ICG

ICG Responsible Investment Report 2017

NEW DIMENSIONS TO ICG'S RESPONSIBLE INVESTMENT PLATFORM

ICG's 2017 Responsible Investment ("RI") report covers the progress and implementation of ICG's Environmental, Social and Governance ("ESG") agenda since its previous report, issued in 2016.

The 2016 report saw the expansion of ICG's RI policy to cover increased assets under management ("AUM"), a new and improved internal online ESG training module and a more detailed and widely distributed ESG survey with our portfolio companies. Since then, ICG has worked diligently on further developing its RI platform.

On-boarding and promotion of ESG

ICG aims to embed RI into most investment strategies across the firm. ICG's RI policy already covered a significant portion of the firm's AUM across European Subordinated Debt and Equity, Asia-Pacific Subordinated Debt, European Senior Debt Partners ("SDP") and Global Credit Fund Management. These strategies represent over 75% of the firm's AUM, as of 30 September 2017.

The most significant step since our last RI report was the full on-boarding of ICG-Longbow, which represents a further EUR 3.5 billion, or 13% of AUM, as of 30 September 2017. David Mortimer, Head of Senior Direct Lending at ICG-Longbow, joined the RI Committee and leads the ESG focus of ICG's dedicated Real Estate business. ICG-Longbow has already completed the Global Real Estate Sustainability Benchmark ("GRESB") debt assessment filing in 2017, to demonstrate its ongoing commitment to ESG principles as it continues to enhance RI procedures. In addition to this, ICG-Longbow formed part of the recent United Nations Principles for Responsible Investment ("UNPRI") filing under its Fixed Income module, which is outlined further in the 'UNPRI filing' section.

In addition to ICG-Longbow, ICG has made further progress integrating both North American Private Debt and Strategic Equity, two North American businesses focused on debt financing and General Partner ("GP") restructuring, respectively. The North American Private Debt business has begun surveying portfolio companies, and as part of ICG's annual ESG survey and Strategic Equity is requesting GPs to complete ESG questionnaires at transaction closing. It is ICG's intention to further integrate these businesses and have investment members join the RI Committee. These two businesses represent approximately EUR 1.6 billion, or 6%, of ICG's AUM, as of 30 September 2017.

As a more formal and dedicated commitment, as well as an effort to improve the communication of ESG internally and externally to investors, ICG is now including ESG within the commercial sections of Private Placement Memorandums ("PPM"). SDP 3, ICG's largest fund to date, ICG-Longbow UK Real Estate Debt Fund V and ICG North American Private Debt Fund II outline ICG's commitment to RI within the Fund PPMs. The ICG Europe Fund VII PPM will also include this specific section.

Surveying Portfolio Companies

ICG's RI Policy now covers a wide variety of investment strategies, from syndicated lending to direct and indirect equity positions. ICG's influence with senior management will vary significantly depending on the type of investment made by the firm.

Where ICG has close relationships with portfolio companies it will work closely with management to increase awareness and the importance of ESG, with the aim to make it a business priority. ICG will also seek to monitor ESG performance and encourage portfolio companies to complete annual ESG surveys where we have relationships to achieve this.

After three years of ICG's ESG survey, 2017 saw the widest distribution of the survey to portfolio companies in European Subordinated Debt and Equity, Asia-Pacific Subordinated Debt, European SDP and North American Private Debt. Following a consultation with Dr. Rory Sullivan and our internal compliance teams, the report remained predominately the same as 2016, with one additional question on anti-bribery policies, taking the survey to 19 questions. The report was distributed to 55 companies, a 40% increase from 2016.

For 2017, this section of the report will concentrate on the responses from 28 portfolio companies in our European Subordinated Debt and Equity & Asia-Pacific Subordinated Debt businesses to allow us to identify any trends between the 2016 and 2017 surveys. Next year we hope to review trends in the Senior Debt Partners portfolio too, by comparing the results to this year's 11 respondents. For the European Subordinated Debt and Equity & Asia-Pacific Subordinated Debt businesses completion rates were at 100% and 86% this year, respectively, up from 90% and 83% in 2016.

Key findings from the annual ESG report across portfolio companies include:

- Approximately 70% of portfolio companies have either conducted an assessment of business risks and opportunities associated with environmental and/or social issues, or developed a sustainability policy. This is broadly in line with last year's results.
- Of those approximately 70%, 84% have assigned specific responsibilities for ensuring compliance with ESG policies, up from 73% in 2016. This figure demonstrates that the companies that are addressing ESG are properly allocating resources to the cause.
- The number of portfolio companies that have either established systems to manage their environmental impact, or monitor their carbon footprint has remained reasonably consistent at approximately 60%.
- In the last twelve months, around a quarter of portfolio companies have made changes to how they manage environmental and/or social issues to improve their focus. This is consistent with what we saw in the prior year.
- Results have shown the number of portfolio companies with independent board members has decreased slightly from 2016, although remains around a third. This drop is partly explained by turnover in the portfolio during the year. ICG can now use this information to work with certain portfolio companies in 2018 to look at elected independent board members.
- Portfolio companies being faced with litigation due to social and/or commercial activities remains extremely low.

There have been encouraging results across the Senior Debt Partners portfolio this year. In the 2017 survey, results have shown that over 90% have either conducted an assessment of business risks and opportunities associated with environmental and/or social issues, or developed a sustainability policy. ICG will be able to monitor trends across these portfolio companies next year.

Two case studies of ESG excellence, one with a new ICG portfolio company and one with an exited ICG portfolio company, are provided in Appendix A and B, respectively. A segment of the 2017 ESG survey provided in Appendix C.

UNPRI filing

As institutional investors, ICG has a duty of care to act in the best long-term interests of our beneficiaries. In this fiduciary role, ICG believes that ESG issues can affect the performance of investment portfolios (to varying degrees across companies, sectors, regions, asset classes and through time). ICG also recognises that applying these principles may better align investors with the broader objectives of society.

As part of our commitment to the UNPRI, ICG completed a fourth filing in March 2017 in the following areas:

- Organisational Overview
- Strategy and Governance
- Direct Fixed Income
- Direct Private Equity
- Closing module

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ICG's fourth UNPRI filing revealed encouraging results across the business, including ICG's highest score to date in its Strategy and Governance module representing ICG's overarching approach to RI and a strong set of scores confirmed for the other modules. Results from the FY2017 filing showed:

- Performance within the Strategy and Governance module was in line with our peers, scoring a Grade A;
- Performance in our Direct Private Equity module outperformed our peers, scoring a Grade A; and,
- Performance in our Direct Fixed Income module was in line with our peers, scoring a Grade B.

ICG's "A grade" in Direct Private Equity, above the median "B grade" score, is evidence of the successful implementation of ICG's RI agenda as European Subordinated Debt and Equity was the first strategy to implement ESG into its investment process.

ICG's merged public transparency report can be found at: https://www.unpri.org/organisation/intermediate-capital-group-plc-142493.

Implementing Training and Awareness

ICG initially launched its internal online training for RI in 2014 with Thomson Reuters, and this was subsequently re-designed in 2016. The 2016 training module had a 93% completion rate and was sent to 158 staff members across the Investment and Marketing and Client Relations teams. ICG feels this online training remains an important part of embedding RI into ICG's investment culture. Since its launch in 2016, an additional 40 people have completed the training.

The aims and objectives of the course are specifically to:

- Understand why Responsible Investment is important,
- Understand Responsible Investment and what it involves, and,
- Recognise what ICG has to do to invest responsibly.

In order to improve education internally the RI Committee members attend key ESG conferences around the world. Recent conferences include the UNPRI conference in September 2017 (Berlin), Asia Venture Capital Journal ESG Forum 2016 in September 2016 (Singapore) and the Willis Towers Watson: Practical implementation of ESG conference in January 2017 (London). Members of the RI Committee also spent time with third party companies to better understand what technology options exist that could be used to help with investment decisions in ICG's Credit Fund Management ("CFM") business. Although the majority of these external services focus on companies with public equity (which is only a subset of the CFM target market), this is an option which will continue to be explored.

Responsible Investment Committee

ICG's RI Committee comprises of senior investment professionals and members of the Marketing and Client Relations team. Following the addition of David Mortimer, at ICG-Longbow, the RI Committee has remained unchanged since our 2016 report, providing consistency in ICG's RI agenda and implementation. Members of the team are based globally, including Europe, North America and Asia-Pacific. The RI Committee is outlined below:

- **Rosine Vitman, Managing Director** – Head of Portfolio Monitoring for European Subordinated Debt and Equity, and Head of Responsible Investment
- **Michelle De Angelis, Managing Director** – Head of Credit Research, Credit Fund Management
- **Jin Tan, Managing Director** – Asia Pacific Mezzanine Investment
- **David Mortimer, Managing Director** – Head of Senior Debt, ICG-Longbow Real Estate
- **Helen Gustard, Associate Director** – Investor Marketing and Communications
- **Daniel Ellis, Manager** – Marketing and Client Relations

It is ICG's intention to expand the RI Committee as required and when investment strategies are fully embedded in ICG's RI Platform.

The RI committee meets formally three to four times a year, via video conference, across various time zones. The quarterly meetings are designed to cover progress and implementation of ICG's RI programme, as well as any agenda topics that call for input from the entire committee. Members of the RI Committee, which is predominantly comprised of investment executives, interact regularly to discuss any specific ESG concerns that may arise. The RI committee is available at all times to support investment executives during the due diligence and monitoring stages of any investment.

Additionally, ICG has engaged with external ESG experts, where required, to assist in further embedding our RI platform.

Examples of ESG through the Investment Process

With ESG now embedded into many investment processes across the firm, ICG has included a number of recent investment decision making examples impacted by ESG into its UNPRI filing. For the benefit of our investors, a selection of these is provided below. These examples originated across European Subordinated Debt and Equity, Asia-Pacific Subordinated Equity, European SDP and ICG-Longbow portfolios.

- A proposed investment with a financial services company identified some shortfalls in governance procedures which were in the process of being addressed by the company. ICG engaged with the company and sponsor of the topic, and proposed a covenant in its financing structure which made the financing subject to progress milestones in relation to those internal processes.

- During the diligence of one investment opportunity, ICG Longbow received advice from a third party advisor that there was asbestos present in one of the properties securing the proposed investment. The asbestos would significantly affect the marketability of the property. The Investment Committee decided to proceed with the investment, subject to a formal loan covenant being placed on the borrower requiring the safe removal of the asbestos within a defined period.

- A proposed investment was taken to the Investment Committee to consider an opportunity in a manufacturing consumer product business containing a mix of organic and synthetic / chemical ingredients. Upon further due diligence the investment opportunity was declined with the conclusion that the associated environmental and reputation risks were too high.

- The Investment Committee considered a radiation treatment and diagnostic services business and asked for ESG matters and governance to be key due diligence items for the deal team if they advanced to the next step. The deal did not progress, but this was not due to any ESG findings.

- The Investment Committee agreed in principle to proceed with a leather manufacturer that supplies the footwear industry. Despite regular customer audits that found the company processes to be eco-friendly, the Investment Committee requested that a full ESG review be performed at a later stage. The deal did not progress.

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Summary

As ICG looks forward to 2018 and sets targets for its RI Committee and wider business, the key focus will be on further education of staff and deepening the ESG focus of its investment strategies, many of which are now covered by ICG's RI Policy.

On education, the RI Committee is already selecting key conferences for attendance in 2018 and has identified the United Nations Sustainable Development Goals ("SDGs") as a focus of understanding. Additionally, following the success of the 2016 ESG training module and its importance to the education of the wider business, the RI committee will update its online training module in 2018 for distribution to the wider business.

ICG will continue to embed ESG into investment strategies, particularly following the successes with North American Private Debt and Strategic Equity in 2017. 2018 will also be a year of consolidation of the fast deployment realised over the recent years.

Appendix A: Case Study on entry, Garnica, ICG Europe Fund VI Investment

Presented here is an example of a strongly ethical and sustainable portfolio company, 'Grupo Garnica Plywood SA' ("Garnica"), a manufacturer of plywood products made primarily from poplar wood for the construction, caravan, marine, flooring and decorative markets.

> *We consider ourselves much more than just a plywood manufacturer. We are also a company, whose production process actively promotes environmental improvement and sustainable forestry, creating jobs in rural areas and producing long-term profitability in agricultural areas with low productivity.*
> **Statement of Garnica**

Garnica was an investment made as part of ICG's European Subordinated Debt and Equity business. In July 2016, ICG Europe Fund VI invested over EUR 100 million into the business. Key facts behind the business and investment are as follows:

- Founded in 1973 and based in La Rioja (Spain), Garnica is the undisputed leader in the European poplar plywood market;
- Garnica manufactures a wide range of plywood products made primarily from poplar wood for the construction, caravan, marine, flooring and decorative markets; and,
- Part of ICG's investment thesis was around the structural growing demand of sustainable and traceable tree plantations (like European poplar) for wood supply, supported by environmental and regulatory tailwinds.

Ahead of the investment, due to the industry Garnica operates in, ICG felt a full ESG review was important before supporting the business. This included:

- Environment, health and safety due diligence carried out by ERM (leading global provider of environmental, health, safety, risk, and social consulting services). This review revealed that Garnica complied with all ESG regulations applicable in Spain and France with no major risk of pollution or safety; and
- Legal due diligence performed by Cuatrecasas, Gonçalves Pereira (Spain) and Gide Loyrette Nouel (France). Both reviews revealed no material issues were found.

In addition to an attractive business model and strong senior management, ESG was a key factor to this investment, due to a number of strong tailwinds supporting Garnica and the European Plywood industry:

- Trees reduce carbon dioxide in the atmosphere, as one cubic meter of wood absorbs one tone of CO^2. Greater use of wood products will stimulate the expansion of Europe's forests and reduce greenhouse gas emissions by substituting for fossil fuel intensive products. The Commission is examining ways to encourage these trends. *European Commission (2003)*
- Wood can often be used to substitute materials like steel, aluminium, concrete or plastics, which require much larger amounts of energy. Replacing other construction materials with wood would save about 30% primary energy in the manufacturing phase. *European Woodworking Industry*

Looking forward, Garnica is currently working on a pioneering carbon footprint project, which will allow it to compare the CO^2 impact on their different types of panels. A new tool was also launched for customers to calculate the carbon footprint of their orders' transport.

Garnica is a clear example of an ICG investee company where part of the original investment thesis included the fact that it operates in an industry with increasing regulation. There is structural growth in demand for sustainable and traceable tree plantations (like European poplar) for wood supply. In addition, the company itself operates to excellent standards, and we provide the case study here to provide greater depth of how ICG assesses the ESG credentials of an investment.

Appendix B: Case Study on exit, Staci, ICG Europe Fund V Investment

ICG invested USD 60 million in Staci in July 2014 and exited the business in July 2017. Staci is a business-to-business logistic solutions and services provider, with a leading position in the niche market of non-trade products. Commitments and actions towards sustainable development have considerably improved under ICG's investment period.

Commitment to Sustainable Development

Staci is an example of a best-in-class player in a sector increasingly concerned with environmental issues:

- Environmental conservation and "sustainable logistics" have been at the heart of the group for years;
- Staci is an active member of Club Demeter, Ecovadis and Vigilog. The aim of these organizations is to promote and implement tangible and measurable actions regarding Sustainable Development (notably in the Environmental, Social and Economic fields); and,
- In March 2017, Staci was awarded with an Ecovadis Gold status, acknowledging outstanding ESG performance, an improvement from its Silver status in 2015: **Staci now ranks in the top 1% of logistics companies and top 3% of all companies in France considering ESG issues**.
    - Ecovadis is a collaborative platform providing Supplier Sustainability Ratings for global supply chains used by more than 30,000 companies to increase transparency and trust between trading partners

Tangible Environmental, Social and Economic Actions

An ambitious Environmental policy

- Partnership with Veolia considering waste sorting issues
- Implementation of Greenhouse Gas ("GHG") Tracker in order to monitor and reduce the carbon impact of the group
- Implementation of a raw material consumption reduction plan. Staci now uses recycled paper for its delivery notes and optimizes its packaging
- Staci implemented a strong action plan to reduce GHG emission and energy consumption. The global platform regrouping system helps reduce the number of deliveries especially in city centres (e.g. less trucks, pollution and traffic jams)

A committed Human Resources policy

- Reclassification policy for employees declared physically unfit.
- Partnerships with several organisations in order to promote the employment of disabled workers.
- A high full-time employment rate of any temporary workers.

Employee well-being at the heart of Staci's priorities

- Implementation of policies to reduce accidents at work and long term illnesses.
- Monitoring of noise pollution in the most exposed work stations.
- Partnerships with ergonomists in order to continuously improve the working conditions.
- Clear identification of first aid trained employees.
- Recruitment of a full time employee with responsibilities for Health & Security prevention issues.
- Implementation of clearly visible security signs favouring secured work stations.
- Implementation of strong corporate policies to promote gender equality, combat discriminations to favour inclusive employment.

Acknowledgements and Certifications

United Nations Global Compact

- Staci is a member of the United Nations Global Compact, an initiative to encourage businesses worldwide to adopt sustainable and socially responsible policies.

Health, Safety & Environment (HSE)

- Staci is fully committed to HSE, the global set of laws, rules, guidance and processes designed to help protect employees, the public and the environment from harm.

Staci's commitment to ESG is evident by its various certifications

- Staci is carbon footprint certified by Agence de l'Environnement et de la Maîtrise de l'Energie ("ADEME") and uses Veolia's GHG Tracker to monitor its carbon footprint.
- All packaging materials used by Staci are Möbius certified, meaning they are fully recyclable.
- All of Staci's processes are ISO certified.

Appendix C: Extract of Annual ESG survey (5 out of 19 questions)

Segment of ICG's RI Company Survey 2017 survey:

Have you conducted within the last five years an assessment of the business risks and opportunities associated with environmental and/or social issues across your business?

- Yes, environmental
- Yes, social
- Yes, both
- No

Have you developed a sustainability policy (or equivalent, e.g. a corporate responsibility policy, an environmental policy) that applies across your business?

- Yes
- No

Do you publish information on your social and/or environmental performance?

- Yes, social
- Yes, environmental
- Yes, both
- No

Do you assess your carbon footprint?

- Yes
- No

Have you set up a profit-sharing system for your employees?

- Yes
- No

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