Alcentra

2023 Stewardship Report

DRIVING SUSTAINABLE CHANGE

Contents

The Financial Reporting Council ('FRC') UK Stewardship Code aims to enhance the long-term returns to shareholders via improvements in the quantity and quality of engagement between companies and investors through integration of Environmental, Social and Governance matters into the investment approach. We have integrated the FRC Stewardship definition within our efforts.

This document outlines our stewardship activities during the reporting period 2023, with a focus on the integration of Environmental, Social and Governance factors into our investment process. We believe that our stewardship activities directly support our objective of delivering strong, long-term investment returns for our clients.

Tim Raeke

Head of European Credit Research

Our approach to stewardship focuses on the responsibility to our clients and wider stakeholders to oversee the creation of long-term sustainable value. Stewardship remains an important part of our investment process and something that we seek to embed in our culture throughout the company. At Alcentra, we have taken great strides in integrating the Stewardship Code principles into our investment decision making. We believe by incorporating sustainability and corporate governance factors into our fundamental analysis, we will be able to create a more complete picture of the risks and opportunities facing issuers today.

Ruth Davis

COO of Global Business Development

We have had a number of successes over the year which highlight Alcentra's commitment to shaping a more sustainable future, including our strong PRI scores, the classification of our second Article 8 fund and a number of thought-leadership pieces on ESG. Going into 2024, we will focus on leadership and collaboration as we continue to evolve our holistic approach to sustainability. It is our continued investment in expertise and people that allows us to enhance our processes and products to be more aligned with responsible investing practices.

Vai Patel

Head of ESG

With evolving investor values, regulatory pressure and global challenges driving interest in ESG, stewardship has become a key pillar of Alcentra's responsible investment strategy. Through engagement, asset managers, like Alcentra, can encourage companies to improve their impact on ESG-related issues, as well as outcomes for all stakeholders. Given the urgency and complexity of the challenges we face as a society, we look to make responsible investment decisions guided by collaboration with clients, companies, policy makers, and stakeholders.

PURPOSE AND GOVERNANCE

PURPOSE AND GOVERNANCE

PRINCIPLE 1

Signatories' **purpose, investment beliefs, strategy and culture** enable stewardship that creates long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society

Business Model and Strategy

From its inception in 2002, Alcentra's primary goal has been to achieve attractive long-term investment returns for clients. We believe that environmental, social and governance ("ESG") considerations are the crux of responsible investment, and we incorporate these factors in investment decisions to achieve our overarching client objectives, whilst endeavouring to contribute to positive change. Alcentra is one of the largest European headquartered credit and private debt managers, with $34 billion of assets under management (AUM) and expertise in Senior Secured Loans, High Yield Bonds, Direct Lending, Structured Credit, Special Situations and Multi-Strategy credit. We employ a disciplined, value-orientated approach to evaluating individual investment and portfolio construction across all of our investment strategies.

We have a highly experienced team of professionals based across the globe who work across asset classes, business sectors and geographies. Our investment team has significant expertise and a deep understanding of corporate debt across our strategies.

AUM by Strategy

51%
Liquid Credit

22%
Structured Credit

23%
Direct Lending

4%
Special Situations

Franklin Resources Inc. became one hundred percent shareholders of Alcentra on 1st November 2022. Post acquisition of Alcentra, by Franklin Templeton, the diversity of the firm – and of senior management – remained a key priority. The senior management team of Alcentra is a diverse group, with female representation in senior roles across the firm, such as: the Co-Head of Direct Lending, the Head of Trading (non-FX), the Head of Structured Credit, the Co-Heads of Product Management, and the COO of Global Business Development. Alcentra's Board of Directors consists of five members, with representation from two independent non-executive directors.

PURPOSE AND GOVERNANCE

Strategy

Our product range has been thoughtfully, and deliberately developed, into a broad, complementary set of investment strategies and products allowing us to work with investors around the world to help them make the most of market opportunities. As a dynamic credit partner, we believe our strategy will, over time, help us make the most of new opportunities as they arise.

Our Strategy Means

We are connected

to the world and our clients and place great importance on keeping in touch with emerging economic trends and major market insights to energise our thinking and keep our business moving forward.

We are solution providers

not product driven, using our unrivalled knowledge to produce smart, credit-led responses and provide client-focused advice with an edge.

We embrace an entrepreneurial spirit

with challenging and fulfilling work in a stimulating environment of learning and expertise to lead the industry by example.

We are invested in

credit and committed to the talent, tech and infrastructure needed to deliver our distinct yet discerning investment solutions that meet a wide range of financial objectives.

Culture

Alcentra's culture is sustained by the following three shared values – **creativity, collaboration, and commitment**. These values are the glue that binds the team together. Within this value system, Alcentra encourages employees to model these beliefs and behaviours. As a company, we are focused on maintaining a culture that values and exemplifies ethical and honest conduct, to protect our investors' capital and to engage with communities to make them a better place.

CREATIVE

- We listen to our partners and team members
- We share our learning and knowledge

COLLABORATIVE

- We are open to new ways of thinking and we assume a solution is possible
- We recognise the importance of diversity in broadening perspectives
- We strive to have fun as a team

COMMITTED

- We act ethically and honestly
- We aspire to deliver outstanding client and career experiences
- We engage with our communities to make them a better place

INVESTMENT BELIEFS

Alcentra's Responsible Investment Policy has been established to outline the principles that guide our investment decisions and stewardship activities. We broadly base our due diligence approach on internationally recognised standards such as the OECD Guidelines for Multinational Enterprises and the United Nations Global Compact. We have been a signatory to the UN Principles for Responsible Investment ("PRI") since 2018.

We believe some corporate activities and behaviours are not compatible with our business values and responsible investment philosophy. Consequently, we have also established ESG exclusion criteria and apply a negative screen to our investments.

As stewards of our clients' capital, we manage our investments in a responsible manner. Alcentra believes that responsibly managed companies are better placed to achieve sustainable competitive advantage and provide strong long-term growth. The consideration of sustainability risk forms an important part of our due diligence process. When assessing the sustainability risk associated with our investments, we assess the potential risk that their value could be materially negatively impacted by environmental, social or governance ("ESG") factors. This analysis requires an understanding of companies' impact on the environment and society. We believe this approach allows us to make better investment decisions.

We have outlined on the next page our priorities across governance, climate change, environment and social matters when assessing and engaging with companies. Our teams collaborate with clients to determine the allocation, management, and oversight of capital.

GOVERNANCE

As a provider of capital to companies, we have a vested interest in ensuring the issuers in our portfolio are able to service their credit obligations in a timely manner and that they maintain a stable credit risk profile. Although we do not have the same ownership rights as shareholders, we share common interests. We believe good corporate governance is fundamental to ensure our client's interests as creditors are protected. An effective board is also essential to oversee the adequate management of environmental and social risks. The board sets the tone for the organisation and influences firms' behaviour on environmental and social matters. As part of our governance due diligence, we take into consideration various factors, including but not limited to i) board structure and composition; ii) remuneration practices; iii) anti-corruption practices; iv) transparency and ethical conduct; and v) oversight of sustainability risks.

SOCIAL

Companies may be exposed to social-related risks through their operations, supply chains and business relationships. As part of our due diligence, we may assess factors related to how companies manage human rights, human capital, the impact of companies' products and services on society, as well as how issuers manage relationships with stakeholders. Social factors may pose reputational, regulatory, and legal risks and costs to companies and, through our rigorous assessment, we aim to identify and mitigate these.

ENVIRONMENT

Environmental risks relate to the quality and functioning of the natural environment and natural systems and the impact of a company's operations on the environment. Companies could face increased compliance costs due to stricter regulatory requirements, fines, litigation risks, reputational risks, and changes in consumer preferences. These risks could impact on a company's ability to service their debt. At Alcentra, we assess issuers' exposure to material environmental issues, which could include water management, waste management, land use change, biodiversity and airborne pollution. Our starting point is to identify the most material environmental risks relevant to the issuer's sector. We seek to understand the company's internal policies to address environmental issues, as well as the impact their operations may have on the environment.

CLIMATE CHANGE

Alcentra believes the economic impacts of climate change will be felt across industries and markets; however, we recognise the magnitude and timing of these impacts remain uncertain. Alcentra supports the goals of the Paris Agreement to limit global warming to 1.5 degrees Celsius. An orderly transition in line with the Paris Agreement goals is important to reduce climate-related risks for the companies we invest in. We became an official supporter of the Task Force on Climate-related Financial Disclosures ("TCFD") in 2020. We believe the TCFD recommendations provide a useful framework for companies to articulate how they identify, mitigate, and manage transition and physical climate risks. Our principles for assessing and engaging with companies on climate change matters are broadly based on the TCFD recommendations. We assess companies' preparedness to manage the climate transition, through incorporation of our internal climate tool and we enquire about company climate targets in our engagements. Please refer to Principle 4 for more details on our approach to TCFD.

Actions We Have Taken to Enable Effective Stewardship

Our strategy, culture and investment beliefs provide the foundation for all interactions; they align our values, set our expectations and improve decision making, ultimately enabling us to effectively engage with stakeholders. Over the period, our investment beliefs have guided our stewardship activities and shaped our interactions with the market. The below initiatives demonstrate how our investment beliefs on the importance of addressing climate change and the need to protect the environment and human rights have led to proactive engagement and alterations in the characteristics of our funds.

Initiative: All Strategies Climate Guides

We have taken a proactive role in providing guidance to borrowers on their climate transition strategies and roadmaps to net-zero, offering support across the different stages of their carbon reduction planning. We authored a guide on how companies can measure their carbon footprints and set reduction targets which was circulated to all borrowers across our Liquid Credit, Direct Lending and Special Situations investment strategies. We also created a separate guide to support CLO managers in measuring the carbon footprint of their investment portfolios for our Structured Credit investment strategy, with the view to enhance climate data disclosure across the industry. Further details on our CLO Manager Guide can be found in Principle 4.

Initiative: Direct lending and Liquid Credit EU SFDR Article 8 Funds to Promote Environmental and Social Characteristics

One of the primary ways that we have taken action to promote our belief in the importance of making environmentally and socially sound investments is through defining these investment beliefs as the key sustainable characteristics of our Article 8 designated funds under the EU Sustainable Financial Disclosure Regime ("EU SFDR") regulation. Over the period, we announced the conversion of our second Article 8 fund under the EU SFDR regulation, highlighting our continued commitment to responsible investing and stewardship. Both Article 8 funds aim to promote environmental and social characteristics through the engagement with and increased awareness of greenhouse gas emissions and circular economy practices, as well as the engagement with and increased awareness of human rights, workplace equality, and workplace diversity. Our ESG processes, which underpin how the funds aim to promote environmental and social characteristics, have been integrated into our responsible investment approach for several years now. As part of the Article 8 classification, those ESG processes will be supported by more detailed disclosure on how the funds embed sustainability into the investment decisions to achieve the best possible risk-adjusted returns for our clients.

Key Outcomes & Effectiveness

Our investment beliefs have a direct and impactful influence over our investment decisions. At the most rudimentary level, our investment beliefs relating to environmental, social and governance factors inform which deals we finance and which we do not. For example, our Direct Lending strategy declined 30 deals, in part, due to ESG considerations during the course of 2023. Beyond our defined exclusions list, we use our investment beliefs to determine which borrowers align to our corporate values.

We believe the establishment of our responsible investment principles, ESG assessment framework and stewardship activities have played an important role in protecting and enhancing the value of our clients' investments and assisting in the delivery of attractive investment returns. Alcentra strives to work collaboratively with clients and beneficiaries, in an effort to continually do what is in their best interest – and to be a responsible steward of capital. We are continually working to further integrate our ESG principles across our firm's culture and investment strategies.

2 PRINCIPLE

Signatories' **governance, resources and incentives** support stewardship

Governance of ESG Risk

Overall responsibility for ESG matters falls under the Alcentra Limited Board of Directors ("the Board of Directors"). The establishment of Alcentra's ESG Committee in 2021 denoted a focus on responsibility for the approval of ESG-related policies and procedures. The ESG Committee monitors issuers with significant exposure to ESG risks and oversees our ethical exclusions.

Additional responsibilities include the:

i

Approval of Alcentra's responsible investment policies and procedures

ii

Approval of financial products with responsible investment credentials; and

iii

Monitoring of relevant regulatory developments

The ESG Committee is comprised of senior members from the investment, business development, product management, responsible investment and risk and compliance departments to ensure relevant and diverse representation from all areas of the firm. The ESG Committee meets at least on a quarterly basis. Alcentra's Responsible Investment policy is approved by the ESG Committee and presented to the Board of Directors. The policy is reviewed on an annual basis.

The Responsible Investment Team

Alentra's dedicated Responsible Investment team, established in 2021, works to further develop the firm's responsible investment strategy, policies and procedures. The Responsible Investment team is made up of the Head of Responsible Investing, the Head of ESG and an ESG Associate. The Head of Responsible Investing is also a member of Alcentra's Liquid Credit Investment Committee and co-chairs the ESG Committee. Our Responsible Investment team is fully integrated into our investment team. The scope of work is broad and includes supporting analysts and portfolio managers in:

- i **Conducting company and sector research**
- ii **Making investment decisions**
- iii **Monitoring credits**
- iv **Providing constructive challenge; and**
- v **Engaging with companies on ESG matters**

In addition, the Responsible Investment team monitors regulatory developments relevant to Alcentra and the companies we invest in.

The Responsible Investment team works across the firm to support the execution of Alcentra's responsible investment strategy, including the integration of ESG factors into investment decisions.

The Head of ESG is responsible for ensuring our investment process incorporates the assessment of ESG risks and for further enhancing the firm's ESG capabilities. The latter involves conducting training and delivering information sessions for the firm on relevant policy, market and technology developments.

Additionally, as our internal processes evolve, the Responsible Investment team provides training to the investment team, to ensure our tools are used appropriately. Training is typically held in person and delivered quarterly.

Notable training sessions over 2023 included upskilling the Liquid Credit Investment team following the conversion of our flagship European Loan Fund to EU SFDR Article 8 status. The training covered the ESG binding elements of the fund, the reporting requirements as well as what we will need from the analysts going forward. Training was also delivered to all four investment teams to cover the TCFD reporting requirement and the engagement needed to collate all appropriate climate data.

Enhancing the Responsible Investment Team over 2023 and into 2024

Over the last 12 months, Alcentra has enhanced the Responsible Investment team through both resourcing and improving the way in which it operates. In August 2023, the team hired a new ESG associate. The role of the associate is strategy-agnostic and primarily focuses on enhancing the level of ESG integration into all credit processes, as well as leading on investor related ESG requests. The team will be expanded further in 2024, with the addition of another ESG associate, to manage the growing scope of work.

Over the course of 2024, we intend to integrate all ESG data including engagements and stewardship activity, as well as live portfolio data, into one aggregated ESG database. This will allow us to analyse engagement statistics across funds and over time and will allow for more enhanced tracking of the effectiveness and outcomes of engagements.

Resourcing and Stewardship

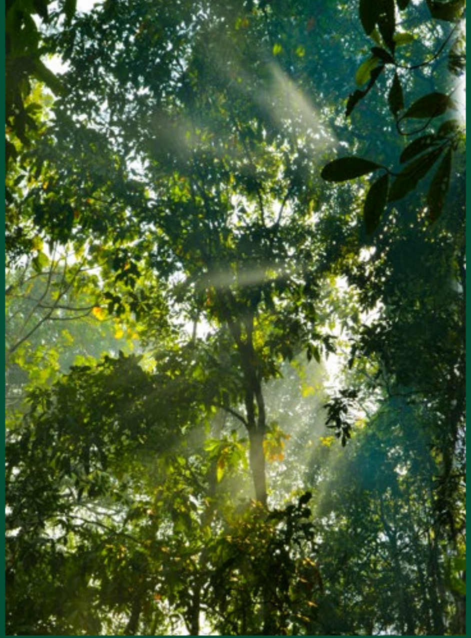
The primary responsibility for conducting stewardship activity sits with our investment professionals. This is because our investment analysts have the most in-depth knowledge on the material risks affecting issuers and the best understanding of the unique risk profiles of each company. Our Responsible Investment team support on engagements and typically step in when dialogue turns to more nuanced topics such as ESG regulation or climate disclosures.

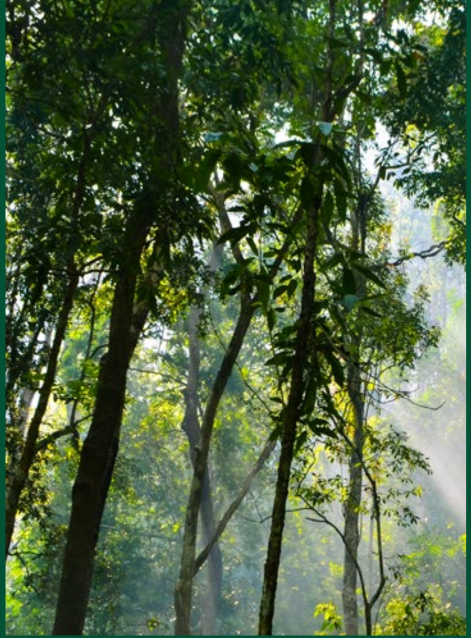
The investment teams are well-resourced, allowing for a favourable issuer coverage ratio. We employ high calibre professionals with strong academic credentials and experience, who can assess the holistic risk profile of an investment, including ESG risk, as well as effectively engaging with our stakeholders in order to assess and manage ESG considerations.

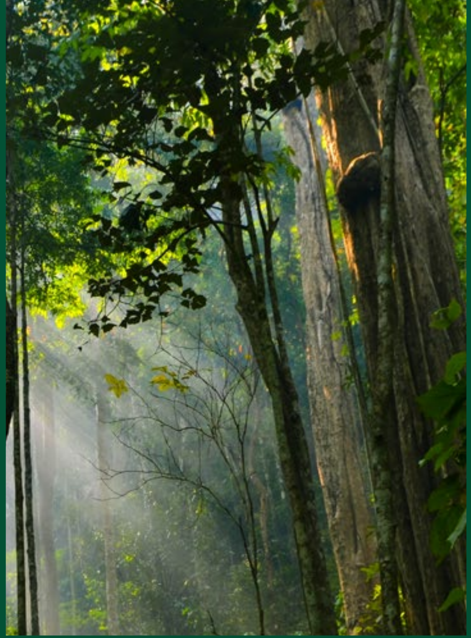
Linking ESG To Remuneration

Alcentra recognises the importance of ESG integration to support our mission of creating sustainable, long-term value and returns for our clients. The Firm's Remuneration Policy promotes non-excessive risk taking by its employees, including its investment professionals. ESG-related activities, including company engagements, are a component of the investment team's individual variable remuneration.

Key Outcomes & Effectiveness







Alcentra's chosen governance structures have been effective in monitoring ESG risk. Between our Head of ESG, Head of Responsible Investment, ESG Committee and Board oversight, we believe we have the appropriate layers of governance in place to effectively manage risk. In addition, the clearly defined responsibilities set out for our Responsible Investment team and ESG Committee help ensure accountability and effective integration of ESG across the business.

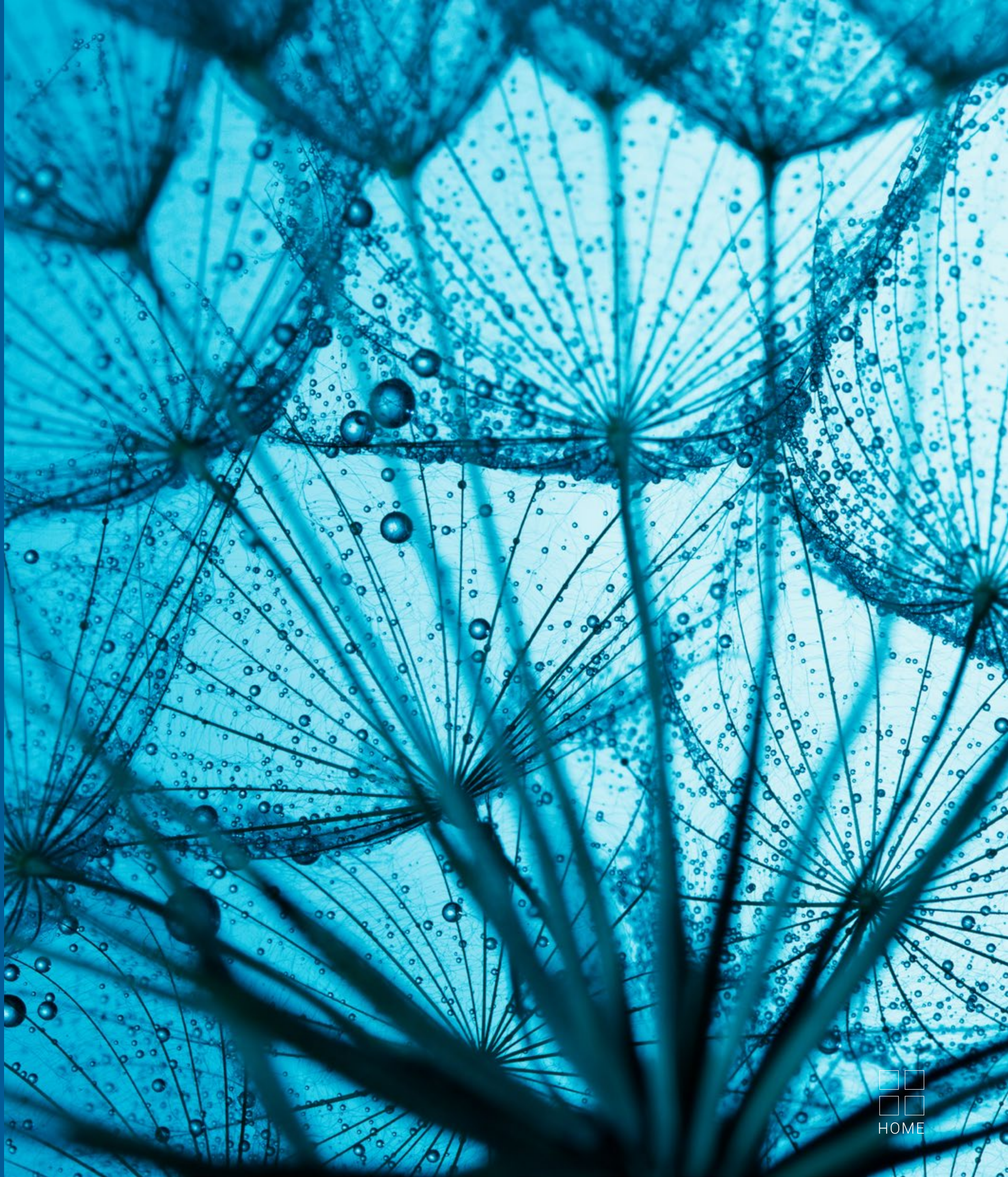
Alcentra's ESG Committee and Responsible Investment team provide the firm with a solid foundation to implement its responsible investment strategy. We will continue to evolve and enhance the ESG capabilities of the organisation across our different investment strategies through ESG training.

The Remuneration and Nomination Committee is tasked with reviewing the structure, size, and composition of the Board (including skills, experience, and diversity). The Committee also makes recommendations for Board appointments and ensures plans are in place for the orderly succession of the Board and Senior Management positions. Ensuring the effectiveness of the Board and appropriate appointment is essential for maintaining proper oversight of risks, which include all ESG matters.

PURPOSE AND GOVERNANCE

3 PRINCIPLE

Signatories manage **conflicts of interest** to put the best interests of clients and beneficiaries first



Managing Conflicts of Interest

Alcentra is committed to ensuring that the highest levels of integrity and ethics are maintained across operations. We are required by global regulators to identify conflicts of interest between ourselves and our clients and between clients. We work to prevent and manage potential conflicts of interest, record conflicts of interest and maintain a Conflict of Interest policy. The policy is managed and approved by our Head of Compliance and Risk. Our Conflicts of Interest Policy is reviewed every other year by our Compliance team. No material changes were made to the policy in 2023.

As part of the policy, staff are required to report any potential conflicts to the Compliance team for assessment. Alcentra maintains a Conflict of Interest Register to capture and measure potential conflicts. All staff are required to follow policies and procedures related to handling confidential and inside information and conflicts of interest. Staff are required to complete mandatory training upon induction to the company and may also be required to conduct annual or more frequent reviews. Some of our key policies and training courses for employees, are outlined to the right.

Firm and Group Policies

- Handling of Complaints
- Error Reporting
- Employee Code of Ethics
- Order Execution Policy
- Aggregation / Allocation Policy
- Inside Information, Firewalls and Market Sounding Policies
- Anti-Corruption Policy
- Personal Securities Trading Policy
- Gifts and Entertainment Policies / Outside Interests
- Proxy Voting Policy
- Conflict of Interest Policy

Training

- Culture of Compliance: The Franklin Templeton Code of Ethics and Business Conduct
- The Franklin Resources Anti-Corruption Policy
- Communication and Information Security at Franklin Templeton
- Privacy and Data Protection Essentials
- Respect in the Workplace
- Anti-Money Laundering at Franklin Templeton
- Annual U.K. Regulatory Compliance Training (U.K. only)
- Personal Investments and Insider Trading Policy
- Annual Compliance Meeting / Firm Element
- HIPAA Security Policy

Mitigating conflicts of interest Alcentra recognises there may be situations that create conflict of interests. In an effort to ensure that any potential risks are mitigated, Alcentra creates a culture of good governance with appropriate policies and processes in place to identify and mitigate such risks. It is of utmost importance that our employees abide by the Alcentra policies and procedures.

We describe some of the identified potential conflict of interests in the following table:

Example	Conflict situation	How we manage the conflict
External Directorship	Where members of staff hold external directorship functions, there may be certain situations that will present a conflict between services provided to the company in which staff hold such positions, and duty of care to one or more clients.	Investment managers have a fiduciary duty to manage the client's best interests. In addition, we do not retain any remuneration. Where the underlying company pays a director, the fee goes to the underlying funds. Therefore, we are incentivised to work for our client, not the issuer or borrower. All Board directorships must be approved by the firm's Compliance Team, prior to acceptance.
Cross Trades	Alcentra funds from time to time engage in intra-fund cross trades; these need to demonstrably be to the interest of all parties.	The Alcentra Order Execution Policy alongside desk procedures addresses how cross trades are to be dealt with. Regular management information is provided to the Alcentra Risk Committee.
Allocation of Trades	A conflict may arise if the aggregation of client orders does not include all eligible accounts, or if the post trade allocation of a partial fill does not evenly distribute the scaled back amounts fairly to the participating accounts.	The Firm has in place an Aggregation and Allocation Policy which provides the high-level principles that the firm employs, including the default methodology of pro rata for scale backs. Each strategy has an agreed allocation methodology. Quarterly Allocation Surveillance results are provided to Alcentra Risk Committee.

Voting-Related Conflicts of Interest

As a credit manager, proxy voting is not material within the context of our activities. The number of occasions when Alcentra will be engaged in proxy voting will be limited. However, Alcentra's Compliance team works to ensure that all potential voting conflicts of interest are mitigated through the following checkpoints:

Alcentra will retain the contractual right not to vote when it perceives potential conflicts between the services offered to the company and the duty of care to clients.

When unsure if voting will create a conflict for Alcentra clients, this must be discussed with Risk and Compliance.

In cases where there are identified conflicts, including but not limited to voting, this should be escalated to Risk and Compliance.

Alcentra's Compliance Department should be informed of situations where the teams have abstained from voting.

4 PRINCIPLE

Signatories Identify and Respond to Market-Wide and Systemic Risks to **Promote a Well-Functioning Financial System**

HOME

In alignment with our purpose, we believe it is essential to identify and work to mitigate systemic risks in order to support a more equitable, sustainable and well-functioning financial system. Alcentra actively works to improve market standards and promotes transparency and ESG data availability. We do this individually, as well as in close collaboration with other stakeholders, including peer investors; for example, through our participation in various working groups or committees in PRI and European Leverage Finance Association ("ELFA"). Please refer to Principle 10 for more detail on our collaboration with ELFA. We also respond to consultations from standard setters to voice our views on matters that are relevant to our business and the companies we invest in. Systemic risks have the potential to impact on the return of our investments.

Climate Change

Climate change is a systemic risk for most sectors we invest in. It presents risks for credit portfolios, although the magnitude and timing of the consequences are uncertain. Climate change is creating complex and interconnected risks that are challenging to measure and manage. Stewardship is a central tool we use to address climate risks. We believe standardised corporate climate disclosures aid us in making better informed investment decisions and help ensure a level playing field.

We seek to enter into dialogue with companies in sectors highly exposed to climate risks to better understand the nature of their exposure, as well as the management of climate risks. Specifically, we seek to understand how companies' business models align with the goals of the Paris Agreement and firms' transition plans for reaching net zero greenhouse gas emissions ("GHG") in 2050. If companies held within our portfolio do not have any transition plans in place, this provides us with an opportunity to engage and collaborate, in an effort to assist in setting targets to reduce emissions in alignment with the Paris Agreement.

Throughout 2023, we accelerated efforts to capture issuers climate data and analyse the climate impacts of our investments through the use of our proprietary Climate Risk tool. Whilst we have been engaging with companies on climate change issues for several years, we intensified our dialogue to help improve the availability of climate data in the sub-investment grade market across 2023. Below are some examples of how we are proactively engaging with our borrowers and the market to address the threat of climate change.

Initiative: All Strategies

Our Approach to Task Force on Climate-related Financial Disclosures

Alcentra became an official supporter of the Financial Stability Board's Task Force on Climate-related Financial Disclosures ("TCFD") in 2020. As Alcentra is deemed to be a Phase Two firm under the FCA requirements, we will be producing its inaugural TCFD report in June 2024.

To enable this:

Over the last 12-months, we have stepped up the level of engagements in preparedness for TCFD reporting, namely:

- Pushed for increased disclosure of climate metrics by borrowers
- Pushed borrowers to set emissions reductions targets (including assessing whether borrowers have set credible transition plans)
- Pushed for integration of climate into wider ESG policy and strategy

Furthermore, as part of TCFD reporting, we are aiming to combine portfolio carbon emissions data with forward-looking metrics – such as issuers' climate targets, temperature alignment, and scenario analysis to better understand the impact of climate change on our portfolio.

Tangibly, as part of this, we will continue to enquire about companies' climate targets in our engagements; and will look to:

- Assess metrics and carry out scenario analysis (1.5°C to 4°C | 2025 to 2050);
- Understand both physical and transition risks faced by the firm and our portfolio companies; and
- Identify climate-related risks and opportunities for our firm and for our investments as part of our climate strategy

Reporting:

- Our TCFD report (both the entity-level and the product-level) will provide detailed scenario analysis including Climate Value at Risk ("CVAR") and Implied Temperature Risk ("ITR") metrics

Additionally, in 2024, we will be onboarding third-party data providers to augment our research and review of relevant macro-considerations and systemic climate risks through a holistic viewpoint.

Initiative: Direct Lending

Increased Engagement on Climate Data and Outcomes

Over the period, climate change represented the highest topic of ESG engagement with our Direct Lending borrowers. We interacted with companies to discuss critical themes including, the importance of disclosure, how to baseline emissions, and how climate targets could be integrated into sustainability linked lending facilities. Through our active engagement with portfolio companies, we have seen a significant year-on-year improvement in the number of companies disclosing quantitative ESG data, particularly around climate metrics and carbon emissions. This highlights the value that data brings for borrowers and its ability to drive financing opportunities, enhance decision-making, and foster long-term value creation. We have seen the largest improvements in data across the following indicators:

Indicator	Percentage of portfolios companies that disclosed data in 2022	Percentage of portfolios companies that disclosed data in 2023
Scope 1	19%	64%
Scope 2	21%	63%
Scope 3	17%	51%
Energy consumed	35%	71%
Renewable energy	15%	45%

Highest ESG Engagement Topics

20%
Environment
Climate change

10%
Social
Human capital management
(e.g. inclusion and diversity, employee terms, safety)

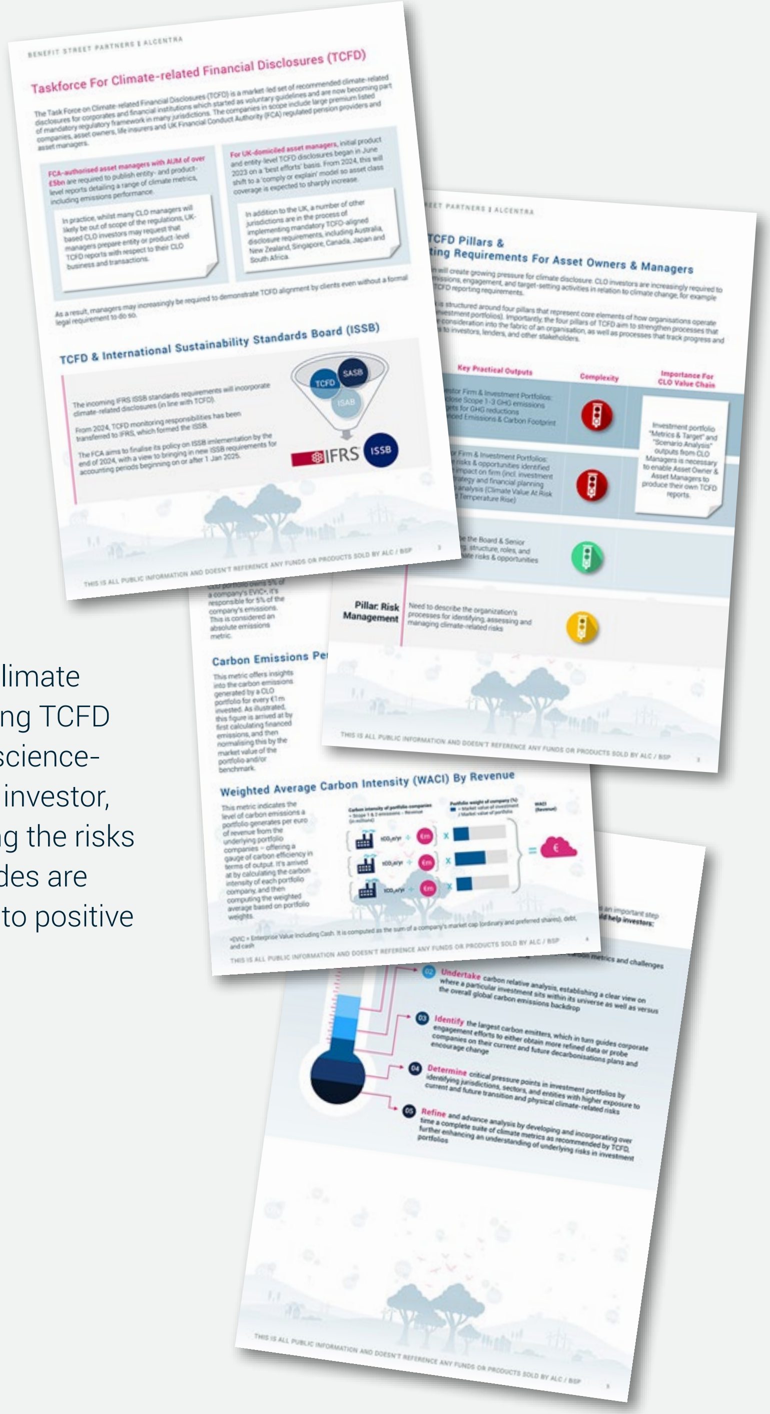
11%
Strategy, Financial and Reporting
Risk management
(e.g. operational risks, cyber/information security, product risks)

10%
Environment
Pollution, Waste

* The remaining Investment Consultants Sustainability Working Group ("ICSWG") topics represented 49%.

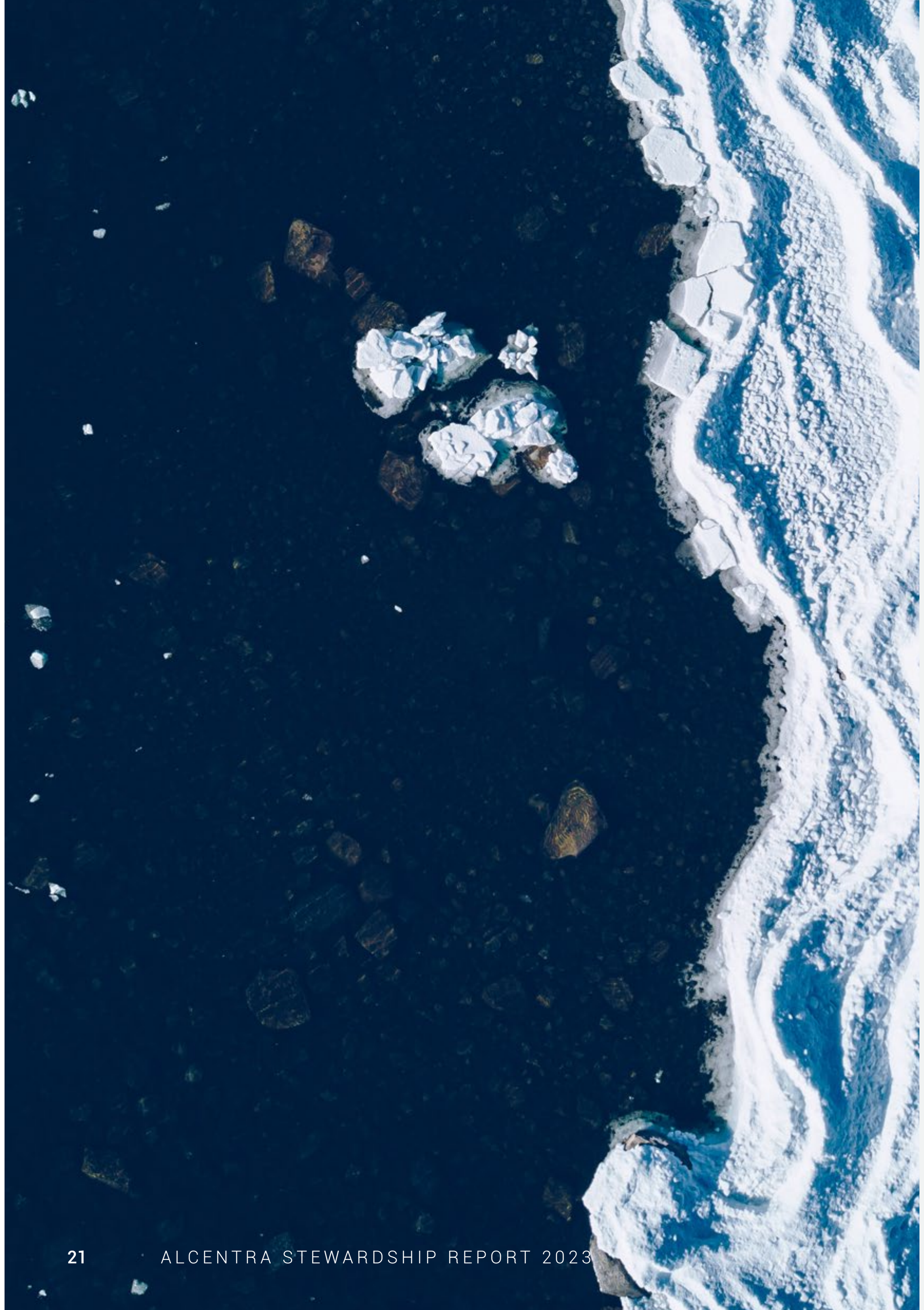
Initiative: Structured Credit
Climate Disclosure Thought Leadership

Driven by intensifying regulatory demand, CLO managers are under increasing pressure to properly measure and disclose the carbon footprints of their investment portfolios. We understand that the importance of addressing climate risks goes beyond just regulatory reporting, it impacts all participants in the investment value chain, across asset owners, managers and borrowers. To help CLO managers understand their climate data reporting requirements and reduce their carbon footprints, our Responsible Investment team and Structured Credit team collaborated to produce a climate guide. This provides a step-by-step resource for understanding TCFD regulations, calculating and reducing emissions and setting science-based emissions targets for their portfolio companies. As an investor, we believe we have a responsibility to play a role in addressing the risks that affect financial markets and our society. Our climate guides are just one initiative we have launched to proactively contribute to positive change and best practice.



Initiative: Structured Credit
Engagement on Climate Data with CLO Managers

Structured Credit conducts a semi-annual carbon mapping exercise, collecting Scope 1,2 and 3 emissions data from CLO issuers on the underlying collateral. In 2023, we engaged with over 40 managers across the EU market to assist us with estimating the carbon emissions for over 100 obligors not directly covered by Alcentra. We collected data from multiple managers per issuer to ensure accuracy and supplemented this with additional public data sources to provide industry average emissions intensity metrics. We then endeavoured to educate managers who were not actively collecting issuers' emissions data on a regular basis. We have emphasised to managers that it is not only important for them to be collecting and storing this data but also to be actively pushing underlying companies to publicly report these metrics. This downstream push is important in making companies focus on their emission outputs and setting targets.



Collective Participation

We also engage in collective action through our participation in industry groups to signal to policymakers the measures we consider are necessary to achieve an orderly climate transition. Alcentra signed the 2021 Global Investor Statement to Governments on the Climate Crisis. Alongside an additional 587 investors, representing over USD $46 trillion in assets (around 40% of the world's AUM), we called on governments to act on the climate crisis. Through this collaboration, we acknowledge that governments' ability to deliver on their commitments will depend on private capital assistance in order to mobilise finance at the scale that is needed to achieve the Paris Agreement's goals.

We closely monitor the development of industry standards that help shape market practices. We will continue to engage with standard setters to express our views on relevant regulatory proposals. During 2023, we have participated in several industry working groups to support the development of frameworks that can help financial institutions assess climate impacts, for example through our work with the Loan Market Association ("LMA") and ELFA. We understand that as investors, we have the opportunity to constructively address and respond to market-wide and systemic risks. We have benefited from collaborations with peer investors to improve market standards and reduce systemic risks, such as climate change. However, we recognise there are opportunities to further collaborate with others in the global investment community, so we will continue to explore and prioritise initiatives and working groups that seek to address systemic risks relevant to the firm.

Risk Management Framework

Alcentra operates a strategy that incorporates 'three lines of defence' in the management of risk. Key roles and responsibilities are defined within the firm's Corporate Risk Management policy. The Board of Directors of Alcentra has overall responsibility for the Corporate Risk Management framework and is supported in the effective deployment of the Framework by its delegated Committees.

There are four key elements to the Operational Risk Management Framework:

Risk Identification	i	Periodic risk assessments; analysis of risk events; scenario analysis; financial analysis; and understanding market practice
Risk Assessment & Measurement	ii	Qualitative and quantitative measurement of risk; and determination of risk capital
Risk Management & Mitigation	iii	Implementing control and process enhancements in response to elements I and II
Monitoring & Reporting	iv	Escalation and oversight, including tracking the reporting of Key Risk Indicators against Board-approved risk appetite

We continuously evolve and adapt our risk management strategies, as and when necessary. The three lines of defence strategy can be summarized, as follows:

First line of defence	i	Business departments responsible for performing activities including the design, implementation and execution of tasks and associated controls
Second line of defence	ii	Compliance and Operational Risk – responsible for advising on and testing the effectiveness of implemented controls
Third line of defence	iii	Internal Audit – report to the Board on the Firm's overall control environment

All members of staff must adhere to the Operational Risk Management Framework in the performance of their roles and responsibilities – and to identify and escalate – where any control gaps are identified. If there are any errors of process detected, employees must immediately report this to Operational Risk.

Alcentra's Compliance team actively review forthcoming regulations and advise the business on any changes that could influence the firm. For example, the team has been closely following the various proposals under the EU SFDR and the UK FCA's rules on TCFD disclosure and UK FCA's Sustainable Disclosures Regime ("SDR") for asset managers. Our Head of EMEA Compliance Advisory, who is a member of the ESG Committee, provides regular updates on relevant regulatory developments to the Committee.

Market Risk Case Study:

Reflections on the Effectiveness of Risk Management System

Global markets saw increased volatility in 2023 and broader fears of contagion following the collapse of Silicon Valley Bank (SVB) and Credit Suisse (CS) in the first quarter of the year.

Alcentra investment teams undertook a thorough analysis of all funds to understand the exposure to CS and SVB and determine the risk to capital.

- From our analysis, at the firm level Alcentra was able to confirm we do not use Credit Suisse for any finance facilities. At the fund level, none of our funds deposit cash with the affected banks.

To control potential risk, when Credit Suisse enacted their operational restructuring late last year, our Liquid Credit team took the prudent decision to reduce trading activity with their trading desks.

Throughout the following months, the teams continued to monitor the situation and review our assets to identify any further liquidity or credit issues.

5 PRINCIPLE

Signatories **Review Their Policies, Assure Their Processes** and Assess the Effectiveness of Their Activities

Review And Assurance of Policy & Processes

Alcentra has established a Responsible Investment policy to help guide our investment decisions and stewardship activities. We review our policies and procedures on an annual basis and conduct audits to ensure that they are adequately implemented and effective.

The ESG Committee meets at a minimum on a quarterly basis to review progress in the implementation of the firm's responsible investment strategy. The ESG Committee is advised on investments in issuers that are deemed to pose high ESG risks, which have been discussed at the Investment Committee.

The ESG Committee reviews and approves Alcentra's Responsible Investment policy. Amendments to the policy are proposed by the Responsible Investment team, which are presented to the ESG Committee for approval. The policy was last updated in September 2023.
As part of the policy review, we made a number of revisions and improvements, the outcomes of which are as follows:

Exclusions Policy

We inserted additional language that caveats the Structured Credit team's work to include restrictive language in their CLO documentation.

"The Structured Credit team works with the CLO Managers they invest in, at the point of appointment, for primary deals, to request wording in the CLO documentation to apply separate restrictions and exclusions, wherever possible. The wording is utilised to prevent CLO Managers from buying assets with exposure to certain industries – as further described in the Structured Credit section below. Most Managers are quite constructive in including this language in their CLO documentation."

Conflicts of Interest

We added a new sub-section to include Conflicts of Interest, as well as a Voting-Related Conflicts of Interest sub-section.

"We work to prevent and manage potential conflicts of interest, record conflicts of interest and maintain a Conflicts of Interest policy. The policy is managed and approved by our Head of Compliance and Risk. Our Conflicts of Interest Policy is reviewed every other year by our Compliance team.

• • •

As a credit manager, proxy voting is not material within the context of our activities. The number of occasions when Alcentra will be engaged in proxy voting will be limited. However, where votes are cast on behalf of clients these are done in line with the best interests of the underlying clients."

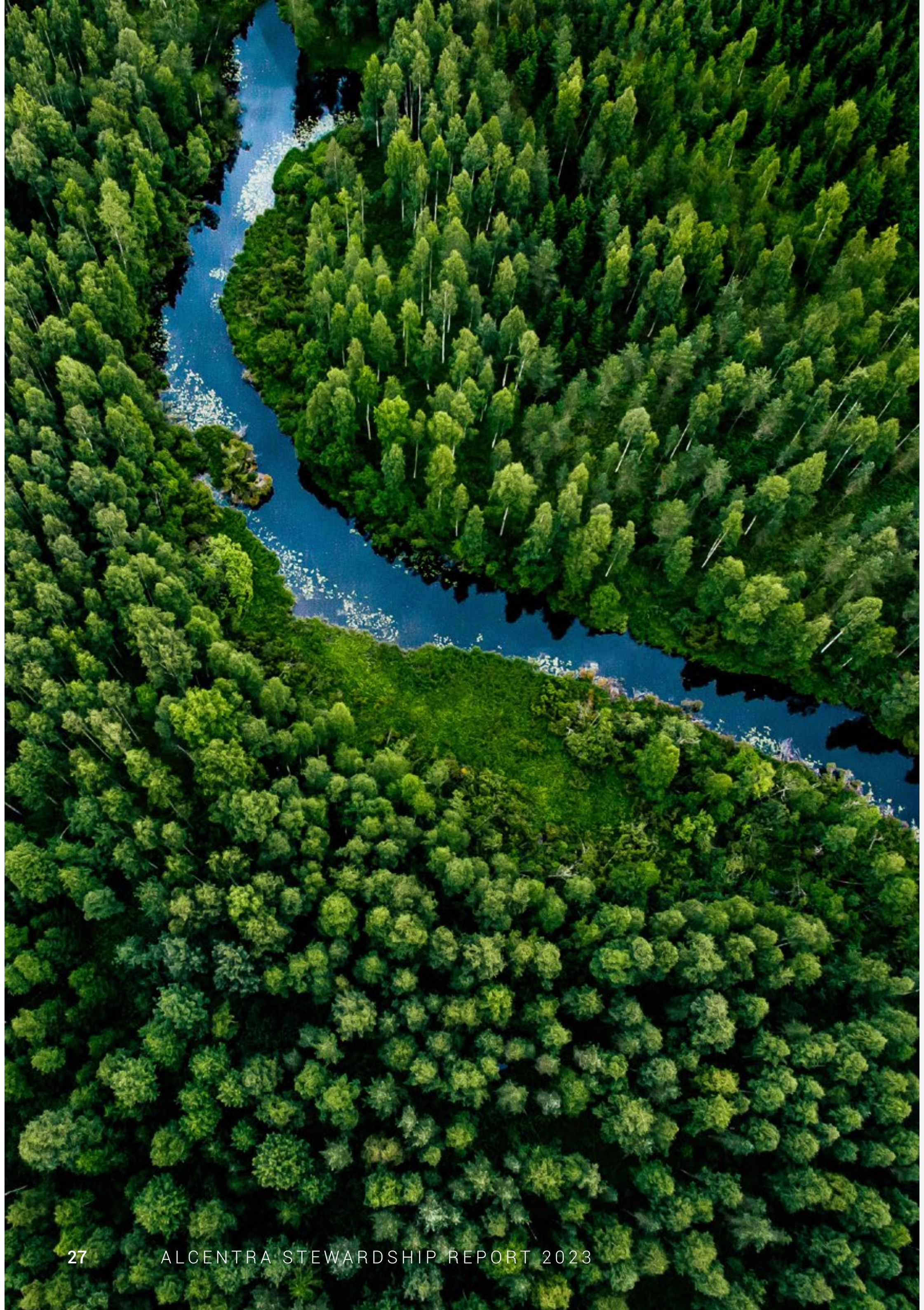
Active Stewardship

Additional information was provided on engagement processes; alongside the UN PRI and FRC Stewardship Reporting initiatives.

"As part of our regular company dialogue, analysts engage with issuers on ESG matters on a regular basis. Engagement may be more frequent with issuers exposed to higher ESG risks or where company-specific or macro risks are developing. Our approach to engagement is explained in more detail further below.

• • •

As a signatory to the UN Principles for Responsible Investment (PRI), we submit an annual report summarising our main responsible investment activities. Additionally, we are a signatory to the Financial Reporting Council's UK Stewardship Code initiative, which further enhances our commitment to adherence to the highest standards of engagement and stewardship reporting."



The ESG Committee is responsible for approving any updates to Alcentra's ESG risk framework, including the tools and data sources used to assess issuers including:

- i **Materiality matrix**
- ii **ESG Checklist; and**
- iii **Climate Risk tool**

The tools were presented and approved by the ESG Committee before their implementation.

Alcentra has adopted criteria for excluding issuers from our investment universe. The exclusion criteria are outlined in our Responsible Investment policy. In 2021, the scope of our exclusions was broadened, and in 2023 we amended our ESG integration tools to tighten our internal controls on exclusions. We conduct primary and secondary research of companies' activities to ensure compliance with the policy.

There is close collaboration between the Responsible Investment team and our different investment teams so that ESG factors are incorporated into our investment processes and engagement is reported in a fair, balanced and understandable way. Alcentra maintains an ESG engagement tracker log to capture and measure the effectiveness of our engagement activities. The engagement log is relied upon to track the progress of our dialogues and to ensure reporting of engagement reflects what happened in an accurate and fair manner. As primarily private-market investors we do not disclose names of companies when reporting on engagement in order to preserve anonymity.

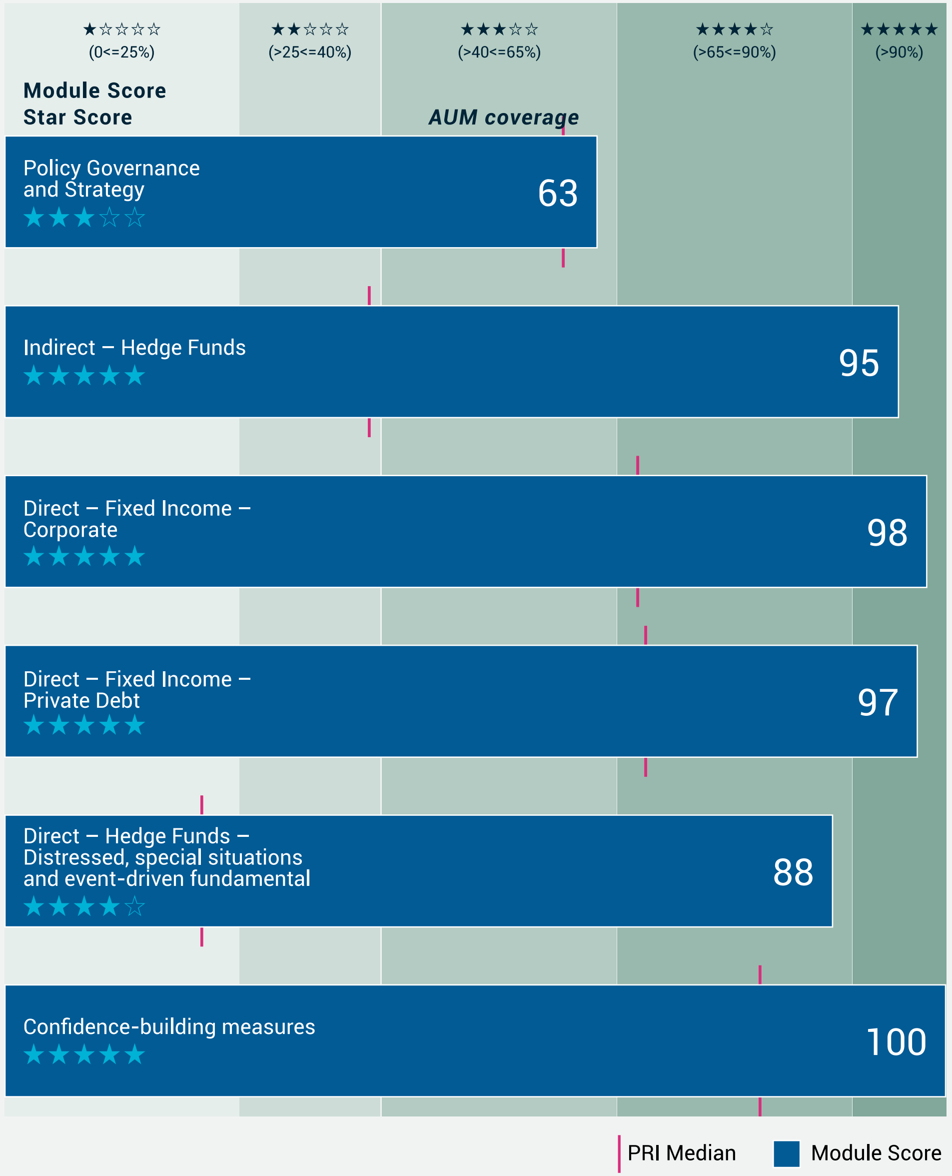
Assurance

All public reporting on Alcentra's ESG integration and stewardship activities, including the PRI Assessment and Stewardship Code are reviewed and signed off by the Head of Responsible Investment, Head of ESG, the Head of Compliance and Risk, our Chief Operating Officer of Business Development and investment teams' Portfolio Managers. The multi-layered approach to approval limits the possibility for engagement activity to be reported on in an unfair or unbalanced manner.

UN Principles of Responsible Investment ("UN PRI")

As a signatory to the UN PRI, we submit an annual report summarising our main responsible investment activities. The external assessment of our approach to responsible investment helps inform our sustainability and stewardship practices and disclosures. As part of the assessment of our 2023 UN PRI report, we received the following scores, please see graph to the right.

Each strategy's score is considerably ahead of the UN PRI median scores for comparable firms. Our Policy, Governance and Strategy score is also above the median, providing us with external assurance that we are acting in accordance with best practice. We deem our assessment by the UN PRI as an appropriate approach to gaining assurance over our Responsible Investing policy and the integration of ESG into our investment process as the institution reviews comparable firms and is therefore able to benchmark our approach against our peers.



INVESTMENT APPROACH

HOME

6 PRINCIPLE

Signatories Take Account of **Client and Beneficiary Needs** and Communicate the Activities and Outcomes of Their Stewardship and Investment to Them

Client And Beneficiary Needs

Alcentra is an alternative asset manager with an institutional client base. Our clients are the focal point of the business. We control individually managed accounts and institutional funds and invest primarily in European and North American markets. As of December 2023, we have $34 billion of assets under management (AUM) and expertise in Senior Secured Loans, High Yield Bonds, Direct Lending, Structured Credit, Special Situations and Multi-Strategy credit. Alcentra's client relationship management team is composed of experienced and dedicated professionals that work to serve our clients' best interests and needs. Our Investor Relations team includes a dedicated client Relationship Management team who work directly alongside our investment teams, focused on serving clients' needs.

We collaborate with clients to suit their specific responsible investment needs. For example, some of our clients have separately managed accounts (SMAs), which may have specific ESG language in the investment management agreement (IMA) and/or side letters, which could include specific ESG exclusion criteria. We utilise a rigorous approach to ensure that we abide by the criteria through internal system control guidelines and measures within our internal CRM system.

- Focus on the financial outcomes that matter to our clients
- Be their investment allies: working tirelessly to overcome their challenges
- Engage with their individual needs, responding with the right solution not just the easiest
- Elevate their experience by matching the right people, advice and expertise to their desired outcomes

Our Investors

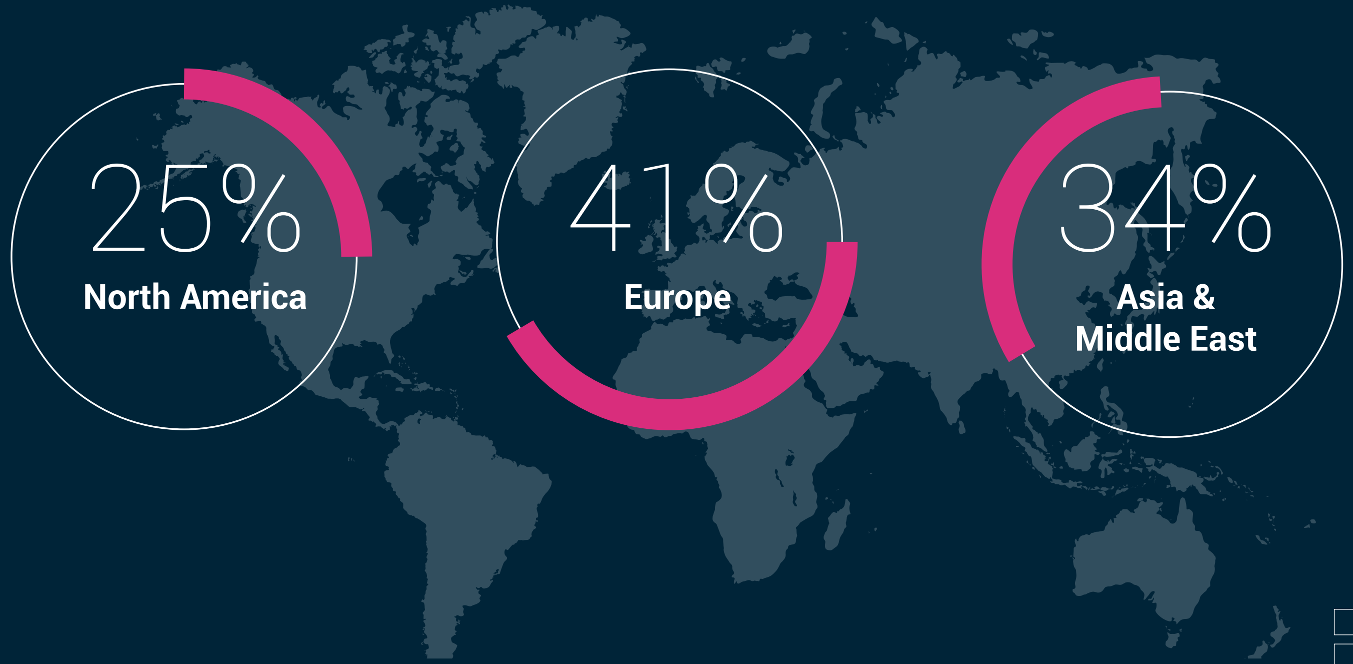
We work with investors around the world to help them make the most of the market opportunities

Our clients gain access through a large range of investment funds and where required we can help them build a portfolio tailored to their own specific needs and requirements.

38%	21%	14%	10%	17%
Pension Funds	Banks	Insurance	Wealth Managers	Government, Asset Managers and Other

As of December 2023, %s refer to non-CLO AUM.

Investor Base by Geography



INVESTMENT APPROACH

Investment Horizon

The investment time horizons vary by strategy and client. For example, European Direct Lending loans tend to have a longer-term horizon with maturity around 5-7 years, in comparison to the European Leverage Loan market or European High Yield market which typically mature within 4-7 years*. This is a reflection of the asset class characteristics as well as clients' preferences. With all of our assets being managed in bottom-up investment strategies, regular interaction with portfolio company management is an integral part of the investment process.

As a result, Alcentra's investment professionals have an in-depth knowledge of individual companies and long-standing relationships with company management teams that can help to support constructive engagement and dialogue. In the case of Structured Credit, instead of portfolio companies, the interactions and relationships are with CLO Managers we invest in.

Investor Engagement

Over the course of 2023, Alcentra responded to 154 dedicated ESG requests for information, representing a 33% increase in requests compared to 2022. We receive direct queries from our clients, as well as from financial consultants who advise clients. Although our ESG requests come from clients and consultants across the globe, in 2023, 77% of enquiries came from UK-based investors.

Some key topics of interest for our clients and consultants included:

- ESG Policy at firm level
- ESG client reporting
- ESG due diligence approach and exclusions
- Climate change data of the portfolio and exposure to fossil fuels
- Business ethics considerations
- Cybersecurity policies, training and data loss mitigation practices
- Implementation of the TCFD recommendations
- Stewardship activities / engagement examples
- Approach to voting.

* Alcentra market observation and experience, as of Dec 2023, which are subject to change.

INVESTMENT APPROACH

Reporting

As an example of our focus on reporting, Alcentra began producing a quarterly ESG report on our Direct Lending business in 2021 and has continued to enhance the reporting quality based upon data availability and client interest. The team receives a wide variety of queries from clients, the quarterly report provides insight into our stewardship activities – which may include engagement examples, ESG-related declines and data from ongoing dialogue with companies.

- Our Direct Lending engagements are tracked and monitored in accordance with the Investment Consultants Sustainability Working Group (ICSWG) engagement categories.
  - On an annual basis, Alcentra's Direct Lending and Responsible Investment team produce more granular, fund-specific ESG reporting to clients – disclosing approximately 50 pertinent ESG data points. A subset of these data points include: GHG emissions, carbon footprint and a selection of PAIs (as highlighted by EU SFDR regulations). The information is gathered through our annual ESG questionnaire which is sent out to all Direct Lending borrowers. For 2022 and 2023, the response rate to our ESG questionnaire increased from 94% to 100%, respectively.
  - This information is used to track borrowers' ESG risk profile, holistically monitor portfolios from an ESG perspective and inform engagement activity.
- Alcentra has received feedback from investors that this report positions the firm as a leader in the ESG disclosure space. We will continue to build out the data points covered in our Direct Lending ESG report. In 2024 we are planning to add questions aligning to our TCFD reporting requirement, around themes such as emissions reductions targets and data verification, as well as more in-depth questions on gender diversity and green revenues.

Feedback From Clients

Alcentra continuously seeks feedback from investors on our activities. For example, we aim to understand i) key ESG information requirements; and ii) how our product offering can be best aligned with their expectations on stewardship and responsible investment. We received the following feedback from a client which has shaped how we enhance our ESG practices.

> **We continue to feel that you have a good firm-level philosophy for various reasons including the fact your firm-level ESG efforts produce tangible outcomes and that you utilise ESG-aligned remuneration policies. Engagement with underlying companies is well pursued and monitored, with good examples provided. Your ESG integration approach remains very strong and is consistently applied. We would like to see further development of your climate risk assessment and your ESG reporting for the next period.**

Our Response and Action

We regularly factor in investor feedback in relation to continued improvements to our ESG reporting. In response to investor feedback, we have taken the following action:

- For our 2nd EU SFDR Article 8 fund, we have committed to quarterly ESG reports due to investor preferences. The report will include ESG scores, engagement statistics, engagement examples and climate data.
- In relation to our TCFD report due June 2024, we have used investor feedback gathered in 2023 to inform our approach on the assessment of climate risk and disclosure. As part of the report, we will look to:
  - Assess metrics and carry out scenario analysis (1.5°C to 4°C | 2025 to 2050).
  - Understand both physical & transition risks faced by the firm and our portfolio companies; and
  - Identify climate-related risks and opportunities for our firm and for our investments as part of our climate strategy.

Key Outcomes & Effectiveness

Through a review of the feedback we have received over the year, we have identified two main points where we can enhance our ESG practices to deliver more effective client benefits; namely ESG data and reporting.

For 2024, we will be entering a partnership with Findox, to capture ESG data across our Liquid Credit platform. We will collaborate with Findox with the aim of enhancing reporting and data standardisation.

Our reporting on responsible investment continues to evolve, and we benefit from clients, consultants, and standard setters' feedback as we seek to enhance our disclosures. In 2024, we have committed to produce additional ESG reporting for our Global Multi-Credit Asset Fund and our European Loan Fund.

7 PRINCIPLE

Signatories Systematically Integrate **Stewardship and Investment, Including Material Environmental, Social and Governance Issues**, And Climate Change, To Fulfil Their Responsibilities

ESG Exclusion Criteria

Alcentra believes that some corporate activities and behaviours are not compatible with our business values and responsible investment philosophy. We have established an exclusion policy which applies to all our investments, with the exception of our Structured Credit strategy*.

- We exclude issuers that derive any revenue from:
  - Development, production or sale of controversial weapons. Alcentra defines controversial weapons as biological weapons, chemical weapons, nuclear weapons, depleted uranium weapons, incendiary weapons, cluster munitions and anti-personnel mines.
  - Production or sale of cannabis for recreational use
  - Payday lending activities. Payday lending refers to small, high-cost short-term consumer loans as defined by the UK's Financial Conduct Authority. Due to the high-cost nature of these loans, it often leads to a cycle of increasing indebtedness from lower-income members of society.
- We also exclude issuers that derive more than 10% of revenues from:
  - Production or sale of tobacco or tobacco products
  - Production, operation and/or distribution of adult entertainment.
- Alcentra has also established exclusion criteria for certain fossil fuel activities. We exclude:
  - Issuers that derive 10 percent or more of revenue from thermal coal mining
  - Issuers that derive 10 percent or more of revenue from oil sands

* The Structured Credit team works with the CLO Managers they invest in, at the point of appointment, for primary deals, to request wording in the CLO documentation to apply separate restrictions and exclusions, wherever possible. The wording is utilised to prevent CLO Managers from buying assets with exposure to certain industries – as further described in the Structured Credit section below. Most Managers are quite constructive in including this language in their CLO documentation. Please refer to Principle 8 for more details on our approach to integrating ESG into our Structured Credit strategy.

ESG Integration

Alcentra takes into account its responsibilities towards its stakeholders, clients, shareholders and employees with regards to investment and performance. Our ESG integration process emphasises the importance of assessing material risks at both sector and issuer level. To that end, we have developed a suite of proprietary tools to support the integration of ESG factors into the investment process, including:

i) Sector Materiality Guide;
ii) ESG Checklist; and
iii) Climate Risk Tool.

The aim of the tools is to provide our investment teams with a consistent framework to assess material ESG risks and to help inform our engagement activities.

Sector Materiality Guide

As a starting point, credit analysts use a sector materiality guide to identify the ESG factors that could have a significant impact on issuers according to Alcentra's industry classifications. The guide helps inform issuers' ESG scores and provides direction for analysts on key factors to focus on during stewardship efforts.

ESG Checklist

Alcentra's ESG checklist was established in 2021 to provide investment teams with a consistent approach to assessing issuers across sectors and markets. Analysts use the checklist to capture relevant information on climate change, environmental, social and governance risks for new issuers. Issuers' ESG scores are used to construct and manage portfolios.

Our ESG scoring system relies on the assessment of more than 20 qualitative and quantitative indicators across each of the E, S, and G pillars. To inform issuers' scores, we rely on corporate disclosures and leverage our credit analysts' in-depth knowledge of their companies, sectors and markets, as well as third-party data. In addition to having individual pillar scores, analysts rate the overall ESG risk profile of the issuer. We use a 1-5 risk scale as defined in the table below. If an issuer scores 4 or 5 at a pillar or aggregate level, it will be referred to the Investment Committee. If an issuer is deemed to pose a very high risk (5) at an aggregate level, it will be excluded from the portfolio. Analysts are required to complete the checklist and include it in the investment paper presented to the Investment Committee.

Score	Risk Scale	Action
1	No risk	No action
2	Low risk	Monitor
3	Moderate risk	Inform relevant Investment Committee during credit approval process
4	High risk	Escalate to ESG Committee/focus issue at relevant Investment Committee
5	Very high risk	Exclude from portfolio and/or prevent further purchases

Climate Risk Tool

Alcentra's Climate Risk tool was developed to support the assessment of companies' exposure and management of transition and physical climate-related risks. We concentrate on sectors highly exposed to climate-related risks, either through their operations or value chains. We gather relevant climate metrics on our issuers, including companies' greenhouse gas emissions (GHG) across Scope 1, Scope 2 and Scope 3 and seek to track performance over time. Where companies do not disclose this information, we use third-party estimated emissions data. In addition, analysts also assess how well-prepared issuers are to manage the climate transition; for example, by considering companies' climate transition plans and targets. The tool calculates a climate risk score, which feeds into the ESG Checklist.

Monitoring

ESG risks and scores are dynamic. The assessment of ESG factors is part of the daily credit monitoring process, where analysts assess risks related to issuers. We monitor companies on ESG risk factors and update risk ratings accordingly. As part of our regular company dialogue, analysts engage with issuers on ESG matters regularly. Engagement may be more frequent with issuers exposed to higher ESG risks or where company-specific or macro risks are developing. We provide further details on our approach to engagements under Principle 9.

Direct Lending

Alcentra's Direct Lending platform often has the ability to exert some influence over borrowers as in many cases, we may be the sole lender and remain invested in the company for a longer time horizon, typically 5-7 years. In combination with our well-established relationships, we engage with companies to ensure their practices are aligned with Alcentra's responsible investment principles. Notably, the Direct Lending strategy offers a unique opportunity to exert additional influence on borrowers, as the strategy offers more granular insight and closer relationships with portfolio companies, given the majority lender position in capital structures.

In 2020, we implemented an ESG questionnaire to assess and monitor companies' exposure to ESG factors. The questionnaire is sent out to companies in our Direct Lending portfolio on an annual basis. Borrowers are required to provide qualitative and quantitative information regarding their sustainability strategy and approach to mitigating and managing key ESG risks. This information is used to track borrowers' ESG risk profile and to monitor portfolios. In 2022, the response rate to our ESG questionnaire was 94%, this increased to 100% in 2023. We will continue to collaborate with companies that have not been able to provide certain ESG data points to support them in their journey of measuring relevant metrics for their business, as well as in the development of their sustainability strategies.

Initiative: Direct Lending

Outcome From Our ESG Questionnaire for Direct Lending

63% of borrowers disclosed **scope 1 and 2** greenhouse gas (GHG) emissions data (↑ compared to 20% in the previous year)

53% of borrowers have disclosed an unadjusted **gender pay gap report** (↑ compared to 34% in the previous year)

63% of borrowers have **board level oversight** of environmental, social, governance matters

Annual ESG Questionnaire sent to all relevant[1] portfolio companies covering qualitative and quantitative ESG data

Engagement Tracker for recording ongoing ESG dialogue with borrowers and sponsors

145 **ESG-related engagements** with portfolio companies in FY23 (↑ compared to 111 engagements in the previous year)

30 deal kills, in part, due to ESG-related concerns in FY23 (↑ compared to 13 ESG-related kills in the previous year)

100% of portfolio companies responded to our ESG Questionnaire (↑ compared to 94% in FY22 and 90% in FY21)

7 out of 10 borrowers reported having a **Diversity and Equal Opportunities Policy** in place

28% of borrowers have set a **climate-based target** aligned with limiting global warming to 1.5°C

ENGAGEMENT EXAMPLE 1

We engaged with several borrowers with the aim of encouraging them to improve their ESG disclosures. This was ahead of the launch of our annual ESG questionnaire which is sent out to all Direct Lending portfolio companies. Through several interactions, Alentra's investment team stressed the growing importance of climate data and ESG disclosure. Alcentra shared details of an ELFA (European Leverage Finance Association) workshop on Carbon reporting; with three portfolio companies successfully registering their attendance. Alcentra circulated the 2023 ESG Questionnaire in March 23. Through comparison with the data provided from FY22 to FY23 we were able to note improvements in the data reported from those that we engaged with as well as those who attended the workshop, indicating that the objective of our engagement was met.

A Look Ahead to the 2024 Enhancement of the Questionnaire

Each year we attempt to enhance our questionnaire to bring it in line with market best practice allowing us to meet the increasing expectations of our investors. In 2024, we have chosen to place a greater focus on important diversity metrics whilst also aligning the climate questions to TCFD recommendations. We have already achieved a response rate of 100% for the 2024 questions and have again seen strong year on year increases in the number of companies reporting climate data. We believe data is particularly important for climate related ESG KPIs as borrowers can clearly evidence the link between their emissions metrics, transition plans and credible pathways to net zero.

[1] The ESG Questionnaire was only sent to companies where Alcentra holds a material debt position, excluding those where a near term exit was anticipated.

Initiative: Direct Lending Sustainability-Linked Loans

As part of our ESG integration efforts, and where the opportunity has arisen in more recent negotiations, we aim to integrate ESG margin ratchets into loan documentations, which look to incentivise borrowers to meet agreed ESG KPIs and targets.

Within our EU SFDR Article 8 Direct Lending fund, in 2023, 77% of funded capital now has language integrated into investment documentation relating to ESG KPIs and margin ratchets, up from 63% in the previous year, with 51% of funded capital having agreed ESG KPIs covering at least one facility. The margin adjustment mechanism is built around ESG criteria, and the borrower's performance will result in an increase or decrease to the margin depending on how it performs against the defined KPIs. We leverage this mechanism to incentivise borrowers to improve their performance on relevant sustainability matters.

Initiative: Direct Lending Sustainability-Linked Loan Thought Leadership

Alcentra is aiming to transition from a focus on ESG-Linked Loans to the more robust framework of Sustainability-Linked Loans (SLLs), with SLLs adhering to the guiding Principles set out by the Loan Market Association. To aid this, the Responsible Investment team created educational packs for borrowers and sponsors explaining SLLs. Following the circulation of these materials, an agreement was reached in principle for the implementation of Alcentra's first SLL, with the margin ratchet expected to go live in September 2024.

In addition to this Alcentra published a thought leadership piece on the evolution of the Sustainability-Linked Loan ("SLL") market. The paper explains the principles of structuring robust SLL facilities and stresses the importance of strong ESG data disclosure for borrowers. Several ESG and private market media outlets have subsequently run articles on the paper.

ENGAGEMENT EXAMPLE 2

Alcentra worked with a portfolio company and their sponsor to structure ESG related KPIs for their loan facility. Initial KPIs proposed by the company and the sponsor focused on general CSR initiatives. Our feedback was that this was not sufficient to be able to structure and execute a facility which aligned to the SLL principles.

After several conversations, we guided the company in structuring three material, robust and ambitious KPIs which were data driven and in line with market best-practice. The document was signed in Oct-23 and the KPIs included: **i)** carry out an SBTI-approved assessment of baseline emissions for the Group and calibrate annual emissions targets for the duration of the loan; **ii)** link CEO and C-suite variable remuneration to ESG criteria (such as diversity, working conditions, health and safety); **iii)** carry out an assessment of eco-design practices (e.g., use of recycled raw materials) and define a roadmap with quantitative objectives for subsequent years. We were able to work with legal counsel to utilise the latest LMA-approved language for SLLs. This helped ensure the loan terms and mechanics were in line with market best-practice for improving ESG outcomes.

8 PRINCIPLE

Signatories **Monitor and Hold to Account Managers And/Or Service Providers** Responsibilities

Service Providers

We continuously strive to enhance the research and data we use to inform our investment decisions. As part of the credit analysis, investment teams are required to assess the ESG risk profile of issuers. To do this, we rely on a variety of sources, including company-reported information, research from sell-side banks, data from specialist firms and third-party ESG data providers. While coverage from third-party service providers in our investment universe is limited relative to other asset classes, the information provided is useful, in particular to obtain sector-level insights.

During 2023, the Responsible Investment team successfully onboarded a new third-party ESG data provider, following approval by the ESG Committee. The data provider focuses on standardised ESG and sustainability reporting for the leveraged finance and private assets markets and is able provide a more extensive data coverage for the sub-investment grade market compared to providers which focus primarily on public assets. The overarching goal of external data is to complement our in-house research and database and to provide a holistic and comprehensive view of ESG risks and opportunities.

Our review process of external data providers consists of understanding the metrics and methodologies used to assess companies, as well as reviewing their coverage of the sub-investment grade credit market. We have continued to build and foster relationships with external data providers to provide feedback on an ongoing basis. We have found that this has been helpful when identifying and querying data points that may have been inaccurate or if we observed gaps in the data. We recognise this is a rapidly evolving space, so we will continue to explore other third-party providers to further enhance our ESG database, for example, on climate, biodiversity and human rights' data.

As a credit manager, voting is not material within the context of our activities. Therefore, we do not use proxy voting providers. We explain our approach to voting in more detail under Principle 12.

Structured Credit

ESG is integrated across the firm, and whilst we share a common philosophy across strategies, there are certain nuances in how strategies adopt this philosophy. Alcentra's Structured Credit strategy invests predominantly in CLO securities, which give indirect exposure to a diverse pool of syndicated loans. The CLO tranches our Structured Credit strategy invests in provides exposure to pools of loans managed by external firms. Due to the nature of these investments, analysts' engagement regarding ESG considerations primarily sits with the CLO Managers - as is standard market practice - as opposed to the underlying investments, as is the case with our Liquid Credit, Special Situations and Private Credit strategies. Over the past year, there has been a significant effort made to enhance the integration of responsible investment and ESG considerations into the Structured Credit's strategy.

ESG remains an important principle for the team, however for our Structured Credit investments, we aim to understand how the CLO Managers we invest in, consider and monitor ESG risk; for example, their governance structure, responsible investment policy, ESG assessment framework, risk tolerances and exclusion criteria.

As part of our monitoring and assessment process, our Structured Credit team:

- Speaks to CLO Managers that we invest with on a regular basis. The calls are to get updates on underlying loans, the Manager's platform and also to engage with managers on their ESG policies
- Send out an annual ESG questionnaire to a large proportion of CLO Managers to get a formal update on their ESG processes and policies, and ESG data on the underlying borrowers (including climate metrics)
- Request CLO Managers to share their ESG & responsible investment reports (both public & private) annually at a minimum
- Request regular updates regarding CLO Managers' dedicated ESG staff and resourcing, and we monitor the appropriateness and suitability of the staff

Throughout the course of 2023, we strengthened the significant efforts that were previously made to integrate responsible investment principles into the strategy, through focusing on the following key areas:

- Enhancing the CLO questionnaire that is sent out to all CLO Managers we invest in. The questionnaire was built out to understand the ESG due diligence process that managers conduct on their assets, their ESG scoring systems and whether there are any internal risk limits / tolerances based on ESG ratings, as well as information on their engagement and exclusions policies.
- Improved engagement with CLO Managers. As part of the strategy's focus on engagement, the Structured Credit team promotes Alcentra's ESG expectations through conversations with every CLO Manager that we invest with on a regular basis.

ENGAGEMENT EXAMPLE *3*

We engaged with a European CLO Manager to discuss the possibility of adding exclusions to the documentation of a primary deal. The CLO Manager is an example of a smaller European platform with an established US franchise. During the negotiation process, the Manager was initially against including our ESG exclusions within their CLO documentation. Through a process of education with the Manager and leaning on the bank arranger of the deal, we emphasised the importance of this topic in the European market. The Manager agreed to accept our exclusions and understood the growing significance of ESG integration within CLOs for future deals.

Key Outcomes & Effectiveness

Throughout 2023, we have improved the level of climate and sustainability data available to us through the successful on-boarding of a third-party data provider. We will use the information provided to drive engagements with borrowers and to inform our feedback to the provider.

The majority of European CLO managers have developed their own ESG investing and monitoring framework. We believe this development is positive for the market, and combined with our continued engagement with CLO managers, will help us and the wider industry drive further ESG integration across the investment strategies.

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9 PRINCIPLE

Signatories **Engage** with Issuers to Maintain or Enhance the Value of Assets

Stewardship Outcomes

As stewards of our investors' capital, we find that engagement is the most effective approach to understanding the ESG risks and opportunities associated with our investments. Our responsible investment principles guide our stewardship efforts, and we take an active role in engaging with existing companies in our portfolio, as well as with new issuers to better understand risks, improve disclosures and to encourage issuers to act in a sustainable manner.

We benefit from our scale and tenure in our markets, which provides access to company management teams, sponsors, and other key stakeholders. Our strong relationships provide us with the opportunity to meet with companies at conferences and road shows. Depending upon the strategy, our engagement efforts will be slightly different and more or less involved, according to the nature of the relationship with the company or the management team. For instance, our Direct Lending and Special Situations teams may often have a more involved relationship with the company and have the ability to exercise additional influence – particularly, if an Alcentra employee holds a seat on the Board of the company.

As indicated in Principle 8, in our Structured Credit investments, we apply a more strategy-specific approach to engagement whereby we engage with CLO managers to understand how they consider and monitor ESG risks. This includes, but not limited to: ESG governance structure; ESG policies; ESG assessment framework; stewardship activities; PRI signatory status and scores; and details on Managers' dedicated staffing. We also proactively engage with managers with regards to ESG exclusions. The Structured Credit team works with the CLO Managers they invest in, at the point of appointment, for primary deals, to request wording in the CLO documentation to apply separate restrictions and exclusions, wherever possible.

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Our Engagement Objectives Include:

- Uncovering information on companies' ESG risk exposures and management practices
- Monitoring issuers' exposure and performance
- Addressing concerns related to governance and management practices, performance and/or controversies.
- Encouraging disclosure aligned with internationally recognized standards; and
- Promoting the adoption of sustainable business practices

Who We Engage With

We engage with management teams, technical experts and, where relevant, board members, shareholders and/or arranging banks. Depending on the nature of our engagements, these may take the form of one-on-one company meetings, investor group discussions and/or written exchanges. The decision to focus on a particular strategic engagement typically occurs based upon the potential urgency of the dialogue. For instance, if a controversy arose, we would work to speak directly with the relevant parties – as soon as possible – either in a face-to-face meeting or on a call with management. Where possible, engagements focus on topics that are material to each business.

Prioritisation Of Engagements

We determine our engagement priorities on a case-by-case basis but may consider such additional factors as the investment exposure, stakeholder concerns and geography. We have focused previously on thematic engagements with carbon-intensive sectors, such as the oil and gas sector. As we consistently monitor headlines – we will engage with issuers that may be subject to an incident requiring further information. Similarly, we will engage proactively with companies following on from an issue that may have arisen from a competitor's misstep to provide our portfolio companies the opportunity to learn and potentially mitigate similar risks.

Engagement Tracking

We implemented an engagement log in 2021 to begin tracking our dialogues with companies and have continued to utilise this tracking tool throughout 2023. Over 2023, we enhanced our engagement monitoring system to align with the ICSWG categorisation of engagement themes, in efforts meet the increasingly standardised approach to stewardship reporting. We monitor companies' responses and have set internal KPIs to track progress over time. Although it can sometimes be challenging to attribute changes in companies' practices to our engagements, we see stewardship as integral to imparting positive change and reducing risks related to our investments.

ENGAGEMENT EXAMPLE *4*

Alcentra's Co-Head of Special Situations was appointed to the Board of Directors of one of our portfolio companies. Through our role as a Board member, we contributed to a number of influential decisions, directly supporting the company as it made alterations and enhancements to its existing operational and ESG strategies.

Through prolonged engagement over a number of years, Alcentra actively promoted and assisted in the publication of the company's first ever sustainability report in 2022. Alcentra provided a framework of required standards and performance indicators as a first step towards a comprehensive sustainability strategy. Since the publication, we have encouraged the company to start the exercise of calculating their current carbon emission and other sustainability metrics. The company has now collected s a wide-ranging set of emissions, waste, sourcing and other environmental data points.

During 2023, a baseline for each of these metrics was established and emissions targets have been set. This baselining activity and the further enhancement to the company's ESG strategy has led to the firm achieving an Eco Vardis gold rating. The gold rating puts the company in the top 5% of 125,000+ companies across 200 sectors globally.

ENGAGEMENT EXAMPLE *5*

The aim of the engagement was to gain comfort on governance considerations following negative headlines surrounding the company's financial disclosures. The issues primarily related to auditor concerns about the purchase and valuation of two smaller enterprises and the subsequent financial controls within the businesses. The concerns resulted in the auditors being unable to issue an unqualified audit opinion on the company. Following the governance concerns, our analyst increased the company's governance score to 'high risk' within our internal ESG risk framework.

Through engagement with the company, our analyst was able to gain comfort over the governance issues stated above. Our analyst confirmed that to resolve the audit concerns the company has now put more prudent financial controls in place, has increased communication flows with bondholders and lenders and has committed to starting their audit work earlier. Our analyst gained comfort from the fact that the company conducted a secondary audit report which concluded that the issues have now been remediated and the controls that have been put in place are sufficient.

Our analyst has encouraged the company to consider more frequent meetings/communication with lenders, including considering quarterly calls. We will continue to engage and monitor the governance situation of the company.

ENGAGEMENT EXAMPLE *6*

Throughout Q3 2023, we engaged with an issuer to gain clarity on two ESG concerns. The first related to the high staff attrition rates across the group. The second issue related to a Health and Safety incident at one of the company's sites. Our analyst engaged with management to understand whether the company had conducted an internal investigation and what kind of changes had been implemented at the centre to avoid further reputational damage occurring as a result of such incidents in the future.

Through continuous engagement with the company, our analyst was able to gain comfort over both issues stated above. Management concluded that staff churn was highest in one particular region and therefore implemented numerous initiatives to address poor local practices. Management did this through bringing in more senior HR executives and giving direct oversight of the regional team to the Group COO.

In addition to this, management took immediate action to remedy the health and safety issue identified at the centre. Management confirmed that deep cleans of the centre had been carried out and all centre team members had been retrained on Food Safety and Hygiene Management Systems. The company also invested significantly in the centre - both in terms of structural improvements and in its team members, completing a full kitchen renovation and enhanced training, support and supervision of the team.

All of this provided our analysts with the comfort they needed to conclude that the firm has sufficiently addressed the ESG issues at hand.

ENGAGEMENT EXAMPLE 7

The aim of the engagement was to obtain details on governance considerations and governance resolutions following negative headlines about corruption involving one of the company's subsidiaries and its vendors.

Through the engagement, our analyst confirmed that the company has replaced executives in procurement roles and individuals that could potentially be involved have been placed on leave. The company also confirmed that all impacted vendors are being replaced and an internal legal and forensic accounting review is being carried out. The company has committed to share key details of the findings with investors. Our analyst was comfortable that the magnitude of the impact was limited and that the company was taking the right steps to rectify and resolve the governance issue.

We will continue to monitor this engagement as further investigations and initiatives are made by the management team to understand how the group plans to strengthen compliance and internal controls.

ENGAGEMENT EXAMPLE 8

Alcentra is a shareholder in a portfolio company that received a Silver Eco Vardis rating as of 2022 (up from Bronze in 2017). Across 2023, the company worked with Alcentra's Head of ESG on achieving a Gold rating by addressing areas flagged in the rating assessment, notably a lack of a supply chain policy. Alcentra's collaboration has focused on the company establishing a best-in-class supply chain policy.

For that the initial guidance provided by Alcentra was for the company to focus on:

1. Ascertaining who all of the company's suppliers were and the economic value linked to each supplier;

2. Find out via a survey of the company's suppliers what they consider their top 3 ESG risks to be (impact vs likelihood) and how they are looking to manage these; and

3. Pick 2-3 international standards or frameworks the company wants to encourage their suppliers to follow (e.g., OECD Guidelines for Multinational Enterprises).

Points 1-3 has allowed the company to craft and then refine their supply chain policy.

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ENGAGEMENT EXAMPLE *9*

We engaged with a company which provides outpatient intensive healthcare. We engaged with the aim of better understanding how they manage key social risks relating to quality of care.

We questioned management on any ongoing incidences of misconduct with respect to quality of care as well as the controls they had in place to limit such incidences. Management confirmed there are currently two pending investigations, both of which are minor, isolated cases based on individual misconduct.

During the engagement, the company confirmed it has strict quality management policies in place. Management stated they have a dedicated and specialized in-house care quality management ("QM") team, which conducts internal audits with regards to care quality and care documentation. Further to this, the company confirmed compliance is ensured through external audits, all of which they have passed.

Our analyst gained comfort that ongoing misconduct issues were minor and were not systemic to the operation of the business. They will continue to monitor the cases until the investigations are closed.

ENGAGEMENT

10 PRINCIPLE

Signatories, Where Necessary, Participate in **Collaborative Engagement** to Influence Issuers

External Collaborations

The team at Alcentra is committed to serving our clients – and working collaboratively with a wider group of stakeholders – to assist in making a transformational change through engagement and collaboration. Alcentra collaborates and engages with peer investors and other stakeholder groups to improve market standards and exchange best practices as we work towards common goals.

We participate in a range of external initiatives. We became a member of the Institutional Investors Group on Climate Change (IIGCC) in 2021, the European membership body for investor collaboration on climate change. We advocate in support of their mission to enable the investment community to drive considerable progress by 2030 towards a net zero and resilient future. In addition, Alcentra became a signatory of the 2021 Global Investor Statement to Governments on the Climate Crisis. Alongside other 587 other investors with around 40% of the world's AUM, we called on governments to act on the climate crisis.

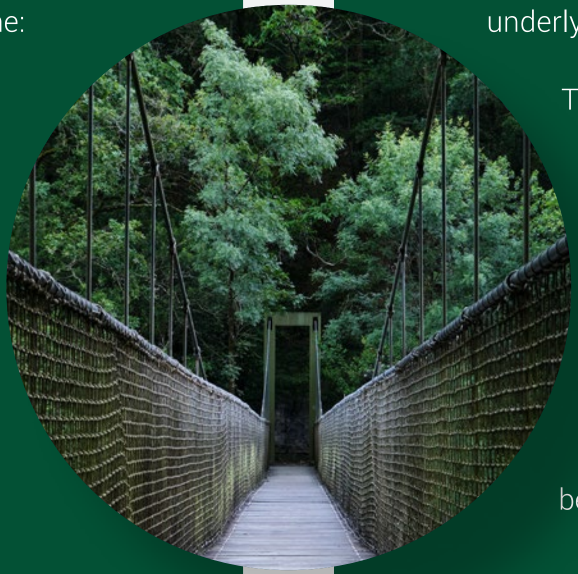
We will continue to explore opportunities to expand our external collaborations across environmental, social and governance topics. A key focus area is to work with other investors to advance the standardisation of ESG disclosures in the private sector. The following three engagement examples detail our wider collaboration activities with various other stakeholders and fellow investors.

ENGAGEMENT EXAMPLE *10*

Our Head of ESG has collaborated with the Loan Market Association (LMA) in the research and development stages of Sustainability-Linked Loan Principles ("SLLP's"), with the aim of working together to create industry-wide standards and best practices. Our Head of ESG attended several working groups and roundtables to share views of how best to shape the SLLP's. During our engagements with the LMA, we were able to share our views on the:

- Setting of KPIs and SPTs
- Materiality and ambition – further guidance on when these standards are/are not met; additional steps required depending on type of KPI, e.g. transition strategy to support emissions based KPIs; more guardrails around 'exceptional circumstances' for sleeping SLLs and consent levels; financing of dividend payouts
- Exceptions to annual target setting
- Margin ratchets – guidance from accounting references, e.g. IASB on treatment of ratchets
- Documentary provisions – guidance on declassification

The information and learnings we shared will go towards informing the SLL principles and their application to loans that we invest in as part of our Liquid Credit and Direct Lending portfolios.



ENGAGEMENT EXAMPLE *11*

Our Head of ESG collaborated with several CLO managers with the objective of sharing knowledge on the TCFD regulation and best practices for reporting on carbon metrics for the CLOs underlying assets. The engagements took place ahead of Alcentra's annual CLO Manager questionnaire, which asks managers to detail their ESG practices as well as provide climate data on the underlying assets.

This involved several calls with CLO managers to share Alcentra's experience and expertise with collecting issuer climate data. Our Responsible Investment team also put together a guide on "How to Measure the Carbon Footprint of CLO Investment Portfolios" to aid the market's understanding on climate reporting. This guide was circulated with all the CLO managers we invest in. The CLO managers confirmed they would take action to engage with borrowers to collect greenhouse gas emissions and reduction targets, allowing managers to disclose climate data at a CLO level. The climate data collected from the questionnaire will be used to inform Alcentra's TCFD reporting.

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ENGAGEMENT EXAMPLE *12*

Alcentra is an active member of ELFA, a professional trade association for investors in the European leveraged finance market. ELFA has been at the forefront of pressing the wider industry for improved ESG disclosure and standards. A key goal of ELFA's ESG committee is to create a framework for issuers in European leverage finance markets to promote transparency of disclosures required for investors to assess the underlying ESG risks in the market.

Members of our Direct Lending team sit on the ELFA Private Debt Committee and regularly discuss pertinent ESG considerations in the Direct Lending market. In 2023, we contributed to an insights paper ELFA published on ESG in Direct Lending. More recently, members of the team have been engaging with discussions on the integration of the Sustainability Linked Loans Principles (SLLPs) for Direct Lending deals.

We also collaborated with ELFA with the objective of helping shape the CLO manager due diligence questionnaire to advance more standardised disclosures across the CLO industry. We contributed to several round-table events with other CLO Managers and Structured Credit Investors to advise on the ELFA CLO manager due diligence questionnaire. This enabled us to meet our objective of sharing our opinions on how best to create a framework for CLO managers to promote transparency and standardisation when disclosing ESG risks. We believe this development is positive for the market, and combined with our continued engagement with CLO managers, will help us and the wider industry drive further ESG integration across the investment strategy.

ENGAGEMENT

11 PRINCIPLE

Signatories, Where Necessary, **Escalate Stewardship Activities** to Influence Issuers

Escalating Stewardship Activities

Engagements with issuers on ESG matters typically involve multiple interactions over a set period of time. These dialogues are conducted in close collaboration between the investment and Responsible Investment teams. Although we do not typically hold voting rights as shareholders, we may still be able to influence companies as a provider of capital.

Alcentra believes that in order to observe meaningful changes in companies' governance and sustainability practices, we need to be i) effective at conveying our messages; and ii) allow sufficient time for companies to take on board our input. We also recognise that in some cases, our engagements may not result in the desired outcomes.

Escalation measures will depend on the scope of our engagement, the severity of the issue, the size of our holdings, the company's response to date and likelihood of enacting change. The Investment Committee and ESG Committee participate in the monitoring of credits that pose elevated ESG risks. If an engagement with a high-risk issuer proves to be ineffective, the ESG Committee may make recommendations to the relevant Investment Committee on potential escalation measures, which depending on the asset class, may include a reduction in position on a particular credit, or divesting entirely.

The time horizons for divestment or the outcome of the escalation process may differ from strategy to strategy, depending on the liquidity of the assets. For example, if a controversy occurs or any ESG risk factor increases to the point that we believe the correct course of action would be to divest of an asset held in our Liquid Credit funds, we will attempt to do so promptly. The assets in these funds and the broader European loan market are reasonably liquid allowing us, in normal market conditions, to typically divest effectively. Prior to making a decision to divest, we would undertake the process of assessing a controversy and would undergo detailed analysis, which includes engaging with the portfolio company and often the owner of the business.

Alcentra maintains an ESG engagement tracker to capture and measure the effectiveness of our engagement activities. The engagement log is relied upon to track the progress of our dialogues and to identify situations where we need to escalate measures; for example, by divesting or reducing our position.

ENGAGEMENT EXAMPLE *13*

During 2023, Alcentra's Liquid Credit team made the decision to divest from a gaming company following governance concerns relating to ongoing legal proceedings between the firm and one of its subsidiaries. Whilst the parties involved stated they were keen for the matter to be resolved quickly, our analyst concluded that the legal disputes presented material event risk for the company due to uncertainty on the timing and magnitude of the outcome. As a result of the heightened risk profile of the company, the decision was made to divest the position.

Key Outcomes & Effectiveness

We escalate our engagements when our objectives are not met. Escalation occurs on a case-by-case basis and the decision to reduce our position, or ultimately divest, is a multi-faceted consideration.

We consider the severity of the engagement issue, the responsiveness of the management team, the strategic plan put in place to mitigate further incidents and the geography of the company's operations.

EXERCISING RIGHTS AND RESPONSIBILITIES

12 PRINCIPLE

Signatories Actively **Exercise Their Rights and Responsibilities**

Exercising Rights and Responsibilities

As one of the leading participants in the syndicated leveraged loan and high yield bond markets across various sectors in both Europe and the United States, Alcentra has some influence as an actual or potential lender or noteholder. Alcentra regularly attempts to effect changes to term sheets, loan agreements, offering memorandums and prospectuses during the marketing stages of the vast number of transactions presented to us. Given our position in the market, our feedback and views are often sought by borrowers, issuers, sponsors and/or arranging banks in pre-marketing stages. This preview, ahead of general launches to the wider market, provides us with a first attempt to change and shape key factors through the introduction of ESG considerations, most commonly with the goal of embedding ESG KPIs.

Our legal review process is robust. Our internal legal team, specialising in leveraged financing, will conduct a detailed review of the legal documentation provided. The result of that review is a list of items that require further attention. Our internal legal team also has access to reports prepared by external document review providers. The analyst covering the relevant transaction will then consult with our internal legal team to determine a further refined list of points, whilst considering the transaction specifics. These details will then be raised with the arranging / underwriting banks. Depending on the circumstances, a discussion with such banks may take place. Our portfolio managers and investment committee members are kept abreast of these movements and often raise queries or engage in related discussions.

A similar process applies to amendment, consent and/or waiver requests, where the borrower or issuer of one of our existing investments is seeking to amend the loan or bond documentation via a voting process. The nature of these requests means that the relevant analyst may also have an opportunity to engage with the borrower, issuer or, if relevant, sponsor to gain a deeper understanding of the context, rationale and impact and present any initial feedback or views. Taking all relevant factors into consideration, we may then seek to influence the path forward by consenting, abstaining, or rejecting with regards to such vote, including, where relevant, proposing changes or conditions.

It should be noted that, when assessing a potential investment, we will consider the legal documentation along with other key decision drivers, including but not limited to, ratings, credit quality, sector, geography, ESG risk profile and economics. As such, if a borrower or issuer holds a relatively strong position and we have strong conviction on its outlook and relative value, we may be more likely to accept document concessions when investing.

ENGAGEMENT EXAMPLE *14*

As part of Alcentra's ESG integration efforts, we look to encourage the sustainable performance by linking borrowers' interest payment to pre-defined ESG targets. The ESG margin adjustment mechanism is built around ESG KPIs and targets, and the borrower's performance will result in a reduction to the margin depending on how it performs against the defined KPI targets. We leverage this mechanism to incentivise borrowers to improve their performance on relevant sustainability matters.

In 2022, Alcentra engaged with a borrower to set ambitious KPIs for their loan facility which were agreed in H2. In 2023, the company wanted to reset the baseline for a metric which they had missed in the latest reporting period, making the targets less ambitious and easier to achieve.

We explained our position clearly to the Sponsor to help them understand that targets are set to be ambitious. The final outcome was to leave the KPIs unchanged. We believe that this is an example of a strong ESG engagement as we were able to uphold the integrity of the loan facility. We understand that weak KPIs do not align with our robust ESG principles and put all parties at risk of green-washing claims.

Restructurings

Restructurings potentially provide us with even greater, and direct, influence over the legal documentation, which we use in striving to obtain the best outcome and value for all relevant parties. Depending on the amount of our exposure or holdings, we may join an ad hoc committee or group of lenders or noteholders, the key aim of which is to lead, formulate, negotiate and manage the relevant restructuring. Given the nature of these special scenarios, lenders or noteholders also tend to possess more bargaining power, relative to par or performing investments. Our internal legal team will be involved in the process, bolstered by external legal counsel and other advisers appointed to assist.

Voting Activity

As a credit manager, proxy voting is not material within the context of our activities. The number of occasions when Alcentra will be engaged in proxy voting will be limited. It is most likely to occur with high yield bond investments, where an allocation may take on formal voting rights. In such instances, Alcentra uses the opportunity to vote on matters concerning governance and corporate responsibility.

Alcentra generally will not be called upon to vote for proxies for its syndicated loan and Direct Lending investments because of the nature of the instruments involved in the investment strategy (i.e., loans rather than securities). An exception may be when Alcentra holds loan investments which could be converted to voting securities.

Proxy votes are also not generally conducted for corporate bonds. In addition, proxy votes may take place from time to time on Structured Credit investments where our fund holds the equity tranche.

When engaged by a client to provide discretionary advisory services, Alcentra is typically delegated the responsibility to vote on matters considered at portfolio companies' shareholder meetings, usually by means of a proxy ballot ("proxy voting"). In these instances, Alcentra has a duty to monitor corporate events and to vote proxies in the best interest of its client and not subrogate the interests of its clients to its own interests. This generally means voting with a view toward enhancing the economic value of the investment.

When it has voting responsibility, Alcentra will make every attempt to vote when given an opportunity to do so. However, there may be instances when the Firm is unable or unwilling to vote because of legal or operational difficulties or because it believes the administrative burden and/or associated cost exceeds the expected benefit to a client. Alcentra reviews the circumstances for each vote to determine which stance would best serve its clients and aims to act accordingly.

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