PortfoLion

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# PortfoLion Venture Capital Fund Management Co.

# INVESTMENT SUSTAINABILITY RISK MANAGEMENT POLICY

Date of entry into force: 20.06.2024

Board resolution approving the regulations: 04/2024 (06.20.)

Budapest, 06.20.2024

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Issuing:
András Molnár,
CEO

## CONTENT





PortfoLion Capital Partners
PORTFOLION KOCKÁZATI TŐKEALAP-KEZELŐ ZRT
1123 Budapest, Alkotás utca 53. C épület V. emelet
-36 1 298 3370 info@portfolion.hu www.portfolion.hu

## I. INTRODUCTORY PROVISIONS

I.1. Under Regulation 2019/2088 on sustainability-related disclosures in the financial services sector adopted by the European Parliament and the Council (from now on: **SFDR Regulation** ), PortfoLion Venture Capital Fund Management Co. (from now on **PortfoLion, Fund Manager** ) is obliged to integrate into its procedures on the one hand, all relevant sustainability risks that may have a significant and relevant negative impact on the financial return of your investments, and on the other hand, all environmental and social impacts that can be considered material from a sustainability point of view. The Fund Manager is obliged to publish information on integrating sustainability risks into the investment decision-making process and also ensure the transparency of information related to adverse effects on sustainability factors.

I.2. The Investment Sustainability Risk Management Policy (from now on: **Policy)** describes in general the sustainability risk management principles that PortfoLion applies during its investment activities, and also defines the publication procedure for information related to adverse effects on sustainability factors

I.3. This Investment Sustainability Risk Management Policy was approved by the Board of Directors of PortfoLion on 07.07.2023 with resolution No. 122023 (07.07.). At the same time, the executive director's directive of the same name will be repealed.

## II. GENERAL PROVISIONS

### II.1. SCOPE OF THE SUSTAINABILITY POLICY

II.1.1 The material scope of this Policy covers all investment and portfolio management activities that the Fund Manager is entitled to perform based on the activity licenses issued to the Portfolio, and for which the creation and operation of the Policy is mandated by law. This Policy applies primarily and primarily to the individual investment decisions of the funds managed by the Fund Manager.

II.1.2. The personal scope of this Policy covers the employees of the Fund Manager and the Funds managed by it, who participate in the investment activities and participate in investment decision-making and/or its implementation, as well as persons in other legal relationships related to work, as well as persons considered to be persons in a senior position concerning PortfoLion.

### II.2. CONCEPTS

#### II.2.1. Double Materiality – double effect:

(a) Financial materiality – evaluation of how ESG (environmental, social, corporate governance) risks affect the value of the portfolio company,

(b) Impact materiality - evaluation of how the portfolio company's activities affect its physical and social environment in the broadest sense.

The link between the two impacts is created by the assumption that market and regulatory mechanisms assign a financial value to impact materiality.


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### II.2.2. Sustainability / ESG risk:

an environmental, social or management event "ESG event" ( **E** : Environmental- **S** : Social, **G** : Governance) or circumstance, the occurrence or existence of which may have an actual or potential significant negative impact on the value of the investment.

The sustainability risk is, among other things, physical or transitional, which are determined primarily from the perspective of climate change. Based on this approach, we can talk about climate risks, which are the financial risks that arise or increase as a result of climate change:

a) **physical risk of sustainability:** Physical risks are risks affecting the business that arise from the physical effects of climate change. These include:
   - *Acute physical* risks arising from specific events, especially weather-related events such as storms, floods, fires or heat waves, which can damage production facilities and disrupt value chains.
   - *Chronic physical* risks resulting from longer-term changes in climate, such as temperature changes, rising sea levels, declining water supplies, loss of biodiversity, and changes in land and soil productivity.

b) **The transition risk of sustainability:** risks affecting the business that arise from the transition to a low-carbon and climate-resilient economy. These include:
   - *political risks* , such as energy efficiency requirements, carbon pricing mechanisms that increase the price of fossil fuels, or policies that encourage sustainable land use.
   - *Legal risks* , such as the risk of legal disputes arising from failure to avoid or minimize adverse effects on the climate or failure to adapt to climate change
   - *Technological risks* , for example, if a less climate-damaging technology replaces a more climate-damaging technology.
   - *Market risks* , for example, if the choices of consumers and corporate customers shift towards products and services that are less damaging to the climate.
   - *Reputational* risks, for example, it is difficult to win and retain customers, employees, business partners and investors if the business is known to harm the climate.

### II.2.3. Sustainability/ESG rating:

means the assessment of the following sustainability risks and the classification based on them, which are the main constituent elements of risks:

(a) Environmental and Climate-related Risks

(b) Social Risks

(c) Governance Risks


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### II.3. RELATED GUIDELINES, LEGISLATION, SUPERVISORY REGULATORY DOCUMENTS

#### II.3.1. Related guidelines, legislation, supervisory recommendations, circulars that form the basis of this instruction

a) The SFDR regulation.

b) Regulation (EU) 2020/852 of the European Parliament and of the Council (June 18, 2020) establishing a framework for the promotion of sustainable investments and amending Regulation (EU) 2019/2088

c) MNB executive circular issued in connection with Decree 2019/2088 on sustainability-related disclosures in the financial services sector.

d) Delegated Regulation (EU) 2022/1288 of the European Parliament and Council Regulation (EU) 2019/2088 defining in detail the content and presentation of information related to the principle of avoiding significant harm, as well as the content of information related to sustainability indicators and adverse effects from a sustainability perspective, its methodology and presentation, as well as the addition of regulatory technical standards that determine the content and presentation of information in pre-contractual documents, websites and periodic reports related to the promotion of environmental and social characteristics and sustainable investment objectives. (RTS regulation)

## III. DETAILED PROVISIONS

### III.1. GENERAL PRINCIPLES OF MANAGING SUSTAINABILITY RISKS

III.1.1 The evaluation of ESG risks is validated during the evaluation of the portfolio companies of the Funds managed by the Fund Manager, with a qualitative evaluation of the business model and corporate governance practices of these portfolio companies according to the criteria set out in the appendix.

III.1.2. Paying attention to technological development, the changing regulatory and complex and significantly changing market environment, as well as the development of ESG metrics and their data sources, the Fund Manager develops a broad and comprehensive risk management system that effectively identifies, measures, monitors and controls risks. , and reviews this risk management procedure annually and, if necessary, amends or supplements it.

III.1.3. The starting point of the ESG risk assessment of the Funds is the ESG assessment of the investment target companies. Which is reviewed in the first quarter of each year by the Fund Manager for all portfolio companies. He will then publish this in the Q1 monitoring reports.

III.1.4. After the entry into force of the regulation, the ESG evaluation of the new investment target companies must be examined. It is necessary to evaluate the obtained result and incorporate this into the investment proposals, thus communicating the ESG evaluation of the target company to the decision-making committee.


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## III.2. THE FUND MANAGER'S POLICY REGARDING THE TRANSPARENCY OF THE MAIN ADVERSE EFFECTS OF THE INVESTMENT DECISIONS ON SUSTAINABILITY FACTORS - THE DUE DILIGENCE POLICY

### III.2.1. Evaluation of sustainability / ESG risks

III.2.1.1. The ESG risk of target companies and portfolio companies is evaluated by filling out the qualitative questionnaire included in the appendix. The ESG risk questionnaire reflects the consensus established in a meeting with the top manager (or an employee delegated by him) of the target company or portfolio company.

III.2.1.2. Interpretation of categories:

| **Interpretation of internal sustainability risk categories** |
|---|
| **Low (AB)** : This category reflects good or excellent ESG performance and a high degree of transparency in the public disclosure of ESG data. These investments have minimal or small environmental and social risks and impacts. |
| **Medium (CD)** : Reflects satisfactory ESG performance and moderate transparency in the public disclosure of ESG data. These investments have limited environmental and social risks and impacts, which can be easily prevented or mitigated through appropriate action plans and measures. |
| **High (EF)** : Reflects weak ESG performance and insufficient transparency in the public disclosure of ESG data. These investments require a more complex risk assessment. |

calculated from the product of the scores obtained and placed on the 6-point classification scale.

| **Classification category** | THE | B | C | D | E | F |
|---|---|---|---|---|---|---|
| **ESG score** | 9 | 6 | 4 | 3 | 2 | 1 |

low Portfolio ESG risk high

III.2.1.3. The sustainability risk classification of portfolio companies and portfolios must be reviewed annually, based on the values of ESG ratings and market values as of the last day of the previous calendar year.

### III.2.2. Targeted exclusion policies

The Fund Manager introduces an Exclusion Policy for the implementation of the investment policy of the portfolios based on the individual ratings determined according to the ESG rating methodology explained above.

The Fund Manager acts in accordance with the standards of the International Labor Organization (ILO), the United Nations Guiding Principles (UNGP), the United Nations Global Compact (UNGC) and the Organization for Economic Co-operation and Development (OECD) guidelines for multinational enterprises, these international agreements guide the assessment of companies' behavior.

In all cases, these general exclusions apply. Also, if there are laws prohibiting the application of exclusions in force in a specific country.

The Fund Manager applies a targeted exclusion policy during its investment management activities, the background of which is the adoption of the provisions and general exclusions of international conventions. One of the directions of these exclusion policies is to take action against companies that violate their obligations established by an international convention on ethics, business or human rights, or that behave against the principles and goals defined therein and internationally accepted.

- Absolute exclusions
    - that repeatedly and seriously violate [1]one or more of the ten principles of the Global Compact without taking credible corrective action.
- Industry Specific Exclusions
    - Arms trading companies
    - Companies active in the tobacco trade
    - Companies engaged in the production or distribution of palm oil, whose main profile is this
    - A game of chance
    - Companies involved in the trade or production of radioactive materials, excluding medical or quality control devices, or devices where the radioactive materials are insignificant or protected
    - Companies engaged in the production or trade of asbestos, with the exception of asbestos-containing cement sheets with an asbestos content of less than 20%
    - Companies using exploitative forced labor or harmful child labor.
    - Companies that generate income by trading, producing or storing large quantities of hazardous chemicals.
    - Companies engaged in the extraction and sale of thermal coal, excluding metallurgical coal or steel coal.
    - Companies dealing with GMO-related activities .
    - Pornography
- Exclusion of companies classified as high ESG
    - As a result of the qualitative questionnaire, the company classified in the high category is automatically excluded.

### III.3. SUSTAINABILITY RISK APPETITE

III.3.1. The Fund Manager, as one of the most important venture capital investors in the Central and Eastern European region, has a significant impact on its wider environment. In connection with maintaining the sustainability risk appetite at an appropriate level, the Fund Manager is committed to improving ESG performance, responsible business activity and a long-term approach. The primary goal of the Fund Manager is to facilitate the direction of capital flows towards sustainable investments.

### III.4. SUSTAINABILITY RISK MONITORING AND ACTION PLANS

III.4.1. As a primary line of defense, the investment directors of the Fund Manager's funds are responsible for monitoring whether the sustainability risk of the given target company or portfolio company is in line with the risk appetite.

III.4.2. If the sustainability risk level of a given portfolio company exceeds the sustainability risk-taking willingness, the portfolio managers are obliged to take measures to reduce the risk.

[1]UN Global Compact: "A call for companies to align their strategies and operations with the universal principles of human rights, labor, environmental protection and anti-corruption, and take action to achieve social goals.


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If the adverse effects are confirmed or the portfolio companies do not make sufficient progress towards the escalation strategy, it may also lead to an exit from the investment.

### III.5. SUSTAINABILITY RISK REPORTING AND DISCLOSURES

III.5.1. In order to comply with legal requirements, the Fund Manager publishes these regulations and its annexes in electronic format, in a searchable manner, on its website. In case of amendments to these regulations, the Fund Manager will also publish an explanation of the amendment.

## IV. FINAL PROVISIONS

IV.1. This administrative instruction will enter into force on the day after its publication, 20.06.2024, and at the same time repeals the CEO's instruction adopted on 07.07.2023 "on the adoption of regulations for the evaluation and integration of sustainability risks".

IV.2. The annual review was carried out during which the policy was updated. There was no extraordinary case that would have required a mid-year adjustment.

IV.3. The Fund Manager shall revise this Policy at least annually, or in exceptional cases (for example, in the event of a significant organizational change in the Fund Manager or a significant change in the relevant regulatory environment) without delay.

Appendix:

1. Annex no.: ESG evaluation table
2. Annex no.: Evaluation guide and instructional questions



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**1. no. Appendix**

## PORTFOLIO ESG EVALUATION BOARD

| | | Double effect | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | Risk | | | Effect | | | Relevance |
| | | *Low (- 10)* | *Neutral (0)* | *High (+10)* | *Negative (-10)* | *Neutral (0)* | *Positive (+10)* | (0-1) |
| ENVIRONMENTAL | | | | | | | | |
| 1. | Climate and Energy | | | | | | | |
| 2. | Responsible consumption and waste management | | | | | | | |
| 3. | Biodiversity and Toxicity | | | | | | | |
| SOCIAL | | | | | | | | |
| 4. | Food and Poverty | | | | | | | |
| 5. | Health and Wellbeing | | | | | | | |
| 6. | Culture and Learning | | | | | | | |
| 7. | Equity and Equal Opportunities | | | | | | | |
| GOVERNMENTAL | | | | | | | | |
| 8. | Business ethics and corruption | | | | | | | |
| 9. | Data Protection and Data Rights | | | | | | | |
| 10. | Transparency and Control | | | | | | | |
| | | Aggregate risk result | | | | Aggregate effect result | | |

| **Final classification:** |
|---|

## 2. no. Appendix

### Evaluation guide and instructional questions:

During the evaluation, it is also necessary to determine a degree of relevance on a scale from 0 to 1.
If the given factor is not relevant for the examined company, then the relevance level is 0. If it is relevant and necessary to examine that factor in the investment, then the relevance level is 1.
When asking questions about risk and impact, it is necessary to indicate the determined risk and impact level in the auxiliary table. After answering all questions, the board calculates the aggregated risk and impact value.

Based on the scores of the evaluation board, we applied the following classification:

| **Risk:** | **Effect:** |
|---|---|
| ***Low*** between -100 and -30 (3 points) | ***Negative*** between -100 and -30 (1 point) |
| ***Neutral*** between -30 and +30 (2 points) | ***Neutral*** between -30 and +30 (2 points) |
| ***High*** between +30 and +100 (1 point) | ***Positive*** between +30 and +100 (3 points) |

calculated from the product of the scores obtained and placed on the classification scale.

| **Classification category** | **THE** | **B** | **C** | **D** | **E** | **F** |
|---|---|---|---|---|---|---|
| **ESG score** | 9 | 6 | 4 | 3 | 2 | 1 |

ESG rating scale (6-factor scale):

| THE | B | C | D | E | F |
|---|---|---|---|---|---|

low

Portfolio ESG risk

high

| | Risk | Effect |
|---|---|---|
| Climate and Energy (E) | The specific manifestations of the climate crisis and/or the potential impact of any related and relevant legislation on the company's financial performance. | The company's impact on greenhouse gas emissions and energy consumption. |
| Responsible consumption and waste management (E) | The potential impact of changing consumer behavior (in terms of consumption and waste management patterns) and/or any related and relevant legislation on the company's financial performance. | The company's impact on consumption and waste management patterns as it is relevant to the health of the local and global environment. |
| Biodiversity and Toxicity (E) | Loss of biodiversity and increase in environmental toxicity and/or potential impact of any related and relevant regulatory acts on the company's financial performance. | The company's impact on biodiversity and environmental toxicity as it is relevant to the health of the local and global environment. |
| Poverty, Food (S) | The potential impact of social unrest and/or any related and relevant regulatory or political acts on the company's financial performance. | The company's impact on social equality in general and the level of socio-economic well-being in the relevant markets in particular. |
| Health and Wellbeing (S) | The potential impact of society-wide health and welfare issues and/or any related and relevant regulatory acts on the company's financial performance. | The impact of the company on the health and physical and psychological well-being of the members of society in the geographical areas affected by the company. |
| Culture and Learning (S) | The potential impact of changes in cultural, educational standards and/or any related and applicable legislation on the company's financial performance. | The impact of the company on the cultural and educational level and the access of the members of the society to cultural and educational goods. |
| Equity and Equal Opportunities (S) | The potential impact of equal opportunity employment issues and/or any related and relevant legislation on the company's financial performance. | How exemplary is the company in its markets in fairness to all stakeholders and providing equal opportunities to all stakeholders, especially the company's employees and suppliers? Does the company actively promote/help fairness and equal opportunities with its products and services? |
| Business ethics and corruption (G) | The potential impact of specific manifestations of unethical behavior and corruption and/or any related and relevant regulatory acts on the company's financial performance (even if through reputational risk). | To what extent is the company a role model in its markets in terms of ethical behavior towards all of the company's stakeholders, especially the company's employees, customers and suppliers? Does the company actively support business conduct and anti-corruption with its products and services? |

| | | |
|---|---|---|
| Data Protection and Data Rights (G) | The potential impact of any stakeholder's data protection rights and/or any related and relevant regulatory act on the company's financial performance (even if through reputational risk). | How exemplary is the company in its markets in protecting privacy and data rights for all the company's stakeholders, especially the company's employees, customers and suppliers? Does the company actively promote/help protect privacy through its products and services? |
| Transparency and Control (G) | The potential impact of non-transparency or manifest dishonesty and/or any related and relevant regulatory act on the company's financial performance. | How exemplary is the company in its markets in being transparent and honest with all of the company's stakeholders, above all with the company's employees, customers, suppliers, investors, and the public? Does the company actively promote/support transparency and integrity in business in general through its products and services? |