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Sustainability Risk Policy (ESG)

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Policy objective
The environmental, social, and governance ('ESG') sustainability risk policy describes the consideration of non-financial criteria in selecting and managing assets in managed portfolios. This policy also sets out Isatis Capital's position on considering principal adverse impacts (PAI) regarding sustainability. As a reminder, Isatis Capital has had an ESG policy since 2018. It describes the integration of ESG criteria into the investment decision process. It has been amended and supplemented to consider regulatory developments in this area. Isatis Capital also has an internal environmental, social, and governance ('ESG') sustainability risk procedure setting out the practical arrangements for implementing this policy.

I. OUR PHILOSOPHY

1.1. Our convictions and objectives

Isatis Capital specialises in growth capital investment. Its teams fund and support growing, innovating French small and medium-sized enterprises ('SME') that are profitable at the time of investment and often already developed internationally or aiming to be. Our objective is to offer our long-term investor clients high-quality, high-performance products that contribute to France's economic growth with environmental impacts in line with the principles of the Paris Agreement and social impacts in line with the principles of international labour law and human rights.

By financing the real economy, we contribute socially, environmentally, and financially to sustainable value creation. We also have a responsibility to invest in the fight against climate change as defined in the Paris Agreement.

Our investment philosophy is based on the belief that considering environmental, social, and governance (ESG) issues is essential to creating sustainable value and performance for the businesses in which we invest.

Integrating environmental, social, and governance criteria into our analyses improves our knowledge of the business by identifying sustainability risks as well as market and competitiveness opportunities that may impact the business's valuation.

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The identification of ESG risks, in particular those associated with global warming, potentially affecting the SME's future development or presenting externalities creating adverse environmental, social, or societal impacts, allows us to raise the business's awareness of these issues, better control its risks, and better anticipate and reduce the costs involved.

ESG analysis is not just about risk. It also provides an opportunity for SMEs to develop new products or services that are more respectful of the environment and human resources, create new markets, and attract new talent. Isatis Capital is making every effort to move in this direction.

1.2. Our commitments

In support of these convictions, Isatis Capital has created an ESG Charter setting out our ESG commitments, available on our website.

Isatis Capital also supports the following initiatives:

- Principles for Responsible Investment (PRI): since 2018, Isatis Capital has been committed to respecting, promoting, and communicating the six United Nations Principles for Responsible Investment:

1. *We will incorporate ESG issues into the investment analysis and decision processes.*
2. *We will be active investors and incorporate ESG issues into our shareholder policies and 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 among the asset management community.*
5. *We will work together to increase our effectiveness in implementing the Principles.*
6. *We will each report on our activities and progress towards implementing the Principles.*

- *Excluded sectors:* we exclude those sectors defined in our Exclusion Policy[1] that we believe have direct or indirect adverse impacts on environmental, social, and governance issues.

- *Task Force on Climate-related Financial Disclosures (TCFD) recommendations:* since April 2021, we have strived to take into account the TCFD recommendations for identifying, managing, and addressing climate factors in structuring governance, strategy, risk management, and the metrics used.

- International Climate Initiative (ICI): in December 2021, Isatis Capital also joined the International Climate Initiative (ICI), originally called 'Initiative Climat 2020', a French project launched in 2015 in France and now supported by the UN PRI as a way to bring together and mobilise private equity players wishing to make a concrete contribution to the fight against climate change.

[1] Isatis Capital's Exclusion Policy is available on the website.

II. FRAMEWORK, OBJECTIVE, AND KEY DEFINITIONS

2.1. Regulatory framework

This policy also meets the transparency requirements of Regulation (EU) 2019/2088 ('Disclosures' or 'SFDR') on disclosures about the integration of sustainability risks in the financial services sector into the investment decision process, as well as the requirements of Article 29 of the Energy/Climate Law on disclosures on risks associated with climate change and biodiversity risks.

This policy aims to increase transparency on how Isatis Capital integrates relevant sustainability risks into the investment decision process and how it incorporates principal adverse impacts in terms of sustainability.

2.2. Key definitions

- **Sustainability risk:** any environmental, social, or governance event or situation that, if it occurs, could have a real or potential adverse impact on the value of the investment. Such an event or situation may also lead to a change in the fund's investment strategy, including the exclusion of securities of certain issuers. More specifically, the adverse effects of sustainability risks can affect the issuers through a series of mechanisms, including 1) a drop in revenues; 2) higher costs; 3) damages or asset impairment; 4) a higher cost of capital; and 5) fines or regulatory risks. Due to the nature of sustainability risks and specific issues, such as climate change, the probability of sustainability risks impacting the returns from financial products is likely to increase in the longer term.

- **Environmental risks:**

  - ✓ **Physical risks:** these are risks resulting from damage directly caused by weather and climate phenomena, such as:
    - The loss of value of investments held by managed portfolios and issued by entities affected by these climate events;
    - The increase in the frequency and cost of claims to be paid to policyholders by insurers;

    Risks relating to climate change or biodiversity loss also fall under this definition of physical risks.

  - ✓ **Environmental transition risks:** these are risks resulting from adjustments made for transition, such as exposure to the changes brought about by the ecological transition, in particular the environmental objectives defined by the Taxonomy Regulation, especially when they are poorly anticipated or occur suddenly.
    These risks are associated with, for example:

- Impairment of assets following regulatory changes penalising or even prohibiting certain activities deemed to emit too much greenhouse gas (GHG).
- Losses following the end of certain funded activities considered to generate excessive pollution or GHG emissions.

✓ Legal and reputational risks: risks relating to the financial impacts of compensation claims from funded companies by those having suffered damage due to climate change, such as:
- Investments that fund the development of industries and activities generating pollution or significant GHG emissions;
- Professional, operator liability, and infrastructure construction insurance.

➢ Social risks: these are risks relating to the business's relationship with each of its stakeholders (employees, clients, suppliers, and civil society). In particular, these include employee health and safety protection, anti-discrimination, employee welfare, and respect for human rights.

➢ Governance risks: risks relating to the competence of the business's management team, business ethics, corporate social responsibility ('CSR') commitments, the pay structure or its legitimacy, the existence of checks and balances (composition of boards of directors, adequacy of directors' profiles with the business's needs, their independence, and respect for minority shareholders).

➢ Principal adverse impacts ('PAI'): these are impacts of investment decisions that result in significant or likely adverse effects on sustainability factors (environmental, social, and labour issues, respect for human rights, and anti-corruption/bribery).

III. IDENTIFICATION AND MONITORING OF SUSTAINABILITY RISKS

3.1. Activities concerned

Isatis Capital applies this policy to its entire Alternative Investment Fund ('AIF') management business, integrating its ESG approach at every stage of the investment process.

Through its funds, Isatis Capital establishes a growth capital strategy for growing, innovative SMEs, often already established internationally. The process of identifying and monitoring sustainability risks presented below therefore refers to our core business: our unlisted investments.

With regard to our funds' listed investments, which remain incidental and limited mainly to regulatory liquidity constraints, a dedicated section below describes our approach.

3.2. Main sustainability risks identified

Sustainability factors may significantly impact the value of assets in the portfolio and therefore the AIF valuation.

In connection with our growth capital activity, we have identified four dimensions of priority issues presented below.

It should be noted that these general sustainability risks must be broken down and adapted for each investment to take each one's distinctive characteristics into account.

➢ GOVERNANCE

Governance structure and operational bodies:

- Typology, structure, and functioning of the board
- Diversity within governance bodies
- Functioning of operational management
- Shareholding structure

CSR strategy and awareness of ESG issues among the business's leaders

Our objective is to align the governance of the businesses with the profession's standards while taking the specific characteristics of our universe of very small enterprises into account.

To conduct our analysis and identify needs and areas for improvement, we have a 'Due Diligence' questionnaire.

The main areas in which we act to help businesses are:

- Establishment of a written operating policy (regularity of meetings, written meeting minutes, and agenda sent to the directors for validation).
- The composition of the Board or committees is analysed from the perspective of member competence for future development thanks to our injection of capital. We encourage the appointment of an independent director whose experience can be an asset for the future development of the business and make them aware of the need to increase the proportion of women on the Board and/or committees.
- In addition, we wish to have corporate social responsibility issues reviewed at the highest level.

➢ HUMAN AND SOCIAL CAPITAL

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Training, skills development, and talent retention

Diversity and equal opportunities

Work/life balance and general employee well-being

Employee health and safety

Multi-generational work environment

We believe that well-being at work is a key factor in the business's performance. It is particularly crucial in certain sectors, such as IT services, software, and digital, to attract and retain the right skills and talent.

To conduct our analysis and identify needs and areas for improvement, we have two questionnaires: 'Due Diligence', sent upon acquisition, and 'Annual KPI Review', sent every year.

Our main focuses include the following:

- A human resources development policy: employee satisfaction and talent retention/appeal are two important criteria. The measurement tools we use to analyse them include the staff turnover rate, the type of employment contracts (permanent/temporary), the use of trainees and temporary workers, training, remuneration and career development policy, and absenteeism.
- An adequate age pyramid for its future development: this is particularly important in the IT, software, and digital services sectors, where the competitiveness in recruiting competent people is significant and costly and can hamper growth.
- A non-discrimination and gender pay equity policy.

➢ ENVIRONMENT

Environmental strategy to combat pollution and global warming

Transition to a greener economy

Waste management

Water consumption

Exposure and ability to adapt to risks relating to climate change and biodiversity loss

The environment is addressed from two angles.

✓ Sectoral: we invest in sectors with relatively low greenhouse gas emissions and low pollution. We exclude highly polluting sectors, such as coal and mineral extraction[2].

[2] Please refer to our Exclusion Policy on our website for all the sector-based exclusions applied.

- ✓ At the candidate business level: our analysis focuses on the environmental impact at two levels:

  - Activity on global warming, pollution, and biodiversity (physical risks relating to global warming). We verify whether the business has taken actions to reduce greenhouse gas emissions, energy consumption, water consumption, and waste management.

  - Products and/or services (eco-design, life cycle, and environmental impact of products or services): we verify whether the business implements solutions to reduce the adverse impact of its products or services through innovation, packaging management, etc.

➢ STAKEHOLDERS

Supplier relations and responsible purchasing

Client relations

Environmental and social risks do not stop at the business's doorstep.

It is important for the business to include environmental and social criteria when choosing its suppliers. In addition, we verify whether the percentage of suppliers is significant in countries showing little respect for environmental, social, and business ethics principles.

We also believe that client satisfaction is fundamental to the business's long-term performance. Using our questionnaire, we seek to identify the actions taken by the business to measure (survey) and improve (quality certification, etc.) client satisfaction.

3.3. Monitoring of sustainability risks: a policy integrated into the investment process

The entire management team is involved in considering ESG criteria. We believe that the best way to successfully guide businesses on the road to progress in taking ESG issues into account is to actively involve the Investment Directors, who are the primary contacts of the businesses they monitor. The instructional aspect is strong and based on a constructive, trusting relationship with the business leaders. We also believe that it is essential for the ESG integration process to be designed and implemented with the Investment Directors to ensure that its formalisation is relevant to our specific universe of SMEs.

The place of ESG is important from the beginning of the investment decision process. Before we commit to a business on a long-term basis, we must be reassured about the ESG sustainability risks. This begins with selecting sectors with relatively low environmental externalities (new information and communication technologies (NICT), business services, health, and high-tech industry).

The failure of the business we analyse to consider ESG issues during the due diligence phase is not a reason to abandon our investment. Nevertheless, before our final investment decision, we confirm certain key points:

- The business model of the analysed business must not be based on operating in the controversial sectors identified in Isatis Capital's Exclusion Policy.
- The business leaders' agreement to Isatis Capital's support role in the future development of their business, within the limits of their tools and powers. This also means respecting good governance rules, respecting human resources, and applying an environmentally friendly policy. This agreement also covers transparency on sustainability risks.

Isatis Capital sends an annual questionnaire to all its portfolio companies to monitor the progress of the various actions implemented or to improve weak points.

The questionnaire, presented in the appendix and reviewed annually, is structured around quantitative and qualitative indicators, allowing the evolution of ESG issues within the entity to be monitored.

Non-financial factors must also be discussed by the governance bodies of the portfolio companies at least twice a year.

Isatis Capital's medium-term objective is to assess the actions taken to reduce the adverse impacts of the business's activities and products and to enhance it, taking financial and non-financial aspects into account.

3.4. Methodological limitations

As a reminder, our investment universe consists of growing, innovative small enterprises (5 to 70 million euros in revenue) that are profitable at the time of the investment and already established internationally or aiming to be.

Isatis Capital's ambition is to help its investee businesses initiate or advance their CSR approach, including tools to measure the implemented actions, within the limits of its tools and powers. To this end, Isatis Capital includes a specific ESG clause in the equity interest contract to make businesses more aware of sustainability risks and monitor their impacts on their activities.

However, their business's management and development strongly mobilise our portfolio companies' managerial teams in terms of both operational actions and strategic structuring or thinking. This makes it difficult for management to find specific time for a formalised CSR approach or to improve the tools for measuring environmental and social impacts. The management teams are often small, and in the vast majority of cases, there is no CSR manager or human resources director (HRD). In addition, the challenge of recruiting and retaining talent is very substantial, particularly in the IT Services, Software, and Digital Technology sector, which accounts for a significant share of our investments.

3.5. Listed investments

To ensure the liquidity of its funds, Isatis Capital invests in equities or listed funds on an ancillary basis. For this type of investment, Isatis Capital only ensures that its exclusion policy is respected.

IV. PRINCIPAL ADVERSE IMPACTS

Isatis Capital applies a growth capital strategy for growing, innovative French SMEs, often already established internationally or aiming to be. The operations that we fund are mainly as a minority shareholder and are intended to fund the organic development or external growth of these businesses.

Isatis Capital considers sustainability issues and adverse impacts once it has identified the investment opportunity, starting from the first contact with the business. However, the failure of the business we analyse to consider these factors during the due diligence phase is not a reason to abandon our investment.

Given the characteristics of the businesses described above, it may be difficult to develop formalised tools to manage adverse impacts. At this stage, Isatis Capital does not systematically incorporate all the mandatory indicators required by Annex 1 of the Regulatory Technical Standards (RTS) of the SFDR when a portfolio management company considers the principal adverse impacts (PAI).

However, we reserve the right to move towards considering these impacts as soon as our internal organisation allows and the underlying data flow is in place.

Furthermore, although the formalisation of a quantitative monitoring tool is under development, Isatis Capital already help the management of portfolio companies identify the main ESG issues and any significant adverse impacts. The support actions take Isatis Capital’s ownership structure (majority or minority) into account and aim to improve the business’s ESG practices, among other objectives.

V. POLICY REVIEW

Isatis Capital’s management committee and head of compliance and internal control review this policy at least annually.

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