novobanco

POLICY FOR INTEGRATING SUSTAINABILITY RISKS IN INVESTMENT MANAGEMENT PROCESSES

novobanco Group

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The publication of the 'Policy for integrating sustainability risks into investment management processes' is carried out in full compliance with the disclosure requirements established in Regulation (EU) 2019/2088, with consolidated application to all companies included in the novobanco, S.A. perimeter.

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1. Introduction

Under the terms of Regulation (EU) 2019/2088 on the disclosure of sustainable finance information (SFDR), the entities that are part of the novobanco, S.A. Group. ('novobanco Group') are obliged to publish information on investment strategies and risk management policies, product classification and adverse impacts of their investment activities on sustainability.

These disclosures, in fulfilment of the applicable legal requirements, are also part of novobanco's effort to strengthen the transparency of its sustainability practices, to which the various objectives and commitments that the novobanco Group has undertaken in recent years contribute.

Accordingly, this document has the following objectives:

- To provide information on the specific approach of novobanco to integrating sustainability risks into its investment processes, and enhancing its transparency;
- To certify the compliance of the novobanco Group with the obligations established in the SFDR and other complementary regulations.

This policy has a consolidated application, and includes the following entities within its scope:

- **novobanco S.A.**, which qualifies as a 'financial adviser' under the terms of the SFDR, on account of its investment advisory services;
- **Banco BEST S.A.**, which qualifies as a 'financial adviser' under the terms of the SFDR, on account of its discretionary portfolio management and investment advisory services;
- **GNB Gestão de Ativos S.A**., which qualifies as a 'financial market participant', as a management company of Collective Investment Undertakings (CIUs), and as a 'financial and investment advisor' on behalf of the portfolio management services provided by *GNB Gestão de Patrimónios*.

The provisions defined here sometimes have a subsidiary or complementary nature to the other policies and regulations established by the entities identified above in terms of sustainability, namely the novobanco Group's Sustainability Policy (available here), as well as the other policies, commitments and regulatory framework of the Group or each entity, defined in line with novobanco's principles, as published on their respective websites.

1.1 Background

The novobanco Group is aware of the important role of the financial sector in meeting the objectives set by the European Union to fight climate change, including the adoption of a more sustainable economic model. To this end, it has set itself the goal of becoming a reference organisation in sustainability and sustainable finance. Through specific provisions and guidelines - both in terms of financing and investment activities - it therefore seeks to promote the Portuguese economy's transition to a more sustainable economic model by proactively managing the reduction of the risks inherent to this transition, i.e. the risks associated with the effort required to adopt more sustainable economic standards or, conversely, associated with the impacts that delays or inability to adopt these standards may generate.

In this way, the novobanco Group - in strict compliance with the applicable regulatory obligations - establishes, through this Policy, processes dedicated to identifying and processing sustainability risks, in terms of:

- Investment advisory activities:
- Portfolio management activities;
- CIU management activities.

In addition to the attention paid to managing sustainability risks, novobanco has endeavoured, as an important economic agent, to help make a positive impact on the communities in which it operates, following the best practices recommended in this context.

The following commitments by novobanco have a positive influence on financing and investment strategies and decisions, and are worth highlighting:

- Establishment of the Social Dividend Model which, through the definition of sustainability goals and short, medium and long-term Environmental, Social and Governance (ESG) objectives, reflects the Group's priorities and initiatives in promoting the Sustainable Development Goals (SDGs);
- Participation in the United Nations Global Compact (UNGC);
- Participation in BCSD Portugal;
- Participation in the Organisations for Equality Forum (iGen);
- Participation in the Target Gender Equality programme (TGE Portugal);
- Participation in the Inclusive Community Forum (ICF) initiative at NOVA University Lisbon (Nova SBE);
- Signing of the Letter of Commitment to Sustainable Finance in Portugal;
- Signing of the Business Ambition for 1.5 ºC commitment.

1.2 Policy objectives

The purpose of this Policy is to establish the internal definition of sustainability risks, to clarify the different types and how they may materialise, and to set out the principles, responsibilities and procedures for assessing, monitoring and controlling these risks.

When managing sustainability risks, there are two important dimensions to take into account:

- The risks to the assets and products advised and managed by the Group – these are the main focus of this Policy and the risk controls it determines;
- The risks to the Group itself, which are not dealt with directly in this Policy, but rather in the Group's specific risk management policies (e.g. reputational risk management or compliance policy).

2. Risk management strategy and principles

2.1 Strategic principles

The ESG strategy as a complement to the mission and values of the novobanco Group

The novobanco Group recognises that the weighting of sustainable investment criteria is in line with its values and mission, particularly the responsible investment aspect of its sustainability policy.

Adaptability of guidelines

It is recognised that the regulatory framework in these matters is not yet complete, which causes some fragmentation and asymmetry in the information available from issuing companies and investees, both within the European Union (where various regulatory reforms are still underway in the ESG field) and outside the European Union (where there are no mandatory measures comparable to those in force at European level).

Therefore, through its internal control structures, novobanco will constantly update the guidelines governing its investment and risk management strategies.

Cross-cutting nature of sustainability risks

The novobanco Group recognises that sustainability risks do not have a self-contained financial impact. In other words, there will always be additional impacts on the other financial and non-financial risk categories.

From this perspective, sustainability factors and risks are identified, assessed, quantified and managed through the processes, controls and methodologies relating to other risks - it follows that this policy does not establish any methodologies for quantifying sustainability risks which, independently, lead to the materialisation of impacts that may already be considered/assessed in other risk categories.

Traditional organisation

In view of the above principle, the Group considers that the establishment of organisational and procedural structures, parallel to existing ones and with the aim of managing and controlling ESG risks, is not justified by the applicable regulations or by the nature of the risks and their impacts.

To this end, this policy controls that the procedures for managing and monitoring sustainability risks should be integrated into the organisation and routines already established for managing the novobanco Group's investments and other risks, without it being considered necessary to create new structures or systems to control them. Without prejudice, this Policy also sets out the additional procedures and controls to be put in place so that the nature, dynamics and impacts of sustainability risks can be properly managed by any entity that is part of the novobanco Group.

Integrating ESG risks into investment and advisory decisions

The novobanco Group adopts common procedures to integrate ESG risks into investment or advisory decisions - these procedures take the form, for example, of exclusion policies or sectoral criteria, as well as the integration of sustainability factors into the selection of UCITS (Undertakings for Collective Investment in Transferable Securities).

Nevertheless, novobanco recognises that the level of integration depends on the ambition of each Group Entity and the investment strategy of each product/mandate. With regard to investment activities, in practice, products or strategies that, by design, have investment objectives related to sustainability issues assume a higher level of integration of these risks in their investment policies and decisions (i.e. these products must apply methodologies that, in their investment universe, limit exposure to assets or issuers with the presence of factors that could affect the performance and return of the products).

Risk assessment for the investor or client

The main concern of this policy is the management of ESG risks for novobanco Group's investors and clients: in other words, the risks implicit in the assets under management or advice which, in materialising, may affect their valuation or remuneration. In this sense, the control approaches set out here only cover the assets managed and advised, and conclusions cannot be extrapolated as to the performance of the assets on novobanco's balance sheet (i.e. assets managed on behalf of its own portfolio).

In addition, it is also stipulated that any indirect impacts of ESG risks whose transmission primarily results from an impact on the novobanco Group (e.g. greenwashing) are not analysed or dealt with by this policy, since they are already managed and controlled by the action of the other risk management and internal control policies.

Risk assessment for the novobanco Group

This policy assumes that the risks for the novobanco Group caused by sustainability issues are mainly dealt with by the other internal control policies and therefore does not specify additional controls. Strictly speaking, the existence of this policy *per se* is a control aimed at ensuring adequate control of the transmission of ESG issues to the Group's other risk categories and processes.

Without prejudice to the above, it is recognised that the legal and reputational risks associated with greenwashing or greenhushing may represent a new category of factors not yet managed in the approaches to other risks.

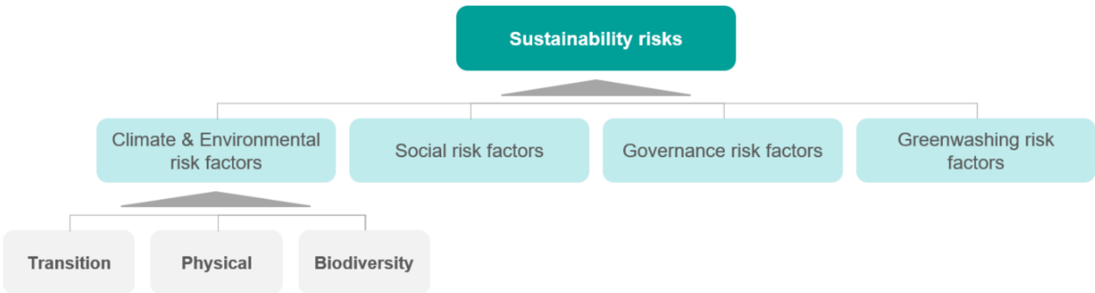
Therefore, this policy establishes additional procedures and controls for managing these factors. These mainly include the proper design and implementation of the methodologies (and respective documentation) that support the identification, selection, organising and/or disclosure of the novobanco Group's investment products, within the scope of its investment activity.

2.2 The taxonomy of sustainability risks and their materialisation

The definition of sustainability risks adopted by this policy follows the guidelines that have been shared by the different regulatory authorities. Therefore, the following definitions are adopted:

- **Sustainability risks** (or, more generally, ESG risks): this is an aggregate concept that summarises the impacts of three risk components, namely climate & environmental risks, social risks and governance risks.

  It is estimated that these impacts will be conveyed through the traditional categories of financial and non-financial risk, namely market, credit, liquidity, counterparty and operational risk.



- **Climate & environmental risks (C&E):** related to the quality and functioning of the environment and natural systems, including elements relating to climate change, biodiversity (or natural capital), pollution and waste management, to the extent that these elements can affect the performance or financial value of financial assets.

- **Social risks:** risks relating to social rights, well-being and the general interest of society and communities, including factors such as equality, health, inclusion, labour relations, hygiene and safety at work, human capital and the development of communities.
- **Governance risks:** these are risks relating to internal governance aspects, including management and supervisory bodies, internal organisation, remuneration policies, internal control, tax practices, conduct and transparency.
- **Risks of greenwashing:** these are the risks associated with communication with the market, clients or other partners and stakeholders of novobanco - whether relating to the products and services offered or the group's strategy and approach to sustainability - which is not in line with or appropriate to its impact on the economy and the market and which, for this reason, creates expectations in these parties which, in practice, do not materialise.

Without prejudice to other types of risk, the novobanco Group recognises the special relevance of C&E risks. For a better understanding of these risks, the C&E category is divided into complementary sets of factors according to:

- **Transition risk factors:** these are the factors associated with the challenges, and their impact, arising from the transition to an economy with low levels of GHG emissions, including the effort associated with changing the energy mix (i.e. switching to renewable sources) and adopting more circular business models.
- **Physical risk factors:** factors arising from the physical manifestation of climate change and environmental degradation, analysed in two categories: a) acute - which occur from climatic and meteorological events with a one-off negative impact; or b) chronic - which are determined by gradual changes in climatic and meteorological conditions, causing progressive degradation of ecosystems.
- **Biodiversity factors (or factors related to natural capital):** factors related to the quality and normal functioning of natural systems, including climatic factors, loss of biodiversity (impact logic) or consumption of physical and energy resources (dependency logic).

The dual materiality of ESG risks

The novobanco Group adopts the regulatory and supervisory perspective on the dual-materiality of ESG risks and, in particular, C&E risks: that is, it recognises that these risks may affect its investments through the impact of their factors on issuers or, directly, on assets ('outside-in perspective' or financial materiality), but these risks themselves may also be aggravated or amplified by the novobanco Group's activity and its investment or advisory decisions ('inside-out perspective' or environmental materiality). This dual-materiality analysis is carried out on a regular basis as part of the fulfilment of the Group's non-financial reporting obligations.

3. Risk management governance framework

The Executive Board of Directors (EBD) is the body that assumes overall responsibility for the novobanco risk management system. It sets out the principles that support it and supervises their application.

Regarding ESG risks, the EBD is directly supported by the ESG Office and the Risk Management Functions (DRG), which support the monitoring and discussion of these aspects.

From an operational point of view, the principle of the three lines of defence is observed, through the functional separation between investment and advisory responsibilities (i.e. taking ESG risks) and responsibilities for monitoring and controlling these risks.

3.1 Management and supervisory bodies

With regard to ESG risk management, novobanco's management and supervisory bodies have the following main responsibilities:

Body	ESG risk management responsibilities
Executive Board of Directors	▪ Approve the current policy and amendments to it; ▪ Approve the ESG risk management strategies and their integration into the investment policies; ▪ Define business and operational objectives to ensure compliance with ESG risk management principles and their integration into investment policies; ▪ Approve the exclusion and sectoral policies that may be proposed; ▪ Approve the methodologies for assessing and monitoring ESG risks; ▪ Monitor the main ESG risk monitoring metrics; ▪ Ensure that there are resources and capacities to implement the organisational responsibilities required to manage ESG risks using the three lines of defence.
Risk Committee of the General and Supervisory Board	▪ Advise the GSB and the EBD on the most effective strategies and actions for managing sustainability risks; ▪ Assess and give an opinion on proposals relating to the management of sustainability risks, and advise the GSB and the EBD on them; ▪ Promote and monitor the application of risk policies, including this policy; ▪ Propose changes to policies that are consistent with the Group's risk management strategies; ▪ Monitor the main sustainability risk metrics.
Forums to support the EBD in ESG matters (ESG Steering)	▪ Propose policies and approaches for managing and controlling sustainability risks; ▪ Analyse and discuss relevant aspects of sustainability risk management, and prepare proposals for consideration and approval by the EBD; ▪ Monitor the Group's exposure to sustainability risks and the assets it manages on a global basis.

3.2 Responsibilities of the first line of defence

The first line of defence in each of the entities responsible for investment activities or advisory activities is responsible for managing and monitoring them - this is where ESG risks can be found. It is also responsible for implementing the limits, procedures and controls laid down in this policy, in other regulations and in guidelines/determinations laid down by the EBD.

This includes departments/units with commercial and other functions relating to the publication, design and preparation of products or services. Overall, these units are responsible for adopting the strategies, initiatives and controls established by the EBD for ESG risk management.

As far as ESG risk management is concerned, and without prejudice to any others that may be defined, its main responsibilities include:

- Interacting and liaising with clients, counterparties, management companies and issuers, to encourage the exchange of information and data necessary to understand the ESG risks inherent in novobanco's investments, products and services;
- Applying the risk controls necessary to prevent or mitigate the ESG risks to which the assets produced or distributed by the Group are exposed, using the information and guidelines prepared by other units, specifically the ESG Office;
- Keeping abreast of market demand and the supply of ESG products and services from competitors, and promoting the potential of novobanco to develop and launch new products or solutions suitable for managing ESG risks;
- Ensuring that an up-to-date and detailed knowledge of ESG-related policies and strategies is maintained;
- Identifying and assessing any risk-increasing conditions in terms of counterparties, management companies, issuers or assets, with relevance to ESG risk management.

ESG Office

The sustainability function at novobanco is carried out by the GESG (ESG Office), which observes a matrix of responsibilities divided between the 1st line (for its business support responsibilities) and the 2nd line of defence (for its responsibilities in promoting effective management and control of ESG risks and the associated compliance requirements).

Therefore, as regards ESG risk management, the GESG's main responsibilities are:

- Promoting communication and commercial orientation with regard to the adoption of the novobanco Group's sustainability strategy and ESG risk management;
- Coordinating the preparation and promotion of the ESG sustainability and risk management strategy;
- Monitoring and promoting compliance with this Policy, and helping to draw up specific procedures for implementing this Policy;
- Coordinating the preparation of exclusion and sectoral policies;
- Providing second opinions on investments with a significant ESG risk profile;
- Monitoring and advising on new products and services associated with the ESG;
- Encouraging coordination and interaction between all the relevant units of the novobanco Group, to ensure effective ESG risk management;
- In partnership with the other relevant areas, participating in the design and implementation of the main methodologies linked to ESG risks, including those relating to the classification and disclosure of products and services associated with ESG;
- Monitoring the ESG implications of the novobanco Group's activity;
- Collecting and transmitting ESG-related information;
- Disseminating good practices and fostering an internal culture aligned with ESG criteria;
- Preparing, in partnership with the other relevant areas, external information on ESG risk management along with other disclosures required by law or regulation.

3.3 Internal control functions

The second line of defence is made up of Risk Management (DRG) and Compliance (DCOMPL - Compliance Department), which work to define the policies, controls and methodologies needed to manage and control ESG risks. Finally, the third line of defence is the Internal Audit (DAI), which is responsible for confirming that this policy has been effectively applied.

Without prejudice to the duties laid down in the respective regulations, where applicable the following responsibilities of the internal control functions are established:

Body	ESG risk management responsibilities
Global Risk Department (DRG)	▪ Propose the strategy and appetite for ESG risks, and ensured that they are regularly monitored ▪ Confirm that the sustainability objectives are consistent with novobanco's ESG risk appetite ▪ Develop, maintain and apply ESG risk assessment methodologies; ▪ Ensure that ESG risks are independently monitored ▪ Support the provision of external information on ESG risks
Compliance Department (DCOMPL)	▪ Promote compliance with the legal and regulatory obligations on sustainability, in terms of products, disclosures and internal activities; ▪ Evaluate the compliance of novobanco's policies, procedures and products with the applicable requirements; ▪ Provide advice on the interpretation and implementation of the main legal and regulatory requirements.

4. Risk management model

The novobanco Group's sustainability risk management model is organised according to the services it offers, i.e. a) according to the Investment Consulting service offered by novobanco and Banco Best; and b) according to the Portfolio Management service offered by GNB GA and Banco Best.

The procedures and controls established within the framework of the products and services produced by GNB GA are described in this organisation's individual policy.

4.1 Due diligence in the selection of Financial Instruments

Novobanco and Banco BEST have their own procedure for analysing the financial instruments they recommend. In line with the set of assets defined in the General Conditions of the Investment Advisory Service, this procedure applies, at novobanco, to UCITS registered in Portugal and, at Banco Best, to UCITS and Exchanged Traded Funds (ETFs), and is based on a proprietary selection model that integrates quantitative and qualitative sustainability factors.

Without prejudice to the other dimensions analysed, this procedure covers at least:

- In its quantitative analysis component, the model includes five categories which may integrate more than one indicator each, and assesses the relative and absolute performance, risk, and activity and longevity of the management of each investment fund from a financial perspective. Since 2023, a new category has been introduced that includes the ESG assessment measured by the Morningstar Sustainability Rating (MSR) variable, which contributes with a 10% weight to the final assessment (score).

  The Morningstar Sustainability Rating (MSR) is based on *Sustainalytics*' ESG ratings for companies (how much a company's value is affected by ESG factors) and governments (the risk associated with a country's socio-economic condition and whether it manages its resources sustainably). The greater the ESG risks, the greater the negative impact on the sustainability rating. By analysing 12 months' historical data and comparing it with the values of its peers (industry or geographical), the fund's rating can be obtained – only funds with more than 67% of assets with an ESG rating are eligible, within their Morningstar category.

- Regarding its qualitative analysis component, the model provides for an analysis:
  - of compatibility between the Fund's sectoral and exclusion policies and those adopted by novobanco (details below);
  - of additional validations in cases where the Investment Funds with the best results in the model have particularly low MSR levels, between 2 and 0.

4.2 Sectoral and exclusion policy

The sectoral and exclusion policies apply to the various entities of the novobanco Group. Without prejudice, the possibility is recognised of a) adapting some of its criteria so that they can be applied more effectively to the activities carried out; and b) monitoring, periodically and on a best-effort basis, the criteria that have been adapted.

Notwithstanding the above, at least the following sector exclusions will be observed:

- trading in war material or weapons not associated with national defence activities, as well as non-conventional weapons;
- casinos or gambling, as well as piracy, prostitution or pornography-based business models;
- Coal mining or energy production based on coal;
- Any activity for which it is possible to reasonably identify indications of risks of money laundering or terrorist financing.

At novobanco and Banco BEST, for a more effective application to the activities carried out, within the scope of asset selection (Funds and ETFs), and in relation to the pre-selected funds, the applicable exclusions are analysed, based on the information disclosed by each fund in its EET (European ESG Template), with a maximum tolerance limit of 10% of potential exposure to excluded activities.

If the information available for the asset is not sufficient to draw reliable conclusions about the alignment, there will be an extraordinary process of validating the alignment at management company level.

4.3 Monitoring and follow-up

On an annual basis, the first line functions - subject to review by the second - must prepare a global analysis of all the financial instruments they advise on, with a view to informing their management of any concentrations (or other anomalies) in positions with some kind of limitation on sustainability.

Without prejudice to other additional information, this analysis should include:

- A review of volumes, from the perspective of flows invested and in stock;
- A re-evaluation of the products recommended under the Asset Selection Model, including analysis of the ESG dimensions present in the model.
- A study of the performance of the main indicators of adverse impact on sustainability (PAIS), available at https://www.novobanco.pt/sustentabilidade/negocio-sustentavel/sustentabilidade-e-investimento.

5. Impact on investment policies

All the investment policies that guide the investment and advisory activities of the novobanco Group recognise the provisions of this policy, in the sense that:

- As far as advisory activities are concerned, common mechanisms are established at pre-investment level (e.g. exclusion policies within the scope of the UCITS selection model) and post-investment level (e.g. monitoring) regardless of the ambition or ESG classification of the products;
- As far as investment activities are concerned, specific control/design procedures apply to products whose investment strategy incorporates ESG objectives.

6. Impact on remuneration and incentive policies

The novobanco Group complies with the applicable regulations in this context, and includes considerations relating to sustainability risks into its remuneration and incentive policies.

To this end, it establishes the adoption of and compliance with remuneration practices that are consistent with prudent, sound and effective risk management, that do not encourage excessive risk-taking within the novobanco Group or risk-taking that is inconsistent with the risk profile of the products advised or managed, that encourages situations that generate conflicts of interest with clients or that disregards the importance of sustainable behaviour in terms of investment and management.

The Remuneration Policy includes remuneration structures that optimise financial results and promote sustainable behaviour without generating or exacerbating systemic risks that could undermine long-term investment interests.

By applying mechanisms that allow changes to the remuneration structure, the novobanco Group ensures that appropriate incentives are implemented to take precautions and mitigate risks.

Bearing in mind the importance of striking a balance between metrics aimed at reducing exposure to risk and those that promote sustainable growth, the novobanco Group includes factors in its Remuneration Policies that mitigate risk, as well as objectives aimed at encouraging business development.

7. Revision

This Policy is regularly reviewed in the light of the experience gained from its application and any legislative changes.