How We Understand ESG at Mouro Capital

We just got an award for **best Sector Specialist Fund** for our ESG practices in the context of the Private Equity Wire European ESG Awards 2023. We are happy to share the news and provide a broader reflection of our ESG journey so far, hoping it can be of use to our industry peers.

The news did not totally come unexpected. We have put a lot of conviction and effort behind the scenes in refining how we think about ESG – for us as a team, throughout our investment process, with our portfolio companies and with the broader innovation community.

Best ESG fund: Sector Specialist

Starting from scratch?

Not really. When we initiated our ESG journey a few years ago now, our portfolio already had several SDG-aligned companies targeting un/under-banked populations, creating technology to avoid money-laundering, or reducing the consumption of resources by bringing in digital into old economies, among many other activities – i.e., addressing environmental, social and governance aspects.

Also, as a team, we have always encouraged a set of values and policies to reflect our strong ESG commitment, which further informs how we do things.

All in all: not a bad place to start, but there is certainly so much more to do!

Striking the right balance(s).

Here is a first mantra from our journey so far: “Sustainability = discovery”. Discovery of new regulations, frameworks, associations, and certifications. In the early days of our journey, it was essential to dedicate time to understand it all – only to discover that to date, most regulations are still moving targets, with a variety of opportunities for each organization to integrate and even contribute to them.

In that sense, we found the Sustainability Financial Disclosure Regulation – SFDR and the United Nations frameworks (Principles of Responsible Investments – PRI, Global Compact - GC and the Sustainable Development Goals – SDGs) most relevant, as we wait for the US SEC and the UK FCA to finalize work on additional regulations.

However, there are also several strategic questions where it is very important to make a consistent decision:

ESG-input vs. ESG-output. It is important to understand the difference between ESG-input, which is a risk framework, and ESG-output, which is an impact framework. Integrating climate risks as part of your investment decisions is fundamentally different to investing in a company innovating in the climate risk space. Correctly building a holistic ESG framework requires firms to be active on both fronts. Having a single-sided ESG strategy might cause your stakeholders to doubt about your firm's commitment and potentially leading to controversy.

Outsourced vs. in-house ESG. Hiring external consultants to develop a firm's ESG strategy is valuable and helpful, but we firmly believe on doing it in-house. An in-house ESG function creates a stronger alignment with the team and the management, and it allows for a higher level of participation in creating unique rules and behaviours for each organization. It further guarantees that ESG is embedded in the values of the corporation – for real impact. There tends to also be a cost-efficiency aspect to in-house, especially in the current state of the market where standards are still lacking, and each firm needs to design their own way. Thanks to this reasoning we found the best way to improve operational impact on our organization.

Vertical vs. Horizontal ESG competences. Managing ESG internally is not enough. Many companies have ESG departments working in silos and outside of the critical decision paths and thus disconnected from decision-makers. We do not share that way of designing the organization – rather, in our case, we have embedded ESG responsibilities and values among all the team, from the investment team, the research function, the compliance and risk office, all the way to the general partners.

So, how have we applied these principles in practice?

Our two-sided ESG strategy.

On the one hand, we have integrated ESG processes in the internal management of Mouro Capital at the highest possible standard:

- By integrating ESG-aligned values into the remuneration policy, we aim to have a higher impact on the team and its incentives.
- By making and executing on a variety of ESG commitments and initiatives, such as yearly carbon offsetting, sponsoring initiatives related to inclusion (such as Included VC and Female Founder Office Hours), and fostering initiatives conducive to create awareness around mental health matters in the ecosystem.
- By adopting clear and transparent ESG internal policies around diversity and inclusion, remote work, ESG-compliant remuneration policy, and many governance policies such as reinforced whistleblowing.

On the other hand, we have integrated ESG factors in Mouro Capital's activity through two interconnected ESG policies:

- **Responsible Investment Policy,** which relies on four different ESG investing strategies:
    - Excluding sectors that are relevant for us as fintech investors and including technology companies that enable those excluded sectors.
    - Investing in fintech companies aligned with the SDGs. For example, some of our portfolio companies such as Ripple, or Creditas.
    - Integrating ESG criteria in the investment decision-making process.
    - Playing an active role in portfolio management, whether at the board level, during monitoring, or by providing bespoke support to our portfolio partners.
- **Sustainability Risk Policy:**
    - Upfront identification of sustainability risks, including the establishment of excluded sectors where these risks are considered inappropriate, not controllable, or excessive.
    - Assessment of sustainability risk exposure during the decision-making process, with a dedicated sustainability due diligence process.
    - Post-investment sustainability risk tracking and mitigation via a dedicated ESG reporting.

The results… so far.

It has been a journey for the past couple of years – and what a journey! We have accomplished more than we could imagine when we started: we have become UN PRI and UN GC signatories, as well as ILPA Diversity in Action members. Even more importantly, the award to the Best ESG fund: Sector Specialist by the Private Equity Wire European ESG Awards 2023 is a recognition by the industry that we are on the right track, and that, as incoming ESG regulations such as SFDR become clearer and more stringent, we have what it takes not only to succeed, but to lead the way.

What now?

The journey is far from over. Our ESG strategy to date has opened our eyes to a new dimension that we are actively incorporating in our modus operandi. In that regard, over the next years will keep working on:

- **Improving the quality and variety of data:** data availability and comparability are known issues in private markets – especially concerning ESG. We will endeavour in creating smart data methodologies and datasets to enhance our ability to track ESG impact and support our companies in making critical management decisions.
- **Increase the portion of SDG-aligned investments in our portfolio**: we aim to explore uncharted thematic verticals and positioning ourselves with new investments and value-add initiatives.
- **Deepening and diversifying the ESG value-add we provide our portfolio companies:** our goal is to continue shouldering new ESG obligations across our portfolio while supporting our CEOs and their teams on their journey towards ESG compliance.
- **Further supporting the creation of ESG standards in the industry**. Standards play a crucial role in establishing common ground for understanding and sharing best practices. In these early stages we have been actively participating in many initiatives on this front and you can expect us to keep on doing it in the future.

Take this as our pledge.