The Growing Role of the Development Finance Institutions in International Development Policy

Dalberg Global Development Advisors

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Foreword

The private sector plays a key role in spurring economic development. This role has long been recognized in the developed economies and is also given an increasingly prominent priority in international development policy. The recent Africa Commission's Copenhagen Statement highlighted the creation of jobs, particularly for young people, as the top priority for development. This signals a renewed interest in private sector approaches to development that has been emerging for some years now.

The colleagues who work in development finance institutions (DFIs) recognize that economic and social development is a long-term undertaking. There is not one single approach that will ensure the development of the business environment in developing countries. Public policy interventions will also always play an important role alongside private sector investment. Today, there is a need for intense examination of the optimal mix of policies and for debate about how we can best stimulate private sector growth, particularly at a time of financial crisis.

This report, written by the advisory group Dalberg Global Development Advisors, offers a contribution to this debate. It presents in a clear and straight-forward way the rationale for private sector investments in international development policy. It also conveys important data about the roles and impacts of the DFIs and links it to the broader debate about global development goals.

The Association of European Development Finance Institutions (EDFI) welcomes the contribution of this report to the debate about the role of DFIs in international development policy. I hope the report will help spark the interest of the public and policy-makers in this important topic.

Jan Rixen,
General Manager
Association of European Development Finance Institutions (EDFI)

Executive Summary

Development Finance Institutions (DFIs) are state-owned risk capital investment funds. Their role in development cooperation is to invest in sustainable and profitable businesses in developing countries. DFIs are well-known in most of Europe where their strong track record in promoting development is widely acknowledged. In the Nordic countries, however, their methods and achievements are less understood.

This report provides an introduction to the Nordic DFIs and their work. It also puts them into the context of current international development policy priorities, including fighting poverty in Africa and preventing the worst effects of the global financial crisis on the world's poor.

The report concludes that the DFIs are an important "Third Pillar" in the international development policies of the Nordic countries with aid and multilateral development banks being the two other pillars. They play a growing role in reaching the development goals of the Nordic governments. They can also act as an important counter-cyclical force in the economic downturn.

A thriving private sector is the engine of growth

The number of people living in extreme poverty worldwide has levelled off over the past few years. Reforms under way in many countries in Africa have produced significant results in terms of growth and stability over the last decade. But many countries are still facing many obstacles to poverty reduction. The continuation of the positive trend in economic growth is essential for poverty reduction.

Private sector investment is strongly associated with economic growth. According to one major global survey by World Bank, more than 70% of the world's poor believe that the best way to escape poverty is to get a job. A recent Gallup survey among people living in Sub-Saharan Africa particularly highlights jobs for youth as a top priority. This means that if the private sector in Africa does not grow very rapidly, many of the half a billion African youths between five and 24 comprising about 50% of the total African population will grow up without prospects of a job.

Small and medium sized enterprises (SMEs) represent the backbone of economic activity in developing countries, just as they do in the Nordic countries. There is a clear relationship between the share of SMEs in an economy and its wealth. But access to finance is often better for large and micro enterprises than for SMEs in developing countries. This gives rise to a problem referred to as the "missing middle" – there are enterprises with the potential to grow and create jobs but without access to the financing they need to fulfil their potential.

The Nordic DFIs

The Nordic DFIs are part of the Association of European Development Finance Institutions (EDFI). There are 16 EDFI members, all state-owned investment funds (except for OeEB and Sifem), all mandated by their governments to invest in developing countries and emerging markets. Together they have a consolidated portfolio of €16.7 billion with 4,221 projects at the end of 2008, in comparison with the International Finance Corporation (IFC) with €25.1 billion and 1,560 projects. The EDFIs have a large share of their projects in developing countries in Africa, the Caribbean, the Pacific, Asia and Latin America. Overall, the EDFIs tend to have relatively small projects in development-related sectors compared with IFC.

The European DFIs all have different areas of specialization and expertise, often reflecting the comparative advantages of partners in their home economies. This diversity is one of the strengths of the DFIs and helps prevent a one-size-fits-all approach to private sector development in the countries where they invest.

Each of the Nordic countries has its own DFI: Finnfund (Finland), IFU (Denmark), Norfund (Norway) and Swedfund (Sweden). These funds cooperate closely, primarily by sharing knowledge and experiences. Each of them is profiled in this report.

The value added of DFIs in international development policy

The rationale behind the DFI business model is to be "additional" and "catalytic". DFIs are additional in the sense that they seek to invest in regions, sectors and segments that would not otherwise have had access to finance for the private sector. They seek to bring in expertise and provide the support needed to ensure real commercial development of their investments rather than taking a buy-and-sell orientation. DFIs are catalytic by partnering with co-investors and enabling other private sector investors to follow in areas and places that they have proven to offer sustainable investment opportunities.

DFIs offer a particular value added to development policy in three areas:

- Investing in under-served project types and settings (SMEs, agribusiness, post-conflict settings, etc.)
- Investing in undercapitalized sectors (specialization in financial services, energy, infrastructure, etc.)
- Mobilizing other investors (by sharing knowledge, setting standards, etc.)

Development impact

DFIs have a significant direct and indirect impact on developing countries in which they operate. A recent study indicates that the European DFIs together sustained close to two million direct and indirect full time jobs through their investments in 2008. In addition, their investments generated around €2 billion in tax revenue for governments in developing countries.

These significant economic effects are also a major contribution to achieving the Millennium Development Goals (MDGs), the eight specific goals to be met by 2015 that measure progress in the fight against extreme poverty around the world, and which were agreed at the UN Millennium Summit in New York in 2000. When DFIs help finance SMEs or contribute to the development of essential infrastructure in developing countries they have a direct and sustainable impact on poverty.

Links to the global financial crisis

The African continent has fared quite well against initial shocks of the financial crisis, but remains vulnerable to longer-term impacts of reduced investment and broken private investor commitments. As private investors withdraw, private sector projects are being delayed or even suspended.

DFIs could play an important role in ensuring that positive developments in Africa over the last decade are not undermined. While private sector investments fluctuate significantly, DFIs have maintained a level of investment similar to that before the global financial crisis. For example, the total African portfolio of the European DFIs grew by about 10% from 2007 to 2008 equalling €4.3 billion at the end of 2008. DFIs can play a particularly significant role in back-stopping local financial institutions.

However, the DFIs have been severely constrained in their ability to take an active counter-cyclical role in the recent financial crisis. Most global recapitalization funds have gone to international financial institutions as part of the collaboration between major economies. Of the Nordic DFIs, Norfund and Swedfund have received annual capital injections the last couple of years, but only Swedfund has received new capital injections (close to €30 million) with a specific mandate to counter-act the financial crisis in developing countries. Several DFIs also experience that their ability to act is constrained by operational rules related to, for instance, the level of participation in individual investments.

DFIs – the "Third Pillar" of Nordic international development policy

DFIs can be seen as a third pillar in Nordic international development policy, alongside:

- Aid – donations provided to public and civil society partners through bilateral and multilateral assistance programmes
- Multilateral development banks – loan, grant and guarantee financing provided through international and regional financial institutions

All three of these pillars are a valid and important component of international development policy. They represent very different and highly complementary strategies for fighting poverty. All three pillars recognize the role of private sector growth in ensuring sustainable development. But DFIs are the channel that most directly delivers this strategy by providing private sector finance where it is most needed in developing countries. It will be very difficult to achieve international development goals without scaling up these efforts.

DFIs are still very much the smaller partner in Nordic development policy. Net capital infusions to DFIs from governments in the Nordic countries over the last decade are less than 1% of official development assistance through other bilateral and multilateral channels.

This report aims to improve the understanding of the value-added of the DFIs and, in doing so, to spark more debate in each of the Nordic countries about the potential benefits of expanding the role of DFIs in development policies.
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Abbreviations

ACP	Africa, Caribbean and Pacific countries
AWS	Austria Wirtschaftsservice Gesellschaft
BIO	Belgian Investment Company for Developing Countries
CDC	CDC Group
CIS	Commonwealth of Independent States
COFIDES	Compañía Española de Financiación del Desarrollo
DEG	Deutsche Investitions- und Entwicklungsgesellschaft
DFI	Development Finance Institutions
EC	European Commission
EDFI	European Development Finance Institutions
EFP	European Financing Partners
EIB	European Investment Bank
ERR	External Rate of Return
FDI	Foreign Direct Investments
FINNFUND	Finnish Fund for Industrial Cooperation
FMO	Nederlandse Financierings-Maatschappij voor Ontwikkelingslanden
GDP	Gross Domestic Product
IFC	International Finance Corporation
IFU	Danish Industrialisation Fund for Developing Countries
IRR	Internal Rate of Return
LDC	Least Developed Country
LMIC	Lower Middle Income Countries
MDGs	Millennium Development Goals
NORFUND	Norwegian Investment Fund for Developing Countries
ODA	Official Development Assistance
OECD	Organisation for Economic Co-operation and Development
OeEB	Oesterreichische Entwicklungbank
PROPARCO	Société de Promotion et de Participation pour la Coopération Economique
SBI-BMI	Belgian Corporation for International Investment
SIFEM	Swiss Investment Fund for Emerging Markets
SIMEST	Società Italiana per le Imprese all'Estero
SOFID	Sociedade para o Financiamento do Desenvolvimento
SME	Small and Medium Enterprises
Swedfund	Swedfund International
TCX	The Currency Exchange Fund
UN	United Nations

1 Introduction

1.1 Context and objectives

Context

The national development finance institutions (DFIs) play an important and growing role in development policies, also in the Nordic countries. However, the approaches and achievements of DFIs are not always visible and well-understood by policy makers and the public in the Nordic countries.

The approach and experience of the DFIs make them an attractive partner in the drive to fight global poverty. Particularly at this time where a global financial crisis is threatening to set back the recent advances, DFIs merit particular attention as a key way to counter-act the crisis by promoting sustainable economic development and job creation in developing economies.

Objectives

The aims of this report are to:

- Improve the understanding among decision makers and informed public of the value-add of DFIs
- Make the case that DFIs are the 3rd pillar of Nordic international development policies. Additional finance for the private sector as offered by the DFIs plays a crucial role next to the other two main pillars of aid and development banks, in particular around creating economic growth
- Spark debate about their potential expanded contribution to international development

1.2 Report process

Dalberg Global Development Advisors was commissioned by Norfund and Swedfund to produce an introduction to the role of the Nordic Development Finance Institutions in international development policy. The research effort took place between August and October 2009. The Dalberg team collected data and perspectives from a range of actors familiar with the work of the Nordic and European DFIs. Economic data was collected from a range of authoritative sources to put development challenges into context. Extensive data was also collected directly from a number of DFIs to build up the fact base for profile and case studies.

Dalberg is an international advisory group focused on global challenges and development. Dalberg serves a broad cross-section of actors across aid agencies, multilateral banks and investors. The group works on the ground in developing countries and provides research and advice at the global level.

2 Priorities in international development policy today

2.1 Development progress has been slow but steady in developing countries

Although achievement of the Millennium Development Goals is behind schedule, progress has been made on some of the goals[1]

The number of people living in poverty has levelled off over the past few years. Africa's poverty rate has fallen by almost 6% since 2000, primary school enrolment has increased by 36% between 1999 and 2005,[2] and infant and child mortality have decreased by 21% between 1990 and 2008[3]. Furthermore, macroeconomic reforms underway in countries in Africa are producing results in terms of growth and stability. Government setbacks in the 1970s and 1980s in Ghana, Uganda, Tanzania and Nigeria have served as important lessons,[4] and success stories have emerged, such as Ghana, which after decades of poor governance has implemented political and economic reforms since the early 1990s leading to significant declines in inflation and poverty accompanied with impressive economic growth[5].

Economic growth has been an important driver for poverty alleviation

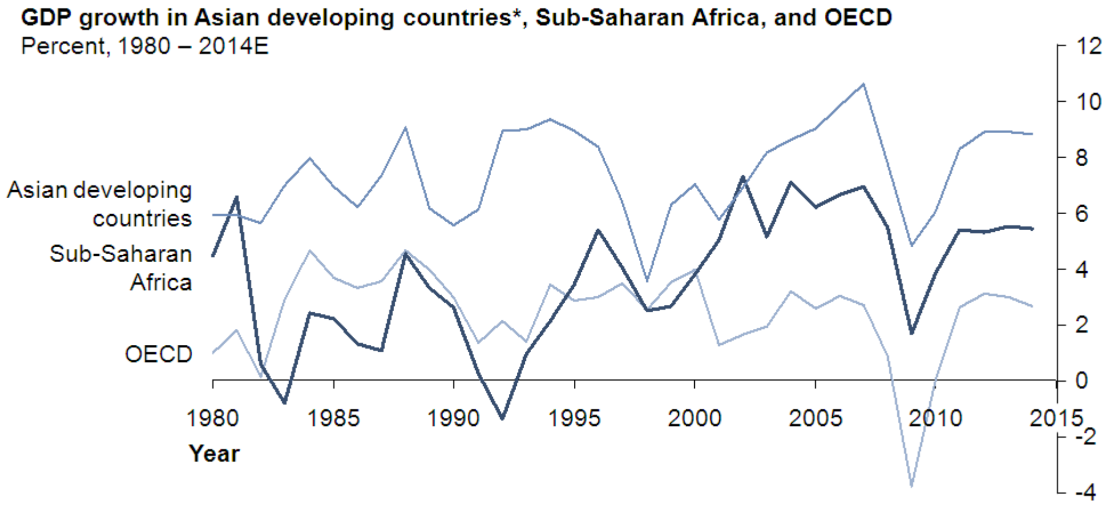
Poverty reduction faces numerous obstacles, especially in the context of several major global economic challenges. The challenges include:

- A financial crisis in the developed countries;
- A growing need for sustainable energy;
- The increasing threat of climate change impacts; and
- A global food crisis.

Despite these challenges and continued high levels of poverty, there is reason for hope as Africa and Asia experience steady growth while OECD countries slow down. GDP per capita has risen steadily in these regions since 1994, and in 2007 Africa had a growth rate of 6.6%, Asian developing countries 9.7%, the Middle East 5.8% and Latin America 5.6%[6].

Exhibit 1 below shows the evolution of GDP growth since 1980 and projected growth through 2014. This positive trend in economic growth is essential for poverty reduction. One significant indication of this link is provided by the World Bank study "Growth Is Good for the Poor" of 80 countries over four decades which shows that as the economy grows, the income of poor people (defined as the bottom fifth of the population) rises by about as much as the income of everyone else[7].

Exhibit 1 – African countries experienced high growth in the past 10 years



* Composed of 23 countries: Bangladesh, Bhutan, Cambodia, China, Fiji, India, Indonesia, Kiribati, Lao People's Democratic Republic, Malaysia, Maldives, Myanmar, Nepal, Pakistan, Papua New Guinea, Philippines, Samoa, Solomon Islands, Sri Lanka, Thailand, Tonga, Vanuatu, Vietnam

Source: International Monetary Fund. (2008): World Economic Outlook database

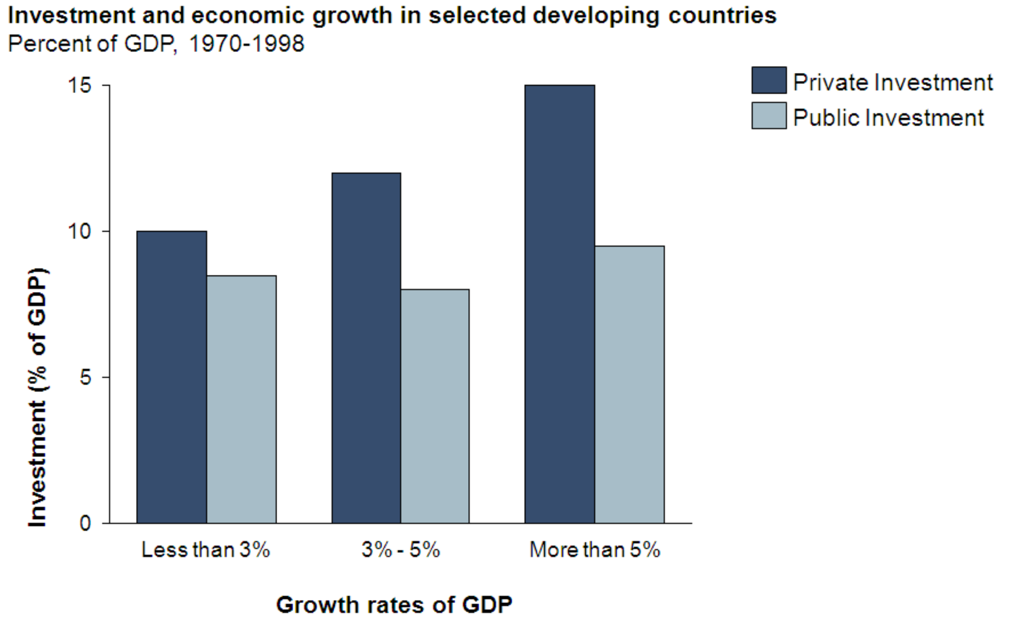
2.2 Growth of the private sector, especially of small and medium enterprises, is essential for economic growth

A thriving private sector is the engine of economic growth

A favourable investment climate helps companies flourish and create jobs. Private investment is strongly associated with economic growth[8]. Research suggests that private investment is more closely associated with growth than public sector investment[9]. This conclusion was especially pronounced during the 1990s where many countries faced public spending constraints but accelerations in private investment, due to market liberalization and reforms.

Exhibit 2 below illustrates the association of private investment with economic growth.

Exhibit 2 – Private investment is strongly associated with economic growth



Source: Bouton, L., and Sumlinski, M. (2000): "Trends in Private Investment in Developing Countries: Statistics for 1970–1998." Discussion Paper 21. International Finance Corporation, Washington DC.

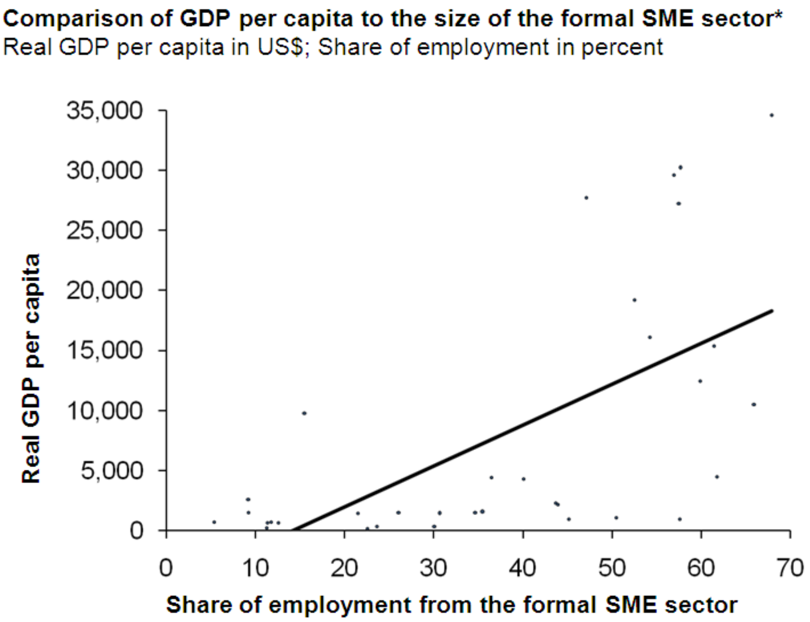
Growth of the private sector is one of the keys to sustainable development[10]. Private firms are a powerful source of job creation in the developing world, which has shown to reduce poverty. Two surveys, from the World Bank and Gallup, support this view. The World Bank survey "Voices of the Poor" highlights the fact that more than 70% of the world's poor believe that the best way of escaping from poverty is to get a job[11]. A survey conducted by Gallup in 26 Sub-Saharan African countries asked 26,506 Africans to rank what they consider as most important to development[12]. Jobs for youth was identified as the fourth most urgent need which was linked to the two first priorities: Reducing poverty and reducing hunger. This means that if the private sector in Africa does not grow very rapidly, many of the half a billion African youths between five and 24 comprising about 50% of the total African population will grow up without prospects of a job[13]. Private enterprises also generate tax revenue and promote investment, information sharing and empowerment of local businesses.

The recent Copenhagen Statement by the African Commission put it like this: "Strong growth and employment opportunities are required to achieve the MDGs, and sustain progress already made in the areas of health, food security and education"[14].

Small and medium enterprises (SMEs) are the backbone of economic activity, and help achieve growth and reduce poverty

At a macroeconomic level, the SME sector is correlated with GDP per capita. Exhibit 3 below shows the positive relationship between the size of the formal small business sector and economic development.

Exhibit 3 – The size of the SME sector is directly correlated with GDP per capita



* 76 countries in sample with results averaged over the 1990s, 17 of which are low-income countries, 31 are middle income and 28 are high income.
Source: Ayyagari, Beck and Demirguc-Kunt, (2003); "Small and Medium Enterprises across the Globe: A New Database", World Bank

SMEs generate a substantial proportion of GDP and employ a large share of the workforce in most developed and developing economies. In OECD economies SMEs and microenterprises account for over 95% of firms, 60-70% of employment, 55% of GDP and generate the lion's share of new jobs.

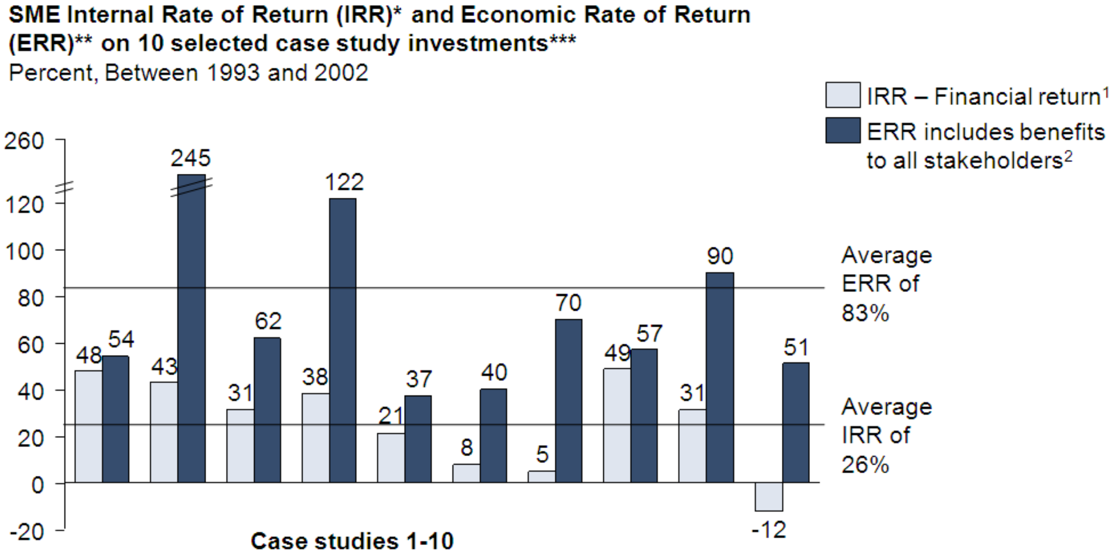
In developing countries, more than 90% of all firms outside the agricultural sector are SMEs and microenterprises, generating approximately 13% of GDP in low income countries and 39% in middle income countries[15]. The examples of Morocco, Bangladesh and Ecuador further demonstrate the importance of the SME sector. In Morocco, 93% of industrial firms are SMEs and account for 38% of production, 33% of investment, 30% of exports and 46% of employment. In Bangladesh, enterprises with less than 100 employees account for 99% of firms and 58% of employment. In Ecuador, 99% of all private companies have less than 50 employees and account for 55% of employment.

Investment in small businesses can realize financial returns and substantial multiplier effects in the economy. At a minimum, small businesses generate impact through job and wealth creation and through the products and services they deliver:

- Employees – wage increases, non salary benefits and labour mobility through training
- Customers – improved quality and/or lower price of goods and services
- Suppliers – increased demand for and sales of goods
- Government – value-added tax revenues
- Broader community – e.g., environmental gains, development of social infrastructure
- Large corporations – supplies and services provided

The 10 selected case studies in Exhibit 4 below demonstrate SME's multiplier effects on the broader community, which leads to high levels of indirect societal returns and benefits, greatly exceeding direct financial returns. These 10 investments in Central and Eastern Europe (CEE) and Latin America show a 26% average return on investment, while the Economic Rate of Return (ERR), which is a broader measure also incorporating the additional benefits and costs to stakeholders in the surrounding community, stands at 83%.

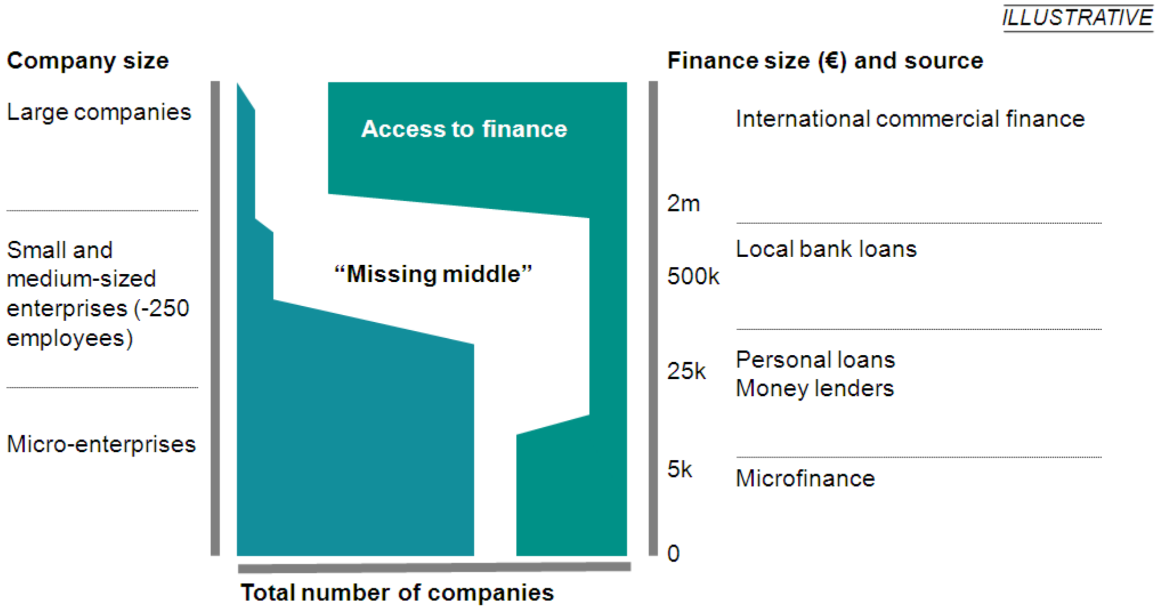
Exhibit 4 – SMEs create positive effects on local communities in developing countries



*Internal Rate of Return is derived from SEAF's valuation of each company, based on European Venture Capital Association methodology
**Economic Rate of Return is derived by SEAF by adding the benefits/costs of investment to stakeholder groups to the model used for calculating the project's financial returns
*** 2 from Poland, 3 from Romania, 1 from Bulgaria, 4 from Peru and 1 from Bolivia
Source: SEAF "The Development Impact of Small and Medium Enterprises: Lessons Learned from SEAF Investments"

However, access to finance is a significant constraint for small businesses in developing countries. Large banks often have a tendency to favour serving larger and wealthier clients. Meanwhile, as shown in Exhibit 5 below, small businesses are too large to qualify for microfinance often lack debt and equity financing, instead relying on informal networks like borrowing from family members or money lenders. This creates a "missing middle" for debt and equity financing.

Exhibit 5 - Lack of access to finance for SMEs is a major barrier to growth

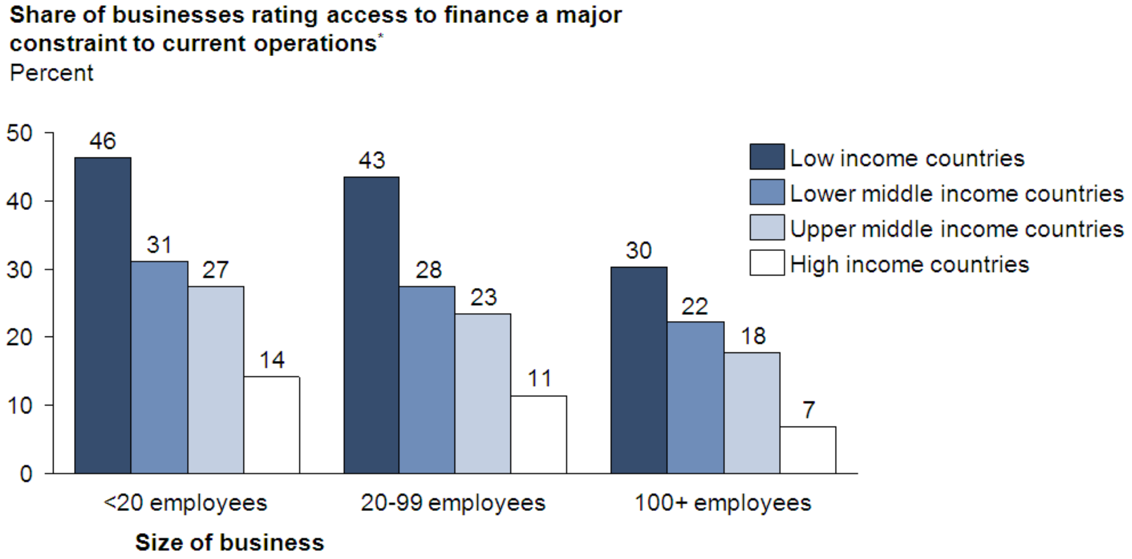


Access to finance is typically better for large and micro enterprises than for SMEs in developing countries

Source: Adapted from CFED Desktop Study: SMEs and Poverty Reduction; Thorsten Beck, Ash Demirguc-Kunt and Vojislav Maksimovic, "Financing Patterns Around the World: Are Small Firms Different?"; Thorsten Beck and Asli Demirguc-Kunt, "Small and Medium Size Enterprises: Access to Finance as a Growth Constraint"

Exhibit 6 below shows that almost half of all small businesses with less than twenty staff in low income countries consider access to finance as a major barrier to their current operations, while only 14% do in high income countries.

Exhibit 6 – Large share of small businesses in developing countries see access to finance as a major constraint



* Countries weighted equally within income groups to calculate overall average; Data collected between 2002 and 2007
Source: World Bank Enterprise Surveys; World Bank List of Economies;

3 Overview of the European and Nordic DFIs

3.1 Definition of a DFI

Definition of a DFI:
A bilateral development finance institution operates almost exclusively in developing countries and countries with transition economies. It is mandated by its respective government to provide long-term financing to the private sector, with specific value-added development objectives, but on a sustainable commercial basis.

Word-by-word definition of a DFI:
Development – Aims to bridge the gap between commercial investments and government development aid and thereby contribute to sustainable economic growth.

Finance – Role of an investor or co-investor who provides structured commercial financing to foreign or domestic companies and financial institutions.

Institution – Specialized investment fund, usually majority owned by the government, with close relations to the national development institutions, but with strong operational independence.

3.2 Overview of the European DFIs

The DFIs vary in size but all have experienced strong growth
The consolidated portfolio of the 16 members of the Association of European Development Finance Institutions (EDFIs)[16], at the end of 2008 stood at €16.7 billion (including un-disbursed commitments) with 4,221 total projects[17]. This marked an increase of €1.8 billion (12%) over 2007. In comparison, the multilateral International Finance Corporation's (IFC) consolidated portfolio (as of June 2008) stood at €25.1 billion with 1,560 total projects[18-19].

The DFIs have demonstrated solid financial performance
Together, EDFIs generated a profit of €145 million in 2008[20]. Over a four year period, the EDFIs have posted a total profit of almost €1.3 billion, and an average profit of €316 million.

The EDFIs have strong presence in Africa and Least Developed Countries
26% of global portfolio was invested in Africa, the Caribbean and Pacific Islands (ACP), compared with 11% by IFC. In total, the EDFI's ACP portfolio equalled approximately €4.3 billion in 2008. The total portfolio in Africa constitutes almost the entire ACP portfolio at €4.3 billion in 2008 with 1,033 projects. New projects in Africa in 2008 amounted to €1.4 billion in 263 projects.

The average size of investments by EDFIs is small relative to IFC
The average project size of the EDFIs' global portfolio was just under €4.0 million, ranging from an Austrian OeEB at €14.3 million and German DEG at €6.6 million to Belgian SBI/BMI at €775,000. In comparison, the multilateral IFC's average project size was four times greater than EDFI (at €16.1 million). IFC sponsored 2.7 times fewer individual projects than EDFI, 1,560 projects in total versus 4,221.

The investment products and mechanisms differ among the EDFIs
Equity comprised 53% of EDFI's €16.7 billion portfolio; ranging from 100% at SIMEST and 91% in Norfund to 0% at AWS and Sofid. Overall, the EDFI portfolio breakdown includes: Equity & Quasi-Equity (53%), Loans (40%), and Guarantees (7%). In comparison, IFC focuses three-quarters of its investments on loans. The corresponding IFC distribution is equity (21%), loans (73%) and guarantees (6%).

The EDFIs invest in sectors considered to have positive social impact but have varied focus areas dependent on their homeland expertise
EDFI average sector split: Finance sector (54%), Industry/manufacturing (21%), Infrastructure (18%), Agribusiness (6%) and Other (2%). In the past three years, the percentage of financial sector investments has increased from 33% in year 2000 to 54% at the end of 2007. The percentage of agribusiness investments has also increased slightly, while the percentage of investments in the remaining three sectors has slightly fallen between 2006 and 2008.

Key statistics from the each of the DFIs, total of the 16 DFIs and IFC follow below.

Exhibit 7 – Overview of the European DFIs, end of 2008[21]

Development Finance Institution	Country	Portfolio in € million[22]	Growth 2007 to 2008, Percent	# of projects	Average project size, € K	Share of portfolio in ACP, Percent
aws erp-fonds	Austria	627.5	26%	474	1,324	1%
bio	Belgium	172.9	37%	77	2,246	27%
CDC	The United Kingdom	3,035.6	(20%)	682	4,451	45%
COFIDES	Spain	431.0	16%	120	3,592	5%
DEG	Germany	4,427.4	24%	675	6,559	13%
FINNFUND	Finland	309.2	29%	106	2,917	29%
FMO	The Netherlands	4,182.1	23%	873	4,791	28%
ifu	Denmark[23]	502.2	2%	303	1,657	19%
Norfund	Norway	491.3	2%[24]	81	6,065	26%
OeEB	Austria	71.5	-	5	14,300	0%
Proparco	France	1,503.1	33%	300	5,010	45%
BMI SBI	Belgium	17.8	(18%)	23	775	12%
SIFEM	Switzerland	250.2	13%	57	4,389	20%
SIMEST	Italian	521.2	9%	361	1,444	5%
SOFID	Portugal	4.0	-	3	1,333	100%
Swedfund	Sweden	172.4	29%	81	2,128	36%
EDFI	European	**16,719.7**	**12%**	**4,221**	**3,961**	**26%**
IFC International Finance Corporation	Global	**25,112.1**	**41%**	**1,560**	**16,098**	**11%**

Source: EDFI, (2009): "2008 Comparative analysis of EDFI members," and Swedfund (2009),

3.3 Profile of the Nordic DFIs

FINNFUND

Background[25]

Finnfund provides long-term risk capital for private projects in emerging markets and Russia. Finnfund was established in 1980 within the context of broader government goals to increase Finnish development aid. It operates as a Limited Liability Company (Oy).

Governance

Finnfund is 84.2% owned by the State of Finland, Finnvera Plc (the Finnish Export Credit Agency (ECA)) owns 15.7% of the share capital and the Confederation of Finnish Industries 0.1%. Finnfund falls under the Ministry for Foreign Affairs. The Finnfund Board consists of six members, one of whom is from the private sector. Three are appointed by the Ministry for Foreign Affairs, one by the Ministry of Finance, one by Finnvera and one by the Confederation of Finnish Industries.

Strategy

Finnfund does normally not finance more than one-third of total investment cost. Undue country concentrations are avoided. Finnfund does not normally invest more equity than the sponsor. An exit strategy must be in place when the investment is made. Investments are done in DAC-countries and others, as approved by the Government. Finnish interest is required in connection with the investments. Finnfund has operating restrictions on tobacco, alcohol/ hard liqueur and beer.

Portfolio

By the end of 2008, Finnfund had 106 projects and a consolidated portfolio of €309.2. It had a 29% growth rate from the previous year and grew further in 2009. Approximately half of its portfolio was in equity and quasi-equity and the other half in loans. A majority of past investments have been in manufacturing and the financial sector, but Finnfund finances projects ranging from agribusiness and power generation to telecommunications and services. See Exhibit 8 below for an overview of Finnfund's investment portfolio.

Exhibit 8 – Finnfund Investment Portfolio

Sector split		Geographic split		Investment type	
Sector	**Percent share**	**Region**	**Percent share**	**Type**	**Percent share**
Financial sector	46%	ACP	29%	Equity	43%
Infrastructure	17%	Latin America	23%	Loans	55%
Agribusiness	-	Asia	25%	Guarantees	2%
Industry	27%	EU, CIS/Russia	9%		
Other	10%	Middle-East	1%		
		Inter-regional	13%		

Source: EDFI. (2009): "2008 Comparative analysis of EDFI members."

Background[26]

The Industrialisation Fund for Developing Countries (IFU) was established by the Danish Government in 1967 as a self-governing Fund. In 1989 the Investment Fund for Central and Eastern Europe was established (IØ).

Governance

IFU/IØ is 100% owned by the Danish government. The two Funds share the same Supervisory Board and Executive Board. The IFU/IØ Board consists of ten members appointed by the government, six of which are from the private sector.

Strategy

IFU invests only in countries with a per capita income below 80% of the World Bank's upper limit for Lower Middle Income Countries (LMIC's) (which in 2009 is US$2.964) plus South Africa, Botswana and Namibia. IØ invests only in Russia, Ukraine and Belarus. IFU has an indicator limit for a single project, which is approximately €13.4million (DKK 100 million), whereas partner risk is limited through the indicative limit that the partner(s) (at group level) should not account for more than 20% of the Fund's total project engagement[27]. Furthermore, as a guideline, the total engagement in a single country should normally not exceed 30% of the Fund's total project engagement. When IFU/IØ withdraws, the shares are normally offered to the other partners. IFU/IØ is tied to national interests as it is a condition that it co-invest with a private Danish partner. IFU/IØ has operating restrictions on, e.g., tobacco and hard liqueur.

Portfolio

By the end of 2008 IFU had 206 projects and an outstanding portfolio at cost of €235 million (DKK1.754 million), with approximately 60% equity and quasi-equity and 40% in loans. IFU have particular focus on industry/manufacturing, infrastructure, agribusiness and the financial sector. See Exhibit 9 below for an overview of IFU/IØ's investment portfolio.

Exhibit 9 – IFU/IØ Investment Portfolio

Sector split		Geographic split		Investment type	
Sector	**Percent share**	**Region**	**Percent share**	**Type**	**Percent share**
Financial sector	10%	ACP	19%	Equity	58%
Infrastructure	14%	Latin America	5%	Loans	38%
Agribusiness	13%	Asia	29%	Guarantees	4%
Industry	52%	EU, CIS/Russia	39%		
Other	11%	Middle-East	6%		
		Inter-regional	3%		

Source: EDFI. (2009): "2008 Comparative analysis of EDFI members."

Background[28]

The Norwegian Investment Fund for Developing Countries (Norfund) was established by the Norwegian Parliament (the Storting) in 1997, under special legislation, as a separate legal entity with limited liability. Norfund is an integral part of Norwegian development cooperation with the mandate to operate as a commercial investor in the private sector in developing countries.

Governance

Norfund is 100% owned by the Norwegian government and managed by the Ministers of the Environment and International Development. The Norfund Board is appointed by the Cabinet and consists of five members, four of whom are from the private sector.

Strategy

Norfund provides loans and invests in equity both directly in companies and through local or regional funds. In geographic terms Norfund focus on four areas; Southern Africa, Eastern Africa, Central America and the Mekong area. Norfund tries to identify commercial viable projects where the lack of capital is greatest. Those projects are often located in the poorest countries and Norfund has therefore a special focus on the least developed countries (LDC). When focusing on LDCs, Norfund often accepts a more substantial role in project development than most commercial investors would find appropriate. Norfund seeks to invest in selected sectors where it already has experience or where it can build on in-depth expertise in the Norwegian business community. Norfund works actively to promote social and environmental sustainability.

Portfolio

By the end of 2008 Norfund had 81 projects and a consolidated portfolio of €491.3 million, 91% of which in equity and quasi-equity, and 9% in loans. Infrastructure with an emphasis on renewable energy and hydropower and the financial sector are Norfund's key focus areas. See Exhibit 10 below for an overview of Norfund's investment portfolio.

Exhibit 10 – Norfund Investment Portfolio

Sector split		Geographic split		Investment type	
Sector	**Percent share**	**Region**	**Percent share**	**Type**	**Percent share**
Financial sector	45%	ACP	26%	Equity	91%
Infrastructure	53%	Latin America	38%	Loans	9%
Agribusiness	2%	Asia	30%	Guarantees	-
Industry	-	EU, CIS/Russia	-		
Other	-	Middle-East	-		
		Inter-regional	6%		

Source: EDFI. (2009): "2008 Comparative analysis of EDFI members."

Swedfund

***Background*[29]**

Swedfund International AB, (Swedfund) has 30 years' experience of investing in emerging markets and operates as a Limited Liability Company (AB).

Governance

Swedfund is 100% owned by the Swedish state and belongs to the Ministry of Foreign Affairs for operational guidelines and overall policy, but reports to the Ministry of Industry and Trade. The Ministry of Industry and Trade nominates its board members (seven at present), with one "owner representative" in the board from the Ministry of Foreign Affairs.

Strategy

Swedfund can provide finance to investments in countries that are eligible for ODA finance. Within this group Swedfund gives priority to the least developed countries (LDCs) and to investments where the development impact is considered to be high. In Eastern Europe, Swedfund can also invest in countries not eligible for ODA and that are non EU members. It cannot make new investments in new EU member states. Swedfund has a policy not to invest more than 15% of its equity in one single project and not more than 20% with one strategic (normally Swedish) partner or more than 20% in any one country. A strategic partner must take a financial risk equal to or exceeding Swedfund's risk exposure. Swedfund has operating restrictions in relation to tobacco, alcohol/ hard liqueur, wine and beer.

Portfolio

By the end of 2008, Swedfund had 81 projects and a consolidated portfolio of €172.4 million. 59% of the portfolio was in equity and quasi-equity, and 41% in loans. Swedfund had a 29% growth rate from the previous year. Swedfund focuses on financial institutions, infrastructure and industry/manufacturing, including telecommunications. See Exhibit 11 below for an overview of Swedfund's investment portfolio.

Exhibit 11 – Swedfund Investment Portfolio

Sector split		**Geographic split**		**Investment type**	
Sector	**Percent share**	**Region**	**Percent share**	**Type**	**Percent share**
Financial sector	38%	ACP	36%	Equity	59%
Infrastructure	29%	Latin America	4%	Loans	41%
Agribusiness	3%	Asia	33%	Guarantees	-
Industry	22%	EU, CIS/Russia	25%		
Other	7%	Middle-East	2%		
		Inter-regional	-		

Source: EDFI. (2009): "2008 Comparative analysis of EDFI members."

3.4 Strength in diversity for the DFIs

Each DFI has different characteristics and strengths

The European DFIs have common mandates but they vary significantly in their strategies and focus[30].

- DFIs have a geographic focus on developing regions and a growing focus on the world's poorest countries. The average share of the European DFI portfolios in Africa, the Caribbean and Pacific countries is 26% but this share varies between 1 and 100%. DFIs also operate in different countries within regions.
- Sector focus also varies. The four sectors with the greatest shares of portfolio are the financial sector, infrastructure, industry/manufacturing and agribusiness. More than half of the DFIs have the majority of their portfolio in the financial sector but the shares of the total portfolios are distributed widely.
- DFIs tend to have a high share of their portfolio in equity or quasi-equity with an average of 53%. However, there are a few DFIs that have the majority of their portfolio in loans with limited holding of equity or quasi-equity.

The DFIs also vary greatly in portfolio and average project size. The portfolio sizes of the EDFIs range from Sofid's €4 million to DEG's €4,427 million with an average of €1,054 million. The average size of investments is €0.8 million in SBI-BMI compared to €14.3 million in OeEB with an average of €4 million[31].

These differences are driven partly by the histories of the individual DFIs and by their expertise. Fund management teams build up their own expertise and investment track record. They are also often able to benefit from the expertise of partners in their home market as well. This allows them to bring technologies and knowhow to their investment projects in developing countries.

Diversity is a strength for the DFIs

The diversity of DFIs mirrors the diversity of the countries in which they invest. Some DFIs may be able to be very successful in a sector or place where others would not invest. Often, the variation in approach is seen to allow DFIs to address needs in many different environments. This diversity helps avoid a one-size-fits-all approach to investing in developing countries and emulates the diversity of the private sector in other settings.

The investment activities of DFIs are related to those of the private sector divisions of multilateral banks, such as the International Finance Corporation (IFC). In the experience of many emerging market investors, IFC and the European DFIs have complementary approaches. IFC has a world-leading expertise in assessing large investment projects in a range of sectors but its processes often consume significant time and resources. On the other hand, DFIs often distinguish themselves by an ability to combine flexible decision-making with good local knowledge and technical standards. IFC is increasingly looking at grassroots business initiatives and stimulating entrepreneurs in low-income settings as it seeks to broaden its own portfolio.

Strategies of the DFIs

DFIs are continuously developing their approach. As emerging market investors and dedicated social investors move into settings where the private sector was previously absent, DFIs develop strategies to extend their reach into new areas. Some of the areas where the Nordic DFIs are currently developing their strategies include:

- Investment in sectors related to clean technologies and local energy generation
- Establishing funds with participation of pension funds and other private sector investors
- Applying new tools to manage environmental, social and governance (ESG) standards to investments
- Frameworks to measure the social development impact of investments
- Closer coordination with traditional development actors like bilateral aid agencies

4 How DFIs have development impact

The DFIs' business model is to be additional and catalytic

The DFIs are "catalytic":

- Catalyze private capital and expertise
- Reduce risk of other parties, increase visibility of opportunities and offer tailored financing solutions
- Create a multiplier effect in which their own investment are paired with additional private investment

The DFIs are "additional":

- Invest in enterprises in developing countries which would otherwise not receive financing or use investment instruments that other private sector investors would not be willing to use
- Bring in expertise and provide support needed to have real commercial development of their investments
- Develop and grow the projects in a sustainable way in opposition to a buy-and-sell orientation
- Invest in small and medium enterprises, with particular focus on Africa

DFIs add value to international development policy in three key ways

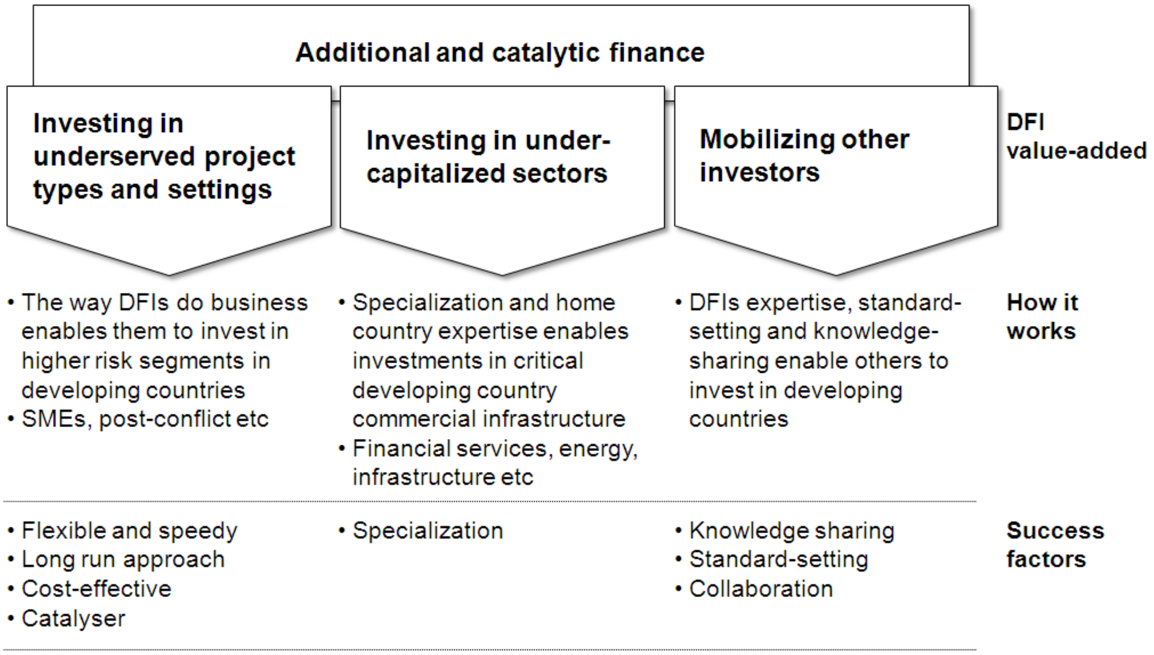
DFIs seek to work in an innovative, non-bureaucratic, effective and collaborative manner. The way they are organized makes DFIs particularly well suited to invest in higher risk markets in developing nations, which are traditionally underserved, particularly in supporting smaller business entrepreneurs. DFIs also have a record of investing in specialized sectors, bringing specific expertise to help secure solid returns on investment over time.

DFIs add value in three main ways:

1. **Investing in underserved project types and settings –** the way DFIs do business enables them to invest in higher risk segments in developing countries
2. **Investing in under-capitalized sectors –** Specialization and home country expertise enables investments in critical developing country commercial infrastructure
3. **Mobilizing other investors –** DFI's expertise, standard-setting and knowledge-sharing enable others to invest in developing countries

Exhibit 12 below provides a framework for these three pathways.

Exhibit 12 - DFIs offer three key areas of value-added in international development policy



Source: Dalberg analysis

4.1 Investing in underserved project types and settings

4.1.1 DFIs are flexible, committed to long-term investing and cost-effective

Flexible and speedy – DFIs have efficient approval procedures

DFIs are relatively small entities with flexible decision making procedures. They can typically decide quickly on investments due to limited bureaucracy in their investment decisions.

DFIs have professional and efficient investment approval processes. The boards of the DFIs constitute of a mix of public and private sector representatives with the necessary expertise to succeed: representatives from the legal and financial sector including private equity/venture capital, from entrepreneurship and innovation, from national politics and from international development.

An example of the speed in which DFIs are able to approve an investment and initiate a new project is captured in the opening address of Jonas Armtoft, Investment Manager at Swedfund, on the Addis Cardiac Hospital in Ethiopia, East Africa's first hospital for cardiovascular diseases: "In October 2006 this was an empty building. Today, just seven months later, we have transformed the building into a hospital. We treat patients here daily and the hospital has more than 50 employees. We have also established an ongoing partnership between doctors and hospitals in Sweden and Addis Cardiac Hospital. And we're saving lives[32]." The hospital is the result of co-investment by Swedfund, Fikmar

Medical, Octupus Medical and Patrik Hjalmarsson AB, Öhman and a few doctors tied to the company.

DFIs can also introduce new products and services quickly in response to market needs, as shown by the DFIs rapid response to the financial crisis. For example, Norfund's €2.7 million loan to the Emergency Liquidity Facility LP (ELF) was quickly approved to enable Latin American microfinance institution (MFIs) to better cope with liquidity problems stemming from the global financial crisis[33]. The investment was spearheaded by the Inter-American Development bank through its Multilateral Investment Fund (MIF) and included other partners, such as Omtrix as the general manager, SECO and Accion. The project uses Omtrix's existing infrastructure, rather than setting up a new funding channel, which would have required additional time.

Another example is Norfund's bridge funding investment in CIFI (Corporación Interamericana para el Financiamiento de Infraestructura, S.A.). CIFI was set up as a financial institution for small and medium sized infrastructure projects in Latin America and the Caribbean. Its 2008 and 2009 results fell short due to the impact of the credit crisis on bank syndication activity. Norfund has been holding equity in CIFI since 2004, when it invested €3.3 million for a 9.3% stake. In 2008, it decided to provide a one year line of credit of up to €6.7 million, as CIFI had been unable to raise sufficient funds under prevailing market conditions[34].

Long term approach – DFIs provide patient capital
Based on a long-term vision and investment commitments rather than emphasis on short term returns, DFIs tend to provide funding for longer periods of time than commercial banks. The average length of investment ranges between 6 and 14 years[35]. For example, Swedfund was in a 14 year partnership with Twiga Cement in Tanzania, which started in 1992. It has posted significant turnover and profit increases during the last years, with operating profits increasing by 60% from 2006 to 2007[36].

Investments in the renewable energy sector, which is a priority area for DFIs such as Norfund and FMO, also require a long-term focus as they tend to involve significant expenditures in the early phases of a project with returns spread over a long period.

Cost effectiveness – DFI's structures and practices facilitate efficiency
DFIs have relatively small and flexible structures and streamlined organizations with authority delegated to investments officers, thereby operating with low transaction costs. EDFIs have standardized their project appraisals, monitoring and the assessments of social and environmental standards, resulting in improvements in cost-efficiency with a correspondent reduction of related costs for their customers. For example, the European Financing Partners initiative described in the case study below has disbursed €280 million to date at virtually no cost by using existing DFI channels[37].

DFI approach catalyzes private sector co-investment
DFIs tend to focus on smaller scale projects in poor countries that are not financed by aid agencies or are not sufficiently attractive to commercial players. They play a catalytic role

by taking a major stake in project risks, thus paving the way for other financiers in areas where commercial investors may not invest on their own on a sufficient scale.

Swedfund's partnership with Engro Energy Limited (EEL) is an example of where DFI financing has been instrumental in helping achieve the goal of setting up a greenfield power plant in Pakistan.[38] Greenfield projects are usually viewed as especially risky by traditional investors, as such projects need to be built up from the ground, increasing uncertainty. Thus the catalytic role of DFIs like Swedfund is particularly instrumental in such cases. The EEL plant will produce much needed electricity by burning a waste product (permeate gas) with no alternative uses. Swedfund's financing has provided the starting point from which Engro Energy has taken off on its path of becoming a major player in the power sector in Pakistan.

Another example was Swedfund's support to Industrial and Financial System (IFS), one of the world's leading developers of business systems[39]. Swedfund was an important partner to IFS in providing counter guarantees for Sri Lankan banks. When IFS wanted to set up operations in Asia, Sri Lankan banks required guarantees in order to finance a newly started project, a project risk Swedfund took on.

A DFI effort showcasing flexibility, good governance, speed and cost savings is the European Financing Partners project (EFP), profiled below.

Case study – European Financing Partners (EFP) and CareWorks Africa Ltd

Large organizational overhead and bureaucratic processes can lead to delays in decision-making and increased costs in the long term. In contrast, DFIs demonstrate their speed and flexible structures leading to cost-savings through the EFP partnership. EFP was created in 2003 as a joint venture between the multilateral European Investment Bank (EIB) and EDFI members to set up a private limited liability company with the double aim of promoting sustainable development of the private sector in African, Caribbean and Pacific States (ACP) and strengthening co-operation between eligible European Development Finance Institutions and the EIB.

The operational structure of EFP is innovative among the institutional investors due to its efficient and fast track process with low administrative overheads[40]. This partnership's objective is to fast track the decision-making process. While it is often difficult to process a project in much less than a year when a number of DFIs are co-financing large projects, the EFP has, as an example, managed to process a large telecommunications project in less than 2 months from first application to disbursement, due to the delegation of authority by the 13 institutions involved in EFP to the single EDFI member in charge of structuring the financing, appraising the project, negotiating the terms and conditions and loan agreement. The EFP does not have any employees and the annual operational costs only amount to €40,000, making it very cost efficient[41]. Through harmonization of procedures, processes, guidelines and checklists EIB and EDFI members have shortened process time and transaction costs, but most importantly, reduced the reporting burden and cost of the investee company considerably.

EFP has financed projects in 11 ACP countries in the following sectors: Agribusiness, banking, communication, health, tourism, housing, industry, infrastructure, power and air transport. It has approved financing to 28 private sector enterprises in Africa, the Caribbean and the Pacific at a total amount of €332 million to date[42]. For example, EFP is disbursing €1.2 million in financing for CareWorks Africa Ltd. in SSA, with IFU as the promoting partner[43]. IFU invested €1.7 million (US $2.5 million) in CareWorks in 2007, (whereby 75% of IFU's investment was syndicated to EFP).[44] CareWorks has rolled out a HIV/AIDS workplace programme and patient management services in subsidiary project companies in SSA countries including South Africa, Botswana, Mozambique, Uganda and Mauritius[45]. EDFI's fast decision-making process has facilitated the mobilization of funds which has enabled the CareWorks program to expand to multiple SSA countries and provide its services to a number of project companies financed by EDFI members and EIB.

Sources: EDFI, EFP, IFU

4.1.2 DFI business model facilitates broader reach

DFIs seek a different risk and return profile than regular investment funds

DFI's local presence in developed and developing countries facilitates their understanding of investment risks.. Some investors refrain from investing in developing markets, for instance in Sub-Saharan Africa, because they are perceived generally to be too high risk. This can mean that good investments opportunities do not obtain financing. The local presence of DFIs helps mitigate potential risks by increasing legitimacy, stabilizing funding and providing know-how.

Internationally, there has been much recent debate about the relative strengths of aid agencies and investors in contributing to development. There are significant differences in approach and practices. While the different approaches are highly complementary more can be done to build shared understanding of potential synergies.[46]

Commitment to investing in underserved markets often positions DFIs among first-movers

The Nordic DFIs invest a large share in countries that stand towards the low end of World Bank and Doing Business' 2010 report ranking on 'Ease of do business.' The Doing Business (DB) system ranks 178 countries based on 10 dimensions in an attempt to measure and compare business regulation related to start-up, operation, and growth of operations[47]. A low ranking on this scale indicates a challenging business environment that traditional investors are hesitant to enter into. Norfund and Swedfund have invested almost half of their portfolios in countries that fall in the bottom half of the ranking, which include Zimbabwe, Afghanistan, Angola and Pakistan.[48] Swedfund also has a project in Somalia which was not even included in the study due to its status as a lawless collapsed state[49]. Finnfund has also invested in frontier markets and is, among other things, engaged in agribusiness in Sierra Leone and forestry in South Sudan.

An example of frontier investment is Swedfund's and FMO's investment in Somalia, where together with the Somali Telecom Group and Celtel Alumni intend to transform the telecommunications industry in Somaliland and Puntland, combining capital, corporate governance expertise, emerging market telecommunications knowledge, and local know how[50].

A final example is the setting up a Private Equity fund targeting medium sized companies in Angola called Fundo de Investimento Privado Angola (FIPA) by Norfund, together with Banco Africano de Investimentos (BAI). FIPA is Angola's first private equity fund[51].

DFIs are able to support higher risk segments such as SMEs
Commercial banks tend to provide finance for businesses to invest in relatively low-risk projects in more developed sectors and regions. DFIs can play an important role in servicing investment needs of smaller scale projects in developing countries and emerging markets.

For example, Norfund invested in APIDC Biotech, a Biotechnology Venture Fund that was formed to make equity, equity-related and mezzanine investments in start-up and early stage life sciences businesses in India[52].

Another example is Aureos, which is a leading global private equity fund providing risk capital for expansion and change-of-control transactions for established businesses in the small to mid-cap segment in emerging markets.[53] Aureos manages 15 regional private equity funds in Africa, Asia and Central America. Since its inception in 2001, Aureos has increased its capital to over US $1 billion, covering more than 50 emerging markets. The Africa Fund specifically raised a total of US $312.8 million. Additionally three regional African funds have been established in East, West and Southern Africa with committed capital of US $40 million, US $50 million and US $50 million, respectively.[54]

4.2 Investing in under-capitalized sectors

4.2.1 Specialization and home expertise enables investments

DFIs provide capital and expertise
Financial sector: SMEs and micro entrepreneurs have specific funding needs which DFIs working in partnership with local banks are well suited to provide. Smaller domestic banks are seen as being particularly adept at providing finance to small businesses in the manufacturing, farming and services sectors of developing countries due to the sectors' relative simplicity, and the banks' local knowledge[55]. Evidence suggests that growth is faster in countries with a larger amount of small domestic banks, in part due to their ability to provide funding to competitive small businesses[56]. For example, FMOs program "Massif" contributes to the development of financial services for SMEs[57]. It offers local financial intermediaries long-term debt and equity in local currency and assumes currency risk. This makes it possible for the financial intermediaries to provide local currency products to SMEs. Other examples are Swedfund's investments in Small Enterprise Foundation (SEF),[58] a microfinance institution in South Africa, and Micro Finance Bank of Azerbaijan (MFBA), a leading microfinance bank in the region[59].

Infrastructure: Infrastructure is indispensable to achieve the main development targets in developing countries, such as industrialization, export promotion, equitable income distribution, and sustainable economic development. Investments in infrastructure can help people in developing countries by extending their access to basic infrastructure and by improving the quality and reliability of infrastructure services. The DFIs invest heavily in infrastructure, for example, Norfund's investment in the renewable energy company SN Power, which have projects and operations in Asia, Africa and Latin America,[60] Swedfund's investment in the water purification company ASCE,[61] Swedfund's investment in Indian Infrastructure Equipment Ltd, Swedfund's investment in the telecommunications company, Enitel, in Pakistan, Finnfund's investment in the AIG African Infrastructure Fund and Finnfund's investment in the Indian telecommunications company Bharti Airtel Limited[62].

Forestry: Sustainable forest management is a key sector for economic development in many countries[63]. Forestry needs to produce sustainable environmental and economic results. The promotion of forest restoration projects and the implementation of sustainable forest management are also important climate change mitigation efforts[64]. Several DFIs aim to support commercial forestry as a viable source of economic growth which is compatible with sustainability. For example, Finnfund's investment in Compania Forestal Oriental, Uruguay's largest wood producer, and in Valley Teak Co, a teak plantation in Tanzania[65].

Agriculture: Local farmers often face barriers to exporting agricultural products on a mass scale. In particular, they are hampered by market fluctuations and buyer uncertainties. Norfund has invested to help the Matanuska banana plantation in northern Mozambique sell its fruit to Chiquita for export to Europe and the Middle East[66]. This will be the first large-scale export of bananas from south-east Africa. The German DFI's (DEG) investment in the Uruguayan company S.A. Molinas Arroceros Nacionales (SAMAN) is another example[67]. SAMAN processes rice from more than 200 local farmers to a consumer product. Some 90% of production is for export and earns vital foreign currency for the country. SAMAN pre-finances farmers' harvest, advises them on planting and provides seed and fertilizer.

A specialized investment in the financial sector is the Currency Exchange Fund N.V (TCX) profiled below.

Case study – FMO and partners Currency Exchange Fund N.V (TCX)

Due to high currency volatility in developing nations, investing and lending in local currencies carries significant risks. FMO and over twenty partners (including Norfund, IFU and 5 other EDFI members, multilaterals and commercial banks in Africa and Europe), have invested in a fund which allows investors to cover their local currency risks – called the Currency Exchange Fund N.V (TCX). TCX is a special purpose fund providing market risk management products to investors active in emerging markets. The fund focuses on currencies and maturities which are not covered by regular market providers[68]. Its service offers are extremely valuable to investment partners in developing nations and serve to catalyze long-term lending in local currencies despite the inherent risks in these non-liquid emerging market currencies.

TCX manages its risk through portfolio diversification across some 30 currencies, such as Bangladesh Taka, Zambia Kwacha, and Dominican Peso. This large and innovative fund started up with a transaction capacity of US $1.2 billion.

The results so far suggest drastically reduced default probability, improved business sustainability, and a major contribution to the development of local capital markets[69]. The importance of such a service offering is underscored by increased currency volatility related to the financial crisis. However, the ongoing crisis also creates a challenging business environment for TCX. Still, TCX's performance indicates that it is well positioned to absorb currency shocks in a global crisis. TCX's biannual figures in June 2009 indicate a profit of US $42.2 million for the first half of 2009; making up for portfolio losses in 2008 associated with the financial crisis and the sharp appreciation in the US dollar against the majority of emerging market currencies. This rapid recovery appears to validate the TCX business model developed in collaboration with a number of financial institution partners.

Sources: TCX and Norfund

4.2.2 DFIs investment in critical sectors underpin growth

Upgrading critical commercial infrastructure

DFI investments in the *financial sector* foster development and strengthen local financial sectors in developing countries. For example, only 4% of people in Sub-Saharan Africa have bank accounts according to the UN Capital Development Fund,[70] suggesting that a great need for credit and augmented financial services. DFIs bring financial sector expertise and work with private local financial institutions in ways that build the long-term viability and sustainability of a financial services sector that meets the needs of local businesses

DFI investments in *infrastructure* increases access to electricity, telecommunications, transport and water, which provides the basis for a sound economic development. World Bank's 2004-2007 Enterprise Surveys indicate that infrastructural limitations are one of most pressing constraints to Africa's private sector as almost 60% of survey participants rank infrastructure as their top constraint[71]. For example, one in four people around the world live without electricity; this includes 500 million people in Africa alone,[72] and 84% of the Sub-Saharan African population has little to no electricity coverage[73]. The DFIs' investments in infrastructure provide people in developing countries with basic infrastructure and help improve the quality and reliability of existing infrastructure services.

DFI investments in *forestry* increases the regeneration potential of national forests and counteracts global warming, thereby ensuring environmental conservation. The forestry sector, which includes pulp and paper, as well as timber, is entirely dependent on natural resources. Natural and plantation forests, which provide the inputs necessary for the survival of forest industries also provide vitally global ecosystem services, habitat for plant and animal species and a wide variety of goods and services to communities.

DFI investments in *agribusiness* increase the food supply and improve the export capabilities, which are particularly important in many developing countries where agriculture forms the backbone of their economies. Agribusiness is the largest source of employment in poor countries, accounting for 64% of employment and 34% of GDP[74].

4.3 Mobilizing other investors

4.3.1 DFIs promote knowledge sharing, standard-setting and collaboration

Knowledge sharing between DFIs and standard-setting allows use of best practices
DFIs share knowledge and expertise among themselves and with other players in the market and harmonize approaches. For example, through efforts under the umbrella of the EDFI, the 16 DFI members can share knowledge and best practices. The EDFIs have collaborated on harmonized standards for comprehensive assessment and monitoring of the environment, social and governance factors (ESG) and an exclusion list, which specifies businesses and activities in which they will not jointly invest. The EDFIs have also developed principles for responsible financing which provide DFIs with a standardized foundation for how to consider social and environmental risks.[75]

DFIs also collaborate with multilateral banks and aid agencies and local partners
The DFI approach has inspired and enabled other investors. DFIs act as facilitators for European companies and other investors in developed countries, who may be interested in participating in projects in developing countries, but lack the means and connections to initiate such collaborations. DFIs lend credibility and inspire trust among potential investors. The innovative nature of the European Financing Partners (described in a case study above) is captured in a 2008/09 evaluation stating: "Larger partners focus on financial leverage and risk sharing while smaller partners focus on the exchange of experience and best practices. These diverse strategic objectives are not only coherent with the objectives of the EFP, but greatly contribute to achieve them. Through its operation, the EFP has proved to be an effective and efficient instrument in strengthening co-operation among partners. Furthermore, overall the partners feel satisfied with the experience and provide concrete examples of reinforced co-operation."

DFIs provide an avenue for investors to get involved and support fellow DFIs and multilaterals by creating a mechanism that spreads risk through co-financing and that draws on the respective expertise of each partner. More than 50% of projects in Swedfund's pipeline for 2010-2012 are joint ventures with fellow DFIs, a quarter is made up of collaborations with Swedish businesses and the remainder is comprised of partnerships with local investors in developing nations, such as African commercial banks[76].

Local entrepreneurs in developing countries may lack connections with partners with specific technical expertise and sources of financing. For example, Swedfund and SAS have collaborated with Dahaco in Tanzania to develop a passenger and freight handling service in Tanzania[77]. In another project, Swedfund partnered with Uruguayan lemon farmers called NYKLauritzenCool. The managing director Mats Jansson stated: "The right partner not only expands the opportunities, but also reduces the risk in a new market"[78].

DFI emphasis on knowledge sharing, standard-setting and collaboration result in innovative solutions which help mobilize investments and support businesses, such as the Norwegian Microfinance Initiative project profiled below.

Case study – Norfund's Norwegian Microfinance Initiative (NMI)

Norfund's Norwegian Microfinance Initiative (NMI) demonstrates a unique collaboration between DFIs, private investors and Norad, (the Norwegian aid agency). Launched in 2008, Norfund has contributed half the capital of €72 million, while the rest was invested by its private partners, Ferd, KLP, Storebrand and DnB NOR /Vital. NMI's partners in Norway have extensive experience and expertise in banking, insurance, pension fund management, and investments. This unique assemblage of partners allows NMI to provide broad and deep financial services resources to portfolio MFIs while Norad contributes technical assistance support.

NMI invests directly and indirectly in microfinance institutions through equity, loans or the issue of guarantees. It also provides professional support (technical assistance) for microfinance enterprise institution-building mainly through the development of human resources. The fund is specifically targeting local currency structures in its direct investments. The funds operate on a commercial basis providing both development effects and financial returns, leading to the strengthened economic position of poor people, jobs and social progress[79].

Sources: Norfund

4.3.2 DFI track records enable other investors

The DFI approach enables other investors to go further

For many private sector investors it is a significant challenge to enter new emerging or developing markets. The opportunity to gain access to the experience and track record of DFIs have often allowed investors to go further than they would otherwise have been able to.

DFIs build local domestic capacity, also at home

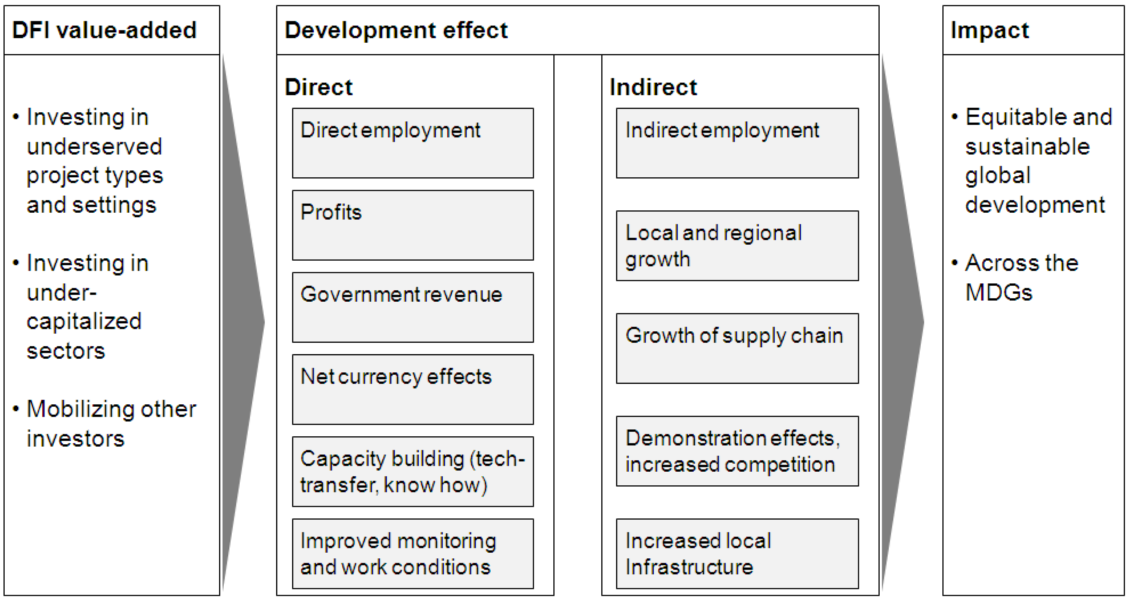
In some developed countries DFI's are among the most significant hubs of expertise and experience in investing in developing markets. The investment professionals that they have trained over the years often go on to deploy their skills in other national and international investment funds.

5 Economic and development impacts of DFIs

DFIs' emphasis on socially responsible and sustainable investment promotes positive economic and development impact

DFIs generate development effects both directly on their projects and indirectly in the broader community in developing countries, along the pathway summarized in Exhibit 13 below. The key impacts include: jobs, project profit, government revenue, net currency effects, as well as capacity building, improved working conditions, environmental standards and broader community benefits like supply chain growth.

Exhibit 13 – DFI's direct and indirect development effects



Source: Swedfund. (2008): "New thinking, new markets - Sustainability report 2008"; Norfund. (2008): "Creates value, combats poverty – Contribution to development 2008"; Dalberg analysis

DFIs measure impact based on key impact indicators – employment, profits, government revenues and net currency effect[80]

DFIs create new jobs and provide productive employment opportunities through the companies they invest in. In 2008, 56,000 new jobs were created as a result of DFI projects; EDFI project companies provided direct employment for 300,000 people and procured another 1,389,000 indirect jobs through their value chains (relations with suppliers) and sub-contractors

The consolidated EDFI portfolio equalled €16.7 billion at the end of 2008. In total European DFIs generated €145 million in profits in 2008[81].

DFI projects contributed to over €2 billion in local taxes in developing nations. This marks a €500 million increase from 2007[82]. This is especially significant as DFIs work in developing countries where governments often lack funding as well as the capacity to raise funds. It is also important to note that these results can be viewed as conservative as they were compiled only for EDFI productive companies and infrastructure projects, and exclude financial sector projects including private equity funds.

DFI projects contributed €4.3 billion in 2008 in total net currency effects. Net currency effects are defined as the percentage of exports and imports in sales and purchases which could assess the level of contribution to the national balance of payment contributed by the investee companies. This is an useful measure because most low income countries have a balance of payments deficit; so contributing to reserves gives stability to the macroeconomic environment. For example, DEG estimates that 91% of African investee countries have payment deficits[83]. The €4.3 billion in total net currency effects can be viewed as conservative as it is only assessed for productive companies, but not infrastructure or financial sector projects including equity funds.

The quantitative development effects contributed by new commitments in 2008 by European Development Finance Institutions are summarized in the table below[84].

Exhibit 14 – EDFI development effects 2008

Indicator	Impact
Jobs	Direct: 56,000 new jobs and 300,000 employed on EDFI projects Indirect: 1.4 million thought value chain
Profit	€145 million
Government revenue	Approximately €2 billion
Net currency effects	€4.3 billion

Source: EDFI. (2009): “2008 Comparative analysis of EDFI members.”

In comparison, IFC noted that its clients provided 2.1 million jobs in 2008 and 700,000 jobs in manufacturing and service sectors in 2007.[85]

The DFIs also have non-financial indirect and direct impact

Direct effects - Capacity building – transfer of technology and know-how: DFI projects provide on-the-job training of local staff and build skills, especially among vulnerable groups like women. DFI projects also provide opportunities for home country professionals to develop their skills in a developing country environment. Furthermore, they encourage businesses to become socially and financially involved in their communities through demonstration effects and provide a means of transferring know-how and technology that in many cases would otherwise only benefit the developed world. For example, the Aureos Africa Fund is a joint venture with CDC contributing staff and overseas offices and Norfund providing cash to help set up new fund management companies on the ground. This project provided capacity building in the form of on the job training for its staff and built up the local management capacity and know-how in running a fund management company.

Direct effects - Improved monitoring and work conditions: Environmental and social standards are promoted through demonstration effects as DFI projects adhere to strict governance and monitoring standards. Thus, local investee companies are incentivized to create more transparent governance structures and better adhere to local labour laws and child labour restrictions, fair wage practices, gender equality and environmental standards. DFIs also introduce governance and accountability standards and expertise which most SMEs lack.

Indirect effect - Broader benefits to local community such as local and regional growth, demonstration effects and increased competition, growth of supply chain, and increased local infrastructure:

- DFI projects foster local and regional growth. It provides employees with direct income which supports their families and increases economic activity through consumption and savings at the local level. The services rendered by DFI companies such as more efficient transport and freight services, directly benefit the local economies and stimulate business
- Successful projects impact the entire value chain from suppliers and subcontractors, who benefit from increased work
- More products and services on the market directly increase competition, and provide incentives to replicate successful DFI project business models
- The broader community benefits from enhanced infrastructure, health and agribusiness as DFI projects create common goods and services, such as roads, electricity, and hospitals; and also promote food security

The four case studies below on the SME fund manager, Aureos Capital; a dairy producer, Fan Milk Limited; a pharmaceutical company, Universal Corporation; and a renewable energy company, Bugoye hydropower station, are examples of the development effects of DFI investments.

Case study – Aureos Capital Partners

Aureos is widely recognized as the leading player in investing in SMEs in developing countries and currently manages 15 regional private equity funds in Africa, Asia and Latin America. Since its inception in 2001 and via the promotion of founding partners CDC and Norfund, Aureos has increased its capital to over US $1 billion, covering more than 50 emerging markets in 25 offices employing 85 investment executives. A new recently established Africa Fund had by end of September 2009 raised more than US$350 million and builds on expertise gained in three original regional funds in East, West and Southern Africa.

Aureos contributes significantly to the growth of the SME sector, job creation and increased government taxes. Aureos estimates that for every dollar invested in SMEs in East Africa, three dollars are paid in government taxes. Furthermore, Aureos has instituted a SME Sustainable Opportunities Initiative, which provides financing for environmental and social improvement projects in particular in clean energy, energy efficiency and carbon emissions' reductions. The first use of this initiative was in a project at the Athi River Steel smelting and manufacturing plant in Kenya in 2008 to reduce factory emissions.

Aureos has also launched two initiatives to build capacity in improved management of SME businesses and to promote responsible HIV/AIDS practices. Aureos' SME practices training programme was established with the support of the government of India and in partnership with a group of top Indian business schools to provide training for management in Aureos' portfolio companies. So far, over 150 managers from SMEs across the world have attended a series of courses. Aureos has further initiated research to identify best practices among its portfolio companies in sub-Saharan Africa with respect to HIV/AIDS by reviewing the supply chain of 14 companies and 150 healthcare providers to see how their distribution networks could be used to deliver healthcare goods and services to remote rural and high density urban populations. Six individual supply chains were identified through which condoms, malaria nets and over-the-counter drugs could be delivered inexpensively throughout East Africa. Aureos' effort is estimated to be able to reach over seven million people on a weekly basis.[86]

Sources: Aureos and CDC

Case study – Finnfund's investment in Universal Corporation in Kenya

The pharmaceuticals company Universal Corporation produces off-patent generic drugs for Kenya and 15 other African countries. While keeping costs low by relying partly on second-hand equipment procured from Europe, the company has built a production facility that is the most modern in East Africa.

Universal Corporation has been awarded the European PIC/S certification and is working to get the WHO prequalification. If successful, the company could become the first pharmaceutical producer between Egypt and South Africa with the necessary quality standards to bid for international tenders for drugs to treat HIV/AIDS, malaria and tuberculosis.

Finnfund invested in Universal Corporation in 2005 and again in 2008 to expand and upgrade the production facilities and processes towards WHO prequalification and to finance the company's environmental investments. Finnfund has also provided technical expertise. Universal Corporation is now one of Finnfund's largest investments.

At the time of Finnfund's appraisal, Universal Corporation had just opened its first production lines. Since then it has expanded production many times over and this year produces more than 600 million pills. The company now employs about 300 people to produce about 100 different drugs ranging from anti-malaria and painkillers to drugs used to treat fungal skin infections and diarrhoeas or to de-worm humans or animals. It exports to 14 neighbouring countries and is currently making investments to triple its production capacity. Much of the production increase will be exported.

Drugs that are both affordable and of high quality have large development benefits in countries where many of the competing products, whether imported or locally made, are not produced under any recognized standards. According to WHO, many of the drugs sold in Eastern Africa do not contain the ingredients they are supposed to have and hence cannot cure the diseases they are used to treat.

Sources: Finnfund

Case study – Norfund's investment in Bugoye hydropower station in Uganda

Norfund has co-invested €6.6 million with Norway's TrønderEnergi in the Bugoye hydropower station in Western Uganda. This is the first commercially financed hydropower facility to be completed in Uganda and is in response to the country's long-standing policy to promote private power generation. Strong demand growth combined with hydrological restrictions on existing power plants on the Nile have lead to both extensive load shedding and heavy dependence on expensive diesel and fuel oil generators. The production of the Bugoye hydropower station will be 6.5% of current electricity demand in the country, and will reduce both power outages and dependence on diesel fuel.

Norfund and TrønderEnergi have emphasized health and safety issues during construction as well as recruitment and training of labor from the project vicinity. The area is densely populated, and the power plant has a relatively large footprint in the local community. Great attention has been paid to compensation and mitigation measures as well as a good dialogue with local residents, formalized through the Bugoye Participatory Committee. Special attention has been paid to gender issues in the resettlement programme, ensuring that women receive title to land and housing as appropriate. The project company also contributes to local development through an ambitious CSR programme, including reconstruction of the local clinic, malaria prevention measures, HIV/AIDS awareness raising, tertiary education for women and support for local sports teams.[87]

Sources: Norfund

Case study - IFU's investment in Fan Milk Limited

Fan Milk Limited Nigeria was incorporated in 1960 to produce milk products including yoghurt and ice cream to complement the protein requirements of Nigerians. IFU invested in the end of the 1990s in order to provide the company with much needed financing for further growth. The financing went to, among other things, the renovation of the diary production plant in Ibadan in Nigeria which is now Fan Milk's flagship in West Africa. Other IFU-financing has also supported Fan Milk's expansion to Benin, Burkina Faso, Côte d'Ivoire, Ghana, Mali, Niger and Togo.

Fan Milk has ensured to customize its products and packaging to local markets. This customization and the effective distribution have made it possible for the populations in West Africa to buy fresh dairy products at affordable prices. The distribution of the products is done by independent entrepreneurs who have acquired one or more of the Fan Milk's bikes with financing from Fan Milk.

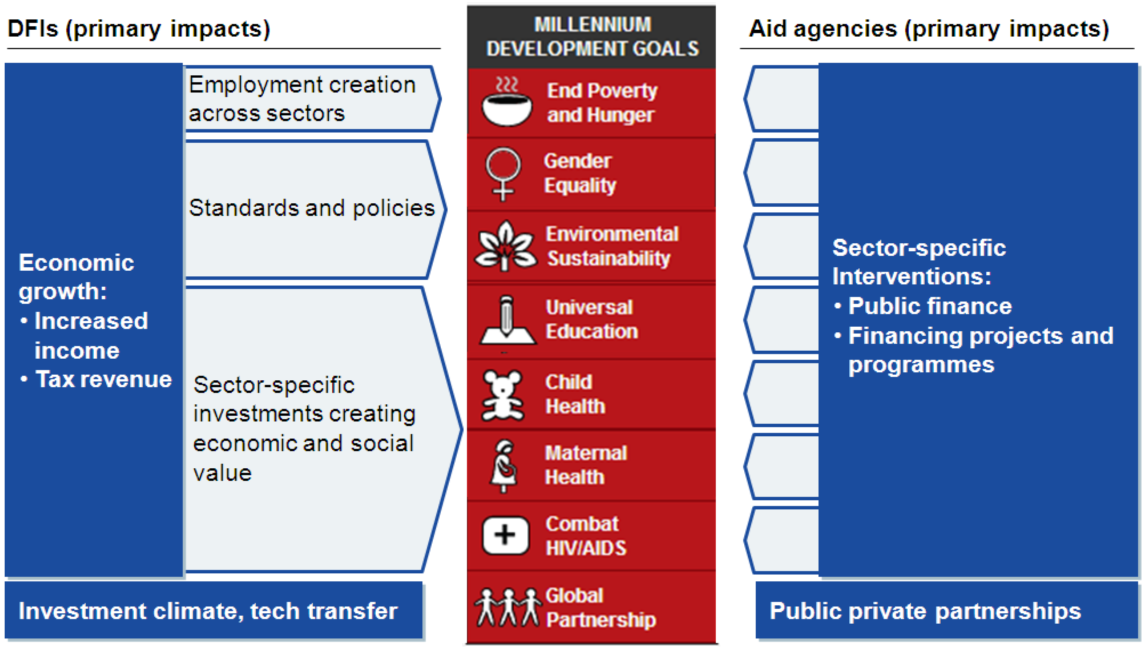
This co-investment by IFU has in Nigeria alone helped create 2,700 direct jobs, including more than 400 jobs at the top-modern diary production plants in Ibadan, and Fan Milk estimates that it has helped create more than 8,000 indirect jobs.[88]

Sources: IFU

Through these direct and indirect development effects, the DFIs contribute to the Millennium Development Goals

DFI projects make direct and indirect contributions to the Millennium Development Goals (MDGs) as described in the exhibit 15 below.

Exhibit 15 – Primary development impacts of DFIs and aid agencies



Note: Goals have been reordered for the purposes of illustration
Source: United Nations. "End poverty 2015, Millennium Development Goals: Make it happen" http://www.un.org/millenniumgoals/; Dalberg analysis

The DFIs also have indirect impact on the MDGs as increased income for individuals makes it possible for them to increase spending on education and health services and increased tax revenues for the government may lead to improved provision of social services.

Swedfund's investment in the Aluminium Sulphate Company of Egypt (ASCE)[89] provides a good illustration of how DFI investments impact the MDGs. ASCE was established in 1986 with Swedfund as a minority stakeholder to fill a market need and produce safe drinking water from contaminated water from the Nile River. Local production of aluminium sulphate, a substance used for water purification, was started for the first time while previously all aluminium sulphate had to be imported. Swedfund not only contributed through providing the extra finance needed, but also was instrumental in bringing in an outside partner specializing in water purification technology, Boliden (today Kemira). Swedfund remained as an ASCE stakeholder for over two decade and helped stabilize its operations and technological capacity. See Exhibit 16 below for an overview of ASCE's impacts on the various MDGs.

Exhibit 16 – Impact on the MDGs by one DFI investment

MDGs	Impact of the investment in ASCE
MDG 1: End poverty and hunger	• 240 direct employees • Increased productivity benefiting financiers through higher profits, and employees receiving higher wages
MDG 2: Universal education	• By increasing economic activity, additional tax revenues and income becomes available for increased spending on education
MDG 3: Gender quality	• Increased access to pure water, removing a laborious task which is traditionally reserved for women • Increased participation of women in the workforce
MDG 4: Child health	• Lower prices on input to purify water lead to cheaper water purification which increased access to clean water and thereby reduces infant mortality
MDG 5: Maternal health	• Company provides health insurance and maternity leave • Indirect impact through increased access to clean water
MDG 6: Combat HIV/AIDS	• Company provides health insurance • Indirect impact through increased access to clean water
MDG 7: Environmental sustainability	• Savings of €8 million help reduce price and increase quantity of clean water resulting in improved access
MDG 8: Global partnerships	• Made available benefits of new technologies in local production of aluminum sulphate

6 Links to the global financial crisis

6.1.1 How the global financial crisis impacts Africa

The African continent fared well against initial shocks of financial crisis but remains vulnerable to longer term impacts related to reduced investment and broken private investor commitments[90]
The African continent was less impacted by the initial shocks of the financial crisis stemming from OECD countries than initially expected. The African countries are doing much better than expected due to progress in diversifying their economies, as seen by the recent proliferation of private equity funds from about €870 million in 2006 to €3.5 billion in 2008.

However, the global financial crisis has become a development crisis with negative investment impacts on Africa and LDCs
Progress has been made in over the last decade in building the foundations for higher growth and poverty reduction, but is now being undermined by the global financial crisis. While the initial effects of the financial crisis were slow to materialize in Africa, the impact is now becoming clear as the global crisis has widened the financing gap on the African continent, reduced trade and capital flows, slowed down private sector lending, contracted foreign reserves and increased fiscal deficits.

The tendency towards more cautious private investment strategies also weakens local confidence in equities and bonds on the African Stock Exchange, as its relatively small size and illiquidity is amplified during times of reduced economic activity. The African Development Bank estimates that the expected shortfall in export revenues amounts to US $251 billion in 2009 and US $277 billion in 2010 for the continent as whole, with oil exporters suffering the largest losses. Africa's growth rate is forecasted to dip below 3% in 2009 (2.8%) for the first time since 2002. The trend in foreign direct investment in Africa in the near future is expected to be highly uncertain.[91]

As private investors withdraw, private sector projects have been delayed or even suspended and regional engines of growth have been the first affected
The financial crisis is sweeping away firms, jobs, revenues, and livelihoods. The financial crisis is a development crisis. Large, financially developed and open economies have been the first to be hit by the crisis through financial markets, e.g., Algeria and Nigeria for exports like oil and South Africa for the mining sector.

For example, the effects in South Africa have been the following:
- Financial sector experienced a steep drop of asset prices, dramatic increases in the cost of capital, and a severe contraction in lending leading to sharp downturns in the retail and manufacturing sectors
- Between May 2008 and March 2009, South Africa's JALSH index has fallen by about 46% and the Rand depreciated by 23% against the US dollar
- The mining sector is experiencing a large fall in output and employment, driven by lower world demand for commodities

6.1.2 The DFIs could play an important role in helping to sustain positive developments in Africa, but are barred by capital constraints

The DFIs can have direct counter-cyclical effects, back-stop financial institutions and function as stabilizers during the financial crisis
Direct counter-cyclical effects - Private sector investments fluctuates greatly while DFIs have direct counter-cyclical effects: although the developing world, especially Africa, has experienced a dramatic reduction in investments by the private sector, DFIs have maintained a similar level of investment as previous years. The African portfolio of EDFIs has increased by about 10% to almost €4.3 billion from 2007 to 2008. However, demand is still exceeding supply. As the African Development Bank (AfDB) Private Sector Department has described it: "The expected overall effect of the credit crisis is a general contraction of private sector activity. No sector will be spared and the weak may not survive. The AfDB and other Development Finance Institutions (DFIs) have witnessed a sudden surge in demand for financing from both the financial and real sectors to fill the void created by the market withdrawal of international commercial banks".

Back-stopping financial institutions - DFIs provide financial institutions with crucial back-stopping when other private investments dry up: the activities of DFIs support the functioning of the private sector, especially in times of crisis, when commercial banks are driven out by risk factors or liquidity shortages and no longer enter into long-term partnerships with private companies. The current financial crisis is an example where DFIs have gradually replaced or will replace the services of commercial banks. By doing so, DFIs enable private sector enterprises to continue to operate or even to survive. This support will also need to continue in the longer-term, as when commercial banks leave, it takes considerable time before they return to operating in these markets.

Stabilizer – During current financial crisis where private investments withdraw, DFIs play a crucial role in stabilizing investments in developing countries, through their role as investment partners. The financial crisis has made it very clear that DFIs are crucial in addition to commercial banks.

However, the DFIs and multilateral banks are not able to respond sufficiently to the needs of the market
Multilateral development banks have received additional funding relatively quickly (governments can jointly decide to do so in forums like G8, G20 and UN fundraising initiatives). But procedures make fast disbursement challenging. For example, the IFC's Bank Recapitalisation Fund[92], which aims to provide additional capital for banks in development countries, had its first closing with US$3 billion in February, 2009. As of September 2009 an insignificant amount of this large capital has been committed to banks in need[93].

The DFIs with their smaller and more flexible structures and efficient decision making processes, would likely be able to act quickly within their existing mandate by modifying operational rules, such as increasing the maximum level of equity participation or by increasing the percentage of total lending to individual projects. Swedfund has received additional capital injections in 2009 (close to €30 million) with the mandate to counter-act the financial crisis. But generally, it is difficult for most DFIs to get funding for this purpose on short notice. This difficulty in acquiring additional funding limits the DFIs' urgent response to the financial crisis.

7 DFIs are still the smaller partner in Nordic development policy

DFIs constitute an important third pillar of investment in addition to aid and multilateral development banks

Differing strategy - In relation to traditional bilateral aid, DFIs employ a different strategy to achieve sustainable development and serve as a path to spreading strategies.

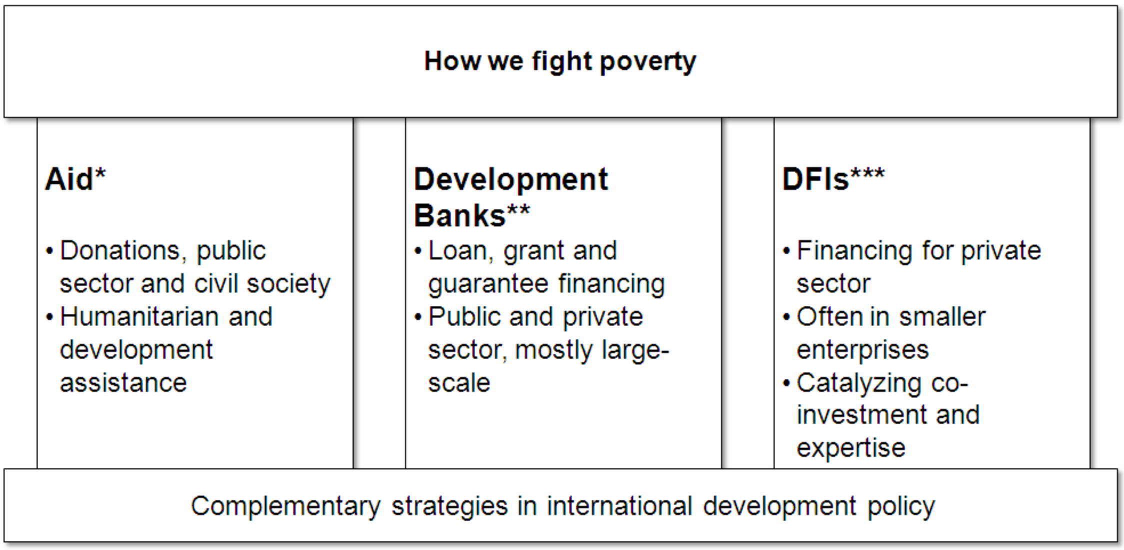
Additionality - DFIs constitute an important addition to aid and multilateral development banks by stimulating the private sector economy in developing nations.

Complementary - DFIs are complementary to multilateral investments (not a substitute or duplicative) and have key differences as they pursue different strategies and focus areas than aid and multilateral development banks.

The Exhibit 17 below describes the different roles and strategies of each of aid, multilateral development banks and national DFIs.

Exhibit 17 – Aid, development banks and DFIs constitute the three pillars of Nordic international development policy

ILLUSTRATION



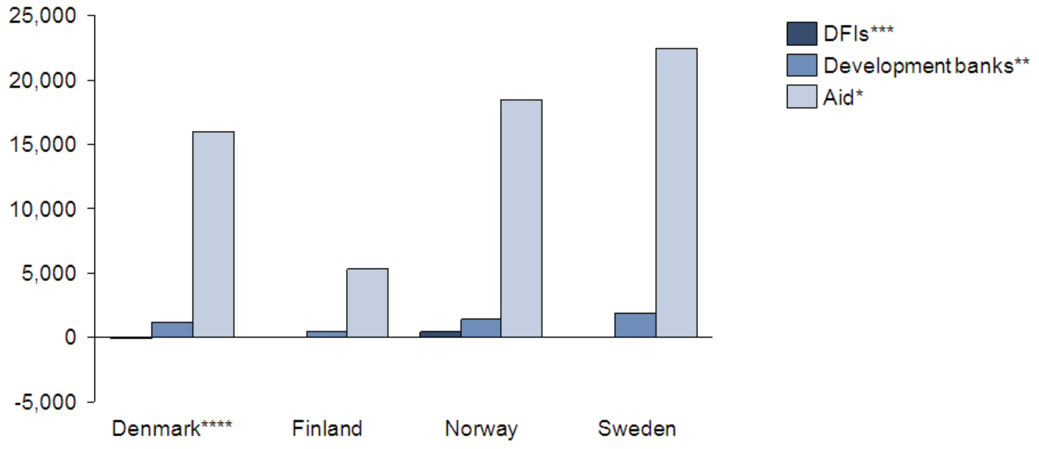
* Bilateral and multilateral (UN, EC)
** World Bank Group institutions (IFC, IDA, IBRD, MIGA); Regional development banks
*** National and regional institutions
Source: Dalberg analysis

DFIs have proven economic and social impact but government funding of national DFIs is much less than to aid and multilateral development banks
Nordic investment in DFIs is comparably small in relation to total aid and multilateral development banks. During the last 10 years the Nordic DFIs have received net capital injections equal to €453 million from their governments. IFU has paid back to the government more than has been paid in (net €87 million paid out) during the last 10 years, while it from inception has a net capital injection of approximately €14 million. The net capital injection over the last 10 years for Finnfund, Swedfund and Norfund amounts to €540 million.

In comparison, bilateral and multilateral aid equalled €62 billion in this time period, and development banks €5 billion.[94] Exhibit 18 below shows a comparison of government capital infusions to DFIs and net disbursements to bilateral and multilateral ODA.

Exhibit 18 – Net capital infusions for DFIs are only a very small fraction of ODA

Government development financing: Bilateral and multilateral Overseas Development Assistance and national DFI financing
€ million, 1999-2008



* Bilateral and multilateral (UN, EC, GEF, Montreal Protocol, other agencies)
** World Bank Group institutions (IFC, IDA, IBRD, MIGA); Regional development banks
*** National and regional institutions; DFI financing includes net government capital infusions (capital infusions minus dividends and taxes)
**** Total capital infusion – capital repayment; Exclude IØ as it is being unwound
Source: OECD, Norfund, Swedfund, Finnfund, IFU

In summary, DFIs are still very much the smaller partner in Nordic development policy. Net capital infusions to DFIs from governments in the Nordic countries over the last decade are less than 1% of official development assistance through other bilateral and multilateral channels.

End Notes

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[23] Includes IØ, which is being phased out.

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