Green Bond

Investor Letter and Impact Report

2021

- In October 2019, SKF launched its Green Finance Framework and the Green Bond to align SKF's funding strategy with the Group's climate objectives. The framework was independently evaluated and was rated by CICERO as Light Green.
- The implementation of the Green Bond is an integral part of SKF's climate strategy. During 2020 and 2021, the Group has further raised the climate ambition level through the commitments to have net zero greenhouse gas emissions in the operations by 2030 and in the supply chain by 2050.
- As part of the Green Bond governance process, several hundred of potential projects have been assessed against defined categories and criteria.
- By the end of 2021, SKF had financed 90 projects through the Green Bond, amounting to EUR 300 million of allocated proceeds, with the following distribution:
  - 39% Europe, 33% Asia and Pacific, 6% North America, 2% Latin America, 20% global.
  - 71% new financing, 29% refinancing.
  - 90% investments and acquisitions, 10% expenses.
- Impact calculations to determine the quantified savings in terms of, for example, energy use, material use, and CO_2 emissions have been supported and verified by the Group EHS experts.

Introduction

Climate change and other environmental issues faced by the world present a critical challenge for business, governments and society. The ability of SKF to run its own operations towards becoming net zero helps to meet those challenges and increases SKF's competitive advantage. At the same time, SKF is well positioned to help its customers reduce their climate impacts, and those of their end customers and products.

SKF provides reliable rotation by combining hands-on experience in over 40 industries with in-depth knowledge across the SKF technology areas: bearings and units, seals, services and lubrication systems. SKF's products and solutions help customers to improve safety, reduce friction, improve process efficiency, reduce waste and use of material, extend service life, and to achieve other sustainability benefits. We also contribute to the growth of transformative cleantech sectors, such as the renewable energy industry and electric vehicles.

Engaging in green financing connects SKF's company funding strategy to the climate objectives. It's a way to engage our stakeholders in our integration of sustainability into SKF's business model and to ensure our strategy, investments and development activities keep to our commitment.

The Green Bond is used to finance projects in whole or in part that support the transition to low-carbon, climate resilient growth and lower environmental impacts. The primary areas are increased energy and material efficiency, use of renewable energy, reduced waste and reduced emissions.

SKF's climate objectives

SKF uses a life-cycle approach to drive improvements across the value chain in four main areas: raw material and components, SKF's own operations, goods transportation, and customer solutions. These areas are selected based on a thorough understanding of the life cycle climate impacts, combined with SKF's ability to influence the changes needed to reduce these impacts.

In July 2021, SKF signed up to the Science Based Targets initiative and committed that the climate targets shall be in line with the Paris Agreement to limit global warming to 1.5°C.

In October 2021, SKF announced its target to achieve net zero greenhouse gas emissions in the full SKF value chain (from raw material to finished product delivered to the customer) by 2050.

Raw material and components

SKF works to influence energy intensive suppliers to implement the ISO 50001 energy management standard. This way of managing energy and emissions is considered a pragmatic approach to reduce energy use and associated CO_2 emissions in the upstream value chain. By the end of 2021 there were 42 suppliers in scope of this initiative, whereof 56% were certified according to ISO 50001.

During 2020 and 2021, SKF has accelerated the collection of energy and CO_2 data from its major steel and forging suppliers representing the majority of value, weight and environmental impact in the upstream value chain. SKF has developed digital tools which support the assessment of each supplier's CO_2 impact in the supplier evaluation process.

SKF's own operations

SKF works to reduce CO_2 emissions from its production facilities in several ways:

- Improve material efficiency and reduce waste by assuring stable and efficient processes.
- Drive systematic improvement in energy efficiency. SKF is certified according to the ISO 50001 energy management standard and has defined clear targets, strategies and actions to reduce energy demand in the factories.
- Procure or generate renewable energy whenever this is practically and commercially viable.

The long-term objective is to have net zero green house gas emissions in SKF operations by 2030 (scope 1 and 2), including 100% renewable electricity. Comparing 2021 to 2015, absolute CO_2 emissions have been reduced by 37%, while revenues have increased by 10%.

The mid-term objective is to achieve a 40% reduction of CO_2 emissions from bearing manufacturing per tonne of bearings sold, by 2025 compared to 2015. By the end of 2021, the Group had achieved a 50% reduction.

Goods transportation

SKF works to reduce CO_2 emissions from transports in several ways:

- Optimize transport network and routing.
- Use energy efficient transport modes and procure transports with low CO_2 intensity (e.g. ocean and rail instead of air, and transports using low-carbon fuels).
- Minimize mileage between suppliers, factories, warehouses and customers.

The mid-term objective is to achieve a 40% reduction of CO_2 emissions per tonne of goods shipped to end customer, by 2025 compared to 2015. Due to increased scope of reporting versus previous years the outcome for 2021 was +23%.

Customer solutions

For many years, the Group has built up knowledge around life-cycle management and how environmental and social impacts can be reduced or avoided. Studies show that the greatest impact is during the use phase of SKF's products in customer applications and systems. SKF can enable improvements in customers' sustainability performance through products, services, business models and value propositions. The improvements include increased energy efficiency, reduced CO_2 emissions, improved safety, reduced water use, increased lifetime of applications, increased material efficiency, reduced noise levels, etc.

SKF has made cleantech one of its strategic focus areas and will continue to add technologies and offerings to the value propositions. The Group enables and drives technology development in industries such as renewable energy generation and sustainable transport systems, including electric vehicles. Moreover, the Group develops new circular business models and works in collaboration with its customers to improve sustainability performance of their applications and systems. To support that work, SKF has established guidelines for product development, environmental pre-evaluation tools and guidelines for quantifying and communicating customer sustainability performance.

As part of the Group's climate objectives, SKF provides yearly aggregated revenue data from SKF customer solutions enabling climate change mitigation in four areas: renewable energy generation, electric vehicles, recycling industry and bearing remanufacturing. The total revenues of these areas amounted to SEK 6.8 billion in 2021.

SKF's Green Bond

As one of the first industrial companies, SKF issued a Green Bond in November 2019. The value of the bond is EUR 300 million with a duration of ten years.

To secure alignment with national and international guidelines SKF has obtained an external opinion on the Green Finance Framework. This second opinion from the Centre for International Climate and Environmental Research (CICERO) rated the Green Finance Framework Light Green with a governance score of Excellent.

Categories and criteria

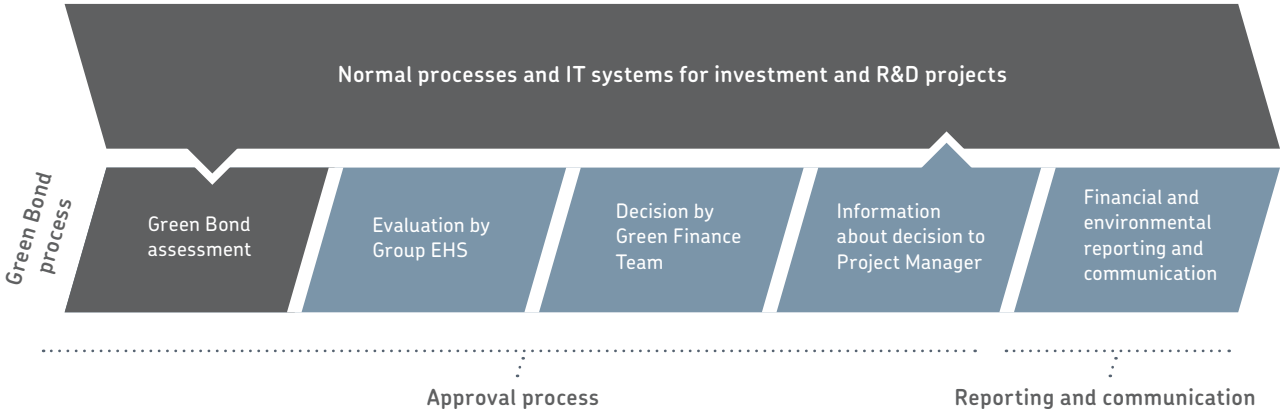
The Green Bond is used to finance assets that support the transition to low-carbon, climate resilient growth and lower environmental impacts. It helps to further align the Group's funding strategy with the climate objectives, to reduce CO_2 emissions from its own manufacturing and supply chain operations, as well as support customers to reduce their emissions. The seven categories eligible under SKF's Green Finance Framework are described below.

SKF'S GREEN BOND

Volume: EUR 300 million
Tenor: 10 years
Interest spread: MS+80 bps
Yield: 0.891%
Coupon: 0.875%
Price: 99.848%
Listing: Luxembourg Stock Exchange (LuxSE). The bond will also be displayed on the Luxembourg Green Exchange (LGX).

CATEGORIES AND CRITERIA

Category	Criteria
Investments in world-class manufacturing	• More than 25% improvement in energy use and/or material use, per unit of output
Investments enabling cleantech	• Investments: 75% or more of the total cost must be related to cleantech, which makes the complete investment eligible. If less than 75% is related to cleantech, then only the actual part will be eligible • Acquisitions: 90% or more of the total business must be related to cleantech, which makes the complete investment eligible
Investments in Green Buildings	• Factories/buildings (new construction or refurbishment of existing) with a plan for LEED certification, minimum Gold level
Investments in renewable energy installations for SKF	• Investments on site or off site in renewable energy generation (wind, photovoltaic, solar thermal) for SKF facilities
Investments in process/facility energy or resource efficiency	• More than 25% improvement in energy use and/or material use, per unit of output
R&D expenses targeting cleantech	• The product/service/technology is being developed for cleantech
R&D expenses targeting green products and processes	• The product/service/technology is being developed for any of these purposes: – R&D related to efficiency technologies which can significantly improve climate performance (reduce energy use, reduce greenhouse gas emissions), or circular economy performance (reduce, reuse or recycle materials) of SKF's products and processes – R&D aimed at eliminating or mitigating harmful substances and materials in products and processes, beyond legislative requirements – R&D related to world-class manufacturing



Process for project selection and evaluation

A Green Bond assessment is done as part of the normal processes for investments and R&D projects. Based on this assessment and the supporting documentation, experts in the Group Environment, Health and Safety organization (Group EHS) make an evaluation against the defined Green Bond categories and criteria. SKF has established a Green Finance Team which approves the evaluations made by the Group EHS experts and decides about Green Bond financing for investments and R&D projects. The Green Finance Team also reviews and approves the Green Bond processes and reporting. Decision-making is made on a unanimous basis and all decisions are documented. The Green Finance Team is chaired by the Group CFO and consists of representatives from finance, treasury, EHS, sustainability and manufacturing.

Projects in the Green Portfolio

By the end of 2021, SKF had financed 90 projects through the Green Bond. An overview of these projects is presented below.

EXAMPLE 1

Milling process automation

Category: Investments in process/facility energy or resource efficiency

Green Bond financing has been used for several investments, to improve energy or resource efficiency in SKF's manufacturing operations. Examples include; upgrading of heating systems based on fossil fuel to electrical systems, RecondOil installations to reuse the lubrication oil and contributing to the circular economy, and investments in more energy efficient production equipment.

To give a specific example, during 2021, it was decided to use the Green Bond to finance the replacement of three old machines in a production line with one automated milling machine, making it possible to exclude several process steps. The expected benefits include an energy efficiency improvement of 61% as well as increased output and quality of products, and decreased maintenance cost. The yearly energy savings from this particular investment are expected to be around 120 MWh.

EXAMPLE 2

Renewable energy generation at SKF sites

Category: Investments in renewable energy installations for SKF

The main source of energy used in SKF's operations is electricity. As part of the journey, to reach net zero greenhouse gas emissions and use 100% renewable electricity by 2030, SKF is investing in renewable energy installations at many sites around the world. During 2021, it was decided to use the Green Bond to finance two projects focusing on photovoltaic solar panels, in addition to the four projects already approved in 2020, at sites in Europe, North America and Asia and Pacific.

These projects help to reduce both energy cost and CO_2 emissions. Moreover, they demonstrate SKF's commitment to employees and local stakeholders. Expected yearly renewable energy generation from these six projects is around 11,000 MWh, corresponding to a yearly reduction of more than 7,400 tonnes of CO_2 emissions based on an estimated world average conversion factor for electricity generation.

OVERVIEW OF PROJECTS

Category	Overview
Investments in world-class manufacturing	• New technologies strengthening SKF's global manufacturing capability, including automation and digitalization, leading to significant energy and material efficiency improvements
Investments enabling cleantech	• Increased production and testing capacity for products enabling renewable energy generation, electric vehicles and railway applications • Increased capacity for the remanufacturing of bearings and units • Acquisition of RecondOil enabling the reuse of industrial oils, supporting a circular economy
Investments in Green Buildings	• Expansion of the global technical centre at SKF in India.
Investments in renewable energy installations for SKF	• Onsite renewable energy generation (mainly photovoltaic solar power) at multiple sites in Europe, North America and Asia and Pacific
Investments in process/facility energy or resource efficiency	• New technologies improving material and energy efficiency in manufacturing operations, such as in HVAC systems and RecondOil installations in SKF factories
R&D expenses targeting cleantech	• Research focusing on technologies and products for renewable energy generation, electric vehicles and railway applications
R&D expenses targeting green products and processes	• Research focusing on significant improvements in service life, friction characteristics, recyclability, etc. including automation and digitalization

EXAMPLE 3

Production capacity increase for products enabling the electric vehicle industry

Category: Investments enabling cleantech

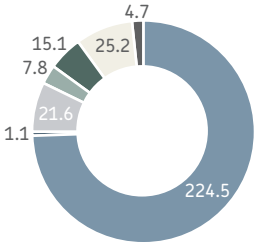
During 2021, SKF has continued to invest in increased production, testing and remanufacturing capacity for products enabling the growth of cleantech, including renewable energy generation, electric vehicles and railway applications. For example, the Group has approved an investment in four new manufacturing channels in Monterrey, Mexico, for production of bearings for electric vehicles. SKF's bearings and related technologies, help to enable mobility using electric vechiles, thereby avoiding the CO_2 emissions related to mobility from other more carbon-intensive technologies, such as, combustion engines using fossil fuels. SKF's expected contribution to the avoided CO_2 emissions from yearly production in Mexico is estimated to around 250 tonnes of CO_2 each year during the lifetime of the vehicles.

Allocation and impact reporting

By the end of 2021, SKF had allocated proceeds amounting to EUR 300 million. The distribution and estimated impact of the Green Portfolio is presented below.

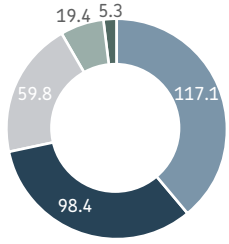
Allocation of proceeds

Per category, EUR million



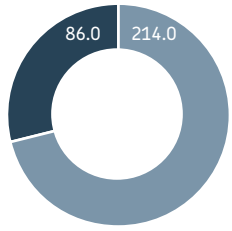
- Investments enabling cleantech
- Investments in Green Buildings
- Investments in process/facility energy or resource efficiency
- Investments in renewable energy installations for SKF
- Investments in world-class manufacturing
- R&D expenses targeting cleantech
- R&D expenses targeting green products and processes

Per geography, EUR million



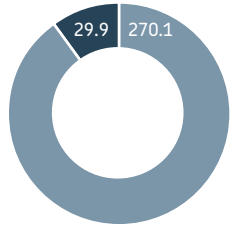
- Europe
- Asia and Pacific
- Global
- North America
- Latin America

Per new financing and refinancing, EUR million



- New financing
- Refinancing

Per investments and acquisitions and expenses, EUR million



- Investments and acquisitions
- Expenses

Green Bond impact

All projects financed through the Green Bond have been assessed against the defined categories and criteria. Experts in the Group EHS organization have checked that necessary supporting documentation relating to the environmental impact of the projects has been collected.

Impact calculations to determine the quantified savings in terms of for example energy use, material use, and CO_2 emissions have been supported and verified by the Group EHS experts. The methodology applied for these calculations is presented in the appendix of this report.

Due to the diversity of projects in the various categories, it is not possible to provide a meaningful aggregated impact figure for the total Green Portfolio. Results from the impact calculations are presented for a selection of examples to demonstrate the type of environmental objectives pursued by the projects, as well as the magnitude of the savings.

GREEN BOND IMPACT

Category	Estimated impact
Investments in world-class manufacturing	Savings in energy use from approved investments amount to 6,000 MWh per year, corresponding to 450 tonnes of CO_2 per year using SKF site specific CO_2 conversion factors, or more than 3,000 tonnes of CO_2 per year using country average CO_2 conversion factors.
Investments enabling cleantech	SKF's investment in increased capacity enables the growth of industries such as wind, electric vehicles and railway. Moreover, SKF has invested in increased capacity to remanufacture bearings, thereby reducing material use and CO_2 emissions in the production phase (compared to manufacturing of new products). SKF has aquired the Swedish company RecondOil that has developed a chemical rejuvenation process for industrial oil.
Investments in Green Buildings	Minimum LEED Gold. This means that the building has been designed to improve performance in areas such as energy savings, water efficiency, CO_2 emissions reduction, indoor environmental quality, and savings of materials. Please note that SKF's new Group Headquarters, which was inaugurated during 2020, has been built and certified according to the LEED Platinum standard. The investment as such meets the Green Bond criteria. However, since the building has been sold during 2021, it is no longer included in the list of Green Bond projects. The corresponding amount has instead been used to finance other projects meeting the Green Bond criteria.
Investments in renewable energy generation for SKF	SKF is investing in onsite renewable energy generation. The expected yearly renewable energy generation from the six projects approved for Green Bond financing in 2020 and 2021, amounts to around 11,000 MWh, corresponding to a yearly reduction of more than 7,400 tonnes of CO_2 emissions based on an estimated world average emission factor for electricity generation.
Investments in process/ facility energy or resource efficiency	For example, Green Bond financing has been used in investments to upgrade and replace heating systems based on fossil fuel to electrical systems. One such example is from the site in Tudela, Spain. By replacing a system based on the combustion of natural gas to a new system powered by 100% renewable electricity, savings in energy use amount to 4,500 MWh per year, energy efficiency is improved by more than 75% and CO_2 emissions are avoided completely. Several investments to install RecondOil in SKF factories have been approved for Green Bond financing. With these systems installed at our sites, SKF will be able to reuse the lubrication oil. Thereby, significant amounts of oil will be saved compared to regular oil filtering and replacement technologies.
R&D expenses targeting cleantech	SKF's R&D focusing on technologies and products for renewable energy generation, electric vehicles and railway applications will help to improve performance of current cleantech technologies as well as enable new cleantech innovations. Thereby, SKF aims to support the growth of these technologies and industries, which in turn, will help to reduce environmental impact on a large scale. However, quantifications of the reduced environmental impact from R&D projects need to be based on several assumptions with many uncertainties and are therefore not presented at this stage.
R&D expenses targeting green products and processes	SKF's R&D related to improving product and application performance in for example friction, service life and reliability will help to reduce the environmental impact in terms of savings in energy use, savings in material use and avoided CO_2 emissions. However, quantifications of the reduced environmental impact from R&D projects need to be based on several assumptions with many uncertainties and are therefore not presented at this stage.

Appendix – methodology

SKF uses a method based on life cycle thinking, to calculate material and energy use related to manufacturing output to assess if investments fulfill the Green Bond criteria. When applicable, these results can be converted to CO_2 emissions using commercially available datasets.

Goal and scope, baseline, and allocation
The aim of the method is to provide a credible and practical way to quantify the improvement in environmental impact from investments. Each calculation starts with a definition of the goal and scope of the study, defining what is to be calculated and the context. The performance of the new technology is compared against that of the existing (baseline) technology. Material and energy used by other processes that are affected by the investment, for example hydraulics or compressed air, are allocated using the principles in ISO 14044.

Data quality and transparency
The method uses both primary and secondary data sources, for example, data measured in SKF manufacturing or obtained from suppliers. The quality is assessed in terms of technology, time, geography, completeness and reliability. Calculations are documented and stored centrally. SKF uses a conservative approach to avoid overestimation. Data is collected to cover the most significant processes (contributing to around 90% of the material and energy use).

Note on cleantech and renewable energy
The environmental impact of investments enabling cleantech is estimated based on the capacity increase made possible by SKF. As an example, the reduced CO_2 emissions from an investment in new production channels for the production of bearings to electric vehicles is estimated based on the enabled production of new electric vehicles. It is calculated as the difference in CO_2 emissions of electric vehicles compared to vehicles using combustion engines, and using economic allocation based on the value of SKF's products in relation to the whole electric vehicle.

PUB GCR/R3 19318 EN · March 2022

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