Alcentra NY, LLC | Alcentra Limited

Responsible Investment Policy

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OUR APPROACH TO RESPONSIBLE INVESTMENT

Founded in 2002, Alcentra's objective is to achieve attractive long-term investment returns for its clients. We seek to achieve this goal by investing in responsibly managed companies. We believe these companies are better placed to achieve sustainable competitive advantage and provide long-term growth. At Alcentra, our primary activity is lending to sub-investment grade companies. We have been a PRI signatory since 2018.

The aim of this policy is to describe our principles and set out our approach to integrating and managing ESG risks in our investment process. Alcentra's ESG investment framework involves the following key activities:

i) exclusion of companies based on defined product or conduct criteria ("Exclusions Policy");
ii) in-depth analysis and ongoing monitoring of ESG risks;
iii) active stewardship; and
iv) collaboration with other investors and standard setters.

While this is a firm wide policy and we share a common responsible investment philosophy across investment strategies, there are certain nuances in how our Structured Credit business adopts this philosophy.

Governance of ESG risks

Alcentra's Board of Directors is ultimately responsible for ESG matters for the firm. Alcentra's Executive Committee, chaired by our Chief Executive Officer, reviews and monitors the implementation of the firm's responsible investment strategy.

Alcentra's ESG Committee is responsible for the approval and implementation 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 ESG 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. The ESG Committee meets at least on a quarterly basis and reports to Alcentra's Global Investment Group. The ESG Committee provides regular reporting to Alcentra's Board's Risk Committee and Executive Committee.

In 2021, Alcentra established a dedicated Responsible Investment team to further develop the firm's responsible investment strategy, its policies and procedures. The Head of Responsible Investing is also a member of Alcentra's Investment Committee and chairs the ESG Committee. The Responsible Investment team works across the firm to support the execution of the Alcentra's responsible investment strategy, including the integration of ESG factors in investment decisions.

Alcentra's ESG policy is approved by the ESG Committee and presented to the Board of Directors. The policy is reviewed on an annual basis.

RESPONSIBLE INVESTMENT PILLARS

Alcentra has established a series of responsible investment principles to 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 outlined our priorities across the key pillars: governance, climate change, environment and social.

Governance

Alcentra is a provider of capital to companies. We have an interest in ensuring the issuers in our portfolio are able to repay 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 a shareholder, we share common interests. We believe good corporate governance is fundamental to ensure our interests as creditors are protected. An effective board is essential to oversee the adequate management of environmental and social risks. As part of our due diligence, we take into consideration various governance factors, including but not limited to the: i) board structure and composition; ii) remuneration practices; iii) anti-corruption practices; and iv) transparency and ethical conduct.

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. 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.

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 a company's ability to repay their debt. At Alcentra, we assess issuers' exposure to material environmental issues, which could include water management, waste management, land use change and biodiversity, as well as airborne pollution. Our starting point is to identify the most material environmental risks relevant to the issuer's sector and regions of operation. We seek to understand the company's internal policies towards addressing environmental issues and the impact their operations may have on the environment.

Social

Companies may be exposed to social-related risks in 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. These factors may pose reputational, regulatory and legal risks and costs to companies.

EXCLUSIONS POLICY

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 antipersonnel 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[1]. 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

[1] https://www.handbook.fca.org.uk/handbook/glossary/G3328.html

ESG RISK ANALYSIS AND MONITORING PROCESS

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 in the investment process, including: i) sector materiality guide; ii) ESG and climate checklist; and iii) climate risk tool. The aim of the tools is to provide our investment teams with a consistent framework to focus issuer engagement and in assessing material ESG risks of an issuer.

Table 1. Alcentra's key ESG tools

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 & climate checklist

Alcentra's ESG & climate 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 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 ESG Committee. If an issuer is deemed to pose a very high risk (5) at an aggregate level, it will be excluded from the portfolio.

Scores at pillar level

Score	Risk Scale	Action
1	No risk	No Action
2	Low risk	Monitor
3	Moderate risk	Inform Investment Committee during credit approval process
4	High risk	Refer to ESG Committee / Focus issue at Investment Committee
5	Very high risk	Exclude from portfolio

Analysts are required to complete the checklist and include it in the investment paper presented to the Investment Committee.

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 and Climate Checklist.

Monitoring

ESG risks and scores are dynamic. The assessment of ESG factors is an important part of the daily credit monitoring process, where analysts assess all risks and opportunities related to the issuer. We regularly monitor companies on these risk factors and update risk ratings when there are any material changes.

As part of our regular company dialogue, analysts engage with issuers on ESG matters at least annually. 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.

Structured Credit

In our Structured Credit investments, we aim to understand how the Collateralized Loan Obligations (CLO) managers we invest in consider and monitor ESG risks, including but not limited to, their governance structure, responsible investment policy, ESG assessment framework, risk tolerances and exclusions criteria. The vast majority of 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 investment processes.

In addition, when purchasing CLO tranches in the primary market, where Alcentra has more influence over the loan eligibility criteria for the CLO, we ask for exclusions of companies involved in certain activities. The exclusions include companies involved in the development, production, maintenance, trade or stockpiling of weapons of mass destruction (in line with Alcentra's ESG policy on excluding controversial weapons) and the production or trade of illegal drugs or narcotics, including recreational marijuana. In addition, we ask for the exclusion of loans to companies whose primary revenues are derived from prostitution-related activities, the manufacture, sale or distribution of pornographic materials or content and the production or sale of tobacco and tobacco products, including e-cigarettes. Businesses that solely derive their revenues by doing business with excluded companies would also constitute an excluded company.

ACTIVE STEWARDSHIP

As investors in the sub-investment grade credit market, Alcentra faces challenges related to availability and transparency of ESG data from issuers. As stewards of our investors' capital, we find that engagement is the most adequate approach to understand the ESG risks associated with our investments. We take an active role in engagement with portfolio companies to better understand risks, improve disclosures and 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 responsible investment principles guide our stewardship efforts.

Alcentra maintains an ESG engagement log to capture and measure the effectiveness of engagement activities. ESG-related activities, including company engagements, are a component of analysts' variable remuneration. When the risk associated with an investment increases beyond the ESG risk appetite of the fund, the portfolio manager will consider selling or reducing its exposure to the issuer.

Typically, investments in instruments that have voting rights is ancillary to the firm's investment strategy, which focuses on investments in private and public sub-investment grade debt. Where applicable to vote on such instruments and in subsequent decisions (dependent on the vote in question), we will follow Alcentra's ESG principles outlined above.

EXTERNAL COLLABORATION

Alcentra collaborates with other investors and key stakeholders to improve market standards and exchange best practices as we work towards common goals. Better corporate disclosures on ESG issues remains a priority for Alcentra. In Table 2 we present the main organisation and industry initiatives we take part in.

Table 2. Alcentra's membership of organisations and industry initiatives

Organisation	Year
Principles for Responsible Investment (PRI)	2018
European Leveraged Finance Association (ELFA)	2019
Task Force on Climate- Related Financial Disclosures (TCFD)	2020
Institutional Investors Group on Climate Change (IIGCC)	2021

FINANCIAL PROMOTIONS

The Firm is required by regulation to ensure that any marketing materials remain consistent and do not contradict any of the Firm's actual approaches to integrating ESG factors into the management of client portfolios or Firm sponsored investment vehicles. As such, the Firm has in place standard descriptions regarding the integration of ESG/sustainability risks within its portfolio management processes and these are consistent with any pre-contractual disclosures that are provided in client and investment vehicle literature. All ESG-related disclosures (including marketing material, website postings, press announcements etc.) are approved by the firm's ESG Committee. Any changes to these descriptions must be approved by the ESG Committee prior to being included in any firm-wide or product marketing material.

DISCLAIMER

This Policy is provided for use by professional investors and/or distributors and should not be relied upon by retail investors.

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The Bank of New York Mellon Corporation ("BNY Mellon") holds the majority of The Alcentra Group (or "Alcentra"), which is comprised of the following affiliated companies: Alcentra Limited and Alcentra NY, LLC. Assets under management include assets managed by both companies.

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A prospective investor should consider the relevant strategy's investment objectives, risks, charges and expenses carefully before investing. Portfolios are subject to investment risks, including possible loss of the principal amount invested. Material in this Policy is for general information only and is not intended to provide specific investment advice or recommendations for any purchase or sale of any specific security or commodity.

Investments in sub-investment grade debt are speculative and involve special risks, and there can be no assurance that an account's investment objectives will be realized or that suitable investments may be identified. Many factors affect performance including changes in market conditions and interest rates and in response to other economic, political, or financial developments. An investor could lose all or a substantial portion of his or her investment. No investment process is free of risk and there is no guarantee that the investment process described herein will be profitable. No investment strategy or risk management technique can guarantee returns or eliminate risk in any market environment.

Conditions of disclosure of this Policy to you