Policy on Integrating ESG and Sustainability Risk into Investment Research

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Muzinich & Co

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We believe ESG factors, which we consider to include "Sustainability Factors" as defined by Regulation (EU) 2019/2088 (the Sustainable Finance Disclosure Regulation or "SFDR")[1], are becoming increasingly material drivers of business risk and opportunity due to tightening regulations, changing consumer preferences, and the need for greater resource efficiency among other reasons. We therefore consider ESG analysis to be a useful lens through which our investment team can analyze a company alongside more traditional financial factors, in order to better identify, monitor and manage potential "Sustainability Risk" (as defined by SFDR)[2] and broader investment risks and opportunities.

- Muzinich defines ESG integration as the explicit consideration of ESG data alongside commonly considered financial data, with the aim of informing investment research and decision making.
- Our investment teams, across the various sub-asset classes of credit that we manage, seek to consider and integrate material ESG factors into their research, investment decisions, and ongoing monitoring of our investments in order to identify and, where possible, manage and mitigate the impact of potential Sustainability Risk.
- We conduct our own ESG research and partner with independent ESG data providers to ensure investment decisions are informed by comprehensive and reliable data where available.
- We are committed, subject to the availability of data, to producing scoring on the ESG attributes of public and private entities in which we invest and to tailor our scoring methodology to the asset classes, industries, and investment vehicles in which we invest.
- We strive to continually improve the coverage of our ESG research and integration process by engaging issuers and independent data providers to address gaps in ESG disclosures and research coverage.
- We commit to periodically review critical ESG services and external data providers to ensure we source high-quality ESG data across the broadest possible range of entities we invest in.
- We are committed to being transparent about how we score entities on their ESG attributes and how our ESG research impacts investment decision making, whether that leads to changes in analyst recommendations, exclusion, engagement activity or otherwise, and to sharing details of our ESG scoring methodology with investors.

Assessing and managing Sustainability Risk

We believe Sustainability Risk can have a material impact on the profitability, liquidity, financial profile and reputation of companies we might invest in, and ultimately on the risk and return of a financial product.

As an investor in corporate credit, one of our primary concerns is to identify and, where possible, manage and mitigate the impact of Sustainability Risk on the returns of our financial products through investment due diligence or research, asset allocation, portfolio management, restrictions or exclusions and ongoing monitoring and engagement of entities we invest in. We seek to assess sustainability issues and potential materiality on a case-by-case basis based on available ESG data. Outside of the specific industry- or conduct-based exclusion policies described in the "Product-specific ESG Policies of Muzinich-branded Funds" document, we do not typically follow an approach whereby ESG metrics necessitate buy, sell or weighting decisions on investments.

Information to identity and assess Sustainability Risk

[1] Sustainability Factors are defined in SFDR as "environmental, social and employee matters, respect for human rights, anti-corruption and anti-bribery matters".

[2] Sustainability Risk is defined as "an environmental, social or governance event or condition that, if it occurs, could cause an actual or a potential material negative impact on the value of the investment".

As part of Muzinich's ESG research and scoring procedures, we consider a number of different types of ESG information including, but not limited to the following (which may be obtained directly from the issuer, or via our own- or third-party research):

- Individual (raw) ESG metrics and quantitative data which may be considered drivers of risk and opportunity;
- Information on issuer involvement in controversies relating to serious human and labor rights abuses; environmental harm, or business integrity failures (e.g., fraud, tax evasion); and
- Information on issuer involvement in industries which may be considered to be controversial (e.g., weapons or tobacco).

Our analysts are not required to consider a prescriptive or exhaustive list of ESG factors when conducting ESG analysis or creating ESG scores. Instead, they aim to identify the issues which they consider to be most material depending on an individual company's regional, sectoral, jurisdictional, social and environmental context. There are, however, certain ESG factors which may exacerbate the potential for a Sustainability Risk to materialize. These factors may be specific to certain industries or applicable to several sectors.

Examples of ESG factors which may be considered as part of our research and ongoing monitoring process, and which are included in our proprietary ESG scoring methodology, are provided below in Figure 1.

Figure 1: Examples of ESG factors which may be considered or scored as part of our integrated research process.[3]

Environmental Factors	Social Factors	Governance Factors
Biodiversity impact management	Access to medicine program	Animal testing policy
Climate risk management	Advertising ethics policy	Audit program
Deforestation program	Collective bargaining agreements	Board diversity
Emergency response program	Community involvement programs	Board independence
Environmental management system	Contractor fatalities	Bribery and corruption policy
Green buildings investments	Contractor safety program	Business ethics program
Green logistics programs	Customer eco-efficiency programs	Climate governance
Green procurement policy	Discrimination policy	Clinical trial standards
Greenhouse gas emissions	Diversity programs	Conflict minerals policy
Hazardous waste management	Drug promotion standards	Cybersecurity program
Non-CO2 air emissions programs	Employee fatality rate	Data privacy and security policy
Oil spill disclosure and performance	Employee training	ESG governance
Product eco-design	Employee turnover rate	ESG transparency
Product stewardship programs	Financial inclusion	Global compact signatory
Real estate life cycle assessment	Freedom of association policy	Lobbying and political expenses
Recycled material use	Gender pay disclosure	Money laundering policy
Renewable energy use	Gender pay equality program	Political involvement policy
Share of green buildings	Health and safety management	Quality Management Systems
Solid waste management	Human Capital Development	Responsible Investment Policy
Sustainable agriculture programs	Human rights policy	Responsible product offering

[3] Source: Muzinich & Co., as of 30 November 2022. Provided for illustrative and example purposes only, not necessarily considered for all investments or all-inclusive.

Sustainable financial initiatives	Lost time injury rate trends	Tax practices
Sustainable products and services	Media ethics program	Underwriting standards
Sustainable sourcing policy	Occupier satisfaction surveys	UNEPFI signatory
Tailings management and standards	Product and service safety program	Verification of ESG reporting
Water intensity	Responsible marketing policy	Whistleblower Programs
Water management programs	Working hours policy	Supply chain management policy
Water risk management		

Sourcing ESG data

The process of gathering and processing ESG data is specialized and resource intensive. Muzinich analysts collect financial and non-financial information as part of their research process but we have also partnered with independent ESG data providers to source ESG data including raw ESG metrics; ESG scores and rankings; involvement in controversial industries, or business conduct issues; greenhouse gas emissions data; climate risk data; and other data required for regulatory disclosures. We may also source data from government and non-governmental organisations, academic sources and other publicly available sources.

To assess issuers of public securities, Muzinich primarily sources ESG data from Sustainalytics and Institutional Shareholder Services ("ISS ESG").

We are committed to reviewing our data sources at least every two years to ensure we are able to source high quality relevant data in a cost-effective manner. Members of our ESG Integration Group periodically review possible data provider options while certain members of Muzinich's board of directors make final decisions on whether to partner with those providers. Among our considerations for choosing ESG data providers are the accuracy, timeliness, coverage, and quality of insight they bring; the efficiency with which we can process the data; and the general user-friendliness of the data platforms provided.

Proprietary ESG scoring methodologies for public and private issuers

Muzinich has developed various proprietary ESG scoring methodologies for public issuers, leveraged loan issuers, private corporates and aviation leasing. These were developed through collaboration of our investment teams and our ESG Integration Group members to ensure those methodologies are useable, produce meaningful results to enhance their understanding of issuers they research, and help them to distinguish between good and poor ESG management for research and investment purposes. Details of the scoring methodologies are summarized below and further information is available on request.

<u>(i) ESG scoring methodology for public issuers (liquid securities including bonds and corporate loans)</u>

Muzinich analysts have selected ESG metrics which they consider most important at the sector level and apply weights to associated scores which are normalized on a 0-5 scale. The ESG metrics are sourced via primary research or from external data providers as raw or processed data. Analysts aim to fill data gaps from publicly available information or engagement with companies. The methodology combines an ESG company score with a separate climate risk score.

In the final stage of the scoring process the analyst can adjust the initial score up or down based on factors including expectations of near-term ESG improvements or deteriorations, recent engagement outcomes, or discrepancies with third party data relating to the target company.

Muzinich's ESG scores will be continuously monitored and updated for new information as analysts cycle through assessments of companies within their research universe. Muzinich's ESG Integration Group members conduct periodic spot checks on aspects such as data quality, materiality weighting, and our analysts' adjustments. Data from independent ESG data providers is automatically fed into Muzinich's IT systems on a monthly basis to ensure it is as current as possible.

We have invested in resources and expertise to be able to integrate our two main independent ESG data sources into our research, trade restrictions, investment monitoring and reporting platforms. This will facilitate further ESG integration for our investment team and ESG reporting at the investment product level as part of monthly reports or annual financial statements from early 2023 onwards.

In 2023 we will roll out our proprietary ESG scores alongside certain third party ESG metrics in the ESG scorecards that appear in our issuer research templates. Analysts are also expected to produce an ESG writeup alongside these scorecards to provide more details on their view of an issuer's management of ESG factors and risks.

(ii) ESG scoring methodology for leveraged loan issuers
Muzinich may score leveraged loan issuers using either our public debt ESG scoring methodology where sufficient data is available, or a dedicated loans methodology. The loans methodology leverages data from a different ESG data provider and overlays the industry-specific weighting applied in our public debt scores to produce a score on the same scale of 0-5. This ultimately allows us to significantly increase the coverage of our research and has been made possible through sharing of ESG information on privately held companies between loan investors and an independent data provider.

(iii) ESG scoring methodology for private corporates
Muzinich's Private Debt team, with support from our ESG Integration Group, has developed a proprietary ESG scoring methodology, the "Private Debt ESG Scorecard", to integrate ESG assessments into the investment committee discussions and ongoing annual monitoring of our private debt investments. The Private Debt ESG Scorecard comprises the following ten ESG factors against which an investment is scored:

1) The ESG credentials of the investee company's beneficial owners e.g. evidence of dedicated ESG-related policies, management function(s) and resources and oversight of ESG
2) ESG management, transparency, accountability
3) Evidence of bribery and/or corruption
4) Lack of risk management
5) Management of climate change impacts
6) Planned natural resource use
7) Evidence of environmental degradation
8) Employee engagement and welfare
9) Stakeholder risks, such as company/product boycotts
10) Diversity and inclusion in HR and/or hiring practices

For each ESG factor, an investment is assigned a score of zero to five, giving a potential total score of 50 out of 50 which may then be scaled down to a 0 to 5 score. The ESG scores are included alongside a summary of ESG strengths, weaknesses, opportunities and threats in the final investment memorandums which are presented to private debt fund investment committees prior to final investment decisions and updated for monitoring annually.

(iv) ESG scoring methodology for aviation leasing
Muzinich's Aviation team, with support from our ESG Integration Group, has developed an ESG scoring methodology, the "Aviation ESG Rating", to integrate ESG assessments into the investment committee discussions prior to making investments.

The Aviation ESG Rating is broken down into two main components and various sub-components and weighted as follows:

Asset rating (50%)

- Aircraft type (35%)
- Aircraft age (15%)

Airline

- Environmental policy (5%)
- Fleet age (10%)
- Aircraft utilization (10%)
- Fleet type (15%)
- Sustainability policy – social (5%)
- Board governance (5%)

Our private debt and aviation ESG scores are produced from sources including, but not limited to: (i) conversations with management; (ii) notes to the investee company's financial statement; and, if available, (iii) the investee company's sustainability statement.

Alongside Muzinich's proprietary ESG scoring methodologies, we also use ESG scores derived from independent ESG data providers including

- An ESG controversy score which measures the severity of sustainability related incidents related to an issuer and which are rated from 1 to 5 where 5 represents an event which has a severe impact, and 1 represents a low impact on the environment or society.
- Absolute ESG scores which are measured on a 0-70 scale ranging from "negligible" ESG risk to "severe" ESG risk.

ESG risk rankings or percentiles which ranks issuer's by their ESG score relative to industry peers or the broader research universe.

We may use one or more of these scoring methodologies as guidelines or binding criteria (e.g., best-in-class scoring thresholds) in our investment strategies as noted in "Product Specific ESG Policies of Muzinich-branded Funds".

Risk warnings: Exclusion Risk: ESG screening can limit the investment opportunities available to a portfolio, such as the exclusion of certain investments for non-financial reasons. As such, a portfolio may underperform other similar portfolios that do not apply ESG screening. ESG Risk: Consideration of Sustainability Risks in the investment process can result in the exclusion of certain investments in a portfolio. Therefore, results may differ, and a portfolio that considers sustainability risks might underperform other similar portfolios that do not consider such risks.

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SFDR - Refers to Regulation (EU) 2019/2088 or the Sustainable Finance Disclosures Regulation (SFDR) a piece of European financial sector regulation which sets out obligations for financial market participants to disclose specific details on their approach to sustainability risks in their investment process and other details on the provenance of ESG claims that are used to market their financial products. Further details on Muzinich's SFDR disclosures are available in relevant product documentation such as fund prospectuses and supplements on our website www.muzinich.com.

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