction targets. Downer also commits to having its GHG emission reduction target validated by the Science Based Target Initiative (SBTi)\(^4\).
  - Related to Health, safety & wellbeing of their people, Downer commits to continuous mental health and first aid training for its employees.
  - Related to Diverse and inclusive workplace, Downer has targeted to deliver cultural awareness training.

- In 2019, Downer’s Asset Services business\(^5\) formed Project 1.5°C. The project explores CO\(_2\) reduction opportunities such as energy efficiency, renewables, alternative fuels, and hydrogen, among others. The project is intended not only to lower Downer’s carbon footprint, but also to support Downer’s customers to lower their footprint as well. The project is a key component to Downer’s commitment to setting and meeting science-based targets.

- In addition to setting an SPT of a Scope 1 and Scope 2 carbon emissions reduction target based on climate science,\(^6\) Downer will submit this target to the Science Based Targets Initiative\(^7\) for verification and approval. Downer will also seek to satisfy the requirements for Scope 3 emissions reduction target setting under the SBTi methodology and submit the appropriate Scope 3 reduction targets for validation. This validation will provide external validation that the targets are ambitious enough to contribute to meeting the goals of the Paris Agreement.\(^8\)

- Downer has implemented several targets and objectives related to governance and ethical conduct. The Board consists of a majority of independent Directors, which is reviewed and assessed by a Nominations and Corporate Governance Committee. Multiple Board committees carry out Downer’s strategic direction including Audit and Risk, Zero Harm, Remuneration, Disclosure, etc. In addition, executive remuneration is aligned with sustainability performance.\(^9\)

Sustainalytics is of the opinion that Downer’s sustainability strategy, management systems, and actions demonstrate the company’s commitment to improving its sustainability performance. The company’s SPTs and KPIs are aligned with the company’s sustainability strategy. Given this alignment and Downer’s approach to sustainability, Sustainalytics is of the view that the SLL will help to advance the company’s overall sustainability strategy.

**Section 2: Target Setting**

The Sustainability Linked Loan Principles state that appropriate SPTs should be negotiated and set between the borrower and lender for each loan transaction. As outlined in the SLLP, a borrower may elect to tie the interest rate of the loan to improved performance on KPIs associated with the company’s material sustainability-related issues. Sustainalytics’ ESG Risk Rating\(^10\) identifies Carbon – Own Operations as one of

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\(^4\) In the context of performance targets under the SLLP, a binary action does not necessarily indicate a performance action. However Sustainalytics nonetheless considers the process for setting carbon reduction targets under the SBTi to be a valuable and meaningful action to ensure the credibility and ambition of emission reduction targets.

\(^5\) The Asset Services business provides maintenance and solutions for industrial services, oil and gas, and power generation customers across Australia.

\(^6\) Targets adopted by companies to reduce greenhouse gas (GHG) emissions are considered “science-based” if they are in line with what the latest climate science indicates is necessary to meet the goals of the Paris Agreement. i.e. to limit global warming to well below 2°C above pre-industrial levels and pursue efforts to limit warming to 1.5°C.

\(^7\) The Science Based Targets Initiative is a joint initiative by CDP, UN Global Compact, WWF, and WRI. https://sciencebasedtargets.org/

\(^8\) https://unfccc.int/process-and-meetings/the-paris-agreement/the-paris-agreement

\(^9\) Executive remuneration has a fixed component and a component that varies with performance (including sustainability performance).

\(^10\) See Appendix for ESG Risk Rating methodology. Payment for performance assessed over one year is a Short-Term Incentive (STI). Payment for performance over a three-year period is a Long-Term Incentive (LTI). Sustainability performance is linked to Downer’s STI.
the most material sustainability issues for the Industrial subindustry (see rationale below). Downer’s SPTs are based on the following KPIs:

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<th>SPT</th>
<th>KPI</th>
<th>KPI definition</th>
<th>Baseline Date</th>
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| Reduction of CO₂ emissions intensity by  | Science Based Target Scope 1 & 2 Emissions Intensity                 | A Scope 1 and 2 greenhouse gas emissions reduction, where reduction methodology is based on climate science. Emissions reduction is on an intensity basis, leading to an absolute reduction. Scope 1 emissions refer to direct emissions that are the result of the firm’s own operations (i.e. company owned facilities or vehicles). Scope 2 emissions refer to purchased electricity, steam, heating & cooling for the company’s own use.  
| 16.48% by 2026, or stretch target of 26.49% by 2026. | Tonnes CO2-e/AU$m                                                    |                                                                                                                                                                                                              | 2020          |
| CO₂ emissions intensity target external approval | Science Based Targets Validated with the Science Based Targets Initiative (“SBTi”) Approval by SBTi | This binary KPI reflects whether the Scope 1 and 2 emissions reduction target described above is validated by the Science Based Targets Initiative. In addition, Downer will satisfy the requirements for Scope 3 emissions reduction target setting under the SBTi methodology and submit the appropriate Scope 3 reduction targets for validation.  
| Deliver 18,654 hours of training between 2021 to 2026 | Indigenous Cultural Awareness Training, Te Ara Whanake & Te Ara Maramatanga Training | Indigenous Cultural Awareness Training (ICAT) consists of two programs including: a 35-minute eLearn training targeted at Supervisor and above level; and a 30-minute eLearn training targeting the remaining workforce. These trainings are designed to develop existing knowledge and cultural competence of Downer’s leaders and workforce to understand the history, cultural norms and protocols of Aboriginal and Torres Strait Islander peoples.  
| Provision of 2,600 certificates of completion between 2021 to 2026 | Mental Health First Aid Training Employees trained annually | Mental Health First Aid Training is an Accredited programme by Mental Health First Aid Australia. It is a one and a half day programme available to all Downer employees. Having initially been offered to the highest risk individuals (Fly in, Fly Out employees), in 2019 Downer expanded the Mental Health First Aid Training out across the entire business. Upon completion of the course the |

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12 According to the SBTi, if a company’s scope 3 emissions account for at least 40% of total scope 1, 2, and 3 emissions, a scope 3 target should be set. The scope 3 target boundary of all scope 3 targets should collectively cover two thirds of total scope 3 emissions. Science-Based Target Setting Manual: [https://sciencebasedtargets.org/wp-content/uploads/2017/04/SBTi-manual.pdf](https://sciencebasedtargets.org/wp-content/uploads/2017/04/SBTi-manual.pdf)
13 Downer is currently in the process of performing their Scope 3 greenhouse gas accounting
14 In FY2020, Downer delivered 3,922 hours of training.
15 In FY2020, Downer trained 763 employees. Mental Health First Aid Training in 2020 was an establishment year hence why numbers are high, training for 2021 and 2022 is forecast to be significantly reduced due to Covid-19 restrictions affecting delivery. Training will gradually increase and accumulate post FY2022 and return to levels that allows Downer to maintain and exceed Gold standard Mental Health First Aid Awareness accreditation levels.
individuals can become accredited Mental Health First Aiders (MHFA). Topics include depression; anxiety; psychotic illness; substance use disorders; multiple crisis scenarios such as suicide, panic attack, critical incident management and aggressive behaviours.¹⁶

Sustainalytics is of the opinion that the KPIs selected by Downer are material to its business model. The KPIs are directly linked to identified material issues, and improvements in performance on these KPIs by Downer is expected to lower the company's carbon emissions intensity and enhance its sustainability, diversity, and employee health and wellbeing more generally. Therefore, on this basis, Sustainalytics is of the opinion that linking performance improvements to its loan is meaningful and appropriate and will contribute to mitigating material Sustainability risks associated with the company’s core business.

With respect to material issue Carbon – Own Operations, Industrial conglomerates involved in manufacturing businesses use large amounts of energy mainly for manufacturing operations, which include processing, producing or assembling products. In addition, extensive facilities have electricity requirements for lighting, heating and air conditioning. Good energy management is necessary for companies in the industry to mitigate risks from energy price volatility and carbon regulations. Energy management can lead to significant operational efficiencies and annual cost savings of up to US 20 million annually for industrial conglomerates. Best practice in the industry includes widespread, group-wide implementation of energy efficiency measures, such as retrofitting or upgrading equipment and streamlining processes; increased renewable energy on-site generation or the purchase of green power; adoption of environmental and energy management systems certified to ISO 14001 and ISO 50001; and collection, monitoring and public reporting of emissions data. Downer has identified some key decarbonization strategies that could include, for example, divestment/disposal of carbon intense business lines, increased uptake of renewables, energy efficiency measures, and fuel switching.

Providing cultural awareness training to its employees promotes a workplace that values diversity and inclusion internally in the company, and with external partners. In FY2020, Downer’s Australian operations spent AUD $47.3 million (EUR 28.3 million) with Indigenous suppliers, demonstrating commitment to engaging with a diverse range of partners.

The mental wellbeing of staff is an emerging issue for Downer, and within the industry. It is estimated that one in six working age people will suffer from mental illness, and one-sixth of the population will have symptoms associated with mental ill-health.¹⁷ Mental Health Management is part of Downer’s Zero Harm strategy.¹⁸ Recognising the importance of mental health, Downer formed its Group Health function in 2018 to initially focus on changing the conversation around mental health by reducing stigma and empowering people by providing strategies and activities that support their mental health and wellbeing. The mental health KPI will enable Downer to further support its employees by offering targeted training for high risk employees, and/or employees who hold significant influence within the firm to be able to assist their peers’ mental health.

The SLLP specify that targets should be based on recent measurements of selected KPI performance. Sustainalytics notes that Downer’s baseline performance was validated by an independent auditor and reported in the company’s Downer Sustainability Report by 2020, which falls within the SLLP’s suggested time period of the previous 6-12 months.

Section 3: Reporting

The SLLP recommends that borrowers make and keep readily available up-to-date information relating to their SPTs. Downer is demonstrating best practice by committing to annual reporting that confirms the annual performance on each of the 4 KPIs and the related impact on the margin. The first report will be provided by no later than 31 October 2021, with each subsequent report published by no later than 31 October each year. The annual KPI values will be disclosed in Downer’s Sustainability Report and certified by an external consultant.

Section 4: Review

Downer’s annual KPI data will be validated by an external consultant. This validation process is a committed undertaking within the facility agreement. GHG emissions reporting is conducted in the Envizi environmental data management system and is subject to an internal review and validation process by Downer’s internal Environment and Sustainability function. Data for training is extracted from the various Learning Management Systems and aggregated for internal review by the Learning and Development function. A process has been

¹⁶ Due to Covid-19, these courses have moved online, however numbers remain restricted to ensure quality of delivery.
established to formalise this review with an internal signoff process, where the Manager Learning and Development and Group Manager Learning and Development will review on a quarterly basis. This will be applied for FY2021 data and beyond.

Additionally, Sustainalytics will review and opine on the alignment of the KPIs, and Downer’s SLL with the SLLP. This is a Condition Precedent to financial close.

Sustainability Review Events can be triggered in cases of pre-defined change of Downer’s scope of Business / emissions profile as well as in cases of pre-agreed variation in number of employees.

Sustainalytics believes that Downer’s external assurance practices will enhance credibility and transparency of underlying information linked to the company’s SPTs.

Conclusion

Sustainalytics is of the opinion that Downer’s SLL will support the company’s overall sustainability strategy and efforts to contribute to the low-carbon transition, strengthen diversity and inclusion within the organization, and foster a safer work environment. In addition, the use of KPIs associated with the company’s sustainability-related issues as a basis for target-setting is aligned with the Sustainability Linked Loan Principles, and the borrower has committed to disclosing progress against their SPT on an annual basis. Based on the above considerations, Sustainalytics is of the opinion that Downer’s SLL is aligned with the SLLP.
Appendix 1: About the Sustainalytics ESG Risk Rating

With a clear focus on financial materiality, Sustainalytics’ ESG Risk Ratings measure the degree to which a company’s enterprise value is exposed to material ESG issues. Specifically, the ratings measure a company’s exposure to industry-specific material ESG risks and how well a company is managing those risks. This multi-dimensional way of measuring ESG risk combines the concepts of management and exposure to arrive at an assessment of unmanaged ESG risk. The ESG Risk Rating for a company is a quantitative score based on a scale from 0-100 and is categorized between five levels of risk: negligible, low, medium, high and severe. The numerical assessments represent units of unmanaged ESG risk, with lower scores representing less unmanaged ESG risk. The risk assessments are absolute, meaning that a high-risk assessment reflects a comparable degree of unmanaged ESG risk relative to any other company in the research universe.
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