GROUP ESG RISK POLICY

January 2, 2023

بنك أبوظبي الأول
FAB
First Abu Dhabi Bank

GROUP ESG RISK POLICY			
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Table of Contents

1 Introduction 5
1.1 Purpose 5
1.2 Objectives 5
1.3 Scope 5
1.4 Control and Maintenance of the Policy 7
1.5 Abbreviation 8
1.6 Structure of the Policy 8
2 ESG risk identification 9
2.1 Relevant laws, regulations, and external standards 9
2.2 Definition of ESG Risk and Transmission Channels 9
2.2.1 Environmental risks 9
2.2.2 Social risks 9
2.2.3 Governance risks 10
2.3 Risk Appetite Statement 10
2.3.1 Quantitative Risk Appetite Metrics 10
2.4 Qualitative Risk Appetite Criteria 10
2.4.1 Negative and exclusionary screening list 11
2.4.2 ESG critical activities 11
2.4.3 High ESG risk areas 12
2.4.4 ESG deals eligible for sustainable financing 12
2.4.5 Net zero considerations within portfolios 12
3 ESG Risk Assessment and Measurement 13
3.1 Materiality assessment of ESG risks 13
3.2 ESG Risk Assessment at Counterparty, Transaction and Vendor Level 13
3.2.1 ESG risk assessment tool 13
3.2.2 ESG risk assessment of counterparties during life cycle (IB and CCIB) 14
3.2.3 ESG risk assessment for investments 15
3.2.4 ESG risk assessment for vendor management 16
3.3 Climate stress testing and scenario analysis 16
4 ESG Risk Mitigation 18
5 ESG Risk Reporting and Monitoring 19

Annual disclosures in line with international standards 19

6 Annexures 20

6.1 Annexure I: Illustrative list of key risk metrics and performance indicators 20

6.2 Annexure II: UN GC Principles, ESG critical activities and high ESG risk sectors 20

6.3 Annexure III: Materiality Assessment 21

6.4 Annexure IV: ESG rating model 21

6.5 Annexure V: IB and CCIB clients in scope for the ESG risk assessment 21

6.6 Annexure VI: Equator Principles Framework 21

<table>
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1 Introduction

Environmental, Social, and Governance (ESG) related issues as well as the impacts they create, the opportunities they provide and risks that they generate are becoming more and more relevant for financial institutions. FAB Group recognizes the importance of incorporating ESG risks as part of the Enterprise Risk Management framework.

Managing ESG risks are just as important as opportunities in the pursuit of sustainable growth and transitioning towards a more ESG friendly environment.

FAB Group's ESG Risk Policy (ESGRP) is designed to integrate ESG risks within the Enterprise Risk Management framework while being fully aligned with the Group's ESG targets and the strategic business objectives of the Group.

1.1 Purpose

The purpose of ESGRP is to establish principles and guidelines for identifying, assessing, managing, monitoring, mitigating, and reporting ESG risks, throughout the FAB Group.

1.2 Objectives

The core objective of the ESGRP is to provide assurance to the Board of Directors, investors, regulators, and other stakeholders that ESG risks threatening the Group's business activities, achievement of its core values and purpose are addressed within an effective integrated risk management framework.

The ESGRP also defines the broad principles for the identification, assessment, and measurement, monitoring and reporting of ESG risks for all business units across the Group. It will act as a guide for embedding strong ESG risk awareness culture within the Group.

The more specific objectives for the ESGRP include:

- Establishing a reference guideline for identifying and assessing ESG risks across the Group
- Defining key ESG risk metrics and performance indicators for monitoring and reporting
- Developing ESG risk assessment tools and defining processes for onboarding of new clients, transactions, and vendors

The following objectives are covered by the ESG Risk framework description:

- Setting an effective ESG risk governance structure and oversight with clear responsibilities across the Three Lines of Defence (addendum to framework)
- Encouraging an ESG risk culture within the Group through building ESG risks awareness and understanding at all levels

1.3 Scope

ESG risks for FAB Group ("Group") arise from its internal business activities as a Company, from its counterparties and from its vendors. Therefore, it impacts a wide range of activities within the Group. There are other policies within the Group that currently address different aspects of ESG risks.

This document serves as the umbrella policy for all ESG risk related topics. However, it does not explicitly address the ESG risks arising from the Group's internal activities as a Company. ESG risks arising from the Group's internal business activities as a Company are covered as part of the following:

- Group ESG Policy
- Group Environmental Policy
- FAB Employee Code of Conduct
- FAB Directors Code of Conduct

The ESGRP lays out the principles of ESG risk management and addresses, primarily, the indirect risks and impacts emanating from counterparties and vendors.

Group policies and documents will be cross-referenced in the ESGRP wherever applicable.

The scope of the ESGRP will be covered in the following four phases:

Phase	Phase 1	Phase 2	Phase 3	Phase 4
Timeline	2022	2022-23	To be decided	To be decided
Scope coverage across business products and operations	• Selected clients from Investment Banking (IB)[1] • Group's own investments[2] in bonds and equity • Group's internal supply chain[3] management with specific focus on vendors	• Private banking • All Group Investment Banking (except FI/NBFI) and Corporate and Commercial Banking[4] Clients	• Consumer Banking • All Group Investment Banking and Corporate and Commercial Banking clients, with either one or more of the following products: ○ Supply chain finance	• Commit to other relevant business activities with material ESG risks (based on the annual ESG risks materiality assessment results and decision by Group ESG Committee)

Note: Products and operations covered under each phase will continue to be in the scope of the subsequent phases. Above implementation plan is tentative and subject.

The ESGRP is applicable to all FAB Group entities (Head Office, domestic and international branches, and subsidiaries) across all countries of operations. Involved stakeholders are expected to know the framework and policy instruction and act accordingly.

[1] *Phase 1 and 2 excludes Financial Institutions (FI/NBFI/CB & Supra). The geographic scope of the clients included in phase 1 will be limited to the UAE, USA, UK, France, Switzerland, Singapore, Hong Kong, Egypt, India, and China..*

[2] *Significant investments, within Global Markets, in bonds and listed equity will be assessed through external ESG ratings. Private equity and securities, including advisory services and supply in Private Banking Group and FAB Securities, are planned for later stages of the ESG roadmap.*

[3] *During Phase 1 of the ESGRP implementation, the Strategic Vendor Management team will conduct ESG risk assessment for the top 100 companies with the highest PO values based on the last two years transactions.*

[4] *The CCIB geographic scope will be limited to the UAE in phase 2.*

In accordance with relevant local guidelines and requirements, the international entities will define specific addenda to address local regulatory and compliance requirements that are not covered by the ESGRP.

1.4 Control and Maintenance of the Policy

This Policy will be approved and issued by the Board Risk & ESG Committee under the authority delegated to it by the Board of Directors (BoD) of the Group.

The ESGRP is intended to be an evolving document as new guidelines and regulations are introduced across different jurisdictions. As the area of ESG risks management evolves and in line with the evolution of Group activities, it is anticipated that the existing policy may require amendments and/or inclusions.

The ESGRP will be reviewed once every year or more frequently (if required), to ensure it is relevant. All amendments, additions or deletions to the Policy will be subject to version control and approvals prior to implementation.

The approved revisions will be provided in both hard copy form and the electronic version (with access restricted to relevant stakeholders). All stakeholders will be immediately informed through an internal memorandum which may also be communicated via email.

The VP & Head of ESG Risk Framework and Assessment (HoESGRFA) shall hold the master register of amendments and records of the approved amendments. A Version Register will be maintained by HoESGRFA that shows the Policy version information relating to the version number, version date, and section amended (as per Document Control Table at the beginning of this document).

1.5 Abbreviation

Abbreviation	Description
BoD	Board of Directors
BRESGC	Board Risk and ESG Committee
CEC	Credit Execution Committee
EP	Equator Principles
ERM	Enterprise Risk Management
ESG	Environmental, Social and Governance
ESGRP	ESG Risk Policy
ESG-SFC	ESG Risk and Sustainable Finance Committee
G-ESGC	Group ESG Committee
GOFRC	Group Operational and Fraud Risk Committee
GCC	Group Compliance Committee
GRC	Group Risk Committee
UNEP FI	United Nations Environment Programme Finance Initiative
NGFS	Network for Greening the Financial System
SFF	Sustainable Finance Framework
TCFD	Task Force on Climate related Financial Disclosures
UNGC	United Nations Global Compact

1.6 Structure of the Policy

The framework description has been divided into the following areas:

- Section 1 – Introduction
- Section 2 – ESG risk identification
- Section 3 – ESG risk assessment and measurement
- Section 4 – ESG risk mitigation
- Section 5 – ESG risk reporting and monitoring
- Support 6 – Annexures

2 ESG risk identification

2.1 Relevant laws, regulations, and external standards

Central banks and policymakers where FAB Group operates are becoming interested in understanding how the banking sector is effectively managing and monitoring ESG related risks within their operations, particularly in response to climate change challenges, socio-economic topics, and governance transparency.

When setting this policy, the Group has considered relevant legislations and guidelines, which are updated from time to time.

2.2 Definition of ESG Risk and Transmission Channels

ESG risks are manifested within the principal risks that are defined under the Key Risk Taxonomy of Enterprise Risk Management Policy and broadly defined as any negative financial and non-financial impacts to the Group stemming from the current or progressive impacts of Environmental, Social and Governance factors on the Group's internal business activities as a company, its counterparties and vendor management.

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

The ESGRP instructions along with risk appetite metrics and risk assessment tools primarily aim to identify, assess, and manage the indirect ESG risks emanating from counterparties and vendors.

2.2.1 Environmental risks

Environmental risks refer to any negative impact to the Group'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, scarcity of freshwater, land contamination, biodiversity loss and deforestation).

2.2.2 Social risks

Social risks refer to any negative impact to the Group's business activities and reputation as a company, its financing to counterparties and sourcing of vendors 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.

2.2.3 Governance risks

Governance risks refer to any negative impact to a Group'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 from the Board.

The ESG risks crosscut the principal risk categories and can materialize from both direct (through operation of the Group's own premises, infrastructure and organizational culture) and indirect (the financial services and support that the Group provides to its customers who may be exposed to ESG risks) channels.

2.3 Risk Appetite Statement

The Group's ESG risk appetite is aligned with the enterprise wide risk appetite framework. The risk appetite has been defined using a set of quantitative metrics (i.e. key risk metrics and performance indicators) and qualitative criteria. The risk appetite statement will be reviewed and approved by the Board on an annual basis and monitored on a quarterly basis.

2.3.1 Quantitative Risk Appetite Metrics

Quantitative risk appetite metrics comprise the following:

- **Key ESG Risk Indicators**: These risk appetite metrics establish the Group's risk tolerance to indirect ESG risk emanating from exposures to counterparties and vendors from high-risk sectors, geographies and third party/ internal ESG risk ratings and cascaded down by products and business functions.
- **Key ESG Performance Indicators**: These risk appetite metrics establish the Group's risk tolerance to Direct ESG risk. The key performance indicators are established to monitor among other things the performance of the Group's own emissions, social responsibility, and governance structure.

The risk metrics and performance metrics used are deemed to be appropriate for the current risk profile of the Group and will be updated on an annual basis.

Note: Please refer to Annexure I for key risk metrics and performance indicators (also see Group ESG Policy and Framework).

2.4 Qualitative Risk Appetite Criteria

FAB Group is committed to identifying, evaluating and managing ESG risks in lending, investment, funding and vendor management processes. On top of the standard Know-Your-Customer and Group Customer Due Diligence process, the Group will identify countries, sectors and activities of heightened sensitivity to ESG risks which could negatively impact the Group 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 the Group towards negative screening list, ESG critical activities and high ESG risk areas are defined below:

2.4.1 Negative and exclusionary screening list

The Group will not knowingly engage with companies or customers including:

1. Unsuccessful resolution of ESG issues on previous engagements with customer
2. Violators of UN Global Compact principles[5]
3. Violates of national or international legislation[6]
4. Potential negative impact on critical natural habitats and areas protected including e.g. UNESCO World Heritage Sites
5. Illegally infringe ownership of land or resources without Free, Prior and Informed Consent (FPIC)
6. Obligors on the Office of Foreign Assets Control (OFAC) blacklist
7. Classified as severe risk under the ESG risk assessment tool and approved by the relevant committees.
8. Financing[7] (including trade financing) of thermal coal (power and mining), and tobacco and alcohol manufacturers[8].

Note: Please refer to Annexure II for the UN GC Principles.

2.4.2 ESG critical activities

In addition, the Group will not knowingly engage in the activities from the "ESG Critical Activities", while not illegal, are not aligned with Group's values, principles and code of conduct if the revenue threshold is not met.

The Group can engage with customer under one of the following conditions as long as the purpose of the transaction and new engagement is in accordance with the Group's vision and principles in order to help the customer to rely increasingly more on ESG friendly business areas:

1. Critical activities make up less than 25% of the total revenue *(With the only exception for thermal coal, which will make up less than 10% of the total revenue),*
2. Risk mitigation actions in place[9].

If a transaction is under the Group's Sustainable Finance Framework, other requirements are in place such as restrictions on the use of proceeds from sustainable finance transactions.

Note: Please refer to Annexure II for the ESG critical activities.

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[5] *No alleged very high-risk breaches of the UN GC principles over the last two years as per the vendor's ESG rating.*
[6] *No alleged very high-risk violation of legislations over the last two years as per the vendor's ESG rating.*
[7] *Other key considerations include respecting current standing commitments to clients, annual renewals, until facility end date and engaging with existing customers to understand their current transition plans and explore transition finance.*
[8] *Tobacco and alcohol wholesale and retail distributor clients will be considered as an ESG critical activity.*
[9] *Will require an action plan attached to the transaction, see section 4.*

2.4.3 High ESG risk areas

The Group recognizes that certain sectors and activities are more likely to be exposed to higher ESG risks. The Group will actively engage with current and prospective clients even if the client is classified as high and severe risk as part of ESG risk assessment process. The ESG Risk/Credit team, as appropriate, will conduct enhanced due diligence assessment, reviewing the client's exposures to high ESG risk activities and reviewing risk mitigation actions in accordance with section 4.

The Group identifies 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. Note: Please refer to Annexure II for high ESG risk sectors and high and very high ESG risk countries.

2.4.4 ESG deals eligible for sustainable financing

ESG deals are assessed for ESG risks and eligibility criteria in alignment with the Sustainable Finance Framework (SFF), as described in section 3.2.2. This includes a due diligence assessment for ESG risks at an obligor(s) and project level, if applicable, using the Equator Principles (EP) framework, which is a risk management framework adopted by financial institutions for determining, assessing and managing environmental and social risks in project finance. The Group is a signatory of the Equator Principles.

Once assessed as acceptable, deals undergo an additional assessment to check eligibility for sustainable financing. Any transaction that does not meet the minimum requirements set out in the SFF are disqualified.

Sustainability linked instruments will be reviewed and assessed for material and ambitious Key Performance Indicators (KPIs) and Sustainability Performance Targets (SPTs). The Group will validate the sustainability linked products issued under the SFF's classification through our due diligence processes, taking into consideratoin the clients material ESG issues and market standards.

2.4.5 Net zero considerations within portfolios

The Group has signed up to the Net Zero Banking Alliance (NZBA), which is an important step towards aligning the Group's lending portfolios with net-zero emission targets by 2050. Three high emitting sectors, namely Oil and Gas, Aviation and Power, were selected and prioritized for setting baseline measures and interim net zero targets for 2030.

For these sectors, additional monitoring measures will be needed to assess our exposure. All new credit facilities with *'Oil and Gas, Aviation and Power'* will be shared with the ESG risk team to have an overview on FAB's net zero performance.

3 ESG Risk Assessment and Measurement

3.1 Materiality assessment of ESG risks

Materiality assessment is an exercise conducted to gather insight on exposure and materiality of different ESG risks for the Group and to proactively manage the identified risks. This exercise helps in identifying the critical ESG risks and understanding which issues are most material or relevant to business and stakeholders. It is aligned with the 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).

Group ESG will hold workshops and meetings with key stakeholders within the Group to conduct the materiality assessment. The materiality assessment will be done biannually or more, based on a need for basis, to assess potential ESG risks likelihood from occurring and severity of impact on business.

Note: Please refer to Annexure III for illustrative Materiality Assessment.

The outcome from the Materiality Assessment will be presented to the Group ESG Committee for review and approval.

3.2 ESG Risk Assessment at Counterparty, Transaction and Vendor Level

The Group is committed to identifying, evaluating and managing ESG risks in lending, investment and vendor management processes. As outlined in Group ESG Policy and Group Environmental Policy, the Group seeks to identify and manage any strategic or reputational risks arising from environmental and social impacts associated with Group's lending and commercial activities.

ESG risk assessment at counterparty and transaction level begins with front line units through negative and exclusionary screening, then and determining the ESG risk rating of the customers through ESG due diligence at the credit life cycle and vendor management process.

Trade Finance deals and clients will be assessed through an external ESG rating agency specialised in supply chain transactions. A pilot phase is initiated for Supply Chain Finance (SCF) clients.

When more clients and products are being taken into scope, the processes described below will be adjusted accordingly.

3.2.1 ESG risk assessment tool

ESG risk assessment tool includes 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, vendors and periodic credit review.

Quantitative assessments rely on a counterparty's ESG risk ratings provided by credible external ESG rating agencies. Meanwhile, the qualitative assessment is an internally developed ESG questionnaire that assesses the counterparty's current ESG policies, commitments and practices in effectively managing ESG risks.

The combined ESG risk rating from quantitative and qualitative assessments will categorize counterparties in three ESG risk categories:

1. Acceptable risk: No further action, approving the counterparty's relationship and transaction, if transactions comply with requirements in section 2.4. The ESG Risk team will undertake a sample check of acceptable risk clients to confirm the combined ESG risk rating and check for those with conflicting external and internal ratings.
2. High risk: Conditionally approved, with well founded motivation (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 or addition of loan covenants, conditions or other requirements attached to the onboarding or transaction.
3. Severe risk: No engagement and exit from the client or vendor relationship, unless overridden by relevant committee.

Note: Please refer to Annexure IV for the ESG rating model.

3.2.2 ESG risk assessment of counterparties during life cycle (IB and CCIB)

Onboarding of new clients

The due diligence for onboarding new clients (including non-borrowing and borrowing clients) is conducted at a parent company level if applicable[10]. The front line units will conduct an ESG risk assessment for the clients in scope as included in Annexure 7.5, covering negative screening, external ESG rating and internal questionnaire with adequate evidence of proof.

New transactions

1. New plain vanilla credit facilities will be assessed against:
    a. The negative screening exclusions and ESG critical activities, outlined in section 2.4
    b. If project financing is included, then the front liner will conduct screening to decide if the Equator Principles[11] will apply. If applicable, then project categorization and relevant assessments will be needed as per the EP requirements described in annexure VI.
    c. If it is a sector that falls within the net zero scope, outlined in section 2.4
2. New ESG deals with credit facilities eligible for sustainable financing, as per the Group's Sustainable Finance Framework (SFF) requirements, will be assessed against:
    a. All assessments mentioned for the new plain vanilla credit facilities
    b. Any additional exclusionary considerations mentioned in the SFF

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[10] *If the counterparty is a subsidiary and belongs to the same sector as the parent company, then an ESG risk assessment will not be performed at the counterparty level. The same ESG risk score of the parent company will apply (if available). If no parent company exists, then complete the ESG risk assessment at the individual counterparty level.*

[11] *The Equator Principles apply to FAB's project financing products (e.g. project finance advisory services, project finance, project related corporate loans, bridge loans, etc.) if they meet certain thresholds and conditions included in the detailed EP guidelines.*

c. An ESG risk assessment completed for the obligor(s), outlined in section 3.2.1 regardless of their inclusion in scope in Annexure 7.5
d. Fullfillment of the eligibility criteria and thresholds included in the SFF

The front line units will complete these assessments with adequate evidence of proof.

ESG risk assessment aligned with periodic credit reviews and/or periodic customer reviews:

When performing periodic credit reviews for clients with credit exposures, front line units will conduct an ESG risk assessment for clients during periodic credit reviews for the clients in scope as included in Annexure 7.5. Ad-hoc events in between credit renewals can trigger an ESG risk re-assessment in cases where potential adverse effects and lower ESG ratings were identified for the client.

ESG risk assessment for ad-hoc event driven reviews:

The ad-hoc event driven reviews enables the Group to identify customers with potential/ emerging deterioration in its ESG risk profile, pro-actively monitor its portfolio and discreetly approach the customer to help remediate potential ESG risk concerns.

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.

The ESG Risk team will perform periodic monitoring for any adverse changes in external ESG ratings for the customer to identify customers with potential ESG issues and to take appropriate and timely corrective action plans. The event-driven alerts are categorized as:

1. Green alert: No further action, if there are unsubstantial changes in external ESG rating.
2. Amber alert: The ESG Risk team will classify the client under watch list and monitor closely, if the external ESG rating changes from acceptable risk to high 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.
3. Red alert: The ESG Risk/Credit team, as appropriate, will raise a flag to front line units for an update on ESG risk assessment, if the external ESG rating changes to severe risk level and ESG related risk incidents materialize for the customer.

3.2.3 ESG risk assessment for investments

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

The ESG risk score for investees will be based on an average score sourced from a number of ESG rating agencies and categrosied into acceptable, high and severe. The investees' combined ESG risk score will be added to a watchlist for monitoring purposes with a special focus on high and severe rated securites and refreshed every 6 months to the relevant ESG committees.

3.2.4 ESG risk assessment for vendor management

ESG risk assessment for vendors of critical activities/ services will be performed by the Strategic Vendor Management (SVM) team when onboarding new vendors. All existing vendors will go through a rapid ESG risk assessment before onboarding through an external ESG risk rating vendor (if the external ESG risk score is high, above 50, then an ESG risk assessment will be needed on the spot). If the external ESG risk score is less than 50, then the vendor will be onboarded.

Once a new purchase order (PO) is set, a detailed ESG risk assessment would be needed for vendors with professional services, IT and Facilities categories with a PO value above 1 million AED.

Note: Please refer to Annexure VII for process illustrations.

3.3 Climate stress testing and scenario analysis

The Group has taken a robust scenario driven and factor push approach for stress testing exercise, combining quantitative and qualitative methodologies to estimate forward-looking ECL impacts adjusted with stakeholder expectation on managing the ESG risk. The purpose for the stress testing tool is to understand the potential impacts on selected portfolios, enhance the methodology, and meet TCFD reporting and supervisor and central bank requirements going forward.

Due to modelling challenges with respect to relatively longer time horizons, limited historical observations and data availability, the climate stress testing and scenario analysis however remains work in progress.

Following are the quantification steps to be followed to conduct stress testing exercise:

Step 1: Design and update scenario library

Scenario library is a living document containing potential external and internal ESG scenarios and their priority level, covering both the climate-risk related scenarios and emerging risk scenarios for social and governance factors. The scenarios will be shortlisted based on the alignment with regulatory recommended scenarios, priority level and the availability of longer horizon estimates for macroeconomic variables to stress the parameters of Expected Credit Loss (ECL) modelling.

Note: Please refer to Annexure VIII for examples of stress scenarios.

Step 2: Quantitative assessment

The modelling of ESG related (including physical and transition risks for climate change) risks is in its infancy. For a start, the Group has taken a simple approach based on external research (NGFS, UNEP FI) and utilization of internal capabilities to estimate the financial impacts of climate change limited to high environmental risk sectors (such as energy, power utilities, mining, transportation, manufacturing, buildings and construction):

1. Identify the key risk drivers of the shortlisted climate change related scenarios on a combination of scenario (GDP forecasts for 30 years horizon available from NGFS) and factor push approach (sector and regional level financial impact on balance sheet or total revenue)
2. Link the key drivers to the transmission functions:
    - Obligor Risk Rating (ORR): Downgrade the credit rating of counterparties who operate in ESG vulnerable sectors by certain notches down and/or historical performance between ORR and EBITDA
    - IFRS 9 ECL model: Revise the baseline GDP forecast for macroeconomic variables used in IFRS 9 modelling
3. Revise the Through-The-Cycle (TTC) PD and consequent Point-In-Time (PIT) PD curves
4. Estimate the net ECL impact under the revised PD curves

Step 3: Qualitative assessment scorecard

The qualitative assessment scorecard is used to understand the management views of actions taken on managing ESG risks and to fine-tune the outcomes of the quantitative assessment (mentioned in step 2) based on the Group's current risk management practices with respect to ESG risks and plans for improvement.

The set of parameters are assessed under qualitative assessment and have been classified as "Control" or "Risk" parameters on a rating scale of 1 to 10 with 1 being Strongly agree and 10 being Strongly disagree.

1. Collect response on the set of parameters from senior management
2. Derive an average score for each parameter
3. Calculate overall weighted average score for ESG risk
4. Derive a mapping table in line with the rating scale to adjust the outcomes of the estimated credit loss due to ESG risks under the stress scenarios
5. Determine the bucket in accordance with overall average weighted score and apply the adjustment factor for the respective bucket to identify the final net financial impact under ESG stress scenarios

While the stress testing exercise will follow ICAAP process and timelines, the estimated impact on ECL and consequent capital shortfall will however not be included in the Pillar II capital charge due to the early stage of stress testing methodology and inclusion of qualitative assessment.

The effort is work in progress, and will evolve over the years as data, taxonomy, assumptions, resources, and insights improve.

4 ESG Risk Mitigation

In line with risk mitigation principles outlined in Enterprise Risk Management policy, the Group adopts following measures and controls as part of risk mitigation for the identified ESG risks:

1. Monitoring vulnerable sectors, geographies and customers, and identifying negative screening and ESG critical activities list as part of ESG risk appetite framework
2. Offering of sustainable finance products, such as Green Bonds, to finance projects that have positive environmental and climate benefits
9. Engaging with high and severe 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 to improve customer's ESG risk profile when engaging with high ESG risk counterparties or if the activity is ESG critical, but can be contained with a risk mitigating action plan. This will be adequately documented as part of process documentation and reviewed by the ESG Risk/Credit team, as appropriate.

ESG Risk/Credit team, as appropriate, will review the recommended mitigation actions plans with respect to following principles:

1. Objective: A well-defined set of actions that will improve customer's ESG profile and ensure to stay away further critical activities
2. Direct: To have a direct impact on the customer's business activities and revenue model
3. Measurable: To touch a material portion of the total revenue, so that the revenue share of non-critical activities reaching revenue threshold of 75%
4. Commitment: Backed by buy-in from senior management to committing objectives
5. Timely: A clear timeline with a target date.

The status of the ESG risk mitigation plans must be monitored and communicated to ESG-SFC for corrective actions to be taken.

5 ESG Risk Reporting and Monitoring

Annual disclosures in line with international standards

The Group strives to disclose all relevant sustainability and ESG related information to external stakeholders via Group's annual reporting on its webpage. Going forward, more granular data and information will be provided in the external reports aligned with national and international guidelines.

6 Annexures

6.1 Annexure I: Illustrative list of key risk metrics and performance indicators

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6.2 Annexure II: UN GC Principles, ESG critical activities and high ESG risk sectors

Table 7. 1: United Nation Global Compact principles

Category	Principles	Definition
Human Rights	Principle 1	Businesses should support and respect the protection of internationally proclaimed human rights
	Principle 2	Make sure that they are not complicit in human rights abuses
Labour	Principle 3	Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining
	Principle 4	The elimination of all forms of forced and compulsory labor
	Principle 5	The effective abolition of child labor
	Principle 6	The elimination of discrimination in respect of employment and occupation
Environment	Principle 7	Businesses should support a precautionary approach to environmental challenges
	Principle 8	Undertake initiatives to promote greater environmental responsibility
	Principle 9	Encourage the development and diffusion of environmentally friendly technologies
Anti-corruption	Principle 10	Businesses should work against corruption in all its forms, including extortion and bribery.

Table 7. 2: ESG Critical activities

Activities:
All restricted activities under the Corporate & Investment Banking Group Credit Policy (CIB GCP)
All excluded activities under Group Customer Due Diligence procedure
Tar sand extraction
Fracking
Ultra-deep-sea drilling
Wholesale and retail distributors with tobacco and or alcohol sales
Arctic drilling
Thermal coal
Palm oil, soy, and timber
Landfill without gas capture
Waste incineration without energy capture
Animal mistreatment
Adult entertainment
Hazardous substances
Speculative transactions
Predatory lending

Hostile takeovers

Table 7. 3: ESG risk sectors classification by FAB

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Table 7. 4: ESG risk countries

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6.3 Annexure III: Materiality Assessment

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6.4 Annexure IV: ESG rating model

Table 7. 5: ESG risk rating structure

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6.5 Annexure V: IB and CCIB clients in scope for the ESG risk assessment

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6.6 Annexure VI: Equator Principles Framework

The Equator Principles (EP) framework is a risk management framework, adopted by financial institutions, for assessing the evaluation, management, and mitigation of environmental and social risks in project finance and project related loans. It aims to provide a minimum standard of environmental and social due diligence to support responsible risk decision-making.

The Equator Principles are based on the International Finance Corporation (IFC) environmental and social performance standards and the World Bank Group health and safety guidelines.

Scope of Equator Principles and applicability screening:

1. Project Finance Advisory Services where total Project capital costs are US$10 million or more.
2. Project Finance with total Project capital costs of US$10 million or more.
3. Project-Related Corporate Loans where all of the following three criteria are met:
    i. The majority of the loan is related to a Project over which the client has Effective Operational Control (either direct or indirect).
    ii. The total aggregate loan amount and the EPFI's individual commitment (before syndication or sell down) are each at least US$50 million.
    iii. The loan tenor is at least two years.
4. Bridge Loans with a tenor of less than two years that are intended to be refinanced by Project Finance or a Project-Related Corporate Loan that is anticipated to meet the relevant criteria described in 2 and 3 above.
5. Project-Related Refinance and Project-Related Acquisition Finance, where all of the following three criteria are met:
    i. The underlying Project was financed in accordance with the Equator Principles framework.

ii. There has been no material change in the scale or scope of the Project.

iii. Project Completion has not yet occurred at the time of the signing of the facility or loan agreement.

Table 7.8 Steps and roles of an EP-aligned project finance process

EP	Subject	Action
EP1	Review and Categorization	Categorize projects as A, B, or C, based on the magnitude of their potential environmental and social risks and impacts.
EP2	Environmental and Social Assessment	For Category A and B projects, borrower conducts an Environmental and Social Impact Assessment (ESIA). Borrower is expected to include assessments of potential adverse Human Rights impacts and climate change risks as part of the ESIA or other Assessment.
EP3	Applicable Environmental and Social Standards	Projects in non-designated countries: Compliance with the IFC Performance Standards on Environmental and Social Sustainability and the World Bank Group EHS Guidelines. Projects located in designated countries: Compliance with national laws and regulations.
EP4	Environmental and Social Management System and Equator Principles Action Plan	For Category A and B projects, borrower develops and maintains an Environmental and Social Management System (ESMS), Environmental and Social Management Plan (ESMP), and/or Equator Principles Action Plan (AP) to address issues raised in the assessment process and comply with the applicable standards.
EP5	Stakeholder Engagement	For Category A and B Projects, borrower demonstrates an effective stakeholder engagement process conducted in a structured and culturally appropriate manner with affected communities.
EP6	Grievance Mechanism	For all Category A and some Category B projects, borrower establishes a grievance mechanism designed to receive and facilitate resolution of concerns about the project.
EP7	Independent Review	For Category A and some Category B projects, independent consultant carries out a review of the assessment documentation to assess EP compliance.
EP8	Covenants	For Category A and B projects, environmental and social covenants linked to EP compliance are incorporated in the financial documentation.
EP9	Independent Monitoring and Reporting	For Category A and some Category B projects, borrower provides periodic reports, verified by an independent

		consultant, that document its compliance with the EP over the life of the loan.
EP10	Reporting and Transparency	Report publicly, at least annually, on transactions that have reached Financial Close and on EP implementation processes and experience.