

**NON-RATING ACTION COMMENTARY**

# **Impact of PPC's Failure to Meet Sustainability-Linked Bond Targets Limited**

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Fitch Ratings-Barcelona-16 March 2023: Public Power Corporation's failure to reach its end-2022 CO2-emissions reduction target for its EUR775 million sustainability-linked bonds (SLB) will have a limited negative impact on the company's cost of debt, Fitch Ratings says. It will not lead to any meaningful changes in the bondholder base and its pricing in the secondary market, even though the proportion of ESG-labelled funds owning the bonds is about 60%. This is because we expect main funds to factor in their decision making that the failure to meet the target is unrelated to PPC's operating performance, a change of strategy or a weakening of its sustainability focus.

PPC, rated 'BB'/Stable, the incumbent electricity utility in Greece, was the pioneer in 2021 in issuing sub-investment-grade SLBs. PPC's SLBs (EUR650 million plus EUR125 million as "additional notes" subject to the SLB framework) issued in March 2021 and due in 2026 include a coupon step-up of 50bp from 2023 if the target of a 40% reduction in Scope 1 CO2 emissions by December 2022 (to 13.9 million tonnes) compared to its 2019 level (23.1 million tonnes) is not met. The failure to meet the target has been confirmed by the company today, ahead of the disclosure of FY22 results.

The steep CO2 target reduction largely relied on a commitment to phase out existing lignite plants by 2023 and the full exit of lignite by 2028 (when the new lignite plant Ptolemaida V was expected to shift to natural gas). This was one of the quickest phasing-outs in Europe. However, security of gas supply concerns due to the war in Ukraine has

led to a temporary increase in lignite-fired electricity production and slowed the decommissioning of the plants.

PPC has reaffirmed its intention to boost investments in renewables in Greece, helping move it towards its decarbonisation goal. PPC's EUR500 million SLB bond issued in July 2021 and due 2028, contains a CO2 target reduction of 57% to be met by 2023. We expect a similar situation to the present one at end-2023.

Another issuer facing similar challenges is Polski Koncern Naftowy ORLEN S.A. (PKN; BBB+/Stable), a petroleum refiner based in Poland, which is already paying a higher coupon on two local-currency SLBs from this year due to a cut in its public ESG rating, to which the bonds' performance target was tied.

SLB bond issuances linked to sustainability goals, such as CO2 emissions reductions or water usage goals or – more residually – ESG ratings level, offer a mutual benefit for issuers (the bonds are priced favourably due to the inclusion of ESG commitments), and ESG-sensitive investors. However, the energy crisis has proved challenging for companies committed to decarbonization targets.

Contact:

Pilar Auguets

Senior Director

+34 93 467 8747

Fitch Ratings Ireland Spanish Branch, Sucursal en España

Av. Diagonal 601 Barcelona 08028

Media Relations: Tahmina Pinnington-Mannan, London, Tel: +44 20 3530 1128, Email: [tahmina.pinnington-mannan@thefitchgroup.com](mailto:tahmina.pinnington-mannan@thefitchgroup.com)

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