Principles for Responsible Investment

Sustainable

Millennium bcp

PRINCIPLES FOR RESPONSIBLE INVESTMENT

ESG (Environmental, Social and Governance) financing and investing is recognized as a specific business management strategy under the umbrella of responsible banking, in which the Bank incorporates ESG considerations in the decisions related to long-term exposures and returns. To this end, ESG factors are evaluated both in terms of their risks and opportunities.

As an overarching principle, responsible investing consists of avoiding and/or mitigating risky ESG aspects and practices to protect the Group's financial sustainability. To this end, ESG is assessed on a double materiality perspective, first, by gauging its influence on the risk-adjusted return of the Group's financial assets (risk management perspective) and, second, by evaluating the impact it produces on the communities and environment to which the Group and its subsidiaries relate (corporate sustainability perspective).

The guidelines, risk and/or performance metrics underpinning both perspectives for the Group BCP are annually updated and included in the Group's Risk Appetite Framework (RAF), which is subject to syndication and local implementation by each Group Entity.

For financial products issued or structured by the Group, the approach considers the applicable regulatory requirements (notably the SFDR (Sustainable Finance Disclosure Regulation), but also the relevant additional guidance for product labelling) that prevail over the provisions herein defined.

Risk management perspective

The integration of the risk perspective into the investment activity addresses the following two concerns:

- Reliance on unofficial ESG labels should not guide investments and the portfolios composition as those labels may not be considered adequate (i.e., risk to the market valuation of those assets);
- The ESG risks, in particular the Climate & Environmental components, may impact the financial profile and activity of the Bank's counterparties, resulting in additional risks to the valuation of their exposures.

As a result, the following key principles are observed:

- The ESG labelling (or related) per se, at this stage, is not a main investment driver;
- Prior to a material investment in green or sustainability-related exposure, the divisions responsible for investment may obtain advice (i.e., second opinion) on the benefits/impact of the transaction from the Sustainability Function;
- The existing exclusion policies are respected by Investment Function for any new investment – whenever applicable, this set of policies may result in knock-out criteria for the investment decision and in any case be granted a positive opinion by the Sustainability Function;

The regular monitoring of the investment activities and portfolios includes an ESG risk perspective, by measuring the Bank's exposure to a) transition and physical risks; and b) to high emitters of GHG (GreenHouse Gases). This information is internally monitored and subject to external and supervisory reporting.

Incorporation of the Group's transition plan goals into investment guidelines

The Group BCP's definition of the transition targets for its own balance sheet and related portfolios condition the composition of the investment portfolios. Those targets can be defined in terms of GHG intensities, exposure to high-transition risk sectors, among other.

To that end, guidelines and targets are internally syndicated (as part of the risk appetite cascading process) and incorporated into the annual budgetary guidelines of the areas managing the investment portfolios.

The performance and accomplishment of those targets is integrated into the ordinary risk appetite monitoring process observing, whenever applicable, the specific risk escalation procedures.

Issuer and counterparty assessment

Due to its idiosyncratic nature, the investment operations are not compatible with the due process established for the origination of loans, especially in what concerns the assessment made prior to the transaction. Instead, when it comes to investment, the ESG risk assessment should focus on the process of approval or renewal of exposure limits (sector, counterparty, type of security) so that the transactions can proceed unhindered by screening duties thereby allowing for the financial markets specific dynamics. For that purpose, the Investment Function requires an opinion from the Sustainability Function ensuring that:

- Any applicable Group-wide or entity-specific exclusion (or sectoral) policy is adequately complied with in the investment process;

- The main Group's counterparties are subject to an internal ESG risk assessment that is part of the ordinary credit rating assignment including the vulnerability to C&E risks and controversies;
- The availability of an external ESG rating should also be considered, whenever available.

ESG risk factors in the post-investment activities

The investment portfolios are subject to risk monitoring procedures which include, inter-alia the following components:

- Sectoral views, highlighting high transition-risk sectors;
- Concentration of exposures in high-physical risk locations;
- Weight of ESG-labelled products/exposures;
- Exceptions to the application of sectoral and exclusion policies.

Asset allocation perspective

Each Entity of the Group BCP can devise an ESG investing strategy provided they ensure that: a) the strategy and associated products ensure the overall sustainability of the investments; and b) they meet the internal standards for the strategy definition and approval.

The Entity (or the Group) may commit itself to obtain a minimum threshold in terms of new ESG business (e.g., green production KPI (Key Performance Indicator). In that case, the computation of the threshold shall verify, at least, the compliance with the BCP's internal Green Taxonomy and, if possible, with the EU Taxonomy.

Instruments for ESG investing

The instruments listed below are accepted in the Group BCP for the purposes of ESG investing. Their use is subject to a new product approval process, where a thorough analysis (Risk and Compliance Functions and other competent areas related with product) shall specifically assess a) the framework formally supporting the issuance/instrument; b) the consistency between the framework and the regulatory requirements at EU level; and c) the availability of a third-party opinion on the issuance.

Securities typology:

- **Green bonds:** a bond instrument that funds projects that provide a clear benefit to the environment, provided they comply with the formal framework of the International Capital Markets Association (ICMA) – Green Bond Principles or, preferably, with the EU Green Bond Standard.
- **Social bonds:** a bond instrument that funds projects that provide access to essential services, infrastructure, and social programmes, provided they comply with the formal framework of the ICMA's Social Bond Principles.
- **Sustainability bonds:** a bond instrument that allows issuers to apply funds in a broader list of projects, still creating a positive social or environmental impact. They are required to comply with the ICMA's Sustainability Bond Guidelines.
- **Sustainability-linked bonds:** a bond instrument that is providing funding to an issuer that committed to specific improvements/targets in terms of its activities and projects. Those targets can be related to any ESG dimension.
- **Transition bonds:** a bond instrument that is providing funding to 'brown' companies (i.e., with high GHG emissions), and are aimed at supporting their transformation towards a greener activity.
- **SDG-linked bonds:** analogously to the above listed instruments, but the issuer is targeting the use of funds towards SDG-related projects.
- **Blue bonds:** the issuer is targeting the use of funds towards projects with clear marine and ocean-based benefits (e.g., sustainable fishing projects).
- **Green securitizations:** they represent Asset-Backed Securities (ABS) instruments, which are based on the mutualisation of green or sustainable (typically illiquid) assets into a new financial security (e.g., portfolio of green loans or aligned with EU Taxonomy).
- **Article 8 and 9 Funds:** investment in an undertaking for the collective investment in transferable securities (UCIT) - i.e., investment fund – that is formally classified under the provisions of the SFDR as an Article 8 or 9.

The remaining and traditional categories of instruments (e.g., sovereign debt, corporate debt, equities, real estate exposures, commercial paper programmes) can be used as an instrument, provided the issuer fits the criteria established under the investment strategy.

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