

Environmental and Social Policy Development Best Practice for Private Equity (PE)

September 2016



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- Welcome & Introduction to the session
- The business case for E&S management for private equity
- What is an E&S policy and why is it needed?
- Key considerations when developing an E&S policy
- Summary of EBRD E&S Requirements
- Best practice elements
- Review of good policy examples
- Session Conclusion & Questions

- **Welcome & Introduction to Panellists**
- *EBRD*
 - Anne Maria Cronin - Senior EBRD
- *ERM*
 - James Stacey - Partner
 - Melanie Mann - Environmental and Social Adviser
- **Webinar purpose:**
 - Opportunity to provide policy guidance Private Equity (PE)
 - Present practical elements of a policy
 - Note on the Importance of Policy requirement to EBRD

ESG issues headline the macro-risks of greatest concern



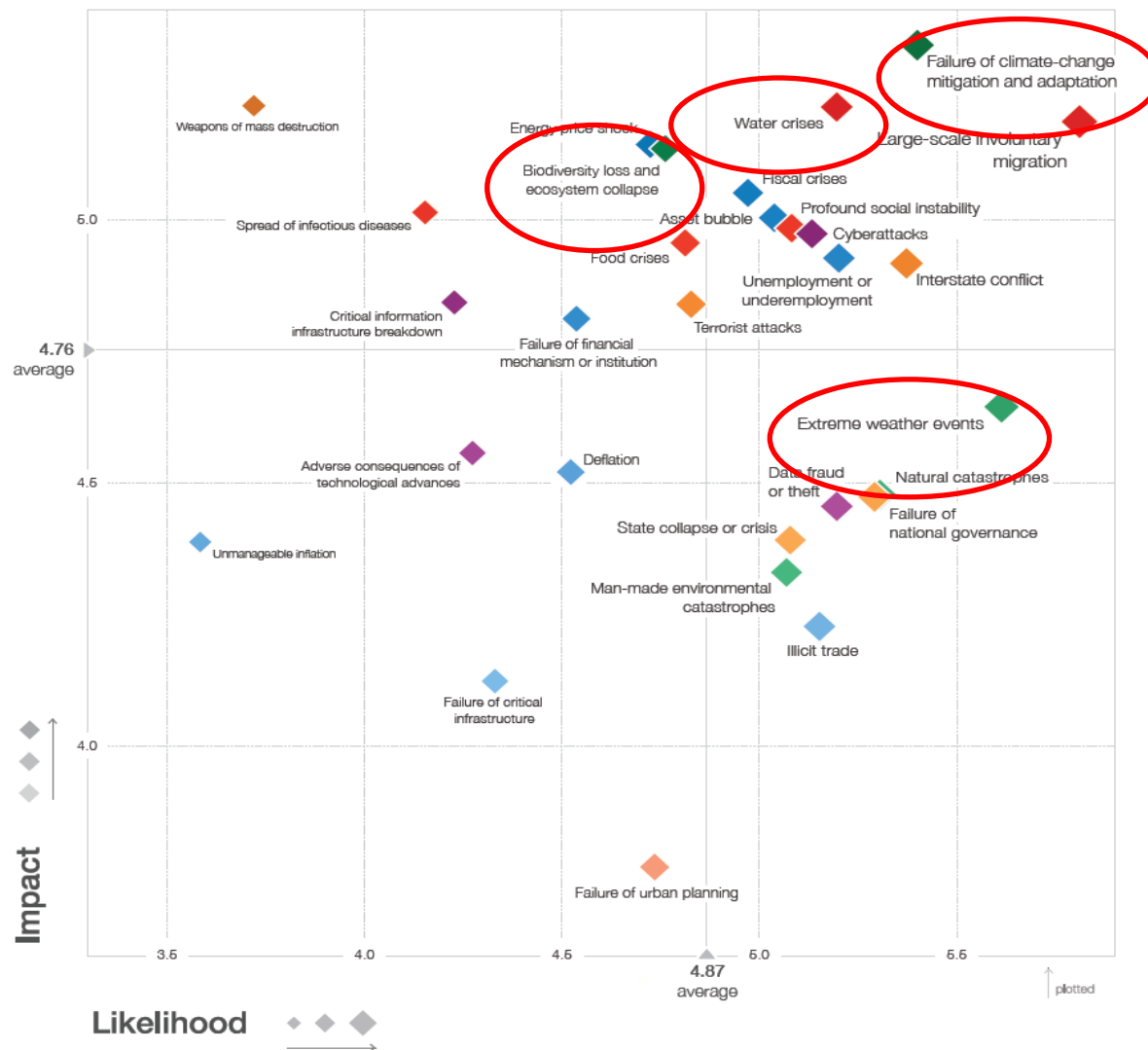
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COMMITTED TO
IMPROVING THE STATE
OF THE WORLD

Categories

- ◆ Economic
- ◆ Environmental
- ◆ Geopolitical
- ◆ Societal
- ◆ Technological



Business risks are growing

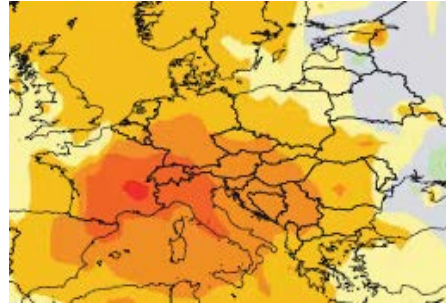


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Supply chains disrupted.

"Thailand floods result in loss of 150,000 units of production and 18% (\$200m) fall in quarterly profits at Toyota" (FT)



Assets impaired.

"French authorities forced to shut down nuclear power plants as heatwave raised river temperature and reduced flow." (UNEP)



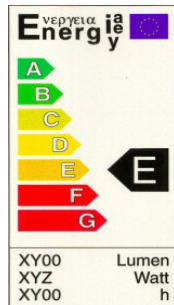
Compliance burden is rising.

"Already 40 countries require GHG reporting. 35 countries and more than 20 states or cities have carbon tax or trading schemes. (World Bank)



Projects delayed or refused licence to operate.

"Obama Administration Rejects Keystone XL Pipeline, Citing Climate Concerns" (Wall St Journal)



Products banned.

"Phased ban on the sale of incandescent lightbulbs is completed following EU directive to reduce energy use of lighting." (Europa)



Markets eroded.

"Peabody is the 50th coal company to file for bankruptcy since 2012 and a startling example of the industry's failure to anticipate how future markets might be limited by tighter environmental regulations." (Forbes)



Disclosure requirements increasing.

"With better information as a foundation, we can build a virtuous circle of better understanding of tomorrow's risks, better pricing for investors ... and a smoother transition to a lower-carbon economy." (Bank of England)



Brands tarnished.

"VW warned of consumer backlash over CO2. Some analysts say understatement of CO2 emissions could hurt car sales more than scandal over diesel pollutants." (FT)

So too are the opportunities



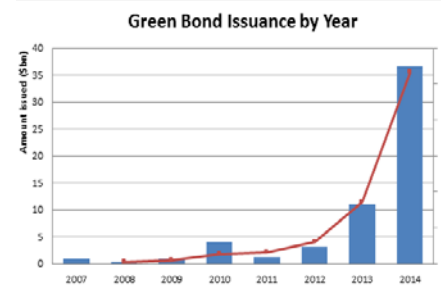
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Building resilience. “Changes to Cisco’s supply chain management, introduced following Hurricane Katrina, ensured losses from the 2011 earthquake and tsunami in Japan were minimized.” (WBCSD)



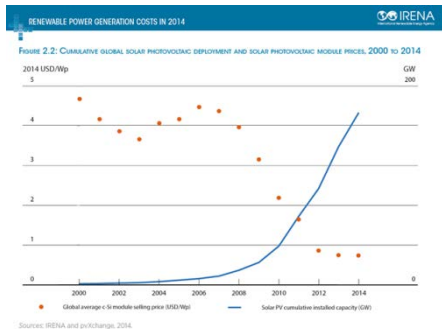
Assets developed. “Southern England...is resembling Champagne and has had several vintages of note.” (Wine Economics & Policy)



New sources of finance. Global investment in activities to reduce GHG emissions and vulnerability to climate change grew 18% to \$391 billion in 2014” (Reuters)



Cost reductions. Additional annual investments in energy efficiency of \$170 billion could generate average internal rates of return of 17%. (McKinsey)



New markets, with disruptive innovations. “Exponential growth and fourfold reduction in unit cost of solar, backed by government policies and incentives” (IRENA).



Demand for some commodities is surging. “Spot price of lithium doubles as demand for high-density energy storage set to surge” (Economist)



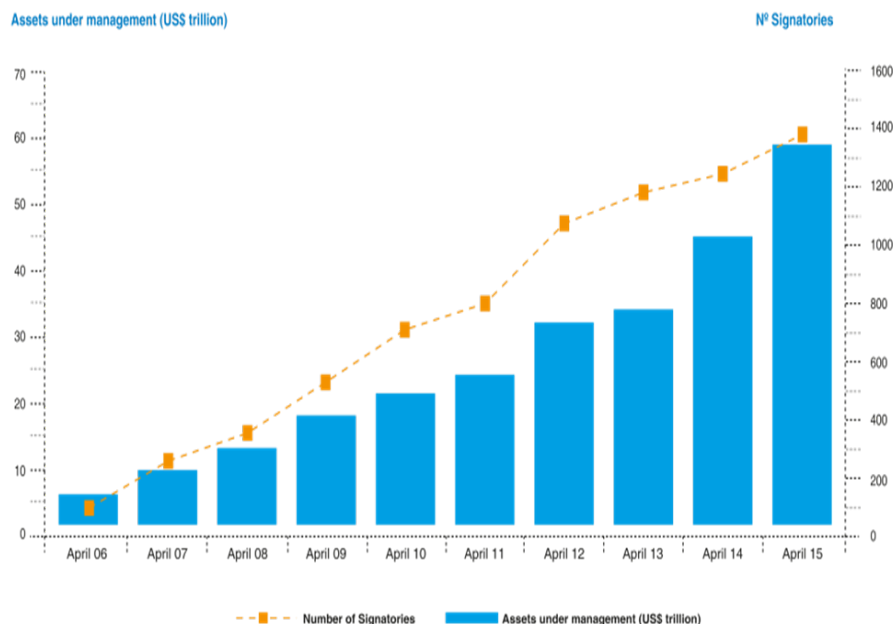
Stronger stakeholder relationships. Partnerships for climate action build engagement and reputation with key stakeholders, including employees.



Build brand trust. By responding effectively to stakeholder concerns, “McDonald’s Deforestation Plan Earns High Praise” (BrandChannel.com)

GPs are building their ESG capabilities

- Over 150 GPs have signed up to the PRI



- GP ESG progress has focussed on*
 - Enhanced firm level ESG processes
 - Technical ESG programmes
 - Product & service sustainability enhancements
- GP ESG progress enabled by*
 - Senior management buy-in
 - Inputs from ESG teams (e.g. dedicated internal ESG expertise TPG, EQT, KKR, Blackstone, Triton, Permira, etc.)
 - Operational integration

Source: <https://www.unpri.org>

* Source: ERM 2016 ESG Survey for Investors

Portfolio Companies are taking the challenge



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- 70% of investors have seen ESG issues materially impact their investments (i.e. at the portfolio company level)*
 - 60% value protection
 - 40% value creation
- Post-transaction, ESG management plans are often developed soon after deal closure
- Increased ESG disclosure requirements e.g.:
 - LP reporting requirements require robust escalation processes at PC level
 - Legal ESG disclosure requirements (e.g. Grenelle 2)
 - Listed company requirements for IPO candidate PCs

Value Creation derived from*

40%

•Margin Enhancement

30%

•Brand & Reputation

20%

•Growth

10%

•Higher Exit Multiple

What is a policy?

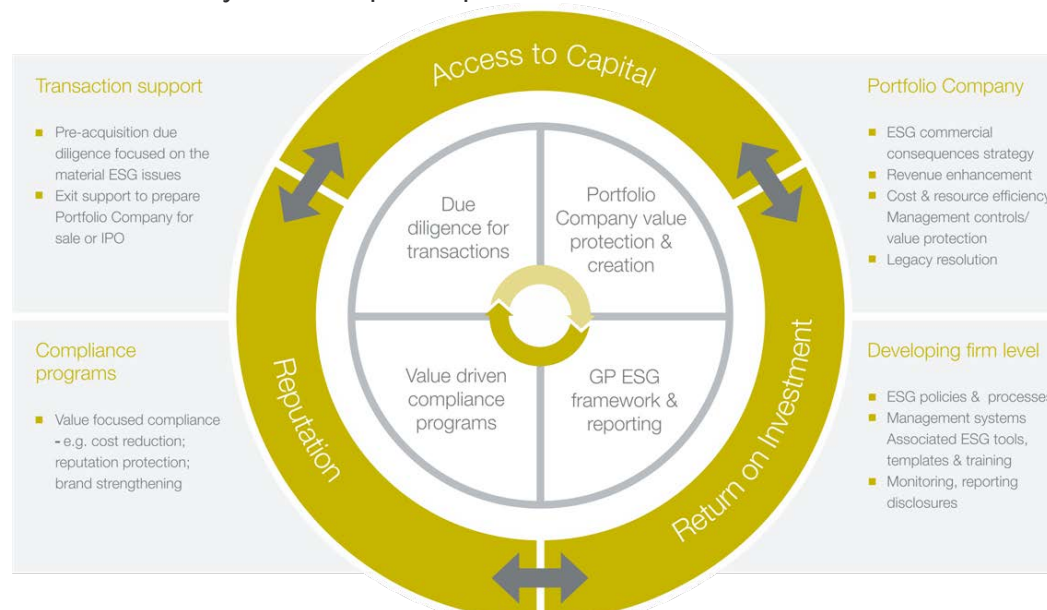


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- **Articulates commitment** to managing E&S risks, direct and indirect impact as well as integrating E&S considerations throughout PE activities for both external and internal audiences
- **Unique - there is no one size fits all.** A policy must be fit for purpose within each Private Equity (PE), its ways of working, and the E&S impacts and risks to its business

Why do you need one ?

- A crucial part of developing an **Environmental and Social Management System**
- **Aligns** public commitment with **strategic** E&S goals and objectives which may be set or revised alongside policy development, review and updates
- **Defines** the PE/GPs overall E&S commitments and ensure that those commitments are clearly communicated in a consistent manner to all relevant stakeholders i.e. portfolio companies
- **Business Imperative** for PE to minimise financial, legal and reputational risks and maximise opportunities through value creation
- **Industry best practice:** recognising the significance posed to business activities by E&S impacts and risk has become standard throughout financial industry. Not unique requirement of EBRD or other International Financial Institutions

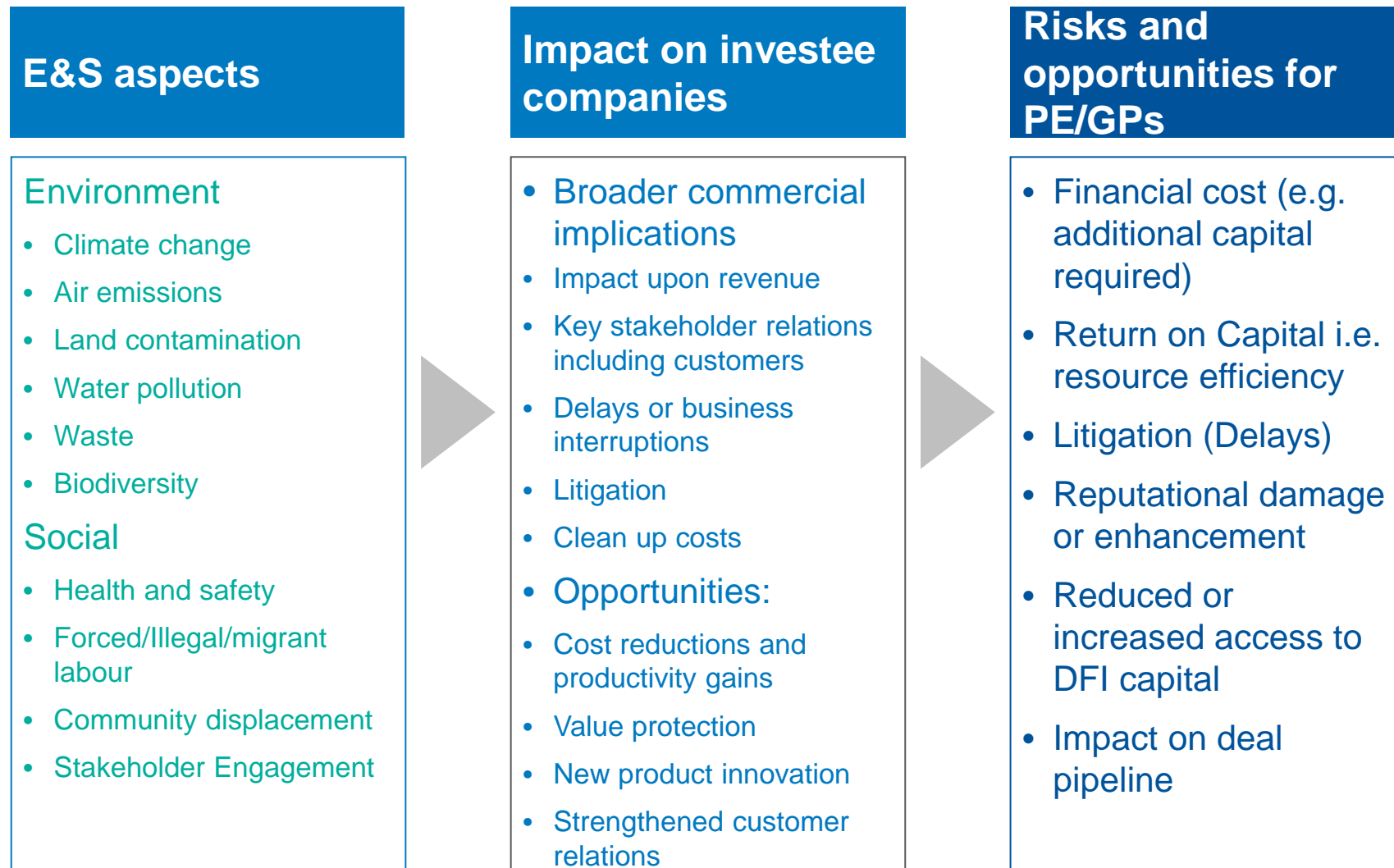


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E&S aspects have an impact on investee companies and lead to risks for PE/GPs



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An opportunity to improve performance of business

Improve business performance by reducing costs:

Environmental

- Minimise waste, re-use or recycle
- Energy efficiency/resource-efficiency
- Process efficiency – reducing emissions and raw material use

Social

- Good health and safety practices and working conditions
- Positive labour relations minimise lost production time
- Effective community engagement minimises disruption

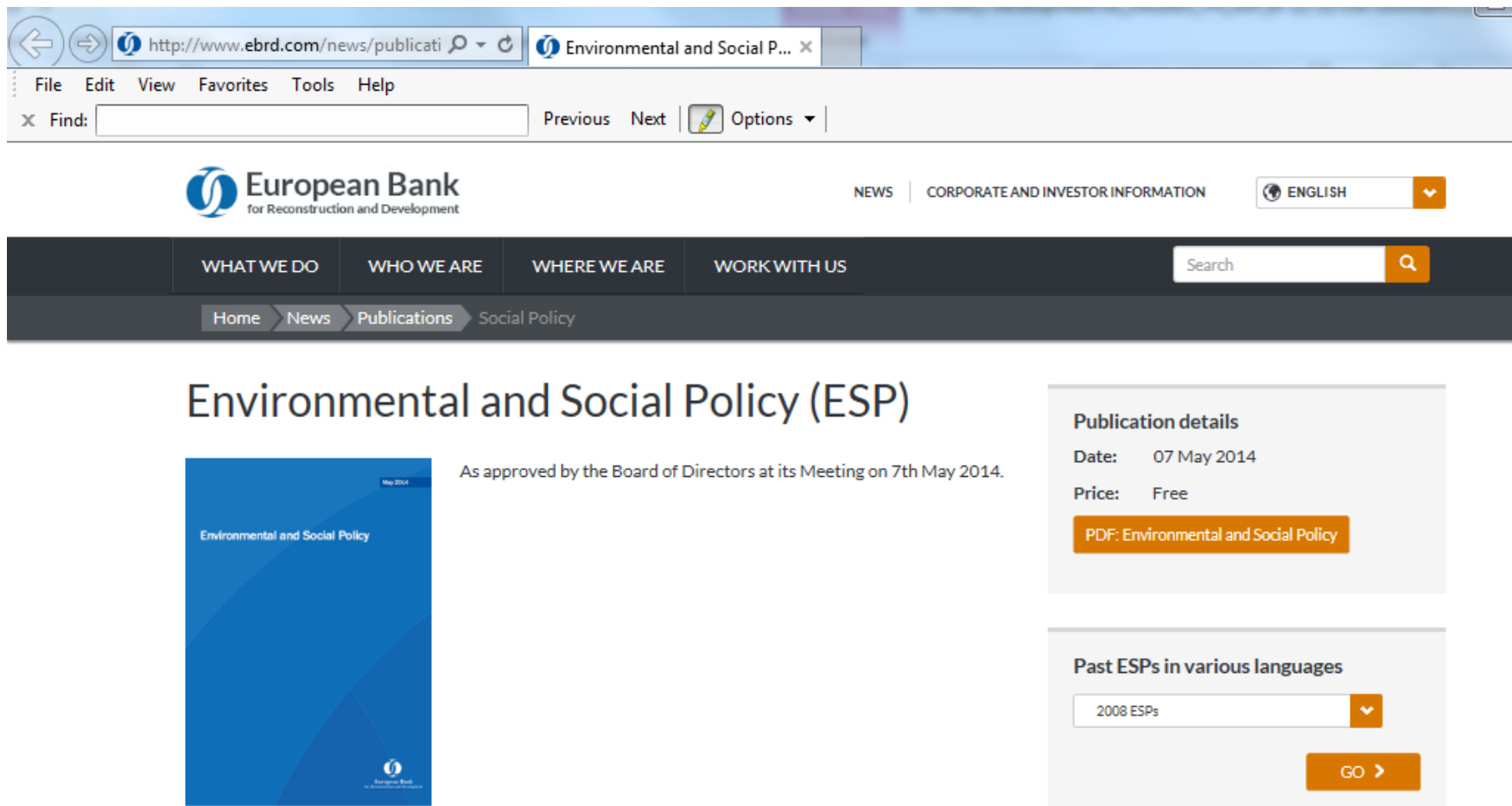


All can lead to lower compliance costs, operational savings and productivity increases

EBRD Environmental and Social Policy

The EBRD E&S Policy can be found at:

<http://www.ebrd.com/news/publications/policies/environmental-and-social-policy-esp.html>



The screenshot shows a web browser window with the URL <http://www.ebrd.com/news/publications/policies/environmental-and-social-policy-esp.html>. The browser's address bar and menu bar are visible. The website header features the EBRD logo and navigation links: NEWS, CORPORATE AND INVESTOR INFORMATION, and a language dropdown set to ENGLISH. A dark navigation bar contains links: WHAT WE DO, WHO WE ARE, WHERE WE ARE, WORK WITH US, and a search bar. Below this, a breadcrumb trail shows: Home > News > Publications > Social Policy. The main heading is "Environmental and Social Policy (ESP)". To the left is a blue cover image of the policy document, dated May 2014. To the right of the image, it states: "As approved by the Board of Directors at its Meeting on 7th May 2014." On the right side of the page, there is a "Publication details" box with the date "07 May 2014", price "Free", and a button to download the "PDF: Environmental and Social Policy". Below this is a "Past ESPs in various languages" section with a dropdown menu showing "2008 ESPs" and a "GO >" button.

Environmental and Social Policy (ESP)

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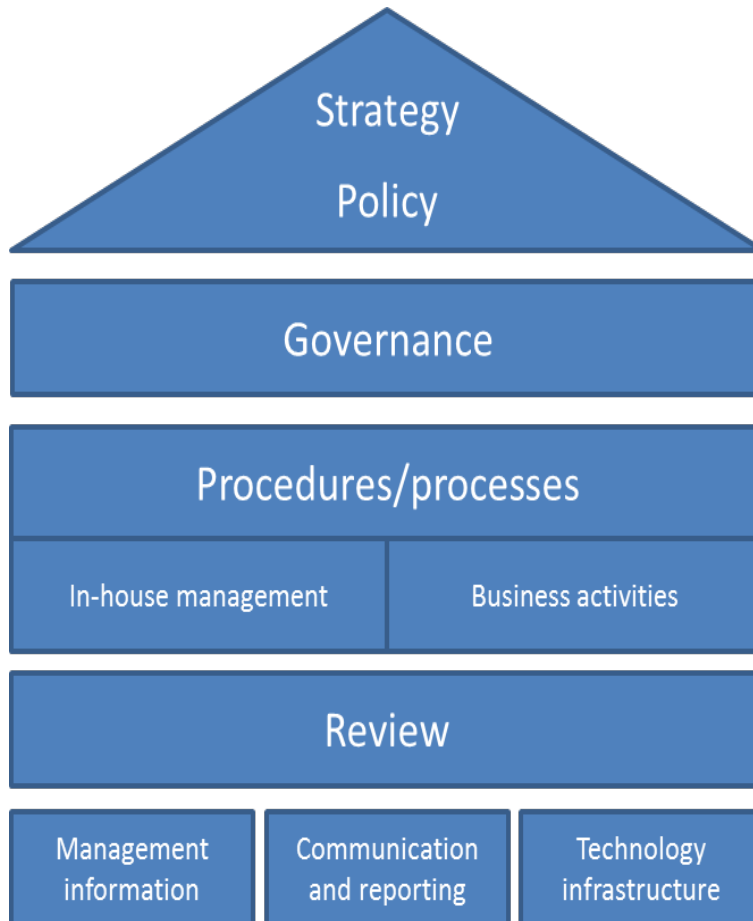
PDF: Environmental and Social Policy

Past ESPs in various languages

2008 ESPs

GO >

E&S Policy & implementation of ESMS (EBRD Performance Requirement 9)



Strategy : An ESMS should be founded on an overarching strategy that outlines the PE's overall approach to sustainability in its business. The strategy should be supported by clearly articulated strategic priorities, goals and milestones.

ES Policy : PE should develop and adopt a policy on E&S management that reflects the PE's commitment to managing these factors. The policy (or policies) should outline the PE's approach to E&S factors in its own operations as well as in its business activities

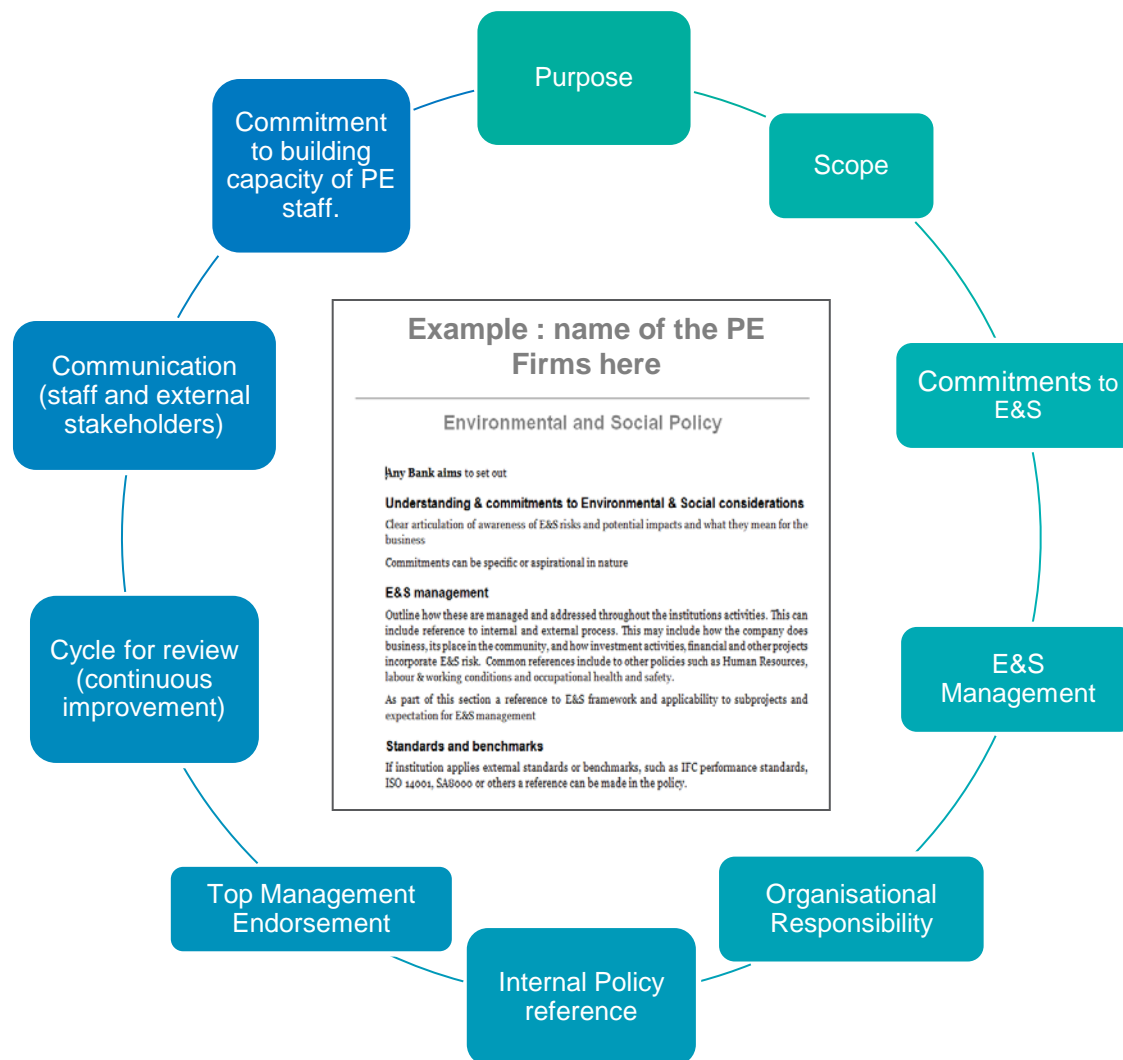
Key considerations



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Best practice elements



Select Examples:

Corcodia 21 - Poland

BaltCap - Baltic States

Meridiam - France

- **No policy template:** Good policies reflect (and are reflection of) the PEs/GPs
- **Most important element** is to convey what E&S means for the business
- **Policy not in isolation:** Document presented within company ESMS or broader sustainability/CSR disclosures
- **Style Variation:**
 - Structure and level of detail may vary depending on the organisation
 - Policy names can vary (CSR, Sustainability, sub policies dealing with Environment and Social separately)
 - Often detail is left to E&S management, process documents or other policy documents

Review of good policy examples: Concordia 21



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ABOUT US OUR PEOPLE CREATING VALUE OUR INVESTMENTS SUSTAINABILITY

An integral part of our day to day work

We are dedicated to ensuring solid governance and high standards of social and environmental responsibility in all aspects of our day to day work and our plans for further improvements.

INTEGRATED INTO OUR ORGANIZATIONAL MODEL

- Clear corporate governance
- Clear roles and responsibilities
- Clear operations and policies

INTEGRATED INTO OUR RISK MANAGEMENT

- To prevent excess exposure
- To prevent conflicts of interest
- To prevent reputational issues

INTEGRATED INTO ALL PHASES OF OUR INVESTMENT PROCESS

- Analysis of potential issues in the deal selection and due diligence phase
- Supporting sustainable growth
- Periodic monitoring

BEST PRACTICES DRAWN UP AT GROUP LEVEL AND IMPLEMENTED LOCALLY

- Dedicated, in-house responsible investment team
- Dynamic diffused by managing partners

<http://www.21concordia.com/>

Review of good policy examples: Concordia 21



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ABOUT US OUR PEOPLE CREATING VALUE OUR INVESTMENTS SUSTAINABILITY

Our process to drive responsibility across our portfolios

During its holding period, 21 works alongside management teams in order to improve performance in high priority areas, including Environmental, Social and Governance issues.

Annual monitoring is carried out in order to keep check of relevant ESG performance indicators and achievements across the portfolio. Annual monitoring is carried out in order to keep check of relevant ESG performance indicators and achievements across the portfolio. Our limited partners, the UN, the UN Global Compact and industry guidelines, can be summarized as follows.

• Strategy

Identify areas of relevance in need of improvement and fix clear objectives and action plan

• Implementation

Focus on important actions which can make a difference

• Monitoring

Periodical assessment of relevant KPIs and achievements

• Assessment and feedback

Give feedback to drive changes and create a responsible investment culture

<http://www.21concordia.com/>

Review of good policy examples: BaltCap



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BALTCAP

BALTCAP

Responsible Investment Policy

As a signatory of the United Nations Principles for Responsible Investment (UNPRI), an investor initiative in partnership with UNEP Finance and the UN Global Compact, BaltCap follows the policies and practices of responsible investment and believes that environmental, social and corporate governance ("ESG") issues play an increasing role in the long-term performance of companies.

We have incorporated our engagement in ESG issues into our investment performance analysis.

We have incorporated ESG issues in investment process and in our daily operations. We are convinced that our engagement in ESG issues is a prerequisite for a sustainable long-term operation improving the performance and attractiveness of our portfolio companies and reducing our overall exposure to risk.

Long Term Value Creation and Sustainability

The commercial and ESG issues are equally important for a long term sustainability in any organisation and when combined can provide additional value increase. The improved economic performance of the portfolio companies also contributes positively to surrounding society.

BaltCap strives to increase value in portfolio companies through improved efficiency and enhanced management placing emphasis on non-financial issues such as:

- Organizational structure
- Corporate governance
- Business model
- Corporate social responsibility
- Customer satisfaction
- Quality of products and services
- Brand strength and reputation
- Innovation
- Environment
- Social participation

We do not invest in companies engaged in arms manufacturing, manufacture of tobacco, hard spirits, gambling, human cloning and genetically modified organisms. Also we do not get involved in hostile bids.

Responsible Ownership and Investment Selection

BaltCap invests in companies with exceptional growth potential and provides them necessary tools in achieving the set targets. We carry out a rigorous evaluation of target companies, including also the ESG aspects, before making any investment and consider the findings carefully in investment decisions.

We do not invest in companies engaged in arms manufacturing, human cloning and genetically modified organisms.

BaltCap always involves key stakeholders in decision-making through board or council membership. The alignment of interest of key stakeholders (our investors, other shareholders of portfolio companies, employees, customers and community) is of utmost importance to BaltCap. When selecting co-operation partners we prefer organisations that follow CSR principles and share similar values with us.

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Ethics and Governance

BaltCap is conducting its operations in accordance with the highest legal and ethical standards and we promote the use of best corporate governance practises in our portfolio companies.

We are committed to:

- Protecting copyright and other forms of intellectual property

We make an effort to educate the local business community by sharing our experiences and knowledge.

Environment

We take our responsibility to the environment seriously and seek to adopt and implement environmentally sound policies in our portfolio companies, and in our own internal operations. All our portfolio companies need to comply with applicable environmental regulations and standards and

- Adopting new and efficient technological solutions
- Reducing the energy consumption, waste and emissions
- Fostering the adoption of environmental management system

People

People are the most valuable asset to us and our portfolio companies. The motivation and well-being of the employees is of utmost importance to us.

We remain committed to:

- Respecting human rights
- Supporting the payment of fair and competitive wages

The Responsible Investment Policy has been adopted by the management and supervisory board of BaltCap in June 2011 and is reviewed on annual basis.

Source: <http://www.baltcap.com/uploads/files/Responsible%20Investment%20Policy%20BaltCap%20June%20202011.pdf>

Review of good policy examples: Meridiam



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Meridiam Sustainable Development Charter

The objective of the Charter

- Define our commitments with regard to environmental, social and governance (ESG) responsibilities, taking into account:
 - Fundamental social rights: the Universal Declaration of Human Rights, ILO Conventions, OECD Recommendations, Global Compact, etc.
 - International principles that we endorse: the Equator Principles and the principles for Responsible Investment (PRI)
 - The investment principles of our partners: EIB, EBRD, CDC

To deliver sustainable infrastructure that improves the quality of people's lives.

Meridiam values

- Passion and commitment towards Meridiam's mission
- Team spirit
- Entrepreneurial perspective
- Integrity
- Light-hearted
- Hard-working
- Flexibility
- Multicultural awareness

ESG principles

- Sustainable and long term investment strategy in PPP infrastructure projects, ensuring stable revenues to our shareholders and investors
- Involvement in projects of general interest whose economic and social purpose has been proven, and that is respectful of the environment in order to contribute to sustainable

development of the concerned geographical areas

- Take into account our environmental and social standards
- Develop sustainable partnerships with stakeholders (public authorities, contractors, suppliers, etc.)
- Implement control measures and audits aiming at managing the main ESG risks and to integrate these in their Risk Management

Protect the environment

During the Investment process

- Ensure that the main environmental impacts are taken into account at project level
 - Prevent negative impacts on
 - Use sustainable materials
 - Contribute to the measure
 - Take into account those contractors and their res
- Favour projects with a high for example waste manage

During the Asset management process

- As a shareholder, address environmental issues and encourage our partners to implement environmental management systems in order to:

Reduce environmental impacts during the construction

During the Asset management process

- As a shareholder, ensure that the contractor is pursuing a constructive dialogue with public authorities and stakeholders concerning:

conditions concerning the construction site; safety of

Ensure compliance of Meridiam internal procedures with the Charter

- ESG performance criteria are integrated in our project selection processes
- ESG performance criteria are integrated in our Investment and Asset management activities
- Formalisation of our ESG demands towards our partners is a requirement of our procedures: commitments associated to environmental and social reporting

- Prevention of all types of discrimination and promotion of equal opportunities
- No use of child labour or of any type of illegal labour
- Acceptable working conditions: remuneration, social security, prevention of violence at work, termination provisions (local workforce)
- The promotion of health and safety in the workplace including the prevention of occupational accidents and diseases

- Promote responsible behaviour towards partners in the consortiums, and ensure that their commitments are aligned with this Charter
- Create awareness among Meridiam team members

Ensure compliance of Meridiam internal procedures with the Charter

- ESG performance criteria are integrated in our project selection processes
- ESG performance criteria are integrated in our Investment and Asset management activities

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Report on performance with the Charter

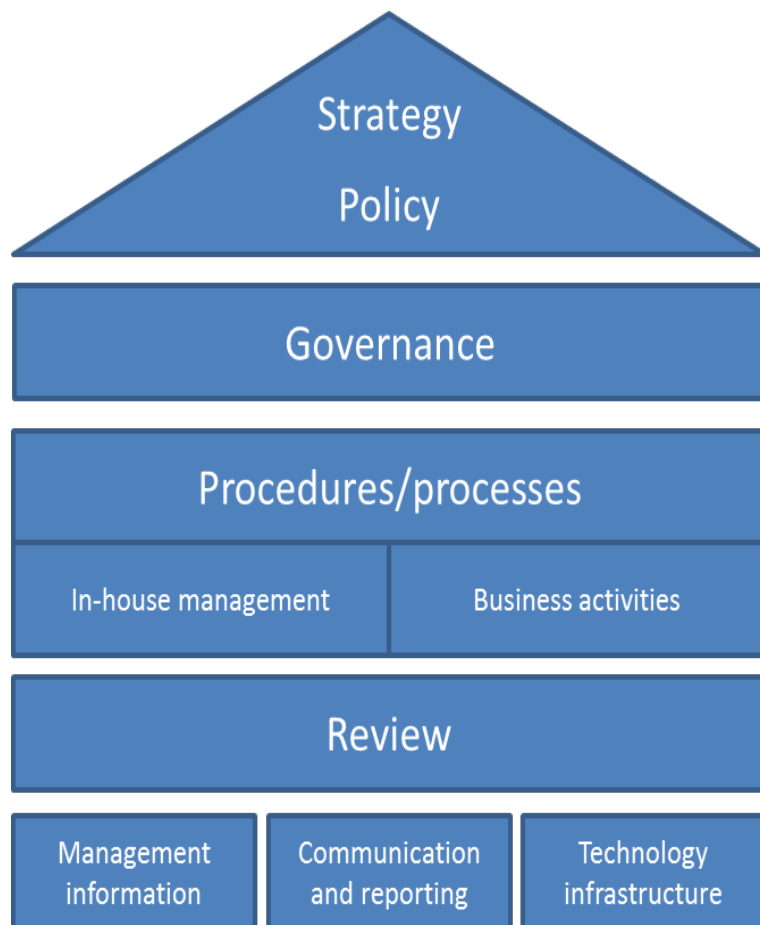
reporting specifically addressing our ESG
ances for our investors
to account these issues in our risk management

Report on performance with the Charter

- Integrate reporting specifically addressing our ESG performances for our investors
- Take into account these issues in our risk management

Source: http://www.meridiam.com/sites/default/files/pages/meridiam_rse_charte.pdf

Session Conclusion & Questions



- Each FI must create a policy that is unique to its ways of working
- Key part of developing and communicating ESMS
- The policy should be supported by senior management