ECO.BUSINESS FUND

Sustainability-related disclosure: statement on integration of sustainability risks

Introduction

This statement is published by the eco.business Fund (EBF, "the Fund") on its website in accordance with Article 3 of Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services sector (SFDR, "the Regulation"). Its purpose is to provide transparency on the Fund's policies for integrating sustainability risks into its investment decision-making process. 'Sustainability risk' as defined by the Regulation means 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. Other documents that are related to this statement include:

- EBF statement on adverse sustainability impacts (March 2021) in accordance with Article 4 of the Regulation
- EBF statement on the promotion of sustainable investment objectives (March 2021) in accordance with Article 10 of the Regulation
- EBF Environmental & Social Policies
- Other periodic reports, fact sheets and information published on the EBF website

This statement is made on 9th March 2021 in reference to the calendar year 2020.

Sustainability risks are defined as an overarching risk of environmental, social or governance events or conditions which have or can have significant negative impacts on the assets, financial and earnings situation, or reputation of the Fund. EBF's risk management processes (particularly in relation to credit risk management) incorporate – or are closely integrated with – the evaluation, ongoing monitoring and control of sustainability risks to ensure proper assessment of the risk profile of the counterparties.

Sustainability risks are also addressed within the overall framework of reputational, legal and ESG risk management, benefiting from the Fund's strong focus on delivering positive environmental and social impact and supporting good governance practices of the investees.

Context

The eco.business Fund (EBF) is an impact investment fund that aims to promote business and consumption practices that contribute to biodiversity conservation, to the sustainable use of natural resources and to mitigate climate change and adapt to its impacts. The investment strategy of the Fund focuses on providing debt financing to financial and real sector intermediaries (with the purpose of on-lending to businesses and producers committed to sustainable practices), as well as to businesses implementing sustainable practices in Latin America, the Caribbean, and sub-Saharan Africa. The Fund focuses on sustainability in four economic sectors: agriculture and agri-processing, fishery and aquaculture, forestry, and sustainable tourism. The Fund's financing instruments focus on debt instruments.

Investees of the Fund are referred to as "Partner Institutions" (PIs). Eligibility requirements and investment criteria include negative and positive screening, monitoring and active management based on internationally recognized environmental, social, and governance (ESG) standards for the identification, avoidance and mitigation of adverse impacts and ESG-related risks.

The combined effect of these product features is that the Fund inherently has limited exposure to potentially material sustainability risks given its sector focus and selection of PIs. Nevertheless, national ESG regulations and enforcement in the emerging and transitional economies targeted by the Fund are sometimes weaker compared to developed markets and may be subject to change and reform. Moreover, at the time of investing, the Fund's PIs may also have limited ESG management capacity and expertise in which case the Fund, via its Development Facilities, can provide support to meet its ESG management requirements.

The Fund therefore integrates ESG considerations (including sustainability risks and potential adverse impacts) into decision-making and investee engagement throughout the investment process, including ongoing monitoring and portfolio management once an investment has been made.

Environmental, Social and Governance Risks

EBF places a priority on effectively managing – i.e. avoiding, minimizing and mitigating – E&S risks and impacts associated with its investments. Key E&S factors that could be relevant considering the Fund's sector focus include, but are not necessarily limited to, pollution prevention and control; protection of biodiversity; natural habitats and cultural heritage; occupational and community health & safety; labor standards and working conditions; indigenous peoples rights; involuntary resettlement; climate change; and human rights.

The EBF's Environmental and Social Policies (E&S Policies) govern the Fund's approach to managing E&S risks and impacts associated with its investments. The Fund's Board of Directors has overall responsibility for setting the E&S Policies and overseeing their implementation, both directly and via the Fund's Board-appointed Investment Committee. Remuneration of Directors shall not favour excessive risk taking, not limited to but explicitly with respect to sustainability risks. Primary responsibility for day-to-day implementation of the E&S Policies rests with the EBF's Advisor[1].

The Fund requires its PIs to carry out their activities (for direct investments) or to use proceeds (for financial and real-sector intermediaries) in compliance with the EBF Exclusion Lists. The EBF Exclusion Lists prohibit financing activities with inherent or elevated sustainability risk, such as activities involving child and forced labor, pesticides/herbicides subject to international bans, logging operations in primary tropical moist forest, among others. Equally, PIs have to carry out activities in compliance with national law and in a manner consistent with the key principles of the relevant IFC Performance Standards and International Labor Organization's core labor standards.

At investee level, PIs are subject to E&S screening, and categorization. EBF's E&S categorization system is closely aligned with those employed as standard by IFC, the Association of European Development Finance Institutions (EDFI) and others.

The investment evaluation includes a thorough E&S due diligence (ESDD), customized according to the initial E&S risk categorization of the investment. The due diligence process includes the use of data intelligence for E&S screening and media reports to identify high-risk factors, which may impact the reputational and/or credit risk. Results of the ESG due diligence form an integral part of the investment proposal and are presented to the Investment Committee, whose investment decision includes the review of E&S factors. Where E&S risks cannot be mitigated to a satisfactory extent, the investment will not proceed.

For direct investments (corporate finance transactions) categorized as medium or medium-high risk, the Fund requires an Environmental and Social Assessment and/or other studies to be undertaken in accordance with the relevant IFC Performance Standards. Typically, such assessments, along with the results from due diligence, will be used to draw up an appropriate E&S action plan (ESAP). Climate risk assessments may be integrated into the E&S assessment and/or due diligence process as appropriate. The Fund does not provide financing to direct investments categorized as high risk.

The Fund requires that all its PIs establish or maintain a satisfactory E&S management system (ESMS). PIs and – in the case of investments to financial intermediaries – projects, financed with proceeds of the Fund must comply with the EBF Exclusion Lists. The Fund also requires that the PI's in-house employment practices conform with key principles of IFC Performance Standard 2 on labor conditions. Responsible Finance aspects are integrated into the PI due diligence process.

The Fund monitors the E&S performance of its PIs on a continuous basis and requires each PI to self-report to the Fund at least every 12 months. Where appropriate, third party consultants may be engaged to support the E&S monitoring of investments and/or to provide independent E&S monitoring reports.

[1] The Fund's Advisor is the impact asset manager Finance in Motion.

Engagement with PIs is an integral component of the Fund's investment process and contribution to positive development impact. This engagement often includes (but is not necessarily limited to) ESG matters. Where appropriate, e.g., when a PI does not meet the required standards of ESG management, technical assistance or capacity building is provided as part of the engagement with a PI.[2]

In addition, the Fund operates a communications and complaint mechanism to allow project affected persons or other stakeholders to raise concerns or grievances about the E&S aspects of the Fund's PIs and investments.

Potentially material sustainability risks identified as a result of the Fund's E&S monitoring of a PI are escalated to the Investment Committee and/or Board of Directors according to the nature of the identified risk. Potential sustainability risks are also given systematic consideration before the Fund's Board approves the use of new financial instruments, the creation of new sub-funds, or entry into new countries of operation.

The Fund, with support of its Advisor, maintains a formal and documented E&S Management System to implement the policies and procedures described above. This includes clear requirements for E&S-related functional clearances and the documentation and retention of information on internal decision-making. E&S procedures and decision-making are also subject to internal and (at certain intervals) external review and oversight. Investment staff of the Advisor receive formal induction and periodic refresher training on the Fund's E&S policies and procedures and are supported by the Advisor's in-house team of experienced E&S experts.

The Fund's objective is to identify, mitigate, monitor or refrain from investments with investee-specific governance risk in order to protect the Funds' stakeholders against reputational risk, financial loss or non-compliance with relevant regulatory standards.

Assessment of the investees' governance, i.e. its market position, ownership structure, composition, quality and independence of the Board of Directors and Management, and the effectiveness of control standards are therefore integrated into the counterparty creditworthiness assessment. Equally, the investees' approach to consumer protection, the availability of complaints mechanisms, the assessment of unethical business practices, involvement in crime (including bribery and corruption), associations with acts of violence, and imposed sanctions are an integral part of the investee due diligence process. Governance-related risk management is further supported through the Fund's risk-based AML/CFT framework. The AML/CFT Policy for Investees defines the minimum standards and principles for investee eligibility, as well as detailed KYC procedures and ML/TF due diligence requirements for all potential investees, the scope of which is determined on a risk-sensitivity basis.

[2] EBF focuses on private debt transactions and has only very limited exposure to publicly traded securities or listed companies and as such does not undertake investor engagement within the meaning and context provided by Article 3(g) of Directive 2007/36/EC on the exercise of certain rights of shareholders in listed companies.

Enhanced due diligence is performed for every high-risk investee. Where deemed necessary, an additional external independent background study is commissioned.

Monitoring and reporting of these governance factors is performed regularly based on the investees' risk profile – e.g., high-risk investees are monitored more intensively.