

Liquidity and Leverage Policy

Baltic Horizon Capital AS

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Introduction

1.1. General

This Policy describes how Baltic Horizon Capital AS manages liquidity and leverage for its Alternative Investment Funds (AIFs) in line with AIFMD and Delegated Regulation (EU) 231/2013.

The Policy forms part of AIFM risk management processes and should therefore be reviewed and adjusted, when necessary, by the employee responsible for the Risk Control Function. The updated Policy is reviewed by the Compliance Function and approved by the Supervisory Board of Baltic Horizon Capital AS.

Fund Manager is responsible for introducing the Policy (including any amendments thereto) to the Fund Administration team.

1.2. Liquidity management principles

The purpose of liquidity management is to ensure that an appropriate level of liquidity is maintained in the AIF to meet its underlying obligations. One of the key factors underpinning liquidity management is the relatively low liquidity of the AIF's real estate assets, in general, and especially when market sentiment is pessimistic. Financial liquidity risks of AIFs are mainly managed through proactive management of covenants, the overall financial position, and daily cash management (see details in section 3).

The liquidity management shall be aligned with

- a) the investment strategy of the AIF, and
- b) leverage and risk profile of the AIF

1.3. Financial leverage

Each AIF has a maximum level of financial leverage defined in its corporate documents, which shall be consistent with the AIF's general risk profile. Usually, the financial leverage ratio is expressed as the ratio of financial obligations to banks or other lenders to the value of the real estate as determined by the latest valuation. In addition, leverage must be calculated using the gross and commitment methods per Article 6 of Delegated Regulation (EU) 231/2013; the methodology is set out in Appendix 1 of this Policy.

2. Responsibilities

2.1. Risk Control Function

The Risk Control Function is responsible for liquidity risk control as stipulated in the Risk Management Framework, oversees liquidity risk limits, ensures regular stress testing, and informs the Management Board of the risk profile of each AIF and the adequacy and effectiveness of the liquidity risk management process.

2.2. Head of Fund Finance and Administration

Head of Fund Finance and Administration ("Head of Fund Finance and Administration") is responsible for managing day-to-day liquidity and financial leverage, including the following actions:

1. Analysis of financing terms in respect to a proposed project including the feasibility of the financing alternatives.
2. Arrangement of financing extension or refinancing.
3. Arrangement of tender for new financing, if needed.
4. Calculation of LTV.

5. Implementation of the AIFM's Management Board's decisions related to the financing.
6. Issue of recommendation on financing to the AIFM's Management Board.
7. Monitoring interest rate risk and issuing recommendations on hedging.
8. Monitoring of covenants continuously.
9. Negotiations on the covenants, pledges and other aspects of the financing.
10. Proactive cooperation with the banks in case of potential breach of the covenants is expected, or any similar issues arise.
11. Regular reporting to the Risk Control Manager and the AIFM's Management Board on liquidity, interest rate, refinancing and currency risk.
12. Regular reporting to the banks.
13. Liquidity stress testing and sensitivity analysis of covenants at least once per year for the annual budget or when the situation in the Fund or financed property considerably deteriorates, triggering a potential breach of covenants or liquidity issues.

Head of Fund Finance and Administration at least annually provides the following information on the AIF's financial risks to the Risk Control Manager and the Management Board:

- c) Current level of financial leverage of each property and the AIF;
- d) Historical and current level of covenants, threshold and estimate of the risk of a potential breach of a covenant (with stress test scenarios, if needed) and in case any of the scenarios show that a breach of covenants is likely, Head of Fund Finance and Administration shall prepare an action plan for mitigating the risk;
- e) Results of liquidity stress testing;
- f) Projected level of covenants (to be updated at least quarterly);
- g) Hedging of interest rate risk and open exposures;
- h) Recent communication and issues with the banks, if any;
- i) Counterparty analysis related to banking relationships including a proposal of the counterparty limits.

In case of a threatened or actual breach of a covenant or other obligations to the bank, the Head of Fund Finance and Administration shall report it without delay to the Risk Control Manager, the AIFM's Management Board and Supervisory Board together with a proposed action plan.

When arranging the financing, the following limitations shall be taken into account:

- Maximum financial leverage level, defined on the AIF level and on the property level.
- Limitations of the use of securities, pledges and other collaterals set in the corporate documents of the AIF.
- Set default financial ratios have sufficient buffer for adverse events.
- The financing term shall comply with the strategy of the investment.
- Reasonable alternatives for remedy of default events or prevention of such.
- The possibility to use excess cash of a SPV for the general needs of the AIF.
- No recourse to other assets of the AIF or cross-collateral or similar guarantees unless it is allowed by corporate documents of the AIF and reasonable from the commercial point of view.

The banks invited to provide financing proposals shall meet counterparty risk requirements in accordance with the AIFM's Risk Management Framework.

3. Cash management

3.1. Main principles of cash management

Management of AIFs' cash shall adhere to the following general principles:

3.1.1. Regular cash planning on the subsidiary level and AIF level shall be implemented to prevent liquidity risk;

3.1.2. Each AIF is a separate unit and cash (or any assets and liabilities) among the AIFs cannot be shared;

3.1.3. Cash Management transactions including, but not limited to, transfers of the funds, exchange of currency or placement of deposits shall be arranged by negotiating the most favourable terms possible at a given moment in time.

3.2. Bank accounts

3.2.1. Number of bank accounts in each AIF's subsidiary shall be maintained at a minimal level; accounts that are not used shall be closed without delay.

3.2.2. All banking relationships are subject to the counterparty analysis: if any agreement with the third party does not restrict choice of a bank, only international, sound and credible banks have to be chosen for cash management.

3.3. Excess cash

3.3.1. Excess cash is defined to be the cash not required by an AIF's subsidiary for its daily operations within a quarter.

3.3.2. Excess cash should be kept in the AIF unless transfer of excess cash to the AIF decreases tax efficiency of the Fund, excess cash is of short-term nature, or transfer to the AIF is restricted by agreements with third parties (banks).

3.3.3. Excess cash shall be deposited short-term with approved banks, unless the additional interest is minimal compared to reduced liquidity flexibility, or unless the AIF investment strategy permits longer-term alternatives.

3.4. Currency

3.4.1. Currency risk shall be hedged according to the AIF's strategy and currency risk hedging strategy defined in the key corporate documents of the AIF, assuming that it is commercially feasible.

3.4.2. Each AIF's subsidiary shall keep excess cash and other short- and long-term deposits in the currency of the AIF;

3.4.3. Special attention to currency risk should be paid in AIFs where the local currency of the investments is floating against the currency of the AIF.

3.4.4. Excess cash must be converted into the currency of the AIF at least once a month. This does not apply if the excess cash is temporary and the cost of the required foreign exchange trades outweighs the risk of losses from currency fluctuations.

3.4.5. If there are regular payments under obligations in currencies other than the income of the AIF, net income (i.e. income after allocation of cash for planned expenses in the same currency) has to be converted into the currency of the obligations until the amount equal to these payments pro rata for the period is accumulated.

3.5. Inter-company transfers

3.5.1. The following considerations must be made before executing a transfer:

3.5.1.1. potential tax impact shall be analysed;

3.5.1.2. need for bank approval beforehand; if required, it has to be obtained in writing and filed properly;

3.5.1.3. effect of the transfer on financial covenants.

3.5.2. Withholding taxes (if applicable) must be estimated; once paid, retrieval thereof has to be arranged at the earliest possible terms.

3.5.3. Information covenants in relation to inter-company transfers must be adhered to.

3.6. Collection of receivables

3.6.1. Invoices for services to tenants shall be prepared and sent without delay according to agreed terms in lease agreements.

3.7. Settlement of payables

3.7.1. Payment systems shall be designed so that payments are made in due time, with financial obligations taking priority over other payments.

3.7.2. Payments and receivables from the same company shall be netted when possible.

3.7.3. To avoid conflicts of interest, payments to related companies for their services have to be made according to the same principles as to other independent service providers.

3.8. Procedure of cash planning and cash monitoring

3.8.1. Annual cash flow projections

To ensure efficient cash flow management for each AIF's subsidiary as well as on the AIF level, cash flow projections have to be prepared. Cash flow projections on an AIF and AIF's subsidiary level shall be revised quarterly, or more often if the liquidity situation in the AIF so requires. If there are several investment projects simultaneously, cash flows must be projected for each project.

During the annual budgeting process, detailed cash flow projections are prepared for the next year and for each AIF's subsidiary, as well as at the consolidated level, on a monthly basis. Cash flow projections shall also include estimations of annual cash flow for the 2 years after the budgeting year.

Annual cash flow projections prepared during the budgeting process shall include sensitivity analyses, which shall be implemented in accordance with the Liquidity Stress Testing Policy. Based on the results of such tests, the Head of Fund Finance and Administration shall draw the attention of the Risk Control Manager, the AIFM's Management Board, and the Supervisory Board to the key factors that might undermine the liquidity of the AIF and propose actions to mitigate the risks.

3.8.2. Monthly cash balance reports

The target of regular revisions of cash balance and cash flow projections is to eliminate unexpected cash shortfalls. The Head of Fund Finance and Administration is responsible for monthly cash flow projections in accordance with this Policy.

Monthly cash balance reports cover the cash positions of the AIF or AIF's subsidiaries, if relevant, on the reporting date. The report might also include upcoming payments and expected cash receipts for the next three weeks. Such reports, with additional information on incoming and outgoing payments, shall be prepared by the Head of Fund Finance and Administration or another team member under the Head of Fund Finance and Administration's supervision.

Notwithstanding the information provided in monthly cash balance reports, the outsourced accounting company shall inform the Head of Fund Finance and Administration of any unexpected payments and any need for a cash injection by the AIF's subsidiary as soon as the need becomes known to the accounting company.

3.9. Procedure of payment arrangement

3.9.1. Inter-company payments

In case financing is arranged at AIF's subsidiary level, Head of Fund Finance and Administration is responsible for arranging intercompany payments required for AIF's subsidiary to meet its financial obligations.

Appendix 1: Methodology of leverage calculation under Gross and Commitment methods

In addition to the regular financial leverage calculation, expressed as the ratio of an AIF's financial liabilities to the market value of its investment portfolio, leverage of an AIF shall also be calculated as the ratio between an AIF's exposure and its net asset value. The exposure of an AIF shall be calculated using either the gross or commitment method.

The Fund Controller of an AIF is responsible for calculating leverage using these two methods and for including it in financial reporting to investors.

Exposure contained in any financial or legal structures involving third parties controlled by the relevant AIF shall be included in the calculation of the exposure; however, any exposure that exists at the level of SPVs or sub-holding companies shall not be included in the calculation of the leverage unless guarantees or other securities are provided by the AIF which might result in potential losses beyond its investment in the respective company.

The calculation of exposure shall also exclude borrowing arrangements entered into if they are temporary and fully covered by contractual capital commitments from investors in the AIF.

Gross method

The exposure of an AIF calculated in accordance with the gross method shall be the sum of the absolute values of all its positions valued as per the AIFMD requirements.

For the calculation of the exposure of an AIF in accordance with the gross method, the Fund Controller shall:

- j) Exclude the value of any cash and cash equivalents which are highly liquid investments held in the base currency of the AIF, that are readily convertible to a known amount of cash, are subject to an insignificant risk of change in value and provide a return no greater than the rate of a three-month high-quality government bond.
- k) Convert derivatives using one of the following methods: - Plain vanilla fixed/floating rate interest rate and inflation swaps: notional contract value. - Currency swaps: Notional value of currency leg(s). - Cross currency interest rate swaps: Notional value of currency leg(s).
- l) Exclude cash borrowings that remain in cash or cash equivalent as referred to in point (a) and where the amounts payable are known.
- m) Include exposure resulting from the reinvestment of cash borrowings, expressed as the higher of the market value of the investment realised or the total amount of the cash borrowed.
- n) Include positions within repurchase or reverse repurchase agreements and securities lending or borrowing or other arrangements.

Commitment method

The exposure of an AIF calculated in accordance with the commitment method shall be the sum of the absolute values of all positions valued in accordance with AIFMD requirements.

For the calculation of the exposure of an AIF in accordance with the commitment method, the Fund Controller shall:

- o) Convert derivatives using the following method: - Plain vanilla fixed/floating rate interest rate and inflation swaps: notional contract value. - Currency swaps: Notional value of currency leg(s). - Cross currency interest rate swaps: Notional value of currency leg(s).
- p) Apply netting and hedging arrangements.
- q) Calculate the exposure created through the reinvestment of borrowings where such reinvestment increases the exposure of the AIF (same as for gross method).
- r) Include other arrangements in the calculation (such as convertible borrowing, repurchase agreements, securities borrowing arrangements).

For the purposes of calculating the exposure of an AIF according to the commitment method:

- s) Netting arrangements shall include combinations of trades on derivative instruments or security positions which refer to the same underlying asset, irrespective — in the case of derivative instruments — of the maturity date of the derivative instruments and where those trades on derivative instruments or security positions are concluded with the sole aim of eliminating the risks linked to positions taken through the other derivative instruments or security positions.
- t) Hedging arrangements shall include combinations of trades on derivative instruments or security positions which do not necessarily refer to the same underlying asset and where those trades on derivative instruments or security positions are concluded with the sole aim of offsetting risks linked to positions taken through the other derivative instruments or security positions.

For a more detailed explanation of the leverage calculation in relation to the estimation of derivatives, please refer to Commission Delegated Regulation (EU) No 231/2013 of 19 December 2012 (<https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:32013R0231>).