

**CAIRN CAPITAL GROUP LIMITED  
 CAIRN LOAN INVESTMENTS LLP  
 CAIRN LOAN INVESTMENTS II LLP**

**ESG POLICY**

AMENDMENT NO.	DATE OF AMENDMENT	CHANGE / UPDATE TO POLICY
1	MARCH 2019	
2	SEPTEMBER 2019	Policy coverage extended to Cairn Loan Investments II LLP; update to ESG Policy Committee members.
3	MARCH 2020	Exclusionary screening criteria expanded to include nuclear weapons and cannabis for recreational purposes. Incorporates Mediobanca’s Group Policy on Responsible Lending and Investing.
4	NOVEMBER 2021	Incorporation of Bybrook Capital’s ESG approach; additional explanation of Cairn Capital’s three-pillar based ESG strategy and corporate responsibility initiatives

## TABLE OF CONTENTS

INTRODUCTION .....	2
THE IMPORTANCE OF ESG .....	2
INTERNATIONAL GUIDELINES.....	3
PRINCIPLES FOR RESPONSIBLE INVESTMENT .....	3
UN GLOBAL COMPACT .....	3
STANDARDS BOARD FOR ALTERNATIVE INVESTMENTS (SBAI) .....	4
APPROACH .....	4
MANAGER LEVEL ACTIVITIES.....	4
PORTFOLIO LEVEL ACTIVITIES AND INDUSTRY COLLABORATION .....	5
<i>Firm-wide exclusionary screening</i> .....	5
<i>ESG integration</i> .....	5
<i>Engagement</i> .....	7
<i>Training</i> .....	8
ESG TEAM .....	8
HEAD OF ESG.....	8
ESG POLICY COMMITTEE .....	8
THE BOARDS .....	8
CORPORATE RESPONSIBILITY .....	9
OUR PEOPLE .....	9
OUR COMMUNITY.....	10

OUR ENVIRONMENT .....	10
MEDIOBANCA GROUP .....	10

## INTRODUCTION

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This policy applies to all financial assets that are managed by Cairn Capital Limited, Cairn Loan Investments LLP and Cairn Loan Investments II LLP<sup>1</sup> (together referred to as “Cairn Capital” for the purposes of this document).

Cairn Capital is committed to adopting and implementing responsible investment<sup>2</sup> principles in a manner that is consistent with our fiduciary responsibilities to clients. This document specifically sets out Cairn Capital’s approach to the management of environmental, social and governance (ESG) issues, including the principles which Cairn Capital aspires to. The policy is supported by a set of procedures which have been implemented in order to integrate these principles into Cairn Capital’s activities. Cairn Capital’s commitment to responsible investment is driven by (i) the belief that ESG issues can be a source of risk and financial performance; (ii) our aspiration to contribute to society as a good corporate citizen; and (iii) our aim to meet evolving sustainability preferences of clients and investors.

Cairn Capital recognises that the management of ESG issues forms a fundamental aspect of a business’s long-term success.

A large number of Cairn Capital’s investors, especially pension funds, insurance companies and endowments, have made explicit and implicit commitments on improving ESG performance across their investment portfolios as they aim to fulfil their social mandates alongside their financial mandates. Some portfolios that are managed for a single investor have additional ESG procedures over and above the firm-wide policy.

### THE IMPORTANCE OF ESG

Considering ESG factors is an essential part of the investment decision-making process. ESG analysis may uncover unintended or mispriced risk; for example, increased regulatory scrutiny and legislative changes have substantial positive and negative impacts on financial performance. Cairn Capital believes that well-run companies tend to have better ESG credentials and generate better returns. Most importantly, improving the ESG performance of a company, in our view, creates value as it is essential for long-term sustainability and it increases the breadth and quality of the potential buyer base on exit. Sub-standard ESG performance is not a barrier to investing if the intention is to improve it via our engagement. In addition, shorting securities of companies with poor ESG performance can trigger positive change.

Often, financial considerations are cited as a reason for poor ESG performance as there tends to be an initial cost to implementing better ESG policies. The payback of an ESG strategy may take some time before which

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<sup>1</sup> Cairn Capital Limited acts as a service provider of credit research to Cairn Loan Investments LLP and Cairn Loan Investments II LLP (for numerous services including credit research).

<sup>2</sup> Responsible investment is an approach to investing that aims to incorporate environmental, social and governance (ESG) factors into investment decisions, with the aim to better manage risk and generate sustainable, long-term returns. ESG integration is the explicit and systematic inclusion of ESG factors in investment analysis and investment decisions.

the benefits are seen. The benefits may be hard to measure or be predominantly non-financial in the form of positive externalities (or fewer negative externalities). Cairn Capital believes that improvements are much more likely to occur if the investment manager community pushes for change, especially if done in a coordinated manner.

By adopting this policy, Cairn Capital formalises its approach to managing ESG issues so that these are integral to our investment process.

## **INTERNATIONAL GUIDELINES**

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### **PRINCIPLES FOR RESPONSIBLE INVESTMENT**

Cairn Capital Group Limited is a signatory to the UN-supported **Principles for Responsible Investment** (PRI). The PRI is a global, collaborative network of investors established in 2006 in recognition of the increasing relevance of ESG issues within the investment process. The Principles set forth by the PRI are a set of best practices for incorporating ESG issues into investment decision-making where consistent with fiduciary responsibilities. As a signatory, Cairn Capital Group Limited commits to the following:

1. We will incorporate ESG issues into investment analysis and decision-making processes.
2. We will be active owners and incorporate ESG issues into our ownership practices.
3. We will seek appropriate disclosure on ESG issues by the entities in which we invest.
4. We will promote acceptance and implementation of the Principles within the investment industry.
5. We will work together to enhance our effectiveness in implementing the Principles.
6. We will each report on our activities and progress towards implementing the Principles.

### **UN GLOBAL COMPACT**

Through Mediobanca S.p.A., Cairn Capital Group Limited and Cairn Capital Limited are participants to the UN Global Compact which seeks to promote responsible corporate citizenship based on the following ten principles across four focus areas.

#### **Human Rights**

Principle 1: Businesses should support and respect the protection of internationally proclaimed human rights; and

Principle 2: make sure that they are not complicit in human rights abuses.

#### **Labour**

Principle 3: Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining;

Principle 4: the elimination of all forms of forced and compulsory labour;

Principle 5: the effective abolition of child labour; and

Principle 6: the elimination of discrimination in respect of employment and occupation.

### **Environment**

Principle 7: Businesses should support a precautionary approach to environmental challenges;

Principle 8: undertake initiatives to promote greater environmental responsibility; and

Principle 9: encourage the development and diffusion of environmentally friendly technologies.

### **Anti-Corruption**

Principle 10: Businesses should work against corruption in all its forms, including extortion and bribery.

## **STANDARDS BOARD FOR ALTERNATIVE INVESTMENTS (SBAI)**

Cairn Capital Group Limited is a signatory to the SBAI and supports the SBAI standards which cover the areas of Disclosure, Valuation, Risk Management, Fund Governance and Shareholder Conduct.

## **APPROACH**

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Cairn Capital's approach is based on three pillars:

- (i) Manager level activities
- (ii) Portfolio level activities
- (iii) Industry collaboration

Cairn Capital is mindful of the fact that ESG regulation and implementation standards are constantly evolving and Cairn Capital aims to be an early adopter. As such, Cairn Capital reviews industry developments at its quarterly ESG Policy Committee meetings or on an ad-hoc basis if necessary.

### **MANAGER LEVEL ACTIVITIES**

Not only does Cairn Capital fully embrace ESG in its investing activities, but it also strives to be a socially responsible company and therefore aims to integrate sustainability into its business strategy and management. The "Corporate Social Responsibility" section below provides further details on how Cairn Capital manages the environmental, social and governance aspects of its business operations, with a specific focus on our people, our community and our environment.

Highlights of this include:

- being carbon neutral at the firm level;
- reducing our travel footprint for all our business travel by the implementation of a travel policy;
- resident in an office that is BREEAM certified that also uses electricity from renewable sources;  
and
- having in place a Diversity & Inclusion Committee.

## **PORTFOLIO LEVEL ACTIVITIES AND INDUSTRY COLLABORATION**

At the portfolio level, Cairn Capital's approach is based on (a) a negative screening/top-down approach using broad criteria to remove certain companies with specific business activities; (b) a bottom-up fundamental approach to assess an investment against asset-class specific ESG criteria; and (c) engagement with companies on ESG topics.

### **Firm-wide exclusionary screening**

Cairn Capital actively seeks to avoid investing in companies (or their affiliates, holding companies or financing subsidiaries) directly involved in the production or sale of cluster weapons<sup>3</sup>, anti-personnel landmines<sup>4</sup>, nuclear weapons, chemical weapons or biological weapons<sup>5</sup>. Cairn Capital also does not intend to invest in businesses involved in the R&D, production and distribution of cannabis for recreational uses.

This exclusion requirement (i) applies across all asset classes, irrespective of an investment's holding period; and (ii) does not apply to passive holdings in index-tracking instruments (or derivatives in them).

A client may have specific sustainability preferences and Cairn Capital can take those into account.

For example, some of our funds or accounts restrict investments in companies that derive significant revenues from thermal coal extraction. Other mandates do not invest in companies principally involved in civilian firearms, tobacco production, pornography, prostitution, payday lending and speculative oil and gas extraction, amongst others.

### **ESG integration**

Cairn Capital adopts a fundamental bottom-up approach to assess an investment against ESG metrics, alongside traditional financial analysis. This means that when evaluating possible investments in terms of the expected risk-return ratio, ESG factors are explicitly and systematically taken into account by analysts. By doing this, Cairn Capital believes it ends up with a better risk-weighted return for investments.

The actual ESG approach differs per asset class and a separate ESG Procedures document provides an overview of the practical implications of each approach. In summary:

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<sup>3</sup> A bomb, missile, rocket or shell that carries multiple explosive submunitions and disperses them over an area, causing widespread and indiscriminate harm and damage. Submunitions generally explode in the area or on impact. If they do not explode, they can be dangerous to civilians long after the weapon has been fired.

<sup>4</sup> A munition that is placed under, on or near the ground or other surface area and explodes by the presence, proximity or contact with a person or upon command by an operator from a remote location. They can cause harm for many years.

<sup>5</sup> Weapons that use pathogens such as viruses, bacteria and disease-causing biological agents, toxins or chemical substances that have toxic properties that kill, injure or incapacitate.

- For leveraged loans, credit analysts systematically integrate ESG factors into the investment process and there is a dedicated ESG section in each investment memo. In addition, the Loans team assigns an ESG score to each corporate borrower in the portfolio.
- For special situations and distressed assets, the approach depends on the level of influence embedded in the investment. For control and high influence positions, Cairn Capital seeks to influence ESG performance to unlock potential value. For passive positions, Cairn Capital aligns with management's existing ESG agenda as a value driver.

#### *Fundamental in-house research*

Through Cairn Capital's internal research process, analysts seek to understand how companies perform on key ESG issues and how companies manage them (and if data is available, how this compares versus peers and how this has changed over time). ESG issues are taken into account, when they are considered to be material or directly relevant to the entity in question.

Whilst the Head of ESG assists the analysts in determining the most relevant ESG metrics for each asset class, the responsibility for identifying (and monitoring) material ESG considerations for each investment lies with the analyst.

With regards to **environmental factors**, the aim is to understand environmental risk (and opportunities) facing the company and the potential impact from this on its operational performance, competitiveness and reputation; for this purpose, analysts may look into how the company manages and reports on emissions, water, energy, waste and other metrics.

With respect to **social factors**, the purpose is to evaluate the management of issues such as labour, health and safety and community relations and understand potential reputational or litigation risk from any mismanagement.

On **corporate governance**, the objective is to identify issues and analyse risks relating to the organisation of the company.

#### *External research*

Cairn Capital has engaged the services of MSCI ESG Research LLC to complement internal ESG assessments on companies. MSCI ESG provides ESG ratings and research on ESG-related business practices of companies. The ESG ratings are industry specific and are calculated relative to industry peers and analysts use these ratings in conjunction with their wider analysis.

For leveraged loans for example, if the issuer/relevant counterparty is rated by MSCI ESG, the rating is (i) included in the credit memo which forms part of the investment decision and (ii) discussed in the Investment Committee. The responsibility lies with the analyst.

For some issuers, there is no coverage from MSCI ESG and, in these instances, the Investment Committee relies on the analyst's assessment alone.

In addition, analysts have access to sell-side ESG research, credit rating agency ESG research and expert knowledge from the third-party consultants we work with, such as ClimatePartner UK Limited.

## **Engagement<sup>6</sup>**

Cairn Capital believes it has a responsibility towards society to endeavour to influence the companies it invests in, or provides financing to, to act in a responsible manner. Engagement on ESG topics forms an integral part of Cairn Capital's investment process. Cairn Capital takes two approaches in engagement: bilateral engagement and collaborative engagement.

### *Bilateral engagement*

For Cairn Capital's leveraged loans business, as debt holders, Cairn Capital can stimulate dialogue with issuers on strategy, risk and any specific ESG issues. For example, analysts can engage directly with the company in the run-up to new issuance or raise issues with the loan sponsor. During this process, analysts share their concerns or the ESG risks that are identified for the company. The objective is to encourage companies to improve their practices and maintain a long-term direct dialogue. Cairn Capital also encourages companies to address ESG issues as part of their annual financial reporting.

For special situations and distressed assets, the approach depends on the level of influence embedded in the investment. For control and high influence positions, Cairn Capital engages with companies at the board level to drive ESG performance. Annual ESG performance targets are set. For passive positions, although Cairn Capital will strive to drive ESG, our inputs are recommendations that are reviewed annually. For debt positions, we communicate to companies the importance of ESG topics and encourage companies to measure and improve their ESG performance.

### *Collaborative engagement*

Apart from bilateral engagement, Cairn Capital also strongly believes in collaborative engagement with like-minded peers. Cairn Capital can make a more significant impact collectively with other investors rather than individually. For example, Cairn Capital works closely with the PRI and the European Leveraged Finance Association (ELFA) to facilitate engagement between investors and corporate borrowers on important ESG topics.

Cairn Capital is also an active member of the PRI Structured Products Advisory Committee, which advises the PRI on its programme to identify how ESG factors are considered in structured products, enabling collaboration for change and impact.

The ELFA is a professional trade association representing the European leveraged finance investor community. Cairn Capital's Head of ESG has been involved in the ELFA's ESG disclosure initiative in her role as co-Chair of the ELFA ESG Committee.

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<sup>6</sup> Engagement refers to interactions between the investor and current/potential investees on ESG issues. Engagements are undertaken to influence (or identify the need to influence) ESG practices and/or improve ESG disclosure.

Cairn Capital is also a member of the Alternative Investment Management Association (AIMA) and SBAI ESG Working Groups. The aim of these working groups is to promote ESG integration and ESG disclosure in the alternative investment market.

### **Training**

All members of the investment team have a thorough understanding of Cairn Capital's ESG policy and ESG approach. The investment team receives an update whenever there is a significant policy update and following each ESG Policy Committee meeting. Additional ESG training where required is organised by our Head of ESG or MSCI ESG Research LLC, for example, to update the team on sector or regulatory developments.

## **ESG TEAM**

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### **HEAD OF ESG**

Tina De Baere, as Head of ESG, is responsible for the development and implementation of the ESG policy. Tina works closely with the investment team in integrating ESG factors into the investment process. Tina monitors compliance and consistency with the ESG policy across Cairn Capital's investment platform and gets ad hoc support from the ESG Policy Committee.

### **ESG POLICY COMMITTEE**

The ESG Policy Committee comprises senior executives from across Cairn Capital's business, including Andrew Burke (CIO Leveraged Finance), Graham Murphy (CRO) and Christian Herrmann (senior credit analyst). Members of the investment team, business development, investor relations, legal and compliance teams also frequently attend. The ESG Policy Committee meets at least quarterly to review the ESG policy and to discuss further enhancements to the ESG framework. ESG concerns on specific issuers are discussed in the Investment Committee.

### **THE BOARDS**

The boards of Cairn Capital Limited and Cairn Capital Group Limited and the partnership boards of Cairn Loan Investments LLP and Cairn Loan Investments II LLP have reviewed this policy. Any further updates to the policy will be subject to their review.

Any progress on ESG and any policy updates are discussed in each board meeting. The Head of ESG prepares an ESG statement ahead of the meeting.

## CORPORATE RESPONSIBILITY

Not only does Cairn Capital fully embrace ESG in its investing activities, but it also strives to be a socially responsible company. The below provides an overview of how Cairn Capital manages the environmental, social and governance aspects of its business operations, focusing on our people, our community and our environment.

### OUR PEOPLE

**Employee wellbeing** Cairn Capital provides good employment conditions and a safe and healthy workplace. Cairn Capital promotes a healthy work-life balance and provides employees with physical and mental health benefits, such as access to virtual/local exercise classes and access to Unmind. Unmind is an independent digital platform that supports mental health and wellbeing, providing tools to manage stress, improve sleep and focus, amongst others. Cairn Capital offers flexible working arrangements, private health insurance, ample holiday allowance and generous maternity leave and shared parental leave packages.

Cairn Capital provides equal opportunities and protection against any discrimination.

**Diversity & Inclusion (D&I)** Cairn Capital strives for diversity and inclusion within its workforce and company management. Cairn Capital’s D&I objective is to uphold and encourage a company culture that seeks and values diverse backgrounds, perspectives and ideas. Cairn Capital aims to create an inclusive environment built on trust, respect and integrity, where people can be themselves and maximise their potential. It strongly believes that this will lead to enhanced collaboration, engagement and decision-making, yielding better results for the firm and its investors.

Cairn Capital’s D&I Committee advises the Executive Management Committee on its D&I strategy and helps it implement identified initiatives. The strategy is reviewed annually to measure progress and establish new objectives for the upcoming year. In 2021, the focus is on two broad themes, racial and gender equality, (these are expected to remain the themes in 2022 but are subject to change) with the aim to drive change in the following three areas:

Priorities to drive change	2021-2022 Initiatives
 <p>Increase hiring and promotion</p>	<ul style="list-style-type: none"> <li>• Conduct staff engagement survey and collect D&amp;I statistics</li> <li>• Enhance current recruitment process</li> <li>• Increase % of women and BAME recruits</li> </ul>
 <p>Train and educate</p>	<ul style="list-style-type: none"> <li>• Raise awareness by sharing information with staff frequently</li> <li>• Invite external speakers on D&amp;I topics</li> <li>• Consider staff training needs</li> </ul>
 <p>Initiatives to promote inclusion</p>	<ul style="list-style-type: none"> <li>• Celebrate and raise awareness of important religious and cultural holidays</li> <li>• Organise team-building days</li> <li>• Encourage employees to be more actively involved with the D&amp;I Committee’s work</li> </ul>

One of the first D&I initiatives from the D&I Committee was to conduct an employee D&I engagement survey run by an external consultant, Pearn Kandola, to improve the firm's understanding of diversity and inclusion within the organisation. The survey received a strong employee participation rate of 82%.

## OUR COMMUNITY

**Charitable donations** Cairn Capital supports various charities and community initiatives, e.g. employees participate in the annual Save the Children Christmas Jumper Day.

**Volunteering** Cairn Capital encourages employees to take two days off each year to volunteer at a charity.

## OUR ENVIRONMENT

**Environmental footprint** In 2019, Cairn Capital removed all plastic water bottles from its office and replaced them with refillable glass bottles. Visitors are now offered water from glass bottles. In 2020, the company moved to an office that is BREEAM certified. The building also uses electricity from renewable sources. In 2021, we engaged ClimatePartner UK Limited to measure the firm's carbon footprint and to assist in achieving carbon neutrality at the firm level.

**Business travel** Cairn Capital aims to reduce its travel footprint for all its business travel.

Travel is one of the business' principal sources of carbon emissions. Whilst travel can have numerous advantages in terms of reaching our investors, exchanging ideas and improving partnerships with peers, service providers and other stakeholders, the environmental impact of travel needs to be recognised and considered. Before making travel plans, employees are asked to consider the use of videoconferencing. Employees are made aware of the environmental impact of travel. When travel is unavoidable, staff are encouraged to minimise the overall number of journeys taken on behalf of the company. Public transport is preferred over private taxis/cars. Rail travel is encouraged over air travel. Cairn Capital is committed to offsetting the estimated carbon footprint of any business travel using a carbon offset scheme, such as the Gold Standard.

## MEDIOBANCA GROUP

Cairn Capital's ESG approach is aligned with [Mediobanca's Group ESG Policy](#), designed to promote sustainable development by integrating ESG criteria into the Group's business model.