Annex O: The Investment Fund for Developing Countries

Contents

1. Overview of IFU and time-line of Danish support

The Investment Fund for Developing Countries (IFU) was established by the Danish government in 1967, and in 2019 had DKK 4.2 billion in equity from the Danish national bank guaranteed by the state. It is governed by a board appointed by the Minister for Development Cooperation and offers advisory services and risk capital to companies to encourage and enable economic growth and social progress in developing countries. As well as managing its own capital, the IFU manages several other public or public-private investment funds as a minority shareholder, and this gives it opportunities to exert considerable leverage beyond its own portfolio. In 1967-2015, the IFU had a fully-tied mandate, meaning that it could invest only in association with Danish companies or other Danish interests (Table 1). Since then, it has had an untied mandate and permission to invest in all developing countries, including the lower-income segment of upper middle-income countries. This allowed rapid expansion, with annual investment volume rising above DKK 1.2 billion in 2016 and 2017, and the number of government and public-private partnership funds and facilities involved rising to 11 in 2017.

Table 1: Overview of mandate changes for IFU, 2005-2017

Period	Country mandate	Tied/untied
2005-2010	Focus on poor developing countries: mainly LICs and LMICs.	Fully tied
2011-2014	At least 50% of investments in poor developing countries (LICs and LMICs), and other investments in UMICs (up to 50% GNI limit) are allowed.	Fully tied
2015-2017	At least 50% of investments in poor developing	Partially untied (Danish

	countries (LICs and LMICs), and other investments in all UMICs are allowed.	interest 2015 and 2016) and fully untied in 2017.

Source: MFA (2019: 97).

2. Capacities and priorities of IFU

The IFU offers two types of investments: (1) direct investments in project companies in the form of share capital and loans; and (2) indirect investments in private equity funds (up to 20% of portfolio value), which act as fund managers and invest in projects on behalf of IFU and other partners. IFU also manages funds on behalf of investors such as Danish pension funds, and they include the following (IFU, 2019a):

- **The Investment Fund for Central and Eastern Europe (IØ)** was established in 1989 with equity of DKK 0.1 billion but is being wound down.
- **The Danish SDG Investment Fund** was established in 2018 with committed capital of DKK 4.9 billion (3 billion from private pension funds, 0.1 billion from MFA development aid, a loan of 0.8 billion from the Danish national bank guaranteed by the State, and the remaining 1 billion from IFU itself). Its purpose is to invest in projects in developing countries that support the Sustainable Development Goals (SDGs), and especially in the areas of food and farming (SDG 2), water and sanitation (SDG 6), sustainable infrastructure (SDG 9), responsible production (SDG 12), climate action (SDG 13), and the financial sector (as an enabling strategy for the others).
- **IFU Investment Partners (IIP)** was established in 2012 with committed capital of DKK 0.5 billion to serve as a co-investor in large IFU projects and a tool for Danish companies to raise additional equity funding in a one-stop process. The investment period ended in 2017.
- **The Danish Agribusiness Fund (DAF)** was established in 2016 with the purpose of investing in agribusiness projects in developing countries across the value chain 'from farm to fork' (committed capital at inception DKK 0.8 billion).
- **The Danish Climate Investment Fund (DCIF)** was established in 2014 with committed capital of DKK 1.3 billion to invest in climate-related projects in developing countries. The investment period ended in 2018.

Since it started, IFU has invested in 1,300 projects in more than 100 countries, with DKK 210 billion in project investments of which the IFU contributed DKK 23 billion in share capital, loans and guarantees. In 2019, new contracted investments by IFU and IFU-managed funds amounted to DKK 1.1 billion in 25 projects, and by the end of that year the active portfolio covering all funds contained 196 projects (Table 2). More than half of these were greenfield investments, and 38% were in Africa, 34% in Asia, 11% in Latin America, and 12% were in Eastern Europe, mainly Ukraine. The last 5% of projects represented investments in companies operating in more than one country.

Table 2: Active IFU portfolio at end 2019 (projects)

Fund	Projects
IFU	170
Danish SDG Investment Fund (SDGI)	8
Danish Climate Investment Fund (DCIF)	13
Danish Agribusiness Fund	5
IFU Investment Partners	3
Investment Fund for Central and Eastern Europe	7

Source: IFU (2019a).

In addition, Danida Sustainable Infrastructure Finance (DSIF) was set up by the Danish Government in 1993 to offer financing on favourable terms to developing countries for 'sustainable infrastructure' projects that not otherwise be commercially viable. Since September 2017 it has been managed on behalf of the MFA by a team inside IFU, but the strategic framework and the authority to allocate funds to individual projects remains with the MFA. DSIF had several previous names, most recently and until January 2020 Danida Business Finance (DBF), which therefore features in documents used by the evaluation.

DSIF continues to operate as an instrument to facilitate or make investments that deliver "measurable results toward the SDGs that create growth and employment in developing countries" in specified countries that include Ethiopia, Indonesia and Vietnam[1]. Only projects that are commercially non-viable can be financed, and two tracks are available, one in which the tender is limited to Danish companies ('DSIF Classic'), and one in which there is an international tender won by a Danish company, which can then attract DSIF support ('DSIF Fast Track'). With annual capital availability defined by parliament and the national budget, a typical ten-year DSIF financing agreement covers interest payments on the commercial loan, export credit premiums and other financial costs, and is accompanied by a cash grant to meet OECD criteria for aid (IFU, 2019c).

3. Effectiveness of IFU mitigation efforts

The MFA is responsible for policy guidelines, supervision and oversight of IFU, and the Minister for Development Cooperation appoints its Board and Chair. Apart from defining its mandate, however, the MFA has never developed explicit policy guidelines for IFU. Despite arrangements on paper, government oversight was quite limited until 2017 when the MFA developed a strategy for IFU for 2017-2021 with specific defined outcomes (MFA, 2019). There was an evaluation of the IFU's activities in 2004-2017 (MFA, 2019), and highlights of its findings are given in Box 1.

[1] www.ifu.dk/en/danida-sustainable-infrastructure-finance-en/

Box 1: Highlights of the MFA (2019) evaluation of IFU.

"Development needs from partner countries were mainly taken into account through the assumption that direct and indirect employment would be created and that the transfer of know-how and adoption of [Corporate Social Responsibility, CSR] standards would promote development in host economies. IFU indeed aimed pro-actively to promote the adoption of CSR standards and to mitigate negative development results. Investment proposals, however, were not selected on the basis of the highest potential development impact." (pages 99-100).

But case studies showed "good to moderate CSR performance (only 12% shows poor performance). Most attention is paid to good labour conditions incl. training of staff, environmental measures such as energy efficiency and adequate waste management, and a large variety of community engagement actions." (page 100). Nevertheless, it was found that IFU's exit evaluations hardly paid attention to development outcomes, other than direct job creation.

For climate and environment specifically "the most important indicator agreed upon is the reduction of GHG emission, which is ex-ante calculated for all DCIF investments by an independent firm. The annual DCIF reports (2014-2017) indicate that expected GHG savings add up to 33,055,000 tCO2e over the entire 20-30 years lifetime of the projects . In [European Development Finance Institutions] there is a strong move to report actual annual savings and IFU intends to capture these in the [Annual Sustainability Reports] in the near future. It is not clear whether ex-post calculations for some or all investments will be carried out." (page 83).

"[The] main positive development outcomes "were job creation, transfer of (Danish) technology and knowhow, [unspecified] climate effects and sector effects such as better access to energy. It is estimated that IFU contributed to the creation of 80,000-100,000 jobs from 2007 to 2017. Most positive outcomes were found in specific sectors where investments in companies contributed to catalysing effects in the value chain or at sector level such as improved capacity and income for smallholders and access to clean and affordable energy for households and enterprises. These effects are most noticeable in the energy sector and to some extent in agribusiness." (page 13).

Source: MFA (2019).

The findings in Box 1 suggest that IFU investments have made a positive contribution to mitigation, but without specific baselines, targets, measurements and value-for-money calculations it is not possible to quantify these effects. Going forward, there was the commitment in line with MFA's 2017 strategy (*The World 2030*) whereby a main objective of IFU would be to "promote investments that support sustainable development in developing countries and contribute to the realisation of SDGs". The subsequent Sustainability and Impact Report (IFU, 2019a: 8-9), based on its sustainability and climate policies, confirms the following commitments and key performance indicators (KPIs) in support of relevant SDGS:

- For SDG 7 (clean energy), "Increasing the share of climate-relevant projects like renewable energy, energy efficiency and climate adaptation to at least 40 per cent of IFU's portfolio by 2030" with the two KPIs of (a) "Installed capacity of renewable energy sources and expected GHG savings during lifetime", and (b) "Share of direct investments that have measures to reduce energy consumption."
- For SDG 13 (climate action), "mobilising climate-relevant private investments to support developing countries' transformation to low-carbon and climate-resilient pathways by

leveraging substantial financing to mitigation and adaptation projects", with the KPI of "Number of contracted climate investments."

These commitments would be expected to be leveraging significant mitigation impact, and IFU's own summary of its activities on climate are contained in Box 2.

Box 2: IFU activities and results in promoting climate stability

"In recent years, IFU has increased its investments in wind and solar projects in several developing countries like Kenya, Pakistan, Egypt and Mongolia.

"In 2019, IFU contracted four climate investments; three new investments and one additional financing for phase two of an ongoing project. Excluding one platform investment in a company working globally, where calculation is not yet possible, the investments will install renewable energy capacity of 336 megawatt and are expected to produce more than 1,000 GWh per annum when fully operational. In total, the projects are expected to represent GHG savings of approximately 9,500,000 tCO_2e during their lifetime.

"In total, IFU's current portfolio includes renewable energy projects with an overall capacity of 1,160 megawatts distributed on 680 megawatts in wind power and 480 megawatts in solar power.

"From 2020, IFU will no longer make new investments in fossil fuel-based power production to the grid. IFU can, however, in a transition period until 2023, invest in transitional hybrid technologies, e.g. gas, in combination with renewables for power production, if strong development impact criteria are met.

Aligned with the Paris Agreement such criteria could be that the investment is in a low-income country, and it is in accordance with the country's national long-term energy plans, and that it meets an acute energy need or secures broader access to energy.

"IFU assesses the climate impacts of its investments by calculating the GHG emissions they cause and by identifying climate change-resilient technologies and adaptation measures to be put in place as part of the investment.

"Projects are required to take all necessary measures to ensure that the project is energy efficient, thereby reducing contributions to global warming to a minimum. The project should over time work towards a level in line with best practice within its sector or set a goal of reducing its CO_2 emissions. During appraisal, IFU estimates the absolute carbon emissions and savings of the project. The estimations are calculated by an independent consultant.

"Projects emitting more than 25,000 tonnes of CO_2 equivalent annually are required to monitor and report on emissions to IFU. The information on emissions will be used to discuss how to reduce the emissions in terms of choice of technology, introduction of mitigation measures, etc.

"In 2019, 59 per cent of the direct investments reported that they have measures to reduce energy consumption. Examples of measures include installation of energy-efficient production equipment and solar panels, use of LED light bulbs and motion sensors to switch off lights and energy saving awareness campaigns and training of employees."

Source: IFU (2019a: 14). See also: https://www.ifu.dk/en/impact/.

4. Conclusion on effectiveness of Danish support

Since the 2019 evaluation, IFU has improved its monitoring efforts and published its first Sustainability and Impact Report (IFU, 2019a). It has also published a Climate Policy (IFU, 2019b) which states that IFU will make "its investment flows consistent with a pathway towards zero GHG emissions and climate-resilient development" (page 1), while increasing the share of climate-relevant projects in its investment portfolio. Such projects will follow the definitions of the multilateral development banks, but the examples given are "renewable energy, energy efficiency and climate adaptation/resilience projects" (page 1). The policy also says that "IFU will promote renewable energy investments and investments in greener technologies", phasing out fossil fuel and hybrid power production technologies from 2020 in alignment with each country's NDC while meeting "acute energy need or secures broader access to energy" (page 2). This strong energy sector mitigation focus is consistent with the past performance noted above.

The policy notes, however, that IFU will also "seek to offset carbon-emitting investments by combining them with renewable energy and carbon sequestering components such as forestry projects in order to be on a path to carbon neutrality at project level." (page 2). Annexed to the *Climate Policy* is a list of eligible actions that include mitigation-relevant aspects of agriculture and forestry but given the policy's focus on energy it is unclear to what extent this can be expected to be reflected in the portfolio, other than as a potential off-set for residual or unavoidable GHG emissions in the energy sector[2]. This is a useful aim but would not on its own qualify IFU as a significant mitigation actor in the LULUCF sector.

Interviews in October 2020 confirmed that IFU is increasingly investing resources in the design phase of its investments, so as to ascertain direct GHG emissions and sustainable benefits, while also undertaking holistic analyses to guide sustainability and impact efforts. Approval processes now include presentation of full baselines including GHG emissions, and implementation phases will include monitoring of impact and outcomes.

This is made necessary partly by international standards that require large companies to measure their emissions, and the lessons from IFU's attempts to comply with those standards may be relevant to other public mitigation actions. the evaluation concluded that IFU is building a capacity to consider, analyse, predict and prioritise its investments in line with climate emergency priorities. This has the potential to make IFU a valuable partner of a Danish government that is raising its climate mitigation ambitions.

[2] Among a total of 839 projects in Africa, Latin America and Asia, the IFU portfolio included a small number of investments in logging and primary wood products companies in Brazil, Congo Republic, Côte D'Ivoire, Ghana, Indonesia and Malaysia, and farming (excluding plantation) enterprises in Brazil, Guyana, Kenya, Nicaragua, Nigeria, Perú, Senegal, South Africa, and Togo (https://www.ifu.dk/en/investments/). The mitigation significance of these cannot be assessed without a detailed inspection of the projects, many of which have now closed.

Annex a: Information sources for the review

This review is based on interviews with **Lars Christian Oxe** (IFU Senior Impact Advisor, 25 Sep 2020, 28 Sep 2020 and 7 Oct 2020), **Shahid Abdullah** (DSIF Investment Director, 28 Sep 20), **Annelise Boysen** (DSIF Investment Director, 28 Sep 20), and **Mikkel Kallesøe** (IFU Vice President, Sustainability and Impact, 7 Oct 20), and on study of the IFU web-site (www.ifu.dk) and documents downloaded from that source or provided by MFA, including its most recent evaluation (MFA, 2019), and the IFU's 2019 *Sustainability and Impact Report* (IFU, 2019a), *Climate Policy* (IFU, 2019b) and *Annual Report* (IFU, 2019c).

Abbreviations and acronyms (IFU)

CSR	Corporate Social Responsibility
DAF	Danish Agribusiness Fund
DCIF	Danish Climate Investment Fund
DKK	Danish Krone (plural Kroner)
DSIF	Danida Sustainable Infrastructure Finance
GNI	Gross national income
IFU	Investment Fund for Developing Countries
IØ	Industrial Fund for Central and Eastern Europe
IIP	IFU Investment partner
KPI	Key Performance Indicator
LED	Light-emitting diode
LIC	Low income country
LMIC	Low-middle income country
SDG	Sustainable Development Goal
UMIC	Upper-middle income country

Bibliography (IFU)

IFU (2019a) *IFU Sustainability and Impact Report*. Investment Fund for Developing Countries (Copenhagen).

IFU (2019b) *IFU Climate Policy 2019*. Approved by IFU's board of directors on 31 October 2019, with effect from 1 January 2020. Investment Fund for Developing Countries (Copenhagen).

IFU (2019c) *Annual report 2019*. Investment Fund for Developing Countries (Copenhagen).

MFA (2019) *Evaluation of the Investment Fund for Developing Countries (IFU) 2004-2017, March 2019*. Carnegie Consult and Ministry of Foreign Affairs of Denmark (Copenhagen).