

# IFU Capital Contribution 2024-2030

**Key results:**  
Create positive developmental and climate effects together with other actors in developing countries that would not be possible under existing market conditions towards 1) building green economies, and 2) building just and inclusive economies.

**Justification for support:**  
Based on an annual capital contribution of DKK 500 mill. towards 2030 IFU will mobilise significant non-ODA capital, which supported by a continued organisational development within IFU, will scale up investments substantially within priority sectors and deliver significant results on climate change and development indicators. Moreover, IFU will be able to attract additional private capital and thereby further increase its portfolio substantially in terms of scope.

**Major risks and challenges:**

Contextual:

- Macroeconomic downturn across emerging markets. IFU will mitigate this risk by supporting companies with services that are essential also during a downturn.

Programmatic:

- Insufficient demand for investment finance. IFU will mitigate this risk by developing stronger networks on the ground, finding partners, and cooperating with peers including other DFIs.

Reputational:

- IFU does not allocate sufficient resources to grow the supportive functions in the organization. To meet this risk, active ownership with regular consultations between IFU and Ministry of Foreign Affairs will take place.

<b>File No.</b>								
<b>Country</b>	Global							
<b>Responsible Unit</b>	GDK							
<b>Sector</b>	Climate, decent jobs, economic growth							
<b>Partner</b>	Investment Fund for Developing Countries (IFU)							
	<i>DKK million</i>							
<b>Commitment</b>	24	25	26	27	28	29	30	<b>Total</b>
	500	500	500	500	500	500	500	3,500
<b>Projected disbursed</b>	500	500	500	500	500	500	500	3,500
<b>Duration</b>	November 2024 – 2030							
<b>Previous grants</b>	Latest general capital contribution: 115 million DKK in 2023							
<b>Finance Act code</b>	§06.38.01.11							
<b>Head of unit</b>	Karin Poulsen							
<b>Desk officer</b>	Jakob Tvede							
<b>CFO</b>	Rasmus Tvorup							
<b>Relevant SDGs</b>								
								
No Poverty	No Hunger	Good Health, Wellbeing	Quality Education	Gender Equality	Clean Water, Sanitation			
								
Affordable Clean Energy	Decent Jobs, Econ. Growth	Industry, Innovation, Infrastructure	Reduced Inequalities	Sustainable Cities, Comm	Responsible Consumption & Production			
								
Climate Action	Life below Water	Life on Land	Peace & Justice, strong Inst.	Partnerships for Goals				

**Objective**

Create positive developmental and climate effects together with other actors in developing countries that would not be possible under existing market conditions towards 1) building green economies, and 2) building just and inclusive economies. On the basis of an annual capital contribution of DKK 500 mill. annually, IFU will scale up investments in priority sectors across all instruments and facilities, supported by increased mobilisation of private capital, access to state on-lending facilities, and a simultaneous continued organisational development within IFU.

**Environment and climate targeting**

	Climate adaptation	Climate mitigation	Biodiversity	Another green/environment
<b>Indicate 50% or 100%</b>	(TBD)	(TBD)		

**Justification for choice of partner:**

The Government has decided to reform its development finance institution, IFU, towards 2030. The ambition is that IFU becomes a leading impact investor, increasing its ability to deliver on central Danish priorities in relation to climate finance, support to Africa, the Least Developed Countries and Fragility and Conflict-Affected Countries (FCACs). IFU has over the last 5-6 years gained experience and built a foundational capacity with new investment instruments, which IFU can build further upon as it scales up activities in line with the reform ambitions. The goal is that IFU operates as One IFU, applying its different investment instruments to deliver on the objectives set in the Ownership Document.

**Summary:**

The MFA will provide an annual capital contribution of DKK 500 mill. This will allow IFU mobilise significant additional non-ODA finance to scale up investments across all instruments and facilities and within defined priority sectors in line with IFU investment strategy, sustainability strategy and Ownership document as represented in IFU strategy 2024-2026. On this basis, IFU will contribute to Green Economies as well Just and Inclusive economies with respect to existing national policy frameworks in the countries where IFU invests. Documentation will be based on IFUs impact measurement system for return of investments and key indicators related to climate and development. On this basis, and supported by a qualitative and quantitative organisational developments, IFU is expected to become a leading European DFI, and to have created the environment for attracting capital and a critical mass of actors to support climate and development action.

**Budget (DKK million):**

Engagement 1 – IFU Capital Contribution 2024-2030 (7*DKK 500m.)	3500.00
<b>Total</b>	<b>3500.00</b>

**DRAFT**  
**Programme Document**  
**(Concept Note)**

**IFU**  
**Capital Contribution 2024-2030**

**17 February 2024**

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# 1 Introduction

The present framework document outlines the background, rationale and justification, objectives, and management arrangements for the capital contribution as agreed between IFU and the Ministry of Foreign Affairs of Denmark (MFA) for a seven-year period covering 2024 to 2030 with an expected annual capital contribution of DKK 500 mill. amounting to a total of DKK 3,500 mill. by 2030.

## 1.1 The IFU reform process:

The Government has decided to reform its development finance institution, IFU, towards 2030. The ambition is that IFU becomes a leading impact investor, increasing its ability to deliver on central Danish priorities in relation to climate finance, support to Africa, the Least Developed Countries and Fragility and Conflict-Affected Countries (FCACs). Over the coming years, IFU will significantly increase its ability to reach development and climate goals: IFU will grow in terms of the amount of capital under management, have more instruments to reach different segments in different markets, and blend these instruments with a higher degree of flexibility. IFU will support this by developing its organisation in line with the current 2024-2026 IFU strategy. This will be further elaborated towards 2030, as continued organisational development is an integral and necessary part of the financial strengthening (for more information see section 7.2 in this document). The organisational development will increase the number of staff and strengthen in-house competencies on climate and development, including an added emphasis on establishing more regional offices, governance, communication and impact measurement. This will also enable IFU to deliver on its climate policy of a net-zero investment portfolio by 2040.

In August 2023, the Minister for Development Cooperation and Climate Policy approved a new Ownership Document, with the purpose to set the strategic direction for the Minister's ownership of IFU in line with the mandate of the organisation. In parallel, in September 2023, the Government approved a reform of IFU – initiated by the Minister in the beginning of 2023 and foreseen in the Strategy for Denmark's Development Cooperation, *The World We Share* from 2021. The reform will enable IFU to significantly increase its impact investments in support of the green transition and sustainable development. A long-term capitalization strategy with new funding from three sources will underpin the reform:

**Table 1: IFU financing sources**

Financing source	Use
1) Official development aid (ODA)	• Capital contribution of DKK 500 mill. pr. year from 2024-2030 (total of DKK 3.5 bn.)
2) Central Bank of Denmark (on-lending)	• Expanded access to state loans of up to DKK 7.5 bn. towards 2030 • Contribution to a new SDG Fund via state loans of DKK 800 mill. • IFU takes over as lender on DSIF projects via state loans of up to DKK 5.4 bn. towards 2030 <sup>1</sup>
3) Private institutional investors	• Mobilisation of DKK 3 bn. from Danish institutional investors for a new SDG Fund.

Combined, the total additional funding to IFU towards 2030 amounts to more than DKK 20 bn. on IFU's balance sheet, and IFU's capital under managements will grow from current 15.6 bn. DKK to 36.2 bn. DKK by 2030. This capitalisation plan will allow IFU to long-term strategic planning and also bring IFU's size at par with the average of other European DFIs<sup>2</sup>. In addition, the government decision also implies a change in IFU's dividends policy, by which IFU no longer pays dividends to the state, but can retain future earnings for new investments.

In parallel, and as an integral part of the reform process, the MFA together with IFU has taken initiative to integrate a number of IFU instruments into IFU's core business. This includes:

- 1) Reviewing the pilot of the development guarantee instrument (Q3-Q4 2024) as a basis for deciding to make the guarantee instrument permanent

<sup>1</sup> The MFA is currently analysing ways to strengthen the governance around DSIF and DSIF's organisational setup.

<sup>2</sup> Measured in absolute numbers

- 2) Redesigning IFU's project development program (PDP) and integrate the PDP into an independent setup in IFU, IFU Impact Ventures (IIV). KLIMA will present IIV to UPR parallel to this program document.
- 3) Exploring new modalities for IFU's existing SME facility so it fits IFU's new mandate
- 4) Strengthening DSIF's development mandate and increasing its financing possibilities via integration of DSIF into IFU and untying DSIF from solely being able to execute projects with Danish partners. KLIMA will present a separate program document to UPR in Q3 2024.

## 1.2. The Program Document

This program document is a framework document for the annual capital contributions of IFU for the period 2024-2030 and will serve multiple purposes: It forms the basis for the Council for Development Policy's (UPR) approval of the first annual capital contribution for 2024 of DKK 500m. For the subsequent six capital contributions (2025-2030) the intention is to use the same document for an annual confirmation of the continued approval by UPR. The document will be updated annually based on the ongoing monitoring by the MFA. IFU will each year appear before UPR to account for progress of the reform of IFU, and provide updates on results achieved based on an update of the result framework in the Framework Document. In its annual consultations with the UPR, IFU will report on results for the year, relevant changes in context, critical assumptions and risks, and explain lack of results together with planned remedial action. The annual consultations will also focus on key issues such as organisational change, impact measurement, communication, and system developments in IFU. On that basis, UPR will approve the capital contribution for the following year. In addition, the MFA plans two reviews for in the period 2024-2030 that can look at progress more in-depth, and which can address concerns, which UPR may raise during the annual consultations.

## 1.3 The new role of IFU in the context of Government policies:

IFU's raison d'être is to deliver impact and provide financing for the private sector where the private sector alone may not be willing or able to invest due to perceived risks or inadequate returns. In that respect, IFU's role is to invest alone, with other DFIs and MDBs or with the private sector to overcome barriers to investments in developing countries (OECD DAC countries). By providing initial funding or risk-sharing mechanisms to investments in countries with higher risk profiles such as in Sub-Saharan Africa, IFU encourages private investors to participate in projects that they might have otherwise considered too risky or uncertain. IFU also mobilises private finance directly from Danish pension funds and other private investors such as e.g. the SDG Fund launched in 2018.

The impact focus is to invest in projects/businesses that promote low-carbon, climate resilient inclusive growth and supporting projects with potential socio-economic benefits that purely profit-oriented entities may not adequately served.

Since its creation in 1967, IFU has reinvested returns from investments into new investments. Occasionally, IFU has paid dividends to its owner, the Danish state, and at other times the MFA has injected new capital into IFU. When the Government decided to untie IFU from only investing with Danish companies in 2017, it also laid the foundation for the current reform of IFU. Between 2017 and up until 2023, IFU has raised funds from the private sector, has delivered on a number earmarked contributions (e.g. High Risk – High Impact, India Climate Finance Initiative), has taken over administration of DSIF and launched the development guarantees pilot facility, all of which have been early exercises leading up to the current reform of IFU

In September 2023, the Government's Economic Committee approved the reform of IFU and the visions towards 2030 jointly submitted by the Ministry of Foreign Affairs and the Ministry of Finance. The reform sets out to deliver on concrete tasks in "The World We Share" (Danish Development Policy) such as climate action, inclusive economic growth, employment creation, gender equality and increased access to basic services for poor households. The reform is also aligned with the Danish Government's policy framework ("Ansvar for Danmark"/Responsibility for Denmark) the Danish foreign policy, and the Danish Government's policies for climate and the environment.

Moreover, IFU's portfolio related to climate action make up an essential part of the Danish contribution to the upcoming COP29, and has the potential to further support subsequent Danish international commitments on global climate action. In fact, IFU expects to be able to more than triple its contribution to mobilisation of private climate finance from its current DKK 2 bn. to DKK 6 bn. towards 2030.

IFU's current strategy runs from 2024-2026 and has a focus on e.g. strategic development, funding and mandates (incl. investment strategies), sustainability and organisational development. IFU will develop a new strategic plan covering the period 2026-2030 continuing the present work in areas such as "One IFU", tools to optimise investments, reach out

to a wider range of partnerships, long-term strategic planning and a strengthened organisation. The ownership document outlines the future mandate, role and relative independence of IFU.

During the period 2024-2030, IFU will continue the work on integrating key performance indicators on investments with data to document impact on development and climate goals. In this way, existing theories of change on investments, risk profiles and rates of return in financial markets will work in tandem with the theories of change, assumptions and indicators related to development and climate change to deliver results in all areas.

#### 1.4. Expected opportunities and development results from the reform

IFU operates in four priority sectors (green energy and infrastructure, health care, sustainable food systems and financing services) with the aim to contribute to two overarching impact objectives guiding the organisation across financial instruments and facilities: 1) the development of a green economy and 2) of a just and inclusive economy. IFU's projected growth including the proposed capital contribution and the different sources of capital gives IFU the possibility to broaden its range of financial instruments, and blend these to cater to different risk-profiles and private sector mobilisation factors.

The financial instruments/facilities range from the SDG Fund that mobilises highly commercial capital from regulated pension funds in larger scale impactful investments such as renewable energy. Microfinance focuses on markets and countries where risks are high compared to mature markets such as Denmark, but where risk are lower than in least developed countries. Other IFU facilities, as e.g. the High-Risk High Impact facility or investments done with IFU's own equity alone, has a higher risk appetite and focus on impact investments in markets such as lower income African and fragile countries.

IFU can also engage in early-stage companies (project development/impact ventures) and investments transforming markets (such as e-mobility, adaptation) where private investors are reluctant to invest, but where the ambition is to mobilise private investors over time and thereby eventually contribute to sustainable energy consumption.

Finally, IFU has funding dedicated to providing project development, technical assistance, IFU's development guarantees and concessional finance to DSIF's public sector investments in areas where the private sector cannot invest.

Since IFU became untied from investing with Danish companies in 2017, IFU has over the last 6-7 years gained experience and built a foundational capacity with new investment instruments, which IFU can build further upon as it scales up activities in line with the reform ambitions. The goal is that IFU operates as One IFU, applying its different investment instruments to deliver on the objectives set in the Ownership Document.<sup>3</sup>

## 2 Programme context

### 2.1 Background and Thematic Context

#### *The financing gap*

The climate and development challenges facing the world require more investments into sustainable and inclusive growth. Private and market-based investments need to scale up significantly and fast especially in emerging and developing markets. Global ODA totals USD ~210 bn. The annual global funding gap for climate alone is USD 3.9 tr, most of which in emerging markets and developing economies. The present climate finance flow is estimated at less than USD 800bn, leaving a considerable financing gap, mostly in low and lower-middle income countries.<sup>4</sup>

The majority of private investors target only a small sub-set of emerging markets – the ones that are considered relatively safe and liquid (easy to exit investments, e.g. by selling shares in companies). Established rating agencies consider most emerging markets “non-investment grade”<sup>5</sup>. Furthermore, private capital flows to emerging markets are transitory and tend to be strongest when growth in the developing world is outpacing developed markets. When emerging markets are

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<sup>3</sup> See Annex 3 for an overview of IFU instruments as well as some of the considerations related to their use and priorities.

<sup>4</sup> E.g. Climate Policy Initiative, [Global Landscape of Climate Finance 2021](#) or IMF 2022, [Mobilize Private Climate Finance in Emerging and Developing Economies](#), [UN Global Crisis Response Group](#) estimates the lack SDG and Climate Funding at USD 4.3tr of which 75% refers to low and lower-middle income countries.

<sup>5</sup> 'Investment grade' refers to the group of credit ratings that imply a low default risk (from AAA to BBB-). Companies with a rating in this range will issue debt at a lower interest rate than others with a poorer credit rating.

going through hardships, private capital tends to dry up and flow out of these markets, especially lower income countries, when it is most needed.

#### *The risk environment in developing countries and emerging markets*

Perceived and real risk is assessed to be too high compared to expected financial returns to allow most private investors (often due to financial regulations) to invest into non-investment grade markets. Risks include:

- **Macroeconomic risks:** exchange rate, economic crises, including crises related to deficient governance that affect the ability of government to uphold payment commitments etc. Many low and lower-middle income countries face these challenges. Global cyclical events and developments (COVID-19, war in Ukraine, supply chain disruptions, inflation, and sharply increased interest rates) often exacerbate these risks.
- **Policy/regulatory risk:** taxation, market specific rules that affect businesses and competition.
- **Rule of law risks:** lack of enforcement of investment agreements, corruption.
- **Other country risk:** e.g., security such as spillover effects from neighbouring countries in conflict
- **Project risks:** delays, cost overrun related to regulatory approvals, licences, deficiencies in implementation of agreed regulatory changes, availability of skilled workforce, power outages, security risk etc.
- **High upfront cost** of climate infrastructure exacerbates other risks. In time of more uncertainty long term investments such as infrastructure tend to fall and interest rates increase making capital intensive projects (like renewable energy projects) more expensive.
- **Lack of liquidity** in the markets, which increases risk of not being able to exit. This is especially so in smaller economies such as most low-income and many lower-middle income countries.

These risks not only lower or prevent external private finance flows. Even state-owned development finance institutions such as IFU face challenges with balancing the mandate of investing in least developed and fragile countries and the aim of doing financially sound and sustainable investments supporting long-term development. Investing in such markets thus entails that a certain share of investments will fail, and that risk-willing capital is required.

A number of impact investors do seek to intervene in these markets and take on these risks to create impact. Impact investors range from NGO driven funds with no return requirements, small transaction sizes and with specialised skills in thematic and geographical areas. Funds driven by NGOs often aim for social impact indicators, e.g. in the area of entrepreneurship where the development of entrepreneurial capacities is seen as important results for the longer term together with the financial viability of the company.

The country and development impact focus that characterise IFU's investments cannot always meet investor requirements in terms of financial returns. If a private investor were to assess these investments merely on a financial and commercial basis these would never materialise. Aside from the financial returns from investments, IFU also considers externalities and associated effects in its investment decisions. Such externalities or effects could in the case of an investment in a processing plant e.g., be indirect job creation in the value chain, either from suppliers, or in relation to use of produced goods or services that would allow downstream enterprises to expand operations. IFU investments must be financially additional and invest in market segments where finance is lacking with the purpose to mobilise commercial investors once a project has demonstrated commercial potential,

The risks perceived by private investors in developing markets may in many cases not reflect the actual risk. IFU's investments can serve to demonstrate that it is possible to carry out investments on commercial terms and to achieve adequate risk-adjusted returns. In addition, by acting as a "first mover", IFU helps pave the way for more commercial followers, who can learn from its experience (good and bad), and benefit from regulatory changes initiated or induced by official commercial investors such as IFU. A recent example of this type of regulatory change is from Ukraine and has to do with the possibility of foreign investors to repatriate returns on investments. While the recent decision by the Government of Ukraine to change its regulation of cross-border capital transfers may not be solely attributable to the efforts of IFU in the official dialogue with the Central Bank in Kyiv, the persistence of IFU in this policy area is likely to have played a role - alongside similar efforts from other partners. Hence, IFU can also in some cases play the role of stimulating and to a certain extent driving policy changes in markets together with other actors. IFU are also at times able to mitigate a number of different risks more effectively than many private investors e.g. through implementation of high ESG standards and deep knowledge of local markets and experience in operating in developing countries.

IFU investments must be additional to private finance, not competing with it. This does not mean that IFU behaves in the same way as commercial investors. But it does mean that IFU operates in market segments where finance is lacking, setting prices that allow commercial investors to enter once the project has demonstrated commercial potential.

## 2.2 Results and lessons learnt

With more than 1000 investments since its foundation in 1967, IFU has accumulated experience in emerging markets and developing economies, and has demonstrated its ability to invest profitably, with an increasing focus on SDG and climate impact. IFU has also successfully mobilised Danish institutional investors (more than DKK 4bn) in various equity funds and has during the last 3-4 years invested more than DKK 400m in high-risk high impact projects in Africa, blending finance from both the MFA and from the EU.

In 2022, IFU invested almost DKK 1.5 bn., more than double the amount invested in 2017. This year was important as IFU from 2017 onwards was no longer obliged to work through Danish companies exclusively. In subsequent years, the amount of investments increased, and capital under management moved from some 9.1 bn. in 2017 to 15.6 bn. by 2022, while the range of financing tools expanded. As part of its portfolio today, IFU manages funds (HRHI), which target investments that focuses on impact in fragile countries and may have low risk-adjusted returns as well as large-scale investments that leverage more commercial co-investments through the SDG Fund. While the risk appetite differs across different types of investments, expectations for impact creation is the same. The table below presents IFU investment results from 2017 onwards:

**Table 2: IFU investment activity 2017-2022**

DKKm	2017	2018	2019	2020	2021	2022
Annual investment volume (DKKm)	640	1,029	1,103	1,965	1,005	1,466
Total capital under management	9,100	11,400	11,200	12,800	12,600	15,600
Number of investments pr. year	37	37	25	31	15	20

The current IFU portfolio contributes to employment of close to 380,000 people and supports 450,000 smallholder farmers. In addition, IFU's investments in microfinance institutions provide financial services to 16 million clients, of whom more than 90 percent are women in support of SDG 1 (target 4). IFU's green energy investments produced more than 5 GWh of clean energy and avoided 3.4 million tons of CO2 emissions during 2022. IFU's investments also contributed to mobilise 1.4 billion DKK of private capital in 2022, equivalent to an almost 100% mobilisation rate on IFU's investments.<sup>6</sup>

IFU has gone through a significant shift in terms of strategic focus over the past seven years: From investing with Danish businesses in developing countries, IFU today is untied and focuses on its mandate as impact investor with international investment partners. In 2019, an evaluation of IFU – a few years after the decision to untie IFU's mandate in 2017<sup>7</sup> - was overall positive and considered IFU to be “fit-for-purpose”, but also raised some issues for further development:

- i. Strengthen the development expertise within the organisation at all levels
- ii. Improve monitoring and evaluation: from focus on compliance with CSR standards to more pro-active monitoring and evaluation of actual CSR performance and development outcomes
- iii. Improve the transparency of IFU, its learning culture and communication further (e.g. in relation to sensitive issues raised by civil society and in the media)
- iv. Set clear criteria for Board membership in investee companies to help increase the non-financial value that IFU can deliver to investee companies
- v. Further strengthen the country/regional offices to originate bankable projects with impact

IFU has responded to the recommendations, and IFU is continuously developing its organisation and ability to deliver. Many of the issues are related to long-term organisational processes (e.g. rec. 1,2 and 3) and continue to be part of e.g. the current IFU strategy 2024-2026. The annual updates from IFU to UPR will also include progress on these issues.

Moreover, new EU legislation on e.g. ESG, CSRD, social taxonomy etc. plays an important role for the legal obligations connected with IFU investments, especially the due diligence processes. These changes oblige IFU to work out tools and processes that can respond to the requirements, and find ways to enable investees to comply with the demands.

<sup>6</sup> Examples of impact created are document further by IFU in its annual report and the SDG report

<sup>7</sup> [Evaluation of The Investment Fund for Developing Countries \(IFU\) 2004-2017](#)

## 2.3 Coherence and synergies

The capital contribution will strengthen IFU's core capital. The increased core capital is what allows IFU to raise additional non-ODA finance, and this will contribute to all IFU's investment activities across instruments. IFU has three main financial instruments: direct equity investments, loans and guarantees. IFU applies these according to different deal structures to create maximum impact and to meet risk and return requirements.

IFU applies its capital for three main investment activities: 1) IFU contribution to IFU managed funds with private investors, such as the SDG Fund; 2) direct equity investments using only IFU capital, and 3) co-financing loans along with capital from state on-lending to cushion loans according to the risk profile of the loan. The guarantees are unfunded sovereign guarantees based on Denmark's AAA rating, and hence do not require funding from IFU's core capital.

### *Allocation of IFU's capital contribution:*

In the period 2024 to 2030, IFU will combine the DKK 3.5 bill. in new capital contribution together with existing and expected future own capital (cash-flows from its investment and loan activities). This will allow IFU to use around DKK 8,6 bill. from its own equity to fund investment activity of close to DKK 23 bill. across its three main investment activities. The expected use of IFU's own capital will be:

**Table 3: Expected use of IFUs own capital:**

IFU own equity (existing, future and MFA capital contribution)	..together with...	Instrument	..results in investment/loans towards 2030:
DKK 5.2 bill. IFU equity		Investments using only IFU equity	DKK 5.2 bill.
DKK 1.2 bill. IFU equity	3 bill. DKK (institutional investors) and 800 mill. state on-lending	SDG Fund II	DKK 5 bill.
DKK 3 bill. IFU equity	DKK 7.5 bill. state on-lending	Green loans using on-lending	DKK 10.5 bill.

Note: In addition to the above, IFU expects to investment DKK 2 bill. from SDG Fund III, of which DKK 0,8 bill. will be IFU own equity and DKK 1,2 bill. will be raise from institutional investors.

The capital contribution will strengthen all IFU's main investment activities, supporting both the raising a new SDG Fund and allowing IFU to utilise its access to state on-lending.

All IFU investment activity will be in accordance with IFU's strategies, priorities and policies. IFU must optimise its use of different instruments to ensure to meet overall targets for IFU's investment activity, while also meeting IFU's risk and return requirements. IFU's instruments complement each other and allow IFU to blend its financing, enabling IFU to have a broader reach in the development finance market. Loans for example meet a different market demand than equity investments and are useful when scaling large projects within renewable energy, where the risk profile typically is lower. The direct mobilisation of Danish pension funds in the SDG Fund investments results in investments with a lower risk appetite than those done using IFU's own equity alone. SDG Fund investments will typically target larger investments in lower risk countries. Historically, IFU's funds with private participation have proved their ability to combine IFU's expertise in developing markets with capital from Danish pension funds. This has helped pave the way for the Danish pensions funds' activity in developing markets, and today they increasingly direct own funds towards development outcomes in the developing countries.

### *Development guarantees and concessional loans*

The Danish Development Guarantee Facility and concessional loans from DSIF supplement the investment activities using IFU's equity, which further expands IFU's reach. IFU's broad coverage of the development finance markets provides IFU with a deep knowledge and knowhow, which IFU can use strategically across projects and instruments. It increases IFU's relevance as an investment partner, thereby strengthening both IFU's access to potential projects as well as co-financing from other like-minded investors. IFU has among others collaboration with other DFIs and participates in several co-investments.

IFU has also expanded its collaboration and alignment with the European Union during the past five years. IFU has drawn upon EU support to complete impact investments in very difficult markets, including support to a debt fund for small enterprises in the Somali region. IFU participated in EU-funded initiatives to increase collaboration between

European institutions working in developing markets, such as European Financing Partners and the Interact Climate Change Facility. In 2022, The European Commission granted IFU three guarantees under the scheme European Fund for Sustainable Development Plus (EFSD+), totalling over DKK 1 bn making IFU one of the larger recipients of support under this EU scheme (negotiations are still ongoing on the specific terms).

#### *Direct synergy with Danish development initiatives*

IFU support and engage directly with bilaterally initiated structures and organizations leading to synergies between development programmes in partner countries. Recent examples include:

- In **aBi Finance** in Uganda, which uses lines of credit and guarantees to support local bank's lending to SMEs in the agricultural value chain, IFU has taken over Denmark's stake and is managing a capital contribution from the EU.
- In Ghana, IFU manages the capital stake of Denmark alongside Ghana's Government in the **Rural Development Finance Institution (RDF)**. RDF provides access to funds and capacity-building services to agriculture, agribusinesses, and renewable energy. RDF continuously reinvests its earnings to support access to finance while leveraging its funding to work with other like-minded institutions. By allowing IFU to step into the investor role on behalf of Danida, it is possible to extend the life of these development programmes and grow them without additional ODA, while retaining the original outcomes and impacts.
- In a similar structure in Tanzania, **Private Agricultural Sector Support (PASS)**, IFU and MFA have for some time been exploring opportunities for a partnership with the Danish Embassy and the Government of Tanzania.

By taking over and/or investing in these financial institutions, IFU helps to ensure commercial sustainability, so that the institutions may continue creating the impact that they were established to generate without further support from Danida. IFU's engagement contributes to long-term sustainability in projects or programs initiated with Danida grant funding.

In addition, IFU has over the years benefitted from engagements with a number of Danish embassies, the Trade Council, and organisations from Danish (and local) civil society. Collaboration with e.g. embassies helps identify potential investment opportunities and provides knowledge of the local conditions in the country and access to key decision makers. Recently, cooperation with EIFO has helped to unfold the respective mandates of the two institutions within export promotion of Danish companies and development financing, respectively. Looking ahead, IFU and the MFA are also considering ways to support the JETPs (Just Energy Transition Partnerships) and EU's Global Gateway.

## 2.4 Justification of programme design

The proposed capital contribution and its consequent influence on IFU's reform and change processes 2024-2030 must be justified in view of aspects such as relevance, efficiency, effectiveness, impact, sustainability, and additionality (the OECD DAC evaluation criteria).

#### *Relevance*

Overall IFU's role is to overcome the challenges related to investments in developing markets. As the official Danish DFI operating as a unique Danish actor in the global space of impact investing institutions and organisations, the Government considers IFU the relevant bilateral partner in terms of promoting private sector investments in developing countries: IFU has the skills and experience to manage investments and ensure that relevant sustainability policies, including environment and social standards, human rights standards, and anti-corruption standards are upheld.<sup>8</sup> Further, IFU's tightened mandate to deliver first and foremost on Danish development priorities, provides good examples for the Danish government to show case at international platforms and negotiations.

#### *Efficiency*

IFU has developed screening and approval processes that are suitable to large-scale investments as well as smaller high-risk projects. As a DFI with a strong track record, IFU has proven able to deploy capital in fragile situations and during periods of macroeconomic headwinds. Aside from financing new investments, the capital contribution into IFU will also contribute to improve IFU's management systems, appraisal and risk management procedures, financial value, and impact creation processes. During this process, one of the key questions will relate to how the advantages of scaling up can at the same time accommodate the need for having diverse instruments that can reach many different kinds of investees and target groups. More flexibility will allow IFU to use the most suited instrument for a given project and ensure the right balance between risk, returns and impact.

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<sup>8</sup> For a full overview, please refer to [IFU Sustainability Policy](#)

### *Effectiveness*

Overall, IFU has contributed to positive development outcomes and been additional to other investors, while achieving a moderately positive return thereby protecting its capital base. IFU has been able to significantly scale up its impact across priorities, and IFU has also been able to use the High-Risk, High-Impact funds to reach geographies that have previously been difficult to reach, such as the Somali region and the Democratic Republic of Congo. The principles of HRHI are now an integral part of the IFU reform and the annual capital contribution will allow IFU to keep growing its investment volumes while creating both impact and returns, also on high-risk markets in line with the directions set in the Ownership Document. Synergies with other DFIs will also improve effectiveness to the extent that IFU achieves a stronger position as a high-impact DFI by 2030.

### *Impact*

IFU's bases its development impact philosophy on the need for financially sustainable investments to assist developing countries in improving the livelihood of people. IFU's will further develop its investment strategy (approved by the Board of Directors in 2020) in the coming years from 2024-2026 including targets that combine return of investment with impact results (cf. results framework below). In this connection, it is necessary to bear in mind that impact results can take time to materialise, sometimes beyond the period of engagement by IFU, and may be difficult to document as part of the project monitoring. IFU will invest in upgrading its result and monitoring systems to better capture results during investments as well as ex-post. As a follow-up to the current strategy 2024-2026, an updated strategy will be made for the period 2026-2030 to guide IFU through the reform period.

### *Sustainability:*

IFU's investments must contribute to sustainable outcomes in terms of environmental impact and climate change (adaptation and mitigation) and/or social impact, and will towards 2030 build a stronger focus on adaptation investments. Development sustainability hinges on carefully selecting investments, active ownership and responsible exit. The financial sustainability of investments hinges on professional underwriting, careful structuring, and not least data analysis and proper risk assessment. An investment will only contribute to more sustainable outcomes if the transaction is financially sustainable. Experience shows that careful due diligence, impact screening, and active ownership (including strong and reliable management) all make a difference for delivering better sustainability. These processes are supported by IFU ownership policies and working processes.

### *Additionality:*

The additionality of IFU refers to the extent to which its participation mobilizes investments and impact that would not otherwise be possible. IFU works within the frameworks of the OECD definition of additionality for DFIs<sup>9</sup>, and IFU's due diligence process serves to ascertain that investments are likely to be additional and not crowd out commercial alternatives and is fundamental in this regard. Addressing additionality is not new in the world of DFIs. It is the same basic question whenever and wherever public funds are deployed to supplement markets with private investors and companies. IFU is working on improving the assessment of financial additionality by having a more rigorous analytical tool and has engaged the Institute of Economics at Copenhagen University to help develop such a tool based on the best available knowledge<sup>10</sup>.

An important function of IFU is to pave the way for other investors. By investing in developing countries, IFU provides assurance to other investors that attractive investment opportunities are available in these markets, and by doing so mobilises private investment that would not otherwise have taken place. During 2024-2030, IFU will also work on putting OECD additionality concepts better in to practice.

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<sup>9</sup> IFU also reports to OECD on additionality.

<sup>10</sup> "Support to Develop IFU's Approach for Assessing Financial Additionality", Henrik Hansen and John Rand, Institute of Economics, University of Copenhagen (forthcoming).

### 3 Programme presentation

#### 3.1 Objectives and outcomes

IFU selects its investments based on their potential to deliver on IFU's two impact priorities of (i) building green societies, and (ii) building just and inclusive societies. For IFU's 'green' impact priority, IFU selects investments based on their potential to support climate mitigation and/or adaption, circular economy, pollution prevention and control, sustainable protection of water and marine resources, and/or the protection and restoration of biodiversity and ecosystems (in line with EU Green Taxonomy). For the 'just and inclusive' impact priority, IFU selects its investments based on their potential to

stimulate the economies of least developed countries, improve incomes for the bottom 40 per cent segment, improve access to goods or services for underserved populations and gender lens investing. Investments need to have significant potential to deliver on at least one of the impact objectives and at least "do no significant harm" in relation to the other.

IFUs Investment and Impact Model describes these issues and applies to all IFU instruments. The model above illustrates the process for the investees in terms of input, return of investment and outputs, while the model below shows how the accumulated results of companies fit into a higher level where IFU instruments, their interplay with private investors, and lays out the eventual impact on societies.

#### IFU'S INVESTMENT AND IMPACT MODEL

Investing risk capital in private companies in developing countries with the purpose of creating impact and return to investors.

##### INVESTEES

###### INPUT

- IFU invests...
- Capital
  - Knowledge and competencies
  - Experience

in private companies  
in developing countries

###### SECTOR

- ...into focus sectors
- Green energy & infrastructure
  - Sustainable food systems
  - Financial services
  - Healthcare

having impact creation plans  
with specific targets

that are reinvested

IFU

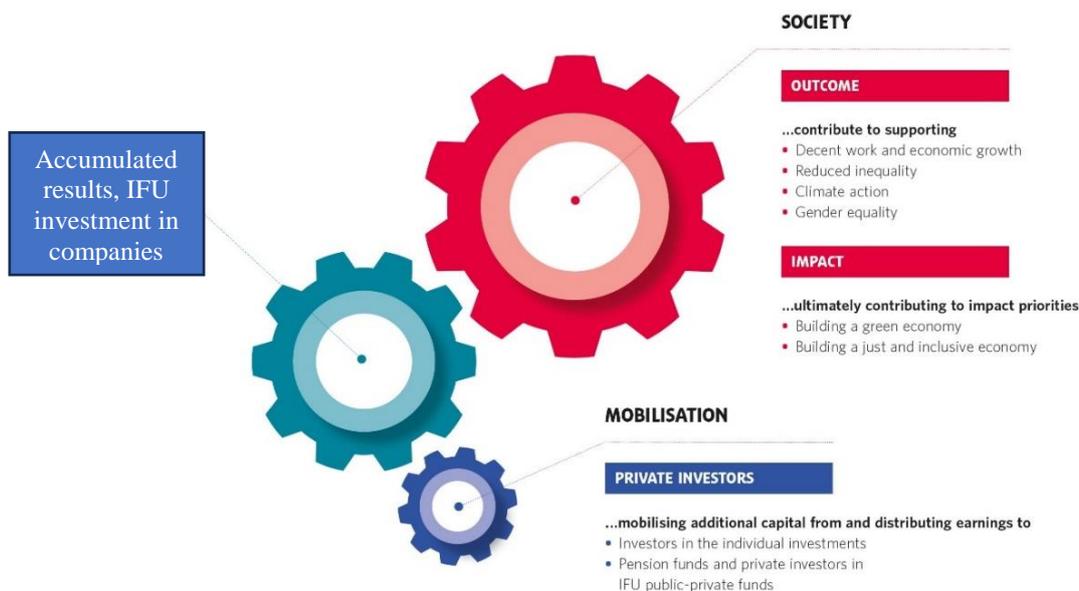
###### RETURN ON INVESTMENT

- and commercial returns...
- Interest
  - Dividends
  - Capital gains

and value creation  
plans for generating  
profits

###### OUTPUT

- ...to achieve measurable results
- Circular business model
  - Climate mitigation and adaptation
  - Improved access to (basic) goods and services
  - Quality jobs
  - Women empowerment



The above models forms the basis for the results framework and the theory of change, and in this way integrate the annual capital contribution and its expected results into IFUs own theory of change.

## 4 Theory of change and key assumptions

### 4.1 Theory of Change

The theory of change sets out the understanding of the changes that will eventually lead to the achievement of the objectives as supported by the organizational development process in IFU:

- IF
- The MFA injects a capital contribution of DKK 500 mill. annually to IFU as described in the Ownership document, and
  - IFU continues to engage in a process of organizational development in quantitative and qualitative terms adequate to manage the financial strengthening of the organisation
- THEN:
- IFU will be able to raise significant non-ODA finance through the state on-lending facility of the Central Bank and capital from institutional investors
  - IFU will be able to manage requirements for growth based on investments across all of its facilities and instruments and substantially increase company-level results
- LEADING TO
- IFU will deliver results that contribute to a green and just and inclusive economy at a significantly higher scale than today documented by in-house impact measurement indicators
- EVENTUALLY LEADING TO:
- IFU becoming a leading impact investor among European DFIs with an overall increase in investments in Africa, for climate and LDC countries by 2030,
  - documented that impact measurement, communication of results and transparency attract investors, inspires DFIs and creates a critical mass of actors to address SDG and climate goals
- BECAUSE:
- the capital contribution in connection with access to on-lending, attracts private investors and other funding sources to support IFU's work
  - IFU will have managed to act as a broker to attract increased private and institutional finance to Africa, climate finance and LDC countries
  - IFU can document positive correlations between the financial markets and development and climate targets and that the focus on additionality by DFIs paves the way to strengthen these linkages
  - The documentation and communication of results is a driving force for attracting other investors and to create Danish public support for the combination of public and private financing of development and climate action

### 4.2 Key assumptions:

- IFU's organisational development for 2024-2030 incl. the substantial increase in staff is carried out as planned in both qualitative and quantitative terms.
- Lack of financing in emerging markets impedes economic development and a green transition.
- There are businesses with profitable business models that currently do not have access to sufficient funding from the market;
- IFU is able to identify relevant investment opportunities and is able to execute on them;
- Political, regulatory, and macroeconomic conditions in developing markets allow for investments by DFIs;
- Investee companies and projects are willing and able to execute on the impact and value creation plans;
- It is possible to achieve positive commercial returns despite the risks inherent in investing in developing markets;

These are generic assumptions that IFU must always assess prior to an investment decision. It will often be the case that one or several assumptions will only be partially met from the outset, and that there may be several degrees of fulfilment that may be acceptable. IFU document, track, and ascertain these assumptions as part of the investment cycle.

## 5 Summary of the results framework

IFU's results framework builds on IFU's impact objectives, as well as the targets set in the updated Ownership Document.

**Table 4: Outline of Results framework:**

Programme	IFU Capital Contribution 2024-2030	
Programme Objective	Contributing to building a greener, more just and inclusive economy with respect to national policies and frameworks in the countries where IFU invests	
Impact Indicator	(To be developed )	
Baseline and Target	Year 2024:	Year 2030:

Outcome 1	Green economy	
	Accumulated IFU investments across all instruments and facilities and within the defined priority sectors contribute to green economy in the countries where IFU invests	
Outcome indicator 1.1	New expected capacity of renewable energy investments	
Baseline and Target	Year 2024:	Year 2030:
Outcome indicator 1.2	Renewable energy produced	
Baseline and Target	Year 2024:	Year 2030:
Outcome indicator 1.3	Avoided emissions (attributed and not attributed)	
Baseline and Target	Year 2024:	Year 2030
Outcome indicator 1.4	GHG sequestered	
Baseline and Target	Year 2024:	Year 2030
Outcome indicator 1.5	Private capital mobilised for green economy objective	
Baseline and Target	Year 2024:	Year 2030

Outcome 2	Just and inclusive economy	
	Accumulated IFU investments across all instruments and facilities and within the defined priority sectors contribute to a Just and Inclusive economy in the countries where IFU invests	
Outcome indicator 2.1	Direct investments that pay more than the national minimum wage	
Baseline and Target	Year 2024:	Year 2030:
Outcome indicator 2.2	Investments with a gender focus	
Baseline and Target	Year 2024:	Year 2030:
Outcome indicator 2.3	Direct investments with more than 40% women in senior management	
Baseline and Target	Year 2024:	Year 2030:
Outcome indicator 2.4	Employees in investments under the age of 25	
	Year 2024:	Year 2030:
Outcome indicator 2.5	Direct and indirect employment	
	Year 2024:	Year 2030:
Outcome indicator 2.6	Serviced provided to underserved groups/access to services: <ul style="list-style-type: none"> <li>- Clients served with microfinancing/access to finance</li> <li>- Number of small-scale farmers benefitting from investments (e.g. through access to inputs, TA and better markets)</li> <li>- Number of patients served/access to health services</li> <li>- Access to electricity for poor households</li> </ul>	
	Year 2024:	Year 2030:
Outcome indicator 2.7	Private capital mobilised for just and inclusive economy objective	
	Year 2024:	Year 2030:

Outcome indicators	Joint outcome indicators for outcome 1 and 2	
Outcome indicator 3.1	Amount in climate investments	
Baseline and Target	Year 2024:	Year 2030:

Outcome indicator 3.2	Amount in LDCs / countries below 50% of LMIC limit	
Baseline and Target	Year 2024:	Year 2030:
Outcome indicator 3.3	Amount in fragile and conflicted states	
Baseline and Target	Year 2024:	Year 2030:
Outcome indicator 3.4	Direct and indirect employment	
	Year 2024:	Year 2030:

Crosscutting outputs (both outcome 1 and 2)	IFU investments made across all instruments and facilities and within defined priority sectors in line with IFU investment strategy, sustainability strategy and ownership document as represented in IFU strategy 2024-2026.
Output indicators	<p><u>Return on investments by company:</u></p> <ul style="list-style-type: none"> <li>• Increased interests,</li> <li>• Dividends, and</li> <li>• Capital gains</li> </ul> <p><u>Climate and development indicators by company:</u></p> <ul style="list-style-type: none"> <li>• Climate indicators (to be developed - related to adaptation and mitigation)</li> <li>• Circular economy models adopted</li> <li>• Improved access to basic goods and services,</li> <li>• Quality jobs created,</li> <li>• Increased women empowerment.</li> </ul>

IFU and the MFA will work closely together to develop indicators, which IFU can measure and track, to form a basis for impact reporting, including a particular focus on climate adaptation and social inclusion.

## 6 Budget

The overall budget of the proposed contribution is DKK 500 million per year as indicated below and up to 3,5 bn. DKK by 20230. Amounts are distributed equally over time. As a general capital contribution to IFU, the funding will be deployed as part of IFU's overall investments using its own capital. From the outset, it is assumed that IFU will strive towards an equal distribution between green and just and inclusive economies. However, as the capital contribution is flexible, the distribution will be reflected in IFU reporting. In this reporting, the distribution against the three key targets in the Ownership document will be used: 50 per cent Africa, 50 per cent climate and 30 per cent LDC/FCAC/high risk countries as for IFU equity investments.

## 7 Management arrangements

IFU was established by the Government in 1967, and the legal basis for IFU is §9 in the Law for International Development Cooperation. The Ministry of Foreign Affairs manages the ownership of IFU on behalf of the State.

The MFA is responsible for the active ownership of IFU. The Minister for Development Cooperation and Global Climate Policy appoints board members (3-year term), the board chair, vice chair, and IFU's CEO. An observer represents the MFA in IFU's board of directors. The Minister meets annually with the Board's Chair, Deputy Chair, the CEO and the Deputy CEO to take stock of performance, approve the annual report as well as discuss the overall strategic issues related to the Ownership Document. The State Secretary for Development Policy meets twice a year with the IFU Chair and Deputy Chair to assess progress on agreed strategic priorities. The Head of the Department responsible for IFU oversight meets with IFU senior management for operational follow-up and to secure close coordination of priorities.

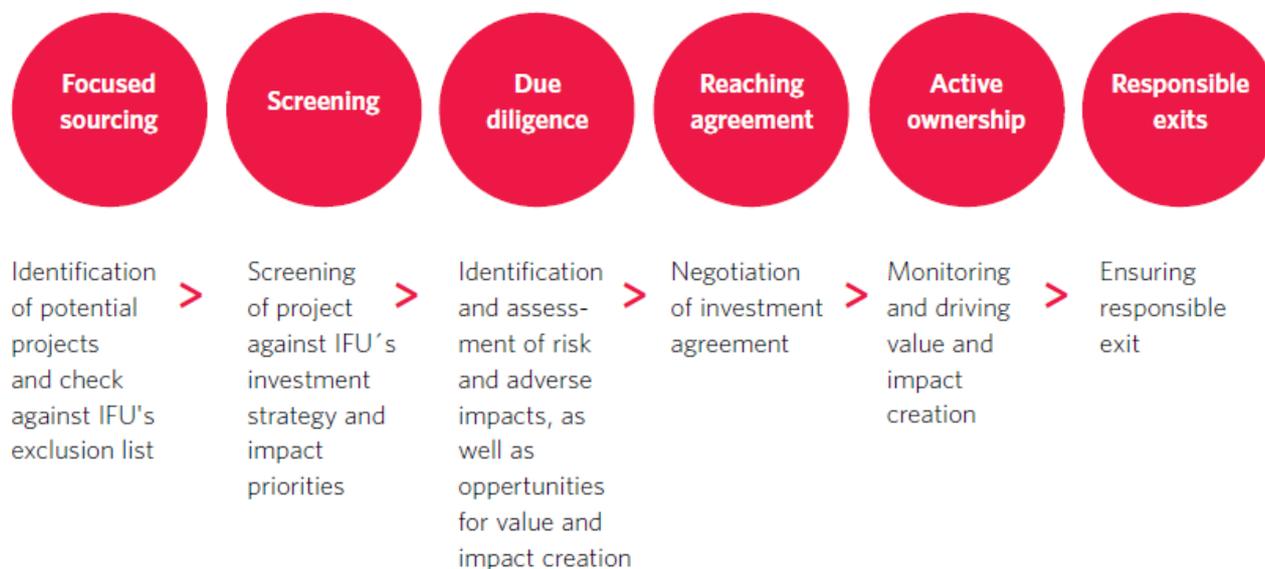
The Minister responsible for Development Cooperation nominates the Board of Directors and its Chairperson. As the owner, the Minister for Development Cooperation and Global Climate Policy meets annually with the Board's Chairperson, Deputy Chairperson, the CEO and the Deputy CEO to take stock of performance as presented in the annual report of IFU. The MFA has an observer on the Board of Directors and participates in all board meetings. Senior management of MFA meets quarterly with senior management of IFU to discuss issues of common strategic interest. In addition, at an operational level several meetings take place between IFU, MFA and relevant Danish embassies.

Based on recommendation from the Board of Directors, the Minister appoints an audit company with international experience, which audits the annual account in accordance with Danish and international audit standards in agreement with the Auditor General (*Rigsrevisionen*). IFU's Board of Directors is responsible for assuring that the strategic management of IFU complies with the Ownership Document (and hence complies with the law as well as with the development policy strategy). The CEO is responsible to the Board of Directors for implementing the agreed strategies and policies. The capital contribution and the resulting investments will follow IFU policies and draw on IFU's capacities in sustainability, legal, financial management and communication. IFU also has board-approved guidelines and policies in place for working with safeguards and ESG requirements. The state attorney (Kammeradvokaten) has established that IFU complies with rules and procedures of Danish anti-money laundering.

In relation to the framework document management, annual consultations will be held with the Council for Development Policy. As the approval of the capital contribution rests with the UPR, these annual consultations will serve to confirm that the annual capital allocation is disbursed according to the seven-year schedule, as IFU is implementing the initiatives of the reform as a mechanism to release capital contributions on an annual basis. But the consultation is also an opportunity for IFU and MFA to present results on key indicators related to the objectives of the framework document, discuss progress made and make adjustments to the process (as needed).

At the level of individual projects, the following figure illustrates the IFU investment process:

**Figure 1: IFU Investment Process**



These processes integrate key IFU policies that reflect the strategic direction of IFU, and set the point of departure for the active ownership of projects. These processes ultimately enable companies to operate independently and enables IFU to exit, typically after 5 to 8 years on average.

## 7.2 IFU strategy and organisational development

Since being untied from only investing with Danish companies in 2017, IFU has set a new direction where large scale impact investments is in focus. The areas where significant changes have happened relate to the process towards becoming a leading impact investor with – among other things - more rigorous due diligence processes, policy development, ESG standards and impact creation through results frameworks. IFU has during this period developed an increasing ability to mobilise private capital directly and at an increasing scale, and developed stronger investment strategies. IFU has during the same period also expanded the number of instruments and scaled-up investments, and embarked on a significant organisational development.

The reform process and its significant capitalisation of IFU, signifies a strategic shift for IFU. Expectations are high and IFU is to deliver a high increase in investment activity while maintaining a strong focus on impact creation and a rigorous investment process. The strategy plan for 2024-2026 sets IFU on the path to deliver. The plan outlines IFU's priorities and the initiatives enabling IFU to meet the reform expectations. IFU's investment priorities are set by a) IFU's impact

priorities that all investments must contribute to either a green economy or a just and inclusive economy, b) IFU's internal policies on sustainability incl. IFU's climate policy and gender policy, and c) the ownership document. The reform capital contributions and access to on-lending necessitates an increase in IFU's investment activities across all instruments. The strategic plan outlines six priority areas to deliver. They are:

1. Funding and mandates
2. Investments
3. Organisation, values and culture
4. Communication
5. Data and technology
6. Governance risk and compliance

Initiatives within each priority areas will collectively strengthen IFU.

#### *Funding and investments*

- Finalise SDG Fund II fundraising and directly mobilise DKK 3 bill.
- Expand IFU's work in blended finance collaborating with MFA, EU and other public donors
- Fully integrated DSIF into IFU and evolve the guarantee facility to be fully IFU managed
- Outline a clear investment strategy for each main instrument and further improve the investment process
- Exploration of synergies across instruments

#### *Organisational growth*

- Grow IFU with 20-25 FTE's annually reaching between 185-225 FTEs in 2030
- Expand IFU's regional footprint with a relative high growth in regional office and potential opening new offices in key markets
- Build and acquire new capabilities to support growing loan activity and improve risk management
- Enhance focus on people development with improved training across all levels and departments

#### *Improved utilisation of data and technology*

- Complete on-going IT transformation and strengthen IT support for key investment process as sourcing, deal management and active ownership, as well as people process and finance processes
- Enhance data collection and reporting abilities to meet requirements from CSRD and to deliver SDG Fund II as an SFDR article 9 fund
- Centralised selected investment process tasks in team of specialists to gain efficiency and quality benefits and free up resources

#### *Strong brand building*

- New communication strategy emphasising proactive communication
- Consistent core narrative that works effectively across IFU's key activities and stakeholders
- Increased brand building in both Denmark and core markets to increase awareness and support recruitment efforts and sourcing
- Increased engagement with investors, owners and stakeholders of all types

IFU's board of directors approved IFU's strategy in February 2024. IFU is responsible for the implementation of the strategy, which will happen during 2024 to 2026 with several initiatives already started. IFU reports regularly to its board of directors on implementation progress.

IFU will develop a new strategic plan during 2026, which will set the direction for IFU for the remainder of the reform period towards 2030. The focus will be to ensure IFU has the necessary organisation and capabilities for the next phase of the reform process.

## 8 Financial management, monitoring and learning

According to *Vejledning for håndtering af kapitalindskud fra Udenrigsministeriet til IFU*<sup>11</sup> general capital contributions with the aim of strengthening IFU's core capital have no additional requirements beyond being invested in accordance with IFU strategies, priorities and policies.

Financial reporting follows IFU's overall financial reporting to the Ministry of Foreign Affairs, reflecting the use of the funds. In addition, IFU Management will update the MFA through quarterly meetings, covering both financial and other relevant reporting (see also section 7 on management arrangements). IFU also publicly reports on its operations and results in e.g. its annual report. Furthermore, the MFA receives reporting on pipeline, investments and exits as well as timely financial reporting.

### Monitoring, evaluation and impact measurement:

At the level of individual investments, since 2020 IFU monitors impact by monitoring key performance indicators according to a results framework. All investments provide regular financial reporting and annual reporting on impact.

During the pre-investment stages, IFU establishes a Theory of Change for each investment, which IFU uses to develop the impact results framework, with indicators and targets mutually agreed with the investee companies. Complimentary to IFU's standard portfolio and sectoral indicators, IFU's adds relevant project-specific indicators to monitor the social and environmental performance of the investment. Portfolio companies are responsible for collecting data and annual reporting during the lifetime of the investment. IFU tracks performance on ESG-related issues annually across portfolio companies.

At portfolio level, IFU collates and analyses data to assess performance against organisational objectives, and develop annual reports on impact performance. Additionally, IFU uses this information to inform quarterly or half-yearly 'active ownership' reviews on financial and sustainability performance of investments. IFU also collects lessons learned during the lifetime of investments, and the Board receives exit evaluations for information and discussion to secure learning from the experiences.

IFU's Investment and Impact Model takes a general approach showing how providing capital and advice to private businesses in developing countries can create impact. IFU's activities cover a broad spectrum (global geographical coverage, different sectors, varying risk levels and multiple instruments) and the type of expected change depends on the specific investment opportunity. For example, a debt investment supporting the green transition in Turkey will not strive to achieve the same change as an equity investment supporting smallholder farmers in Somalia.

For each investment, IFU develops a detailed Theory of Change overview, highlighting how IFU's investment is expected to create impact. IFU develops its Theory of Change for an investment prior to the due diligence and serves as an analytic tool to evidence the company's (and IFU's) expected contribution to the impact. It also serves to identify the relevant assumptions, around impact but also the business model that should be tested during the due diligence.

During the investment period, the Theory of Change also helps to map the linkages between the intended changes, and the KPIs that are being tracked in IFU's results framework, which can be a useful tool to understand why the expected performance on the impact targets may not be achieved. Finally, the Theory of Change is a powerful tool to build common understanding within IFU on why IFU is considering the specific investment, as well as to communicate that story to other stakeholders, including co-investors.

IFU is a signatory to the Operating Principles for Impact Management<sup>12</sup>. In 2021, IFU engaged BlueMark, a leading provider of verification services in the impact investing market, to independently assess and verify IFU's impact management system and processes. This verification concludes that IFU has well-established impact objectives, has integrated impact considerations throughout its investment process, and has a clear process for assessing each investment's expected impact. On the basis of this system, IFU is able to report on the return of investment as well as developmental or climate change indicators (including decent work, employment creation, gender equality, reduced CO2 emissions etc.) at the level of investees and subsequently present data for the entire portfolio of IFU investments.

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<sup>11</sup> "Vejledning for håndtering af kapitalindskud fra Udenrigsministeriet til IFU", opdateret 23. februar 2022, Sag: 2020-38642.

<sup>12</sup> [Signatories & Reporting | Operating Principles for Impact Management \(impactprinciples.org\)](https://www.impactprinciples.org/)

## 9 Risk management

IFU has an elaborate system for risk management in relation to portfolio companies. The risk categories relate to financial and non-financial risks, business risks, operational risks and reputational risks<sup>13</sup>. The current IFU strategy period has also identified a number of gaps in the risk management system that IFU will address. For each of the IFU instruments, IFU has separate risks management systems. As an example, the SDG Fund has its own risk management system, as do the other IFU instruments based on the profile of their partners, the markets they operate in or the types of investors (depending on their risk willingness). The following are the key risks in relation to the achievement of the climate and developmental results:

**Table 6: Key contextual, programmatic and reputational risks.**

Contextual risks					
Risk Factor	Likelihood	Impact	Risk response if applicable	Residual risk	Background to assessment
Macroeconomic downturn across emerging markets	Medium	Medium	IFU generally supports companies with services that are essential also during a downturn. Economic downturns are not likely to happen simultaneously	Medium	Overall economic climate has deteriorated in the wake of the Russia-Ukraine war and the rising interest rate environment. This is a financial risk that may influence the balance of IFU in a negative way.
Political unrest, conflicts and wars	Medium	Large	Thorough assessment of the risks at the time of investment. IFU has good experience and would also draw upon partners and experts on the ground.	Medium	The risk of unrest, or full blown conflicts, increase as economic conditions worsen. IFU's exposure can be mitigated by assessing the risk and structure the deals appropriately in unstable geographies.
Programmatic Risks					
Risk Factor	Likelihood	Impact	Risk response	Residual risks	Background to assessment
Insufficient demand for investment finance	Low	Large	Developing stronger networks on the ground, finding partners, cooperating with peers including other DFIs	Small	Evidence indicates benefits to large pipeline and network to find good opportunities
Decreased interest of private investors for developing markets	Low	Large	Increased use of blended finance, achieving good exits to demonstrate potential	Small	While economic conditions may make private investors more wary, private investors are increasingly finding attractive opportunities in developing markets
Crowding out of private investors	Low	Large	Assessment of additionality, focus where additionality is greatest	Small	While private interest is increasing, there will still be sub-sectors and geographies where IFU's capital is additional
Institutional Risks					
Risk Factor	Likelihood	Impact	Risk response	Residual risk	Background to assessment
That IFU does not allocate sufficient resources to grow the supportive functions in the organization	Medium	Large	Active ownership with regular consultations between IFU and Ministry of Foreign Affairs	Small	Risk that the management and governance set-up is not strong enough

Accusations of any fraudulent, corrupt behaviour or not operating in line with e.g. labour standards or tax policies, can be damaging to IFU as a reputable impact investor and also damaging to the MFA. IFU takes this risk very seriously and performs significant checks on the investees and the management team to minimise the risk of any such behaviour. IFU has also recently strengthened its capacity and established a specific anti-bribery and corruption function, which specifically screens all investments for any related risk indicators.

IFU's approach to active ownership also helps mitigate the risk: By being up to date on what the company is doing and actively engaging in decisions, IFU is better able to discover any inappropriate business behaviours at an early stage. Accusations of fraud, corruption and other illicit or irresponsible behaviour is widespread in markets where IFU invests, and difficult to avoid. IFU has policies and procedures to ensure that measures are in place not only to mitigate the risk, but also to investigate allegations and follow-up according to international best practice. The MFA is aware that investments in fragile and conflict afflicted countries, including Ukraine, increases risk exposure.

<sup>13</sup> See slides for IFU strategy