

Environmental and Social Management System (ESMS)

Version 3

The Fund's Environmental and Social Management System ("ESMS") sets a systematic procedure for the Fund in assessing E&S Risk and anticipating E&S Impact.

CONFIDENTIAL

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1 Summary

Below summarises the Fund's Integrated E&S Management System (ESMS) across the investment lifecycle.

Stage	E&S Risk Management	E&S Impact Assessment
Pre-investment	<i>Approach and tools</i>	<i>Approach and tools</i>
Screening Memo	Compare activities against the Microfinance Exclusion List	Summary of how investment meets criteria and aims of Fund
Due Diligence	<p>Review of client SE Management System and complete E&S risk assessment form</p> <p>Assessment of portfolio risk for FIs: (i) request data on lending by product/sub-sector; and (ii) conduct survey on sample of existing loans</p> <p>Categorise financial institutions (FI-1/2/3) and projects (Category A/B/C)</p> <p>Consult with financial sector regulatory authorities</p> <p>Review ESIA or equivalent for non-financial services companies</p>	<p>Request projection of portfolio by lending product and assess prospective E&S impact</p> <p>Benchmark proposed issuance terms against market norms clarify domestic participation</p>
IC Proposal	<p>Complete evaluation template for IFC Performance Standards and complete E&S Diligence Report</p> <p>Reconcile ESIA with IFC Performance Standards</p>	<p>Detailed explanation of how the investment (including terms, use of proceeds) meets the criteria and aims of the Fund</p> <p>Complete E&S Diligence Report</p>
Execution	Covenants and/ or a "Side Letter" outlining reporting commitments	Covenants and/ or a "Side Letter" outlining reporting commitments Report list of investors at issuance
Post-investment	<i>Approach and tools</i>	<i>Approach and tools</i>
Monitoring/ Reporting	<p>Complete E&S risk template and compliance with IFC Standards</p> <p>Report on E&S risk in annual E&S Performance Report, categorising financial institutions (FI-1/2/3) and projects (Category A/B/C)</p>	<p>Complete E&S impact template</p> <p>Annual E&S Performance Report (for publication)</p>
Remedies	<p>Remedial or corrective measures through technical assistance, e.g. improvements to their ESMS</p> <p>Require put option on the issuer in the event of non-compliance</p> <p>Sell-down bond and unwind swap where E&S risk is unacceptable</p>	<p>Remedial or corrective measures through technical assistance, e.g. improvements to their ESMS</p> <p>Exercise put option on the issuer in the event of non-compliance</p> <p>Support market development through future issuance</p>

2 E&S Risk Assessment

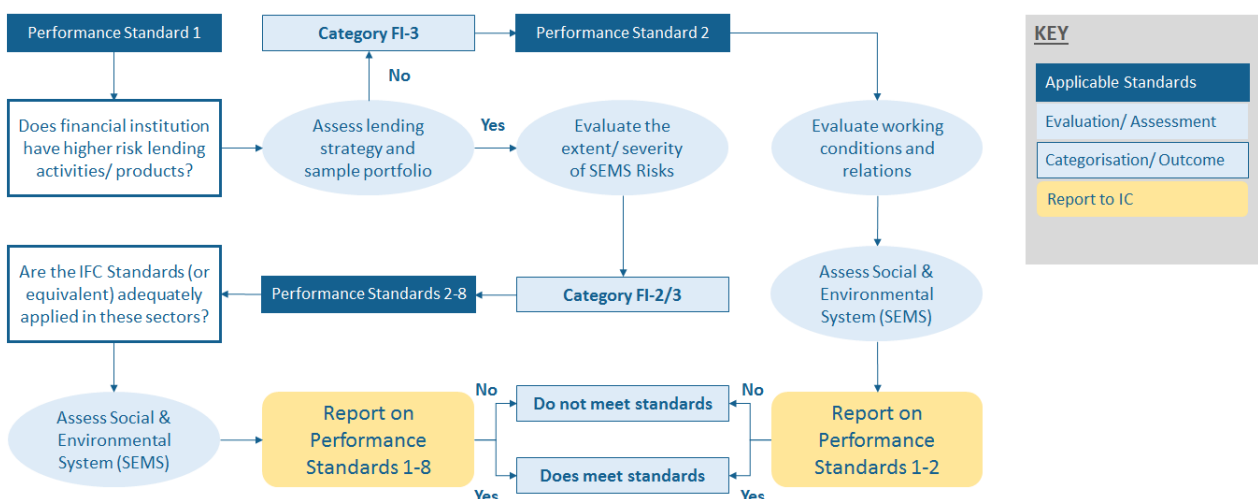
2.1 Classification

As stated in its E&S Policy, the Fund is overall expected to maintain a low level of E&S risk, since it will have exposure to financial institutions that provide microfinance or financial institutions that provide SME, commercial and corporate (wholesale) financing to non-sensitive industries.

Nonetheless, the Fund shall apply the IFC Performance Standards in relation to evaluating E&S risk in prospective investments. The matrix below summarises the expected E&S risk in the Fund’s target sectors and among target issuers. The key in the right panel applies the applicable IFC Performance Standards.

Issuer Type	Financial Institutions	Structured Finance Vehicles	Companies	Risk Category	IFC Performance Standard
Sector/ Activity					
Financial Inclusion	[Green]			Little or no SE Risk	1-2
Housing					
Renewables	[Orange]			Asset finance with waste management needs	1-3
Agriculture					
				Unacceptable SE risk	NA

Based on the guidance notes for the IFC Performance Standards in relation to financial institutions, the following analytical framework shall be applied when assessing E&S risk among FIs. Primarily, Performance Standard 1 requires assessment of the level of SE risk in the portfolio (through disclosure or lending strategy and portfolio composition) followed by an assessment of the quality/ adequacy of the issuer’s E&S Management System (ESMS).



2.2 Assessment

The primary aim of assessing the issuer’s lending activities is to determine E&S risk, and specifically the extent of lending to higher risk sectors (as set out in the Fund’s E&S Policy). In

addition, Performance Standard 2 in relation to labour practices shall be applied for all FIs. Finally, for asset financing companies or structured finance vehicles, the Fund shall apply Performance Standard 3 in relation to waste management practices and policies.

Due diligence in relation to E&S risk shall be implemented by the Fund Manager during ex ante due diligence and as part of subsequent portfolio monitoring. In relation to the former, this information on SE risk shall be collected through: (i) requests for information in the upfront due diligence request; (ii) a sample survey of the issuer's loan book (assessing use of proceeds, lending practices and rates, maturity, etc.); and (iii) completion of an evaluation template for SE risk. On-site visits are a requirement for all investments regardless of categorisation.

The Fund Manager shall, during the due diligence and prior to investing, offer all Issuers the opportunity to obtain an „Indicative Credit Rating“ (sometimes known as a shadow credit assessment which remains private and unpublished), supported by the TAF. The Issuer has the option to subsequently publish or renew the rating.

Error! Reference source not found. provides a template assessment form for E&S risk. In addition, for financial or non-financial institutions, a full assessment of E&S risk in relation to the full list of IFC Performance Standards, reconciled with other relevant standards such as the Equator Principles, ILO Core Labour Standards, and local laws and regulations, must be provided. Specifically, this will classify the use-of-proceeds and Category A, B or C to summarise E&S risk.

Each Proposal presented to the Investment Committee shall contain a qualitative “SE Diligence Report”. The key features are set out below, using the logical framework of (i) Evaluation Instrument, (ii) Diligence Undertaken, (iii) Risk/Impact Assessment and (iv) Action Points (including any covenants or remedial TA).

For financial services companies, the below assessment shall apply. In all instances, the review will determine whether the issuer complies with the relevant IFC Performance Standards.

Diligence Undertaken	Findings	Action
Portfolio Review		
Policy Review		
ESMS Review		
Site Visit		
Risk Assessment Form		

For other types of issuer, the Fund Manager shall report on the below. The Fund may seek external verification and validation of an ESIA to ensure compliance.

Evaluation Instrument	Diligence	Assessment	Action
Relevant IFC Performance Standards			

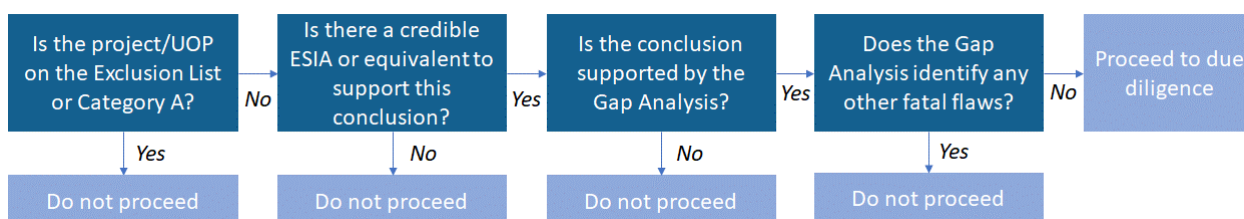
ESIA or equivalent (where applicable, e.g. for corporate/ infrastructure bonds)	
Applicable SE laws in the relevant country (labour, occupational health and safety, environmental standards, land, etc.)	

2.3 Category A Projects

The Investment Policy specifies eligibility criteria for non-finance companies including infrastructure related companies (i.e. those who build, own and operate capital intensive assets including in the infrastructure sector). Such companies must demonstrate all required environmental consents according to national law, including an approved Environmental and Social Impact Assessment (ESIA), meeting International Finance Corporation (IFC) performance standards, the Equator Principles (which refer to the IFC standards). If applicable, the project should also be assessed in alignment with the World Bank Group’s EHS Guidelines (which are referenced in the IFC performance standards).

The Fund does not invest in bonds where the use of proceeds (“UOP”) is for “Category A Activities”, as defined in Appendix C in the E&S Policy. Depending on project specifics, the E&S risks of individual projects included in these activities may considered to be medium. In such cases detailed rationales for categorization must be documented.

During due diligence, the Fund Manager will undertake a Gap Analysis of the documentation (ESIA or equivalent document) supporting the categorization of the project/UOP as “medium” risk or lower. This Gap Analysis shall usually require a verification report from a qualified third-party. In some instances, the third-party may be required to engage the Issuer (and their advisers) further, and/or be required to undertake a site-visit.



2.4 Action Plan

Where the issuer’s ESMS is found to be inadequate relative to the activities it undertakes (usually for an FI-1/2 or a Corporate), the Fund shall require in the Side Letter that the issuer takes remedial measures as a condition of investment. This might include the adoption of additional policies and procedures, or the addition of new criteria in an existing policy.

Where the issuer’s ESMS is inadequate relative to its risk profile, a more comprehensive reinforcement might be required. For example, for a housing finance company, this might include

expanding the scope of an existing ESMS in order to mitigate the greater E&S risk associated with investing in housing development (e.g. safety of construction sites, land tenure, etc.).

In certain instances, where a lack of E&S capacity is identified upfront, the Fund may negotiate a put option that allows it sell back the bonds unless standards are subsequently met.

3 E&S Impact Assessment

The Fund is committed to having a positive E&S impact, as set out in the E&S Policy. This covers the development of local African capital markets; improved resilience and financial strength for issuers; and investment in high development sectors that benefit low income households and MSMEs. In its deal origination, screening and due diligence, the Fund Manager will identify and progress transactions that are likely to contribute to positive E&S impact. The details proposal submitted by the Fund Manager to the Investment Committee will explain the E&S impact in detail.

To reflect the Fund's mandate to promote a credit culture in target markets, the Fund will also publicise the public ratings of portfolio companies and promote ratings among potential Issuers.

In order to prepare an annual Environmental & Social Performance Report ("ESPR"), the Fund Manager will collect qualitative and quantitative information for each active investment. The ESPR will consolidate and present these reports across the portfolio for general publication. The Fund Manager will also monitor the issuer's use of proceeds and any other commitments made by the issuer at the time of investment, such as adherence to the SMART Campaign.

The information collection template is presented below:

COMPANY DETAILS					
Name of Financial Institution					
Date of Assessment					
Share management accounts for financial year-end					
LOAN PORTFOLIO					
	Number of Clients	Outstanding Loan Balance (as at Year End)		Past Due Loans Over 90 days (at Year End)	
		Number of Loans	Amount (USD)	Number of Loans	Amount (USD)
Retail Loans	0	0	0	0	0
Mortgage Loans	0	0	0	0	0
Newly Constructed Home					
Existing Home					
Home Equity Loan/Improvement					
Student Loans					
Retail Loans					
Micro-enterprise					
Education					
Health / Emergency					
Housing					
Consumption					
Other					
Commercial Loans	0	0	0	0	0
USD 0 - 1,000					
USD 1,001- 10,000					
USD 10,001-100,000					
USD 100,001-1,000,000					
USD 1,000,001-2,000,000					
USD >2,000,000					
Total Loan Portfolio	0	0	0	0	0
Are any related to Climate / Green Financing? If so, please provide					
Gender Disaggregated Loan Data					
Commercial Loans to Women-Owned Enterprises (out of total)	0	0	0	0	0
USD 0 - 1,000					
USD 1,001- 10,000					
USD 10,001-100,000					
USD 100,001-1,000,000					
USD 1,000,001-2,000,000					
USD >2,000,000					
Specify Your Definition of the Following					
Please explain what the women-owned enterprise data is based on? (if applicable)					
Please explain what the full-time employees data is based on? (if applicable)					

LIABILITIES							
Overview		Amount	Insert Comments (if any)				
Total Borrowings							
Borrowings in Foreign Currency							
Borrowings in Local Currency							
Average Maturity (Months)							
Total Fixed Rate Borrowings (Amount)							
Deposit Accounts		Number of Clients	Outstanding Balance (Year End)				
			Number of Accounts	Amount (USD)			
Total Deposits		0	0	0			
Individual							
Micro-enterprise							
Commercial (SMEs)							
Corporate							
Government							
Gender Disaggregated Deposits Data							
Deposit Accounts to Women-Owned Enterprises (out of total)		0	0	0			
Individual							
Micro-enterprise							
Commercial (SMEs)							
RATIOS							
Indicators		Amount	Insert Comments (if any)				
Non-Performing Loans (NPLs at PAR90)							
Capital Adequacy Ratio (CAR)							
Open Credit Exposure (OCE) [(NPL - Provisions) / Total Equity]							
Covenant (if any)			(Covenant type)				
Covenant (if any)			(Covenant type)				
Covenant (if any)			(Covenant type)				
Covenant (if any)			(Covenant type)				
DOMESTIC MEDIUM TERM NOTE DETAILS							
Issuance #	Issuance Date	Currency	Amount	Outstanding	Interest Rate	Listed or Unlisted?	Insert Comments (if any)
#1							
#2							
#3							
#4							
#5							
#6							
#7							
#8							

INVESTORS						
NUMBER (#) OF INVESTORS BY INVESTOR TYPE						
Issuance #	Pension Funds	Asset Managers	Insurance Companies	Other Banks/ FIs	Other	Insert Comments (if any)
#1						
#2						
#3						
#4						
#5						
#6						
#7						
#8						
AMOUNT INVESTED BY INVESTOR TYPE						
Issuance #	Pension Funds	Asset Managers	Insurance Companies	Other Banks/ FIs	Other	Insert Comments (if any)
#1						
#2						
#3						
#4						
#5						
#6						
#7						
#8						

PLEASE COMPLETE THE BELOW FOR ALL PRODUCTS THAT COMPOSE MORE THAN 5% OF THE COMPANY'S PORTFOLIO

STEP 1:

Choose the loan amount and tenors that fit the description of the product

LOAN NAME:	
PRODUCT DESCRIPTION	
PERCENTAGE OF TOTAL PORTFOLIO	

Average Loan Amount	
Minimum Loan Amount	
Maximum Loan Amount	

Average Loan Tenor (mths)	
Minimum Loan Tenor (mths)	
Maximum Loan Tenor (mths)	

Payment Frequency (Weekly, mthly, yearly)	
Monthly Interest Rate	
Fees (% or Fixed Amount)	
Relevant % or Amount	
Fees (% or Fixed Amount)	

STEP 2:

In the matrix below, insert the total amount paid by the client over the life of the loan product (including principal, interest and fees) for each scenario.

INPUT: Instalments					
Loan Amount / Tenor	0	0	0	0	0
0					
0					
0					
0					
0					

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4 Monitoring and Reporting

The Fund's E&S performance will be comprehensively reviewed by the Fund Manager on an annual basis, through collection of up-to-date qualitative and quantitative information that is reported in the ESPR. Monitoring is predominantly desk-based; with information provided by the issuer. For specific investments that are deemed to be of greater E&S risk, or in the event a credible grievance has been observed, the Fund Manager may consider a more comprehensive monitoring process (e.g. appointment of E&S consultant to review action plan implementation or site visit).

E&S Performance Reports for external investors include: (i) Portfolio breakdown by sector, high-risk transactions and E&S due diligence process (e.g. E&S Risk categories); (ii) Cases of non-compliance and significant E&S incidents¹ related to a transaction; (iii) Information on the implementation of and changes to the FI's ESMS; and (iv) Information on E&S impact indicators as agreed with the client.

E&S risk will be summarised for each issuer based on the following:

- E&S Risk Category (FI-1/2/3 or Category A/ B/ C)
- E&S Issues Identified at Appraisal
- Update on E&S Action Plan
- Additional E&S Concerns to be Addressed
- Other requirements, such as reporting of milestones for construction projects and ongoing oversight by local environmental regulators

The SE Policy sets out the information to be recorded in the ESPR in order to measure SE impact.

5 Corrective Measures

As set out in the E&S Policy, the corrective measures available to the Fund are limited as a bond investor. However, the Fund Manager, will report E&S risk in the portfolio and specific events that lead to unacceptable E&S risks and outcomes at the investee level. Such measures include:

- (i) Ensuring that the issuer plans and implements actions to remove or mitigate additional E&S risk;
- (ii) Engagement with other investors in the note program in relation to E&S risk and possible remedial measures; and

¹ Defined as any significant social, labor, health and safety, security or environmental incident relating to an issuer or project for which the ALCB Fund has invested which could reasonably be expected to have a material adverse effect on the implementation or operation of the issuer or project in accordance with the ALCB Fund's E&S requirements and applicable standards.

- (iii) Ultimately, in the event that such measures are not implemented to the satisfaction of the Board, the Fund Manager will make best efforts to sell its position and unwind the swap.

6 External Communications and Complaints Resolution

The Fund Manager will ensure that members of the public have a channel to easily provide comments or express grievances. The Fund seeks to provide a clear framework that ensures grievances are appropriately addressed and are used to prevent similar complaints in the future. The methods of doing so are highlighted in the table below.

Consideration	Method
Provide public with the means to easily communicate grievances, including anonymous ones.	The ALCB Fund website provides an email address that members of the public may use to file complaints confidentially.
Implementation of a clear process that includes assignment of responsibility and monitoring of outcomes	The Fund Manager's E&S Officer will maintain a log book to monitor progress towards resolution of all complaints as shown in Appendix E. The E&S Officer is responsible for reviewing and recording any complaints received. He/she is also responsible for working with any relevant staff or stakeholders to investigate the complaints, determine the necessary response, and report on the outcome.
Ensure grievances are used as a source of continual learning	The E&S Officer will periodically compile all grievances in order to improve operations and proactively prevent future grievances.
Provide public with the means to understand the Fund's E&S requirements	Publication of summary of Fund E&S Policy and ESMS on website.
Informing stakeholders of material E&S incidents	Any material change in investee or portfolio E&S risk will be immediately reported back to the Fund and Investment Committee. The Investment Committee shall decide whether it is deemed appropriate to inform investors, or a broader group of stakeholders, of the developments.

7 Roles & Responsibilities

An overview of the roles and responsibilities for the implementation of the ESMS is summarised in the table below.

Task	Roles and Responsibilities
E&S Risk Assessment	The Investment Officer (IO) is responsible for the initial E&S classification and assessment of the issuer. The evaluation, gap analysis and proposed action plan are reviewed by the E&S Officer.

E&S Impact Assessment	Collection of E&S impact data for each issuer is the responsibility of the relevant IO. The Fund's middle-back office team is responsible for collating impact data and drafting the impact section of the ESPR. The ESPR is reviewed by the E&S Officer before submission to the Fund's board for approval.
Monitoring & Reporting	Monitoring of E&S risks and action plan implementation (if applicable) is the responsibility of the relevant IO, with support provided by the E&S Officer.
Corrective Measures	E&S Officer will oversee the implementation of any corrective measures
External Communication & Complaints Resolution	The E&S Officer is responsible for managing external communication and complaints.

8 E&S Officer

The Fund Manager's E&S Officer is James Doree.

9 ESMS Policy Updates

To ensure continuous improvement, the Fund will review the ESMS Policy at a minimum once every two years. The policy will be amended to ensure alignment with possible changes to international best practices, reference materials, investor requirements and Fund investment activities. Changes to the ESMS Policy is approved by the Fund's board of directors.

10 Policy Log

Version	Date Approved	Approval Process
2	11 April 2018	Board Minutes
1	11 September 2017	Board Minutes