ALGEBRIS INVESTMENTS FOSSIL FUELS INVESTMENT POLICY

2022

Algebris Investments (the "Firm" or "Algebris") is committed to responsible investing, and a key part of this commitment is 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 degree 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 indicated 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 recommends phaseout of thermal coal investments and more thorough disclosure on financial institutions' fossil fuel investments and related activities.

This document outlines Algebris' policy with regard to investment in the fossil fuels industry (summarised in the tables below). The policy applies to all Algebris Article 8 and Article 9 funds – with a distinction between strategies that we have already committed to manage in line with attaining net zero emission under our NZAM pledge ("Net Zero Aligned")[1], and strategies that are not yet committed. Further details on the individual exclusions are available in the dedicated sections.

Exclusion thresholds for companies that are directly involved in a restricted activity (e.g. thermal coal mining) are based on the share of total revenues that those companies derive from such activities. This gives us an indication of how reliant a certain business is on activities that we deem environmentally harmful and progressively less and less viable from an economic standpoint.

Whenever feasible based on (currently scarce) available data, we also add to exclusions a financing overlay, focusing on the financing chain of restricted activity. This overlay targets companies that, while not being *directly* involved in a restricted activity, are responsible for a significant share of the outstanding global financing available for such activity.

Exclusion Thresholds – overview across strategies

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

Watchlist rule (fracking, CBM, heavy, ultra deep-water oil)

	Article 8 Non-Net Zero Aligned	**Article 8** Net Zero Aligned	**Article 9** Net Zero Aligned
Unconventional % of production	--	≥ 40%	≥ 40%
Short-term expansion	--	20 mmboe	20 mmboe
Unconventional % of expansion	--	≥ 50%	≥ 50%

[1] As at January 2022, 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. These represent 79% of our AUM excluding mandates, as at December 2021. See our Net Zero Asset Managers commitment disclosure for details.

1. Thermal Coal Mining and Power Generation

Coal emits the highest amount of CO_2 in relation to the energy it produces when burnt. In its 2018 report, the IPCC estimated that primary energy from coal must decrease by 59-78% by 2030 compared to 2010, for the world to have a chance at limiting global warming to 1.5°C. The net zero pathway laid out in the IEA 2021 report requires that no new unabated coal plants and no new coal mines or mine extensions be approved from 2021 on. Coal is also becoming an increasingly un-economic investment: research shows that the share of uncompetitive coal plants is on track to hit 73% by 2025[2] globally, with peaks of 95% and 85% in China and India respectively. And yet, according to publicly available data compiled annually by the German NGO Urgewald, many new coal plants are still being planned or are under construction.

The SBTi urges financial institutions to reduce exposure to thermal coal as quickly as possible and to reach zero by 2030. This includes immediately ceasing all financial support to thermal coal companies[3] that are building new infrastructure or investing in new or additional expansion, mining, production, utilization, retrofitting, or acquiring of coal assets. The Paris Aligned Investment Initiative similarly recommends that no additional capital be allocated to companies planning or constructing new thermal coal projects and infrastructure, and that existing shareholders and bondholders in such companies engage to ensure no new thermal coal generation is developed.

Algebris subscribes to these recommendations and thinks coal extraction and power generation shall be stopped as a matter of priority. For all the Algebris Funds that are managed in line with the objective of Net Zero Emissions by 2050 or sooner, we apply the following restrictions to investment in companies connected to thermal coal.

Direct Involvement: investment in companies directly involved in thermal coal mining and/or thermal coal power generation is subject to strict limits (see table below). Our Net Zero aligned funds are prevented from investing in companies deriving any revenue from coal. All other funds are prevented from investing in companies deriving more than 5% of their revenue from coal mining and/or more than 10% of their revenue from thermal coal power generation. We also restrict investment in any company that has a significant ownership in the companies excluded under this rule[4].

Exclusion threshold (% of company's revenues)

	Article 8 Non-Net Zero Aligned	**Article 8** Net Zero Aligned	**Article 9** Net Zero Aligned
Thermal Coal - Mining	5%	0%	0%
Thermal Coal – Power Generation	10%	0%	0%

Expansion: in line with the recommendations put forward in the IEA 2050 Net Zero report, for our Net Zero aligned funds we also exclude companies that are listed on the Global Coal Exit List (GCEL) as having coal power or coal mining expansion plans – regardless of the share of revenues they derive from thermal coal. These are companies planning to develop new coal-fired power capacity of at least 100 MW, or companies engaged in coal exploration activities, planning to develop new coal mines or planning a significant increase of at least 1 Mt annual thermal coal production.

Coal Investors and Financers: Many banks and investors are still involved in coal finance. Algebris is a global investment manager with a historical focus on financials, with over 80% of the Firm's AUM invested in this sector and a clear investment bias to high quality Global Systemically Important Financial Institutions (G-SIFIs). We believe that financial institutions are gatekeepers of the transition to a greener and more sustainable economy, due to the role

[2] Rocky Mountain Institute (2020), Carbon Tracker Initiative, Sierra Club 2020. "How to Retire Early: Making Accelerated Coal Phaseout Feasible and Just"

[3] Coal companies are defined as companies with greater than 5% of revenues from thermal coal mining, exploration and drilling, mining services, processing, trading, transport and logistics, equipment manufacturing, operations and maintenance (O&M) services, engineering, procurement and construction (EPC) services, transmission and distribution of coal-fired electricity, coal to liquids (CtlG) and coal to gas (CtG).

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

they play in allocating capital across sectors. As such, coal finance is an activity we monitor closely, in our investee banks. We apply the following financing overlay across all funds:

- **Coal equity and bond holding**: the buyers of coal plant developers' bonds and shares are the ultimate enablers of new coal business. Algebris will not invest in debt or equity issued by the top-5 global coal share and bondholders – each accounting individually for more than 2% of global share and bondholding in coal power plant developers who are planning expansion. In 2020, these were[5]: BlackRock (8% of total), Vanguard (8%), Capital Group (4%), State Street (3%) and Japan's Government Pension Investment Fund (3%).

- **Coal Lending**: banks have a key role to play through restrictions on their own lending policy towards harmful activities like coal mining and coal power generation. Algebris will not invest in debt or equity issued by Agricultural Bank of China, Bank of China, China Construction Bank, Industrial Bank, China CITIC Bank and ICBC. These banks accounted for 50% of lending to the 30 top coal mining and coal power companies between 2016 and 2020, and each accounted individually for more than 6% of the total loans extended over the same period[6]. Complementary to this exclusion, we monitor the fossil fuel policies of major global banks and aim to select names exhibiting stronger policies and lower fossil fuel funding as part of our financial portfolios.

2. Unconventional Oil and Gas

Unconventional hydrocarbons such as shale oil and gas extracted by fracking, tar sands oil and coalbed methane or Arctic oil and gas are particularly harmful for the environment and are often more carbon- and methane-intensive than conventional oil and gas.

a. Tar sands

Tar sands are one of the most destructive and carbon-intensive means of oil production. The extraction process of tar sand deposits that are relatively close to the surface has an environmental impact comparable to that of lignite mining – typically involving deforestation, draining of wetlands and alteration of the natural course of rivers and streams. The production of one barrel of bitumen from open pit mining requires 3 to 4 barrels of water, and yields as a by-product a poisonous slurry that is typically stored in tailings ponds exposed to high leakage risks[7]. Deeper tar sands deposits are exploited though in-situ extraction methods that do not require tailings ponds, but generate wastewater that can seep into the surrounding soil.

b. Arctic Oil

The exploration and drilling of oil in the Arctic poses the risk of an irreversible severe impact on a unique ecosystem, and risks accelerating climate change in a region already very exposed to it[8]. Climate change makes onshore oil and gas extraction in the Arctic easier, and at the same time more dangerous. As the Arctic tundra is thawing due to global warming, this creates gigantic sinkholes and destabilizes the ground under pipelines and waste pits, making spills of wastewater, gas and oil more likely. Moreover, oil and gas production and the connected industrialization emits soot (black carbon), which falls onto the nearby ice and turns it black. As a consequence, the ice absorbs more heat, melts faster, and accelerates the warming.

c. Fracking

Fracking is an extraction method used to access gas and oil trapped in deep rock formations, by pumping fracking fluid into the ground to crack open the rock and release the trapped hydrocarbons. To extract unconventional oil and gas through fracking, companies need to drill more wells than for conventional oil and gas production, thus increasing the risk of gas leaks and severely affecting the natural landscape. Fracking also poses a threat to ground and surface water. The extensive use of water increases the risk of water shortages and droughts in fracking regions. Oil, gas or

[5] Based on the data released by Urgewald, Banktrack and other NGOs, and accessible here: https://coalexit.org/finance-data.

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

[7] See the Global Oil and Gas Exit List: https://gogel.org/en/

[8] According to the Intergovernmental Panel on Climate Change (IPCC), the Arctic is heating up twice as fast as the rest of the globe. See: https://www.ipcc.ch/2021/08/09/ar6-wg1-20210809-pr/

fracking fluids can seep through the cracks in the rock and into the groundwater. In addition, spills, deliberate dumping or inadequate storage and disposal of fracking fluid or wastewater contaminate soil and surface waters.

d. Extra Heavy Oil, Ultra Deepwater, CBM

Extra heavy oil is a high-density oil, difficult to produce, transport and process. Its recovery is very water-intensive and production often draws from the same water source as neighbouring communities, increasing the risk of water shortages. Extra heavy oil is chemically complex, and it contains heavy metals and high levels of sulfur. The removal of this component creates toxic waste that can leak into the environment.

Ultra deepwater wells are located at least 1,500mt below sea level. This production is riskier than offshore production on the shelf, as accidents at these depths are almost uncontrollable and can have catastrophic effects. While the risk of accidents is the biggest threat related to ultra deepwater production, routine drilling can also have severe impacts on the fragile ecosystems at the bottom of the sea.

Coalbed Methane (CBM) is fossil gas, trapped by pressurized water in coal seams located between 200 and 1,100 meters underground. Extraction typically requires a combination of dewatering and fracking, which can have negative effects on the groundwater level. The water that is pumped out of the coal seams contains heavy metals and radioactive components, posing the risk that leaks can contaminate surface waters or seep into groundwater supplies.

Our Net Zero aligned funds are prevented from investing in companies deriving any (0%) revenues from exploration/extraction of either Tar or Arctic oil. All other funds are subject to strict revenues thresholds when investing in companies operating in those areas (10% of revenues for Tar Sands and 5% for Arctic). Algebris will also not invest in any company having a significant ownership in the companies excluded under this rule (see table below).

We currently do not have data tracking the share of companies' revenues derived from fracking, CBM, extra-heavy oil and ultra deep-water oil, although we expect most of these to currently fall within the perimeter of what our ESG data provider Sustainalytics includes in the total revenues from oil and gas (see next section). However, we use the data collected in the Global Oil and Gas Exit List (GOGEL) as an input to the investment process and we strictly watchlist investment in companies for which (i) these unconventional fuels account for 50% or more of total production, and which are (ii) planning significant short term expansion, where (iii) the majority (50% or more) of this expansion is unconventional. Investment in companies fitting this profile is subject to closer scrutiny by Algebris ESG team, and we expect to be adding a revenue-based exclusion threshold in the future, as soon as the data needed will become available.

Exclusion threshold (% of company's revenues)

	Article 8 Non-Net Zero Aligned	**Article 8** Net Zero Aligned	**Article 9** Net Zero Aligned
Oil Sands extraction	10%	0%	0%
Arctic oil & gas exploration	5%	0%	0%

Watchlist rule (fracking, CBM, heavy, ultra deepwater oil)

	Article 8 Non-Net Zero Aligned	**Article 8** Net Zero Aligned	**Article 9** Net Zero Aligned
Unconventional % of production	--	≥ 50%	≥ 50%
Short-term expansion	--	32 mmboe	32 mmboe
Unconventional % of expansion	--	≥ 50%	≥ 50%

3. Conventional Oil and Gas

While having a significant footprint, conventional oil and especially gas are likely to remain a bridge fuel in the transition towards full decarbonization, at least in the short term. Recent discussions on the inclusion of gas in the EU Taxonomy of sustainable economic activity, following the late 2021 spike in energy prices, provide clear 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.

For all the Algebris Funds managed in line with attaining net zero emissions by 2050 or sooner, we restrict investment in companies that derive more than 40% of revenues from the production of conventional oil and gas. Our Article 9 Green Transition Fund is subject to stricter restrictions on account of its thematic focus (see table below).

Exclusion threshold (% of company's revenues):

	Article 8 Non-Net Zero Aligned	**Article 8** Net Zero Aligned	**Article 9** Net Zero Aligned
Oil & Gas – Production	--	40%	0%
Oil & Gas – Power Generation	--	--	40%

4. Implementation

4.1 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 specialised ESG data provider Sustainalytics, 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.

4.2 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 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.

4.3 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. 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 reported in Algebris end-year Climate report. As of December 2021, only one such exemption had been authorised by the ESG team (see box 1 for a detailed discussion of this particular case).

BOX 1 – Case Assessment: Public Power Corporation (PPC)

In July 2021, the ESG team authorised one of Algebris funds to buy a sustainability-linked bond issued by the Greek utility company **Public Power Corporation (PPC)**. PPC would have been restricted according to the thermal coal policy that Algebris had in place at the time of the request, because the company derives more than 10% of its revenues from thermal coal power generation. Following enhanced due diligence on the company and the specific bond, the ESG team decided to authorise the trade based on the following considerations:

1. PPC has a very ambitious decarbonization plans and a track record of reducing Scope1 emissions fast over the past 2 years (-9Mtons from 2017 to 2019).
2. PPC has embarked on a lignite decommissioning plan, aiming to shut down all existing lignite plants by 2023 and exit from coal completely by 2025. PPC also committed to gradually shut down all mines by 2023, except for one mine which will continue to serve one specific plant until 2025. After that date, the plant will be converted to a combined-cycle gas turbine.
3. Concurrent to the phaseout from lignite, PPC plans to step up significantly its Renewable Energy Sources (RES) capacity. From <2% 2019, RES generation is planned to reach ~15% in 2023.
4. PPC's transition plan has been included in the National Energy and Climate Plan submitted by the Greek Government to the EU Commission in December 2019, and hence is subject to strict independent oversight.
5. Algebris' exposure to PPC is accrued through a Sustainability-Linked Bond (SLB) linking the interest rate payable to achievement of a de-carbonization target (57% reduction in Scope 1 emissions by end-2023 compared to an end-2019 baseline). From and including 2024, the interest rate payable on the SLB will increase by 0.5% per annum (Target Step-Up) unless PPC notifies the Trustee and Paying Agent that it has attained the Sustainability Performance Target and received an Assurance Letter from a third party evaluator.
6. PPC's SLB Framework has been assessed by Sustainalytics to be in line with the core components of the SLB Principles. Sustainalytics also came to an overall positive conclusion regarding materiality and strength of the selected KPI, its alignment with PPC's sustainability strategy, and credibility of the methodology used for the calculations.
7. The European Bank for Reconstruction and Development (EBRD) invested EUR 75.5 mn across two SLBs issued by PPC, in what is the first SLB subscription ever by the EBRD. The EBRD's Environmental and Sustainability Department undertook an in-house due diligence on PPC that produced a positive outcome.