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Second Party Opinion

CTT Group's Sustainability Linked Financing Framework

Jan. 24 2023

CTT Group (CTT) is a publicly listed company headquartered in Lisbon, Portugal. It is a multi-service postal and financial operator and the incumbent postal public service provider in Portugal. In 2021, the company transported 484.6 million items of addressed mail and 32.7 million express parcels in Portugal, in addition to 41.1 million express parcels in Spain. Although CTT has its own fleet of 4000 vehicles, it primarily leverages outsourced transportation from third parties.

In our view, CTT's Sustainability Linked Financing Framework, published in January 2023, is aligned with:

-  Sustainability-Linked Bond Principles, ICMA, 2020
-  Sustainability-Linked Loan Principles, LMA/LSTA/APLMA, 2022

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Issuer's Sustainability Objectives

CTT has developed its sustainability linked financing framework to further align its funding activities with its sustainability commitments. It hopes that the framework will display to its stakeholders its long-term sustainability strategy, with ESG one of the main pillars for its internal transformation and long-term growth.

A core focus of CTT's ESG strategy is to reduce its greenhouse gas emissions. The company received approval from the Science Based Target Initiative (SBTi) for its target in 2017, which is the sustainability performance target (SPT) that the framework references. The target set in 2017 was adopted from that set by the International Post Corp. (IPC) for the wider sector. The company is now in the process of validating a newer target with the SBTi, given the initiative requires targets to be revalidated every five years. Therefore, this new target is not covered under this framework.

Selected Key Performance Indicators (KPIs) And Sustainability Performance Targets (SPTs)

KPI	SPT	Baseline	2021 performance
Absolute scope 1, 2, and 3 carbon emissions	Reduce absolute scope 1, 2, and 3 emissions 30% by 2025 versus the 2013 base year in tons of carbon dioxide equivalent (tCO2e)	60,719.7 tCO2e (2013)	48,317.3 tCO2e

Second Party Opinion Summary

Selection of key performance indicators (KPIs)

Alignment  CTT's Sustainability Linked Financing Framework is aligned with this component of the Principles.

KPI 1 Absolute scope 1, 2, and 3 carbon emissions Not aligned Aligned **Strong** Advanced

Calibration of sustainability performance targets (SPTs)

Alignment  CTT's Sustainability Linked Financing Framework is aligned with this component of the Principles.

SPT 1 Reduce absolute scope 1, 2 and 3 emissions 30% by 2025 versus the 2013 base year Not aligned Aligned **Strong** Advanced

Instrument characteristics

Alignment  CTT's Sustainability Linked Financing Framework is aligned with this component of the Principles.

Instruments under the framework will be subject to a step-up margin, margin adjustment, or premium payment, which will result in an overall increase in interest rate for the period. The specific mechanism will be specified in the respective instrument's transaction documentation. CTT does not describe any fallback mechanisms for the case where performance cannot be measured in a satisfactory manner.

Reporting

Alignment  CTT's Sustainability Linked Financing Framework is aligned with this component of the Principles.

Score Not aligned Aligned **Strong** Advanced

CTT commits to publish reporting on the progress of the KPI against the SPT on an annual basis in its integrated annual report, Carbon Disclosure Project (CDP) report, or similar report. This will include a verification assurance report produced by an independent external auditor on the progress against the KPI and information to help investors monitor the progress of the KPI against the SPT.

Post-issuance review

Alignment  CTT's Sustainability Linked Financing Framework is aligned with this component of the Principles.

CTT commits to independent and external verification of its performance level for the KPI. This certificate will be published on CTT's website on a yearly basis.

Framework Assessment

Selection of key performance indicators (KPIs)

The Principles make optional recommendations for stronger structuring practices, which inform our relevancy opinion as aligned, strong, or advanced. For each KPI, we consider how relevant the KPI is for sustainability by exploring the clarity and characteristics of the defined KPI; its significance for the issuer’s sustainability disclosures; and how material it is to the issuer’s industry and strategy.

 CTT’s Sustainability Linked Financing Framework is aligned with this component of the Principles.

KPI 1 Absolute scope 1, 2, and 3 carbon emissions	Not aligned	Aligned	Strong	Advanced
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We consider the KPI selected by CTT to be strong, with its scope, objective, and calculation clearly outlined. Carbon emissions, particularly those related to outsourced transportation (scope 3) are highly material for the sector, including CTT. We view favorably that the scope of the KPI covers approximately 74% of the company’s total emissions, including the most material emission categories for scope 1, 2, and 3, notably fuel consumed by its own fleet (scope 1) and outsourced transportation (scope 3). We particularly view the inclusion of scope 3 emissions as a relative strength of the framework, given their materiality in the industry. On the other hand, the KPI excludes CTT Express Spain due to data consolidation issues. Furthermore, scope 3 emissions do not include those related to CTT’s banking services. However, we do not view these to be material given the services are aimed at individuals, not corporations, and therefore are typically less energy intensive.

The KPI is directly related to CTT’s sustainability strategy and vision to be at the forefront of environmental commitments and reducing carbon emissions. Furthermore, the company carries out an annual materiality assessment in consultation with its stakeholders. The 2021 assessment found that climate change is the most relevant topic for such stakeholders.

A further strength of the framework is that CTT outlines its reasoning for selecting the KPI. The KPI is in line with that used for a target previously set by the IPC. The company adopted this target in 2017 and subsequently received validation from the SBTi.

Calibration of sustainability performance targets (SPTs)

The Principles make optional recommendations for stronger structuring practices, which inform our ambition opinion as aligned, strong, or advanced. We consider the level of ambition for each target by assessing its clarity and characteristics, how the issuer defines the target with reference either to its past performance, or to external or competitor benchmarks, and how it explains what factors could influence future performance.

 CTT’s Sustainability Linked Financing Framework is aligned with this component of the Principles.

SPT 1 Reduce absolute scope 1, 2, and 3 emissions 30% by 2025 versus the 2013 base year	Not aligned	Aligned	Strong	Advanced
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We believe the ambition, clarity, and characteristics of the SPT are strong. The SPT clearly outlines the expected timeline for target achievement and the baseline. About 20% of the target was achieved between 2013 and 2021 (eight years), with the remaining 10% required between 2021 to 2025 (four years). As such, the level of ambition is in line with historical performance.

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In addition, CTT has benchmarked its target compared to international peers in the sector, finding that it is roughly in line with their short-term targets. Furthermore, the company is identifying external factors beyond its control that may affect the SPTs, such as regulation.

The strategy to reach the target is well outlined, with the largest share of reductions expected from more efficient transport including a switch to electric fleets and route optimization. We anticipate this to be more challenging than previous steps, which have primarily focused on scope 2 emissions such as a shift to more renewable energy sources. This further supports the ambitiousness of the target, in our view. Future energy consumption reduction (scope 2) is planned through more efficient technology, investments in on-site renewables, and the purchase of guarantee-of-origin energy from renewable sources. Although the use of guarantee-of-origin certificates is very common, we view it as having less benefit than other mechanisms that directly translate into an expansion of renewable energy generation, such as power purchase agreements, or increases in energy efficiency.

One limitation of the framework is that the target has not been validated by the SBTi since 2017, having been submitted in line with a well below 2 degrees Celsius (°C) scenario. The SBTi requires targets to be reviewed every five years from the date of approval to remain valid. Furthermore, the target is less ambitious than those currently being submitted to the SBTi, specifically given the SBTi now encourages greater efforts toward a 1.5°C trajectory.

Baseline

2013	2025
60,719.7 tCO2e	42,500 tCO2e
	Equivalent to 30% reduction

Instrument characteristics

The Principles require disclosure of the type of financial and/or structural impact involving trigger event(s), as well as the potential variation of the instrument's financial and/or structural characteristics.

 CTT's Sustainability Linked Financing Framework is aligned with this component of the Principles.

We consider the instrument characteristics aligned. CTT discloses that instruments under the framework will be subject to a step-up margin, margin adjustment, or premium payment should it fail to satisfy the SPT at the target observation date. This will result in an increase in the interest rate for the period. Furthermore, some sustainability-linked loans issued under the framework may also include step-down margin provisions when SPTs are reached in a timely manner. There will be no more than one step-up margin or margin adjustment over the life of each instrument. The details of the KPI, SPT, and instrument characteristics will be specified in the specific documentation of each transaction.

One limitation of the framework is that it does not describe any relevant fallback mechanisms for the case where performance cannot be measured in a satisfactory manner. In addition, considering the short time frame between the framework (2022) and SPT (2025), the financial materiality of the incentive structure of certain debt instruments issued under the framework could be limited.

Reporting

The Principles make optional recommendations for stronger disclosure practices, which inform our disclosure opinion as aligned, strong, or advanced. We consider plans for updates on the sustainability performance of the issuer for general purpose funding, or the sustainability performance of the financed projects over the lifetime of any dedicated funding, including any commitments to post-issuance reporting.

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CTT's Sustainability Linked Financing Framework is aligned with this component of the Principles.

Disclosure score

Not aligned

Aligned

Strong

Advanced

We consider CTT's overall reporting practices to be strong.

CTT commits to reporting progress made on the KPI, in addition to the achievement of the SPT, annually until the target date of all financing issued under the framework. The reporting will also include a verification assurance report conducted by an independent external auditor outlining the progress of the KPI against the SPT.

In addition, reporting will include information that may help investors monitor KPI progress against the SPT. A strength of the reporting is that it will include information about recalculations of the level of carbon emissions in the base year, if any.

Reporting will be available in CTT's integrated annual report, CDP report, or a similar report.

Post-issuance review

The Principles require post-issuance review commitments including the type of post-issuance third-party verification, periodicity and how this will be made available to key stakeholders. Our opinion describes whether the documentation is aligned or not aligned with these requirements. Please note, our second party opinion is not itself a post-issuance review.



CTT's Sustainability Linked Financing Framework is aligned with this component of the Principles.

We consider the post-issuance review commitments aligned. CTT commits to having its performance against carbon targets verified by an external auditor on a yearly basis. In particular, a limited assurance certificate will be made available in CTT's annual sustainability report.

Mapping To The U.N.'s Sustainable Development Goals

The Sustainable Development Goals (SDGs), which the United Nations (U.N.) set up in 2015, form an agenda for achieving sustainable development by 2030.

CTT's Sustainability Linked Financing Framework intends to contribute to the following SDGs:

KPI	SDGs
Absolute scope 1, 2, and 3 carbon emissions	 13. Climate action [§]

[§]The KPI is likely to contribute to the SDGs.

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