ALGEBRIS INVESTMENTS
ESG Exclusion Policies

2022

1. Introduction

Algebris Investments (the "Firm" or "Algebris") has a commitment to responsible investing. An important part of this commitment is to ensure the Firm is not involved in the financing of activities and/or business practices that we deem unethical or detrimental to environment or society at large. This document outlines ESG exclusions policies grounded on normative, ethical, or climate related considerations. It applies across all Algebris funds where Algebris controls the investment policy of the entire fund in its capacity as sole investment manager.

Algebris is a global investment manager with a historical focus on the financial sector and over 80% of the Firm's AUM invested in this sector. We consider the financial sector to be the 'gatekeeper' of the transition to a more sustainable economy, due to the key role it plays in allocating funds across sectors. Whenever possible under existing data limitations, our sectoral ESG exclusion policies add a 'financing overlay' to the more traditional exclusions based on companies' direct involvement in controversial activities. Through this overlay, we exclude companies that play a major role in the *financing* of the economic activities we restrict – either through significant ownership stakes in directly involved companies, or through financing. Table 1 offers a summary overview of the ESG exclusions we apply across our funds at Firm level. More details are available in the next sections.

Table 1 – Overview of RI approaches at Firm level

	Article 8 Non Net Zero	**Article 8** Net Zero	**Article 9** Net Zero	**Financing Overlay** (all funds)
Norms (UNGC)	■	■	■	
Ethics – Controversial Weapons	■	■	■	■
Ethics – Tobacco	■	■	■	■
Ethics – Predatory Lending	■	■	■	■
Climate – Thermal Coal	■	■	■	■
Climate – Oil Sands	■	**	***	■
Climate – Arctic Oil	■	**	***	■
Climate – Oil and Gas		■	***	****
Ethics - Alcohol			■	■
Ethics – Military Contracting			■	■
Ethics – Small Arms			■	■
Ethics – Gambling			■	■

Note:** = stricter than for Article 8 non Net-Zero; *** = stricter than for Article 8 Net Zero; **** = only applies to Article 9

2. Norm-based Exclusions – UNGC

The ten UN Global Compact Principles are derived from the Universal Declaration of Human Rights, the International Labour Organization's Declaration on Fundamental Principles and Rights at Work, the Rio Declaration on Environment and Development, and the United Nations Convention Against Corruption. They are intended to lay out a framework for assessing corporate sustainability in view of a company's value system and a principles-based approach to doing business. The UNGC principles hence serve as a compass to assess companies' behaviour against their fundamental responsibilities in the areas of human rights, labour, environment, and anti-corruption.

By incorporating the Ten Principles of the UN Global Compact into business strategies, policies, and procedures, and establishing a culture of integrity, companies are not only upholding their basic responsibilities to people and planet, but also setting the stage for long-term success.

Algebris ESG research team carries out a UNGC screening underpinned by data from ESG data providers Vigeo Eiris (VE) and MSCI, as well as internal research. The aim of our UNGC screening is to minimize exposure to companies with especially poor practices in key UNGC-relevant areas and identify potential issues on which to engage with companies in the portfolio.

From an operational standpoint, the UNGC screening restricts investment in companies that are identified to be involved in very serious violations of any of the UNGC principles (human rights, labour rights, non-discrimination, environment, corruption). We define a very serious violation as the case of a company being involved in persistent UNGC-related controversies, where the controversy is of critical severity and the company is non-reactive.

3. Ethics Exclusions

Algebris applies several activity-based exclusions on grounds of ethics considerations. Investment in companies directly involved in the manufacturing of controversial weapons, manufacturing of tobacco products and predatory lending activities is restricted for all Algebris liquid funds. Algebris Article 9 Funds are subject to a broader range of ethical ESG restrictions.

Table 2 – Ethics Exclusion – Revenue Thresholds

	Article 8 Non Net Zero	**Article 8** Net Zero	**Article 9** Net Zero
Ethics – Controversial Weapons	0%	0%	0%
Ethics – Tobacco Products	0%	0%	0%
Ethics – Tobacco services	5%	5%	0%
Ethics – Predatory Lending	0%	0%	0%
Ethics - Alcohol			0%
Ethics – Military Contracting			0%
Ethics – Small Arms			0%
Ethics – Gambling			0%

3.1. Controversial Weapons

Certain weapons are internationally recognised as controversial and/or regulated by international conventions. While the scope of the definition will expand over time, at this date we consider the following types of weapons to be controversial:

- *Anti-Personnel Landmines (APLM):* APLM can indiscriminately kill or injure civilians, including children, peacekeepers, and aid workers. The use, stockpiling, production, and transfer of anti-personnel landmines is prohibited under the Ottawa Treaty (1997).

- *Cluster Munitions:* munitions designed to disperse or release explosive submunitions[1]. They pose a serious and indiscriminate threat to the civilian populations during and long after an attack. The use, stockpiling, production, and transfer is prohibited under the Convention on Cluster Munitions (2008).
- *Chemical and Biological Weapons:* complex systems that disseminate disease-causing organisms or toxins to harm or kill humans, animals, or plants[2]. The use, stockpiling, production, and transfer of these weapons is prohibited under the Biological Weapons Convention (1975) and the Chemical Weapons Convention (1997).
- *Nuclear Weapons and Depleted Uranium:* Nuclear weapons have the potential to kill millions and jeopardize the natural environment and lives of future generations through long-term catastrophic effects. The UN has long sought to eliminate them[3], and several multilateral treaties have been established with the aim of preventing nuclear proliferation and testing, while promoting progress in nuclear disarmament, including the Treaty on the Non-Proliferation of Nuclear Weapons (1968).
- *Non-Detectable fragments, incendiary, blinding laser weapons*: covered by Protocols I, III, and IV of the UN Convention on Certain Conventional Weapons (1980) which seeks to prohibit or restrict the use of weapons considered excessively injurious or with effects that are indiscriminate.

3.1.1 Companies directly involved in manufacturing of controversial weapons

Algebris will not invest in companies we believe to be involved in, and derive any (0%) revenue from, the manufacturing of controversial weapons (as above). This includes both companies involved in production of the core weapon system and companies providing components/services for the core weapon system even if they are not tailor-made or essential for the lethal use. Algebris will also not invest in any company having a significant ownership in the entities excluded under this rule.

3.1.2 Financers of Controversial Weapons

Transparency on the financing of controversial weapons is scarce, and the underlying data is still not collected by third-party ESG data providers. The limited data available is gathered by NGOs active in the field (eg. PAX, ICAN)[4] and it suffers from limited coverage and intermittent updates frequency. Yet, we consider this data to be value added to ESG integration in our investment process and we use it as an input to our controversial weapons exclusion framework.

Investors in Nuclear Weapons: Data on financing to the top-25 nuclear weapons producers published in 2021 by ICAN[5] shows that shareholding and loans constitute 81% of the outstanding financing to the top-25 nuclear weapons producers (Figure 1).

Algebris will not invest in debt or equity issued by the top-5 nuclear weapons shareholders and lenders – unless they have reduced their positions compared to the previous year. As of end 2021, the top-5 shareholders were[6]:

1. Vanguard (USD 50bn, down from USD 73bn in 2020)
2. State Street (USD 45bn, down from USD 60bn in 2020)

[1] As defined in the text of the Convention on Cluster Munitions: https://www.clusterconvention.org/

[2] See more information at: https://www.unog.ch/80256EE600585943/(httpPages)/29B727532FECBE96C12571860035A6DB?OpenDocument

[3] See the UN Office fo Disarmament Affairs work at: https://www.un.org/disarmament/wmd/nuclear/

[4] See the 2021 report "Perilous Profiteering: the companies building nuclear arsenals and their financial backers", the 2019 report "Shorting our Security: Financing the companies that make nuclear weapons" by ICAN and PAX, and the 2018 report "Worldwide investments in cluster munitions – a shared responsibility" by PAX.

[5] See the 2021 report "Perilous Profiteering: the companies building nuclear arsenals and their financial backers"

[6] See the 2021 report "Perilous Profiteering: the companies building nuclear arsenals and their financial backers"

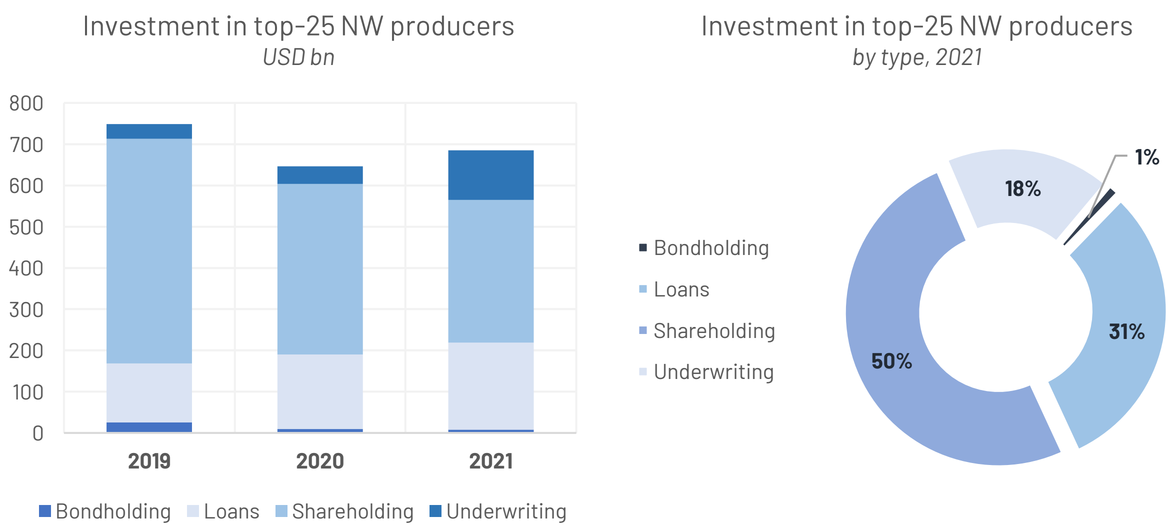
3. Capital Group (USD 42bn, down from USD 64bn in 2020)
4. BlackRock (USD 41bn, down from USD 53bn in 2020)
5. Wellington Management (USD 17bn, stable from 2020)

As of end 2021, the top-5 lenders were[7]:

1. Citigroup (USD 24bn, down from USD 28bn in 2020)
2. Bank of America (USD 19, down from USD 24bn in 2020)
3. JPMorgan Chase (USD 14bn, down from USD 17bn in 2020)
4. Wells Fargo (USD 12bn, down from USD 18bn in 2020)
5. Mitsubishi UFJ Financial Group (USD 9bn, down from USD 12bn in 2020)

As of December 2021, none of the top-5 shareholders or lenders qualified for exclusion under the rule described above. Data will be updated annually or depending on the frequency with which the underlying source report will be published.

Figure 1: Financing of the Top-25 Nuclear Weapons Producers



Source: Algebris based on PAX. As at November 2021.

Investors in Cluster Munitions: Algebris will not invest in debt or equity issued by the top-5 global investors in cluster munitions. As of 2019, these were: China Construction Bank (US$ 950 mn, 10.7% of total), China Merchants Group (US$ 940 mn, 10.6% of total), NongHyup Financial (US$ 527 mn, 6% of total), CSC Financial (US$ 475 mn, 5.4% of total) and National Pension Service, South Korea (US$ 427 mn, 4.8% of total)[8].

The List will be updated as soon as new data is released – with the addition of a dynamic policy focused on phasing out, aligned with the one we apply to investors in nuclear weapons.

[7] See the 2021 report "Perilous Profiteering: the companies building nuclear arsenals and their financial backers".

[8] This list is based on data compiled ny NGO PAX in the context of the "Worldwide investment in cluster munitions report". The data cover all investments found in the 7 producers of cluster munitions listed in the report.

Active Engagement with Global Bank: As an investor in global banks, we actively engage with investees on their controversial weapons investment and financing – particularly in the space of underwriting, which has increased in recent years. This engagement is carried out by the investment team on a case-by-case basis, when warranted by findings of the internal research process.

3.2. Predatory Lending

Predatory Lending broadly refers to any type of unscrupulous lending practice where a lender takes advantage of a borrower[9]. It usually involves borrowers being charged high-cost loans over a short-term horizon, with little or no credit checks, often with irresponsible collection practices. The lack of assessment of ability to repay can lead to the borrower being trapped in a cycle of loan renewals and debt accumulation[10]. Low-income, elderly, or otherwise vulnerable populations tend to be the target of this activity. During the Covid-19 pandemic, reports emerged of lenders targeting borrowers in financial difficulties, by circumventing advertising bans and other restrictions[11].

Common Predatory Lending practices include:

- *Payday Loans:* typically for small amounts and very short maturity, due in full by the borrower's next pay-check and charging Annual Percentage Rates (APR) well into three-digits territory. While payday loans are marketed as a way to cover emergency expenses, research shows that borrowers mostly use the loans to pay for recurring expenses[12] and that most payday loans are rolled over repeatedly[13].
- *High-interest Instalment Loans:* partly as a response to regulatory tightening on single payday loans, lenders have been diversifying into instalment loans[14] – with repayment stretching over a few months. By allowing borrowers to take on larger amounts of debt, however, these structures risk becoming a way for lenders to circumvent the regulatory caps on high interest rates existing for payday loans[15].
- *Rent to Own schemes:* contracts under which property such as furniture, consumer electronics, motor vehicles etc. are rented by the customer in exchange for weekly or monthly payment with an option to purchase at some point in the agreement. A typical contract may be for 12, 18 or 24 months and it can cost double or triple what the borrower would pay for the item with cash, on layaway, or on an instalment plan[16]. Moreover, the industry is renowned for abusive payment collection practices[17].

As a global investment manager with a historical focus on the financial sector, Algebris is especially careful not to invest in financial companies associated with these practices.

Algebris will not invest in debt or equity issued by companies that derive any revenues (0%) from predatory lending activities (as defined above). Algebris will also not invest in any company having a significant ownership in the entities excluded under this rule.

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[9] See https://www.law.cornell.edu/wex/predatory_lending

[10] See https://www.consumerfinance.gov/about-us/newsroom/cfpb-finds-four-out-of-five-payday-loans-are-rolled-over-or-renewed/

[11] See for example https://www.wsj.com/articles/how-payday-lenders-target-consumers-hurt-by-coronavirus-11591176601

[12] See https://www.pewtrusts.org/~/media/legacy/uploadedfiles/pcs_assets/2012/pewpaydaylendingreportpdf.pdf

[13] See: https://files.consumerfinance.gov/f/201403_cfpb_report_payday-lending.pdf

[14] For a discussion, see: https://www.pewtrusts.org/fr/research-and-analysis/issue-briefs/2016/08/from-payday-to-small-installment-loans

[15] See e.g. https://www.bloomberg.com/news/articles/2013-05-29/payday-lenders-evading-rules-pivot-to-installmant-loans?sref=ZROBPrgd or https://www.bloomberg.com/news/articles/2019-10-29/america-s-middle-class-is-getting-hooked-on-debt-with-100-rates?srnd=premium&sref=ZROBPrgd

[16] See https://www.consumer.ftc.gov/articles/0524-rent-own-costly-convenience

[17] See https://www.nclc.org/images/pdf/criminal-justice/report-rent-to-own-racket.pdf

3.3. Tobacco

Algebris supports the World Health Organisation (WHO) Framework Convention on Tobacco Control – the first global public health treaty, aimed at tackling some of the causes of the tobacco epidemics[18]. Tobacco has long been demonstrated to be unhealthy: more than 7 million people a year die as a result of direct use globally, and around 1.2 million deaths are the result of non-smokers being exposed to second-hand smoke – testifying that there is no safe level of exposure[19].

Tobacco is also a leading cause of impoverishment: as over 80% of the 1.3 billion tobacco users worldwide live in low- and middle-income countries, consumption can contribute to poverty by diverting household spending from basic needs such as food and shelter. Moreover, the sector has in the past demonstrated questionable work practices, and in some countries children from poor households may be employed in tobacco farming to boost family income.

Algebris will not invest in debt or equity issued by companies that derive any revenues (0%) from the manufacturing of tobacco products, and/or derive at least 5% of revenues from supply of tobacco-related products or services. For our article 9 funds this threshold is reduced to 0%.

Algebris will not invest in any companies having a significant ownership in the entities excluded under this rule.

3.4. Other Ethics Exclusions

For strategies with an enhanced sustainability profile (classified as Article 9 under EU SFDR[20]) , Algebris applies an additional set of ethical ESG restrictions. These strategies are prevented from investing in companies that derive any revenues from alcoholic beverages, gambling, military contracting and small arms.

4. Climate related Exclusions

Algebris Investments is committed to actively fight climate change. Aware that our largest impact on climate occurs through choices we make in our investment process, in 2021 we joined the **Net Zero Asset Managers Initiative (NZAM)**, committing to manage a progressively larger share of our AUM in line with net zero emissions by 2050 or sooner. To achieve this goal, we take a strict stance on investment in fossil fuels.

As set out in the 2018 IPCC 1.5 degrees scenarios and the 2021 IEA Net Zero scenario, achieving net zero by 2050 will require a rapid reduction in emissions from fossil fuel combustion and phase out of investment in fossil fuels. The pathway laid out in the IEA report requires that no new unabated coal plants, no new oil and gas fields, and no new coal mines or mine extensions be approved from 2021 on. In its guidance for the financial sector, the Science Based Target Initiative (SBTi) also recommends that financial institutions seeking to align with the Paris Agreement transparently address the role of fossil fuels in their investment portfolio. The SBTi recommended phaseout of thermal coal investments and more thorough disclosure on financial institutions' fossil fuel investments and related activities.

Algebris subscribe to these recommendations and applies strict limits to investment in fossil fuels.

[18] For more details see https://www.who.int/fctc/cop/about/en/

[19] See https://www.who.int/news-room/fact-sheets/detail/tobacco

[20] This currently comprises only the Algebris Green Transition Private Equity strategy

Table 3 – Climate Exclusion – Revenue Thresholds

	Article 8 Non Net Zero	**Article 8** Net Zero	**Article 9** Net Zero
Coal – Mining	5%	0%	0%
Coal – Power	10%	0%	0%
Arctic Oil	5%	0%	0%
Tar Sands	10%	0%	0%
Oil & Gas – Production		40%	0%
Oil & Gas – Power Generation			40%

The funds that the Firm has committed to manage in line with attaining net zero emission under our NZAM pledge ("Net Zero Aligned")[21] and article 9 funds, are prevented from investing in companies deriving any (0%) revenue from coal (mining and power generation), and/or companies pursuing significant coal power or coal mining expansion plans (regardless of the share of revenues they derive from coal). Our other strategies are also subject to strict limits.

Algebris also restricts investment in any company having a significant ownership in the entities excluded under this rule[22], and screens investment in banks and other financial institutions playing a significant role in global coal finance.

In particular, Algebris will not invest in debt or equity issued by the top-5 global coal shareholders and bondholders, nor in debt or equity issued by Agricultural Bank of China, Bank of China, China Construction Bank, Industrial Bank, China CITIC Bank and ICBC – which accounted for 50% of lending to the 30 top coal mining and coal power companies between 2016 and 2020[23]. Complementary to this exclusion, we monitor fossil fuel policies of global banks and aim to select names exhibiting relatively stronger policies and lower fossil fuel funding for our financial portfolios.

Besides coal, we also apply strict revenues thresholds to investment in companies operating in the production of unconventional oil and gas. Algebris' Net Zero aligned funds and article 9 funds, are prevented from investing in companies deriving any (0%) revenues from exploration/extraction of either Tar Sands or Arctic Oil. Algebris will also not invest in any company having a significant ownership in the companies excluded under this rule.

While having a significant footprint, conventional oil and gas are likely to remain a bridge fuel in the transition towards full decarbonization, at least in the short term and more so considering the recent geopolitical developments. Recent discussions on the inclusion of gas in the EU Taxonomy of sustainable economic activity, following the late 2021 spike in energy prices, provide further evidence to this effect. At the same time, the IEA 2050 Net Zero report recommends that no new oil and gas levels fields be approved for development starting from 2021.

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[21] At the moment, these are: Algebris Financial Credit Fund, Algebris Financial Credit Fund IG, Algebris Financial Equity Fund, Algebris Financial Income Fund, Algebris Long Only, Algebris Financial Bond Fund, Algebris Green Transition Fund. See our Net Zero Asset Managers commitment disclosure for details.

[22] Significant ownership data are sourced from ESG data provider Sustainalytics. Significant ownership is typically defined as an ownership stake of 10% or above.

[23] Based on the data collected by the BankTrack and 5 other NGOs in the report "Banking on Climate Chaos – Fossil Fuel Report 2021"

For all the Algebris Funds managed in line with attaining net zero emissions by 2050 or sooner, we therefore restrict investment in companies that derive more than 40% of revenues from the production of conventional oil and gas. Our Article 9 Green Transition Strategy is subject to stricter restrictions.

More details on these climate-related exclusions are available in our fossil fuel policy and in our Net Zero methodological documents – both available on our website.

5. Implementation

5.1. Monitoring, Control and Transparency

The Firm will at all times maintain an exclusion list (the "Exclusion List") of companies that meet the criteria listed above. This list is compiled by the Algebris ESG team, combining data from specialized ESG data providers, data published by NGOs, as well as internal research.

The Exclusion List will be updated at least once a year, or more frequently to respond to relevant developments.

All ESG exclusion lists are coded into the Algebris Order Management System ("OMS"). The OMS has fully integrated pre- and post-trade controls which include the relevant investment guidelines for a particular fund, and restricted/black-lists and any additional risk limits that may be required. Any attempts at trading a security that is restricted on ESG grounds would trigger a pre-trade alert.

Breaches of ESG pre- and post-trade controls are communicated systematically to the ESG Committee as well as representatives from the Risk, Trading and Compliance departments via automated e-mail notification. Algebris has also set up a dedicated ESG incident log – under the more general risk log – where any breach or incident related to the application of the Firm's ESG policy and exclusion lists is timely recorded and then followed upon resolution.

Any breaches will be rectified as soon as reasonably practicable. If an Algebris Fund holds positions in a company that is subsequently added to any of the ESG exclusion lists, the fund will exit such positions as soon as reasonably practicable and, in any event, no later than thirty (30) days after the most recent exclusion list update.

In its FI-R11 recommendation, the Science Based Target Initiative (SBTi) urges financial institutions to disclose the value of their annual investments (public equity, private equity, corporate bonds), direct project financing and lending to fossil fuel (oil, gas, and thermal coal) projects and companies. Algebris firmly believes in transparency, and the Firm is committed to publish aggregate data on exposure to companies active in fossil fuel industries across its portfolios in its end-year Climate reporting, starting in 2022.

5.2. Baskets and Indices

The assessment of the ESG eligibility or ESG-related credentials of holdings that comprise securities issued by more than one issuer (e.g. basket of securities, ETF or indexes) or assets with no issuer (e.g. futures on commodities or basket of commodities) is based on their breadth and theme concentration. Indices or baskets with a large number of constituents and no theme or generic themes (e.g. S&P500) are not subjected to ESG restrictions. Narrower and often industry specific baskets/indices are reviewed, and if these are found to comprise high concentration of ESG excluded issuers or assets that contradict the eligibility ESG criteria, then these shall also be removed from the investable universe.

The concentration assessment is performed pro-rata, based on either the weights assigned to the constituents, or, in their absence, based on the market value of the constituents. A concentration limit of 25% in excluded issuers shall lead to exclusion. Indices/baskets with lower concentration may also be excluded, if the theme and/or the objective of the investment (where this is defined, e.g. in ETFs) contradicts the eligibility ESG criteria applied to single securities. Concentration analysis is performed on an annual basis, when material changes to indices are identified, or at the pre-investment phase for baskets/indices that have never been assessed.

5.3. Derivatives

The assessment of the ESG eligibility or ESG related credentials of a derivative holding is performed on a look-through basis, by assessing the underlying of the derivative. When the underlying is a transferable security (stock, bond etc), then the issuer of the underlying is examined, following the same approach defined for direct (non-derivative) holdings. In the case of a basket of transferable securities or a reference to such basket (an index, for example), a look-through approach is followed based on the constituent securities and not on the issuer of the index/basket (see section 4.1). In case where no tangible transferable security can be established as the underlying (e.g. an interest rate swap), the derivative in question is not assessed for its ESG credentials.

For all derivative holdings, irrespective of whether they are securities or baskets, any ESG considerations are only made when the resulting economic effect of the holding benefits from a rise in the value of the underlying (bull position), for example a short position on put option on a security or a short position on an inverse ETF. Conversely, positions that benefit from a fall in the value of the underlying (bear positions), are not subjected to ESG restrictions.

5.4. Exemptions

In limited and rare occasions, exemptions to the general rules outlined above might be considered. In principle, exemptions could concern:

- Affiliates of restricted companies, which may be allowed if their activity is not related to the excluded fossil fuels, and in any case subject to an enhanced due diligence by the ESG team.
- Green bonds or sustainability bonds emitted by restricted companies, which may be allowed subject to an enhanced due diligence by the ESG team.
- Companies that exceed the revenue thresholds only marginally, but that display credible transition plans and track record may be allowed, subject to an enhanced due diligence by the ESG team.

These exemptions are intended to remain exceptional, and they will be transparently made public. As of December 2021, only one such exemption had been authorized by the ESG team – pertaining a company exceeding the exclusion thresholds in our coal sector policy - and this case is discussed in detail in our fossil fuel policy.