INCORPORATION OF ENVIRONMENTAL, SOCIAL AND GOVERNANCE INTO ATLAS INVESTMENT PROCESS

1. INTRODUCTION

ATLAS's approach to the environmental, social and governance aspects of investment is one which aims to understand the implications of each of ESG factor at a company level and to account for these factors within our models through their impacts on company cash flows and through asset stress testing. In summary, our investment process incorporates ESG factors as follows:

- Environmental: We divide environmental influences into two categories: environmental performance and climate change. Environmental performance is monitored through company and regulatory disclosures, and we reflect that performance within the cash flows of our company models. These may include fines or changes to allowed returns. We model the impact of climate change very specifically, as discussed in Section 3.
- Social: ATLAS recognises that infrastructure assets operate under an implicit social contract and that companies which fail to perform in line with that contract (through overcharging, or under delivering) may be subject to penalties or reduced allowed returns. ATLAS's financial models make explicit assumptions about the level of profits that are earned by infrastructure assets and our forecasts assume that companies earn "fair" returns over time, provided that the company provides a service in line with customer and regulator expectations. Whilst historically some companies have earned significant excess returns, we have experienced that these are eroded over time (through regulation or other means) and so our models migrate these returns to more normalised levels over time. In doing so we avoid assumptions that companies can earn excessive profits over extended periods at the expense of their customers and other stakeholders.
- Governance: Governance is considered on multiple levels. In evaluating the impact of the company's management and oversight we make specific assumptions around management's ability to generate (or undermine) the company's value over time. A key element is the capability and incentivisation of management to make value accretive (or value destructive) investment decisions, both within the existing business and in the context of a company's strategic aspirations. This also incorporates assessment of capital structure decisions and subsequent uses of cash.

2. ESG FACTOR INTEGRATION IN INVESTMENT PROCESS

The following table provides further detail of the specific ESG factors that we include in our research and investment processes.

ESG area	Topic	Incorporation in Investment process and analysis	Portfolio construction impact
Environment Climate transition & policy risk	CO2 Intensity	Trajectory of emissions used in company profile report, emissions data included as specific risk field in portfolio construction	The Global Strategy guideline is for lower emissions than the universe which will place a limit on the selection of high emission companies for the portfolio
	Carbon Beta	The carbon beta for each company is calculated in the financial model and stored in the company profile as well as the ATLAS database	The Global Strategy guideline is for lower carbon beta than the universe which will place a limit on the selection of high carbon beta companies for the portfolio
	Scenario modelling	Prior to upload, each scenario (including fast transition and delayed action) is run and the cashflow	The Global Strategy has a guideline of positive exposure to fast transition which will limit the ability to hold assets with

ESG area	Topic	Incorporation in Investment process and analysis	Portfolio construction impact
		outputs stored in the ATLAS database such that scenario returns always appear alongside portfolio returns in portfolio construction	negative exposure to fast transition scenarios
Environment physical risk & resilience	impacts of climate events	Increased costs of climate events will increase capex forecasts which will either directly reduce returns or will impact any excess returns earned through regulatory outcomes	Lower forecast returns will result in companies with high physical risk not being selected compared with similar risk / return assets
Social	Regulatory contract	We make explicit assumptions for regulatory pain / gain sharing which in turn influence the amount of any excess returns retained	Companies with strong regulatory relationships will keep more returns and therefore be more likely to be included than similar risk / return assets.
	Social contract	Long term excess returns need to be justified with social contract in company profile, strong social contract leads to higher returns for longer	Companies with strong social contract have higher equity returns and similar risk / return assets.
	Corporate citizenship & Workforce engagement	Poor corporate citizenship and engagement is reflected in base case returns and in potential stress case results	A company showing a lower return or a greater risk of loss in a stress scenario would be harder to place in the portfolio
Governance	Alignment & Incentives	We incorporate poor alignment and incentives through explicit forecasts for reinvestment and capital discipline which can increase or decrease equity returns	Companies with poor reinvestment will show lower returns and higher risk and will be less likely to form part of a portfolio
	Ownership	ATLAS financial models can forecast changes in ownership including dilution and accretion which impact equity returns	In portfolio construction we would see the direct impact in expected returns and monitor expected equity dilution as a separate risk factor

The inclusion of these factors in our processes is that we do not need to introduce separate ‘qualitative overlays’ in portfolio construction which might conflicting signals with the ‘quantitative’ outputs. The ESG exposures and risk for each asset are reflected in either base case cashflows or scenario / stress case outputs or both and therefore are directly and automatically part of each portfolio decision.

Incorporation of external ESG data providers

We utilise external ESG data providers to complement our internal process. We have identified two areas so far where utilising third party data complements and extends our understanding and analysis in a way which would be hard or inefficient to attempt internally:

- Trucost carbon disclosure – Trucost provide estimates of Scope 1, Scope 2 and some Scope 3 emissions for companies in our universe. This is available in a single comparable dataset and avoids the risk of relying on individual company and country level reporting standards

- Reprisk ESG – Reprisk provide a comprehensive ‘outside in’ view of corporate ESG by monitoring external parties such as NGOs and local language sources that are often not picked up by standard financial news services (which tend to be English centric and focussed on financial updates).

Trucost data is included and monitored as part of our portfolio reporting and risk analysis. Reprisk reports are monitored weekly and changes are flagged for further consideration at ATLAS’s Research Meeting.

ESG incorporation in Investment Committees

We record ESG risks and key issues for each company as part of the research process. A summary of the key ESG issues is also included in all proxy voting recommendations that are considered at Investment Committee. Hence ESG identified risks and issues are brought to the attention of Investment Committee in three ways:

- ESG issues identified through the research process will be raised at research meetings which are attended by the ATLAS IC members and will be incorporated into the investment scenarios and stress cases which form the inputs to the IC decision process
- ESG issues that are central to the investment case will be recorded in company assertions and monitored by the investment team on an ongoing basis with any incidents or potential breaks reported at weekly workflow
- ESG issues and risks are included in proxy voting recommendations to IC (see proxy voting below).

Engagement, proxy voting & assertions

Engagement relating to ESG factors is undertaken as part of research and investment due diligence by the relevant ATLAS sector teams. Deep understanding of and frequent engagement with portfolio company management teams and boards provides one of the best forms of risk management and return optimisation. We believe that it is also possible to create value by working collaboratively with management teams to implement strategies at the asset level which are consistent and aligned with the interests of our clients.

For each company, a summary of current ESG metrics and active issues is stored in the ATLAS research management system (RMS). At each company meeting, investment team members from the relevant sector team (which may often include members of the Investment Committee of ATLAS) will use the latest information from the RMS to ask further questions and identify any changes or developments. Where possible we highlight to company management where underperformance on an ESG issue will be reflected in our cashflow forecasts and therefore will negatively impact our ability to invest in their company. Following every company meeting, notes are recorded in the RMS and any updates to active ESG issues are also recorded ready for the next meeting and follow up.

The Investment Committees of ATLAS have a responsibility to support and provide direction to this engagement in two ways:

- Proxy voting: proxy votes submitted for a portfolio holding are the responsibility of the relevant Investment Committee. The proxy vote recommendations submitted to IC contain a summary of all ESG risks and key issues identified for that company including, where relevant, recommendations for voting on specific issues.
- Company assertions: As part of the IC decision process on a portfolio trade, specific assertions (up to 3) are made for each portfolio investment that detail the key assumptions on which IC has made the decision. These assertions are required to be specific, falsifiable and able to be shared with company management and boards so that all ATLAS investee companies can be made aware of the basis on which we have made our investment and the actions or decisions which would cause us to review our investment.

Engagement Escalation

ATLAS's engagement escalation process is as follows:

All ESG issues are identified through the research due diligence process (including research meetings) outlined above and recorded in the ESG key risks and priority issues for management follow up in our meeting notes.

The notes are stored in our internal research management system. The issues are also reviewed as part of the proxy voting process outlined above.

We have the option to escalate to a formal written communication from ATLAS Infrastructure to the Board of a company in the event that:

- An issue has been raised with management and has not been resolved to our satisfaction; or
- We have voted against a company sponsored shareholder resolution and the resolution has been passed with no subsequent review or amendment; or
- The ESG issue identified relates specifically to a board level governance or strategy decision

These written engagements are proposed by the relevant ATLAS investment partner and reviewed through the ATLAS investment research meeting. Each written engagement is recorded in the ATLAS RMS and any subsequent follow up, including an assessment of the success of the engagement is also recorded prior to close.

3. CLIMATE CHANGE

Whilst ATLAS regards all ESG factors as important to our analysis, we believe that climate change and energy transition are the risks that will have the most fundamental impact on the companies in our investment universe and so are the risks to which we pay most attention and on which we spend the most time modelling.

We believe that it is inevitable that governments will implement material climate policy actions over time and that the combination of these climate policies, together with technological evolution, will lead to material changes in global energy systems. This is likely to have profound implications for infrastructure assets, some of which will be beneficiaries of this change whilst others may see their businesses significantly disrupted.

ATLAS has an integrated approach to measuring the impact of future climate policies within all its financial models. The ATLAS approach evaluates the expected investment return of each company universe under three different climate policy scenarios:

- Base Case: The world implements climate policy at a firm but moderate pace. Energy transition occurs in a meaningful but relatively orderly manner. Certain assets become stranded.
- Fast Transition: Climate policies implemented at an accelerated pace, disrupting several industries and leading to stranded assets in a number of fossil fuel related sectors.
- Delayed Action: Minimal climate policy in the near term. However, physical climate change prompts more severe policies over the longer term which leads to market disruption and stranded assets.

For further details please refer to our *'Climate Change Summary Paper*' and '*Climate Change Risks to Energy Infrastructure Assets*' documents, available upon request.

The table on the following page provides some of the key assumptions embedded within our climate change policy scenarios. The detailed scenario forecasts are available on request.

Element	Base Case	Fast Transition
Mapping to other scenarios	Roughly reflects the IEA 2-degree scenario.	Roughly reflects the IEA 1.5-degree scenario.
Coal fired generation progression	No new coal generation. All coal fired facilities are closed from 2022-28 in Europe and 2025-32 in North America.	No new coal generation. All coal fired facilities are closed from 2020-22 in both Europe and North America.
Gas fired generation progression	No new gas fired generation after 2033 in Europe and from 2040 in North America. Gas fired generators forced shut down from 2060 in Europe and 2070 in North America.	No new gas fired generation after 2022 in Europe and 2025 in North America. Gas fired generators forced shut down in 2040 in Europe and North America.
Renewable penetration	Renewables take on half of all coal shutdowns from current and take on all closed coal generation from 2033.	Renewables take on half of all coal shutdowns from current and take on all closed coal generation from 2025.
EV penetration	50% of all car sales from 2028 in Europe and 2040 in North America. 100% of all car sales from 2038 in Europe and 2045 in North America.	50% of all car sales from 2022 in Europe and 2025 in North America. 100% of all car sales from 2028 in Europe and 2030 in North America.

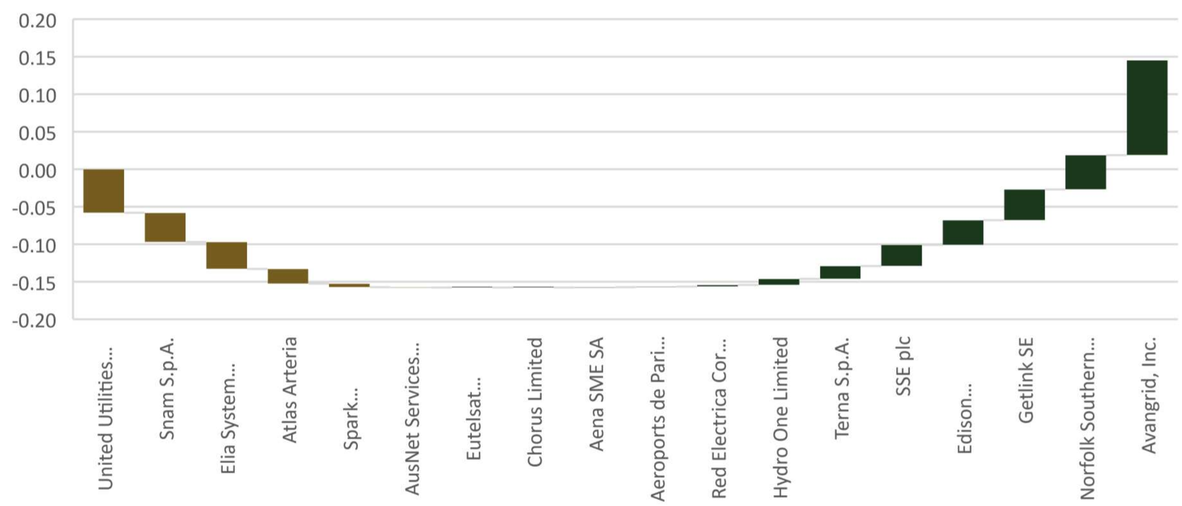
Source: ATLAS Infrastructure forecasts

Climate Change Modelling – Stock and Portfolio Level

As noted above, all ATLAS models include cash flow and IRR forecasts under three climate scenarios. ATLAS then utilises these IRRs in constructing portfolios. Our primary assumption in stock selection is that events will conform to our Base Case, however we also take account of expected IRRs under both Fast Transition and Delayed Action scenarios. ATLAS aims to ensure that at the total portfolio level, the portfolio has the same or a better IRR under a Fast Transition scenario than under its Base Case such that the portfolio is not negatively exposed to such a scenario.

The following chart demonstrates the contribution of each stock in the portfolio to the Fast Transition exposure of the portfolio, relative to the Base Case on a 10 year IRR basis. Whilst the portfolio does contain stocks that may perform less well in a Fast Transition scenario, the portfolio return as a whole would be expected to be c.15bps higher in a Fast Transition climate policy environment than under the Base Case. This differential is driven by its exposure to rail and utilities with renewable energy businesses, which we would expect to benefit from a strong climate policy.

Base Case vs Fast Transition 10-year hold DCF IRR as at 31 December 2019



Source: ATLAS Infrastructure

ATLAS has engaged two well recognised experts in the climate change field in its two main governance and oversight committees to assist in establishing and monitoring key elements of its ESG and climate change process:

- The assumptions underlying the climate change scenarios are reviewed at least every six months in conjunction with the Firm's Macro Advisory Board. Ben Caldecott, the MAB member with particular responsibility for climate change, is the founding Director of the Oxford Sustainable Finance Programme at the University of Oxford Smith School of Enterprise and the Environment. He has been an Academic Visitor at the Bank of England and a Visiting Scholar at Peking University. He is also a Policy Associate at the UK's Department for Environment, Food and Rural Affairs (DEFRA). He is widely regarded as one of the foremost experts on the intersection of finance and environmental issues.

- ATLAS's engagement with the climate change and the social agenda is also addressed and investigated regularly by the Firm's Investment Governance Board (IGB). One of the IGB members is Danyelle Guyatt who specialises in ESG integration and climate-related investment issues across investment portfolios. Previously she was Global Head of Research for Mercer's Responsible Investment team in London, where she led a large-scale research project on the implications of climate change for asset allocation. Danyelle has an MSc in Investment Management with distinction from the Cass Business School and completed a PhD in Economic Psychology at the University of Bath, researching the behavioural impediments to long-term responsible investing.

4. EXTERNAL AFFILIATIONS

ATLAS is a member of the Institutional Investors Group on Climate Change ("IIGCC"). ATLAS participates in the IIGCC's AGM and other events during the year, where it relates to ATLAS's investment sphere. ATLAS contributes to member elections and to policy drafts on an ad hoc basis.

Over the last year ATLAS has started working with GRESB (the Global Real Estate Sustainability Benchmark), an industry-driven organization committed to assessing the environmental, social, and governance performance of real assets globally, including infrastructure assets, to investigate the application of its processes to the listed infrastructure sector.

ATLAS is a signatory to the UN Principles of Responsible Investment.

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