



**AUGA GROUP, AB**

GREEN BOND  
FRAMEWORK

OCTOBER, 2019

## 1. COMPANY OVERVIEW

AUGA group, AB (the **Company**), based in Lithuania, together with its direct and indirect subsidiaries (the **Group** or **AUGA**) is Europe's largest organic food producer from field to shelf. The period of 2015 - 2018 marked the Group's conversion journey from conventional farming to organic food production, with approx. 38,000 ha of EU-certified organic arable land currently under management.

The Group of 1200 employees and 136 legal entities has been developing a sustainable farming model, based on innovative technologies. Using in-house and contracted manufacturing, the Group produces a wide range of organic food products from commodities to end-consumer goods. The Group's exports to more than 30 markets worldwide amount to around 80% of total revenue. Consolidated revenue of the Group in 2018 was around EUR 55 million.

The Company's shares are dual-listed on the Nasdaq Vilnius and Warsaw stock exchanges. The shareholders of the company include Baltic Champs Group, UAB (55.04%) fully-owned by the incumbent CEO of AUGA group Kestutis Juscius; European Bank for Reconstruction and Development (EBRD) (8.71%) and other shareholders (36.25%).

One of the reasons behind the Company's strategic decision to transition from conventional to organic farming was also a concern about the industry's environmental impact as well as an aim to find more environmentally sustainable ways of farming and food production. Globally, agriculture along with the emissions from deforestation due to land conversion, accounts for around 23% of total human activity-caused greenhouse gas (GHG) emissions<sup>1</sup>. These are typically attributed to carbon dioxide (CO<sub>2</sub>) released during soil cultivation with agricultural machinery, methane (CH<sub>4</sub>) associated with livestock enteric fermentation and manure, nitrous oxide (N<sub>2</sub>O) arising from the use of fertilisers and manure. Agriculture is the key contributor to climate change and, under current conditions, projected to increase by 18% and 30% in 2030 and 2050 respectively<sup>2</sup>. With an aim to tackle some of the causes at present, the Company has already started applying sustainable farming methods on a large scale.

On the basis of this Green Bond Framework, the Company intends to provide institutional and retail investors an opportunity to invest in the Company's Bonds. Proceeds of these shall be used to cover part of the costs of the transition to a more environmentally-sustainable farming and food production model as well as finance the Group's initiatives and innovations which are expected to support a low-carbon, climate resilient and healthier society in the long run.

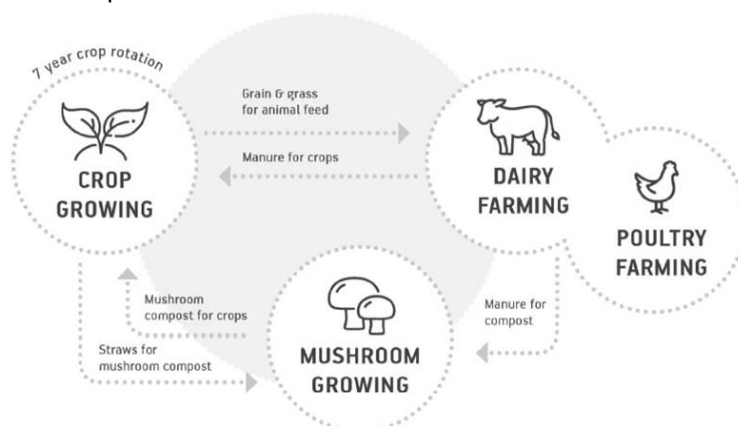
It is, therefore, important to underline that the Company firmly believes that its operations represent a green project in its own right since the Group already delivers certified organic food with an all-encompassing approach to making agriculture more environmentally sustainable, foreseeing a GHG footprint reduction throughout the production chain as the ultimate goal.

## 2. SUSTAINABILITY APPROACH

### 2.1. Current practices

Since the beginning of the Group's transition to organic agriculture, the Company based its sustainability efforts on three main pillars, i.e.:

1. **Closed-loop organic farming model.** The Group is using synergies among different branches of agriculture efficiently with an end-goal of a fully-functioning circular economy model. Such a model facilitates more efficient use of existing resources, where the inputs for each branch of agriculture are found in the other business segment deliverables or waste generated by processes in the loop. It also ensures full traceability in organic production and the indirect reduction of the GHG footprint to nature.<sup>3</sup>



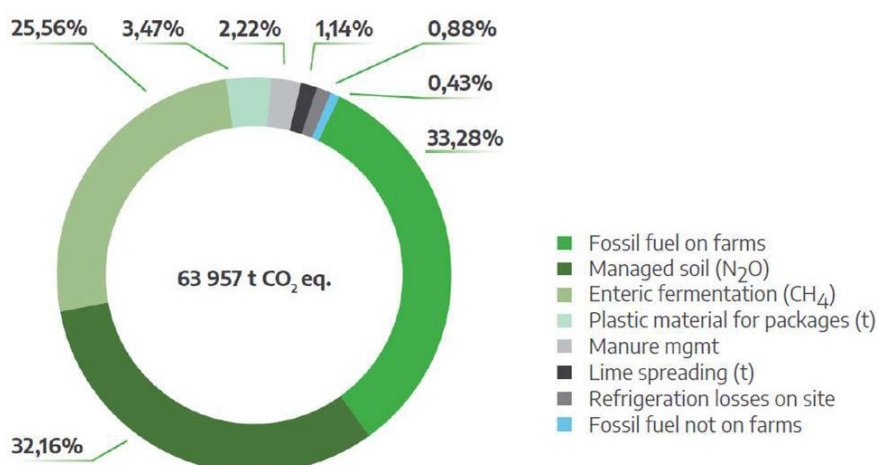
2. **Min-till technology.** The Group is implementing sustainable organic agriculture practices via the use of the latest eco-friendly machinery and min-till technology, currently applied to 85% of the total cultivated land. Rather than applying traditional ploughing techniques, the min-till approach involves disturbing only the first 5-7 cm of soil, which results in preservation of soil from erosion, saving biodiversity and reduction of fuel consumption, i.e. lower GHG emissions. The use of advanced machinery is viable due to AUGA's economies of scale when compared to the typically far smaller areas of land to be cultivated using organic principles.
3. **Green energy.** The Group also runs all its production and administrative facilities on certified green electric power. Every single company within the Group whether producing crops, livestock, mushrooms or at the headquarters in central Vilnius purchases only green electricity generated from renewable sources.

## 2.2. Innovation initiatives / projects with long-term carbon reduction potential

The long-term objective of the Group is a neutral CO<sub>2</sub> footprint throughout its core business segments

In 2018, 91% of the Group's direct and indirect GHG emissions (amounting to 58,201 t of CO<sub>2</sub> equivalent [eq.]) originated mostly from three areas of agricultural activities, i.e.:

- (a) fossil fuels on farms (CO<sub>2</sub>);
- (b) cultivated soil (N<sub>2</sub>O);
- (c) enteric fermentation (CH<sub>4</sub>).



In line with the continuation and further application of the current sustainability practices (as listed in Section 2.1), the Company has also envisioned and commenced preparations for a number of projects aimed at reducing GHG emissions from its operations, of which the following are the main ones:

1. Introduction of a **biogas cycle in the Group's agricultural operations**, from extraction and purification of biomethane through to running own-designed agricultural machinery on the self-processed biogas. The Company puts a strong focus on the secondary use of waste and by-products, emerging from other branches of the Group's business. For instance, manure from dairy and poultry farms can be utilised in the production of biogas that can be purified into biomethane. In turn, biomethane can power tractors and other vehicles, including the possibility to supply the biogas to municipal transportation systems with infrastructure available in the main economic hubs of Lithuania and, possibly, other regional centres (i.e. compressed natural gas [CNG] filling stations and buses running on CNG). The extraction of biogas from manure and the usage of purified biogas for fuel, is one of the most efficient ways for second-generation biofuel to be reintroduced to farm mobility systems. A Lund University study finds that such an approach is up to 148% more beneficial to the climate compared to using fossil fuels<sup>5</sup>. In addition, the organic waste (digestate) left after biogas production can be used as an effective fertiliser for the fields increasing soil productivity by 18%<sup>6</sup> and, hence, decreasing emission proportion per unit of agricultural produce. All in all, a significant positive impact can be sustained on the environment when the biogas cycle is introduced to the Group's agricultural activities.

2. Establishment of **specialised feed technology, with an aim to reduce methane emissions** from bovine enteric fermentation. As referred to previously, enteric fermentation – a natural digestive process that occurs in ruminant animals such as cattle – accounts for almost 26% of the Group’s GHG emissions and, according to the Food and Agriculture Organization (FAO), for about 40% of global agricultural production emissions in the past 27 years<sup>7</sup>, making it the number one source of GHGs from agriculture<sup>8</sup>. Given that dairy farming is an integral component of the Group’s closed-loop business model, it is essential for AUGA to address the issue. The specialised feed technology concept relates to the innovative process and technology, associated with proprietary feed production, treatment, adapted formulations of forage, all the way through to monitoring and measuring the effect on the cattle on the farm. The adapted feed formulations would target to significantly reduce the ruminant emission of methane to the atmosphere per unit of milk produced. Such a programmed set-up would ensure best animal welfare practices and contribute to the abatement of methane (CH<sub>4</sub>) emissions.
3. Improvement of **crop rotation in relation to carbon sequestration and nitrogen accumulation capabilities**. The leguminous perennial grasses (alfalfa, clover, etc) have a property that fixates nitrogen from the atmosphere with the help of symbiotic bacteria within the nodules of their root systems. Moreover, they absorb CO<sub>2</sub> to soil organic matter, while, conversely, cereal cultivation releases CO<sub>2</sub> into the atmosphere leaving organic matter depleted. Additionally, when cultivating perennial cultures, these do not necessitate the kind of fertilisation application onto fields which are typically associated with emission of nitrous oxide gases to the atmosphere. Increased volumes of the leguminous crops would not only add to sequestration, but also could take up a larger proportion in the feed chain, whereby gaining a secondary role in the farming cycle and increasing its value-added in the farming chain. Within the frame of the Group’s closed-loop business model, this diversification of the crops would allow growing less-pollutant feed with lower N<sub>2</sub>O emission properties, in part, replacing the currently-used cereals.
4. **Alternative farming technologies** demonstrating a sizeable impact on the reduction of GHG emissions in the farming loop and exemplifying circularity potential.

### 2.3. Recognition

Although only halfway through its journey to more sustainable farming and food production, the Company has already been recognised for its initiatives and efforts in this area, namely:

1. The EBRD “Sustainable Energy Gold Award” 2019 for incorporating an innovative closed-loop circular process into the production cycle and developing biogas production to reduce fossil fuel consumption;
2. Stockholm School of Economics (SSE) Riga Environmentally Sustainable Development 2019 award;
3. Shortlisted in the Sustainable Development category at the Swedish Business Awards organized by the Swedish Chamber of Commerce in Lithuania in 2017.

## 3. GREEN BONDS

AUGA’s Green Bond Framework covers the Company’s bonds planned to be issued in multiple tranches during the period of 2019 IVQ – 2020 IVQ under both private placement as well as public offering formats. This represents the bond programme (collectively “**Bonds**”).

The Framework has been developed in line with the ICMA Green Bond Principles (**Principles**) and follows the four key components:

1. Use of proceeds;
2. Evaluation and selection process;
3. Management of proceeds;
4. Reporting.

### 3.1. Use of proceeds

The Company shall use the proceeds of the Green Bonds for:

1. Working capital and general corporate purposes related with the ongoing sustainability initiatives of the Company (as per Section 2.1); and
2. Financing those R&D projects of the Group with the potential to provide favourable solutions for reduction of the Group's GHG emissions within the greatest emitting areas of the Group's operations (as per the list of main projects/areas in Section 2.2).

Given the specifics of the sustainable organic farming and food operations and financial cycle, financing of the Group's working capital should be considered eligible for green bond financing due to the following reasons:

- (a) AUGA's transition from conventional to organic farming contributed to the reduction of the impact of the agricultural supply chain on the environment. This was financed from the Group's working capital and bank financing, hence using the Bond proceeds for working capital would also effectively represent refinancing of such costs.

The Group's current consolidated balance sheet carries the burden of the expenditure incurred to finance the former conversion process, namely:

- (i) The share of adjusted working capital<sup>10</sup> attributable to the total organic land area in 2015 IIQ (at the time, the land in conversion) and 2019 IIQ amounted respectively to EUR 11.6 m and EUR 42 m, demonstrating a tangible increase by 262% (whilst total cultivated land increased by only 52%);
  - (ii) 2019 IIQ EUR 42 m adjusted working capital represented 75% of the total net financial debt (EUR 56 m).
- (b) Introduction and continuous application of sustainable practices (as per Section 2.1) and investment into sustainability enhancing R&D projects (including those indicated in Section 2.2) have been financed from the Group's working capital, equity (part of the 2018 follow-on public offering of the Company's shares) and bank financing. Hence using the Bond proceeds for working capital would also effectively mean refinancing of such costs.
  - (c) Diversification of the Group's working capital financing sources enable the Group to continue with its already recognised and workable green initiatives, as well as providing flexibility to allocate more funds for the development of innovative ideas for sustainability-enhancing R&D projects and finance them at the seed stage (until they become eligible to be financed as separate green projects within the Group).

Sustainable investments typically share a precondition of not only a protracted return on investment (ROI), but also make it difficult to monetize the value of the long-term environmental objectives (i.e. pollution prevention and control, biodiversity conservation and climate change mitigation). Most of the bank financing instruments available on the market, on which the Group currently relies, have limited/short-term cash return cycles and thus creating a mismatch to accommodate financing of sustainability practices and innovation investment plans. In addition, the nature of volatility in the industry of agriculture combined with increasingly unpredictable weather conditions caused by climate change, predetermining the outputs in any given year, further decreases the bankability of financing operations of organic farming and sustainability-increasing R&D innovations in the area.

Bond financing would enable the Group to allocate more funds that traditionally have fallen under working capital to the development of higher-impact technologies. Such allocation is important as it allows to extend the financing timelines needed to ensure the financial viability of disruptive R&D innovation typically associated with the methodological difficulty of measuring exact positive impact to the environment and preconditioning longer-term returns. Successful Bond issues will contribute to the attainment of the Group's long-term vision to increase sustainability of its operations and reduction of impact through, amongst other, further reduction of GHG emissions in the field and farm operations, integration and consolidation of the farming and field inventory to the highest environmental standards.



### 3.2. Evaluation and selection process

Immediately after issuance of the first tranche in the Bond programme, Selection committee shall be created in the Company with the following composition: CEO, CFO, Head of Business Development and Innovation, Head of Legal, Head of Quality and Environmental Specialist. Other responsible persons shall be included, if necessary. The Selection Committee will be responsible for both negative screening guidance and selection of the green projects.

Part of the proceeds intended to be used for working capital purposes shall be utilised for partial repayment of existing bank debt, payment of outstanding amounts of agricultural land acquisitions and other working capital purposes, ensuring that it is allocated in accordance with the management of proceeds principles as per Section 3.3 herein and serves as refinancing of completed and on-going green practices of the Group as per Section 3.2.

In respect of future financing of green projects, eligible projects will be selected and approved by the Selection Committee or, should the volume and size of the projects to be considered so merit, by the Board of the Company. At the selection and approval stage the expected impact of the innovation projects shall be evaluated, including, but not solely focusing on the GHG emission reduction potential along with additional positive externalities to the animal welfare, business efficiency, consumer health, recyclability and circularity (closed-loop) considerations.

### 3.3. Management of proceeds

The Group commits to transparent allocation and management of Bond proceeds.

To ensure that the part of Bond proceeds allocated for working capital financing are used in compliance with the Principles, the Company shall undertake negative screening, i.e. ensure that the proceeds are not knowingly allocated to the objectives that do not comply with the environmental sustainability objectives of the green bonds (e.g., proceeds should not be used for covering/refinancing the costs of purchasing fossil fuel or vehicles powered by fossil fuel). Proceeds to be used for future financing of the green projects shall be placed in one or several separate bank accounts dedicated for the purpose to ensure traceability and transparency of the use of those funds for the green projects / initiatives as per Section 2.2 of this Framework. Starting with the first tranche of the Bonds dedicated for future green project financing, the Company will establish internal tracking systems to monitor and account for the allocation of such proceeds.

Any unallocated proceeds of the first tranche will be kept in a separate bank account dedicated for the Bond proceeds. Prior to further issue/s of tranches, the Company will adopt a liquidity policy (Company's conduct with short-term money market instruments).

### 3.4. Reporting

The Company shall publish a Green Bond report on its website at least annually. The first such report will be made available within 14 months as of the settlement of the first tranche of the Bonds. Such reports shall, amongst other matters, include (when relevant) a description of eligible projects, their expected impact, total amount of investments and expenditures of eligible projects, as well as the balance of unallocated proceeds.

Initiatives and projects, achieved impact of which the Company will be able to measure and monitor with reasonable certainty, may also be included in regular sustainability / ESG reports of the Company. Such reporting should disclose direct and indirect abatement of GHG emissions (in tonnes of CO<sub>2</sub>) in relation to respective projects.

## 4. EXTERNAL REVIEW OF THE FRAMEWORK

This Framework shall be reviewed by the Centre for International Climate and Environmental Research – Oslo (CICERO), who will issue a Second Party Opinion.

This Framework and Second Party Opinion will be made public and available at the Company's website's investor section.



## MORE INFORMATION ABOUT AUGA GROUP

- (i) Link to Nasdaq Baltic website info about the [Company](#) and financial reports;
- (ii) Link to the Company's [website](#);
- (iii) [Video](#) links on sustainable operations.

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## SOURCES

- 1 The Intergovernmental Panel on Climate Change at the United Nations report 2019, [https://www.ipcc.ch/site/assets/uploads/2019/08/Edited-SPM\\_Approved\\_Microsite\\_FINAL.pdf](https://www.ipcc.ch/site/assets/uploads/2019/08/Edited-SPM_Approved_Microsite_FINAL.pdf)
- 2 Food and Agriculture Organization of the United Nations report 2014, <http://www.fao.org/3/a-i3671e.pdf>;
- 3 AUGA group's closed-loop organic farming model and its positive impact on the environment is explained in detail in Sustainability report 2017, <http://auga.lt/en/for-auga-investors/sustainability-report/#tabs>;
- 4 AUGA group's Sustainability report 2018, <http://auga.lt/en/for-auga-investors/sustainability-report/>;
- 5 "Life Cycle Assessment of Biofuels in Sweden" Pål Börjesson, Linda Tufvesson & Mikael Lantz 2010;
- 6 Ecofys "Biofuels and food security" Carlo Hamelinck, 2013, "Report on analysis of sustainability performance for organic biogas plants": SUSTAINGAS 2014;
- 7 Food and Agriculture Organization of the United Nations, <http://www.fao.org/faostat/en/#data/GT/visualize>;
- 8 Ellen Macarthur Foundation, Completing the Picture: How the Circular Economy tackles Climate Change, <https://www.ellenmacarthurfoundation.org/publications/completing-the-picture-climate-change>
- 9 ICMA Green Bond Principles, <https://www.icmagroup.org/green-social-and-sustainability-bonds/green-bond-principles-gbp/>;
- 10 Adjusted working capital = Current biological assets + Trade receivables, advance payments and other receivables + Inventory – Trade payables – Other payables and current liabilities.