Responsible Investment Policy: Climate Addendum

Park Square Capital
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I. Introduction

The Intergovernmental Panel on Climate Change ("IPCC") have warned that ambitious, urgent and accelerated actions are required to minimise the future risks associated with climate change. These risks can be defined into two categories:

1. **Physical Risks** - Manifest through climate change having unpredictable (acute) and predictable (chronic) effects on the physical environment and supply chains. These risks can include climatic events such as wildfires, storms and floods.
2. **Transition Risks** - Manifest through mitigation or adaptation to climate change. These risks can include policy and regulatory risks, technological risks, market risks, reputational risks, and legal risks.

These risks can result in unexpected capital and operational expenditure across an investment's lifetime, cutting into return and potentially diminishing value.

As a leading private credit investor, Park Square and its affiliates[1] recognise a responsibility to monitor and engage with portfolio companies regarding climate risks to mitigate financial risk, as well as minimise the climate impact of its own operations. As a signatory of the Task Force on Climate-Related Financial Disclosures ("TCFD"), Park Square has incorporated climate risk into its governance, strategy and risk management processes.

II. Climate Governance

Park Square's governance structure ensures that its investment activities are aligned with the Firm's position on responsible investment and climate change.

Park Square's Executive Committee acts as the governing body of the Firm. It sets the strategic direction and looks to ensure its long-term success.

Reporting to the Executive Committee are a number of committees with delegated responsibilities including the Investment Committee, Risk Committee and ESG Committee.

Park Square's Executive Committee has mandated the ESG Committee, chaired by the Co-Head of Direct Lending, to maintain oversight of ESG integration, which includes the monitoring of climate-related issues and their risk to Park Square and its funds.

The ESG Committee are responsible for informing other committees, including the Executive Committee and individual Fund Advisory Boards of any climate-related issues that are material to the Firm's operations, strategy and the performance of its funds under management.

The ESG Committee is supported by a dedicated ESG team as well as additional resources across the business including legal and compliance functions.

The investment team are responsible for identifying any climate-related issues that may impact portfolio company performance. The investment team are supported by a number of tools developed by the ESG team including a proprietary ESG Risk Screen which includes dedicated climate guidance, an in-house ESG team and access to a third-party specialist ESG consultant.

Park Square approaches climate-related risks in a manner similar to its assessment of financials and other investment risks. The ESG and Investment Committee are regularly updated with ESG, including climate risk, considerations throughout the lifecycle of a deal, from business selection to exit.

Note: [1]includes Park Square Capital Luxembourg Management Services S.à r.l

Pre-Investment: Due Diligence

- RepRisk – Third-party provider identifies any public, historic climate-related controversies.
- Initial screening tool – Where SASB and / or MSCI materiality frameworks flag climate change risk as potentially material to a sector, this will be identified as an area for further investigation. Where companies are operating in countries ranked in the bottom quartile of the Environmental Performance Index, climate risk is flagged as an area for further investigation.
- Collection of sustainability indicators – Where available, climate-related indicators are collected during the due diligence process such as greenhouse gas ("GHG") emissions, carbon intensity, exposure to the fossil fuel sector and renewable energy consumption.
- ESG Risk Profile – Park Square's ESG risk screen contains dedicated climate guidance to assist deal teams in their assessment of the potential exposure to climate risk.
- Analysis of available environmental and/or sustainability reports.

Post-Investment: Monitoring and Engagement

- Scenario Analysis – Park Square completes high-level, sector-based scenario analysis across the portfolio annually to identify potential exposure to climate risks.
- RepRisk – RepRisk provide ongoing alerts to any climate-related incidents at portfolio companies. RepRisk ratings are also included in Park Square's quarterly portfolio review where deal teams are expected to highlight emerging risks or incidents identified in the quarter.
- ESG-Linked Loans – Park Square holds a number of loans where the margin is tied to the achievement of certain KPIs. Often, these KPIs are related to GHG emissions reduction and management.
- Annual Data Collection – Park Square's annual ESG questionnaire contains specific metrics related to climate risk including scope 1, 2 and 3 GHG emissions, fossil fuel sector exposure, energy and renewable energy consumption.

In the event that Park Square is uncomfortable with how a portfolio company is managing its risks, and/or a change in industry dynamics, competitive positioning or company performance would warrant a re-evaluation of the original investment thesis, a business is placed on a "watch list" and given a heightened degree of scrutiny by the Investment Committee. If the Investment Committee's concerns cannot be successfully mitigated or addressed, a decision to seek divestment will be considered by the Investment Committee.

III. Strategy

The following pillars form the foundation of Park Square's approach to integrating climate-related considerations into its strategy and practices:

- Continuous Progress: Park Square is committed to developing its climate practices in-line with internationally established guidelines and industry best practices.

- A Culture of Responsibility: Park Square has a strong culture of responsibility. It has considered ESG factors in its decision-making since its inception. 'Operating Responsibly' upholds the third pillar of Park Square's strategy of building a firm with 'Enduring Value' and climate change is a critical part of that. Park Square considers it a fiduciary duty to recognise and address climate risks that could impact a business throughout the investment process. Park Square believes that these risks and opportunities transcend environmental impact and include socioeconomic dimensions of climate change. The Firm also provides the investment team with annual ESG training to develop their sustainability and climate-related expertise.

- Collaboration: climate change is a complex and systemic issue, requiring industry-wide collaboration. Park Square is focused on engaging with industry groups, portfolio companies and equity sponsors to identify and minimise the effect of climate change on its portfolio companies. Park Square also participates in industry groups to promote progress on the integration of ESG factors in the private debt asset class.

- Quantification & Monitoring: Park Square supports the notion of 'what gets measured gets managed'. Where possible, the Firm aims to quantify its impact and track meaningful materiality-based KPIs of the portfolio. Regarding climate change, Park Square collects, monitors, and reports data related to the GHG emissions of its own operations and portfolio companies. The Firm has committed to offset carbon emissions from its own travel and office operations. Park Square's scope 1 and 2 emissions for the year 2022 were 426.04tCo2e.

IV. Scenario Analysis

Park Square is in the progress of developing a comprehensive, bespoke scenario analysis tool to effectively identify current and emerging climate risks. The analysis will take into account a minimum of three scenarios aligning to differing levels of temperature increases:

1. A 'Hot House World' scenario with potential high physical risks;
2. An 'orderly' transition scenario where temperature is limited to below 2 degrees; and,
3. A 'disorderly' transition scenario with stringent policies, a quicker phase out of fossil fuels and higher transition risks.

Analysis of transition risk uses heat maps developed by the UN Environment Programme Finance Initiative in collaboration with Oliver Wyman that flag levels of risk for a range of sectors across four key areas: Direct Emissions Cost, Indirect Emissions Cost, Low-Carbon CapEx, Revenue.

The Firm also conducts additional assessments of carbon pricing risk across the portfolio.

Analysis of physical risks are evaluated based on the countries in which a company primarily derives its revenues and their exposure to acute and chronical risks such as sea level rises, crop yield, heat stress, productivity losses, increases in disease and exposure to extreme weather events.

V. Metrics and Targets

One of the challenges facing private market investors is the lack of consistent, comparable climate-related data. It is therefore important that Park Square collects and monitors climate-related data.

Park Square calculates the weighted average carbon intensity for all funds using a combination of directly sourced and estimated data. This data is disclosed to investors in the Firm's quarterly reports. The Firm also reports additional engagement highlights as they pertain to climate change to investors.

Park Square funds which are subject to article 8 of the EU SFDR, promote environmental characteristics aligning to the Sustainable Development Goal 13, "Climate Action". Reporting to LPs is consistent with the prescribed SFDR template.

Park Square will continue to expand its climate-related KPIs in line with market best practices and regulatory requirements

VI. Climate Ambitions

We are pleased with our progress to date but are committed to climate considerations being a core part of Park Square's pre-acquisition due diligence and portfolio company management strategy. As Park Square looks to increase its focus on climate-related risks and opportunities, near-term priorities will include:

- Publishing annual TCFD-aligned disclosures;
- Developing a bespoke scenario analysis tool over multiple time horizons and scenarios;
- Further embedding climate-related risk and opportunities in due diligence, in line with industry best practice; and,
- Continuing to build on existing knowledge at the Firm to support its work on overseeing and implementing climate strategy and programmes.

VII. Policy Updates

Policies are reviewed by the ESG Committee and updated at least annually to reflect changes in circumstances and actual practice.

For more information, please contact: ESG@parksquarecapital.com