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INVESTMENT POLICY OF THE CLIMATE FUND

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1. Introduction

1.1. Objectives and content of the Climate Fund's investment policy

The Climate Fund (Ilmastorahasto Oy) is a fully state-owned special-assignment company. Its operations focus on combating climate change, boosting low-carbon industry and promoting digitalisation.

The Climate Fund's investment policy defines and sums up the company's approach to investment, operative investment principles and objectives, funding criteria and categories, instrumentation and investment process, and the principles and objectives of the company's liquid asset management. The Climate Fund's Board of Directors confirms the company's investment policy on an annual basis.

1.2. Regulatory and guidance framework

The Climate Fund's operations are guided by the Limited Liability Companies Act (624/2006), Securities Markets Act (746/2012) and State Shareholdings and Ownership Steering Act (1368/2007). In addition to the above, the company follows the government resolution on state ownership policy, as well as a possible special-assignment company act passed in future. Along with the legislation in force and the Fund's Articles of Association, the company's operations are also guided by national and international treaty obligations where applicable, regulations on State Aid and the principles of good governance.

The Ministry of Economic Affairs and Employment is responsible for the company's ownership steering and has issued the Climate Fund's operational guidelines. The company's decision-making and oversight mechanisms are described in the Governance Report appended to this investment policy.

1.3. Framework for determining the investment policy

As a special-assignment company, the Climate Fund aims at fulfilling its mission as efficiently as possible and creating societal impact instead of seeking to maximise its own revenue. However, the company's investments and funding must be self-sustainable in the long term when assessed as a whole.

The Climate Fund's operational guidelines require the Fund to primarily operate on the yield of its capital, such as the return on investments and funding. The owner has provided an option for additional capitalisation of the company, however, and an appropriation of EUR 300 million was allocated to the company for the years 2020–2022.

1.4. The Climate Fund’s asset management and long-term holdings

The Ministry of Economic Affairs and Employment is responsible for the company’s ownership steering, with the exception of matters involving Neste shares, which are the remit of the Ownership Steering Department of the Prime Minister’s Office and are described in more detail in the company’s Governance Report.

1.5. Responsibility in the company's investments

Financial, environmental and societal impact and responsibility are key elements of the criteria guiding the Climate Fund’s financing activities, so the company does not have separate sustainability targets. The reporting obligations of investment targets, including with regard to impact criteria, are agreed on in the financing agreements. These reports also lay the foundation for the Climate Fund’s annual CSR reporting, for example.

The environmental responsibility of investment targets is assessed against several criteria, both by the company’s own analytics and by third-party experts. One of the three preconditions in the Climate Fund’s funding criteria is compliance with the “do no significant harm” (DNSH) principle. The principle is used to identify the essential environmental objectives with regard to the investment targets and ensure compliance with the EU's environmental and climate regulations relevant to those objectives. Each investment target is also assessed according to its emissions reduction potential. The Climate Fund also monitors compliance with the EU's sustainable investment framework, i.e. the taxonomy, even though this is not a precondition for funding. The monitoring of other aspects, such as biodiversity, can also be relevant depending on the investment target.

The company follows anti-money laundering and terrorist financing practices in its investment process by applying the customer due diligence recommended by FIN-FSA to the due diligence analyses of investment targets where applicable. If necessary, the company reports any suspicious transactions to the Financial Intelligence Unit.

The Climate Fund requires its client companies to follow applicable tax regulations and best practices in tax matters. In the role of a public funding provider, the Fund seeks to identify cases in which various structures have been used to eliminate or reduce tax liabilities.

The Climate Fund's approach to responsibility is described in more detail in the company’s Code of Conduct. It obliges the company’s contract partners to also follow the principles of responsibility, for example with regard to employee rights and compliance with labour legislation, data security and privacy, and the prevention of bribery and corruption.

1.6. Responsibilities, authorities and reporting in investment activities

The Climate Fund’s AGM, Board of Directors, Investment Council and CEO are responsible for the company’s governance. The company has an executive team tasked with assisting the CEO.

Each year, the Climate Fund's Board of Directors confirms the guiding principles of the company’s investment policy prepared by the Fund's operative management. The Climate Fund’s CEO and executive team are responsible both for implementing these guiding principles in the company’s operating models and processes, as well as reporting on the company’s operations to the Board. The Board is regularly informed of the progress of investment activities and the company's financial standing in order to ensure that policies are appropriate and implemented at the correct time.

The Climate Fund's Board of Directors typically discusses each project three times before an investment decision is made. According to the operational guidelines, the Board makes all investment decisions under EUR 20 million. The Ministry of Economic Affairs and Employment brings decisions on investments in excess of EUR 20 million to be confirmed by the Ministerial Committee on Economic Policy.

The owner requires the Climate Fund to give regular financial and operative reports to the Ministry of Economic Affairs and Employment, which is responsible for the Fund's ownership steering, as well as to the Prime Minister’s Office, Ministry of the Environment and Ministry of Transport and Communications. For its part, the Ministry of Economic Affairs and Employment reports on the company’s operations to the Ministerial Committee on Economic Policy.

The meetings of the Investment Council primarily address current issues related to the company’s investment activities and overall business environment. The Investment Council does not discuss or participate in the making of individual investment or financing decisions.

2. Operative investments

2.1. Funding principles and objectives

The company aims to achieve a full return on invested capital over time and across the portfolio. However, the Climate Fund's operations involve significant risks concerning the return of capital in the case of individual investment decisions, and the time span for the return of capital is long.

The target volume of investment operations is EUR 50 million 2021 and EUR 80 million going forward from 2022. These annual targets should give the Fund adequate tools to achieve the goals set out in its operational guidelines.

2.2. Funding criteria

The Climate Fund's operational guidelines specify investment criteria and a three-stage assessment model for the Climate Fund, consisting of financial and other preconditions, cross-cutting impact goals and more detailed, investment-proposal-specific impact goals. Funding will only be granted if the investment proposal meets all of these preconditions. The final comparison and choice between investment proposals that meet the preconditions is made based on the Fund's impact goals.

The Climate Fund's Board has approved the following three-step criteria for assessing investment targets.

1. Preconditions
2. Climate Fund impact criteria
3. Investment proposal specific analysis

PRECONDITIONS

Each investment proposal has to meet the Fund's preconditions:

1. Each investment target must have a credible plan with regard to, e.g. the competencies and financing required for creating business that is at least self-sustaining.
2. The Climate Fund's investment must provide verifiable added value as part of the project's overall funding: it must either be necessary for the project to be realised in the first place or enable the project's realisation earlier or on a larger scale, or allow the project to include Finland in a manner that would not be achieved otherwise.
3. Compliance with the "do no significant harm" principle: if implemented, the investment must not cause significant harm to any of the six environmental objectives of the EU's sustainable investment framework.

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THE CLIMATE FUND'S IMPACT CRITERIA

Each investment decision is assessed against the Climate Fund's general impact criteria. An individual mechanism for monitoring and verifying the intended impact is also created before each investment decision.

The Climate Fund's general impact criteria are:

4. Emissions reduction potential in Finland and globally.
5. Productivity potential, which can be assessed with indicators such as the growth of national RDI inputs, high-value employment impact, or increases in intellectual capital.
6. Alignment with the EU taxonomy. Compliance with the EU's sustainable investment framework is an advantage, but not a condition for Climate Fund financing.
7. Business potential, productivity benefits and added value that the investment package enables for other registered actors operating in Finland.

INVESTMENT PROPOSAL ANALYSIS

The key aspects for assessing impact and risks can vary widely between investment targets. A proposal-specific analysis can provide more in-depth information about, for example, biodiversity impact, export potential, social justice issues or potential for leveraging EU funding.

2.3. Investment categories

The operational guidelines state that the Climate Fund's primary investment targets are industrial scale-ups of, for example, new technology demonstration projects. The Fund can invest in both private and public projects. The Climate Fund can also participate in various public platforms for enhancing the use of data, and in public-private joint projects. The operational guidelines require approximately 65% of the Climate Fund's investments to relate to climate change and about 35% to digitalisation. The focus of the Fund's investment activities must be on combating climate change and accelerating the transition to low-carbon industry.

The Climate Fund's Board of Directors has decided to focus operations on two investment categories in the initial phases of the Fund's operation:

1. *Scaling up the deployment of climate solutions:* demonstrating the viability of new technology and/or business models using such technology for the first time on a commercial scale. It can also involve scaling up a technology and/or business model that has been shown to be commercially viable on a small scale to a significant, industrial scale for the first time. Financing can be granted for projects such as plant investments or accelerating the deployment of existing commercial climate solutions, whether physical or digital.

2. *Platforms enabling emission reductions:* physical or digital environments used by one or more operators, which enable emission reductions and/or scalable

climate business for the platform's users. Financing can be granted for projects such as shared piloting infrastructure for emission reductions, carbon binding or climate solutions, or digital platforms that promote the use of data for reducing emissions.

2.4. Instrumentation and ticket size

The Climate Fund's operational guidelines permit the Fund to grant equity financing, debt financing and mezzanine financing. Capital loans have been defined as a suitable instrument for the Fund’s initial stages. The operational guidelines state that the Climate Fund can establish funds, invest in funds and use state aid for its financing instruments. Leveraging EU funding is also listed in the operational guidelines as one of the Climate Fund’s duties.

The Climate Fund’s Board has decided that the company will initially operate mainly with two types of financing instruments:

1) capital loans; and
2) special investment funds and other special funding instruments.

Capital loans

The interest and principal of capital loans are subordinate to all other debts in case of liquidation or bankruptcy of the company. Principal is repaid and interest paid only to the extent by which the aggregate amount of the company’s unrestricted equity and all subordinated loans at the time of payment exceeds the losses recognised on the balance sheet in the company’s latest financial statements. In the debtor's accounting, a capital loan does not increase the company’s equity but can be added to equity for the purpose of calculating solvency in certain cases.

The Climate Fund’s capital loans are offered on market terms by setting the interest rate according to the reference interest rate table published by the EU. The reference interest rate table specifies minimum interest rates based on the loan applicant’s credit rating. The Climate Fund can go above, but not below, the minimum interest rate. Alternatively, the Climate Fund can offer a capital loan jointly and on equal terms with a private investor if the private investor in question contributes a significant share of the total investment (> 30%).

The Climate Fund’s risk management policy limits its investment to a maximum of 50% of the total investment and requires agreeing on a yield unit and linking it to the capital loan for each investment target. The yield unit can consist of an interest rate premium exceeding the minimum rate, a convertible and/or a profit sharing. Furthermore, the amount of the Climate Fund’s individual investments is limited so that the Fund can spread its risk over several investment decisions within its annual investment volume. At the launch phase of its operations, the Climate Fund’s ticket size is EUR 2–20 million in the category of industrial scale-ups and EUR 1–10 million in the category of enabling platforms.

Special investment funds and other special funding instruments.

Special investment funds and other special funding instruments come into play when the Climate Fund does not invest directly in companies and projects that produce climate solutions, but makes its investment through an intermediary that manages the Climate Fund's stake by virtue of a fund agreement or other management agreement.

2.5. Target companies

The investment targets consist of private companies, state-owned enterprises and public-private partnerships. The financed projects must meet the preconditions set in the Climate Fund's funding criteria and generate clear impact in line with the criteria.

The focus of the Climate Fund's investment operations is on companies registered in Finland. According to the Climate Fund's funding criteria, each investment target is assessed according to its business potential, productivity benefits and added value that the investment package enables for other registered actors operating in Finland.

2.6. Funding process

The funding process is the Climate Fund's core process. Dealflow management has a pronounced role in its early phases, for example in generating project flow and providing customer service to potential investment targets. Dealflow management and analysis provides an overview of the field of potential investment targets. It also identifies promising investment targets that are in an appropriate stage of development in light of the Climate Fund's funding criteria and picks them out for more detailed analysis.

The investment analysis includes analysing individual investment targets, preparing the investment decision, and managing and monitoring the investment for the project's entire lifespan. The analysis of investment targets is based on the Climate Fund's funding criteria in all stages of the decision-making process. The Fund's operational guidelines stipulate that every investment must meet the preconditions set in the funding criteria. The final comparison and choice between investment proposals that meet the preconditions is made based on the Fund's impact goals.

The Climate Fund makes significant investments in a wide variety of different solutions. The careful and credible preparation of investment decisions requires bringing in external subject matter expertise to support the investment decisions on individual investment proposals. The validation and assessment of the sought-after impact also frequently requires special expertise in the investment target's field, which the Climate Fund also acquires from outside experts. The Climate Fund's Board of Directors typically discusses each project three times before an investment decision is made.

The Climate Fund’s investment process does not end with the investment decision. Monitoring and reporting on the societal impact sought by the Climate Fund begins immediately after the investment decision has been made. Impact monitoring is carried out as part of the long-term cooperation with investment targets. The actual terms of the investment are also often tied to the realisation or verification of the sought-after impact. In certain cases, the Climate Fund can even take the role of owner for the duration of the investment. The funding process is described below in Finnish (Figure 1).

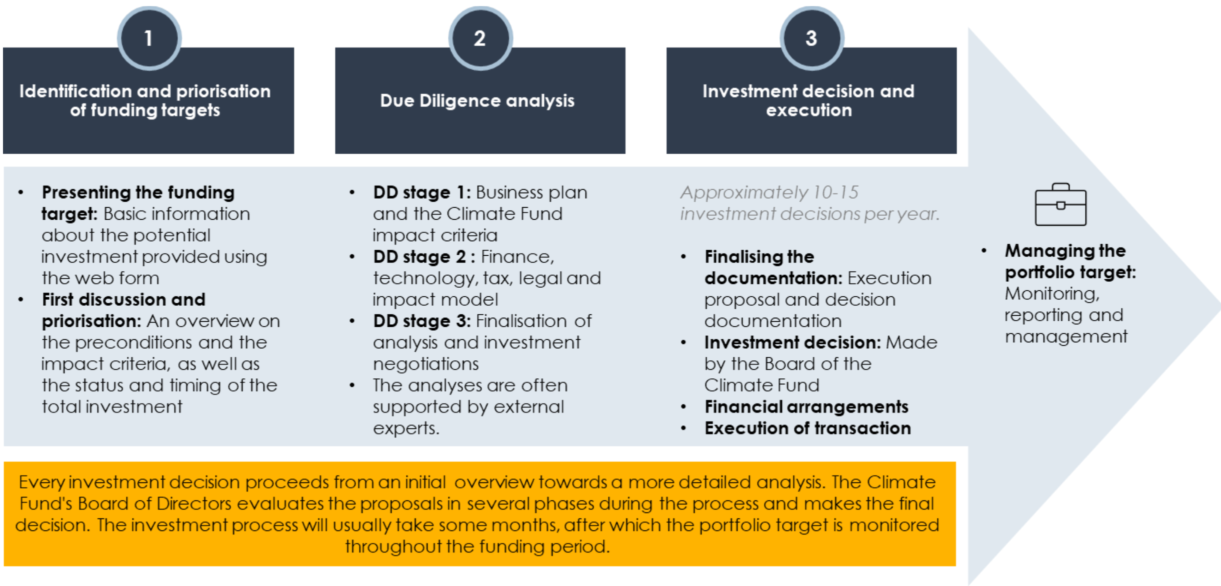

Figure 1 Funding process

2.7. Risks and risk management

The company’s key risk categories are operative risks, financial risks, strategic risks, compliance, and reputational and sustainability risks. The greatest financial risks of the company’s operations are related to the development of the dividend revenue from Neste and the success of risk management in the company’s operative financing activities. It is the task of financial risk management to ensure the continuity and profitability of operations, secure the company’s assets and property, and provide the true and fair view of the company’s finances and operations required by regulations. The company's risk management approach, processes and reporting are discussed in more detail in its Internal Auditing and Risk Management Guidelines.

2.8. State aid

Within the framework of the provisions and regulations on state aid, the company can take bigger risks or accept smaller profits than private investors in its investment activities. The Climate Fund does not offer instruments defined as state aid during its launch phase. The market-based nature of each investment decision is established individually.

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3. Liquid assets

The company shall have sufficient liquid assets available to cover its open investment commitments and operative expenses. At least the amount of funds required to ensure the company's day-to-day operations is always kept on the company's bank account. Other liquid assets are invested in either bank accounts, fixed-term deposits or low-risk and liquid bond funds, taking into account the company's investment commitments and the liquidity requirements of its investment activities.

The liquid assets are distributed over several investment targets to reduce risk. As a rule, the company avoids negative interest rates when investing its liquid assets. Factors such as the fund's investment policy, counter-party risk, size, liquidity, risk profile, past performance, time span and cost structure are taken into account in selecting investment targets for the Climate Fund's liquid assets.

The principles of responsible investment are taken into consideration when investing assets, and the Climate Fund prefers to invest in funds with a confirmed climate or low-carbon policy or which otherwise seek to minimise the negative climate impact of their investment activities.

The company's management ensures sufficient liquidity, invests the company's liquid assets and realises liquid assets from the investment targets within the investment authorisations issued by the Board of Directors.