S&P Global Ratings

Tracking efforts towards achieving Article 2.1(c)

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S&P Ratings' Approach to Supporting Transparency on Transition and Sustainable Financing

Our mission is to provide high-quality, objective and independent analytical information to the marketplace

Sustainable finance assessments		Research	Credit ratings
Second Party Opinions	Climate Transition Assessments	Sector materiality maps Decarbonization pathways Transition technologies and market dynamics	Climate transition risk may, in some cases, materially influence creditworthiness
Shades of Green Approach			

Source: S&P Global Ratings.

Differentiation in the green labelling market helps increase transparency of alignment to Article 2.1c

- Our **Shades of Green Approach** was co-developed by a former climate finance negotiator and an IPCC AR6 WGIII Chapter 15 Lead Author, and we apply this to labelled investments (debt & equity). This enables greater transparency on how aligned an investment is with Article 2.1c.

- In our scale we apply a scale from activities consistent with a low carbon and climate resilient (LCCR) future to those inconsistent.

- We factor local **Taxonomies** into the analysis of how green an investment can be. These policies are helpful guides as to what is considered green, or sustainable, locally.

- 44% of our Green Second Party Opinions achieved a Dark Green Shade in Q2 2024, with 20% achieving Medium Green & 36% Light 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

LCCR = Low carbon climate resilient future

Renewable Energy	Dark green
Sustainable Transport	Dark green
Energy Efficiency	Medium green
Water Efficiency	Medium green
Sustainable Construction	Medium to Light green
Circular Economy	Light green

Most Rated Sustainability-Labelled Debt Nearing Maturity is Investment Grade

- Sustainability-labelling is still emerging in the public** capital markets ($2.6 trillion in outstanding labelled bonds vs ~$120 trillion in bonds; and ~$130 trillion in equity markets; Private** markets make up ~$14 trillion)

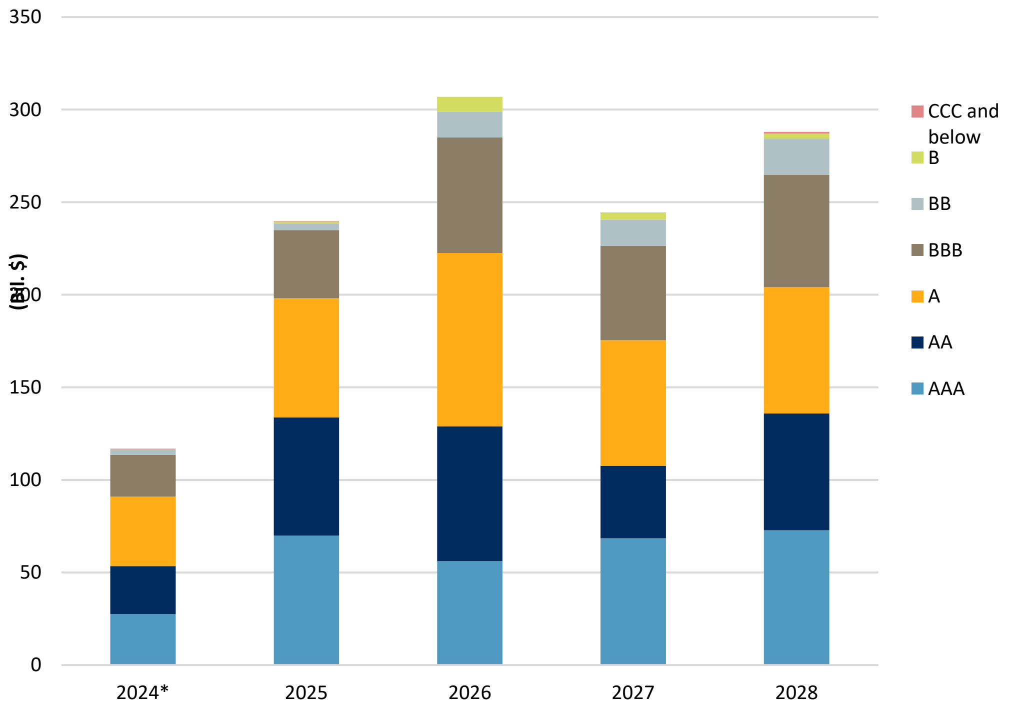
- Early positive developments: 14% of new debt is labeled, with Middle East & Latin America the fastest growing. In 2023, 33% of issuance was in currencies other than euro & US – up from 24% in 2019.

- Most of the maturing (older) market that we rate is investment-grade – sub-investment-grade instruments are most concentrated in the non-financial corporates.

- Bonds are typically an area that investors tap for stable returns, which can affect the utility of bonds as an instrument for new and unproven business ventures.

- Still, energy, transportation and buildings makeup the largest sectors in green bonds.

94% Of Rated GSSSB Debt Maturing Through 2028 Is Investment-Grade



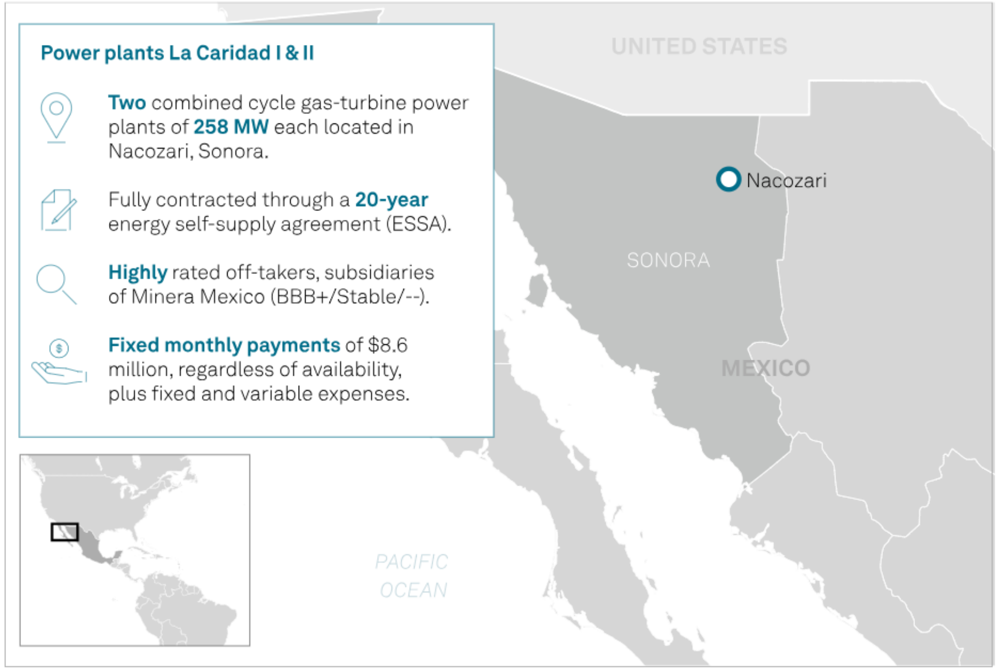
* from 01/04/2024 to 31/12/2024. Data as of April 1, 2024. Sources: Environmental Finance, S&P Global Market Intelligence, S&P Global Ratings Credit Research & Insights.

** In this context, public markets means that the assets are traded, and any investor can invest; in private markets investment flows are made between a set of parties, e.g. directly from a firm to a company

Climate Transition Policy Could Impact Locally Financed Projects

- We highlight how ESG does and could impact credit in our ratings looking out on what is **visible** and **material**
- Oil & gas industry's risk was elevated in 2021 – reflecting energy transition risks – and has remained elevated despite record earnings
- On the other hand, for these MGE gas-fired power plants in Mexico for the copper mining sector: climate transition policy could impact their asset life, but don't yet (see red box)
- This project's foreign currency debt (BBB+/Stable) is not capped by the sovereign rating owing its strong and predictable cash flow and high ratings of the off-takers

México Generadora de Energía S. de R.L.



Source: S&P Global Ratings.

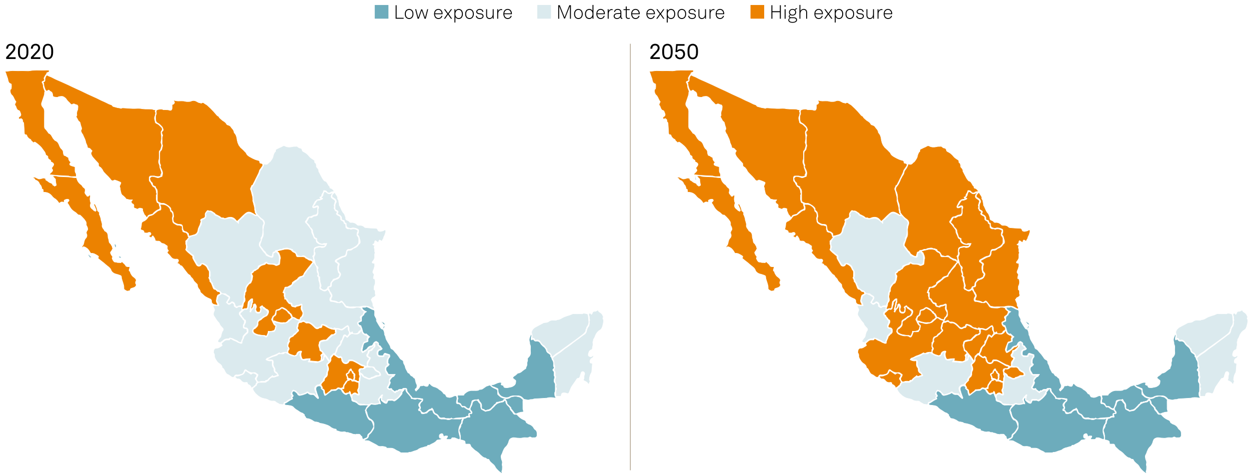
Environmental, Social, And Governance

Environmental factors are a negative consideration in our credit rating analysis of MGE, given its fossil-fuel fired generation assets. However, because Mexico's energy policies currently hamper the expansion of renewables generation and considering the low increase in renewable capacity compared to the expected energy demand, we don't expect substitution risk to emerge in the next several years.

Exploring the future using scenario analysis – why exploratory research is necessary

- When things are not clearly visible nor material, we use scenario analysis in exploratory research
- See, for example, work assessing the impact of water stress under climate scenarios on the ratings of local governments in Mexico
- Some companies in water-sensitive industries are beginning to move operations away from Mexico's industrialized and highly drought-prone northern region. We expect economic and fiscal risks stemming from exposure to high water stress in Mexico will continue to rise and could ultimately weigh on Local and Regional Governments' (LRG) credit quality over the medium to long term.
- The impact of water stress on our LRG ratings will depend in large part on the cooperation between various levels of government in planning and investing to ease water stress.

Water Stress Represents A High Physical Risk for Mexican States



Estimate based on analysis under a moderate stress scenario (SSP2 -4.5). Source: S&P Global Ratings.

Key drivers are a physical shortage of water sources or inadequate infrastructure

2/3 of Mexico's territory is in arid or semi arid areas.

76% of water supply in Mexico is used in agriculture.

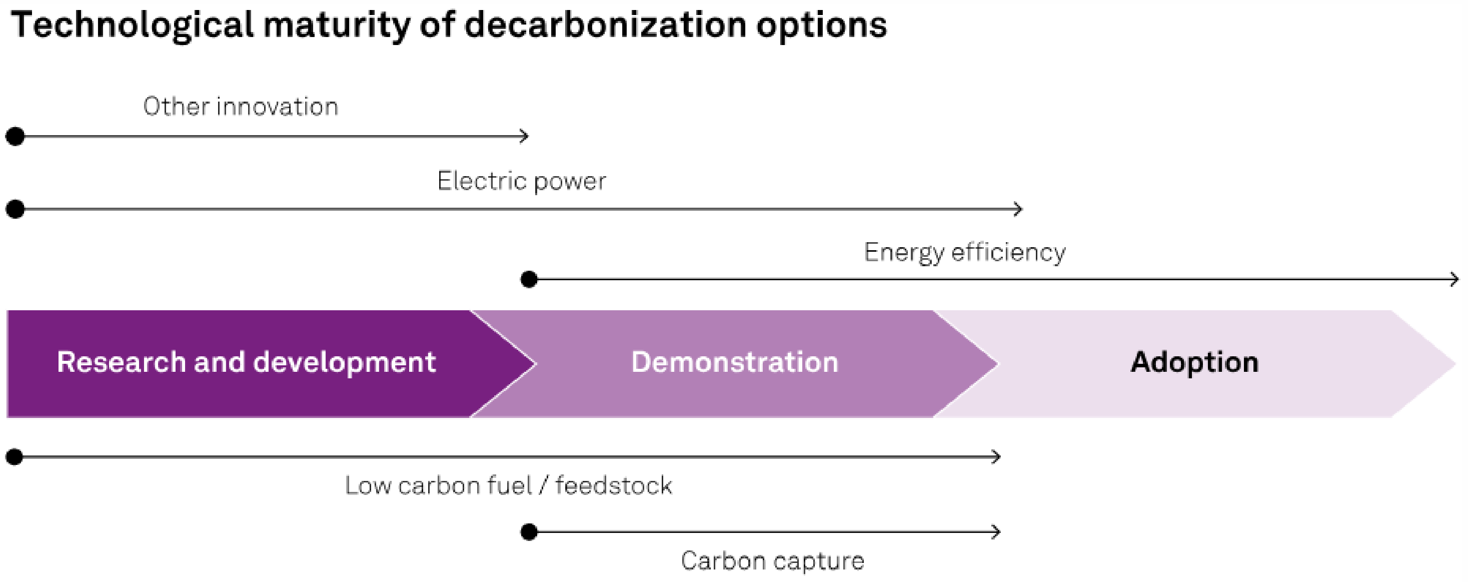
Water stress has a potential negative impact on ratings through

Economic assessment
Constrained economic development

Public finances
Stressed budgetary performance
Larger funding needs

Financial management
Ability to address infrastructure needs
Handling of debt and liquidity

Post 2030, Decarbonization Is Heavily Reliant On The Scalability Of Technology, Which Limits Credit Rating Visibility



Source: S&P Global Ratings.

- Leveraging our credit teams' knowledge of technological maturity, we have published in-depth research on decarbonization in several hard-to-abate sectors, including chemicals, cement, and metals (steel and aluminium).
- Within the hard-to-abate sectors, **under current policies**: Most policy and private sector decarbonization targets, out to 2030, **appear manageable from a credit and operational perspective**, and rely largely on electrification, use of greener energies, and efficiency measures.

Thank you

Further Reading

[Analytical Approach: Shades Of Green Assessments | S&P Global Ratings (spglobal.com)]

[Second Party Opinions | S&P Global Ratings (spglobal.com)]

[Sustainability Insights | S&P Global Ratings (spglobal.com)]

[Climate Finance in Lower-Income Countries | S&P Global Ratings (spglobal.com)]