Baltic International Bank

POLICY FOR INTEGRATING ESG APPROACH INTO THE ASSET MANAGEMENT PROCESS

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1. Organisational Properties of the Document

Version No	***With effect from:***	***Summary of amendments***	***Pages***
1.	10.03.2021	This is a newly articulated Policy.	8
2.	21.04.2022	Bank has slightly revised the Policy, and the Policy continues to be current. Bank submits the Policy for approval in accordance with the *document update schedule* approved by the Management Board.	8

2. Terms and Abbreviations

For the purposes of this Policy:

Bank means Baltic International Bank SE.

Member State means a Member State of the European Union or of the European Economic Area.

ESG refers to considering the environmental, social and governance issues. The ESG concept determines the respective model of organisation's behaviour. Organisations committed to integrating ESG factors into their processes focus on

1) environmental protection (contributing to reducing greenhouse gas emissions, preserving biodiversity, reducing environmental pollution, reducing carbon dioxide emissions, switching over to renewable energy);
2) social responsibility (in respect of employment, forced displacement of people from their locality or environment or occupational activities (for instance, in connection with inclusion of civilian areas into industrial zone), human rights, health and safety, financial services to low-income people and people with disabilities);
3) principles of good governance (implementing anti-corruption and anti-bribery policies, maintaining a good reputation, ensuring the effectiveness of corporate governance).

ESG Approach means Bank's long-term strategy that implies conformity to international standards. The ESG concept focuses on environmental protection, social responsibility, and adherence to and implementation of the principles of good governance.

Sustainability Risk 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.

ESG Score means a score (expressed as a numeric value) determined according to the methodology, as described in this Policy, and assigned to a financial instrument to be included into each Portfolio.

ESG Rating means a rating determined under ESG Approach. ESG Rating is designed to measure the likelihood of occurring of Sustainability Risk event or condition. The larger ESG Score assigned to each financial instrument, the lower likelihood of occurring of Sustainability Risk event or condition for the given financial instrument. ESG Rating represents Portfolio's rating calculated as weighted average ESG Score appearing on the ESG Rating scale.

Regulation means REGULATION (EU) 2019/2088 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 27 November 2019 on sustainability–related disclosures in the financial services sector.

ECB is the abbreviation for the European Central Bank.

FCMC is the abbreviation for the Financial and Capital Market Commission, the primary financial regulator in the Republic of Latvia.

Assets means cash funds and financial instruments owned and possessed by Client by virtue of the ownership right and transferred by Client to Bank for subsequent management.

Asset Management means a portfolio management service, namely, management of Client's financial instruments and other Assets in accordance with mandates given by Client on a discretionary basis, on Bank's behalf and for the best interests of Client, at Client's sole risk and expense, in accordance with the Agreement and Client's investment strategy;
Bank conducts transactions in Financial Instruments to gain profit for Client.

Financial Instruments (FI) means financial instruments as specified in Article 3(2) the Financial Instruments Market Act [*Finanšu instrumentu tirgus likums*] of the Republic of Latvia, or other financial asset specified in the Investment Declaration as defined in Bank's "Asset Management Procedure".

Client means Bank's client to which Bank provides an investment service, namely, a personalised management of FI in accordance with mandates given by investors on a discretionary investor-by-investor basis (a portfolio management service).

Portfolio means a collection of Client's FI and cash funds that Bank holds in custody and manages under the asset-management arrangement.

Policy means the "Policy for Integrating ESG Approach into the Asset Management Process".

Internal Rules and Regulations (IRRs) means internal regulatory and guidance documents, such as policies, procedures, charters and others, as approved by Bank.

3. General Provisions

3.1. The purpose of this Policy is to ensure the transparency with regard to the integration of ESG Approach, the consideration of sustainability impacts in the Asset Management process, and the provision of sustainability-related information with respect to Asset Management.

3.2. This Policy lays down Bank's guidelines on assessment and monitoring of Sustainability Risk during the Asset Management process, including responsibility conferred upon Bank's functional units involved into the process.

3.3. This Policy articulates the substantive conditions for the publication of information (referred to in the Regulation) related to the integration of ESG Approach into the Asset Management process.

3.4. This Policy becomes effective upon final approval by the Supervisory Board.

4. Guidelines

4.1. Bank lays down the following guidelines with respect to Portfolio management and the integration of Sustainability Risk in Bank's investment decision-making process (based on consideration of potential negative impact of Sustainability Risk or positive impact of integrating ESG factors):

4.1.1. as far as Asset Management is concerned, estimation of the risk/return trade-off is always viewed as the most important factor while Portfolio's choice takes into account the level Client-specific risk;

4.1.2. Bank integrates Sustainability Risk into the overall risks assessment process in order to achieve possibly high ESG Rating. Simultaneously, Bank does not reduce Portfolio's return and does not increase the level of Portfolio-inherent risk. Bank assesses Sustainability Risk based on ESG Rating, as Sustainability Risk and ESG Rating are inversely linked (the higher ESG Rating, the lower Sustainability Risk).

4.2. Bank is aware that taking into account ESG factors in making investment decisions can exert impact on risks inherent in and return generated by financial products. Bank therefore strives to avoid situations in which the respective decisions trigger or foster consequences that in turn can result in negative effects on Portfolio's overall risk and return.

4.3. During the Asset Management process, Bank assesses on a continuous basis not only all relevant financial risks but also including all relevant Sustainability Risks that might have a relevant material negative impact on the financial return of an investment.

4.4. Bank assesses every single FI to be included in Portfolio, assigns ESG Score to the FI, and assigns the overall ESG Rating to each Portfolio.

4.5. Bank builds model Portfolios according to the level of risk. Bank is driven by the intention to

- offer its Clients standardized investment solutions aimed at providing Client with the best possible risk/return trade-off and
- achieve the best Portfolio's ESG Rating, i.e. to make the Portfolio more sustainable as far as possible.

4.6. As far as bespoke Portfolios are concerned, each Portfolio is tailored to Client's investment objectives and the choice of the instruments is based on the risk/return maximization. In a bespoke Portfolio, evaluation of each FI takes into consideration of ESG factors and ESG Rating is assigned to the respective Portfolio. From among similar FIs, am FI carrying a better ESG Score is chosen. However, Bank enables Client to choose to make an investment that is not ESG-compliant. In doing so, Bank informs Client that the respective Portfolio will

- carry a low ESG Rating and
- be exposed to a high Sustainability Risk.

4.7. To determine potential impact of Sustainability Risk, Bank:

1) analyses whether FIs to be included in Portfolios are ESG-compliant and evaluates every single FI on an individual basis and the entire Portfolio holding on an aggregate basis;
2) evaluates each FI (before purchasing FI and comprising it within Portfolio) and assigns ESG Score to the FI;
3) evaluates (once every year) each Client's Portfolio in order to ascertain whether the respective Portfolio fits in with the assigned ESG Rating.

4.8. Bank assesses the potential ***negative*** impact of Sustainability Risk on Portfolio's return. For this purpose, Bank uses the screening method and identifies areas wherein investments foster the negative impact, fuel the negative consequences, and increase the likelihood of occurring of Sustainability Risk. As one of the criteria, Bank relies on classification of the respective undertaking as belonging to a certain sector that exerts a negative impact on sustainability and hence excludes the sector's undertakings from the target market or drives down investments in the respective sectors, such as arms, alcohol and tobacco trade. To assess the negative impact of Sustainability Risk, Bank uses the method of integrating ESG Approach. For this Purpose, Bank determines relevant ESG Rating according to the methodology described in this Policy (see Section 5 hereof).

4.9. Bank also assesses the ***positive*** impact of integrating ESG Approach into the decision-making process. For this Purpose, Bank determines relevant ESG Rating according to the methodology described in this Policy (see Section 5 hereof).

4.10. Bank sets forth the requirements related to the application of the respective assessment in its IRRs governing the Asset Management process.

4.11. The AMD assesses the impact of Sustainability Risk and ensures the integration thereof into the overall risks score. For this purpose, the AMD determines relevant ESG Rating according to the methodology described in this Policy (see Section 5 hereof).

4.12. Bank prepares and publishes the informative materials in accordance with the provisions of the Regulation, thus ensuring compliance with the transparency requirements regarding ESG Approach (see Section 7 hereof).

5. Methodology for Determining ESG Score and ESG Rating

5.1. Bank determines ESG Score depending on the respective FI issuer (undertaking, government or fund) while complying with additional provisions with respect to FIs categorised as bonds.

5.2. ***ESG Score that is based on the issuer (the company having issued the FI).***

5.2.1. To determine ESG Score, Bank uses a model for assessing ESG factors. The assessment model is based on relative intra-sector assessment principle.

5.2.2. The assessment relies on the Industry Classification Benchmark (the ICB uses a system of 10 industries partitioned into 19 super-sectors) to form unified groups for undertakings in each industry.

5.2.3. Based on the information (the annual financial statements of the undertakings) available on the Bloomberg Professional Terminal, Bank determines variables attributable to the respective undertaking depending on the undertaking's size (i.e., income, assets and workforce).

5.2.4. For each variable in each sector, the Table of Percentages is used. The Table shows thresholds for percentage values, namely, 5% and 95% (lower and upper thresholds) and the calculated critical values with a 10-percent increase (i.e. 5%, 10%, 20%, ..., 95%).

5.2.5. The assessment of each individual undertaking compares/reconciles each variable's value against the values (as appearing on the Table of Percentages) in the respective sector in which the undertaking operates.

5.2.6. After ascertaining that the value corresponds to a certain percentage band (e.g. 24.3% corresponds to 20% and 30%), the variable scores a certain number of points. The value is rounded off upwards to the nearest integer of 10% (in this example: 30%). Thereafter, the value is transformed according to a 10-point scale (30% corresponds to 3) where the larger number of points signifies the greater compliance with ESG Approach.

5.2.7. If the assessment uses an inverse scale, this means the following: the largest negative impact requires scoring less points (e.g. with respect to greenhouse gas emissions). In this case, Bank adjusts the final score as follows: according to the 10-point scale, the calculated result is subtracted from 11. Thus, the final value still is measures according to the 10-point scale.

5.2.8. Based on the significance scale and data availability, the assessment of each ESG factor focuses on the following variables included in the total calculation:

5.2.8.1. ***Environmental factor:***

1) greenhouse gas (GHG) emission intensity: an undertaking's GHG annual emission, normalized by revenue output;
2) energy intensity: total amount of energy used by an undertaking annually, normalized by revenue output, assets and workforce (normalized geometric mean of three parameters is computed);
3) water intensity: total amount of water used by an undertaking annually, normalized by revenue output, assets and workforce (normalized geometric mean of three parameters is computed);
4) waste intensity: total amount of waste generated by an undertaking annually, normalized by revenue output;

5.2.8.2. ***Social factor:***

1) female representation (percentage) in an undertaking's workforce;
2) female representation (percentage) at all levels of management;
3) the number of accidents: total number of accidents per 100 employees expressed as the number of full-time equivalents (FTE), a unit used to measure employed persons;

4) general public: total sum of money that an undertaking allocates towards public events (in millions), normalized by revenue output;
5) negative sector screening, by halving the number of points scored by social criterion of tobacco companies and defence companies in order to reflect their negative impact on public. Bank adheres to the precautionary principle when analysing the companies;

5.2.8.3. ***Governance factor:***

1) the proportion (percentage) of independent directors;
2) the proportion (percentage) of independent directors in the audit committee;
3) the terms of office of an undertaking 's board
4) research and development (R&D) costs: annual R&D costs, normalized by revenue output.

5.2.9. If any of the variables lacks proper assessment, all of the variables (a 10-point scale) are assigned a zero value. The approach adds conservative partiality to the assessment. Bank, however, believes that such a provision is appropriate and precautionary.

5.2.10. Total scores for each ESG factor are computed as weighted average scores in the following manner:

1) the Environmental factor-specific and Social factor-specific variables are assessed in equal proportion;
2) the number of points scored by the variables of governance factor-specific R&D costs and the variables of independent directors is twofold higher than that scored by other variables.

5.2.11. Computation of the final ESG factors-specific scores takes into account the respective ratios (scores) developed by *RobecoSAM* and *Sustainalytics*. To each of the three scores (assigned by Bank, *RobecoSAM* and *Sustainalytics*), the weighting algorithm dynamically assigns weights, depending on the degree of their dispersion.

5.2.12. If scores provided by *RobecoSAM* and *Sustainalytics* are consistent (e.g. do not differ much from each other) but differ much from Bank's scores and their total weight is larger (while their individual weights are equal, e.g. 30% and 30%, etc.), then the weight of Bank's score is lower.

5.2.13. If scores provided by *RobecoSAM* and *Sustainalytics* are somewhat conflicting, then the weight of Bank's score is larger.

5.2.14. The computed ESG factors-specific scores are summarised in the uniform value scale that ranges from 0 to 100 and reflects the undertaking's overall progress according to ESG Approach. Furthermore, the summarisation is carried out on a sector-by-sector basis, rather than on a universal basis, because the value of the impact, as exerted by different sectors on different ESG factors, differs as well.

5.2.15. The total ESG factors-specific score assigned to the respective undertaking represents ESG score assigned to the FI issued by the undertaking.

5.3. ***ESG Score that is based on the issuing country.***

5.3.1. ESG Score is assigned according to Bloomberg's ESG Scores. Bloomberg scores firms based on ESG disclosure transparency using a scale from 0 to 100.

5.4. ***ESG Score that is based on the issuers of FI included in the funds.***

5.4.1. For each fund, the assessment according to ESG factors focuses on 10 most sizeable investments and obtains the result in respect of their proportional weights.

5.4.2. This method is used as for most funds it is impossible or it is difficult to find the full composition of assets and their respective proportions.

5.4.3. When choosing an index fund, it is impossible to conduct FI-specific negative screening and to filter out undertakings exerting adverse impacts on ESG factors.

5.5. ***ESG Score assigned to FI categorised as bonds*** depends on types of bonds (sovereign bonds or corporate bonds).

5.5.1. Sovereign bonds: ESG Score is assigned according to cl. 5.3 hereof. If the respective bond is issued jointly by several countries, ESG Score is calculated on a pro rata basis (proportionally to each country's involvement).

5.5.2. Corporate bonds: ESG Score is assigned according to cl. 5.2 hereof (as ESG Score that is based on the parent undertaking involved in the bond issue).

5.6. ***Determination of Portfolio's ESG Rating.***

5.6.1. Bank assesses all FIs held in each Portfolio, even in the absence of relevant data required to determine ESG Score. Thus, the FIs are assigned a zero-point result.

5.6.2. To calculate the overall Portfolio's ESG Rating, Bank summarises ESG Score (appearing on the scale that ranges from 0 to 100) for FI comprised in the respective Portfolio and determines the overall weighted score for FI comprised in the respective Portfolio. The result obtained through the 0-100 scale is transformed into Bank's internal ESG Rating scale ranging from D to AAA:

AAA	90 – 100
AA+	80 – 90
AA	70 – 80
A+	60 – 70
A	50 – 60
B+	40 – 50
B	30 – 40
C+	20 – 30
C	10 – 20
D	0 – 10

6. Management and Monitoring of Sustainability Risk

6.1. The AMD determines a first-time ESG Score and ESG Rating. For this purpose, the AMD builds standardized Portfolios or bespoke Portfolios and evaluates FIs before inclusion thereof into particular Portfolios.

6.2. The AMD resets Portfolio's ESG Rating whenever the respective Portfolio undergoes changes. The AMD also revises FI-specific scores every year (once the audited financial statements of the undertakings have become available). This provision relates to both standardized and bespoke Portfolios.

6.3. The Compliance Department's officer conducts (once every year, on the basis of spot-checks) due diligence on ESG Rating in order to ascertain whether Portfolio's ESG Rating is still appropriate.

6.4. Bank's IRRs governing the Asset Management process prescribe the modalities and requirements for keeping Clients informed of ESG Ratings assigned to Portfolios and the changes in ESG Ratings.

7. Disclosure of Information Regarding Integration of ESG Approach into Asset Management

7.1. According to the disclosure requirements laid down in the Regulation, Bank should publish (and amend such information, if necessary) on its website information regarding the integration of ESG Approach into the Asset Management process. The information is disclosed in the following reports:

7.1.1. „Pre-contractual disclosure of information regarding transparency of the promotion of ESG factors and transparency of sustainable investments";

7.1.2. Report on the due diligence processes (the report is included within the report referred to in sub-clause 7.1.1 above;

7.1.3. „Report addressing the negative impact on sustainability in asset management".

7.2. The Legal Department, AMD, and Compliance Department jointly prepare the reportable (disclosable) information in a way that it is understandable to Clients or potential Clients. It is important that Clients or potential Clients are able to understand the nature of offered investment service and of a particular FI type and hence make informed investment decisions.

7.2.1. While preparing the reports, Bank complies with the provisions laid down in relevant delegated and implementing acts for the Regulation.

7.2.2. Bank ensures that the disclosures (the information published on Bank's website) are accurate, fair, clear, simple, concise and succinct.

7.2.3. To prepare the reports referred to in cl. 7.1 hereof, Bank may use the information included into

- the management reports in accordance with Article 19 Contents of the management report of DIRECTIVE 2013/34/EU OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 26 June 2013 on the annual financial statements, consolidated financial statements and related

reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC, or
- non-financial reports in accordance with Article 19 paragraph (a) the undertaking's likely future development (in the respective case).

7.3. The Chairperson of the Management Board approves the prepared reports before the publication.

7.4. The disclosable information referred to in sub-cl. 7.1.1 hereof is published on Bank's website in the respective prominent easily accessible area of the website and is updated on an as-needed basis but at least once every year.

7.5. The report referred to in sub-cl. 7.1.3 hereof is published on Bank's website in the respective prominent easily accessible area of the website before 30 June and cover the previous period from 1 January to 31 December.

7.6. The MCD posts the reports on Bank's website in the manner prescribed by relevant IRRs governing.

7.7. Bank ensures that any information published in accordance with the requirements set forth herein is kept up to date. Where Bank amends such information, Bank publishes a clear explanation of such amendment on the same website.

8. Responsibility

8.1. The Supervisory Board approves the Policy and supervises how the Management Board ensures the implementation of the Policy.

8.2. The Management Board articulates and adopts the Policy and approves other related IRRs required for implementing the Policy.

8.3. The Internal Audit Department assesses (in accordance with the work plan approved by the Supervisory Board) the effectiveness of integrating ESG Approach into the asset management process.

8.4. The Compliance Department's officer is responsible for conducting due diligence on ESG Rating in order to ascertain whether Portfolio's ESG Rating is still appropriate.

8.5. The AMD is responsible for ensuring adherence to the Policy, indicating the methodology as described in the Policy, and revising and updating the Policy in the light of the changes in Bank's strategy and market situation.

8.6. The AMD and the Legal Department are jointly responsible for preparing the disclosable information (Section 7 hereof) in accordance with the provisions laid down in the Regulation and for publishing and updating the disclosures in a timely manner.

Related IRRs and Legal Framework

Related IRRs:

- Policy Governing Fiduciary Activities;
- Asset Management Procedure;
- Procedure for Preparing and Publishing Disclosable Information on Bank's Website
- other relevant IRRs.

Legal Framework

This Policy has been drawn up with reference to:

- Financial Instruments Market Act [*Finanšu instrumentu tirgus likums*] of the Republic of Latvia;
- REGULATION (EU) 2019/2088 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 27 November 2019 on sustainability–related disclosures in the financial services sector;
- relevant delegated and implementing acts for REGULATION (EU) 2019/2088 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 27 November 2019 on sustainability–related disclosures in the financial services sector;
- other applicable laws and regulations.