

# Engagement Policy – Direct Lending

MV Credit has been in operation for over 20 years and recognises its role within the asset management industry as fulfilling its duties to its investors, the economy, the environment and society.

This Engagement Policy outlines the processes and guidelines followed by MV Credit when putting these responsibilities into practice.

Opportunities for lenders to engage borrowers are typically determined by the level of access the lender can get to senior management and/or the private equity sponsor (if the company is owned by one). This is typically governed by the number of investors involved in the deal. Direct loans made by a small number of lenders (a club) or just one lender allow them greater influence in determining the terms of the deal and engage with the borrower on ESG issues.

Lenders can engage borrowers throughout the investment process, from initial assessment to the post-transaction phase. While lenders lack the influence on management that private equity investors enjoy, there can be productive exchanges between borrowers and lenders during the initial assessment and due diligence phases, and between lenders and shareholders during the holding period.

In public or broadly syndicated markets, where investors either exercise less influence or where coordination problems exist, engagement with portfolio companies is harder to achieve. Conversely, private credit managers typically face reduced agency problems and may offer a more direct means for investors to put their ESG commitments into practice. Applying a tailored approach to ESG engagement by virtue of the direct relationship with management teams and private equity sponsors can also set private credit apart from other markets and allow for a higher degree of engagement.

## Scope

This Engagement Policy applies to all direct lending investment funds managed by MV Credit. MV Credit's engagement activities are executed within the organisation as they are not outsourced. This Policy is updated annually or more frequently as required.

## Engagement: Pre-investment phase

### Due Diligence

During the due diligence phase, MV Credit has several options to engage borrowers. Good engagement seeks to identify relevant ESG issues, set objectives, track results, and incorporate findings into the investment decision making process.

As part of the ESG Investment Procedure the MV Credit Deal Team is required to perform a Controversies Analysis. The controversies are rated with a severity score from 1 to 5. For any borrower having experienced a controversy with a severity level of 4 or 5, the MV Credit Deal Team will need to engage, alongside the ESG Officer, with the management team of the borrower and/or the private equity sponsor to clear the issue and document it in the Investment Memorandum in order to proceed with the investment.

The MV Credit Deal Team, along with the ESG Committee and the ESG Officer, is also responsible for identifying, evaluating, and managing ESG opportunities and issues within each potential investment. To this end, the team engages with senior management of prospective borrowers for disclosure of potential ESG risks and opportunities via Q&A sessions, as well as the sponsoring company.

Finally, to assess the underlying borrowers' ability to report on ESG on an ongoing basis, the MV Credit Deal Team is required to always request ESG reporting as part of the borrower's mandatory information undertakings when negotiating the relevant loan documentation, even though this is not a pre-requisite to signing.

### Sustainability-Linked Products

MV Credit has been at the forefront in the growth of the Sustainability Linked Loan ("SLL"), a recent development gaining increased acceptance in the private credit industry. The defining feature of the SLL focuses on incentivising the borrower to improve the company's performance against certain pre-determined ESG criteria within the loan terms. This is then typically implemented via a ratchet mechanism on the margin. The structures of the loans have evolved from the use of standard third-party rating agencies to more bespoke KPIs. MV Credit will continue to offer SLLs across all its Direct Lending funds, aiming to positively incentivise the behaviour of the underlying borrowers, bearing in mind that MV Credit's main priority is to make sure that the KPIs of such structures fit the borrower's main challenges and that they are material to its business.

## Engagement: Post-investment phase

Post-investment governance generally lies with the controlling sponsor (majority private equity owner) however this is increasingly supplemented by covenants within loan documentation (see previous paragraph). It is also key for MV Credit to focus its engagement on portfolio companies – as well as their respective sponsors - that show the lowest ESG performances over the life of the investment. MV Credit will regularly engage in conversation with the sponsor as it will often lend to multiple portfolio companies.

### Open dialogue

MV Credit monitors all relevant investment and ESG risks on an ongoing basis. Investment and ESG monitoring responsibilities lie predominantly with the Credit Monitoring Team and the Deal Team. During the investment hold period, both teams are required to raise attention to any ad-hoc ESG related events and/or incidents concerning a borrower. If such monitoring results in, or requires risk mitigating activities, the MV Credit Team will work closely with the controlling private equity owner and related parties to understand the issue and the plans in place to mitigate the relevant risk.

Throughout the year, MV Credit will engage with all borrowers either through quarterly management calls, annual lender calls, ad-hoc Q&As or direct conversations with the relevant sponsor. Collaborative engagement concerning a borrower's ESG agenda will be tailored to the underlying business relevant size, industry, and business model; and is typically based on fundamental themes highlighted through the borrowers ESG Assessment Score, Controversies Analysis and relevant ad-hoc ESG findings.

To further strengthen collaborate engagement across the Privat Debt / Lending industry, MV Credit further participates in cross-collaboration between ESG focussed associations (such as ELFA), our Privat Debt / Lending peers and sponsors. Our dedicated ESG Team regularly liaises with such business relationships to foster more transparency in our industry and to ensure progress alignment in our engagement practices.

### Transparency and reporting

In addition to ad-hoc reviews of ESG related incidents or material matters, the MV Credit Deal Team and the ESG Committee annually review a third-party ESG specialist's report which independently evaluates and scores every borrower's ESG performance. MV Credit has established and co-designed its own proprietary framework, comprised of 56 KPIs (Key Performance Indicators) to date (including the mandatory Principal Adverse Impact indicators as per SFDR<sup>1</sup> regulation requirements), in order to assess portfolio borrowers' ESG performance. Using this framework, MV Credit collects individual qualitative and quantitative indicators on an annual basis, directly from the borrowers. KPIs are categorised into themes (E, S, G and Stakeholders) and sub-themes. Each KPI is scored, allowing the consolidation of scores by sub-themes, themes and ultimately global ESG Score for each borrower from 0 to 100.

Based on these analyses, the MV Credit Deal Team will engage borrowers experiencing the lowest response rate to its ESG Questionnaire. MV Credit will seek to understand whether this was due to a lack of time to fill in the questionnaire, or if the borrower is not tracking ESG KPIs yet. Here it is important to note that significant challenges with respect to the materiality, availability, quality and consistency of ESG data persist across the market. Many borrowers have not experienced the same focus on ESG as financial markets. Building the knowledge and capacity required to measure and consistently report ESG data is a considerable investment for private businesses and implementing an appropriate process will take time. In recognising this challenge, MV Credit will offer to have a dedicated discussion to help the borrower identify the main ESG metrics to focus on, based on its activity and improve its capacity to make requested disclosures. The team will also engage if the low scoring is a result of poor ESG performance, in order to provide some guidance on how to improve it.

In addition, on an ad-hoc basis and upon borrowers' requirement, MV Credit can provide some dedicated education sessions to provide guidance on how to improve the borrower's ESG Score.

## Relationship with Private Equity Sponsors

MV Credit exclusively invests in sponsored transactions with focus on senior and subordinated private debt instruments. Therefore, MV Credit does not have direct control or ownership but actively engages with private equity sponsors on management of ESG factors. MV Credit is often the sole lender or one of a small club.

The positive impact of an engaged sponsor, for example one who can provide technical assistance to portfolio companies and help them formalise ESG practices is extremely valuable. Thus, MV Credit engages with sponsors on a regular basis to address any ad-hoc ESG-related event during the lifetime of the investment.

In addition, MV Credit's ESG Officer organises quarterly meetings with key private equity partners (i.e. sponsors holding a big proportion of portfolio companies), to (i) share data collected on both sides, (ii) define priority work streams, potentially together with other majority lenders, (iii) plan site visits dedicated to sustainability.

<sup>1</sup> Sustainable Finance Disclosure Regulation (EU)

Finally, MV Credit engages with sponsors in the context of annual ESG performance reviews, to optimise the data collection process. MV Credit has developed these relationships over a period of over 20 years and works collaboratively with private equity sponsors to achieve shared ESG objectives.

## Governance

### Fiduciary duty

MV Credit is deeply committed to fulfilling its fiduciary duty to clients and beneficiaries, reflecting the unique investment needs of its diverse investor base. MV Credit's fiduciary duty is also deeply integrated into its sustainability culture. MV Credit's Engagement Policy is closely aligned with its investment strategies and thus aims to use research-based, quality driven processes to produce the best possible long-term results for its clients. Therefore, the firm's engagement activities are aimed at long-term value creation in its investee portfolio companies, based on the company-wide philosophy that companies which act in a sustainable way towards the environment, society, and all its stakeholders are better equipped to manage unforeseen and diverse risks, including systemic challenges.

### Conflicts of interest

As a management company focused on private debt, MV Credit respects the principles of professional ethics applicable to it. The firm conducts its business in accordance with FCA Principle 8 which requires the firm to manage conflicts of interest fairly, both between the firm and its clients as well as between one client and another client. MV Credit's policy ensures that all appropriate steps are taken to maintain and operate effective organisational and administrative arrangements to identify, and to prevent or manage potential and actual conflicts of interest, always placing the best interests of investors at the forefront.

Throughout the firm, all teams are committed to complying with internal policies and procedures on which they are regularly trained and made aware. The head of compliance and internal control ensures compliance with these principles through regular monitoring and the use of professional ethics teams.

## Conclusion

As the role of ESG continues to expand for all key stakeholders across the private credit industry, MV Credit views engagement as a key element of its overall ESG integration strategy. By rigorously implementing the above standards and guidelines, MV Credit seeks to maintain its commitment to ESG at the core of its investment strategy.

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