

# SUSTAINABILITY RISK POLICY

Procedure Number:	PR_FARAD IM_REG33
Enter into effect last version:	25/01/2022
Approval by FARAD I.M. Executive Committee:	25/01/2022
Line Managers or departments involved	Compliance Risk Management Portfolio Management
Legal requirements	SFDR (Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019)
Aim and application	This policy describes the investment guidelines principles and is to explain how sustainability risks are integrated into investment decision-making and investment advice activities.
Accessibility	In accordance with the legal requirements a digital copy of the policy is accessible on FARAD I.M. website and is delivered within the investment management agreement or other terms and conditions for a portfolio/fund management service.
Updating / Review	<ul style="list-style-type: none"> <li>- Change of applicable legislation;</li> <li>- Any new legal requirement;</li> <li>- Any other change that would have an impact on the policy.</li> </ul>
Communication to the CSSF	Upon request of the CSSF

## I. Introduction

FARAD I.M. vision is being a sustainable investment firm that takes responsibility for its actions and engagements, as a member of society with its own impact on the planet and on people, but also as a provider of financial services with an indirect impact through the activities of its clients and investments. The mission will be achieved by fully incorporating sustainability into the investment firm's daily business, and by bolstering the investment firm's sustainability risk management.

For FARAD I.M., sustainability means adhering to the values and business principles of the investment firm and bringing sustainable solutions to the current and future environmental, economic and social challenges of the investment firm's stakeholders and the organization itself, that are in line with the investment firm's risk profile.

By managing Environmental, Social and Ethical risks, mitigating their impacts and grasping the opportunities deriving from sustainable solutions, the Sustainability Risk Policy has incorporated sustainability into the investment firm's business objectives.

In line with SFDR (Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019) FARAD I.M. Sustainability Risk Policy defines the investment guidelines principles.

FARAD I.M. has first identified which are the sustainable risks that intend to affect in its decision-making processes and then FARAD I.M. has built the Risk Management framework in order to identify, analyze, monitor, mitigate and report them for its investment choices.

FARAD I.M. implements its Sustainability Risk Policy and underlying policies according to the three lines of defense. This approach ensures that sustainability risk management has a firm basis within the organization by dividing risk management responsibilities between different roles. The first line of defense (business management) has risk ownership, the second line (risk management and supporting functions) has risk control while the third line (audit) verifies risk assurance.

FARAD I.M. ensures that its financial portfolios are financially efficient and as much sustainable as possible.

## II. Sustainability Risks

Sustainability Risk is an environmental, social or governance event or condition that, if occurs, could cause an actual or a potential negative impact on the value of the investment. Such events may concern but not be limited to damage from climate change, scarcity of natural resources, pollution, poor working conditions, corruption and/or poor governance. Finally the scope of sustainability risks is wider because not only individual companies but entire sectors can be negatively affected by sustainability risks

Sustainability factors are often referred to ESG criteria which stands for environmental ("E"), social ("S"), and governance ("G"). ESG events and conditions can be of influence on all types of investments. There is not a single exhaustive list of ESG factors.

FARAD I.M. takes into consideration the following sustainability risks:

a. **Environmental sustainability risks for the value of our products' portfolios may include but are not limited to:**

- Climate change
- Carbon emissions
- Air and water pollution
- Deforestation

- Energy inefficiency
- Poor waste management practices
- Increased water scarcity
- Rising sea levels / coastal flooding
- Wildfires / bushfires

**b. Social sustainability risks for the value of our products' portfolios may include but are not limited to:**

- Human rights violations
- Human trafficking
- Modern slavery / forced labour
- Breaches of employee rights / labour rights
- Child labour
- Discrimination
- Restrictions on or abuse of the rights of consumers
- Restricted access to clean water, to a reliable food supply, and/or to a sanitary living environment
- Infringements of rights of local communities / indigenous populations

**c. Governance sustainability risks for the value of our products' portfolios may include but are not limited to:**

- Lack of diversity at board or governing body level
  - Inadequate external or internal audit
  - Infringement or curtailment of rights of (minority) shareholders
  - Bribery and corruption
  - Lack of scrutiny of executive pay
  - Poor safeguards on personal data / IT security (of employees and/or customers)
  - Discriminatory employment practices
  - Health and safety concerns for the workforce
  - Poor sustainability practices in the supply chain
  - Workplace harassment, discrimination and bullying
  - Restrictions on rights of collective bargaining or trade unions
  - Inadequate protection for whistleblowers
  - Non-compliance with minimum wage or (where appropriate) living wage requirements
- FARAD I.M. assesses the risk exposure of each target investment principally against these factors.

FARAD I.M. has implemented a proprietary ESG investment process and integrated within the portfolio management and risk management processes in order to analyse, monitor, mitigate and exclude sustainability risks.

Before investments are performed each single target investment has to be assessed via the ESG Score Card, which takes into account qualitative and quantitative metrics for the ESG segments.

Each target investment is rated in a range from 5 (the highest) to 0 (the lowest) and is accepted only if its overall score is higher than 3.5 over 5. No exceptions will be granted.

For the time being, and until further harmonised data on sustainability risks will be made available from our underlying vehicles, the metrics taken into consideration to assess the sustainability risks have been mainly focused on assessing the internal investment policies/procedure/reports focused on Environmental, Social and Governance factors.

The source of the data used to assess the sustainability risks are mainly coming from a third-party provider data: currently FARAD IM is using Morningstar Direct / Sustainalytics. Complementary, especially in case the third party provider data is absent or not satisfactory. FARAD I.M. uses data received directly from the Investment Manager of the target investments. The entire data is challenged during the due diligence process part of the investment process preceding the investment itself.

Data from all the target investments are monitored and reviewed at least once per year, to assess if the underlying investments are still compliant with FARAD I.M. requirements, including:

- The ESG scores;
- The ESG data collected through the third party provider or received from the relevant fund managers, which are used;
- The Sustainable Development Goals (SDG) mapping which represents the breakdown of the portfolio showing the percentage of alignment to each SDG. At portfolio level, the ESG scores of each issuer are attributed according to the weight of the issuer in the portfolio. FARAD I.M. assesses the overall ESG rating of the portfolio by following the above mentioned ESG calculation methodology and by applying the above mentioned thresholds.

FARAD I.M. monitors the ESG score of its investment portfolio, both at single security level and on an aggregate basis. ESG scores on each individual investment are taken into consideration alongside the traditional criteria of analysis and evaluation: this means that FARAD I.M. ensures that its financial portfolios are financially efficient and as much sustainable as possible.

FARAD I.M. is furthermore committed to implement one or more of the following methods within their investment strategies or investment processes, and therefore monitors the extent of the application of these methods in the underlying funds/investments:

- **Positive selection:** where the investor actively selects the companies in which to invest; this can be done either by following a defined set of Environmental, Social and Governance (ESG) criteria or by the best-in-class method (where a subset of high performing ESG compliant companies is chosen for inclusion in an investment portfolio,), or using a norms-based screening that allows investors to assess the degree to which each assets in their portfolio respects issues that impact Environmental, Social and Governance ESG criteria by adhering to global norms on environmental protection, human rights, labour standards and anti-corruption.
- **Engagement and Voting:** investment funds monitoring the ESG performance of all portfolio companies and leading constructive shareholder engagement dialogues with each company to ensure progress, also through strategic voting by shareholders in support of a particular issue, or to bring about change in the governance of the company.
- **Exclusion:** the removal of certain sectors or companies from consideration for investment, based on ESG specific criteria. FARAD I.M. has defined a specific exclusion list. The list indicates the base-level exposure that FARAD IM is willing to have to certain sectors / activities considered controversial and/or harmful and to avoid investing in controversial behavior flagged companies. FARAD IM is wary of expanding the exclusion criteria to encompassing other sectors / activities

of controversy as we believe that blanket exclusion is not always the best conduit to addressing the challenges posed by such sectors / activities. ESG analysis, engagement and active ownership can be at least equally effective, if not better, at improving such practices. FARAD IM excludes from its investment universe specific companies that generate more than a certain threshold revenue of their revenues from specific economic activities, as well as disregarding totally funds and/or companies that operate or invest in sectors and/or activities that do not comply with the UNGC principles, that are considered controversial, that are listed in controversial jurisdictions and that are involved in controversial behaviour.

Figure 1. Revenue threshold per exclusion category

	Category	Description	Company's Revenue threshold
Activity-based exclusion category	Controversial Weapons	FARAD IM believes that any company or investment involved in controversial weapons fail to meet the criteria established by the United Nations SDGs. Companies that are involved in the production, sales and distribution of controversial weapons are excluded. The controversial weapons category include cluster munitions, personnel landmines, biological, nuclear, and chemical weapons.	0%
	Tobacco	FARAD IM considers tobacco as an unhealthy practice, which clashes with the SDG 3, which promotes "good health and well-being". Companies that are involved in the production, sales and distribution of tobacco products and supporting services (e.g. cigarettes, cigars, smoking and chewing tobacco, filters, and next generation products such as e-cigarettes ).	5%
	Coal Extraction	FARAD IM considers coal extraction activity as polluting and not in line with the development of a cleaner and sustainable future society. Coal is a resource that does not comply with the clean and affordable energy criteria established in the SDG 7. Therefore, FARAD IM excluded any investment involved in the coal energy business.	5%
	Gambling	FARAD IM restricts the investment in companies that operating in the gambling supply chain, meaning all companies that own gambling facilities (e.g. casinos, online gambling), produce gambling equipment, and provide associated services to the industry.	5%
	Alcohol	FARAD IM limits the investment in companies that produce, distribute, and sell alcohol beverages. According to the WHO, excessive alcohol consumption are responsible for premature mortality, home violence, and mental health issues. Alcohol consumption clashes with 13 out 17 SDG goals.	5%
	Adult Entertainment	FARAD IM limits the investment in companies produce, distribute, or sell adult entertainment content. Adult content may be linked to human trafficking and a cause or gender inequality. This topic fails to meet the goals aimed by SDG 5,8, and 16	5%
	Palm Oil	FARAD IM acknowledges that the palm industry has contributed to eradicating poverty and social equality in numerous developing nations. However, the extensive production may be linked to environmental risks such as deforestation, and we have decided to restrict the exposure in this industry.	5%
Normative	Controversial Behavior	FARAD IM acts in accordance with the UN Global Compact and the OECD Guidelines for Multinational Enterprises standards to assess the behavior of the companies.	0%
Country-based	Controversial Jurisdictions	FARAD IM excludes all investments issued or listed in countries that are considered controversial and deemed as high risk jurisdictions by the United Nations Security Council.	0%

- **ESG Integration:** the inclusion of ESG risks and opportunities into traditional financial analysis of equity and bonds/debt instruments value.
- **Sustainability themed strategies and impact investing:** strategies that include a variety of themes, which allows investors to choose specific areas of investments, typically with a close link to sustainable development. Impact investing concerns strategies focused on assets that have a positive measurable impact on environment or society.

Finally the main environmental objectives of the target investments will be, but not limited, to contribute to at least one of the environmental objectives defined by article 3 and 9 of the Taxonomy Regulation the below:

- Climate change mitigation
- Climate change adaptation
- Transition to a circular economy
- Sustainable use and protection of water and marine resources
- Pollution prevention and control

The promotion of the above mentioned environmental objectives is implemented through investing into Target Funds or investments that promote these environmental objectives in their investment policy, and/or that disclose in public reporting their positive contribution to the above environment objectives.

### III. Disclosure of the policy

The SFDR requires that FARAD I.M. must publish on its own website information about this policy. The policy is published on <https://www.farad-im.com/services> under section GreenEthica.

The SFDR also requires that FARAD I.M. must include, in the pre-contractual disclosures of own financial products, a description of the manner in which sustainability risks are integrated into own investment decisions. Thus, a copy of this policy is delivered within the investment management agreement or other terms and conditions for a portfolio/fund management service.