

BlackRock

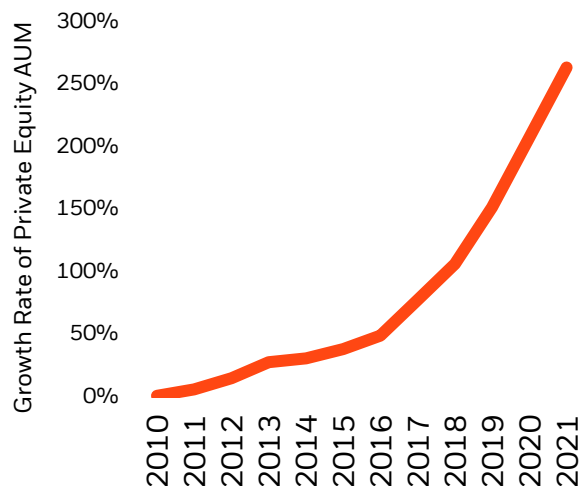
ESG in Private Debt

FOR PROFESSIONAL CLIENTS AND QUALIFIED INVESTORS / QUALIFIED CLIENTS ONLY

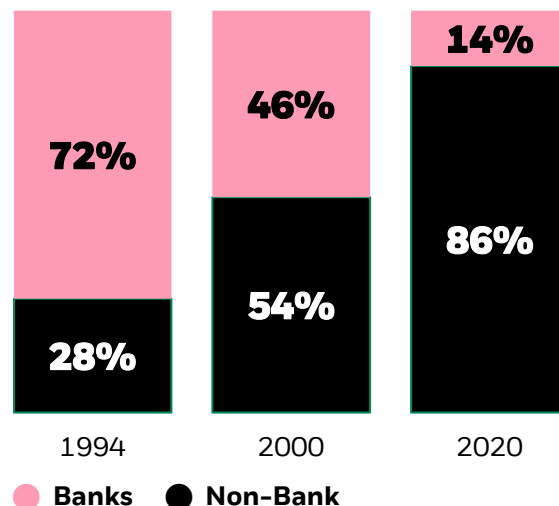
Private markets play an increasingly prominent role in economic growth.

Long-term growth in private company ownership¹

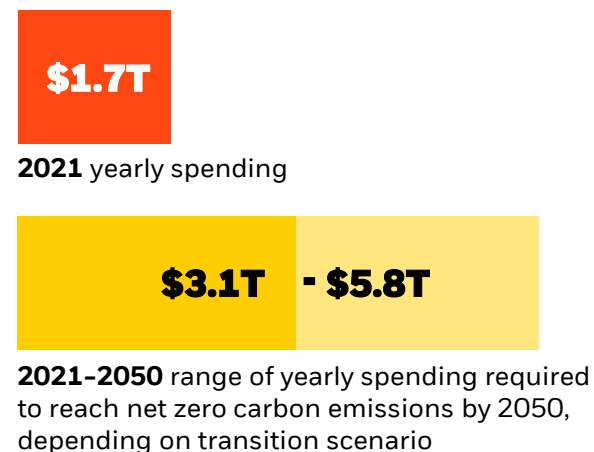
Private Equity AUM (as of Sep 2021) = **\$8.06tn**



Banks retreating from credit markets has opened up new sources of funding²

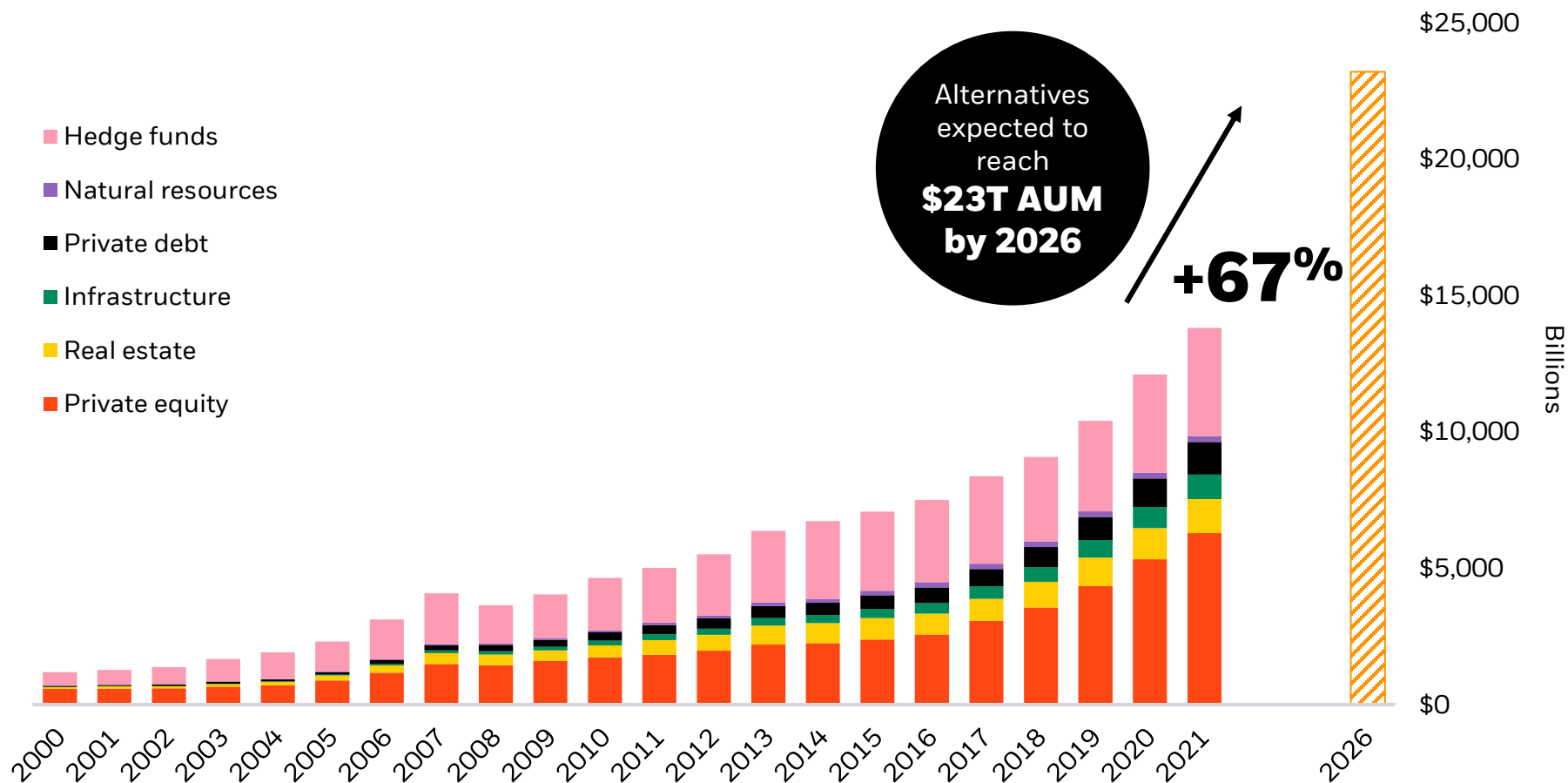


Transition to net-zero carbon increases need for infrastructure and energy investments³



¹ Preqin. Private Equity AUM as of 30/09/2021. ² Oaktree Capital, S&P LCD, 31/12/2020. ³ Bloomberg NEF 'New Energy Outlook 2021' 31/7/2021. Total yearly investments into energy infrastructure needs to more than double in order to achieve the energy transition. All dollar figures are in USD. For illustrative purposes only. Forecasts are not guaranteed and subject to change.

Private markets are larger, deeper and more complex. They continue to expand...



Source: Preqin. Annualized AUM as of 30/6/2021, except Hedge Funds data which is from HFR Industry Reports as of 31/10/2021. \$23T AUM estimate from 12/1/2022 Preqin "Alternatives in 2022" Report. All dollar figures are in USD. **Forecasts are not guaranteed and subject to change.**

...With ESG-specific strategies seen as increasingly important...

76%

of investors in alternatives say their organizations' **ESG interests or capabilities** have increased over the past 12 months.¹



84%

of investors in alternatives believe that **ESG integration will have at least neutral or positive effect on risk-adjusted returns.**²

¹ Preqin Investor Outlook Alternative Assets H2 2021. 76% of survey respondents when describing the change in their organizations' ESG interests or capabilities over the past 12 months have said they have increased. ² [LGT Capital Partners](#) – last accessed 24/1/22.

“

Our investment conviction is that sustainability – and climate-integrated portfolios can provide better risk-adjusted returns to investors. With the impact of sustainability on investment returns increasing, we believe that sustainable investing is the strongest foundation for client portfolios going forward.”

Source: Larry Fink, 2020 Annual Letter to CEOs

Sustainability is at the heart of our approach, from risk management to active engagement with borrowers



1 Core to our investment process

ESG risk considerations are fully embedded in our fundamental research, due diligence and investment decision processes across our Global credit platform

2 Proprietary ESG scorecard

Our investment teams make informed judgements about material ESG risks and opportunities, using both internal and external data tools. Our proprietary scorecard brings consistency and transparency on ESG risk in our portfolios

3 Enhanced data and reporting

Availability of ESG data is a key challenge for investors in private mid-market companies. We have built reporting solutions to enhance the ability to report ESG data to our investors on sustainable outcomes

4 Engagement

As lenders with privileged access to our portfolio companies, we play an active role to help them progress in their ESG journey through a series of initiatives, focusing on climate among others

5 The Fund is Article 8 under SFDR

BAI's sustainable investing governance provides multiple lines of defense in driving accountability

BlackRock Alternative Investors

BlackRock Sustainable Investing (BSI)







Team of 35 that oversees the firm-wide strategy, including investment management, solutions, data & technology, stewardship, ESG research and transparency & reporting

Executive Sponsors

Edwin Conway, Global Head of BAI; **Todd Slattery**, COO of BAI; **Jim Barry**, CIO of BAI

BAI Sustainable Investing Team

Dedicated team responsible for implementing firm-wide strategy across Alternatives

 Kristen Weldon Managing Director, Global Head of BAI Sustainable Investing London	 Sally Michalski Vice President, Head of ESG Strategy & Engagement Seattle	 Brianna Barrett Director, Head of BAI Sustainable Investing for the Americas New York	 Tom Snape Vice President, BAI Sustainable Investing – Climate Focus London	 Katherine Sherwin Director, Global Head of Real Assets Sustainable Investing Paris	 Ioannis Armaos Associate, BAI Sustainable Investing – Real Assets Focus Paris
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BAI Sustainability OpCo

BAI Exco + Senior ESG Champions meet quarterly driving ownership, accountability & knowledge sharing

Risk & Quantitative Analysis (RQA) + CIO Office review

ESG risk analysed with the same rigor as traditional measures such as credit or liquidity risk.

Investment Businesses

Private Equity







Real Assets

Global Credit

Hedge Funds

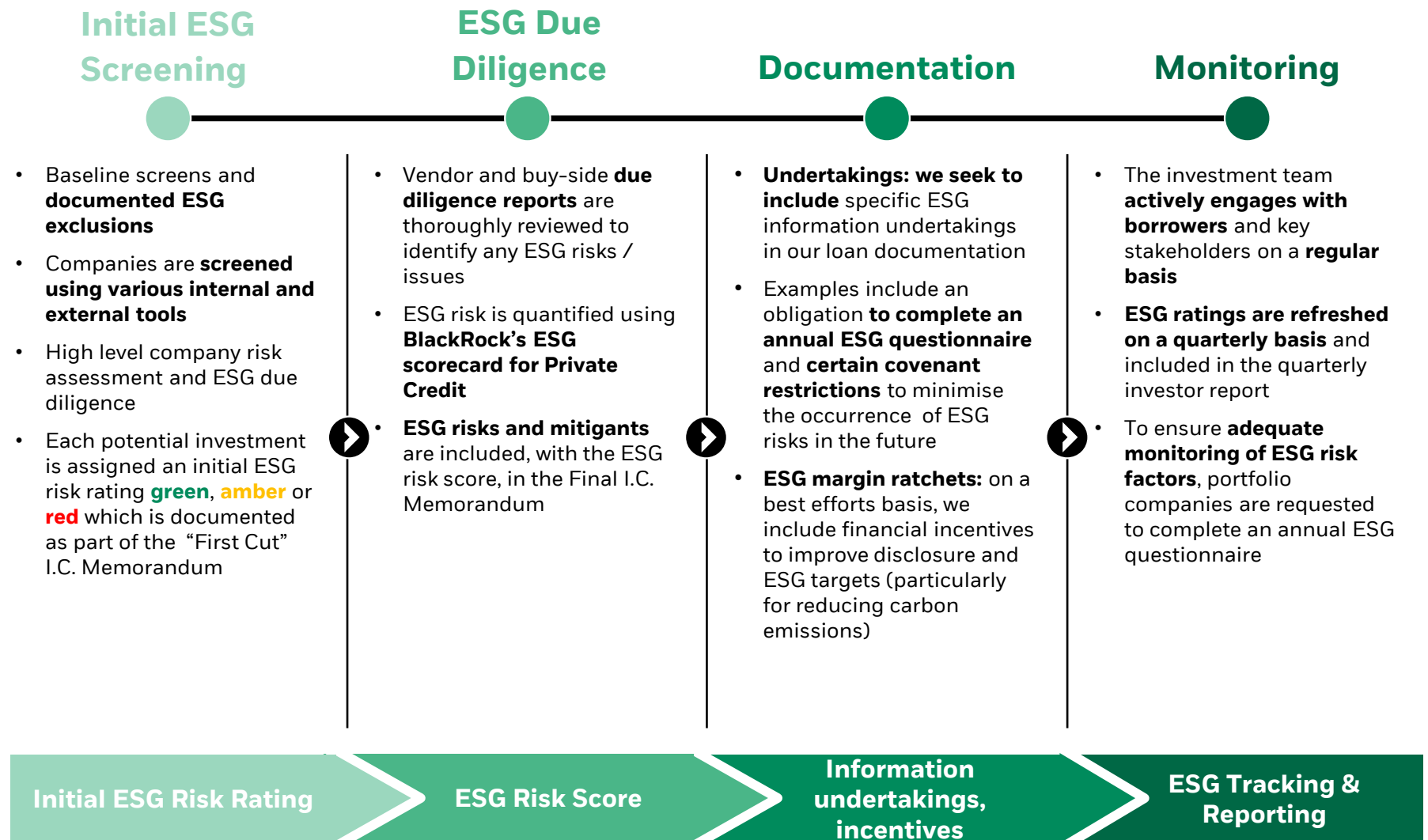
Alternative Solutions Group

Credit Sustainable Investing Leadership Team

 James Keenan Co-Head & CIO Global Credit	 Matt Kaczmarek Head of Credit Sustainable Investing	 Sonia Rocher Managing Director, Global Private Credit	 Dave Delbos Managing Director, Liquid Credit	 Katharine Field Managing Director, Product Strategy	 Venn Saltirov Director, Training & Governance
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Source: BlackRock, as of 30 September 2021. Subject to change.

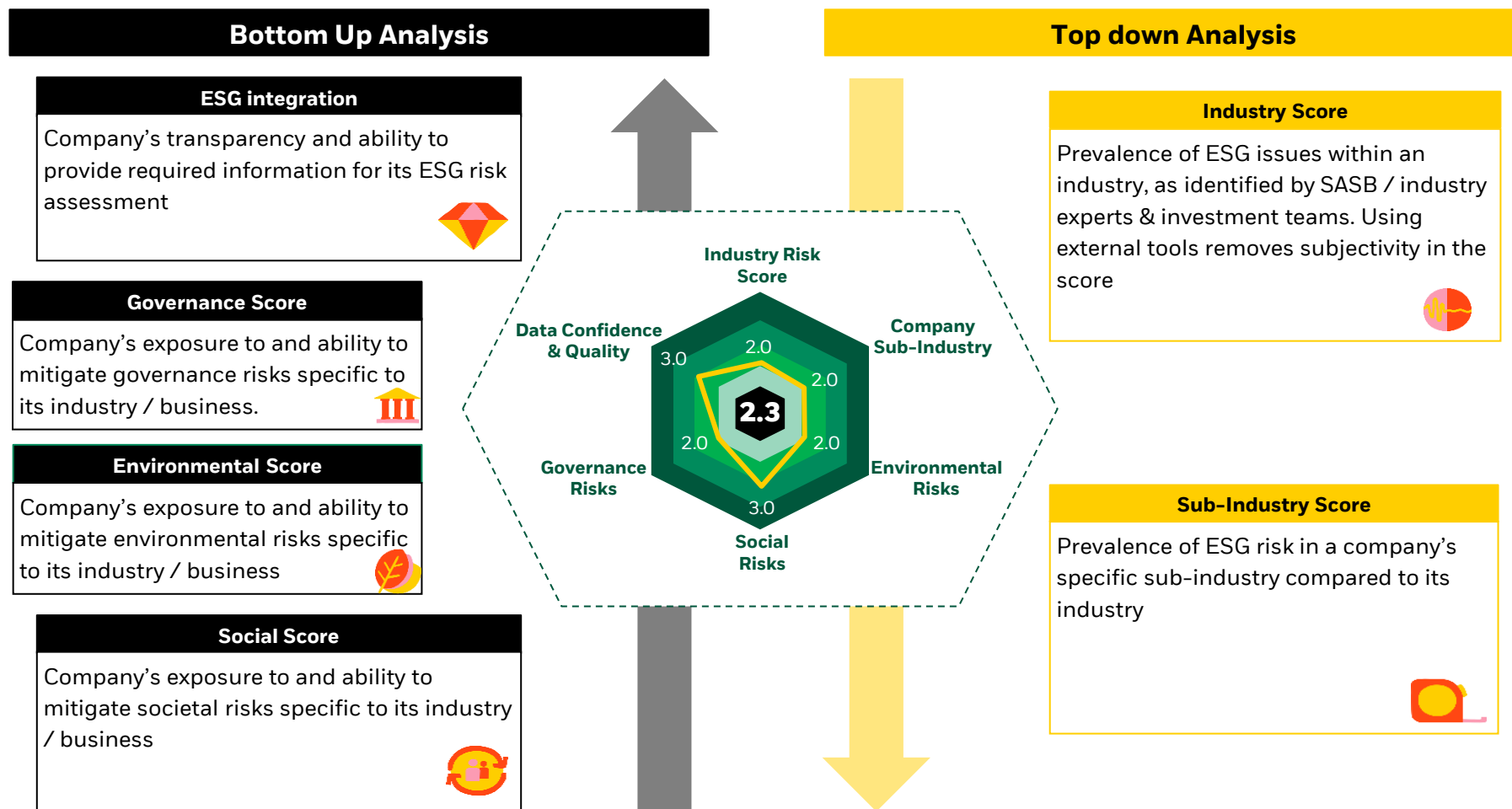
1. ESG factors are fully integrated in the underwriting process



Source: BlackRock, as of 30 September 2021. Investment process is subject to change and provided here for illustrative purposes only.

2. BlackRock Proprietary ESG Scorecard for Private Credit

Each company is assigned an ESG risk score which is the weighted average of its Industry (industry and sub-industry) and Company (ESG integration and individual “E”, “S” and “G”) scores. The scoring model promotes transparency and consistency in this process and provides a rich data source for ESG monitoring and analytics.



Source: BlackRock, as of 30 September 2021. Investment process is subject to change and provided here for illustrative purposes only.

3. Enhanced data and reporting

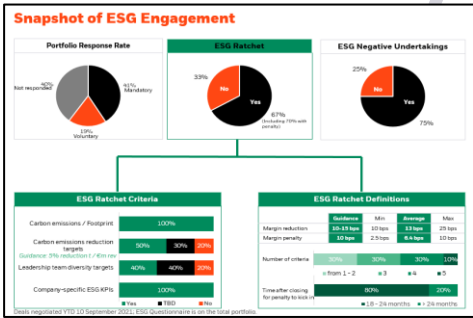
The tools we have built

- 1 Proprietary ESG scorecard**
- 2 Annual ESG Questionnaire**
- 3 ESG Process (incl. engagement)**

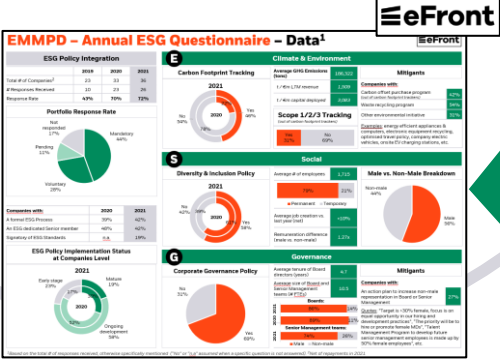
Client Reporting



Portfolio risk view



Engagement



ESG Data

4. Engagement with portfolio companies¹

- We maintain an **active dialogue** with our portfolio companies and industry associations to **drive sustainable outcomes**:

ACTIVE ENGAGEMENT TO DRIVE SUSTAINABLE OUTCOMES

Annual ESG Questionnaire

Subsidising some climate reporting

ESG ratchets

Sharing best practices

Industry associations committees

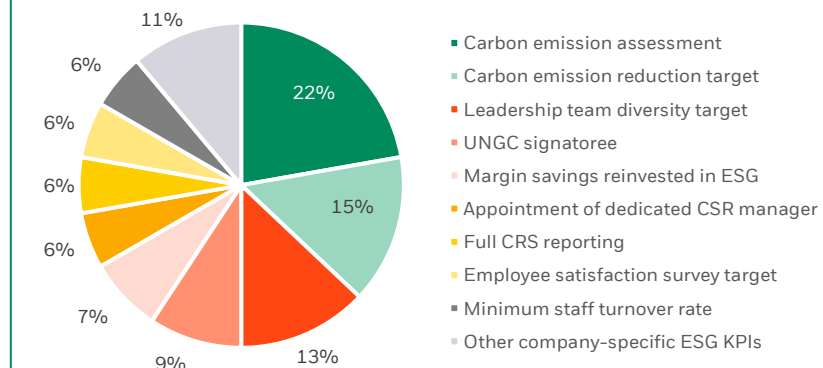
- We include **financial incentives (e.g. ESG ratchets)** on a best efforts basis in our loan documentation to **make our portfolio companies accountable**:

FOCUS ON ESG RATCHETS

ESG Ratchet Adoption²



Range of ESG Ratchet Criteria



“67% of EMMPD III transactions have ESG margin ratchets”

“80% of 2021 European transactions¹ have ESG Information Undertakings”

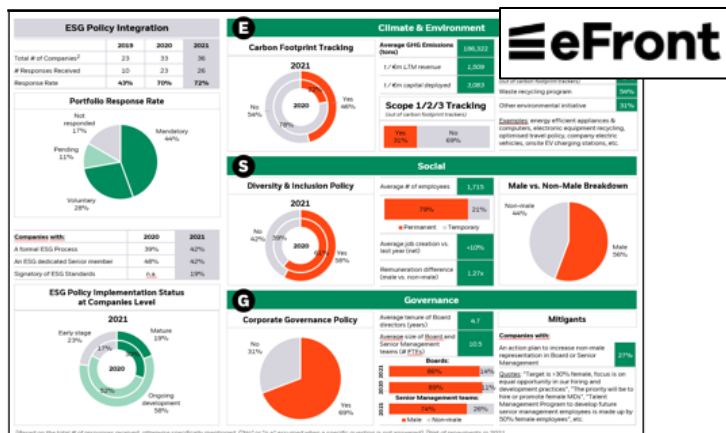
Source: BlackRock, as of 30 September 2021. ¹ Figures are for BlackRock European Middle-Market Debt Fund III as of 30 September 2021

4. ESG Data from Portfolio Companies¹

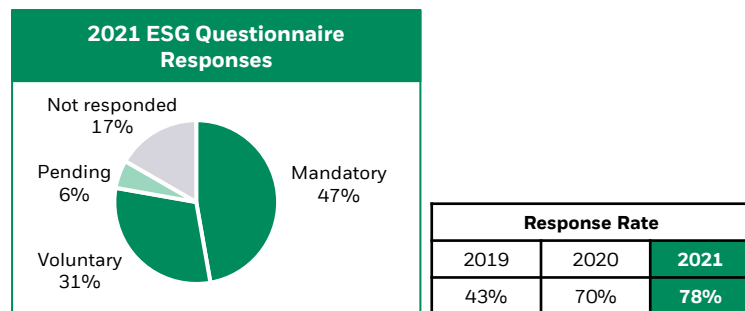
- We have developed **proprietary tools** to address information gaps in Private Debt so that we can **effectively monitor our portfolio companies' progress towards their ESG objectives** as well as **ESG risks in our portfolios**

GRANULAR ESG DATA...

- Our proprietary ESG questionnaire allows us to gather granular ESG data from our portfolio companies

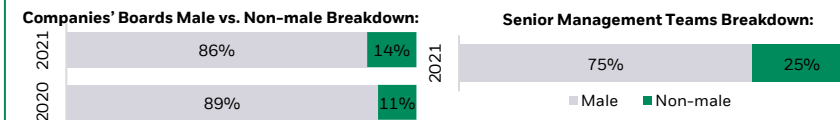
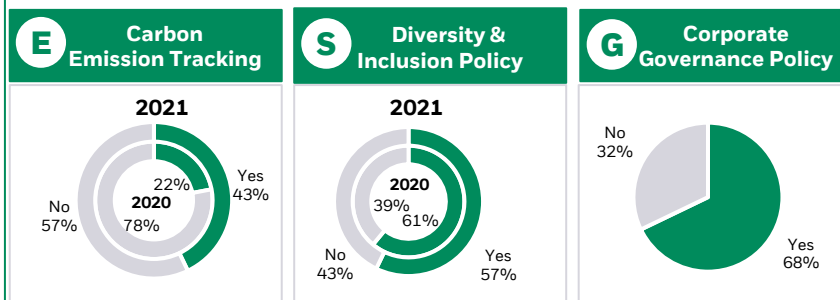


- Almost 80% of our portfolio companies have responded this year

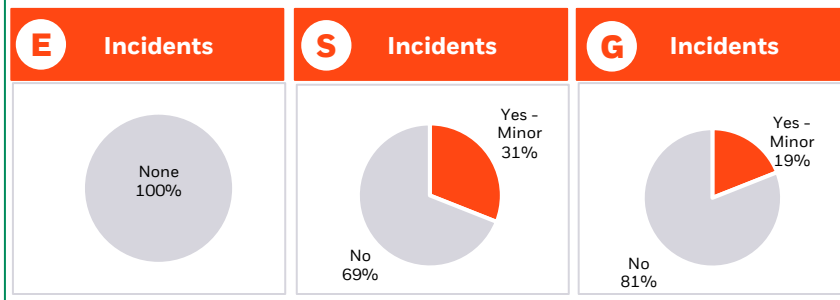


... FOR DETAILED ANALYTICS

- We use this information to effectively monitor our portfolio companies' progress against set KPIs...

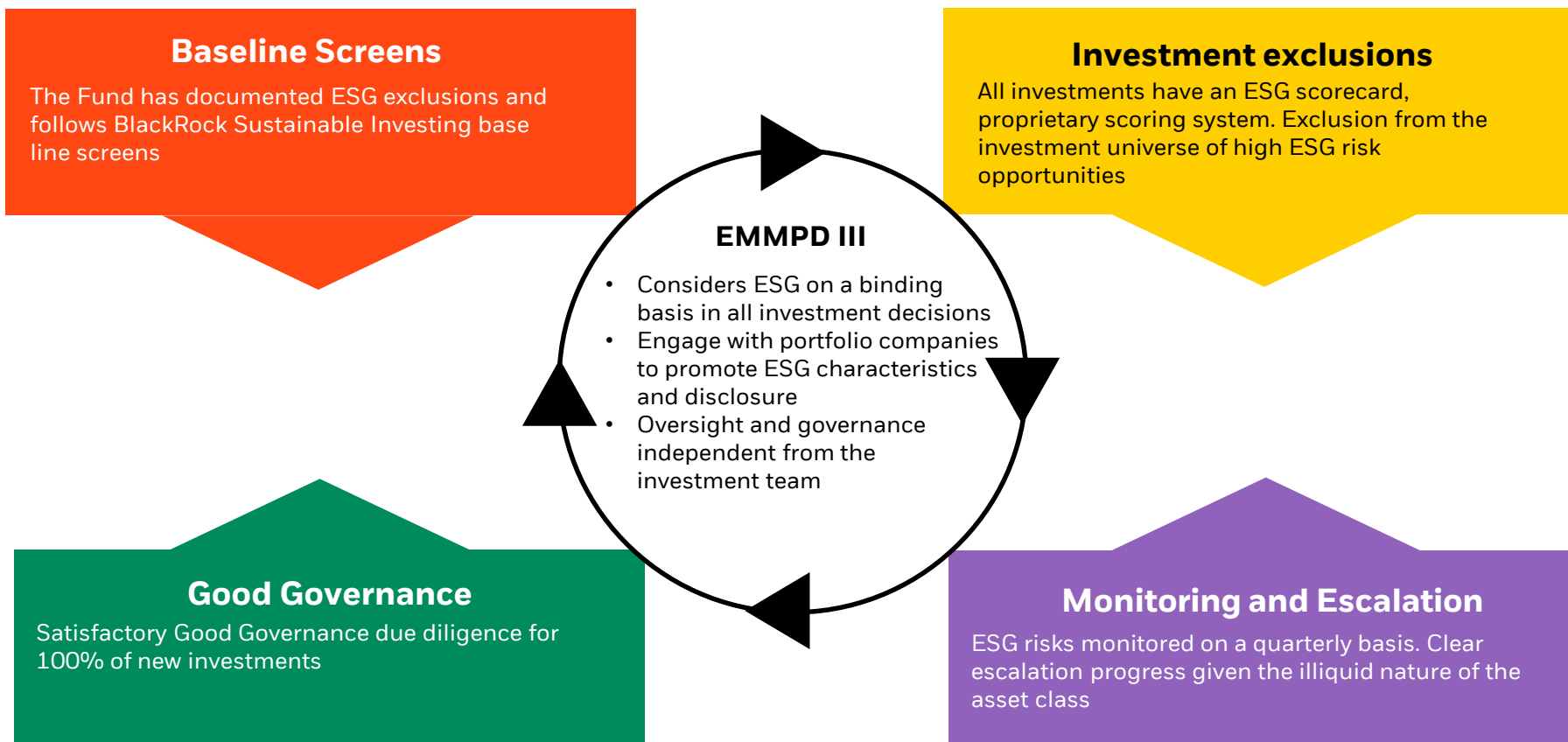








- ... as well as ESG risks in our portfolios.



Source: BlackRock, as of 30 September 2021. ¹ Figures are for BlackRock European Middle-Market Debt Fund III as of 30 September 2021

5. EMMPD III: SFDR Article 8



Excluded Industries						
	Mining and/or extraction of thermal coal	Tar (oil) sand production or extraction	Production/distribution of palm oil	Production/distribution of weapons, firearms & ammunitions	Production/distribution of tobacco products	Adult Entertainment

Cases studies - ESG engagement

Sustainability is fully embedded in our analysis and investment decisions

Project Forrest

- ✓ ESG ratchets
- ✓ Positive environmental impact
- ✓ Sustainability included in management strategy



Project Balance

- ✓ ESG ratchets
- ✓ Additional ESG due diligence
- ✓ Sustainability at the centre of management's strategy with ESG targets



Project Nausicaa

- ✓ ESG ratchets
- ✓ Management increased ESG engagement
- ✓ Sustainability included in management strategy



European network service integrator and maintenance provider



Deal Summary: BlackRock provided a senior secured loan for a primary buy-out by an ESG-focused private equity investor.

Process: The company drives a **positive environmental impact** by building, upgrading and maintaining IT infrastructure to newest standards which allows for energy monitoring and CO2 savings due to more efficient network levels.

Outcome: Credit documentation includes an **ESG Ratchet** mechanism with interest margin step-downs if the company is compliant with the majority of ESG criteria (including carbon footprint assessment) and an interest margin step-up if no ESG criteria are fulfilled.

Global outsourced physical marketing material procurement



Deal Summary: Senior secured loan to a leading printed material procurement outsourcer to support its acquisitive growth strategy.

Process: Concerns around the environmental sustainability of printing were mitigated through **in-depth diligence**, highlighting (i) a key benefit for clients of outsourcing is improved sustainability; and (ii) the company's strong ESG policies and track record of realising environmental savings recognised through numerous ESG awards (e.g. in the top 5% of companies rated by EcoVadis).

Outcome: **ESG ratchets** criteria including (i) commitment to 100% use of renewable energy and reduce emissions by 25% by 2025, (ii) board diversity and (iii) sustainable supply chain targets.

French veterinary clinics network



Deal Summary: BlackRock provided a senior secured loan and an acquisition and capex facility to a leading French veterinary clinics network to support its growth through acquisitions and greenfield development.

Process: The management did not have any ESG policy in place at the time of investment, but has shown **increased engagement since** (highly diverse employee profile, increasingly focused on recycling, plastic reduction, proximity services).

Outcome: Credit documentation includes an **ESG Ratchet mechanism** with interest margin step-downs if the company is compliant with the majority of ESG criteria (including carbon footprint assessment and reinvestment in ESG initiatives) and an interest margin step-up if no carbon footprint assessment is conducted post-close.

Source: BlackRock, 30 September 2021. Investment has been chosen as it is the most recent available case study of ESG integration practices in this asset class. Case studies are for illustrative purposes only; they are not meant as a guarantee of any future results or experience, and should not be interpreted as advice or a recommendation.

Case studies - Transactions declined due to ESG risk

Transactions abandoned during the due diligence process due to ESG risks

Environmental

- ✗ Adverse impact on the environment
- ✗ Concerns for local communities



French theme park group

Deal Summary: Opportunity to partly finance the greenfield expansion of a French group of theme parks into a new country.

Process: The European Private Debt team was approached by the company's debt advisor to consider a financing, which was declined largely due to inherent ESG concerns brought to light by local ecologists and political groups (e.g. related to the use of water resources, cutting down of trees, requirement of changes to municipal/regional laws to permit noise pollution).

Outcome: The team declined the financing at an early stage as a result of these ESG / **Environmental** concerns.

Social

- ✗ High social risk
- ✗ Reputation risk



Spanish producer of narcotic raw material for medical applications

Deal Summary: Primary buyout of one of the largest producers, and one of only nine globally licensed and accredited (only one in Europe) suppliers, of narcotic raw materials for medical and pain relief applications.

Process: The European Private Debt team was approached by a top-tier internationally recognised healthcare specialist private equity investor to consider a financing which was declined due to (i) social considerations around the opioids crisis (particularly in the USA); and (ii) negative public perception around these raw materials – even though the investment considered was exclusively related to licensed and approved medical applications.

Outcome: The team declined the financing at an early stage as a result of these ESG/ **Social** concerns.

Governance

- ✗ Concerns over Governance
- ✗ High risk operations
- ✗ Risk of corruption / AML



Italian Global logistics Group refinancing

Deal Summary: Refinancing for an Italian logistic and B2B customs services company involved in the worldwide shipping of jewellery, precious gems and luxury goods. Privately owned.

Process: The European Private Debt team was approached by a financial advisor to consider a financing which was declined due to (i) negative findings from BlackRock-commissioned background checks on the management team; and (ii) inadequate governance structure and internal controls.

Outcome: The team declined the financing at the due diligence stage as a result of these ESG / **Governance** concerns.

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