



VGP Group

Green Finance Second Opinion

06.11.2019

VGP is a developer, owner and manager of logistics real estate. The company is headquartered in Belgium and owns logistics centers in 11 countries across continental Europe as of year-end 2018. The issuer owns, in whole or in part, 81 buildings and an additional 1 buildings in different stages of development. The issuer is the operator of each building while third party tenants rent the buildings for their logistics activities. The issuer has accelerated its climate related activities recently and is taking the first steps to position itself as a driver of transition in the real estate sector.

Proceeds will be allocated to renewable energy, green buildings, energy efficiency, pollution prevention and control (waste management), clean transportation and sustainable water management. Proceeds can be allocated to projects in all regions where VGP is active. All project categories are connected to the logistics buildings. According to VGP, initial proceeds will be allocated to refinancing while new developments are added on an ongoing basis.

Several of VGP's buildings use natural gas from existing gas networks for heating, however, efficiency improvements in such heating systems are not eligible under this framework. Buildings with gas-fired heating systems may be eligible under the green building category, given environmental certification.

The issuer has appropriate policies in place to support the framework. The rollout of rooftop solar systems across the portfolio and mandatory BREEAM "very good" certification for new buildings from January 2020 have been decided. The selection process is clearly defined. The issuer will provide annual reporting to investors and lenders on a portfolio basis. The Sustainability Executive Committee is willing to remove controversial projects. Currently, VGP does not report on emissions but is preparing to do so in the future.

Based on an assessment of the framework's alignment with the Green Bond and Green Loan Principles, the project categories and governance score, the framework receives the overall **CICERO Medium Green** Shading and **Governance Score of Good**. The proceeds of the inaugural transaction will be allocated to green buildings, shaded light-to-medium green, and renewable energy, shaded dark green. The overall shading assumes that proceeds will be allocated in a balanced way. The buildings category would be strengthened by energy efficiency targets to systematically reduce emissions from fossil heating and electricity in regions with high grid emission factors. The governance score would be strengthened by emissions reporting, targets for reducing emissions, and scenario analysis with a focus on transition of the transport sector.

SHADES OF GREEN

Based on our review, we rate the VGP's green finance framework **CICERO Medium Green**.

Included in the overall shading is an assessment of the governance structure of the green finance framework. CICERO Shades of Green finds the governance procedures in VGP's framework to be **Good**.



GREEN BOND / GREEN LOAN PRINCIPLES

Based on this review, this Framework is found in alignment with the Green Bond and Green Loan Principles.





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1 Terms and methodology

This note provides CICERO Shades of Green's (CICERO Green) second opinion of the client's framework dated October 2019. This second opinion remains relevant to all green bonds and/or loans issued under this framework for the duration of three years from the launch of the first transaction under the framework, as long as the framework remains unchanged. Any amendments or updates to the framework require a revised second opinion. CICERO Green encourages the client to make this second opinion publicly available. If any part of the second opinion is quoted, the full report must be made available.

The second opinion is based on a review of the framework and documentation of the client's policies and processes, as well as information gathered during meetings, teleconferences and email correspondence.

Expressing concerns with 'shades of green'

CICERO Green second opinions are graded dark green, medium green or light green, reflecting a broad, qualitative review of the climate and environmental risks and ambitions. The shading methodology aims to provide transparency to investors that seek to understand and act upon potential exposure to climate risks and impacts. Investments in all shades of green projects are necessary in order to successfully implement the ambition of the Paris agreement. The shades are intended to communicate the following:

CICERO Shades of Green



Dark green is allocated to projects and solutions that correspond to the long-term vision of a low carbon and climate resilient future. Fossil-fueled technologies that lock in long-term emissions do not qualify for financing. Ideally, exposure to transitional and physical climate risk is considered or mitigated.



Medium green is allocated to projects and solutions that represent steps towards the long-term vision, but are not quite there yet. Fossil-fueled technologies that lock in long-term emissions do not qualify for financing. Physical and transition climate risks might be considered.



Light green is allocated to projects and solutions that are climate friendly but do not represent or contribute to the long-term vision. These represent necessary and potentially significant short-term GHG emission reductions, but need to be managed to avoid extension of equipment lifetime that can lock-in fossil fuel elements. Projects may be exposed to the physical and transitional climate risk without appropriate strategies in place to protect them.



Brown is allocated to projects and solutions that are in opposition to the long-term vision of a low carbon and climate resilient future.

Examples



Wind energy projects with a strong governance structure that integrates environmental concerns



Bridging technologies such as plug-in hybrid buses



Efficiency investments for fossil fuel technologies where clean alternatives are not available



New infrastructure for coal

Sound governance and transparency processes facilitate delivery of clients' climate and environmental ambitions laid out in the framework. Hence, the governance aspects are carefully considered and reflected in the overall shading of the green finance framework. CICERO Green considers four factors in its review of the client's governance processes: 1) the policies and goals of relevance to the green finance framework; 2) the selection process used to identify and approve eligible projects under the framework, 3) the management of proceeds and 4) the reporting on the projects to investors. Based on these factors, we assign an overall governance grade: Fair, Good or Excellent.



2 Brief description of VGP's green finance framework and related policies

VGP Group is developer, manager and owner of logistics real estate. VGP is headquartered in Belgium but has operations in 11 countries all across continental Europe. VGP owns and operates some buildings under its own name. Other projects are sold to two Joint Venture (JV) companies, in which VGP and Allianz Real Estate hold 50 % each. VGP is always responsible for facility management, including those assets that are owned by one of the JVs. As of year-end 2018, VGP's portfolio consists of 13 completed buildings and 15 buildings under construction. The JV portfolio consists of 68 completed buildings and 4 buildings under development across continental Europe.

Environmental Strategies and Policies

According to the issuer, VGP has been paying increased attention to climate and environmental matters over the past year. The driving forces behind this were tenants, expressing growing interest and demands for improving the environmental footprint of facilities, and the management leadership of VGP, which wants to position VGP as an active contributor to the climate related transition. According to the issuer, ambitions for building certifications, renewable energy installations and other environmental investments are strategic and will be pursued irrespective of obtaining green financing.

As per its company building code, the issuer develops all buildings, including those sold to the JVs, in accordance with the BREEAM "Very Good" standard. Up to this point, the actual certification has only been obtained if the tenant in question requested this. However, VGP has decided that all new buildings will obtain the official BREEAM "Very Good" or equivalent certification from January 2020, including projects under construction. According to the issuer, tenants bear the costs of certification and VGP will turn away potential customers should they not be willing to bear these costs. VGP has not defined any additional targets for energy efficiency in its buildings.

The company has installed rooftop solar panels on 9 of its buildings with a total installed capacity of 12,5 MWp, with another 17 MWp under construction. VGP aims to fit all its facilities' roofs with solar panels. Fixed timelines or targets for installed capacity have not been adopted. According to the issuer, the complexity of the various national regulations for rooftop solar make it difficult to precisely schedule the rollout.

Currently, VGP does not include emissions data or climate risk reporting according to the recommendations by the TCFD in its reporting. According to the issuer, the assessment of climate risks is currently being updated while internal capacities are being established in order to be able to report on climate risk exposure at a later point in time.

The issuer does not employ climate scenarios at this point. The assessment of physical risk and resiliency happens according to industry standards or under the BREEAM certification regime. Policies for suppliers and contractors currently safeguard local laws and regulations in climate and environmental matters. Policies that may pose stricter demands for suppliers and contractors are still under development. For construction projects, the management of local environmental concerns is guided by the BREEAM framework in addition to local laws and regulations.



The framework allows for the issuing of green bonds, green private placements and green (syndicated) loans. In the following these will collectively be referred to as green financial instruments.

Use of proceeds

Proceeds from green financial instruments issued under this framework can be used to finance or refinance, in whole or in part, projects from the mitigation categories renewable energy and energy efficiency. In addition, the framework defines as eligible project categories green buildings, pollution prevention and control (waste management), clean transportation, and sustainable water management. The latter categories are summarized under the term “environmental friendly projects” in the framework. All eligible types of projects are connected to VGP’s buildings. Eligible projects can be enacted in all regions where VGP is active. According to the issuer, the main share of proceeds will be allocated to green buildings and renewable energy solutions.

According to the framework, eligible projects can be enacted in logistics assets which are wholly owned by VGP as well as those owned by the JV companies. According to the issuer, proceeds will initially be allocated to refinance existing projects, while new projects will be added on an ongoing basis.

The issuer confirmed that proceeds will not be allocated to fossil or nuclear energy assets. However, many of VGP’s buildings use natural gas for heating, according to the issuer. It was confirmed that the energy efficiency category does not allow for investments in such fossil heating systems.

Selection

The selection process is a key governance factor to consider in CICERO Green’s assessment. CICERO Green typically looks at how climate and environmental considerations are considered when evaluating whether projects can qualify for green finance funding. The broader the project categories, the more importance CICERO Green places on the governance process.

As a precondition to be considered for green financing, assets need to comply with all local laws and regulations, including environmental and social requirements. Projects are proposed by internal departments at VGP’s headquarters. The proposed projects will be assessed by the Sustainable Executive Committee. This committee is expected to consist of members from Executive Management, Finance and the Technical department. Some committee members from the Project Development Department have experience with the BREEAM certification process. It is the committee’s responsibility to control whether projects comply with internal policies and the eligibility criteria. If accepted, eligible projects are added to the Green Portfolio Register. The Sustainable Executive Committee is currently being established. Thus, governance around decision making has not been finalized yet.

VGP’s building code is modeled after the BREEAM certification standard. This is the framework which guides the issuer’s assessments of potential ESG risks for new developments. The issuer is open to remove such projects from green financing that cause considerable public opposition.

Management of proceeds

CICERO Green finds the management of proceeds of VGP to be in accordance with the Green Bond Principles.

VGP’s Finance department is responsible for managing net proceeds from green financing instruments. According to the issuer, proceeds will not be credited to a separate account as the issuer expects full allocation upon issuance. Proceeds will be allocated to eligible projects on a portfolio level on an annual basis or in shorter intervals.



Proceeds will be tracked and managed on a portfolio basis as opposed to tracking of each green financing instrument individually. The Finance department will keep track of eligible assets in the Green Portfolio Register.

It is the responsibility of the Finance department to ensure that allocations of proceeds from green finance instruments to eligible projects are proportional to the ownership share VGP holds in the asset where a project will be financed. This is the case for all assets owned by the two JV companies in which VGP holds a 50 % share.

Projects that do no longer fulfill the eligibility criteria are removed from the register and replaced with other eligible projects if possible. If there are no eligible projects available, temporarily unallocated proceeds will be managed along VGP's financial criteria. According to the issuer, these criteria allow bank deposits only.

Reporting

Transparency, reporting, and verification of impacts are key to enable investors to follow the implementation of green finance programs. Procedures for reporting and disclosure of green finance investments are also vital to build confidence that green finance is contributing towards a sustainable and climate-friendly future, both among investors and in society.

The issuer will provide reporting to investors and lenders on an annual basis as part of VGP's annual report, or more frequently. Reporting is led by the Finance department and will include information on the total outstanding amounts in Green Bonds, Green Private Placements, and Green (syndicated) Loans issued under this framework; the Green Portfolio Register; the allocation of proceeds per project category; any unallocated loan amounts and the distribution between financing of new projects and refinancing. At this point, instruments with a maturity of under one year are not planned. Should such instruments become an option in the future they will be included in the reporting.

VGP's annual impact reporting will cover the amount of renewable energy capacity installed on properties owned by VGP and the JV companies. Depending on the availability of data, the issuer aims to also report on annual generation of renewable energy (KWh), the related avoided CO₂ emissions¹, the number of environmental certifications and the certification level, energy savings from energy efficiency projects (KWh), quantity of recycled material (metric tonnes), number of electric vehicle charging stations installed, freshwater savings (m³), and possibly other indicators. Impact reporting will be done on a portfolio basis.

The issuer confirms that its ownership share of a facility will be taken into account in the reporting.

The issuer intends to obtain post-issuance verification of its reporting of the use of proceeds by an external party upon full allocation. The verification report for the use of public green bond proceeds will be published, while reports for other types of instruments, like loans and private placements, may only be presented to private placement investors or lenders. The issuer has not taken a final decision on these details yet. This independent review will be published on VGP's website.

¹ The issuer has not yet finalized the methodology for calculating avoided emissions.



3 Assessment of VGP's green finance framework and policies


The framework and procedures for VGP's green bond investments are assessed and their strengths and weaknesses are discussed in this section. The strengths of an investment framework with respect to environmental impact are areas where it clearly supports low-carbon projects; weaknesses are typically areas that are unclear or too general. Pitfalls are also raised in this section to note areas where VGPs should be aware of potential macro-level impacts of investment projects.

Overall shading

Based on the project category shadings detailed below, and consideration of environmental ambitions and governance structure reflected in VGP's green finance framework, we rate the framework **CICERO Medium Green**.

Eligible projects under the VGP's green finance framework

At the basic level, the selection of eligible project categories is the primary mechanism to ensure that projects deliver environmental benefits. Through selection of project categories with clear environmental benefits, green bonds aim to provide investors with certainty that their investments deliver environmental returns as well as financial returns. The Green Bonds Principles (GBP) state that the "overall environmental profile" of a project should be assessed and that the selection process should be "well defined".

Category	Eligible project types	Green Shading and some concerns
Renewable Energy 	<ul style="list-style-type: none">Onsite renewable energy generation facilities. This includes solar, wind and geothermal energy projects.	Dark Green <ul style="list-style-type: none">✓ Increasing the share of renewable energy in national electricity mixes is an essential part of achieving the long-term net zero emissions future.✓ The issuer should be mindful of the potential for heavy metal pollution from geothermal energy.✓ Wind power projects have caused public opposition in several countries lately. The issuer has confirmed the willingness to remove controversial projects from green financing if opposition is widespread.



Green
Buildings



- Buildings which have received or will receive BREAAAM “Very Good” certification (or equivalent DGNB/LEED rating)

Light to Medium Green

- ✓ Several existing eligible facilities use natural gas for heating. Also new buildings with natural gas-fired heating systems can qualify under this category, provided certification.
- ✓ Buildings with gas-fired heating systems are connected to existing gas networks. VGP does not have buildings with oil-fired heating in its portfolio.
- ✓ Be aware of potential for lock-in effects with regards to new developments which use fossil fuel for heating.
- ✓ BREEAM “very good” does not require improvements in energy efficiency. Additional targets to improve energy efficiency would be a more effective measure to reduce the energy footprint of buildings especially since many facilities are heated with natural gas and are often located in areas with a high grid emissions factor (e.g. Germany).

Energy
Efficiency



- Measures in existing (logistics) buildings, warehouses and installations
- insulation, LED relighting, motion detectors, energy monitoring tools

Medium Green

- ✓ Energy efficiency thresholds would make improvements more transparent and traceable
 - ✓ The issuer should consider the potential for rebound effects for energy consumption
 - ✓ The issuer has confirmed that efficiency improvements in fossil installations are not eligible.
-



Pollution
prevention and
control



- Projects, investments and expenditures which promote better waste recycling rates.

Dark Green

- ✓ Waste recycling is an essential activity in a low carbon society and part of the long-term solution.
- ✓ Investments aim to improve third party tenants' adherence to local recycling rules. Concrete targets have not been defined. Waste to energy is not included.
- ✓ Due to the geographic spread across continental Europe it is unclear how separated plastic waste will be treated after separation by a tenant (e.g. waste to energy incineration, recycling)
- ✓ The issuer should consider life-cycle emissions of waste and be aware of potential lock-in effects where plastic waste is incinerated after collection.

Clean
Transportation



- Electric vehicle charging stations
- bike facilities

Dark Green

- ✓ Supporting infrastructure for electric transportation is part of the long-term net zero emissions future.
- ✓ Installation of charging stations depends on the third-party tenant and is not automatically included in new developments.
- ✓ The issuer informs us that access to public transport is a key criterion for land purchase for new developments

Sustainable
water and
wastewater
management



- reduction of freshwater consumption
- capturing and recycling rainwater
- green roofing

Dark Green

- ✓ Sustainable water and wastewater management is part of the necessary adaptation to a changing climate

Table 1. Eligible project categories



Background

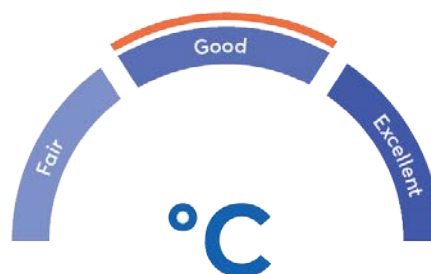
In a low carbon 2050 perspective, the energy performance of buildings is expected to be improved, with passive house technology becoming mainstream and the energy performance of existing buildings greatly improved through refurbishments. Efficiency of building envelopes needs to improve by 30% by 2025 to keep pace with increased building size and energy demand – in addition to improvements in lighting and appliances and increased renewable heat sources.² Energy efficiency improvements in buildings are thus important building blocks towards reaching the 2°C goal. In addition to energy efficiency, CICERO Green assess if there is any screening for potential impacts from more extreme weather events, such as flooding. Flood risk for properties, is of particular concern in vulnerable geographic regions such as close to rivers or lakes. We also factor in if there have been any considerations around transportation solutions and environmental impacts in the construction phase of the building (building material and waste considerations). CICERO Dark Green shading is in particular difficult to achieve in the building sector because buildings have a long lifetime. CICERO Dark Green shading in the building sector should therefore conform to strict measures and is reserved for the highest building standards, Zero-Energy buildings and passive houses that comply with a 2050 low-carbon perspective.

According to the issuer, a large part of the building portfolio is located in Germany. In terms of number of added heating devices in 2016 in Germany, according to the Bundesverband der Deutschen Heizungsindustrie e.V., 76% were gas based, 10.3% oil based, 3.3% biomass based and 11.5% were heat pumps³.

Governance Assessment

Four aspects are studied when assessing the VGP's governance procedures: 1) the policies and goals of relevance to the green finance framework; 2) the selection process used to identify eligible projects under the framework; 3) the management of proceeds; and 4) the reporting on the projects to investors. Based on these aspects, an overall grading is given on governance strength falling into one of three classes: Fair, Good or Excellent.

VGP has appropriate policies in place to support the framework. The issuer has decided to fit all new roofs of its buildings with solar panels and to obtain BREEAM “very good” certification for all of its buildings. The lack of concrete targets for the rollout of solar installations can be explained by the geographic and regulatory spread of VGP's operations. The selection process involves a dedicated committee with environmental competence. Screenings of resiliency, environmental impact and supply chain are guided by the BREEAM framework. The management of proceeds complies with the Green Bond Principles. The issuer will provide reporting on an annual or more frequent basis to investors and lenders on its green finance activities and achieved impacts on a portfolio basis. The issuer will obtain external verification for the reporting of the use of proceeds. The overall assessment of VGP's governance structure and processes gives it a rating of **Good**. The governance score would be strengthened by emissions reporting, targets for reducing emissions, and scenario analysis with a focus on transition of the transport sector. Also, dedicated climate related policies for the supply chain and procurement which would complement the BREEAM framework and define ambitions and goals would be a strength.



Strengths

The issuer's decision to fit solar systems on all available suitable rooftops in due course is a clear strength. It is notable that the issuer's scope for this roll out encompasses the entire building portfolio in all regions where the company is active. The issuer informs us that the pipeline for rooftop solar projects is significant, including plans

² <http://www.iea.org/tcep>

³ <https://www.baulinks.de/heizung/heizungsmarkt.php>



for the largest rooftop solar system in Europe for a new logistics and industrial park near Munich, Germany. Rooftop solar systems do not use up land and thus reduce the environmental impact compared to ground mounted utility scale arrays. Such systems contribute to increasing the share of renewable energy in a country's power grid. The issuer confirmed that only warehouses will be fitted with rooftop solar panels.

The BREEAM system provides a reasonable framework to screen building projects. The issuer has decided that all buildings will need to obtain BREEAM "very good" certification from January 2020, including projects currently under development. We take note of the fact that the issuer, as a developer of logistics centers for third party tenants, accepts the risk of losing potential clients should these not be willing to carry the costs of certification. Proximity to public transport as well as Electric charging stations, which a tenant can request, support the transition to low emissions transportation.

Weaknesses

There are no apparent weaknesses in the framework.

Pitfalls

The level BREEAM "very good" can be achieved without dedicated efforts to improve energy efficiency beyond industry standard in certain regions, like Western Europe. The issuer has not defined any addition energy efficiency targets or thresholds. This is a missed opportunity to track energy efficiency improvements, establish experiences on best practice, and report on achievements. This is particularly relevant given the use of natural gas heating systems and the relatively high grid emissions factor in some of the countries where VGP has a strong presence, e.g. Germany. According to the issuer, BREEAM "Very Good" does represent a significant improvement over national building codes in parts of Eastern Europe. Setting best practice examples by private sector actors is positive, and we would encourage the issuer to quantify and benchmark such improvements.

Investors should be aware of the risk of locking in emissions from heating systems with natural gas which the framework does not prohibit in new buildings.

The logistics industry in general is a part of light and heavy road transport. There are currently few electric or hybrid solutions for this kind of transport available. The issuer informed us that one large new development will feature charging stations for trucks. This is encouraging; however, the larger picture is dominated by fossil powered vehicles. We encourage the issuer to engage with tenants early in the planning phase and to consider the increased installation of charging stations to facilitate both the increased electrification of employees' personal cars as well as the electrification of trucks as they come to the market in increasing numbers.

The renewable energy category allows for investments in onsite wind power and geothermal energy. Wind power developments have lately been under heightened public scrutiny in several countries. We encourage the issuer to engage with stakeholders, such as affected communities, early in the development process. The risk for substantial opposition is somewhat reduced as wind turbines will be installed on sites that are being commercially used already, which also limits the scale of possible wind power developments. The issuer has confirmed that controversial projects will not be financed or refinanced with green bond proceeds. Geothermal energy can be a significant source of emissions, with some plants generating higher GHG emissions than fossil fuel equivalents. In order to be considered net environmentally positive, standards call for new and existing geothermal projects to have direct emissions of less than 100g CO₂/kwh⁴. We encourage the issuer to consider potential negative

⁴ <https://www.climatebonds.net/standard/geothermal>



environmental aspects, e.g. local water quality, pollutants from geothermal fluids and emissions of non-condensable gases.

Under the category pollution prevention and control the issuer aims to increase on-site waste separation by tenants. The recycling of plastic waste is essential for reaching a low emissions and climate resilient future. Currently, plastic waste is treated in different ways depending on the national context, e.g. incineration for waste to energy. An effective system for waste separation, which the framework aims to support, is a precondition for achieving higher recycling rates in the future. This framework does not finance any waste incineration.



Appendix 1:

Referenced Documents List

Document Number	Document Name	Description
1	VGP Green Finance Framework	The green finance framework structured after the ICMA green bond- and green loan principles
2	Annual report 2018	VGP Group's annual report



Appendix 2: About CICERO Shades of Green

CICERO Green is a subsidiary of the climate research institute CICERO. CICERO is Norway's foremost institute for interdisciplinary climate research. We deliver new insight that helps solve the climate challenge and strengthen international cooperation. CICERO has garnered attention for its work on the effects of manmade emissions on the climate and has played an active role in the UN's IPCC since 1995. CICERO staff provide quality control and methodological development for CICERO Green.

CICERO Green provides second opinions on institutions' frameworks and guidance for assessing and selecting eligible projects for green bond investments. CICERO Green is internationally recognized as a leading provider of independent reviews of green bonds, since the market's inception in 2008. CICERO Green is independent of the entity issuing the bond, its directors, senior management and advisers, and is remunerated in a way that prevents any conflicts of interests arising as a result of the fee structure. CICERO Green operates independently from the financial sector and other stakeholders to preserve the unbiased nature and high quality of second opinions.

We work with both international and domestic issuers, drawing on the global expertise of the Expert Network on Second Opinions (ENSO). Led by CICERO Green, ENSO contributes expertise to the second opinions, and is comprised of a network of trusted, independent research institutions and reputable experts on climate change and other environmental issues, including the Basque Center for Climate Change (BC3), the Stockholm Environment Institute, the Institute of Energy, Environment and Economy at Tsinghua University and the International Institute for Sustainable Development (IISD).

