

## APPENDIX IV POLICY FOR THE MONITORING OF ESG RISKS

This policy is an appendix of Fondaco Lux SA Risk Management Process related to UCITS and Alternative funds.

### OBJECTIVE

With the aim to comply with the EU Regulation 2019/2088 on sustainability-related disclosures in the financial sector ("SFDR"), Fondaco Lux SA (the "Company") has defined this policy in order to identify procedures and method for the assessment, measurement and monitoring of environmental, social and governance ("ESG") characteristics and risks as well as the impact of the sustainable investments decided and implemented for the Funds for which the Company act as Management Company (the "Funds"). The policy includes also data sources, screening criteria for the asset universe and sustainability indicators used to measure the ESG characteristics of the Funds.

This policy is to be considered as an appendix of the Risk Management Process for Fondaco UCITS and Alternative Funds.

This policy takes into consideration the EU Regulation 2019/2088 on SFDR as well as the EU Regulation 2020/852 on the establishment of a framework to facilitate sustainable investment and amending EU Regulation 2019/2088.

Moreover, the Company follows the United Nations Principals of Responsible Investments ("PRI") as in 2020 it become member under the status of Service Provider. Therefore, the Company follows the six principles of responsible investment and is engaged in regular reporting as requested by the United Nations PRI.

The six principles are the following:

Principle 1: We will incorporate ESG issues into investment analysis and decision-making processes.

Principle 2: We will be active owners and incorporate ESG issues into our ownership policies and practices.

Principle 3: We will seek appropriate disclosure on ESG issues by the entities in which we invest.

Principle 4: We will promote acceptance and implementation of the Principles within the investment industry.

Principle 5: We will work together to enhance our effectiveness in implementing the Principles.

Principle 6: We will each report on our activities and progress towards implementing the Principles.

Other values inspiring the Company and its activity are also expressed in the International Conventions issued by universally-recognised organisations, namely:

- respect for human rights, thereby meaning all the fundamental rights and freedoms of each individual as set out in the 1948 United Nations Universal Declaration;
- respect for workers' rights and suitable working conditions, sanctioned by the standards issued by the International Labour Organisation (ILO), including the abolition of child and forced labour and all forms of discrimination;
- respect for the environment, i.e. environmental strategies, prevention and control of pollution and atmospheric emissions, protection of diversity, management of water and waste and increasing energy efficiency;

- respect for corporate governance, including compliance with the main international and local corporate governance codes (the Stewardship Code);
- prevention of all forms of corruption and conflicts of interest and refusal to pay grants, fraud, extortion, money laundering and the illegal financing of political parties;
- banning of controversial weapons; i.e., cluster bombs, landmines and chemical and biological weapons, as envisaged by the Oslo Conventions, the Ottawa Convention, the Chemical Weapons Convention and the Biological Weapons Convention.

## TAXONOMY

Based on the SFDR, there are essentially four types of portfolio that can be managed in relation to the ESG profile:

- Art. 9 SFDR "Dark Green Portfolios": portfolios which has sustainable investments as its objective and therefore the ESG risk is crucial in the portfolio management activity. The investment guidelines, objective and limits reflect this objective.
- Art. 8 SFDR "Medium Green Portfolios»: portfolios which promotes, among other characteristics, environmental or social characteristics, or a combination of those characteristics, provided that the companies in which the investments are made follow good governance practices.
- Art. 6 SFDR "Light Green Portfolios": portfolios in which ESG risk factors are taken into consideration in the portfolio management activity and sustainability risks are integrated in investment management decisions. In this case there may not be precise limitation, exclusion in the investment universe or qualitative and quantitative limits imposed by the prospectus in relation to ESG risks.
- Art. 6 SFDR "No Green Portfolios": portfolios in which ESG and sustainability risks are not relevant and are not taken into consideration in the portfolio management activity and, according to Art 6 of SFDR, a precise explanation of this exclusion is provided.

Based on the above taxonomy both the Investment Manager (being delegated to external asset managers or managed directly by the ManCo) and the ManCo within its compliance and risk management controls, performed its activities in different ways and with different objectives and goals.

In general, sustainability risks or ESG risks are defined by the SFDR as an environmental, social or governance event or condition that, if it occurs, could cause an actual or a potential material negative impact on the value of the investment.

## PORTFOLIO MONITORING OF ESG RATING FOR SECURITIES AND FUNDS

For Dark Green Portfolios, Medium Green Portfolios and Light Green Portfolios, the ManCo performs at least on a monthly basis a monitoring of the ESG rating and scores of the securities and funds included in the portfolios.

The monitoring process is based on different sources and data:

- Regarding securities (both Equities and Bonds), the ManCo utilize ESG profile and data on each issuer produced and diffused by third party dedicated entities which are in charge of analysing for each company issuing stocks and bonds their profile in relation to social (S), environmental (E) and governance (G) aspects as well controversies and special events in the life of the company that may change its ESG profile. The synthetic result is a rating related to Environment, Social and Governance risk as well an overall synthetic indicator for the whole ESG profile. With the availability of such ratings, it is possible to evaluate for each issuer in a single portfolio and globally – aggregating all ratings for each issuer with a weighted average

process – at overall portfolio level, the profile for each of the three components (E, S and G) and at overall ESG level.

It is also possible to mix the ESG risk profile based on the available rating per single issuer with other risk factors such as credit ratings, exposure to countries, sectors, industries, currencies, etc in order to fully integrate the ESG risk monitoring with the monitor of all other risk factors. Finally, the availability of such rating data on a continuous basis each month allows the ManCo to monitor the evolution through time of the ESG profile (eventually broken by E, S and G) of a single issuer and of the overall portfolio in different periods and compare such developments with time weighted or money weighted performance data as well as performance contribution analysis in order to globally assess (once again at single instrument and at aggregate portfolio level) the effect of ESG risks in the portfolio profitability.

- Regarding funds (both traditional and alternative, both closed ended and open ended) there are two methods used to assess the ESG profile, based on the data availability:
  - o Bottom-Up process, which consists in using the portfolio composition on a look-through basis and apply the same methodology used for securities described above to each issuer in the target fund's portfolio. In this way it is possible to assess the ESG profile of the target fund and its evolution through time
  - o Top Down Process, which consists in analysing the target fund's management company and portfolio manager, investment strategy, prospectus limits and characteristics, inclusion of ESG profile in the investment process, use of ESG compliant benchmark, use of white and black lists, procedures, adherence of the fund or the management company to international standards, and other elements to evaluate the overall ESG profile of the fund independently from its actual portfolio composition, which is the result of the elements listed above. In order to facilitate this analysis, the ManCo may also use third party rating and data on single funds or investment managers.

## **MONITORING OF INVESTMENT GUIDELINES**

Based on the investment guidelines indicated in the prospectuses or in the Investment Management Agreement (if any) for each Fund and with particular reference to Dark Green Portfolios and Medium Green Portfolios in which ESG factors are crucial in the portfolio management process, the ManCo may need to monitor the adherence of the portfolio to precise investment limits which are related to ESG aspects. The spectrum of limits in this case may be wide, but some we report here some examples of limits:

- Minimum ESG rating per issuer
- Minimum ESG rating at portfolio level (weighted average)
- Maximum allocation to issuers with no ESG rating
- Use of a pre-approved white list of issuer and maximum allocation to issuer outside the list
- Use of third-party funds with ESG limits in the investment guidelines
- Investments in third party funds with ESG compliant benchmarks
- Investments in third party funds with investment managers associated to UN PRI

The ManCo monitors these ESG related limits and apply to such limits all process and provisions valid for all other investment limits, including breaches process, as described in the policy ex CSSF Circular 02/77 issued by the ManCo.

## **MONITORING OF INVESTMENT MANAGERS**

Regarding Funds for which the Company acts as Management Company and for which portfolio management activity is delegated to an external investment manager via an Investment Management

Agreement and depending on the taxonomy of the Fund, the ManCo may perform additional monitoring on the delegated investment manager, during initial and ongoing due diligence as well as during the continuous oversight. In particular, among others, the following elements may be monitored:

- Adherence of the investment manager to internationally recognized ESG standards such as UN PRI
- Procedure in place at investment manager levels to manage Dark Green Portfolios, Medium Green Portfolios or Light Green Portfolios in terms of experience of the management team, internal organization, procedure, controls in place, availability of data on issuers and other investments
- Reporting including ESG data, factors and analysis to the ManCo
- Effectiveness of investment restriction controls applied to ESG related factors

## **REPORTING ACTIVITY**

Depending on the typology of each Fund according to the taxonomy described and on the investor's characteristics the ManCo is involved in the preparation of different reports which includes ESG factors.

- Executive Report: for each Fund the ManCo already prepared on a monthly basis an Executive Report at the attention of the ManCo Management Committee and Board of Directors as well as SICAVs' Board of Directors (if any) which includes all the details of the Fund as well as the result of the controls implemented at risk management, operational and compliance level. Depending on the Fund typology (which may also be different at Sub-Fund level within each Fund) the executive report includes also the result of the ESG monitoring activity performed based on the criteria described above.
- External Reports: The ManCo has also the possibility to produce ad-hoc reports for investors or other external entities (such as investment committees, advisors, investment managers, etc) regarding the ESG profile of the Funds based on the data of underlying issuers and target funds and according to the monitoring process reported above. The goal of these reporting process may be different: for information and monitoring purposes; to assess the impact of the ESG profile of the investments in the overall performance of the portfolio; to help competent bodies to take informed investment decisions.
- Audited Financial Statements: the management reports included in the audited financial statements of the Funds provides an update on the activities performed by the ManCo and/or the delegated investment managers regarding the ESG principles including in the portfolio management activity and the monitoring and reporting process on ESG risks related to each portfolio.