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Second Party Opinion

ENN Energy Holdings Ltd. Green Finance Framework

Oct. 1, 2024

Location: China

Sector: Gas Utilities

Alignment With Principles

Aligned = ✓ Conceptually aligned = ○ Not aligned = ✗

- ✓ Green Bond Principles, ICMA, 2021 (with June 2022 Appendix 1)
- ✓ Green Loan Principles, LMA/LSTA/APLMA, 2023

See [Alignment Assessment](#) for more detail.

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Dark green

Activities that correspond to the long-term vision of a low-carbon climate resilient future.

Our [Shades of Green Analytical Approach](#) >

Strengths

ENN Energy conducts an in-depth assessment of climate-related transition and physical risks and opportunities. The company references the recommendations of Task Force on Climate-related Financial Disclosures (TCFD) and applies multiple sector-specific scenarios for transition risks. It also identifies physical risks for its projects through feasibility study, environmental impact assessment, risk forecasts using multiple national and international databases, as well as specific climate scenarios.

Weaknesses

No weaknesses to report.

Areas to watch

Some projects categories do not have specific performance requirements. These include water reduction threshold from the use of reclaimed water and rainwater, and energy efficiency criteria for green buildings projects that solely rely on certifications. This limits visibility on the projects' environmental benefits.

Eligible Green Projects Assessment Summary

Over the three years following issuance of the financing, ENN Energy expects to allocate all proceeds to the renewable energy category. The issuer expects more than half of proceeds to finance new projects, with the rest to refinancing.

Overall Shades of Green assessment

Based on the project category shades of green detailed below, and consideration of environmental ambitions reflected in ENN Energy Holdings Ltd. Green Finance Framework, we assess the framework as Dark green.

Eligible projects under the company's green finance framework are assessed based on their environmental benefits and risks, using Shades of Green methodology.

**Dark
green**

Activities that correspond to the long-term vision of a low-carbon climate resilient future.

Our [Shades of Green Analytical Approach >](#)

Renewable Energy Dark to Medium green

Support the production and use of renewable energy

Sustainable Water Management Light green

Installation of drainage canals in construction sites

Installation of mud pools to avoid infiltration into groundwater or rivers

Use of reclaimed water and rain water in the production process, adoption of water-saving appliances

Green Buildings Light green

Renovation of buildings that have obtained selected certification systems

On-site renewable energy installations

See [Analysis Of Eligible Projects](#) for more detail.

Issuer Sustainability Context

This section provides an analysis of the issuer's sustainability management and the embeddedness of the financing framework within its overall strategy.

Company Description

ENN Energy engages in the sale and distribution of natural gas, and the investment, construction, operation and management of gas pipeline infrastructure in China. The company was founded in 1989 and is headquartered in Langfang, China. It is listed on the Hong Kong stock exchange.

ENN Energy's revenue was Chinese renminbi (RMB) 113.8 billion (US\$ 16.1 billion) in 2023, through its retail gas sales business (53%), wholesale of gas (26%), integrated energy business (13%), construction and installation (5%) and value-added business (3%). The company distributes and sells piped gas, liquefied natural gas (LNG), and other multi-energy products; operates vehicle gas refueling stations; and provides services related to low-carbon integrated solutions.

ENN Energy is a top-five gas distributor in China by gas volume. As of end-2023, the company, through its investees, owned 259 piped city-gas projects and 296 integrated energy projects spanning 23 provinces, cities, and autonomous regions. It had 29.8 million residential customers and more than 243,000 commercial and industrial customers. In 2023, ENN Energy sold 33.6 billion cubic meters of gas.

Material Sustainability Factors

Climate transition risk

Climate transition risks are highly material to stakeholders but they tend to have more bearing on electricity and gas networks. This is given the networks' critical role in the energy delivery value chain and their direct exposure to upstream generators, which are a leading cause of greenhouse gas emissions. The sector is therefore highly susceptible to growing public, political, legal, and regulatory pressure to accelerate climate goals. The ongoing decarbonization of the energy sector is likely to triple its reliance on renewable power, which comes with significant grid expansion. In the gas network sector, continued focus on reducing reliance on methane-emitting natural gas could diminish growth prospects, making it more difficult to effectively manage regulatory risk. China has national commitments to reach peak carbon emissions before 2030 and achieve carbon neutrality by 2060.

Physical climate risk

Networks operate fixed assets that span large service territories, making them highly exposed to physical climate risks. These events can cause network service disruptions for large populations, elevating stakeholder materiality. Issuers have been impaired by wildfires, hurricanes, and winter storms. During these events, the utility may incur higher costs, which typically leads to higher leverage. Unabated climate change could lead to estimated GDP losses of 0.5%-2.3% as early as 2030 for China, according to the World Bank. Chinese provinces account for half of the most exposed global spots to extreme weather events by 2050 as per 2024 XDI Gross Domestic Climate Risk Report.

Access and affordability

The affordability and reliability of networks are under pressure from climate-related risks, exacerbating the materiality for stakeholders. Energy and water are essential services supporting human health and well-being, and global economic development. Service disruptions or steep increases in prices are likely to be amplified by the energy transition and physical climate risks. These dynamics can affect households' purchasing power and the competitive strengths of local industries, making network reliability highly material for stakeholders. Moreover, while utility bills are rising, they tend to rise at a rate lower than inflation. Additionally, regulators continue to allow utilities to use mechanisms to smooth volatility and to offer income assistance programs, underpinning a more moderate impact. China is the world's third-largest gas market, consuming 364.6 billion cubic

meters of gas in 2022. To compete with falling spot LNG prices, China's national oil and gas companies are likely to lower prices for their 2024-2025 pipeline gas sales contracts on the back of ample supply from both domestic production and imports, market participants said.

Impact on communities

Community impacts are more acute for stakeholders given how close networks are to where people live and work. Moreover, energy and water services are essential for community health and well-being globally. Stakeholder impacts arise from the construction and siting of lines-- especially in areas unaccustomed to industrial development and in indigenous territories--which is accelerating to meet climate goals and in places where eminent domain is granted by local governments. Moreover, service disruptions, fires, gas explosions, inadequate or contaminated drinking water, and untreated wastewater pose severe, and sometimes irreversible, community health and safety hazards.

Issuer And Context Analysis

The framework's project categories may address ENN Energy's most material sustainability factors. The company's strategic design and daily operations aim to align with China's 14th Five Year Plan's goals for carbon peak and carbon neutrality. The financing framework's project categories--renewable energy, sustainable water management, and green buildings--aim to address climate transition risk and, indirectly, access and affordability. Physical climate risk and impact on communities are relevant, given the exposure to extreme weather and diversified geographical coverage of ENN Energy's assets.

ENN Energy focuses on achieving emissions by 2050. The company has committed to reduce its scope 1 and 2 emissions intensity by 20% for its city gas business and by 48% for its integrated energy business by 2030 (compared to 2019). As of 2023, the company has achieved 28.5% and 36.5% reductions in emissions for its city gas and integrated energy businesses, respectively. However, the nature of using emission intensity means absolute emissions could increase, should the growth in cubic meters of gas or unit of energy sold exceed the reduction in emissions. The largest source of direct emissions (54.7%) is from energy consumed by the company's retail and wholesale gas businesses. ENN Energy has reported Scope 3 emissions since 2022 and expects to reduce such emissions by providing customers with low-carbon solutions and products. However, it has not yet set specific target for reducing these emissions. Nevertheless, the company has installed methane detection laser platforms at gas stations and storage and distributions stations. These enable monitoring of methane emissions and improved control measures. The company also utilizes digital intelligence technology to optimize energy efficiency.

ENN Energy assesses climate-related risks and opportunities and sets targeted measures, referencing the recommendations ofTCFD. Given the company operates in the gas sector, it uses the International Energy Agency (IEA)'s World Energy Outlook scenarios, including the Net Zero by 2050 Scenario (NZE), Sustainable Development Scenario (SDS), and Stated Policies Scenario (STEPS), in addition to Intergovernmental Panel on Climate Change (IPCC) scenarios, for its climate risk assessment. We view this as a strong practice, when compared with peers in China's gas industry.

Physical risks matter for ENN Energy due to its geographical diversity and the fixed nature of its assets. Construction of renewable energy infrastructure and green buildings are eligible for financing under the framework. ENN Energy has operations in 23 provinces, cities, and autonomous regions in China, with high exposure to physical climate risks such as typhoon, flood, and temperature increases. The company conducts flood assessments and implements enhanced flood designs that reduce substantial damage to its natural gas pipeline network, ensuring safe and stable operations. ENN Energy also conducts online monitoring system for third-party projects along the pipeline network, enabling timely identification of potential safety risks. We take a positive view of the fact that ENN Energy applies IPCC RCP 8.5 and RCP 4.5

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scenarios when assessing physical risks, covering three different time horizons (short term, 0-3 years; medium-term, 3-10 years; and long-term, above 10 years). Based on the identified materiality of the risks, the company commits to implementing the necessary adaptation measures, which are detailed in its 2022 Climate-related Financial Disclosure Report.

ENN Energy provides accessible and affordable energy services to various socioeconomic groups. The company serves different types of customers, from large industrials to small business owners. For city gas customers, ENN Energy utilizes digital intelligence to enhance demand forecasting, resource coordination, and supply stability across various scenarios. For integrated energy business clients, including small and micro enterprises, the company supplies energy in a centralized manner, optimizing energy utilization efficiency and supporting the intelligent management of energy systems. ENN Energy adheres to government policies on gas prices, aligning with established norms.

ENN Energy engages with communities, ensuring transparency and addressal of concerns. In instances of opposition to projects, ENN Energy has shared that it takes an open communication approach, includes feedback, and provides additional assistance to mitigate adverse effects. It may also take remedial measures such as conducting further environmental impact assessments (EIA) and adjusting project plans to mitigate negative community impacts.

Alignment Assessment

This section provides an analysis of the framework's alignment to Green Bond/Loan principles.

Alignment With Principles

Aligned = ✓ Conceptually aligned = ○ Not aligned = ✗

- ✓ Green Bond Principles, ICMA, 2021 (with June 2022 Appendix 1)
- ✓ Green Loan Principles, LMA/LSTA/APLMA, 2023

✓ Use of proceeds

We assess the framework's green project categories as green. ENN Energy commits to allocating the net proceeds from issuances under the framework exclusively to eligible green projects. Please refer to the Analysis Of Eligible Projects section for more information on our analysis of the environmental benefits of the expected use of proceeds. ENN Energy indicates a lookback period of three years, in line with market practice. Moreover, the issuer will disclose the share of financing and refinancing, adding transparency to its allocation reporting.

✓ Process for project evaluation and selection

ENN Energy's ESG Working Group (EWG) comprises the president, the chief director of investor relations (IR) and environmental, social and governance (ESG), the head of the quality, health, safety and environment (QHSE) department, and the head of human resources department. The EWG will meet at least annually to review and select projects according to the criteria set in the framework, internal environmental guidelines, and feasibility reports. Shortlisted projects will then be presented to the ESG committee (involving senior management including the chief executive officer) for approval. The EWG will identify and manage environmental and social risks related to green projects through feasibility reports conducted by third-party agents or consultants. The framework outlines an exclusion list that includes coal-based energy generation and distribution infrastructure, nuclear fuels, and activities related to hazardous chemical and radioactive substance.

✓ Management of proceeds

ENN Energy's accounting and finance team will manage the net proceeds, which will be deposited in the general funding accounts and be earmarked to eligible projects. Any unallocated proceeds will be held in accordance with the issuer's liquidity guidelines in short-term time deposits or investments. The issuer will maintain a register to keep track of the net proceeds. If a financed project ceases to fulfil the framework's eligibility criteria, the net proceeds will be re-allocated to replacement projects that meet eligibility criteria as soon as reasonably practicable.

✓ Reporting

ENN Energy commits to providing allocation and impact reporting through its sustainability report, annual report or website. It will report the information on an annual basis until full allocation of net proceeds. The company will also report in case of material ESG controversies associated with eligible projects. Allocation reporting will include aggregate amount allocated to eligible projects, brief description of projects, and remaining balance of unallocated funds and type of temporary investment. The impact reporting will include the invested projects' environmental and social (where relevant) impacts, such as energy produced by renewable sources, greenhouse gas emissions avoided, and annual energy savings in green buildings.

Analysis Of Eligible Projects

This section provides details of our analysis of eligible projects, based on their environmental benefits and risks, using the Shades of Green methodology.

Green project categories

Renewable energy

Assessment



Dark to Medium green

Description

Projects supporting the production and use of renewable energy, such as:

- Generation of energy from renewable sources, including solar, biomass, and geothermal
- Transmission and distribution projects that have the sole purpose of connecting renewable energy production
- Development of boilers powered by biomass, which only utilize agricultural and forestry waste

Analytical considerations

- Renewable energy projects such as solar photovoltaic (PV) and geothermal are key elements in limiting global warming to well-below 2°C, provided their negative impacts on the local environment, and physical risks are sufficiently mitigated. Biomass projects can have climate mitigation benefits depending on the feedstock and risks related to land use and associated emissions. Transmission and distribution projects are vital to support the increased electrification required for the low-carbon transition.
- The company's investments in solar and geothermal support the modelled pathways under the Paris agreement. Almost all electricity will be supplied from zero or low-carbon sources by 2050. This is important, considering China's generation mix is still heavily reliant on coal, which accounts for 60% of electricity supply in 2023 (source: [S&P Commodity Insights](#)). The company also stated the lifecycle emissions from the generation of heat/cool from geothermal projects are no higher than 100gCO₂e/kWh. These projects are therefore Dark green.
- Biomass projects will use waste- or residue-based feedstock, with procurement sites situated close to project locations. The company also use intelligent systems to optimize the routes of trade transport vehicles to improve vehicle scheduling and operational efficiency, further minimizing transportation emissions. However, the biomass feedstock is exposed to supply chain risks, such as biodiversity and change in land use. For example, visibility is limited on the sustainability of the feedstock if it is sourced from a sustainably certified forest. Hence, biomass projects are assessed as Medium green.
- Transmission and distribution projects will focus on connecting small and micro industrial park customers with renewable energy. As customers from emission-intensive industries will not be eligible, these projects are Dark green.
- Given that the company expects most of this category's allocated proceeds will be dedicated to solar PV projects, with less than 10% to biomass projects, we assign the category Dark to Medium green.
- Renewable energy projects can have negative impact on local biodiversity. ENN Energy has a biodiversity protection policy, which details the requirements on managing biodiversity risks in projects involving construction of new facilities. For instance, the company ensures project sites are outside ecological conservation areas, adheres to the principles of net-zero deforestation (maintaining the balance of forest land area), and requires its operation and supply chain partners to avoid any operational activities near World Heritage sites and the International Union for Conservation of Nature (IUCN) Category I-IV protected areas. Furthermore, ENN Energy references the Task Force on Nature-related Financial Disclosure (TNFD) framework, and includes biodiversity considerations in its risk assessment and management. It also published its first Biodiversity Conservation Report in May 2022, demonstrating its commitment in incorporating biodiversity conservation considerations into its strategies and operations.

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- ENN Energy identifies project's physical risks through feasibility study and environmental impact assessment. The company builds forecasts for four categories of extreme weather events (typhoons, extreme precipitation, extreme hot weather and extreme cold weather) using multiple national and international databases. It develops specific impact assessment and control measures to continuously monitor and manage the risks. Furthermore, the company applies the IPCC climate scenarios when assessing physical risks, and it will implement necessary adaptation measures.
- There are carbon emission considerations at various steps of the life cycle of renewable energy assets, which range from material sourcing, manufacturing, transportation, and equipment end-of-life management. ENN Energy conducts EIA to understand the lifecycle impact of assets such as solar equipment and works with suppliers and industry partners to improve equipment's durability and recyclability.

Sustainable Water Management

Assessment

 Light green

Description

Installation of drainage canals in construction sites to discharge wastewater into urban sewage pipelines if emission standards are met

Installation of mud pools to avoid infiltrating into groundwater or rivers

Use of reclaimed water and rainwater in production process, and adoption of water-saving appliances to reduce water consumption

Analytical considerations

- Infrastructure related to wastewater drainage and water conservation is important from both the environmental and climate perspective. While the projects help water quality by reducing pollution, they also contribute to reducing water scarcity and improving water supply resilience.
- Installation of drainage canal projects help redirecting wastewater from ENN Energy's construction sites into the municipal sewer pipelines for further treatment. The company typically sets up sewage treatment facilities at its construction sites, with regular monitoring and sewage testing reports. This is to ensure the wastewater discharged complies with local or national standards before exiting construction sites. ENN Energy also installs mud pools to better manage the slurry generated during construction activities, facilitate sedimentation, and prevent sediment runoff into groundwater and nearby waterway. ENN Energy shared that financed projects aim to ensure, if not exceed, regulatory compliance. The projects involve the high usage of fossil fuel equipment, and therefore receive a Light green shading.
- The use of reclaimed water and rain water is part of ENN Energy's integrated energy solution services. These focus on providing clients electricity, steam, cooling and heating services while adopting lower-carbon energy sources. The financed projects aim to improve overall water efficiency of the company's integrated energy solutions by reclaiming water and using water-saving appliances. However, the lack of thresholds for water reduction limits insight of the projects' potential environmental impacts, restricting the category shading to Light green.
- The company conducts feasibility report, EIA, and runs IPCC's climate scenarios to assess its assets' exposure to physical climate risks.

Green Buildings

Assessment

 Light green

Description

Renovation of buildings (including industrial premises), certified in accordance with any one of the following selected certification systems

- Chinese Green Building Evaluation Label (GBL) – 2 star or above
- U.S. Leadership in Energy and Environmental Design (LEED) – Gold or above







Renovation of buildings, leading to an at least 15% reduction in energy use

On-site renewable energy installations, i.e. solar PV, which may be instead included in renewable energy depending on the scale of the projects

Analytical considerations

- The IEA emphasizes that reaching net-zero emissions in buildings demands major strides in energy efficiency and abandonment of fossil fuel. In renovation projects, enhancing energy performance and minimizing embodied emissions from building materials and construction are essential for achieving low-carbon objectives. Additionally, addressing physical climate risks is crucial for strengthening climate resilience across all buildings.
- The project category receives a Light green shade, reflecting the framework criteria give the option of relying on building certifications that exceed local regulations' energy efficiency requirements, or projects leading to 15% energy use reduction. This leads to uncertainty of the future energy performance of the financed projects under this category. While ENN Energy conducts an assessment of physical climate risks, consideration is limited on embodied emissions associated with building materials.
- All properties are exposed to physical climate risks. ENN Energy shared that it relies on feasibility study, environmental impact assessment, as well as the IPCC's climate scenarios to assess its assets' exposure, with main risks being typhoons, floods, and temperature increase.
- Fossil-fuel heating/ cooling may be included in the eligible asset portfolio, creating risks of lock-in emissions. The company shared an example of the recent renovation project of its headquarter building, which utilizes its existing integrated energy facilities (including gas) in addition of renewable energy sources such as installation of rooftop PV system and air source heat pumps.
- Although green building certifications cover a broad set of environmental issues, they differ considerably in their requirements for energy efficiency, embodied emissions of construction materials, and climate resilience. Typically, their point-based system does not guarantee low carbon construction nor highly energy efficient existing buildings. Their robustness depends on a variety of factors, such as levels achieved and the type of certification. Buildings should obtain a target green certification within three years of completion.
- While embodied emissions in building materials are significant, the framework does not include specific sourcing criteria and the company does not yet have policies in place to seek to reduce such emissions. This is a limitation for eligible projects' green benefits.

S&P Global Ratings' Shades of Green

| Assessments | | | | | |
|--|---|---|--|---|--|
| Dark green | Medium green | Light green | Yellow | Orange | Red |
| Description | | | | | |
| Activities that correspond to the long-term vision of an LCCR future. | Activities that represent significant steps toward an LCCR future but will require further improvements to be long-term LCCR solutions. | Activities representing transition steps in the near-term that avoid emissions lock-in but do not represent long-term LCCR solutions. | Activities that do not have a material impact on the transition to an LCCR future, or, Activities that have some potential inconsistency with the transition to an LCCR future, albeit tempered by existing transition measures. | Activities that are not currently consistent with the transition to an LCCR future. These include activities with moderate potential for emissions lock-in and risk of stranded assets. | Activities that are inconsistent with, and likely to impede, the transition required to achieve the long-term LCCR future. These activities have the highest emissions intensity, with the most potential for emissions lock-in and risk of stranded assets. |
| Example projects | | | | | |
|  Solar power plants |  Energy efficient buildings |  Hybrid road vehicles |  Health care services |  Conventional steel production |  New oil exploration |

Note: For us to consider use of proceeds aligned with ICMA Principles for a green project, we require project categories directly funded by the financing to be assigned one of the three green Shades.

LCCR--Low-carbon climate resilient. An LCCR future is a future aligned with the Paris Agreement; where the global average temperature increase is held below 2 degrees Celsius (2 C), with efforts to limit it to 1.5 C, above pre-industrial levels, while building resilience to the adverse impact of climate change and achieving sustainable outcomes across both climate and non-climate environmental objectives. Long term and near term--For the purpose of this analysis, we consider the long term to be beyond the middle of the 21st century and the near term to be within the next decade. Emissions lock-in--Where an activity delays or prevents the transition to low-carbon alternatives by perpetuating assets or processes (often fossil fuel use and its corresponding greenhouse gas emissions) that are not aligned with, or cannot adapt to, an LCCR future. Stranded assets--Assets that have suffered from unanticipated or premature write-downs, devaluations, or conversion to liabilities (as defined by the University of Oxford).

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

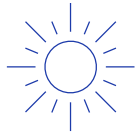
Where the Financing documentation references the Sustainable Development Goals (SDGs), we consider which SDGs it contributes to. We compare the activities funded by the Financing to the International Capital Markets Association (ICMA) SDG mapping and outline the intended linkages within our SPO analysis. Our assessment of SDG mapping does not impact our alignment opinion.

This framework intends to contribute to the following SDGs:

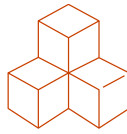
Use of proceeds

SDGs

Renewable Energy



7. Affordable and clean energy*



9. Industry, innovation and infrastructure*

Sustainable Water Management



6. Clean water and sanitation*

Green Buildings



11. Sustainable cities and communities*

*The eligible project categories link to these SDGs in the ICMA mapping.

Related Research

- [Analytical Approach: Second Party Opinions: Use of Proceeds](#), July 27, 2023
- [FAQ: Applying Our Integrated Analytical Approach for Use-of-Proceeds Second Party Opinions](#), July 27, 2023
- [Analytical Approach: Shades of Green Assessments](#), July 27, 2023
- [S&P Global Ratings ESG Materiality Maps](#), July 20, 2022

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