

# Second-Party Opinion

## H&M Group Sustainability-Linked Bonds



### Evaluation Summary

Sustainalytics is of the opinion that the H&M Group Sustainability-Linked Bonds aligns with the Sustainability Linked Bonds Principles 2020 and considers the KPIs to be relevant and material to the issuer and the SPTs to be ambitious and impactful. This assessment is based on the following:



**Selection of Key Performance Indicators (KPIs)** H&M Group has selected three KPIs – (i) Share of recycled materials / total materials used, (ii) Scope 1 and 2 CO<sub>2</sub>-e emissions and (iii) Scope 3 CO<sub>2</sub>-e emissions – for the Sustainability-Linked Bonds (SLB). Sustainalytics considers the KPIs chosen to be relevant and material for the H&M Group, and further considers the KPIs and methodology to calculate KPI performance to be clear.



**Calibration of Sustainability Performance Targets (SPTs)** H&M Group has established SPTs to increase the share of recycled materials as inputs to 30% by 2025, to reduce the Company's Scope 1 and 2 emissions by 20% by 2025 and Scope 3 emissions by 10% by 2025 compared to a 2017 baseline. Sustainalytics considers the SPTs to be aligned with the Issuer's sustainability strategy. Sustainalytics further considers the SPT 1 to be highly ambitious based on past performance and in comparison with peers' targets. The achievement of the SPTs contribute to SDGs 9 & 12.



**Bonds Characteristics** H&M Group has disclosed that each of the three KPIs is tied to a step-up in coupon rate if their respective SPTs are not achieved. The KPI's step-up rate is weighted as follows: KPI 1 40%, KPI 2, 20% and KPI 3, 40%. As such, the step-up of the coupons can be 0%, 20%, 40% 60%, 80% or 100% of the total step-up rate (as specified in the security documentation) depending on H&M Group's achievement of the three SPTs tied to the KPIs. If all three SPTs are achieved and reporting and verification has been made public in accordance with the processes outlined in the Framework, the financial characteristics of the bonds/schulscheins issued under this Framework shall remain unchanged. This is aligned with market practice.



**Reporting** H&M Group commits to report on an annual basis on its performance on the KPIs in a Sustainability-Linked Bonds Progress Report on its website, which is aligned with market practice.



**Verification** H&M Group commits to have external limited assurance verification conducted annually on its KPI performance against the SPTs, which is aligned with market practice.

<b>Evaluation date</b>	January 15, 2021
<b>Issuer Location</b>	Stockholm, Sweden

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## Introduction

Founded in 1947, H&M Group (“H&M”, the “Company”, or the “Issuer”) is a Swedish multinational clothing-retail company and is the world’s second-largest global clothing retailer with operations in 74 countries and over 5,000 stores. Central to the Company’s business model is the outsourcing of non-core business operations, including garment manufacturing and production.

H&M Group intends to issue Sustainability-Linked Bonds (SLBs) where the coupon rate of the bonds/schuldscheins is tied to the achievement of Sustainability Performance Targets based on three KPIs, the first of which is related to increasing the share of recycled materials as inputs and the second and third of which relate to Scope 1, 2 and 3 GHG emissions. The KPIs apply to the H&M Group’s entire business operations.

H&M Group has engaged Sustainalytics to review the SLB and provide an opinion on the alignment of the bonds with the Sustainability-Linked Bonds Principles (SLBP).<sup>1</sup>

### Scope of work and limitations

Sustainalytics’ Second-Party Opinion reflects Sustainalytics’ independent<sup>2</sup> opinion on the alignment of the reviewed SLB with the Sustainability Linked Bonds Principles 2020, as administered by ICMA.

As part of this engagement, Sustainalytics exchanged information with various members of H&M Group’s management team to understand the sustainability impact of their business processes and SPTs, as well as reporting and verification processes of aspects of the SLB. H&M Group representatives have confirmed that:

- (1) They understand it is the sole responsibility of H&M Group to ensure that the information provided is complete, accurate or up to date;
- (2) They have provided Sustainalytics with all relevant information; and
- (3) Any provided material information has been duly disclosed in a timely manner.

Sustainalytics also reviewed relevant public documents and non-public information. This document contains Sustainalytics’ opinion of the Bonds and should be read in conjunction with the Bonds Documents. Any update of the present Second-Party Opinion will be conducted according to the agreed engagement conditions between Sustainalytics and H&M Group. Sustainalytics’ Second-Party Opinion, while reflecting on the alignment of the Bonds with market standards, is no guarantee of alignment nor warrants any alignment with future versions of relevant market standards. Furthermore, Sustainalytics’ Second-Party Opinion addresses the anticipated SPTs of KPIs but does not measure the KPIs. The measurement and reporting of the KPIs is the responsibility of the Bonds issuer. No information provided by Sustainalytics under the present Second-Party Opinion shall be considered as being a statement, representation, warrant or argument either in favor or against, the truthfulness, reliability or completeness of any facts or statements and related surrounding circumstances that H&M Group has made available to Sustainalytics for the purpose of this Second-party Opinion.

The Second-Party Opinion is valid for issuances aligned with the respective Framework for which the Second-Party Opinion was written and aligned with the methodology to calculate the KPI performance outlined in the Second-Party Opinion up to 24 months or until one of the following occurs:

- i) There is a material change to the external benchmarks<sup>3</sup> against which targets were set;
- ii) There is a corporate action (such as an M&A or change in business activity) which has a material bearing on the achievement of the SLBs or the materiality of the KPI.

<sup>1</sup> The Sustainability Linked Bonds Principles (SLBP) were launched by ICMA in June 2020. They are administered by the ICMA and are available at: <https://www.icmagroup.org/assets/documents/Regulatory/Green-Bondss/June-2020/Sustainability-Linked-Bonds-PrinciplesJune-2020-100620.pdf>

<sup>2</sup> When operating multiple lines of business that serve a variety of client types, objective research is a cornerstone of Sustainalytics and ensuring analyst independence is paramount to producing objective, actionable research. Sustainalytics has therefore put in place a robust conflict management framework that specifically addresses the need for analyst independence, consistency of process, structural separation of commercial and research (and engagement) teams, data protection and systems separation. Last but not the least, analyst compensation is not directly tied to specific commercial outcomes. One of Sustainalytics’ hallmarks is integrity, another is transparency.

<sup>3</sup> Benchmarks refers to science based benchmarks.

## Sustainalytics' Opinion

### Section 1: Sustainalytics' Opinion on the Alignment of H&M Group's Sustainability-Linked Bonds with the Sustainability-Linked Bonds Principles.

Sustainalytics is of the opinion that the Sustainability-Linked Bonds Framework aligns with the five core components of the Sustainability-Linked Bonds Principles 2020 (SLBP). The KPIs and SPTs used by H&M Group are defined in Tables 1 and 2 below.

**Table 1: KPI definitions**

KPI	Definition
Share of recycled materials / total materials used in commercial goods	<p>This KPI is defined as the proportion of recycled materials used in production out of the total amount of material used in production of commercial goods. The metric is calculated as a percentage (share of recycled materials in tonnes/total tonnes of materials used).</p> <p>Recycled materials are defined as materials that have been reclaimed from waste streams and includes recycled/reclaimed textiles.</p>
Scope 1 and 2 GHG-emissions <sup>4</sup>	<p>Scope 1 and 2 GHG emissions are defined by the GHG Protocol as follows:</p> <ul style="list-style-type: none"> <li>• Scope 1 emissions are direct emissions from owned or controlled sources.</li> <li>• Scope 2 emissions are indirect emissions from the generation of purchased energy.</li> </ul> <p>Emissions are measured in metric tonnes of CO<sub>2</sub>-e (t/CO<sub>2</sub>-e).</p> <p>All emissions are calculated as per the GHG Protocol methodology.<sup>5</sup></p>
Scope 3 GHG-emissions	<p>Scope 3 GHG emissions are defined by the GHG Protocol as follows:<sup>6</sup></p> <ul style="list-style-type: none"> <li>• H&amp;M's Scope 3 emissions calculation includes upstream emissions related to fabric production, garment manufacturing, sourcing of raw materials, and transport, thus downstream emissions are not included. All categories are based on the GHG Protocol.<sup>7</sup></li> </ul> <p>Emissions are measured in metric tonnes of CO<sub>2</sub>-e (t/CO<sub>2</sub>-e).</p> <p>The calculation methodology is as follows: number of products/spend is multiplied by life-cycle assessment-based conversion factors. Calculations in the footprint analysis are based on a combination of H&amp;M group data and the best available public data sources on CO<sub>2</sub>e emissions.</p> <p>Sustainalytics notes that, for both KPI 2 and KPI 3, the levels of CO<sub>2</sub>e emissions during the baseline year 2017 will be recalculated to reflect any <i>significant</i> changes in H&amp;M Group's structure (e.g., acquisition, divestiture, mergers, insourcing or outsourcing). Recalculated levels of CO<sub>2</sub>e emissions for KPI 2 and 3 will be reported to Science Based Targets initiative. The threshold value for a significant change is a change that impacts the Sustainability Performance Target, in aggregate, by 5 percent or more (which threshold for recalculation is in line with the recommendation by the SBTi). Any recalculations of levels of CO<sub>2</sub>e emissions during the baseline year 2017 for KPI 2 and 3 must be reported in the annual Sustainability-Linked Bond Progress Report (see the reporting section below) verified by an independent, qualified external reviewer as outlined in the Framework.</p>

**Table 2: SPTs and Past Performance**

<sup>4</sup> Emissions for the entire Group.

<sup>5</sup> GHG Protocol, "Standards", (2020), at: <https://ghgprotocol.org/standards>

<sup>6</sup> Scope 3 emissions are all indirect emissions (not included in Scope 2) that occur in the value chain of the reporting company, including both upstream and downstream emissions.

<sup>7</sup> GHG Protocol, "Product Standard", (2020), at: <https://ghgprotocol.org/product-standard>

KPI	2017 (baseline)	2018	2019	SPT 2025
Share of recycled materials / total materials used in commercial goods	0.5%	1.4%	2.2%	30%
Scope 1 & 2 emissions CO <sub>2</sub> -e (tonnes)	63,690	56,978	61,462	20% decrease in Scope 1 and 2 emissions by 2025
Scope 3 emissions	13,479,100	N/A <sup>8</sup>	13,069,880	10% decrease in Scope 3 emissions by 2025

## 1) Selection of Key Performance Indicators (KPIs)

### Definition and methodology of KPIs

- H&M Group's Sustainability-Linked Bonds includes three KPIs: (i) Share of recycled materials / total materials used in commercial goods, (ii) Scope 1 and 2 CO<sub>2</sub>-e emissions and (iii) Scope 3 CO<sub>2</sub>-e emissions
  - Sustainalytics considers the definition and calculation methodology of the KPIs to be clear and credible. (See Table 1 above for further detail). Sustainalytics positively notes that the methodology to calculate Scope 1, 2 and 3 GHG emissions follows the GHG Protocol methodology for upstream emissions established by the World Resources Institute and World Business Council for Sustainable Development.

### Relevance and Materiality of KPIs

- Sustainalytics considers the use of recycled materials as inputs and reducing CO<sub>2</sub>-e emissions as relevant and material sustainability issues for H&M Group.
  - Regarding the use of recycled materials, Sustainalytics notes that turning raw materials into textiles may involve thousands of chemicals, approximately 10% of which are hazardous substances, including phthalates, PFCs, formaldehyde and heavy metals. Big brand retailers, such as H&M, have been under pressure for their role in environmental damage from textiles production, and are increasingly leveraging their bargaining power to require stronger environmental management from textile factories in their supply chains, including promoting innovative processes and the phaseouts of harmful chemicals. H&M's KPI to increase its share of recycled materials addresses part of this issue as the use of recycled materials reduces raw material inputs, which reduces the need for conversion of virgin raw materials, thus reducing life-cycle impacts. H&M's first KPI is directly related to the core operations of the Company and is material to its business. The Company's Board of Directors have incorporated the KPI as a key component of its sustainability strategy.
  - Regarding Scope 1, 2 and 3 GHG emissions, together, the apparel and footwear industry is responsible for 8% of global emissions.<sup>9</sup> This speaks to the tremendous impact that the global apparel industry has on GHG emissions. Sustainalytics notes that H&M's KPI 3, which is related to the reduction of Scope 3 emissions, includes only upstream emissions, which account for approximately 74% of the Company's total Scope 3 emissions.

### Ability to be benchmarked

Sustainalytics notes that the first KPI does not have an external standard to be benchmarked against. Additionally, Sustainalytics notes that industry peers often merge the metric of recycled materials as an input together with sustainable sourcing targets, while H&M discloses these separately. For the second and third KPI, H&M will report on Scope 1, 2, and 3 emissions in accordance with the GHG Protocol, which is a commonly used external reference in the industry and can therefore be benchmarked against external carbon trajectories as well as peer performance.

### Overall assessment

In Sustainalytics' opinion the selected KPIs are relevant and material to the H&M Group. Sustainalytics considers the definition of the KPI's to be clear and the methodology to calculate KPI performance credible and positively notes the ability to compare against peer performance and low-carbon trajectories for the Company's GHG emission KPIs.

<sup>8</sup> No calculation done in 2018.

<sup>9</sup> Quantis, "Measuring Fashion: Insights from the Environmental Impact of the Global Apparel and Footwear Industries", (2018), at: <https://quantis-intl.com/report/measuring-fashion-report/>

## 2) Calibration of Sustainability Performance Targets (SPTs)

### Alignment with issuer's sustainability strategy

- H&M Group has set the following SPTs for its KPIs:
  - SPT 1: Increase share of recycled materials to 30% by 2025
  - SPT 2: Decrease Scope 1 and 2 emissions by 20% by 2025
  - SPT 3: Decrease scope 3 emissions by 10% by 2025
- Sustainalytics considers the SPTs to be aligned with H&M Group's sustainability strategy; these SPTs are related to core operations and align with the Company's Board approved sustainability targets (please refer to Section 2 for analysis of the overall strength of H&M Group's sustainability strategy). Regarding SPT 1, H&M has set a 2030 goal to move away from all virgin polyester and only use recycled polyester and has a long-term goal of having 100% recycled or sustainably sourced materials as inputs. Additionally, H&M has established 2030 targets for its Scope 1 and 2 emissions that have been verified by the Science-Based Targets Initiative and that are aligned with a well-below 2-degree global warming scenario. Achieving these SPTs will contribute to a reduction in the Company's overall emissions and help achieve its 2030 goals.

### Strategy to achieve the SPTs

- H&M Group intends to achieve its SPTs through the following strategies:
  - Regarding SPT 1, H&M aims to identify different opportunities within the production chain to increase the amounts of recycled materials in clothing. Beyond procurement of recycled materials, H&M intends to invest and collaborate with start-ups, peers and organization including the Hong Kong Research Institute of Textiles and Apparel<sup>10</sup> to increase the availability of recycling technology for fibres.
  - Regarding SPTs 2 and 3, H&M's strategy to reduce the GHG emissions of its own operations and the operations of its supply chain identifies three priority areas:
    - Energy efficiency – focusing on energy efficiency improvement in stores, transport and distribution centres, and providing advice to suppliers on how to increase energy efficiency. For example, H&M will create a team of engineers focused on reducing energy consumption of H&M's suppliers.
    - (ii) Renewable energy – focusing on supporting renewable energy through the purchase of Power Purchase Agreements (PPAs) and solar PV systems for roof tops. The Company has also placed a ban on new coal-fired boilers from 2025 and plans to support suppliers with financing of emission reduction measures.
    - (iii) Circularity – Moving towards a circular business by, for example, switching to recycled materials, increasing the technical capacity to recycle textiles and implementing other initiatives focused on reducing the use of virgin materials and optimizing resource use.

### Ambitiousness, Baseline and Benchmarks

- Regarding SPT 1, historically, H&M has used very little recycled materials as a share of its total materials used. Starting from a baseline of 0% recycled materials inputs in 2016, H&M only began using recycled materials in 2017, resulting in a share of 0.5% of recycled materials out of total materials used. Although recycled materials as inputs does not lend itself to an external reference for benchmarking, and due to the different reporting metrics used by industry peers, it is difficult to precisely compare with peer performance. Nonetheless, H&M's target is highly ambitious as it clearly exceeds the goals of industry competitors, including Inditex, for example, which aims to increase its procurement and sourcing of recycled/sustainable inputs<sup>11</sup> and has initiated efforts to implement garment collection schemes at all its stores and improve downstream recycling, but has not established concrete targets for increasing recycled materials as inputs.<sup>12</sup> The high degree of ambitiousness of H&M's recycling goal is demonstrated by the Company's commitment to financing the technology and infrastructure that is required for textiles recycling, which is currently severely limited.<sup>13</sup> As such, by considering the entire value chain of a product (from sourcing to disposal) H&M is committing to a highly ambitious recycling target. Moreover, considering the Company's past performance (2017 baseline of 0.5%) Sustainalytics is of the opinion that H&M's goal to reach 30% recycled materials as inputs is a highly ambitious SPT and represents leadership in the clothing industry.

<sup>10</sup> HKRIT, "Home page", (2020), at: <https://www.hkrita.com/home.php>

<sup>11</sup> Inditex, "Sourcing", (2020), at: <https://www.inditex.com/how-we-do-business/our-model/sourcing>

<sup>12</sup> Inditex, "Collect, Reuse, Recycle", (2020), at: <https://www.inditex.com/en/our-commitment-to-the-environment/closing-the-loop/collect-reuse-recycle>

<sup>13</sup> Recovery, "The limitations of textile recycling", (2019), at: [https://www.recovery-worldwide.com/en/artikel/the-limitations-of-textile-recycling\\_3411757.html](https://www.recovery-worldwide.com/en/artikel/the-limitations-of-textile-recycling_3411757.html)

- Regarding SPT 2, in 2019 H&M established science-based targets to reduce its absolute Scope 1 and 2 emissions by 40% by 2030 below a 2017 baseline. This target was verified by the Science-Based Targets Initiative and is consistent with reductions required to keep warming well-below 2°C. As an interim target, H&M has established SPTs for 2025 (20% reduction by 2025), which the Company has indicated are aligned with the 2030 verified SBTi targets. In order to develop these interim targets, H&M Group halved the goals (from 10-year goals to 5-year goals). Sustainalytics notes that this is an ambitious target but acknowledges that some peers have established more ambitious targets.<sup>14</sup>
- Regarding SPT 3, in 2019 H&M established science-based targets to reduce Scope 3 emissions by 20% by 2030<sup>15</sup> compared to a 2017 baseline, which were also verified by SBTi. Similar to SPT 2, H&M has established an interim 2025 target to reduce Scope 3 emissions by 10% by 2025, which is commensurate with peer targets.<sup>16</sup> Based on this, Sustainalytics is of the opinion that this is an ambitious SPT.

### Overall Assessment

Sustainalytics considers H&M Group's SPTs to be consistent with its overall sustainability strategy and considers its strategy to achieve the SPTs to be credible. Sustainalytics views SPT 1 to be highly ambitious and SPTs 2 and 3 to be ambitious, highlighting the alignment of the SPTs 2 & 3 to a 2030 trajectory, approved by the SBTi.

### 3) Bonds characteristics

For the bonds/schuldscheins issued under this Framework, there will only be one Trigger Event impacting the financial characteristics of the security, which will be in the form of a step-up in the coupons. The Trigger Event is the Company's achievement of (or lack thereof) its three KPIs and corresponding SPTs. In addition to the achievement of SPTs (or lack thereof), H&M has committed to full compliance with the reporting and verification processes outline in the Framework.

The weighted step-up of the coupons for each KPI is set as follows:

KPI	Relative weight of each KPI to the aggregate coupon step-up (%)
KPI 1	40%
KPI 2	20%
KPI 3	40%

Consequently, the step-up on the coupons can be 0%, 20%, 40%, 60%, 80% or 100% depending on the Company's overall achievement of its SPTs and compliance with reporting and verification processes. In the event all three KPI's are met and the reporting and verification processes outlined here have been fully complied with, the financial characteristics of the security issued shall remain unchanged.

### 4) Reporting

H&M Group commits to report on an annual basis on its KPI performance and expects to include the relevant figures in a Sustainability-Linked Bonds Progress Report (SLB Progress Report). The SLB Progress Report shall be made available on H&M Group's website no later than the reporting end date (the date falling 120-days post target observation date), which is aligned with the SLB Principles. The SLB Progress Report will contain relevant information to assess if any changes to the bonds/schuldscheins characteristics are to be made, including but not limited to:

- The performance of the KPIs as per the Target Observation Date including the calculation methodology and baselines where relevant;
- Information about recalculations, if any, of the levels of CO<sub>2</sub>e emissions during the base-year 2017 for KPI 2 and 3;
- A verification report relative to the KPIs outlining the performance against the SPTs and the related impact, and timing of such impact, on the bonds characteristics; and

<sup>14</sup> For example, Inditex commits to reduce absolute scope 1 and 2 GHG emissions 90% by 2030 from a 2018 base year, which is consistent with reductions required to keep warming to 1.5-degrees. Similarly, other industry peers have established SBTi targets which are consistent with reductions required to keep warming to 1.5-degrees.

<sup>15</sup> Sustainalytics notes that H&M's Scope 3 emissions are related to upstream activities included in the SBTi approved target, representing 74% of the Group's total Scope 3 emissions.

<sup>16</sup> Inditex commits to reduce absolute scope 3 GHG emissions 20% by 2030 from a 2018 base year.

- Information on any updates to H&M Group’s sustainability strategy and/or governance with an impact on the KPIs and SPTs.

When feasible and possible, the SLB Progress Report will also include:

- Qualitative and/or quantitative explanations of the contribution of the main factors, including M&A activities, behind the evolution of the performance on the KPI(s) on an annual basis;
- Illustration of the positive sustainability impacts of the performance improvement;
- Any re-assessments of KPIs and/or restatement of the SPT and/or pro-forma adjustments of baselines or KPI scope;<sup>17</sup>
- Updates on new or proposed regulations from regulatory bodies relevant to the KPIs and the SPTs.

## 5) Verification

H&M Group commits to having an external verifier provide limited assurance on the published KPI performance figures for each fiscal year ending in 2021 up to and including 2025, which is aligned with the SLB Principles on verification.

### Alignment with Sustainability Linked Bonds Principles 2020

Sustainalytics has determined that the H&M Group’s SLB Framework aligns with the five core components of the Sustainability Linked Bonds Principles (2020).

## Section 2: Assessment of H&M Group’s Sustainability Strategy

### Credibility of H&M Group sustainability strategy

The Company’s management of its sustainability and ESG-related issues is directly overseen by the CEO and Executive Management team. Moreover, in January 2020 the Group appointed its former Sustainability Manager as Chief Executive, demonstrating the Group’s commitment to sustainability as core to its corporate strategy and to a sustainable fashion industry.<sup>18</sup>

In line with its vision to “lead the change towards a circular and climate positive fashion industry”, H&M integrates sustainability across its business focusing on circularity and tackling GHG emissions.<sup>19</sup> Concerning circularity, Sustainalytics notes that H&M’s use of recycled materials as inputs has grown from 0.7% to 2.2%. With respect to cotton, in 2019, 97% of inputs were recycled, certified organic or certified under the Better Cotton Initiative (BCI), and H&M intends to increase this level to 100% by 2020. With regards to emissions, Scope 1 and 2 decreased by 22.68% between 2016 and 2019, while in 2019 Scope 3 emissions increased by 4% from 2018 levels.<sup>20</sup>

H&M Group has outlined specific targets aligned with their sustainability pathway, including: (i) by 2025, reduce the Group’s electricity intensity<sup>21</sup> by 25% (compared to a 2016 baseline) and absolute transport-related emissions by 2030 (compared to a 2018 baseline), (ii) by 2030, as confirmed by the Science-Based Targets Initiative (SBTi), source 100% renewable electricity, reduce GHG emissions by 40% (Scopes 1 and 2), and 59% (Scope 3 from purchased raw materials, fabric production and garments) compared to 2017, (iii) by 2030, only use 100% recycled or sustainably sourced materials,<sup>22</sup> and (iv) by 2022, recycle 15% of the total water consumed during production.<sup>23</sup>

<sup>17</sup> Sustainalytics notes that any adjustments in baselines will have no impact on the Company’s SPT’s.

<sup>18</sup> H&M Group, “Stefan Persson will step down as Chairman of the Board of H & M Hennes & Mauritz AB at the AGM and proposes that Karl-Johan Persson succeed him. Helena Helmersson has been appointed new CEO”, (2020), at: <https://hmggroup.com/media/news/financial-reports/2020/1/3552412.html>

<sup>19</sup> H&M Group, “Sustainability”, at: <https://hmggroup.com/sustainability.html>

<sup>20</sup> H&M Group, “Sustainability Performance Report 2019”, (2020), at: [https://sustainabilityreport.hmggroup.com/wp-content/uploads/2020/10/Sustainability\\_Performance\\_Report\\_2019.pdf](https://sustainabilityreport.hmggroup.com/wp-content/uploads/2020/10/Sustainability_Performance_Report_2019.pdf)

<sup>21</sup> kWh/sqm/opening hour.

<sup>22</sup> H&M’s approach to sustainable sourcing using: (i) third-party verified lifecycle assessment (LCA) data, (ii) external material benchmarks based on LCA data, such as the Sustainable Apparel Coalition’s Material Sustainability Index, and (iii) credible third-party certification schemes, including organic and recycled standards, and material-specific verification initiatives.

<sup>23</sup> H&M Group, “Goals and ambitions”, at: <https://hmggroup.com/sustainability/leading-the-change/goals-and-ambitions.html>

Given H&M's quantitative goals, corporate-wide strategy and past performance, Sustainalytics is of the view that H&M has a suitable sustainability strategy and that its performance is on track to achieve the established objectives, while encouraging the Company to further mitigate emissions from its supply chain.

### H&M Group's environmental and social risk management

Sustainalytics considers the Company's overall management of material ESG risk to be average.<sup>24</sup> Sustainalytics also recognizes that, while the H&M Group's defined targets are impactful, its business activities bear environmental and social risks related to worker rights, occupational health and safety, the management of emissions from its operations to the environment, biodiversity loss, land use change, and community relations from sourcing and supply chain. In the following section Sustainalytics comments on H&M Group's ability to mitigate such potential risks.

- The Group implements a set of standards and policies to assist its sustainability efforts, namely the Human Rights Policy, Modern Slavery Statement, Global Health and Safety Policy, and Global Labour Relations Principles.<sup>25</sup>
- H&M business partners are covered by the following standards and policies: Sustainability Commitment, Child Labour Policy, and Sandblasting Policy.<sup>25</sup> These incorporate requirements to ensure adequate environmental and social risk management in H&M's supply chains.
- H&M is a member of the Sustainable Apparel Coalition (SAC) and uses its HIGG Index to increase supply chain transparency.
- Sourcing of materials and products used in H&M's manufacturing and global supply chain must abide to the Animal Welfare and Material Ethics Policy and Chemical Restriction list.<sup>25</sup>
- H&M uses the World Wildlife Fund's water risk filter to assess the overall impact of water in their value chain.<sup>20</sup> This assessment informed strategic development targeting water risk reduction at H&M and pointed areas where the most urgent actions needed to be taken.

Overall, Sustainalytics considers that the H&M Group has established management programs and policies to mitigate risks that could be associated with attaining the selected SPTs and encourages H&M to continue improving its management of human right issues across its global supply chain.

## Section 3: Impact of the SPTs chosen

### Importance of reducing the impact of the fashion industry

Globally, it is estimated that more than 50% of fast fashion clothing items produced is disposed of in under a year, and less than 1% of materials used to produce clothing is recycled into new clothing.<sup>26</sup> The fashion industry is responsible for 92 million tonnes of solid waste reaching landfills in a year,<sup>27</sup> it is projected that by 2030 this figure will grow by 42.5% to 134 million tonnes a year.<sup>28</sup> In the US, the Environmental Protection Agency estimates that discarded clothing is the main source of textiles in municipal solid waste.<sup>29</sup> In 2018, 13% of clothes that reached waste management sites in the US were recycled, the rest was landfilled, or in a smaller proportion incinerated for energy generation.<sup>29</sup> Comparably, in the EU the amount of textile waste has doubled over the last 20 years.<sup>30</sup> Disposed clothes can emit GHG or toxic substances over time as they decompose in landfills.<sup>30</sup>

The fashion industry accounts for 10% of annual GHG emissions globally,<sup>31</sup> these emissions amount to more than all international flights and maritime shipping combined.<sup>26</sup> Moreover, the industry is on track to increase

<sup>24</sup> Based on Sustainalytics' Risk Rating Management Score, which assesses the management of material manageable social and environmental risks by the company.

<sup>25</sup> H&M Group, "Standards & Policies", at: <https://hmgroupp.com/sustainability/sustainability-reporting/standards-and-policies.html>

<sup>26</sup> Ellen MacArthur Foundation, "A new textiles economy: Redesigning fashion's future", (2017), at: [https://www.ellenmacarthurfoundation.org/assets/downloads/publications/A-New-Textiles-Economy\\_Full-Report\\_Updated\\_1-12-17.pdf](https://www.ellenmacarthurfoundation.org/assets/downloads/publications/A-New-Textiles-Economy_Full-Report_Updated_1-12-17.pdf)

<sup>27</sup> UN Environment, "Why fast fashion needs to slow down", (2018), at: <https://www.unenvironment.org/news-and-stories/blogpost/why-fast-fashion-needs-slow-down>

<sup>28</sup> BBC News, "Why clothes are so hard to recycle", (2020), at: <https://www.bbc.com/future/article/20200710-why-clothes-are-so-hard-to-recycle>

<sup>29</sup> EPA, "Facts and Figures about Materials, Waste and Recycling", at: <https://www.epa.gov/facts-and-figures-about-materials-waste-and-recycling/textiles-material-specific-data>

<sup>30</sup> Netherlands Ministry of Foreign Affairs, "The European market potential for recycled fashion", (2020), at: <https://www.cbi.eu/market-information/apparel/recycled-fashion/market-potential>

<sup>31</sup> WEF, "These facts show how unsustainable the fashion industry is", (2020), at: <https://www.weforum.org/agenda/2020/01/fashion-industry-carbon-unsustainable-environment-pollution/>

greenhouse gas (GHG) emissions by 50% by 2030, driven by a projected global increase in consumption of 65% in the next decade.<sup>32</sup>

In recent years, industry stakeholders and consumers have become increasingly aware of the negative environmental and social impacts of the fashion industry and consumer behavior.<sup>33</sup> This recent awareness has resulted in collective efforts such as the UN Alliance for Sustainable Fashion (the “Alliance”) to address sustainability in fashion.<sup>34</sup> The Alliance advocates for a coordinated action to drive a major change throughout the value chain, production processes, distribution, consumption and disposal patterns to reduce fashion’s negative environmental and social impacts.<sup>34</sup> In practice, designers and manufacturers are working to increase the durability of products, use materials closer to their raw state or innovative fabrics, replace synthetic fabrics, and source materials from certified suppliers.<sup>35</sup> While current levels of commitments and efforts are not likely to achieve a net positive impact from the fashion industry they represent a signal for change.<sup>36</sup>

Based on the above context, Sustainalytics is of the opinion that H&M’s investments into increasing recycled materials content in new clothing garments and reducing Scope 1, 2 and 3 emissions can be expected to contribute to sustainability in the fashion industry.

### Alignment with/contribution to SDGs

The Sustainable Development Goals (SDGs) were set in September 2015 and form an agenda for achieving sustainable development by the year 2030. This sustainability linked bonds advances the following SDG goals and targets:

KPI	SDG	SDG target
Share of recycled materials of total materials used in commercial goods.	12. Responsible consumption and production	12.5 By 2030, substantially reduce waste generation through prevention, reduction, recycling, and reuse
Scope 1 and 2 GHG emissions. Includes CO <sub>2</sub> and other GHG emissions as defined by GHG Protocol.	9. Industry, innovation, and infrastructure	9.4 by 2030, upgrade infrastructure and retrofit industries to make them sustainable, with increased resource-use efficiency and greater adoption of clean and environmentally sound technologies and industrial processes, with all countries taking action in accordance with their respective capabilities
Scope 3 GHG emissions. Includes CO <sub>2</sub> and other GHG emissions and is defined as emissions related to fabric production, garment manufacturing, raw materials, and upstream transport.	12. Responsible consumption and production	12.6 encourage companies, especially large and transnational companies, to adopt sustainable practices and to integrate sustainability information into their reporting cycle

### Conclusion

H&M Group intends to issue Sustainability-Linked Bonds which will tie the coupon rate to the achievements of the following SPTs (2017 baseline):

- I) Increase the share of recycled materials to 30% by 2025;
- II) Reduce scope 1 and 2 emissions by 20% by 2025;
- III) Reduce scope 3 emissions by 10% by 2025.

Sustainalytics performed a review of the SLB information and considers the KPIs to be relevant and material and aligned with H&M Group’s sustainability strategy. Sustainalytics considers the SPTs to be aligned with

<sup>32</sup> WBG, “How Much Do Our Wardrobes Cost to the Environment?”, (2019), at: <https://www.worldbank.org/en/news/feature/2019/09/23/costo-moda-medio-ambiente>

<sup>33</sup> Gazzola, P. et al (2020), “Trends in the Fashion Industry. The Perception of Sustainability and Circular Economy: A Gender/Generation Quantitative Approach”, Sustainability, MDPI, at: <https://www.mdpi.com/2071-1050/12/7/2809/pdf>

<sup>34</sup> UN Alliance for Sustainable Fashion, “The UN Alliance for Sustainable Fashion”, at: <https://unfashionalliance.org/>

<sup>35</sup> Forbes, “Why Sustainable Fashion Matters”, (2019), at: <https://www.forbes.com/sites/elleveate/2019/10/07/why-sustainable-fashion-matters/#4b5a55f571b8>

<sup>36</sup> C&A Foundation, “The Future of Sustainability in the Fashion Industry”, (2019), at: <https://www.candafoundation.org/en/resources/future-sustainability-fashion-industry-delphi-final-report-futureimpacts-ca-2019-v7.pdf>

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peers' and to represent a material improvement over baselines and considers SPT 1 to be highly ambitious when compared to peers and SPTs 2 and 3 to be ambitious. Furthermore, Sustainalytics considers reporting and verification commitments to be aligned with market practice.

Based on the above, Sustainalytics considers H&M Group's SLB Framework to be in alignment with the five core components of the SLBP and the prospective of achievement of the SPTs to be impactful.

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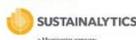
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