CGF8 - POLICY ON ENVIRONMENTAL, SOCIAL AND GOVERNANCE SUSTAINABILITY

SUB POLICY OF CORPORATE GOVERNANCE FRAMEWORK OF PMF

Version 1.0

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Contents

1.0 Purpose of the policy

The Sustainable Finance Policy governs the approach that PMF Finance PLC (PMF) adopts towards sustainable finance and confirms its commitment to responsible financial practices. The Policy governs PMF's efforts to meet the strategic ambitions on sustainability laid out in the "Roadmap for Sustainable Development" published by the Central Bank of Sri Lanka in 2019.

PMF embraces the system thinking approach to growth and acknowledges the powerful synergies that could potentially result from connecting the financial sector with the broader ecosystem. PMF understands the importance of its role in redressing environmental degradation, global warming, rising greenhouse gas emissions, and pollution as well as poverty, inequality, and unemployment, among other challenges.

In light of the above, PMF emphasizes its commitment to achieving growth while advancing sustainable development. PMF understands that its commitment to delivering value creation to its stakeholders and the ecosystem is subject to its understanding and implementation of sustainable finance in its business operations. Therefore, it integrates sustainability matters into financial solutions, processes and governance.

PMF believes that sustainable finance is a driving force for economic, environmental, and social development, which depends on upholding governance rulings. PMF understands that sustainable finance represents the integration of the environmental, social, and governance aspects in all business operations along with the economic aspect. Accordingly, this implies that PMF's business operations respect and advance the protection of the environment, human rights, labor rights, good governance, and business ethics.

This policy asserts PMF's commitment to implementing sustainable finance across its lines of business by integrating the Environmental, Social, and Governance (ESG) principles into its policies, procedures, operations, and culture. This policy defines and sets a comprehensive framework that translates the PMF's commitments into actions and instils a governance framework to monitor proper implementation in compliance with the guideline issued by Central Bank of Sri Lanka on sustainable finance activities and Section 9 of the Listing Rules of Colombo Stock Exchange.

2.0 Scope of the policy

PMF's Sustainable Finance Policy is applicable to all the departments, functions, and lines of business. It provides guidance to all internal stakeholders who are responsible for aligning with the requirements of this policy in their respective areas of responsibility.

3.0 Guiding principles

3.1 PMF will strive to align its business strategy to be consistent with and contribute to individuals' needs and society's goals, as expressed in the Sustainable Development Goals set at the national level.

3.2 PMF will continuously strive to increase its positive impacts while reducing the negative impacts on, and managing the risks to, people and environment resulting from its activities, products and services. To this end, PMF will set and review targets where it can have the most significant impacts.

3.3 PMF will work responsibly with its customers to encourage sustainable practices and enable economic activities that create shared prosperity for current and future generations.

3.4 PMF will strive to proactively and responsibly consult, engage and partner with relevant stakeholders to achieve society's goals.

3.5 PMF will implement its commitment to these principles through effective governance and a culture of responsible financing.

3.6 PMF will periodically review its implementation of these principles and be transparent about and accountable for its positive and negative impacts and its contribution to society's goals.

4.0 Sustainable lending practices

PMF is committed to assess and mitigate environmental, social and governance risks in its lending portfolio. Accordingly;

4.1 PMF's lending activities will comply with applicable Sri Lankan laws and regulations along with any multilateral environmental, social and biodiversity agreements and/or conventions ratified by Sri Lanka.

4.2 PMF will ensure that lending is provided for following priority sectors that have robust environmental and social management systems that enable early identification of risks and impacts and their effective mitigation.

- Forestry and logging
- Agriculture
- Manufacturing
- Electric power generation, transmission, and distribution
- Water supply, sewerage and waste management
- Construction
- Transportation and storage
- Tourism and recreation
- Information and communication technology
- Financial Services
- Other activities such as gas, steam and air conditioning supply, underground permanent geological storage of CO_2, Hydrogen storage

4.3 Through its lending activities, PMF will seek to uphold the protection of human rights and assure fairness, inclusion and development opportunities for all its stakeholders.

4.4 PMF strives to support the growth of small and medium enterprises and entrepreneurs. PMF is also committed to serving un-banked/ under-banked segments of society by facilitating access to finance, financial products, and services with close emphasis on women and youth empowerment.

4.5 PMF is keen on offering products and programs to customers addressing environmental or social challenges such as promoting financial inclusion and/or the mitigation of climate change.

4.6 PMF will implement screening, appraisal and monitoring procedures to safeguard the commitments related to sustainable financing.

4.7 PMF commits to ensure that funds will not be used to finance the following type of activities (Exclusion list);

- Manufacture and marketing of banned drugs
- Production and distribution of pornographic material
- Dealing in narcotics
- Dealing in banned wildlife related products
- Polluting industries unless the units have clearance from pollution control authorities and have installed effluent treatment plants
- Setting up of new units consuming/producing Ozone Depleting Substances (ODS) such as chlorofluorocarbon (CFC)
- Standalone Casino, and Gambling / Betting in any form
- Production or trade in any product or activity deemed illegal under host country laws or regulations or international conventions and agreements, or subject to international bans
- Production or trade in weapons and ammunitions
- Production or trade in radioactive materials

5.0 Sustainable operational practices

PMF is committed to pursuing environmental and social responsibility in the it's day-to-day operations

5.1 PMF is committed to improving it’s environmental footprint. PMF strives to meet satisfactory standards for safety and limit the environmental impact of its premises by regulating its emissions and ensuring the safe removal and management of its waste.

5.2 PMF is committed to contributing to the development of human capital through its business operations by promoting gender equality, fair working conditions, talent management and development, diversity and inclusion, and social engagement. PMF does not tolerate discrimination or any form of harassment based on gender, age, disability, ethnicity, or religious belief.

6.0 Sustainable investment initiatives

PMF aspires to make a positive contribution to the broader society by investing in and sponsoring initiatives and projects that have a positive impact on the environment and society at large.

7.0 Digital transformation

PMF is committed to introducing innovative financial solutions that are integral to its commitment to financial inclusion and to having a positive economic, social, and environmental impact.

8.0 Stakeholder engagement

PMF is committed to achieving long-term value creation for all stakeholders. PMF's Sustainable Finance approach is built around growth achieved through establishing connections with its stakeholders and the ecosystem at large. This ranges from employees, clients, investors, regulators, and peers.

8.1 Employees

As employees represent its most valuable asset, PMF is committed to attracting qualified candidates regardless of gender, age, disability, or belief. PMF ensures proactive and effective management of its employees' well-being, work-life balance, and development. PMF is committed to fostering a diverse and inclusive workforce that encourages innovation and ensures the sustainability of its operations and its competitive position in the market.

8.2 Customers

PMF is committed to supporting its customers and helping them achieve their financial targets and to grow their businesses. PMF is committed to ensuring customer privacy, data protection, and responsible customer management.

8.3 Community

PMF is committed to helping the economic development and societal prosperity of the communities it serves whether directly through its operations or indirectly through its guiding principles for this purpose.

8.4 Regulators

PMF is committed to having a proactive approach with regulators and other national authorities to deliver timely and correct information, ensuring compliance and transparency.

8.5 Investors

PMF is committed to keeping shareholders and the investment community informed at all required instances. This is to establish long-term relationships with its shareholders, which entails value creation, trust and transparency. PMF is committed to provide current and future shareholders with relevant and timely information.

8.6 Peers

PMF is committed to actively engaging with its peers in the financial sector and promoting ESG and sustainability practices within the industry.

9.0 Roles and responsibilities

9.1 ***Board of Directors (BOD)***

- Approving the Sustainable Finance Policy of PMF.
- Ensure the integration of ESG into PMF's governance structure via its policies, operations and the culture.
- Ensure the right resources are assigned to integrate the sustainability into PMF's strategies and systems.
- Monitor the periodic progress made by PMF in terms of ESG.

9.2 ***Senior Management Team***

- Policies, operational procedures, metrices and controls implemented by PMF related to ESG, must be reviewed and update at least annually.
- Allocate resources, skills and expertise to the implementation and management of sustainable finance activities.
- Clearly articulate the roles and responsibilities of business units and functions in managing risks associated with sustainable finance activities.
- Inform the BOD in a timely manner on the progress and material issues relating to sustainable finance activities.

9.3 ***Heads of departments***

- Identifying the ESG compliance requirements and obligations relevant to their function.
- Support to embed sustainability across all lines of business and departments.

9.4 ***Compliance department***

- Facilitate to ensures the centrality of sustainable finance as a core business strategy and provides a solid platform to integrate environmental, social, and governance (ESG) principles across PMF's functions.

9.5 ***All staff***

- Acting with integrity and honesty in all their duties and ensure the adherence to the ESG requirements in his/her area of responsibility is the responsibility of all staff for compliance.

10.0 Key Performance Indicators (KPIs)

ESG related KPIs which can be adopted by PMF are as follows;

- ✓ % of energy in kwh from renewable energy sources as of total energy consumed
- ✓ % of energy saved due to implemented improvements
- ✓ % of waste recycled
- ✓ Water use intensity (total water usage divided by the building sq. ft.)
- ✓ % of credit loans undergone ESG screening
- ✓ % of female employees as of total
- ✓ % of female members in the management as of total
- ✓ % of female board members as of total
- ✓ Average training hours per employee
- ✓ Employee turnover %
- ✓ Employee’s health and safety incidents p.a.
- ✓ Average expenses on training per employee p.a.
- ✓ % of workforce to retire in next 5 years
- ✓ Number of man-days lost per employee p.a

11.0 ESG Risk Management

Managing ESG risks are just as important as opportunities in the pursuit of sustainable growth and transitioning towards a more ESG friendly environment. ESG risks can be broadly defined as any negative financial and non-financial impacts to PMF stemming from the current or progressive impacts of Environmental, Social and Governance factors on PMF's internal business activities.

ESG risks can emerge from the customers' activities, inherent from sector-specific activities and externally from the stakeholders they interact with (e.g. customers, regulators, shareholders, etc.). These risks are not bound by timelines and can occur within the short, medium, and long-term.

11.1 ESG risk identification

11.1.1 Environmental risk

Environmental risks refer to any negative impact to IMFL’s premises, reputation and credit exposures to counterparties that may potentially contribute to or be affected by climate change and other forms of environmental degradation (such as air pollution, water pollution, biodiversity loss and deforestation).

Financial impact on PMF’s portfolio and activities from climate change can materialized through;

- ✓ Physical risks result from climate change and environmental factors that are event driven or longer-term shifts. For example: risk of default and/or financial loss by the exposure to counterparty due to physical risks (eg: earthquake, flood) that may damage counterparty's production facilities and disrupt value chains.

- ✓ Transition risks can arise from the shift to a low-carbon economy. For example: risk of financial loss by the exposure to counterparty that may be negatively affected by the shifts in market sentiment, customer demand and technological advances, and tightening regulations that would lead to rating downgrades and increasing fines.

11.1.2 Social Risk

Social risks refer to any negative impact to PMF's business activities and reputation as a company and its financing to counterparties due to social factors, such as violation of human rights, unfair labour practices, unsafe working conditions and mishandling of customer privacy. For example: the risk of default and/or financial loss by the exposure to counterparties who are exposed to potential fines and reputational damage due to fatalities and incidents in the workplace.

11.1.3 Governance Risk

Governance risks refer to any negative impact to PMF's business activities and reputation as a company, its financing to counterparties and sourcing of vendors due to weak governance structure and failures in business ethics. For example: the risk of default and/or financial loss by the exposure to counterparties who are affected by the disruptions in business, reputational damage, and regulatory fines due to acts of negligence.

PMF should be committed to identifying, evaluating and managing ESG risks in lending, investments, and vendor management processes. On top of the standard Know-Your-Customer and Customer Due Diligence process, PMF should identify sectors and activities of heightened sensitivity to ESG risks which could negatively impact PMF based on prior experience of engagement with the customer and external third party ESG risk assessment from credible sources. Based on this, the appetite of PMF towards different sectors should be defined.

PMF should identify sectors particularly susceptible to ESG risks based on external sources, along with additional inputs from internal portfolio analysis and monitors significant changes in sector performance on a periodic basis.

11.2 ESG risk assessment and measurement

11.2.1 Materiality assessment

Materiality assessment (an exercise conducted to gather insight on exposure and materiality of different ESG risks for PMF)should be carried out which supports to proactively manage the identified risks. This exercise will be helpful in identifying the critical ESG risks and understanding which issues are most material or relevant to business and stakeholders.

Principles of materiality as described in Global Reporting Initiatives (GRI) standards and recommendations of Task Force on Climate related Financial Disclosures (TCFD) and Sustainability Accounting Standards Board (SASB), can be used for this purpose.

The materiality assessment will be done annually based on two dimensions; probability and the impact.

The outcome from the Materiality Assessment will be presented to IRMC for review.

ESG risk assessment should include quantitative and qualitative assessments, which collectively, provide a combined ESG risk rating outcome for counterparties. This assessment is completed at the onboarding phase of new clients and periodic credit review.

ESG risk rating will categorize counterparties in three ESG risk categories:

- ***Low risk:*** No further action, approving the counterparty's relationship and transaction

- ***Medium risk:*** Conditionally approved, with more in-depth due diligence and reasoning, encouraging the client to improve its ESG risk profile with agreed-upon mitigation action plan, performance-enhancing measures, conditions or other requirements attached to the onboarding or transaction.

- ***High risk:*** No engagement and exit from the client relationship, unless overridden by relevant committee.

11.2.2 ESG risk assessment of counterparties during life cycle

11.2.2.1 The ESG risk assessment related to due diligence for onboarding new clients, shall be conducted by the front-line staff by referring to exclusion list and publicly available information, etc. with adequate evidence of proof.

11.2.2.2 During the periodic credit reviews, ESG risk assessment should be carried out for the sectors with high ESG risk exposure.

11.2.2.3 The ad-hoc event driven reviews enable PMF to identify customers with potential/ emerging deterioration in its ESG risk profile, pro-actively monitor its portfolio and coordinate with the customer to remediate potential ESG risk concerns.

11.2.2.4 Front line units as their role under the 1st line of defense will identify new ESG risk incidents for the customer through regular dialogue with customer and/or third party information, and perform ESG risk assessment to update the ESG risk rating

11.2.2.5 The event-driven alerts are categorized as:

- ✓ ***Green alert:*** No further action, if there are unsubstantial changes in external ESG rating.
- ✓ ***Amber alert:*** The client will be classified under watch list and monitor closely, if the external ESG rating changes from low risk to medium risk category and potential changes in existing ESG related regulations and/or emerging new ESG regulations that will have a direct impact to client's business activities are expected.
- ✓ ***Red alert:*** Credit team, as appropriate, will raise a flag to front line units for an update on ESG risk assessment, if ESG rating changes to high risk level and ESG related risk incidents materialize for the customer.

11.2.3 ESG risk assessment for investments

The ESG risk assessment for investments will rely on data provided by external ESG risk rating agencies or any other reliable source due to the limited direct relationship with investees compared to other counterparties.

11.2.4 ESG risk assessment for vendor management

ESG risk assessment for vendors of critical activities/ services should be performed by the relevant officer (who recommends the vendor), when onboarding new vendors.

11.3 ESG risk mitigation

PMF should adopts following measures and controls as part of risk mitigation for the identified ESG risks:

- ✓ Monitoring vulnerable sectors and customers
- ✓ Offering of sustainable finance products that have positive environmental and climate benefits
- ✓ Whenever possible, engaging with medium and high ESG risk counterparties with mitigation plans to assist in reducing customer's exposures to ESG risks and transition towards sustainable business practice

Front line units, based on discussions with the customer, will recommend risk mitigation action plans (whenever possible) to improve customer's ESG risk profile when engaging with moderate or high ESG risk counterparties, but can be contained with a risk mitigating action plan. This should be adequately documented as part of process documentation and reviewed by the compliance team, as appropriate.

The status of the ESG risk mitigation plans must be monitored and communicated to IRMC as appropriate.

12.0 Disclosure and reporting

PMF should disclose the following information related to sustainable finance activities in their annual reports.

i. An overview on sustainable finance policies and activities of the company

ii. Identified ESG and sustainable finance related risks and associated mitigation measures

iii. The environmental and social impact of current and proposed investments and business activities

iv. The progress made on sustainable finance related activities including implementation of the roadmap and the action plan for the next year

v. The total annual amounts of sustainable funds raised for and funds allocated to sustainable finance related activities.

13.0 Review of the policy

This policy should be reviewed and updated once in every two years or whenever there are regulatory changes therein. Any amendments to this policy have to be reviewed by the Nomination and Governance Committee and approved by the Board of Directors.