

COMMUNICATION ON ENGAGEMENT (COE) 2014



INVESTMENT FUND FOR
DEVELOPING COUNTRIES

Dear reader

The overall mission of IFU and the funds managed by IFU is to enhance sustainable economic growth, development and more equitable income distribution by financing private sector investments in developing countries and reforming economies.

Our sustainability policy is ambitious and is based upon international UN, ILO and OECD conventions, declarations and agreements. We hereby seek to contribute to the global achievement of the UN Millennium Development Goals.

It is our objective that our investments contribute to a lasting economic, environmental and social sustainable development through the creation of healthy and safe workplaces and the transfer of know-how and cleaner technologies. We wish to contribute to the social and economic development of the local community – and we also encourage the project companies to engage themselves locally.

We are committed to securing high sustainability standards as a fundamental aspect of sound business management of our investments and business practice. IFU's board of directors, management, employees and advisers must conduct all their business operations in accordance with the values and the spirit laid down in the sustainability policy.

We signed up to the 10 UN Global Compact principles in 2008, because they are a set of universal principles that help us underline our sustainability policy wherever in the world we create business, and we are committed to implementing and advancing these principles together with the project companies and within IFU's sphere of influence.

Copenhagen, May 2015
Tommy Thomsen, CEO

IFU as a partner

IFU – Investment Fund for Developing Countries was established in 1967, and for almost fifty years our work has proven that it very often means good business for all parties if investment and development go hand in hand.

IFU's activities are based on the following:

- We invest risk capital on market terms in the form of share capital, loans and guarantees in private sector companies that are established or will be established in developing countries or emerging markets. We call them project companies.
- We provide professional advice regarding the business environment, investment terms and sustainability issues as well as cultural and political barriers, etc., with assistance from our regional offices in developing countries and emerging markets and through our global network of advisers.
- We provide continual know-how and active support to the project companies.

IFU as a fund manager

IFU is fund manager for the Arab Investment Fund (AIF), IFU Investment Partners (IIP), the Danish Climate Investment Fund (KIF) and the Investment Fund for Central and Eastern Europe (IØ). Any projects under these funds are included in the reporting below.

IØ was founded in 1989. The Danish government decided in 2010 that IØ's activities are to be phased out, and IØ cannot enter into new commitments. However, IØ still has a portfolio of projects and is a signatory to the UN Global Compact.

Sustainability reporting

This Communication on Engagement, required annually of all signatories to the UN Global Compact, constitutes IFU's mandatory reporting as required by the Danish Financial Statements Act, section 99 a (7).

New sustainability policy

In 2014, IFU reviewed its CSR policy and updated it to a Sustainability Policy, which now provides the framework for the environmental, social and governance (ESG) requirements in the companies in which IFU invests. IFU is committed to ensuring that investees reduce sustainability risks, contribute to sustainable development and in general achieve high sustainability standards, which IFU believes adds value to the investee and enhances business opportunities.

IFU is a signatory to the UN Global Compact, and our commitment to this important UN initiative remains undiminished.

IFU promotes the Global Compact principles through its investments and thereby strives to create shared value by:

- respecting and promoting all basic human rights, including labour rights and occupational health and safety, and addressing adverse human rights impacts that the investment may cause or contribute to as outlined in e.g. the UN Guiding Principles on Business and Human Rights;

- enhancing positive development effects, including the creation of jobs and income, payment of taxes, contribution to government revenue, transfer of know-how and cleaner technologies, training and education, gender equality, community health and food security and other corporate social responsibility-related activities;
- securing corporate governance and business ethics, including anti-corruption, anti-fraud, transparency and stakeholder engagement;
- improving environmental performance through a preventative and precautionary approach that addresses environmental challenges, including climate change, loss of biodiversity and land use changes; and
- ensuring good animal welfare, including proper treatment of animals used for food production and for other commercial purposes and testing.

The investees must continuously work towards achieving satisfactory long-term results in sustainability, and such activities must be anchored in the business plan.

Working towards international standards

Identifying sustainability impacts is an integrated part of IFU's appraisal process, and we expect our partners to share IFU's aspirations regarding sustainability. IFU requires investees to comply with national regulations in the host country in which they operate and to work towards

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A grant from the Danida CSR Training Fund, managed by IFU, helped finance OHS training at Kosan Crisplant in Cameroon. Read more about Danida grants on page 6.

implementing relevant international standards. IFU defines international standards as standards based on UN, ILO and OECD conventions, declarations, agreements and principles. International standards could be the IFC Performance Standards or other credible, globally or regionally recognised standards that encourage continual improvements. For each investee, international standards are defined as specifically and operationally as possible.

During the appraisal process, IFU assesses the impacts and mitigation measures related to the investment considering factors such as the sector, technology, location, host country regulations, climatic conditions and cultural issues. This process identifies significant issues that are relevant for the project, and an assessment is made of which international standards the investee needs to comply with. In case of gaps, an action plan with a reasonable time frame to meet these standards and comply with IFU's sustainability requirements is prepared. The action plan must be adopted before IFU disburses its financial contribution.

IFU works actively to overcome challenges and dilemmas

IFU works with projects in several developing countries and is aware of potential challenges and dilemmas in relation to sustainability. Therefore, addressing significant sustainability issues in a responsible business plan is crucial for a project to achieve a satisfactory long-term result, and it is the objective of IFU's sustainability efforts to assist its partners in setting up clear sustainability strategies that benefit the company.

Implementing this sustainability objective in a company's business strategy helps reduce the risk to the business, but it can also make a company more profitable and generate business opportunities. A fair salary can minimise costly employee turnover, saving energy can reduce expenses, and high health and safety standards can limit loss of working days of employees and increase productivity. A good reputation may also create new business.

UN Guiding Principles on Business and Human Rights

In 2013, IFU updated its due diligence tools – the UN Global Compact Self-Assessment tool – making it consist-



Training session at Restaurant Gustu in Bolivia.

ent with the UN Guiding Principles on Business and Human Rights and putting a broader human rights lens to contextual and linked risks to a project. Furthermore, in 2014, IFU added a couple of other UN Guiding Principles-related adjustments to its sustainability processes:

IFU decided to launch a formal grievance mechanism; and IFU sharpened its requirements to projects meaning that they must have their own sustainability policy in place and adequate systems and qualified staff to implement and enforce this policy.

Assessment of sustainability performance

Each year, IFU carries out an internal assessment of its portfolio on compliance with its sustainability policy. Each project is classified into one of five categories as follows: Excellent, Good, Fair, Poor and Critical.

In 2014, compliance assessments were carried out for 165 IFU projects and projects in IFU managed funds (excluding IØ). The exercise did not include 13 projects that were in the process of being established, 13 projects with no physical activities or inactive for other reasons, and six projects being exited. Furthermore, it did not include IFU's three investments in own managed funds. Similarly, for IØ, compliance assessments were carried out for 26 IØ projects. The exercise did not include one project with no physical activity.

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Sustainability classification	Total score (%)		Environment (%)		OHS (%)		Human rights and labour practices (%)		Anti-corruption (%)	
	IFU	IØ	IFU	IØ	IFU	IØ	IFU	IØ	IFU	IØ
Excellent	31	35	36	38	31	31	33	42	22	31
Good	51	53	46	50	50	58	50	46	59	58
Fair	16	11	17	8	17	11	14	12	16	11
Poor	2	1	1	4	2	0	3	0	3	0
Critical	0	0	0	0	0	0	0	0	0	0

The classification is a combination of four separate classifications: 1) environment, 2) occupational health and safety (OHS), 3) human rights and labour practices and 4) anti-corruption.

The total scores in 2014 are very similar to those of last year. The Poor scores are related to six projects and related to a mix of conditions, including labour issues, safety issues and no adequate procedures to fight corruption, but also a lack of adequate reporting. Four of the eight companies that scored Poor in 2013 are no longer on the list because IFU has exited or improvements have been made. There are two new projects on the list. None of the projects scoring Poor are high risk projects, which are projects with significant potentially adverse sustainability impacts. The total scores of IØ are very similar to those of previous years. The Poor score is related to one project with specific environmental challenges.

More project companies prepare sustainability policies

IFU encourages its investees to prepare their own CSR or sustainability policy or to comply with a policy prepared

by their parent company. IFU started using this as a KPI in 2009, and every year since the number has increased.

There has been a change for 2014 in that the same number of companies is used for the assessment as for the assessment of sustainability performance, as explained above. Recalculated according to this new methodology, 71 per cent of the companies had a policy, which is seven percentage points higher than in 2013. IFU is proud of this development, and with the recent update of IFU's sustainability policy it has become a requirement that every investee must have its own sustainability policy. As a result, the number should grow even higher over the coming years.

Stakeholder engagement

IFU participates in several fora in order to monitor stakeholder expectations and keep up-to-date on developments in standards for good ethical conduct, dilemmas and risks. For this purpose, IFU is a member of the Danish Ethical Trading Initiative (DIEH).

IFU's own initiative is the IFU Sustainability Advisory Board, which has four members, each representing important IFU

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Members of the IFU Sustainability Advisory Board:



Dr Poul Engberg-Pedersen,
Development researcher



John Nordbo,
Head of Conservation Department,
World Wildlife Foundation, WWF



Allan Lerberg Jørgensen,
Department Director,
Danish Institute of Human Rights



Malene Østergaard,
Director, Group Sustainability,
Danfoss

stakeholder issues: human rights, environment, development and corporate policy. The advisory board meets regularly to discuss and advise on key issues, such as due diligence tools, supply chain dilemmas and anti-corruption and facilitation payments, and media communication.

Danida CSR Training Fund

IFU manages the Danida CSR Training Fund, which can provide training grants to IFU's project companies. In 2014, IFU made grant commitments for 11 CSR training programmes. The total annual budget is DKK 3m.

IFU FOCUS

IFU FOCUS is interactive seminars on sustainability and HR, facilitated by IFU and delivered in cooperation with international and local experts.

IFU FOCUS has run for five straight years from 2010-2014 and has covered six regions in Asia and Africa.

Sustainability and HR are important elements in building strong and sustainable companies. This often poses a challenge in developing countries, and in that sense IFU FOCUS provides an important framework for training, new insight and sharing of best practice. The seminars offer inspiration to sound business development within four key areas:

- Sustainability strategies and tools that work for the business
- People strategy, HR management and organisational development
- Avoiding bribes and facilitation payment
- Corporate governance

An IFU FOCUS seminar was held in New Delhi, India in February 2014. Subjects covered included benefitting from corporate CSR activities, corporate governance, middle managers and team leaders, bribes and facility payment and reward strategy.

Participants have mainly been management-level staff from the project companies, Danish partners, local partners and, depending on the size of the company, sustainability and HR managers. By the end of 2014, close to 340 people had participated in IFU FOCUS.

CSR Abroad award 2014

For the fourth time, the Danish CSR Foundation (CSR Fonden) organised a national CSR event, CSR Awards 2014, which served as an overarching award ceremony for granting CSR-related awards to people, organisations and companies in recognition of their contributions to excellent CSR initiatives.

IFU has taken part in this initiative from the beginning, and in 2014 IFU together with Danida and the Danish Trade Council established a special award, CSR Abroad, for sustainable investment in developing countries. An independent jury composed of experts on sustainability issues was appointed to determine the winner.

The award is granted to a company in a developing country, which has made a special effort within sustainable development and has demonstrated a strategic approach to sustainability while also in practice contributing proactively to the fulfilment of one or more of the international principles as defined in the UN Global Compact and the UN development goals – Millennium Development Goals.

In 2014, the winner was Scancom, Vietnam, which was nominated together with LM Wind Power, India and Danfoss, India.

In his motivation, the Danish Minister for Trade and Development highlighted Scancom's commitment to social policies in their own operations, their commitment to ensuring that best practice is implemented in their supply chain combined with their effort to promote the Forest Stewardship Council – FSC standards and make it a quality mark in the market.



Ole Lund Andersen, member of the board of Scancom International, accepted the CSR Abroad award on behalf of Scancom, Vietnam.

CASE

Gustu – a social impact business - living CSR

Gustu is a fine dining restaurant in the Bolivian capital of La Paz working exclusively with Bolivian products from all regions of the country to demonstrate to the world its diversity and richness.

Gustu is not a business with a department for CSR; it is a Social Impact Business. Its drive is not only to maintain a striving business, but also to generate positive outputs as a motor for Bolivia's socio-economic development. The Gustu Social Impact Business Program is constantly evaluating its footprint on the surrounding economy, environment and society, and Gustu has mechanisms to efficiently increase its positive impact. The Bolivian president has announced that Gustu is a source of Bolivian pride.

A showcase of Bolivia's true potential in food culture

Some 740,000 Bolivians earn their livelihood from family farming, and there is a huge potential for poverty reduction and improved food security. These family farms provide for 70 per cent of the internal Bolivian market demand, and they are the main providers of ingredients and other raw materials to Gustu.

All products used in Gustu's food and beverage services must be farmed, produced, grown, processed and developed on Bolivian territory and by Bolivian hands. Gustu works to source from small-scale producers, farmers and artisan businesses.

"By helping these small-scale producers gain access to greater commercial opportunities, we can boost employment and take them to the next level in terms of farming methodologies and technology and at the same time get excellent products for our restaurant," says Michelangelo Cestari, CEO of Gustu. ■

High sustainability standards

Living this objective and understanding the context in which the objective has to be fulfilled, Gustu has to maintain awareness of the sourcing of its products. Therefore, Gustu investigates the actors of the entire production chain to ensure fair prices for itself and its suppliers, providing feedback to the small-scale producers in order to motivate them to improve quality and production.

FACTS ABOUT THE INVESTMENT

Project name: Gustu Restaurant

Danish partner: Claus Meyer

Start: 2012

Country: Bolivia

Status: In operation

IFU's shareholding: DKK 3.7m

Expected total investment: DKK 6.7m

Expected direct employment: 37

A basic requirement in Gustu's efforts to improve the conditions is that providers must have proper legal status. They must have a transparent and honest organisational structure, good working conditions for their employees and make sure that children do not work on the farm. The products must be grown, farmed and produced under clean and healthy conditions. Gustu also helps train the farmers so that they can guarantee that environmental responsibility is undertaken during planting, growing and harvesting.

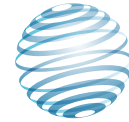
Quality products needed

Gustu works with its providers to fulfil a set of principles and accomplish all the necessary activities to being a social impact supplier. Gustu knows that it makes high demands on its providers, and that it is a difficult route to take for them, as especially the lack of logistics is a big challenge.

The supplier has a quality product that is ready for use by a restaurant, but they do not have the means to transport the product. They often resort to selling their product to an intermediary, who may not know about the diligent care needed to maintain the quality of the product, which means a lot of nutrients and taste and other values of the product may be lost. Such challenges must be solved in order to create proper commercial opportunities throughout the value chain for all parties.



Young Bolivians being trained at Gustu.



1. Scope

IFU is a development finance institution providing share capital participation, loans and guarantees on commercial terms to the private sector in developing countries and emerging markets. IFU's strategic objective is to be Denmark's main engine for shaping and enhancing sustainable and profitable private sector growth opportunities in developing countries in collaboration with Danish know-how, risk capital and commercial enterprises.

This sustainability policy defines sustainability - in the context of sustainable development - as the framework for the environmental, social and governance (ESG) requirements in IFU's investee companies, IFU-managed funds and their investee companies (hereafter collectively referred to as investees) and strives to achieve high sustainability standards. IFU's board of directors, management, employees and advisers must act in accordance with this policy.

2. Commitment to sustainable development

IFU is committed to ensuring that investees reduce sustainability risks and contribute to sustainable development, which IFU believes adds value to the investee and enhances business opportunities.

The investees must continuously work towards achieving satisfactory long term results within sustainability, and such activities must be anchored in the business plan. Investees should contribute to creating jobs and income, improving corporate governance, sound environmental and social performance and development in the local community.

IFU has signed up to the UN Global Compact principles. IFU promotes these principles, and through its investments IFU strives to create shared value by:

- Respecting and promoting **all basic human rights**, including **labour rights** and **occupational health and safety**, and address adverse human rights impacts that the investment may cause or contribute to. This includes providing for or cooperating in the remediation of affected individuals and communities.
- Enhancing **positive development effects**, including creation of jobs and income, payment of taxes, contribution to government revenue, transfer of know-how and cleaner technologies, training and education, gender equality, community health and food security and other corporate social responsibility related activities.
- Securing **good corporate governance and business ethics**, including **anti-corruption**, anti-fraud, transparency and stakeholder engagement.
- Improving **environmental performance** through a preventive and precautionary approach that addresses environmental challenges, including **climate change**, loss of **biodiversity** and land use changes.
- Ensuring good **animal welfare**, including proper treatment of animals used in food production and for other commercial purposes and testing.

In this way IFU seeks to contribute to the UN Millennium Development Goals and the UN Sustainable Development Goals.

3. Appraisal process

Identifying sustainable development effects is an integrated part of the appraisal process, and IFU expects its partners to share IFU's aspirations regarding sustainability. IFU requires investees to comply with national regulations in the host coun-

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try in which they operate and work towards implementing international standards. International standards are based on UN, ILO and OECD conventions, declarations, agreements and principles. Standards could include the IFC Performance Standards or other credible, globally or regionally recognised standards that encourage continual improvements. For each investee, international standards are defined as specifically and operationally as possible.

During the appraisal process, risks, impacts and mitigation measures related to each investment are assessed, considering factors such as the sector, technology, location, host country regulations, climatic conditions and cultural issues. This process identifies the significant issues that are relevant for the investee, and an assessment is made of the extent to which international standards are or will be implemented. An action plan with a reasonable time schedule to meet these standards and comply with IFU's sustainability requirements¹ is elaborated, as appropriate for each investee. The action plan must be approved by the project partners, including IFU, and is a condition for IFU's disbursement.

4. Sustainability requirements

In order to implement IFU's sustainability policy, IFU requires investees to:

- Operate in compliance with host country regulations.
- Comply with international standards for significant issues identified during appraisal.
- Adopt a written sustainability policy approved by their board of directors or similar governance body, which is communicated to relevant stakeholders.
- Appoint a person with overall responsibility for sustainability, including the management of activities and resources and delegation of tasks.
- Establish a system to ensure continuous improvement and implement sustainability decisions relevant to the company size and sector as well as the environmental, economic, cultural and social context in which the activity operates.
- Promote sustainability issues in interaction with suppliers and business partners.
- Prepare an annual report that provides a status on sustainability issues, including the implementation of the action plan, for discussion and approval by their board of directors or similar governance body. A copy of the report must be sent to IFU.

5. Exclusion list

IFU will not finance activities that are set out in IFU's exclusion list.²

6. Active ownership

IFU seeks active ownership of investees through board membership, where IFU shares and disseminates its experience, facilitates networking and partnerships regarding the business environment and sustainability issues. Where IFU is a lender only, IFU also works to have a similar influence as when IFU is a shareholder.

IFU monitors each investee's sustainability activities through visits, reports and dialogue to ensure improvements over time. In case an investee breaches this policy, IFU is entitled to take the necessary measures, including exiting the investment.

IFU has developed a number of tools and templates to support sustainability efforts in investees, and draws on its regional offices and global network of advisers.

7. Stakeholder dialogue

IFU is committed to stakeholder engagement and will, where appropriate, engage in policy dialogue with all relevant stakeholders in society on issues related to sustainability. IFU seeks continuous dialogue with its stakeholders to keep up to date with developments within sustainability to be able to take qualified decisions and act proactively on stakeholder concerns.

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IFU cooperates with other development finance institutions to harmonise environmental, social and governance procedures. Harmonisation improves efficiency during appraisal, monitoring and the engagement process, as well as simplifies and increases negotiation leverage towards investees.

8. Transparency and accountability

IFU provides transparent, accountable information about IFU's sustainability activities and performance and continuously endeavours to improve the quality of this information.

IFU encourages investees to be transparent and informative about their business and performance in order to create the best possible platform for a continuous and proactive stakeholder dialogue.

9. Grievances

Complaints related to investees should be promptly addressed in a manner that is fair, objective and constructive. IFU encourages investees to establish a procedure to handle complaints by individuals and communities, who may be adversely affected by the activities of the investee. If the investees do not effectively respond to complaints, IFU has a grievance mechanism through which stakeholders can report alleged breaches of this policy.

The above policy was approved by IFU's Board of Directors on 20 November 2014.

1) Specified in IFU's Sustainable Investment Handbook, which can be found at <http://www.ifu.dk/en/sustainability-handbook>

2) IFU has adopted the EDFI exclusion list, which can be found at <http://www.ifu.dk/en/exclusion-list>