Extra-Financial Risks – Experience within UniCredit

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CIB Devision

Istanbul, –October - 2010
UniCredit Group – at a glance

- **Employees**: ~174,000
- **Customers**: ~40 million
- **Branches**: ~10,200
- **Total Assets exceeded €1 Trillion**
- **International network spanning ~50 countries**
- **Global player in asset management**: ~€200 billion in managed assets
- **Strong regional player in Investment Banking** with leading position in Emerging Europe
- **Ratings**: A/Aa3 long-term ratings (S&P, Moody’s)

Note: Figures as at September 2008
Close co-operation with leading multilateral organisations ...

### Top Participants In EBRD Loans Global

<table>
<thead>
<tr>
<th>Lender</th>
<th>Country</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 RZB AU</td>
<td>Austria</td>
</tr>
<tr>
<td><strong>2 UniCredit Group</strong></td>
<td><strong>Germany/Italy/Austria</strong></td>
</tr>
<tr>
<td>3 ING Groep NV</td>
<td>Netherlands</td>
</tr>
<tr>
<td>4 Calyon</td>
<td>France</td>
</tr>
<tr>
<td>5 Erste Bank</td>
<td>Austria</td>
</tr>
<tr>
<td>6 BNP Paribas</td>
<td>France</td>
</tr>
<tr>
<td>7 Bayerische Landesbank</td>
<td>Germany</td>
</tr>
<tr>
<td>8 Nordea Bank Sweden AB</td>
<td>Sweden</td>
</tr>
<tr>
<td>9 RBS/ABN Amro</td>
<td>UK/Netherlands</td>
</tr>
<tr>
<td>10 Société Générale</td>
<td>France</td>
</tr>
</tbody>
</table>

Source: EBRD as of 31.12.2009

### Top Participants In IFC B-loans Global

<table>
<thead>
<tr>
<th>Lender</th>
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<tbody>
<tr>
<td>1 Calyon</td>
<td>France</td>
</tr>
<tr>
<td>2 Cordiant Capital</td>
<td>Canada</td>
</tr>
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<td>4 BNP Paribas Fortis</td>
<td>France</td>
</tr>
<tr>
<td>5 Banco Santander</td>
<td>Spain</td>
</tr>
<tr>
<td>6 ING Groep NV</td>
<td>Netherlands</td>
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<tr>
<td>7 Société Générale</td>
<td>France</td>
</tr>
<tr>
<td>8 ABN Amro Bank NV</td>
<td>Netherlands</td>
</tr>
<tr>
<td>9 West LB</td>
<td>Germany</td>
</tr>
<tr>
<td>10 Itaú Group</td>
<td>Brazil</td>
</tr>
</tbody>
</table>

Source: IFC as of 31.12.2009
Norway

Korea

Turkey, 2007

PNG LNG

PNG LNG

USD 14,000,000,000
Project Finance
(incl. SACE)

MLA
PNG 2009

Erection of a rolled metal plant in Tyumen City

EUR 182,779,760
Structured Export Finance Facility
(SACE)

MLA & Lender
Russia 2008

Paper Plant

EUR 171,000,000
ECA Buyer Credit
(HERMES, EKN, FINNVERA)

Solo Lender
Russia 2008

Avea İletişim Hizmetleri A.Ş.

USD 1,952,000,000
Long Term Refinancing Facility
(incl. EKN, IFC, SACE)

MLA
Turkey, 2007

TÜV Turk

USD 552,000,000
Project Financing
(incl. GKA)

MLA & Structuring Bank
Turkey, 2007

Damietta

USD 1,020,000,000
Term Loan Facility
(incl. EIB)

MLA & Hedge Provider
Spain, Egypt 2007

Antalya International Airport

EUR 981,000,000
Project Financing
(incl. EKA)

MLA & Structuring Bank
Turkey, 2007

Facility

Turkey, 2007

Over 100 ECA Framework Agreements in force with banks and 60 counterparts worldwide

Leading arranging position for European and Japanese ECAs supported by a global staff of 150 professionals

Total ECA-covered portfolio of approximately EUR 10 bn

Recognised advising and structuring capabilities, strong distribution and bookrunning capacity

... and with all major export credit agencies
Update on UCGs policy

Unicredit signed up the following collective policies:

- Carbon Disclosure Project (CDP)
- Equator Principles
- Global Reporting Initiative (GRI)
- UN Global Compact (UNGC)
- UNEP Finance Initiative (UNEPFI)

In 2009, a revised **Nuclear Energy Policy** and a **Defense/Weapon Industry Policy** were formally approved by the UniCredit Group Risk Committee and distributed to Group entities for formal adoption.
Fundamentals

Introduction to Environmental & Social Risks
Commercial Banks and Sustainability in Finance

- High Profile NGO campaigns against commercial banks
  - 2000 Three Gorges Dam campaign
  - 2000 ABN v Greenpeace, Indonesian palm oil
  - 2001 Dutch banks announce environment and social policies for lending
  - 2002/03 Citigroup vs. Rainforest Action Network
  - 2002 West LB 480km oil Pipeline in Ecuador
  - 2002 Barclays Karahnjukar dam, Iceland

- 2002 Barclays, West LB, Citi, ABN Amro initiative
- 2003 Equator Principles launched by 10 banks including HVB (now Unicredit Bank AG) supported by IFC
- 2006 Equator Principles II
- 2010 by now 69 banks adopted the Equator Principles for sustainable project finance
Environmental Risks are often Hidden Risks

Scenario: Motorway in CEE
Project Scenario:

- The new motorway will significantly relief the villages and small towns which are located along 80 kilometres of national road presently suffering from heavy traffic including transit trucks.
- The route will mainly pass through agricultural lands at distance from villages, a forest section will use the alignment of a regional road to minimise impacts by forest cutting. Route passes near and cuts an edge of an EU Natura 2000 site, but this is no problem since no significant impact was identified in the local EIA and the permitting authorities have expressed the same opinion.
Environment: Commission warns Poland and Bulgaria over nature protection shortcomings; closes German case

The European Commission is pursuing legal action against Poland and Bulgaria for failing to adequately assess the impact of construction projects on protected nature areas. The Commission is also closing a long-running case against Germany on the designation of special bird protection sites.

EU Environment Commissioner Stavros Dimas said: "Natura 2000 – Europe’s network of protected areas – is crucial to the long-term survival of our most valuable and threatened species and habitats. The network gives us healthy ecosystems, which supply vital services such as air and water purification. Whenever sites are affected, it is essential to prevent or reduce any impacts, and I call on Poland and Bulgaria to do so. I also welcome the closure of the case against Germany concerning areas protected under the Birds Directive: this confirms that progress is being made towards completion of the Natura 2000 network."

First warning to Poland over express road cutting through Natura 2000 sites

The Commission has sent a first written warning letter to Poland for breaching nature protection laws by approving and almost completing an express road that cuts through four Natura 2000 sites. The Commission considers as clearly inadequate the original impact assessments for the Szczecin - Gorzów section of the S3 expressway, on which the authorisation of the project was based. Additional detailed assessments carried out after the construction works started also concluded that there were no significant effects on the Natura 2000 sites. However, this goes against factual evidence that priority forest habitats would be destroyed in several locations in Natura 2000 sites and bird habitats compromised in another site. The Commission considers that, by authorising and partially executing the project, Poland has breached the Habitats Directive. It is therefore sending a first written warning.

First written warning to Bulgaria over systematic breach of nature protection law

The European Commission is sending a first written warning to Bulgaria for systematic failure to provide adequate protection for its bird sites. The Commission has received a number of complaints about ongoing tourist, urban infrastructure and wind farm developments in different areas for bird protection throughout Bulgaria. The Commission believes that Bulgaria is systematically violating its obligations to safeguard areas eligible for protection under the Birds Directive and to properly assess the cumulative effects of the numerous authorised plans and projects on the environment and on bird habitats and species. Bulgaria has two months to respond.


- October 2009: EU warns Poland and Bulgaria about serious Natura 2000 deficits

- Express Road Poland vs. Natura site

- Wind Farms Bulgaria vs. Bird Protection Areas
Hidden Risks exist also in Renewables

**Scenario**: Wind farm Turkey

You are invited as lead arranger for a wind farm in Western Turkey on the coast comprising 50 turbines. The project is located with ideal yield conditions on a crest above the coast near a town with touristic beaches which is a summer destination for charter flight tourists. The Greek islands are visible within a few kilometres off the coast. The government has recently introduced a policy to promote wind energy as a renewable source, and the regional directorate of the Ministry of Environment has exempted the Project from EIA.
Hidden Risks

- Wind Farm in Spain – conflicts with griffon vultures (protected under EU Wild Birds Directive) that feed from a cattle carcass landfill – some birds 200 killed
- Conflict potential had not been fully considered during project planning and EIA process and permitting by the local regulators.
- Further, allegations that the permits were given to the Company by the regulators under dubious circumstances (investigation by the Provincial prosecutors).
- Protests of NGOs; Regional Government issued a temporary closure order, was legally disputed by company.
- Interim arrangement: the park could only operate at night, having to stop during day time which means a substantial loss in energy harvest.
- Closing of landfill – alternative sites for vulture feeding
Fundamental Procedures

For Environmental & Social Risks
Management of E&S Risks within UCG

- Board and relevant Departments to define E&S Agenda and include internal stakeholders.
- Develop Bank Procedures and Policies like Sector Policies
- Define Roles and Responsibilities (reflected in the Policies)
- Create Tools and Checklists
- Build Management Capacity (Senior Management Awareness, staff capacity, competence and resources)
- Communicate Needs to internal stakeholders and clients
- Disclose Performance
# Making Efficient Decisions

## Risks associated with the investment

<table>
<thead>
<tr>
<th></th>
<th>High</th>
<th>Medium</th>
<th>Low</th>
</tr>
</thead>
<tbody>
<tr>
<td>High</td>
<td>Consult credit risk and sustainability teams and management</td>
<td>Consult credit risk and sustainability teams</td>
<td>Delegate decision to deal /investment team</td>
</tr>
<tr>
<td>Medium</td>
<td>Consult sustainability team and seek advice on issues before on due</td>
<td>Consult sustainability team</td>
<td>Delegate decision to deal /investment team</td>
</tr>
<tr>
<td>Low</td>
<td>Consult sustainability team</td>
<td>Delegate decision to deal /investment team</td>
<td>Delegate decision to deal /investment team</td>
</tr>
</tbody>
</table>

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This is an example. Each bank needs to develop its own model and processes.
Definition of Basic Ethical Values in the Group General Credit Policy and Product Specific Special Policies

- General and Sector specific questionnaires
- Internal website with links to international standards
- **Project Finance Only**: Categorization and example list
- Implementation of project data base
UCG Risk Policies

- Definition of World Bank Standards as the Basic Ethical Values in the UCG General Credit Policy and additional requirements in the Special Risk Policies (e.g. of Equator Principles for Project Finance in the Special Risk Policy Project Finance)
- Definition of Processes also in the Reputational Risk Policy
- Basic Ethical Values define:
  1. Preclusion of Loan granting to Counterparts that do not follow the World Bank Standards
  2. For project finance: Categorization of all GPF transactions according to the Equator Principles Screening Tool to reflect the World Bank/IFC A/B/C Rating Scheme required.
  3. For other forms of financing Sector Policies apply (or are currently under development)
  4. Deals not meeting the Sector Guidelines or EP Requirements are up for Reputational Risk Decision in the Relevant Commities
**Equator Principles:**
1. Review & Categorisation
2. Social & Environmental Assessment
3. Applicable Social & Environmental Standards
4. Action Plan & Management System
5. Consultation & Disclosure
6. Grievance Mechanism
7. Independent Review
8. **Covenants**
9. Independent Monitoring & Reporting
10. EPFI Reporting

**IFC Performance Standards:**
- PS1: S&E Assessment & Management System
- PS2: Labour & Working Conditions
- PS3: Pollution Prevention & Abatement
- PS4: Community Health, Safety & Security
- PS5: Land Acquisition & Involuntary Resettlement
- PS6: Biodiversity Conservation & Sustainable NRM
- PS7: Indigenous Peoples
- PS8: Cultural Heritage

**IFC EHS Guidelines:**
- General EHS Guidelines
  - Environmental
  - Occupational Health & Safety
  - Community Health & Safety
- Industry Specific Guidelines
  - e.g. Wind Energy Projects

**Good Practice Guidance Documents**

**EP Best Practice Loan Doc.**

for non high income OECD countries
Sector Policies and IFC PS Relationship

1. Sector Policy Checklist
2. Social & Environmental Assessment
3. Applicable Social & Environmental Standards

Loan in compliance with Sector Policy

Loan not complying with Sector Policy - Need for a Transactional Risk Committee Decision

IFC Performance Standards:
- PS1: S&E Assessment & Management System
- PS2: Labour & Working Conditions
- PS3: Pollution Prevention & Abatement
- PS4: Community Health, Safety & Security
- PS5: Land Acquisition & Involuntary Resettlement
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IFC EHS Guidelines:
- General EHS Guidelines
  - Environmental
  - Occupational Health & Safety
  - Community Health & Safety
- Industry Specific Guidelines
  - e.g. Wind Energy Projects

for non high income OECD countries
UCG Loan Decision Process
Compliant Process incl. Settlement of Reputational Risks

1. Project Screening for Reputational Risk and Environmental & Social Risk (Screening Tool) Sector Policy
2. Send Credit Request including Sector Policy Screening Tool to Credit authority
3. Data Collection and Analysis of Environmental and Social Data
4. Assessment of credit request proposal Credit Approval of transaction including Screening Tool and if deviation from Sector Policy go ahead of Transactional Risk Committee

Reputational Risk is reported prezentation of deal to Transactional Risk Committee

Transactional risk Committee Decision Decision (no-go/go)
THE EQUATOR PRINCIPLES
Best Practice Loan Documentation

- UCG prescribes in the Special Credit Policy Project Finance the usage of the Best Practice Loan Documentation developed by the EPFI and available at http://www.equator-principles.com/bestpractices.shtml

- Definition of Equator Principles and IFC Standards in the Loan Documentation as Environmental and Social Requirements

- **Conditions Precedent to First Drawdown:** Project ESAP and ESMS in place and in form and substance satisfactory to Lenders and –as appropriate: Independent Review by Independent Environmental and Social Advisor

- **Covenants:** Compliance with Environmental & Social Requirements and the Project ESAP

- **Monitoring and Reporting:** Provision of periodic implementation reports on EP Implementation in accordance with the KPI defined in the Project ESAP, where necessary independent review or environmental and social audits

- **Measure in Case of Non-Compliance:** Cure Periods in case of Non Compliance and measures to bring client back to compliance. Use of Dividend Stoppers, Event of Default
Possible sources of information for E&S Risk Screening

... Project Type/Process Risk, Company Risk, Country Risk, Site Location Risk ...

- How does the Company deal with HSE and CSR? -> Company website
- Is the project located in a non-OECD high income country? [http://go.worldbank.org/D7SN0B8YU0](http://go.worldbank.org/D7SN0B8YU0)
- How does the country in which the project is located rank on the Corruption Perceptions Index? [www.transparency.org/policy_research/surveys_indices/cpi](https://www.transparency.org/policy_research/surveys_indices/cpi)
- Is the project located in an area with biodiversity of note? -> Integrated Biodiversity Assessment Tool (IBAT) [http://www.ibatforbusiness.org/](http://www.ibatforbusiness.org/)
- Does a media/web scan raise any concerns about the public reputation of the client or project? [www.corporatewatch.org.uk](https://www.corporatewatch.org.uk), [www.hrw.org](https://www.hrw.org).
- How does the company and the country of project implementation rank in terms of E&S risks? oekom Commodity ESG Screening (available from ExF Risk Advisory Desk)
- Are there any human rights allegations against the company? [www.businessandhumanrights.com](https://www.businessandhumanrights.com)
- Where is the project site located, do people live nearby? [http://earth.google.com/](http://earth.google.com/)
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- Where is the project site located, do people live nearby? [http://earth.google.com/](http://earth.google.com/)
- Is the project located in an area with biodiversity of note? -> Integrated Biodiversity Assessment Tool (IBAT) [http://www.ibatforbusiness.org/](http://www.ibatforbusiness.org/)
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Overview of UCG Project Finance in 2009

<table>
<thead>
<tr>
<th>Equator Principles: number of projects financed by risk category</th>
<th>2009*</th>
<th>2008**</th>
</tr>
</thead>
<tbody>
<tr>
<td>Category A</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>Category B</td>
<td>11</td>
<td>14</td>
</tr>
<tr>
<td>Category C</td>
<td>1</td>
<td>11</td>
</tr>
<tr>
<td>Total</td>
<td>14</td>
<td>26</td>
</tr>
</tbody>
</table>

* Projects financed within HWB including one project financed by UniCredit Mediocrédito Centrale SpA where HWB provided due diligence services

**Projects financed within HWB, including one project financed by Bank Austria where HWB provided due diligence services

<table>
<thead>
<tr>
<th>Equator Principles: number of projects financed by risk category and sector, 2009</th>
<th>Category A</th>
<th>Category B</th>
<th>Category C</th>
</tr>
</thead>
<tbody>
<tr>
<td>Resources*</td>
<td>2</td>
<td>3</td>
<td></td>
</tr>
<tr>
<td>Energy</td>
<td>5</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Infrastructure</td>
<td>3</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>2</td>
<td>11</td>
<td>1</td>
</tr>
</tbody>
</table>

* Including oil & gas, mining and metals

<table>
<thead>
<tr>
<th>Equator Principles: number of projects financed by risk category and regions, 2009</th>
<th>Category A</th>
<th>Category B</th>
<th>Category C</th>
</tr>
</thead>
<tbody>
<tr>
<td>Europe: EU</td>
<td>3</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Europe: non-EU</td>
<td>1</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>North America</td>
<td>5</td>
<td></td>
<td></td>
</tr>
<tr>
<td>South America</td>
<td>1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Asia &amp; Australia</td>
<td>1</td>
<td></td>
<td></td>
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<tr>
<td>Africa</td>
<td>1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>2</td>
<td>11</td>
<td>1</td>
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</tbody>
</table>
THANK YOU!

Karen Wendt