Toolkit on ESG for fund managers

Adding value through effective environmental, social and governance (ESG) management

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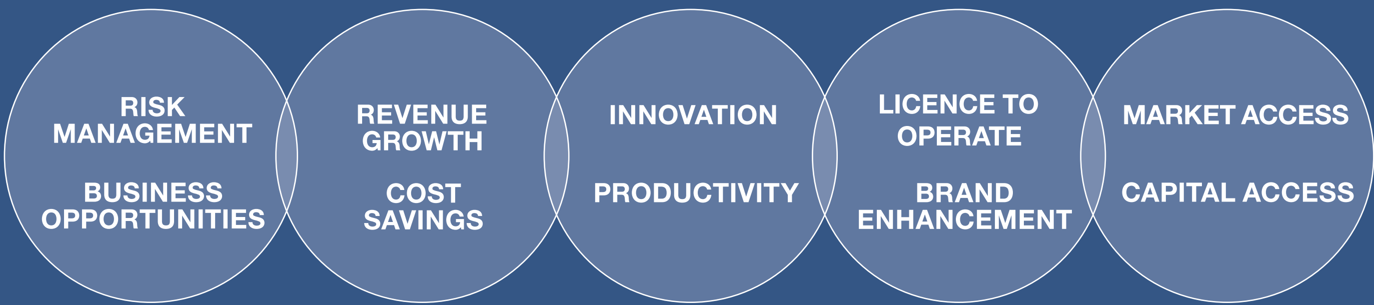

Toolkit on ESG for fund managers

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Initial screening → Due diligence → Investment decision → Investment agreement → Investment monitoring → Exit

Initial screening	• Check investment proposition against ESG policies and exclusions • Assess opportunities to add value through ESG improvements • Rate ESG risks	CDC standards Tools 1, 2, 5 & Appendices 1-5; 8-10	9 21, 25, 33 63-144 163-182
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Contents

Toolkit on ESG for fund managers

Introduction

1. What is this Toolkit for? An introduction to ESG analysis

The term 'ESG' is commonly used to refer to environmental, social and governance matters relevant to a company's strategy and operations. There is growing recognition in the financial community that an effective analysis of ESG risks and opportunities is a fundamental part of the assessment of a company's value. Addressing ESG risks and realising opportunities for ESG improvements during a fund's investment period are important levers for fund managers to add value to their portfolio companies.

'Integrated ESG analysis' and 'ESG management systems' mean processes which take ESG factors into account alongside more traditional financial and business performance considerations in the assessment and management of a company.

This Toolkit is designed for fund managers, particularly for private equity fund managers investing in the emerging markets of developing countries. Its aim is to:

- explore the business case for assessing and managing ESG risks and opportunities arising from investments;
- provide tools for integrating ESG analysis into investment decisions and investment management;
- help determine when specialist expertise is required;
- consider how to report to boards, investors and the public; and
- provide guidance on how to apply international ESG standards, notably those used by development finance institutions (DFIs).

With increasing investor attention to ESG matters, policies, guidelines and standards are converging across the investment industry.

DFIs, including CDC, use the International Finance Corporation's Performance Standards on Social and Environmental Sustainability (IFC Performance Standards) and the associated World Bank / IFC Environmental, Health and Safety (EHS) Guidelines as the reference standards for investments in industries with significant risks in emerging markets. These standards are also used as reference for the signatories to the Equator Principles for project finance in emerging markets, including leading global financial institutions such as Barclays, CitiGroup, Credit Suisse, HSBC, JP Morgan Chase and Société Générale, the so-called 'Equator Banks'.

The United Nations Global Compact and the United Nations Principles for Responsible Investment (UNPRI) have gathered increasing numbers of corporate and investor signatories from around the world.

The US Private Equity Council, with members including many of the world's best known private equity firms such as Apax Partners, Blackstone Group, Carlyle Group, Kohlberg Kravis Roberts and Permira, issued a set of Guidelines for Responsible Investment in 2009, which builds on these globally accepted standards.

Despite the convergence in internationally recognised ESG standards, there is often a lack of clarity on how to implement such standards in fund managers' investment processes. This Toolkit provides practical guidance for fund managers to implement CDC's Investment Code on ESG, see p. 9-13, which is consistent with international best practice and standards on ESG. Appendices to this Toolkit provide guidance on relevant international ESG reference standards and how to apply these for fund managers and for companies. This Toolkit also includes appendices on ESG matters for specific industries, regions and different types of funds. It furthermore includes specific appendices on climate change and gender considerations, which are summaries of more extensive guidance materials on these topics to be found on CDC's website:
www.cdcgroup.com

'Our ambition is to build stronger and more valuable businesses, which means that a concern for their long-term sustainability has to be at the centre of what we do. As such, consideration of the social and environmental impact of our funds' activities is embedded into our day-to-day operations, the funds' investment process and the way we think about the governance of the funds' portfolio companies.'

Permira: a leading global private equity fund manager with total committed capital of €20 billion and investments in over 190 companies.

www.permira.com

Introduction

An introduction to CDC

CDC is the British development finance institution (DFI). Owned by the UK government's Department for International Development (DfID), CDC provides capital for fund managers to invest in promising businesses in emerging markets, with a particular emphasis on sub-Saharan Africa and South Asia. By supporting the private sector, CDC contributes to long-term poverty reduction in developing countries.

Responsible investment has always been core to CDC's mandate. No longer a direct investor since 2004, CDC currently promotes sound business practices through its fund managers. Across CDC's portfolio, fund managers take long-term stakes in portfolio companies and in this way can help companies improve their ESG standards over time. CDC insists on sound ESG management from a fundamental conviction that this is critical to ensure that development does not come at the expense of a damaged environment, poor conditions for local workers or negative impacts on communities. CDC also insists on improving standards because of growing evidence that ESG improvements help build higher value for businesses to grow into leading companies and provide superior returns to investors.

The fund managers that invest CDC's capital commit to implement the ESG policies, exclusion list and ESG management systems described in CDC's Investment Code through formal legal agreements.

This Toolkit is intended to provide the practical step-by-step guidance that fund managers may need to implement CDC's Investment Code on ESG.

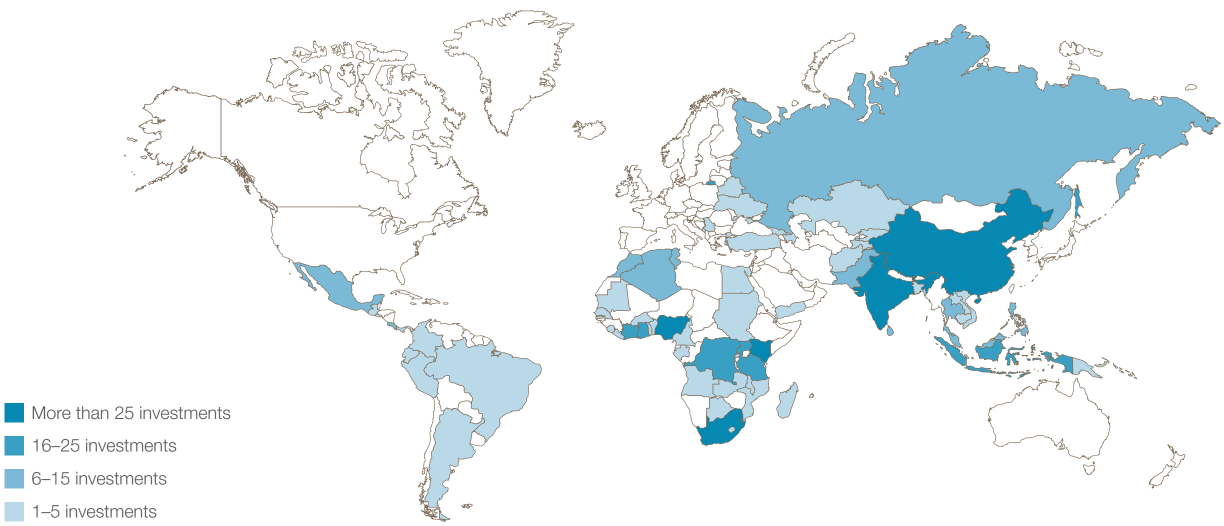
At the end of 2009, CDC had invested capital with 65 different fund managers who between them had offices in 37 developing countries. These fund managers had invested CDC's and other investors' capital in 794 portfolio companies in 71 countries.

'Companies seeking to grow and perform at the highest level need to pay close attention to maintaining quality standards across their business, including being aware of their impact on the environment and the increasing relevance of climate change and energy efficiency. For each investment that Actis makes, we aim to ensure that best practices are implemented in all aspects of the business including those relating to the interactions with society.'

Actis: a leading emerging markets private equity fund manager which was spun out of CDC in 2004 and which has subsequently raised US$2.9 billion in capital.

www.act.is

CDC's investments at year end 2009: 794 companies in 71 countries



Introduction

2. Why is this Toolkit useful? The business case for ESG

The business case for embedding ESG analysis and management in investments and corporate strategy is becoming stronger for many reasons, as described below.

2.1 Stakeholder interests

Governments in developed and many developing countries are strengthening environmental, social, anti-corruption and corporate governance regulations. Companies need to be able to respond. In many developed countries, governments are increasingly applying their substantial purchasing power to the procurement of sustainable goods and services, with impacts on supply chains also in developing countries.

Consumers know and care more and more about what they buy, how it is made, what it is made from, how far it has travelled and how it is packaged. As demonstrated by numerous surveys and studies, there is an increasing demand for products that are produced sustainably, for the benefit of people and without causing harm to the environment. According to a study by PricewaterhouseCoopers, 58% of UK consumers buy fewer sustainable products than they would like to do.[1] According to another survey, approximately 50% of US consumers considered at least one sustainability factor in selecting consumer goods and choosing where to shop for those products.[2]

Mainstream investors were historically not drivers towards more long-term or integrated ESG management, partly because there was a perception that consideration of ESG issues was not compatible with fiduciary duties and maximising profits. This has changed, as indicated by the recent UNEP Finance Initiative's report *Fiduciary responsibility: legal and practical aspects of integrating environmental, social and governance issues into institutional investment*[3] and the CFA Institute's report *ESG factors at listed companies*.[4] A recent study by

ESG value addition comes from multiple sources

Percentage of respondents*

Ways in which ESG programmes improve a company's financial performance**

* Including CFOs, investment professionals and ESG professionals

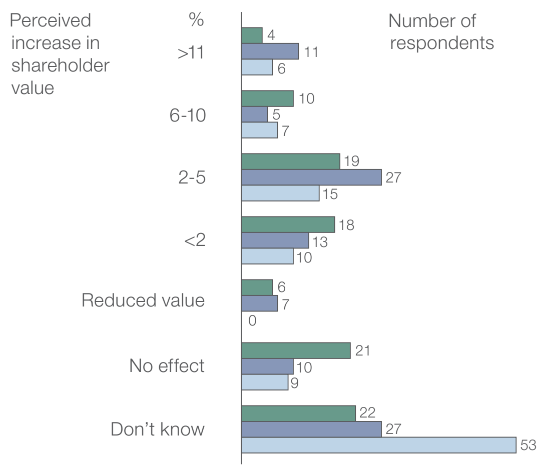
** Excluding any changes stemming from the economic crisis

Source: S. Bonini, N. Brun, and M. Rosenthal, 'Valuing corporate social responsibility,' The McKinsey Quarterly, February 2009.

ESG programmes are perceived to increase shareholder value

CFOs, n=84
Investment professionals, n=154
ESG professionals, n=87

Effects of ESG programmes on an organisation's shareholder value in typical times*



* Excluding any changes stemming from the economic crisis

Source: S. Bonini, N. Brun, and M. Rosenthal, 'Valuing corporate social responsibility,' The McKinsey Quarterly, February 2009.

1 *Sustainability: Are consumers buying it?* PricewaterhouseCoopers, 2008.

2 *Information Resources, Inc.,* 2009.

3 *Fiduciary responsibility: legal and practical aspects of integrating environmental, social and governance issues into institutional investment,* UNEP Finance Initiative, 2009.

4 *Environmental, social and governance factors at listed companies,* Centre for Financial Market Integrity CFA Institute, 2008.

Introduction

The business case for ESG

Boston College Centre for Corporate Citizenship and the consulting company McKinsey & Company argues that there are clear financial reasons for companies to invest in ESG improvements, indicating that ESG programmes can generate substantial direct financial returns. This study quotes investors and corporate managers as thinking that ESG improvement programmes have substantive impact on total quantifiable shareholder value.[5] There are currently moves among powerful groups of investors to require their asset managers to incorporate more long-term ESG thinking into their company valuations (as in the Enhanced Analytics Initiative[6]) and to require companies to report to investors on key ESG issues (as in the Carbon Disclosure Project[7]). Around 200 asset owners have signed up to the UN Principles for Responsible Investment, along with 300 investment managers. These developments build the case for effective ESG analysis throughout the financial sector, including for private equity.

Leading companies are demonstrating that businesses benefit from embedding sound ESG management into their operations. The expectations of consumers and investors will continue to rise, leading to increased demands for disclosure and increased differentiation between companies and their products and services on the basis of ESG performance.

Company directors are increasingly recognising the need to take ESG matters seriously at board level. The importance of good corporate governance and the need for directors to ensure transparency and accountability were highlighted during the financial crisis. Some insurers are considering withholding directors' liability insurance from companies that do not have appropriate ESG management processes.

Mainstream analysts are beginning to understand, accept and incorporate ESG aspects into their capital allocation recommendations. This is particularly true in high-risk sectors such as oil and gas and in sectors which would most immediately suffer the effects of unsustainable practices, such as consumer goods where brand and reputation are increasingly key for successful sales.

Climate change poses numerous opportunities for forward-looking companies as well as risks for those that fail to adapt. Carbon markets are already worth US$126 billion[8] and are expected to grow significantly in the years to come. There are new markets for products that help society adapt or which enable other entities to reduce their emissions. The carbon content of products is likely to increasingly become a differentiator in the marketplace, enabling companies in every sector to benefit from improving performance relative to their peers.[9]

Private equity fund managers have a long-term investment horizon and are ideally placed to implement improvements in ESG management over time in their portfolio companies, which add value to their investments. It is sometimes perceived that private equity firms' success comes simply from structuring deals so that their investors make quick financial returns with substantial 'carry' payments for fund managers, without regard to the health of the underlying company and its employees, not to mention wider stakeholders. In the long term, to build stronger portfolio company businesses but also to improve fund managers' own brands and to avoid excessive new regulations, it is in the private equity industry's interest to make and structure investments in a way which ensures that benefits accrue to society as well as to investors and fund partners.

[5] *How virtue creates value for business and society: investigating the value of ESG activities,* Boston College Center for Corporate Citizenship and McKinsey & Company, 2009.

[6] www.enhanced-analytics.com

[7] www.cdproject.net

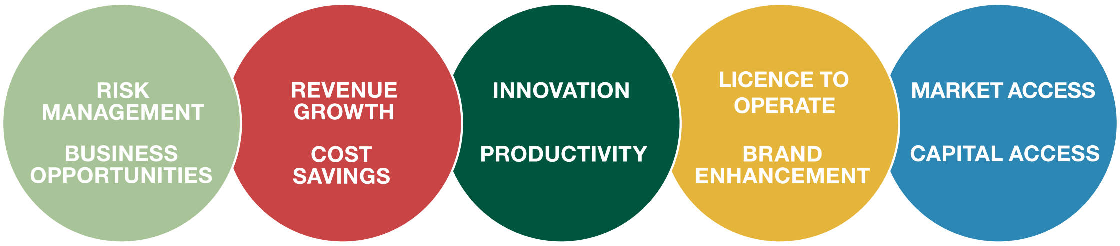
[8] *State and trends of the carbon market 2009,* Karan Capoor & Philippe Ambrosi, World Bank, 2009.

[9] *Climate change guidance for fund managers,* Forum for the Future for CDC Group plc. 2010.

Introduction

The business case for ESG

2.2 ESG value drivers



Risk management

Some private equity investors regularly undertake environmental, social and business integrity assessments as part of their due diligence in order to establish whether there are liabilities which have not been accounted for elsewhere. The assessment should be extended to cover a wide range of questions about cost efficiencies and advantages arising from improved environmental, labour, health and safety, community, ethical practices and corporate governance. Engaging with local communities can improve a company's ability to adapt better to changing political and social situations, with lower risks of disrupted operations and lower security costs.

Business opportunities: market access and revenue growth

Sales into a new market may require a company to adapt its products or services to satisfy different regulations and standards. Establishment of a subsidiary in, or sourcing from, a new market requires a company to understand specific local ESG risks. In some cases, this goes beyond compliance with the local legislation where local standards fall short of those expected from the company's brand or by its investors. Producers in emerging markets can access markets in Europe and the United States through certifications on environmental, product safety and 'fair trade' grounds. Opportunities may also arise from looking at markets which have not been part of the company's traditional strategy, for example, new ways to market products or services to customers at the 'bottom of the pyramid', i.e. the poorer segments of the population.[10] A recent example is the consulting company Hystra's report *Access to Energy for the BOP*[11] based on work for three leading French energy companies. Local ESG efforts and community dialogue can facilitate entry into new markets with lower risks of disrupted operations and lower security costs.

Cost savings

There is often potential for substantial cost savings through energy efficiencies, reduced use of water and other resources and improved waste management. These are partly environmental issues, but also clear business concerns. The importance of energy efficiency will continue to grow, particularly in industries with energy-intensive manufacturing systems such as cement. Transport efficiencies will also be critical, not only for companies in the transportation sector per se but also for those with a wide distribution network. With water supplies diminishing in many countries, a company's use of water in its manufacturing process could become critical for its competitive advantage. Cost savings can also come from reduced employee turnover and improved productivity by using ESG improvements to build staff motivation.

Innovation

Product design needs to adapt as consumer preferences change and new technologies emerge. Pressures are growing on companies to produce goods which recognise the limitations of the natural environment and which are therefore based less on a 'consumption' mentality of create-use-dispose and more on a 'life-cycle' mentality of create-use-reshape-and-reuse. Winning companies constantly seek to develop cutting edge technology and innovative products and services for unmet environmental or social needs that could translate into business uses, patents, proprietary knowledge, etc.

Productivity through improved management

Improvements in portfolio company management is the obvious focal point for private equity investors. The CEOs who are more likely to deliver growth will be those who have analysed future trends in the market-place for their products and services, considered which resource constraints will

[10] *The fortune at the bottom of the pyramid,* Prahalad 2002.

[11] *Access to energy for the bottom of the programme,* Hystra 2009 www.hystra.com

Introduction

The business case for ESG

impact on their access to raw materials or other inputs and anticipated the direction of future consumer preferences and regulations. In all of these areas, an integrated ESG analysis provides important insights. ESG analysis can develop leadership skills, enhance employee productivity and improve the company's long-term strategy.

Productivity through more efficient supply chains

Strong relationships with suppliers are key to successful corporate performance. Long-term relationships usually depend on mutual trust, which requires careful nurturing. Many companies have found that an enhanced focus on supply chain management, especially support for small and medium-sized (SME) suppliers to enable them to grow with the company, has been a key factor for efficient production. Engaging in community welfare and development can be an important way to secure consistent, long-term and sustainable access to high quality raw materials and products.

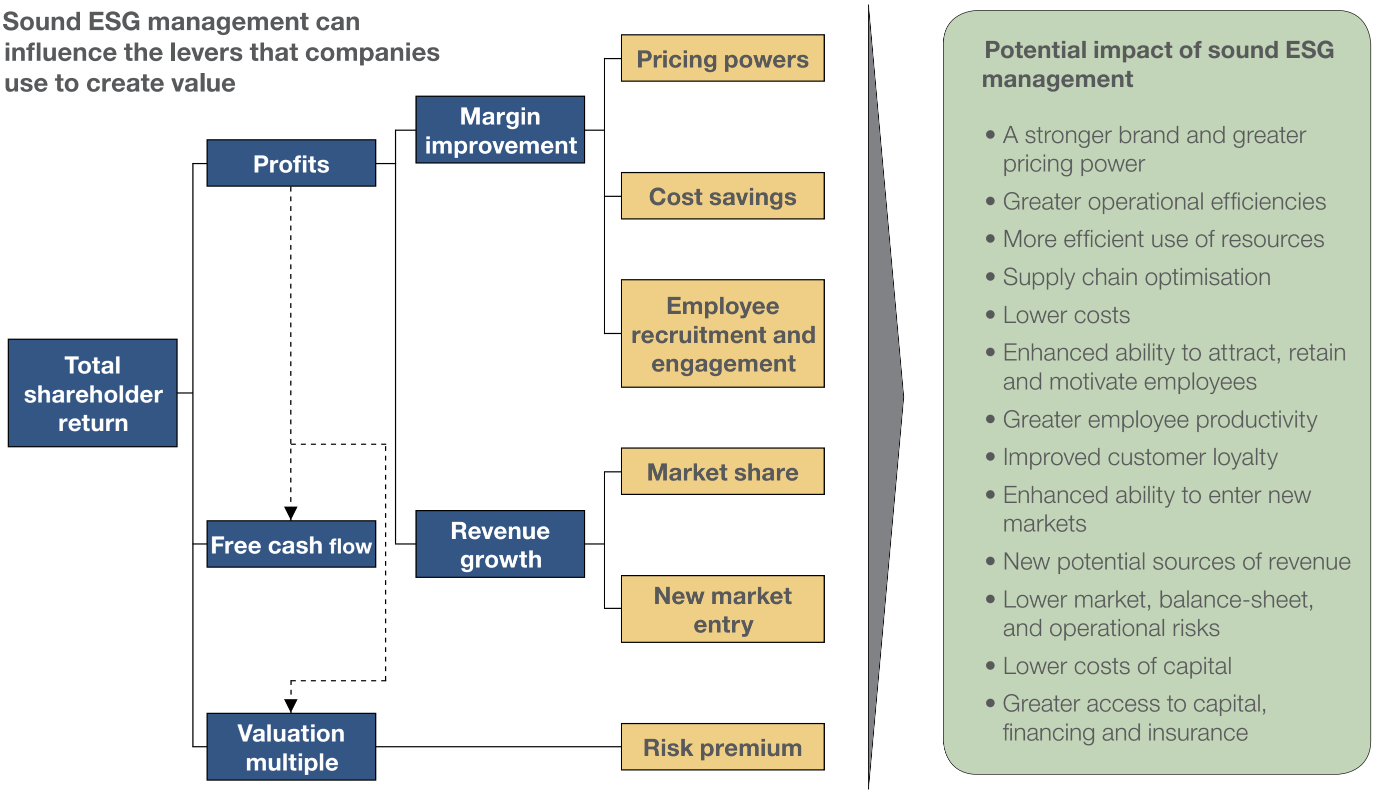
Brand enhancement

There are multiple examples of companies that successfully use ESG factors to engage with consumers and build brands, from Starbucks' 'fairtrade' coffee to the Bodyshop's responsible sourcing to GAP's and American Express' 'RED' product lines.[12] A reputation for sustainable business practices can build brands for which customers are willing to pay a price premium. Successful ESG programmes can be an important way to foster brand loyalty, improve company reputation and gain goodwill with customers and stakeholders. Attention to ESG issues is also important to avoid negative publicity and boycotts.

Capital access

Trade buyers and investors pay increasing attention to ESG matters. Sound ESG management can substantially improve a fund manager's potential for a successful exit. Increasingly, there are ESG requirements associated with initial public offerings (IPOs) in emerging markets, e.g. full compliance with environmental regulations in line with international standards for IPOs in China.

Sound ESG management can influence the levers that companies use to create value



Source: *The Sustainability Initiative Survey* 2009, Boston Consulting Group and MIT Sloan Management Review. Adapted by CDC and Rosencrantz & Co.

[12] 'RED' products provide a share of corporate profits from their sales to the Global Fund to Fight AIDS, Tuberculosis and Malaria www.theglobalfund.org

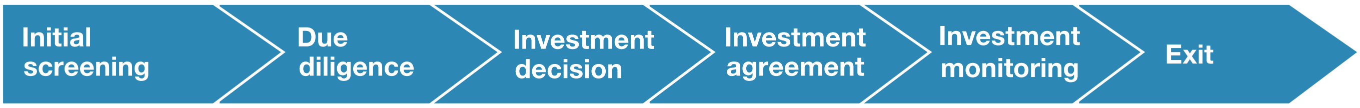
3

Introduction

3. How to embed ESG management into the investment process? The Toolkit

This Toolkit shows step-by-step how ESG analysis and management can enhance a fund manager's investment processes. It is designed to help fund managers focus their time and resources efficiently, to increase awareness of ESG opportunities and risks, which may need to be addressed and monitored, and to flag complex areas where specialist external support may be required. Each *Tool* covers a specific area and is intended to be practical and easy to use. There is, however, no substitute for a detailed assessment where ESG risks are high and the quality of a company's ESG management systems is inadequate. The Toolkit should help target detailed work to where it is the most needed.

Tools 1 - 4 apply to all investment activities. The other *Tools* in this Toolkit apply to specific stages of the investment process as indicated below.



Tool 1 Adding value through ESG improvements

Tool 2 ESG policies and guidelines

Tool 3 ESG considerations at each stage of the investment process

Tool 4 Questions to assess a fund manager's ESG management systems

Tool 5 Rating ESG risks

Tool 6 ESG due diligence

Tool 7 Environmental and social impact assessments

Tool 8 Questions to assess a company's ESG management systems

Tool 9 Investment paper and action plan for ESG improvements

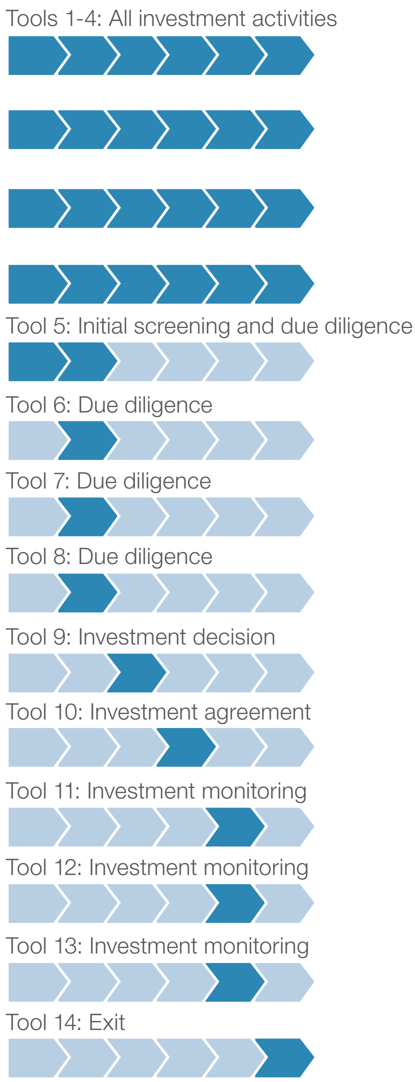
Tool 10 Investment agreement

Tool 11 Investment monitoring

Tool 12 ESG reporting

Tool 13 Information for the public: annual reports and websites

Tool 14 ESG considerations at exit



Introduction

Appendices

Appendices to this Toolkit provide important supplementary information.

Appendix 1	ESG due diligence questions
Appendix 2	Sector-specific ESG risks and opportunities for improvements
Appendix 3	ESG risks in different regions and selected countries
Appendix 4	ESG management for different types of funds: SME, microfinance and debt funds
Appendix 5	International ESG reference standards and conventions
Appendix 6	CDC's monitoring and evaluation system
Appendix 7	CDC's reporting templates and example of an ESG report
Appendix 8	Investments from different development finance institutions (DFIs): comparing standards and procedures
Appendix 9	Climate change considerations: risks and opportunities
Appendix 10	Gender considerations: good practices for investors and businesses

Appendix 5 is particularly important, as it provides brief summaries of key international standards and conventions on ESG. Many of these standards and conventions are referred to in CDC's Investment Code on ESG, see p. 9-13. These standards can be used to benchmark the performance of companies and to implement improvements as relevant over the investment period. Some of these standards are relevant for all fund managers and companies, while others are relevant only for fund managers that invest in high risk assets or in certain sectors. For example, the IFC Performance Standards and the associated Environmental, Health and Safety (EHS) general and industry specific Guidelines are relevant for fund managers that invest in sectors with significant risks, whereas the Extractive Industries Transparency Initiative is only relevant for fund managers that invest in mining and other extractive industries. The different *Tools* included in this Toolkit refer to how to use these international standards at different stages of the investment process, as relevant.

CDC's standards and requirements

1. Investment Code on ESG

All fund managers that invest CDC's capital are required to commit to the ESG principles, objectives, policies, exclusion list and management systems described in CDC's Investment Code on ESG through a binding legal agreement. Where a fund manager has effective control or significant influence over a portfolio company in which it invests, that portfolio company must also commit to the Investment Code[1] by way of an investment undertaking. Fund managers should not invest CDC's capital in companies that do not operate in-line with the Investment Code if they are not able to influence improvements in company practices over time.

Fund managers are expected to implement CDC's Investment Code even where local laws and customs may fall short of CDC's requirements. While fund managers may invest in portfolio companies with weak ESG practices, they must ensure that improvements are implemented during the investment period.

The international reference standards referred to in CDC's Investment Code are explained in *Appendix 5* to this Toolkit.[2]

1.1 Principles

CDC and the businesses in which its capital is invested will:

- comply with all applicable laws;
- as appropriate, minimise adverse impacts and enhance positive effects on the environment, workers and all stakeholders;
- commit to continuous improvements with respect to management of the environment, social matters and governance;
- work over time to apply relevant international best practice standards,[3] with appropriate targets and timetables for achieving them; and
- employ management systems which effectively address ESG risks and realise ESG opportunities as a fundamental part of a company's value.

1.2 Objectives and policies

1.2.1 The Environment

Objectives

- to reduce adverse impacts and enhance positive effects on the environment, as relevant and appropriate, from the businesses in which CDC's capital is invested;
- to encourage the businesses in which CDC's capital is invested to make efficient use of natural resources and to protect the environment wherever possible; and
- to support the reduction of greenhouse gas emissions which contribute to climate change from the businesses in which CDC's capital is invested.[4]

Policy

Businesses in which CDC's capital is invested will:

Mandatory

- operate in compliance with applicable local and national laws (as a minimum);

As relevant

- assess the environmental impact of their operations as follows:
  - identify potential risks and appropriate mitigating measures through an environmental impact assessment where business operations could involve loss of biodiversity or habitat, emission of significant quantities of greenhouse gases, severe degradation of water or air quality, substantial solid waste or other significant negative environmental impacts;[5] and

[1] A fund manager is deemed to have significant influence over a portfolio company where its fund has (i) an ownership interest in the portfolio company in excess of 20%, which is presumed to be a level that allows for participation in the financial and operating policies of a portfolio company (if the percentage is lower but gives rise to the same participation, this will also meet the definition of significant influence); or (ii) board representation to a level that allows for participation in determining the financial and operating policies of the portfolio company; or (iii) rights to influence the financial and operating policy decisions of the portfolio company pursuant to a shareholders' or similar agreement. See *Tool 10* for the text of such an investment undertaking.

[2] CDC's Investment Code is compatible with the International Finance Corporation's (IFC) Policy and Performance Standards on Social and Environmental Sustainability (IFC Performance Standards). A fund manager that follows the IFC Performance Standards fulfils the requirements on the environment and social matters set out in this Investment Code. The Investment Code is also compatible with the 2007 agreement for common environmental and social standards among the European Development Finance Institutions (EDFIs).

[3] As referred to in this Investment Code and as may develop over time.

[4] In line with the 1994 United Nations Framework Convention on Climate Change (UN Framework Convention), the associated 2005 Kyoto Protocol and the associated 2009 Copenhagen Accord. These may be amended from time to time. See www.unfccc.int

[5] Activities with potential significant adverse environmental impacts that are diverse, irreversible or unprecedented; mindful of potential cumulative, secondary or synergistic impacts that may occur as a consequence.

CDC's standards and requirements

1. Investment Code on ESG

  - consider the potential for positive environmental impacts from business activities; and

- take appropriate actions to mitigate environmental risks, ameliorate environmental damage and enhance positive effects as follows:
  - where an activity is assessed to present significant environmental risks, work over time to apply the relevant IFC policies and guidelines,[6] even if these are more stringent than local legislation, with appropriate targets and timetable for improvements; and
  - as appropriate, work over time towards international environmental best practice standards.[7]

1.2.2 Social matters

1.2.2.a Labour and working conditions

Objectives

- to require the businesses in which CDC's capital is invested to treat all their employees and contractors fairly and to respect their dignity, well-being and diversity; and
- to encourage the businesses in which CDC's capital is invested to work over time towards full compliance with the International Labour Organisation (ILO) Fundamental Conventions[8] and with the United Nations (UN) Universal Declaration of Human Rights.[9]

Policy

Businesses in which CDC's capital is invested will:

Mandatory

- comply with applicable local and national laws (as a minimum);
- not employ or make use of forced labour of any kind;
- not employ or make use of harmful child labour;[10]
- pay wages which meet or exceed industry or legal national minima;
- treat their employees fairly in terms of recruitment, progression, terms and conditions of work and representation, irrespective of gender, race, colour, disability, political opinion, sexual orientation, age, religion, social or ethnic origin, or HIV status;
- allow consultative work-place structures and associations which provide employees with an opportunity to present their views to management; and

As relevant

- for remote operations involving the relocation of employees for extended periods of time, ensure that such employees have access to adequate housing and basic services.

[6] The IFC Performance Standards and the 2007 IFC Environmental, Health and Safety Guidelines (EHS Guidelines), as may be amended from time to time and adopted by CDC. IFC EHS Guidelines include general guidelines and industry sector guidelines for forestry, agribusiness / food production (including fisheries), general manufacturing, oil and gas, infrastructure, chemicals (including pharmaceuticals), mining and power.

[7] Including the range of internationally certifiable environmental standards issued by the International Organisation for Standardisation (ISO), the ISO 14000 series, notably including standards for environmental management systems (ISO 14001) and greenhouse gas emissions (ISO 14064-65), as may be amended from time to time.

[8] The ILO Fundamental Conventions are the Conventions on Freedom of Association and Collective Bargaining; Forced Labour; Child Labour; and Non-Discrimination, as may be amended from time to time. See www.ilo.org for the texts of these Conventions and a list of the countries that have ratified each of them.

[9] www.un.org

[10] As defined by ILO Convention 138 on the minimum age for work from 1973 and ILO Convention 182 on the worst forms of child labour from 1999.

CDC's standards and requirements

1. Investment Code on ESG

1.2.2.b Health and safety

Objectives

- to attain safe and healthy working conditions for employees and contractors of the businesses in which CDC's capital is invested; and
- to safeguard the health and safety of all those affected by the businesses in which CDC's capital is invested.

Policy

Businesses in which CDC's capital is invested will:

Mandatory

- comply with applicable local and national laws (as a minimum);

As relevant

- assess the health and safety risks arising from work activities; and
- take appropriate actions to eliminate or reduce risks to health and safety as follows:
  - where an activity is assessed to present significant health and safety risks,[11] work over time to apply the relevant IFC policies and guidelines,[12] even if these are more stringent than local legislation, with appropriate targets and timetable for improvements; and
  - as appropriate, work over time towards international best practice standards for health and safety.[13]

1.2.2.c Other social matters

Objectives

- To be objective, consistent and fair with all stakeholders of the businesses in which CDC's capital is invested; and
- To recognise and, as appropriate, promote the social development impact from the businesses in which CDC's capital is invested.

Policy

Businesses in which CDC's capital is invested will:

As relevant

- take account of their impact on employees, contractors, the local community and all others affected by their operations as follows:
  - identify potential adverse effects and appropriate mitigating measures through a social impact assessment in cases involving resettlement, critical cultural heritage, indigenous peoples, non-local labour or other issues where the negative impact could be significant;[14] and
  - consider social development contributions; and
- take appropriate actions to mitigate risks, ameliorate negative impacts and enhance positive effects.[15]

[11] Activities that could have a severe health or safety impact for workers or affected communities.

[12] The IFC Performance Standards and the IFC EHS Guidelines, as may be amended from time to time and adopted by CDC.

[13] Including OHSAS 18001, the international occupational health and safety management system specification, and industry specific international good practice standards related to the safety of product use, e.g. the international Good Manufacturing Practice (GMP) standards for food and pharmaceutical products promoted by the World Health Organization (WHO).

[14] Activities with potential significant adverse social impacts that are diverse, irreversible or unprecedented.

[15] As relevant, by applying IFC Performance Standards on Land Acquisition and Involuntary Resettlement; Indigenous Peoples; and Cultural Heritage; as may be amended from time to time and adopted by CDC.

CDC's standards and requirements

1. Investment Code on ESG

1.2.3 Governance: business integrity and good corporate governance

Objectives

- to ensure that CDC, and the businesses in which CDC's capital is invested, exhibit honesty, integrity, fairness, diligence and respect in all business dealings;
- to enhance the good reputation of CDC; and
- to promote international best practice in relation to corporate governance in the businesses in which CDC's capital is invested.[16]

Policy

CDC and the businesses in which CDC's capital is invested will:

Mandatory

- comply with all applicable laws and promote international best practice,[17] including those laws and international best practice standards intended to prevent extortion, bribery and financial crime;
- uphold high standards of business integrity and honesty;
- deal with regulators in an open and co-operative manner;
- prohibit all employees from making or receiving gifts of substance in the course of business;
- prohibit the making of payments as improper inducement to confer preferential treatment;
- prohibit contributions to political parties or political candidates, where these could constitute conflicts of interest;
- properly record, report and review financial and tax information;[18]
- promote transparency and accountability grounded in sound business ethics;
- use information received from its partners only in the best interests of the business relationship and not for personal financial gain by any employee;
- clearly define responsibilities, procedures and controls with appropriate checks and balances in company management structures; and
- use effective systems of internal control and risk management covering all significant issues, including environmental, social and ethical issues.

1.3 Exclusions

CDC's capital will not be invested in the following businesses or activities:

- production of or trade in any product or activity deemed illegal under applicable local or national laws or regulations, or banned by global conventions and agreements, such as certain:
  - hazardous chemicals, pesticides and wastes;[19]
  - ozone depleting substances;[20] and
  - endangered or protected wildlife or wildlife products;[21]
- production of or trade in arms, i.e. weapons, munitions or nuclear products, primarily designed or primarily designated for military purposes; or
- production of, use of or trade in unbonded asbestos fibres.[22]

[16] Including the 2004 Organisation for Economic Co-operation and Development (OECD) Principles of Corporate Governance, as may be amended from time to time. See www.oecd.org

[17] Including the 2005 UN Convention against Corruption; the 1997 OECD Anti-Bribery Convention; the 2005 Extractive Industries Transparency Initiative (EITI), as relevant; and the UK Bribery Act as may be amended from time to time.

[18] CDC promotes the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB); and the International Private Equity and Venture Capital Valuation Guidelines (IPEVC).

[19] Including those specified in the 2004 Stockholm Convention on persistent organic pollutants (POPs); the 2004 Rotterdam Convention on the prior informed consent procedure for certain hazardous chemicals and pesticides in international trade; and the 1992 Basel Convention on the control of transboundary movements of hazardous wastes and their disposal.

[20] As covered in the 1999 Montreal Protocol on substances that deplete the ozone layer.

[21] As covered in the 1975 Convention on International Trade in Endangered Species or Wild Flora and Fauna (CITES).

[22] This does not apply to purchase and use of bonded asbestos cement sheeting where the asbestos content is less than 20%.

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CDC's standards and requirements

1. Investment Code on ESG

CDC's capital will not be invested in businesses for which the following activities or products are, or are intended to be, a significant source of revenue:

- gambling;
- pornography; or
- tobacco or tobacco related products.[23]

1.4 Management systems for CDC's fund managers

In order to implement CDC's Investment Code effectively, CDC requires its fund managers to enter into a formal agreement pursuant to which each fund manager commits to an investment undertaking similar in substance to CDC's Investment Code.[24]

Where fund managers have effective control or significant influence over portfolio companies,[25] CDC requires its fund managers to procure that such portfolio companies sign an undertaking confirming that they will operate in line with CDC's Investment Code (see *Tool 10* and *Appendix 5*).

CDC also requires its fund managers to establish and maintain ESG management systems which:

- assess all new investments from an ESG perspective as an integral part of the investment appraisal process (see *Tools 5-8*);
- give new investments a risk rating on ESG issues to determine the appropriate level of management and monitoring (see *Tool 5*);
- if an investment is made despite identified shortcomings in relation to ESG issues, or if any issues arise during the investment period, assist the portfolio company concerned to develop an action plan to address such issues, with appropriate targets and a timetable for improvements (see *Tool 9*);
- encourage the managers of portfolio companies to work towards continuous improvements in these areas, with targets for improvements as appropriate (see *Tool 10* and *Appendix 5*);
- encourage the managers of portfolio companies to adopt and implement policies relating to ESG matters, particularly where businesses entail significant risks (see *Tool 10* and *Appendix 5*);
- monitor portfolio companies' performance on ESG matters and their progress towards relevant action plans and targets for improvements (see *Tool 11*);
- report periodically to the fund's governing body and annually to investors on the performance of portfolio companies from an ESG perspective (see *Tool 12*);
- monitor and record incidents involving portfolio companies that result in loss of life, material effects on the environment, or material breach of law, and promote appropriate corrective actions and report such incidents to the fund's governing body and investors (see *Tools 11* and *12*);
- consider ESG matters at the time of divestment /exit (see *Tool 14*).

[23] Except, in the case of tobacco production only, with an appropriate timeframe for phase-out.

[24] By side letter or equivalent agreement.

[25] A fund manager is deemed to have significant influence over a portfolio company where its fund has (i) an ownership interest in the portfolio company in excess of 20%, which is presumed to be a level that allows for participation in the financial and operating policies of a portfolio company (if the percentage is lower but gives rise to the same participation, this will also meet the definition of significant influence); or (ii) board representation to a level that allows for participation in determining the financial and operating policies of the portfolio company; or (iii) rights to influence the financial and operating policy decisions of the portfolio company pursuant to a shareholders' or similar agreement.

CDC's standards and requirements

2. Business integrity compliance programme and policies

CDC requires each of its fund managers to make the following representation against corruption, anti-money laundering and terrorism financing on the closing of a fund and each time they draw down capital from CDC for an investment:

- neither we, nor any person on our behalf, has been engaged in (i) corrupt practices, fraudulent practices, coercive practices or collusive practices in connection with the fund or any investments made by the fund; (ii) money laundering or acted in breach of any applicable law relating to money laundering; or (iii) financing of terrorism; and
- we have complied with all applicable anti-money laundering (AML) and 'know your customer' (KYC) legislation with respect to each (i) investor in the fund; and (ii) portfolio company investment made by the fund.

CDC expects its fund managers and their portfolio companies to adopt a code of ethics. In addition, CDC expects its fund managers and their funds to commit contractually to the adoption and implementation of business integrity compliance policies which include AML and KYC guidelines.

CDC's fund managers must consider business integrity issues carefully when they undertake due diligence on prospective portfolio companies. Fund managers are also expected to review the adequacy of the due diligence and compliance policies of potential portfolio companies, including their AML, anti-corruption and KYC policies.

2.1. Code of ethics

In many of the countries where CDC's fund managers invest, corruption and questionable business practices are common. Each fund manager and their portfolio companies should adopt codes of ethics, which include the key elements of business integrity in accordance with CDC's Investment Code, section 1.2.3, p.12.

2.2. Recommended business integrity compliance programme and policies

In addition to adopting an appropriate code of ethics, CDC's fund managers should adopt and implement:

- business integrity compliance programmes and procedures which include compliance with the code of ethics;
- an AML policy;
- a policy against financing of terrorism;
- an anti-corruption compliance programme; and
- a KYC compliance programme to be utilised in connection with due diligence performed on potential investors in a fund and including the identification of all beneficial owners involved in a transaction.

These policies should be updated on a regular basis to ensure that they comply with relevant laws and reflect international best practice. Employees should receive regular training.

In accordance with their AML / KYC policies, fund managers are expected to undertake character risk due diligence (CRDD) to ascertain relevant information regarding the character, reputation and background of entities and individuals with whom they plan to transact. CRDD information should be considered during the screening of potential portfolio company investments and prior to accepting subscriptions from potential fund investors.

Fund managers should obtain the identifying information needed (e.g. birth date, place of birth, current address, passport numbers, social security numbers, company registration numbers and tax identification numbers) to perform effective background searches.

Fund managers should perform background searches on both portfolio companies and investors, as described below.

Portfolio companies

- the portfolio company and any subsidiaries;
- owners of the portfolio company unless they are entities publicly traded on a major stock exchange or are otherwise well known institutional investors (e.g. pension funds, multilateral or bilateral financial institutions); and
- individuals with a significant managerial relationship to the portfolio company.

Investors

- all individual investors in the fund; and
- all entities investing in the fund and their beneficial owners, unless they are publicly traded on a major stock exchange or are otherwise well-known institutional investors.

CDC's standards and requirements

2. Business integrity compliance programme and policies

Background searches, whether performed in-house or out-sourced (usually to fund managers' external legal counsel), should include a comprehensive search of publicly available data using products from commercial database search companies (e.g. Complinet, Lexis-Nexis, West Law, Regulatory Data Corporation, World-Check, World Compliance, ISI Emerging Markets, Dow Jones Factiva, Owens Online). These companies offer products which include coverage of international news and media, government lists and records, legal and regulatory authority actions and records on politically exposed persons (PEPs).

Where appropriate, the fund manager should visit a potential investee company, its customers, suppliers and shareholders and applicable government agencies to conduct local due diligence. In addition, due diligence advisers with a local knowledge base should be considered to supplement the fund manager's own in-country due diligence.

Background information searches should identify relevant information regarding the reputation and character of entities and individuals with whom the fund manager is contemplating doing business. Relevant information may include information on criminal activities (e.g. money laundering, terrorism financing and corruption) or non-criminal matters (e.g. bankruptcy, civil litigation, regulatory investigations, PEPs, employment and credit history).

Special requirements regarding PEPs

CDC expects enhanced due diligence to be carried out to verify the source of wealth and funds where the investor in a fund or a business or its beneficial owner is a PEP.

A PEP is broadly defined as any individual (or a family member or close associate of such individual) who is or has been entrusted with a prominent public function by a state or an international body, including:

- heads of state, heads of government, ministers and deputy or assistant ministers;
- members of parliament;
- members of supreme courts, of constitutional courts, or of other high-level judicial bodies;
- members of courts of auditors or of the boards of central banks;
- ambassadors, chargé d'affaires and high-ranking officers in the armed forces; and
- members of the administrative, management or supervisory bodies of state-owned enterprises.

Enhanced due diligence

If concerns arise as a result of an initial background information search, fund managers should consider whether additional due diligence should be performed on a specific entity or individual. Additional due diligence may include the use of third parties such as a local legal counsel or an independent due diligence / business intelligence contractor to perform a more in-depth background search or an independent integrity check using a variety of methods including reference checks, discreet personal inquiries, interviews and research using local databases that are not accessible on the internet. A number of international firms provide these services (e.g. Kroll, Hill & Associates, Hakluyt, Control Risks, Risk Analysis, TD International, Advance Point Global, GPW and Exclusive Analysis). Fund managers should also consider using other available in-country resources for business intelligence and due diligence, such as local databases, local business contacts and networks and relevant embassies and chambers of commerce.

Enhanced due diligence may also be necessary where a potential investee company operates in a particularly high-risk country and / or industry. See *Tool 5* for guidance on rating of ESG risks, including business integrity risks.

Case 1: Business integrity: A CDC portfolio example from Kenya

An essential part of good governance for fund managers is to focus attention on business integrity matters among portfolio companies. During a visit by CDC's staff to a Kenyan printing company, its managing director told CDC that the investment by CDC's fund manager enabled him to enforce zero tolerance on corrupt payments throughout his company; 'I tell the buyers who expect a kick-back that our international investor just will not accept such practices.'

CDC's standards and requirements

2. Business integrity compliance programme and policies

Fund managers should document CRDD performed and any decisions made related thereto. Relevant CRDD information should be filed and made readily accessible during the investment decision process.

Background information searches should be updated prior to the fund's closing where significant time has elapsed since the initial searches were performed. Fund managers should pay particular attention to parties that become involved in a transaction at the later stages of the investment process to ensure that all appropriate information is collected and the appropriate due diligence performed.

Where enhanced due diligence is required, on-going monitoring following an investment should also be emphasised.

2.3. Business integrity due diligence and monitoring of portfolio companies[26]

In addition to a code of ethics a business integrity compliance programme, CDC expects its fund managers to integrate business integrity elements into their due diligence programme. In establishing due diligence procedures, the principles described below should be adopted.

The fund manager should not proceed with an investment without knowing who the beneficial owners and prospective co-owners of a portfolio company would be.

KYC is a fundamental principle which must be applied in all operations of a fund. Before examining any transaction, the fund manager should be satisfied that he / she has gathered information sufficient to gain a view as to the identity of the ultimate beneficial owners, the source of wealth and the ownership structure. To protect the fund, it may be necessary to identify the beneficial owners of other counterparties in the transaction, including, but not limited to, equity sponsors, co-investors, lenders, shareholders, suppliers or other service providers. These principles also apply when divesting any interest in a portfolio company.

Where the fund's, fund manager's or its investors' reputational risk is linked to individual owner(s) involved in a transaction, it may be necessary to understand the full extent of the individual's business dealings (in particular partners in and activities of the business group) to determine if there are any potential areas of risk beyond those associated with the particular transaction under consideration.

The fund should not enter into transactions wherever it is suspected, or where there are substantiated allegations, that opaque corporate structures or corporate vehicles are being used. Reliance on legal documents, such as letters by private lawyers or copies of shareholder registers in jurisdictions that permit nominee shareholders, may not always protect the fund from potential damage (either material or reputational), particularly where there are credible doubts about ownership. The fund manager is responsible for disclosing to the relevant governing body of the fund and the fund's investment committee any doubts about ownership. All potential issues should be recorded and should be part of the investment assessment. Such records should be available to the fund's investors if so requested.

The fund manager should not engage in a relationship with anyone convicted of, or under investigation for, a serious criminal offence nor should they undertake transactions where there is credible evidence of existing links to organised crime and criminal activities.

Conviction of a serious crime should in almost every case be a reason to turn down a transaction. As a general principle, in the case of an on-going criminal investigation, or where an individual has been indicted, the fund manager should avoid entering into the relationship until such time that the investigation is either dropped or a decision is made whether to prosecute. This also applies to individuals who may be the subject of international arrest warrants or who have been charged with, or found to have violated, UN sanctions. The opening of a criminal proceeding should also result in postponing consideration of any possible engagement.

Aside from criminal convictions, conclusive evidence of criminal activities or associations is frequently not available. In such a case, an independent integrity report might be commissioned from a reputable risk advisory firm. See 2.2 above. These reports should assess the level of certainty or reliability of the allegations raised. The fund manager may consider evidence that the allegations are

[26] Adapted from EBRD Integrity Guidelines for Funds.

false, unfounded, or politically or commercially motivated in making its decision whether to proceed with a transaction.

In the context of an existing relationship, the fund manager should inform the relevant governing body of the fund immediately if a criminal investigation is opened, a criminal prosecution is initiated, or a criminal conviction is handed down.

Investigations or sanctions by regulatory bodies, such as securities and exchange commissions or financial oversight authorities, are warning signs which need to be carefully evaluated before proceeding. Disclosure of actions by regulatory bodies, such as regulatory fines or sanctions against existing clients, must be brought to the attention of the fund's governing body by the fund manager.

The fund manager should not engage with any person or any entity on an internationally recognised 'black list'.

Once beneficial ownership has been determined, the fund manager should assess the risk profile of the potential counterparty, its relevant shareholders and its management. Widely accepted and internationally recognised 'black lists' (e.g. UN Security Council, US Department of Treasury, FBI, financial market regulators such as the SEC or FSA, OFAC, central banks, EU Travel Ban, World Bank, Interpol, etc) should be consulted to verify whether the proposed persons, entities or their management or shareholders, appear on any list. If there is information that someone was on a black list but was later removed, the period of time on the list as well as the reason for deletion or removal from the list should be ascertained if possible. Where such lists are not accessible or available, the fund manager should seek guidance from CDC.

Integrity and reputational risks should be fully disclosed to the fund's relevant governing body and investment committee.

Awareness of matters that may give rise to integrity or reputational risks should be brought immediately to the attention of the fund's governing body which will then decide on further steps to be taken which may include obtaining external opinions. Any reputational or integrity risks with regard to a fund's existing investments or new investment proposals should be given objective consideration taking account of any mitigating factors.

Where concerns are identified, the fund manager should draw these to the attention of the fund's investment committee.

Tool 6 and *Appendix 1* contain a sample of business integrity questions to be asked during investment due diligence.

All transactions should be monitored for integrity risks throughout the life of the project.

Integrity and reputational risks may arise at any time during the duration of an investment. Monitoring implementation of governance-related obligations is particularly important to identify early warning signs and to develop appropriate responses. During investment monitoring, the fund manager should verify that implementation of any applicable obligation agreed with the portfolio company is proceeding according to schedule. In addition, fund managers should update the due diligence on company owners / managers during the course of the investment and should ensure that the appropriate due diligence is performed on any new owners / managers that emerge after the initial investment. The fund manager should carefully consider any exception, or new potentially adverse information, and, where appropriate, bring it to the attention of the fund's governing body where corrective actions should be considered.

2.4 Portfolio company policies

As part of their due diligence on potential portfolio companies, fund managers should carefully review the adequacy of their policies, including their anti-corruption, AML and KYC policies.

Where possible, fund managers should ensure that they can enforce such policies through appropriate mechanisms including through rights to sell (so-called 'put rights'), adequate board representation or financial control of a portfolio company in the event of non-compliance. Fund managers should be satisfied before investing that each portfolio company has in place (or will have in place shortly after an investment has been made) appropriate internal controls to ensure implementation of these policies and procedures. Fund managers should require appropriate certifications from portfolio companies that address terrorism, money laundering, corruption, fraud, bankruptcy, criminal investigations and judgments and other similar matters in the legal agreements relating to the investment.

CDC's standards and requirements

2. Business integrity compliance programme and policies

Appendix 5 contains overviews of relevant international standards and guidance materials against corruption, including those developed by Transparency International and the Extractive Industries Transparency Initiative.

2.5 CDC's monitoring and legal agreement requirements

In the legal agreements evidencing CDC's investment in a fund, CDC requires the fund (and its fund manager) to provide CDC with certain rights allowing it to review the fund's compliance with CDC's Investment Code, see p. 9-13, and the fund's AML / KYC policies.

Representatives of CDC must have the right to visit each portfolio company and to access their books of accounts and records to the extent reasonably necessary to monitor compliance with CDC's Investment Code and the fund's AML / KYC policies.

Should CDC notify the fund manager of a concern that there has been a violation of the provisions of either CDC's Investment Code or the fund's AML / KYC policies, the fund manager is required to cooperate with CDC in good faith to mitigate the risks posed by any violation to CDC, the fund, the fund manager and other investors.

CDC also requires the fund and the fund manager to agree that: (i) the repeated and material failure of the fund to comply with CDC's Investment Code; or (ii) the repeated failure of the fund and / or the fund manager to enforce implementation of CDC's Investment Code; or (iii) the repeated and material failure of the fund and / or the fund manager to apply CDC's Investment Code properly will give CDC the right to cease making capital contributions to the fund for future investments without penalty.

Finally, the fund and fund manager are expected to agree that should CDC request information to confirm that the fund has complied with CDC's Investment Code, the fund will promptly provide such information.

Case 2: Development of a national industry leader through improvements in governance: El Rashidi El-Mizan (MEF), Egypt

El Rashidi El-Mizan (MEF) is Egypt's leading producer of Halawa and Tahina, two traditional staple food products made from sesame seeds. CDC's fund manager Actis acquired a 65% equity share in the business.

Actis has helped MEF to implement world class standards in corporate governance and ESG management. One aim behind these improvements was to transform MEF from a family business to a leading corporation. The ESG improvements were achieved by Actis and MEF's management developing and agreeing upon a comprehensive ESG action plan at the time of Actis' investment. A strong board with independent directors was introduced shortly thereafter and the company's financial reporting capabilities were strengthened. In addition, Actis helped MEF to improve its ESG management systems with the help of a dedicated ESG expert. MEF has implemented ISO and OHSAS management systems and established reporting mechanisms on ESG to its board and investors.

When MEF was sold to Citadel Capital, a Cairo based private equity firm, the sale generated an investment cost multiple of 4.4 and an IRR of 35%. The high sales price of 410 million Egyptian pounds was attributed to MEF's excellent market position and the overall strong quality of the business. By the time of exit, MEF was a market leader, exporting to 25 countries with double the production capacity compared to at the time of Actis' investment.

CDC's standards and requirements

3. Reporting and evaluations

3.1 Reports from fund managers to CDC

CDC requires its fund managers to report on financial and non-financial parameters as specified below. For more guidance on ESG reporting for fund managers, see *Tool 12*. For CDC's recommended reporting templates and an example of a completed annual ESG report, see *Appendix 7*. For a description of CDC's monitoring and evaluation framework and indicators, see *Appendix 6*.

Fund managers are required to report to CDC as specified under 3.1.1, 3.1.2 and 3.1.3, below. Reporting as per 3.1.4 is also highly welcomed by CDC.

3.1.1 Financial performance indicates whether investments are profitable; thus returning capital to the fund's investors and demonstrating to other investors that profitable investments can indeed be made in emerging markets where some investors are traditionally reluctant to invest. For fund investments, financial performance should be measured by the net IRR of the fund and the IRR of each realised investment.

Fund managers are required to report to CDC:

- current valuations of their investments quarterly or at least annually;
- IRR for each realised exit; and
- the current net IRR of their fund, quarterly or at least annually.

3.1.2 Economic performance indicates the extent to which investments generate benefits for the local economy in terms of commercially successful and growing businesses that provide employment and generate tax revenues.

Fund managers are required to report annual data for each portfolio company to CDC as follows:

- employment;

Suggested template for annual non-financial reports

ESG and economic data: annual report for [name of fund]

<table>
<tr><th rowspan="2">Country[1]</th><th rowspan="2">Sector</th><th colspan="3">Rating of ESG risks & opportunities for improvements[2]</th><th rowspan="2">Quality of ESG management systems[3]</th></tr>
<tr><th>Environment</th><th>Social matters</th><th>Governance</th></tr>
<tr><td></td><td></td><td></td><td></td><td></td><td></td></tr>
<tr><th>Reporting period for data</th><th>Employee numbers (full time equivalents)</th><th>Currency of data</th><th>Taxes paid[4]</th><th>Turnover</th><th>EBITDA</th></tr>
<tr><td></td><td></td><td></td><td></td><td></td><td></td></tr>
<tr><th>ESG issues / opportunities for improvements at the time of investment:</th><td colspan="5"></td></tr>
<tr><th>ESG improvements achieved:</th><td colspan="5"></td></tr>
<tr><th>Status / further actions to be undertaken, with timeframe:</th><td colspan="5"></td></tr>
<tr><th>Other information:</th><td colspan="5"></td></tr>
</table>

[1] Country or countries of operation.

[2] High, medium or low. See *Tool 5*.

[3] Good, moderate or poor. See *Tool 8*.

[4] Taxes paid for last year as shown in the cash flow statement, not taxes payable in the profit and loss (P&L) statement.

3. Reporting and evaluations

- taxes paid;
- turnover; and
- profitability (EBITDA).

3.1.3 ESG performance indicates whether fund managers and their portfolio companies adhere to responsible investment and business practices and whether portfolio companies over time improve upon their practices from an ESG perspective.

Fund managers are required to report annual data for their portfolio companies to CDC as follows:

- risk ratings on ESG (high / medium / low) (see *Tool 5*);
- assessment of the quality of each portfolio company's ESG management system (good / moderate / poor) (see *Tool 8*);
- any ESG issues;
- improvements undertaken and underway, including any certifications if relevant, and future targets; and
- as relevant:
  - development outlays, e.g. charitable contributions; and
  - environmental products or services.

3.1.4 Private sector development indicates whether investments have broader positive effects for the local economy and communities including increased availability of capital from third party investors; more efficient capital markets; improvements in standards and regulations; and increased availability of better quality goods, services and infrastructure for the benefit of local communities.

Fund managers are encouraged to provide information to CDC in the form of case studies on the private sector development contributions of their fund(s) and their portfolio companies.

3.2 Serious incidents

In accordance with CDC's Investment Code, CDC's fund managers are required to monitor and record serious incidents involving portfolio companies that result in loss of life, material effect on the environment or material breach of law, promote appropriate corrective actions and report such incidents to CDC, with plans for corrective actions. Such serious incidents involving a portfolio company can have negative reputational implications for the fund manager as well as for investors in a fund. CDC takes any notification of a serious incident very seriously.

CDC's portfolio director responsible for a fund investment where a serious incident has been reported follows up with the fund manager as corrective actions are undertaken to ensure that adequate measures are being implemented in a timely manner. CDC follows up with the fund manager until there are sufficient assurances that the situation has been dealt with in a satisfactory manner and that risks for reoccurrence are mitigated appropriately.

For CDC's recommended template for reporting serious incidents, see *Appendix 7*.

3.3 Evaluations

CDC and other development finance institutions (DFIs) periodically perform in-depth evaluations of their fund investments. This is also the practice of some private sector investors. CDC's evaluations follow CDC's monitoring and evaluation framework to assess the development effects of investments as described in *Appendix 6*, using the evaluation template enclosed in this appendix. CDC's framework for evaluations is consistent with, while not identical to, that used by the IFC. See *Appendix 8* for a comparison. Evaluations can either be performed by CDC's investment professionals, assisted by ESG specialists, or by external consultants.

Since 2008, all of CDC's fund investments are evaluated:

- at the end of a fund's investment period or the half-way point of the duration of a fund, which would typically be 5 years after a standard fund has commenced; and
- at the end of the duration of a fund, which would typically be 10 years after a standard fund has commenced.

Fund managers are expected to collaborate with CDC's monitoring and evaluation framework. Fund managers normally assist CDC or CDC's evaluation consultants with interviews, access to portfolio company records, site visits and in other ways as appropriate to provide an in-depth understanding of a fund and its investments. Site visits to portfolio companies would normally focus on high-risk investments.

Findings from evaluations are shared by CDC with the relevant fund manager, and recommended actions are discussed. Recommendations from mid-point evaluations are expected to be implemented by fund managers and their portfolio companies during the remainder of the investment duration for a fund. The recommendations and findings in evaluation reports contribute to CDC's due diligence and decision making for investments in successor funds.

The Toolkit

Toolkit on ESG for fund managers

Contents

The Toolkit

1

Tool 1

Adding value through ESG improvements

Opportunities to add value to businesses from ESG improvements often depend on the industry sector and country. Examples include:

- access to a wider range of customers from improving production and operating standards to comply with international best practice, e.g. for pharmaceutical or food companies;
- cost reductions from efficient energy use, e.g. in cement production;
- access to carbon credits from reduction of greenhouse gas emissions, e.g. avoided venting / flaring from gas exploration or transportation, or fuel switching;
- compliance with ESG standards to obtain a licence to operate in a market or to list a company on a stock-exchange through an initial public offering (IPO);
- improved productivity, e.g. retention of personnel from corporate HIV / AIDS programmes in Africa; and
- improved management from good corporate governance and business integrity standards and practices.

An investor can benefit from a systematic approach to review the specific ESG factors that are the most relevant to key business success factors for the companies in which he / she considers investing. The matrix below illustrates a way to consider how each ESG factor can drive or contribute to different business success factors.[1] Working through the different ESG factors, this matrix can help a fund manager clearly articulate the areas where improvements during the investment period can help business success.

There are numerous examples where sound ESG management is a key business success factor. Fund managers should consider how each ESG factor can drive or contribute to different business success factors as per this matrix.

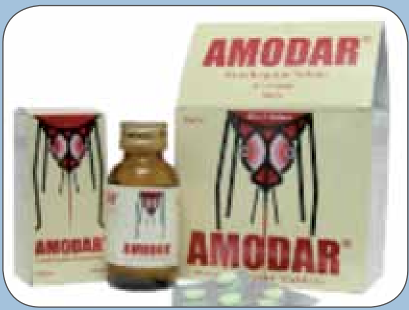
		ESG factors: improvements during the investment period						
		Environment		Social matters			Governance	
		Environmental standards & processes	Environmental products / services	Labour & working conditions	Health & safety	Other social matters	Business integrity	Corporate governance
Business success factors	Revenue growth and market access							
	Cost savings and productivity							
	Access to capital							
	Risk management and license to operate							
	Human capital							
	Brand value and reputation							

[1] *Developing Value, The business case for sustainability in emerging markets,* SustainAbility, IFC and Ethos Institute, 2004. www.sustainability.com Adapted by CDC and Rosencrantz & Co to align with CDC's Investment Code.

Adding value through ESG improvements

Case 3: Example of the business case for ESG improvements: Shelys Pharmaceuticals, Tanzania

CDC invested in Shelys Pharmaceuticals through its fund manager Aureos. Following Aureos' advice, Shelys has obtained World Health Organization Good Manufacturing Practices (WHO GMP) certification although this is not mandatory for a pharmaceuticals company in Tanzania. Moreover, although Tanzania has no formal codified environmental requirements for the pharmaceutical sector, Shelys has worked to ensure that WHO standards on effluent discharge are met as well.



The effect of obtaining such certification for the company has been pronounced. Shelys' improved production standards have allowed its products sales access to eight countries across Central and Eastern Africa.

Moreover, when Aureos decided to sell Shelys it was able to do so for a premium price. Shelys' leading position in East Africa, coupled with improvements in manufacturing standards and improved corporate governance, persuaded Aspen Pharmacare, Africa's largest pharmaceutical manufacturing and distribution company, to acquire a majority stake in Shelys as part of its African expansion strategy. Aureos achieved well over two times its initial cash investment from the sale.

Example of how ESG factors contributed to expanding sales for Shelys Pharmaceuticals and to a high exit premium for Aureos.

		ESG factors: improvements during the investment period						
		Environment		Social matters			Governance	
		Environmental standards & processes	Environmental products / services	Labour & working conditions	Health & safety	Other social matters	Business integrity	Corporate governance
Business success factors	Revenue growth and market access	■			■			
	Cost savings and productivity							
	Access to capital	■			■			■
	Risk management and license to operate	■			■			■
	Human capital							
	Brand value and reputation	■			■			■

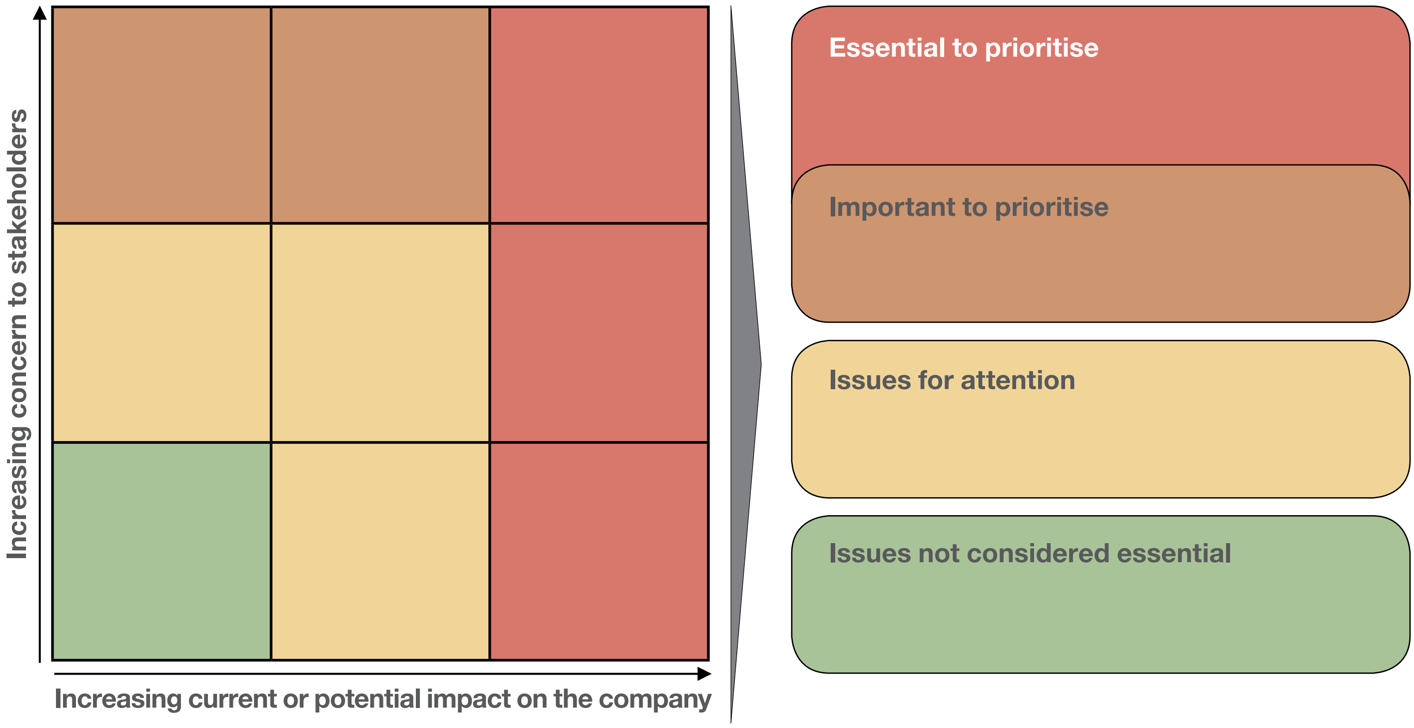
Materiality focus

For an integrated ESG analysis to add the most value during screening, due diligence and throughout the investment duration, a fund manager's approach towards investee companies should be pragmatic and focus on the key areas where a strategic focus on ESG improvements can make the most difference. The key ESG issues will be different depending on the sector, the country, the markets the company serves and so on, and should align with the company's core business and capabilities. Having identified the key ESG issues for a particular company, management should prioritise actions based on which ESG matters have the highest current or potential impact for the company's business and which issues are of the highest concern for the company's stakeholders. The matrix overleaf illustrates such an analysis.

Tool 1

Adding value through ESG improvements

Materiality matrix: categorising ESG areas for improvement according to their current or potential impact on the company and their concern to stakeholders



Source: SustainAbility. Adapted by CDC and Rosencrantz & Co.

Adding value through improvements in corporate governance

One of the most important ways in which fund managers can add value to their portfolio companies throughout the investment duration is through improvements in corporate governance. Improvements in corporate governance strengthen the way a company is managed with benefits for performance and brand.

Small firms and family-owned and -run businesses are among those where even initial improvements to implement minimum standards of good corporate governance can quickly result in improved transparency and better decision making and thus in better run and more profitable companies.

The matrix[2] opposite illustrates how fund managers can analyse whether potential investee companies adhere to minimum good corporate governance standards and how they can help portfolio companies make continuous improvements towards best practice over time. The elements of best practice for corporate governance in this matrix mostly concern larger companies.

A useful exercise for investment professionals during their due diligence is to use this matrix as a basis for discussions with the management of a potential investee company to map out the company's current corporate governance practices on the scale from minimum (or less) to good practice towards best practice. The fund manager can then use this analysis to propose an action plan for improvements over the investment duration.

[2] This matrix illustrating the three levels of advancement in good corporate governance is based on the OECO Principles of Corporate Governance, material from the IFC and the work of a DFI working group on corporate governance, adapted by CDC and Rosencrantz & Co. See *Appendix 5*.

Adding value through ESG improvements

Elements of good corporate governance	Minimum	Good Practice	Best Practice
1. Commitment to good corporate governance	The basic formalities of corporate governance are in place, including: • A board of directors which meets regularly. • Annual shareholders meetings. • Shareholders recorded. • Remuneration policy which rewards the achievement of corporate objectives.	Written policies addressing key elements of corporate governance: • Audit and control systems. • Annual meetings of shareholders. • Shareholders' rights, including minority. • Codes of ethics, corporate conduct and ESG. • Annual, board approved, calendar of corporate events.	• Corporate governance, accounting, auditing, internal controls and shareholder information practices are equivalent to those of leading public companies and in line with the country's voluntary code of best practice.
2. Structured and functioning board	• A board of directors is constituted, meets regularly and deliberates independently of executive management.	• Board meetings are held according to a regular schedule. Agenda is prepared in advance. Minutes are approved. • Board composition (competencies / skill mix) is adequate for oversight duties. • Audit committee of non-executive directors established, at least 1 independent director.	• A majority of board directors are independent of management / owners. • Audit committee is composed entirely of independent directors. • Board committees are established, including for nominations, remuneration and ESG.
3. Control and risk management	Adequate internal control and risk management systems are in place and periodically reviewed by independent external auditors.	Internal audit and risk management systems are in accordance with highest national standards.	Internal audit and risk management systems are consistent with highest international standards.
4. Transparency and disclosure	Adequate accounting and auditing systems are in place, including: • quarterly financial reports approved by the board; and • annual financial statements audited by a recognised firm.	• Accounting and reporting according to highest international standards (IFRS or US GAAP). Annual reporting on ESG matters. • The annual audit is performed by a recognised independent external auditing firm. Financial statements are publically disclosed.	• Financial statements and other material information is disclosed on the internet in a timely manner. • Shareholder concentrations and controlling ownership are clearly disclosed.
5. Rights of minority shareholders and treatment of stakeholders	Annual shareholders' meetings are held. All shareholders are provided with all material information and a detailed agenda in advance.	• Minority shareholders have the right to nominate / appoint board representative(s). • Consultation policy is in place for company stakeholders.	• Clear and enforceable policy and voting mechanism to protect minority shareholders. • Clear and enforceable policy to consult with and protect stakeholders. • Full and timely disclosure of all material shareholders' agreements.

Tool 2

ESG policies and guidelines

Sound investment management of ESG issues starts with a policy commitment from the fund manager. Such a policy statement should include concrete benchmarks for investment standards from the ESG perspective and an exclusion list detailing businesses and activities in which the fund manager will *not* invest. Investors in funds, as well as the general public, are increasingly expecting to see explicit ESG policies from fund managers.

An explicit ESG policy facilitates the interaction between a fund manager and a potential investee company in clarifying expectations for both parties. A fund manager should discuss its ESG policy with a potential investee company at an early stage in their interactions to ensure that the company is willing and able to comply with the expected standards, or to bring about appropriate improvements during the investment duration.

Full compliance with all local environmental, social, business integrity, disclosure and other laws is always the very minimum standard for an ESG policy.

An exclusion list identifies any sectors, businesses or activities that the fund manager will *not* invest in since they are judged to be inherently unsustainable and / or not in line with the ethical vision of the fund manager and investors in the fund.

ESG standards beyond local laws are often necessary for investments in countries where the local legislation is weak or poorly enforced. In formulating its ESG policy, the fund manager should consider the advantages that higher standards have for its portfolio companies in terms of reduced risks and access to markets with higher standards; the positive influence on the fund manager's reputation and ability to attract capital; and potential new and enhanced exit opportunities which could come from improved standards.

Development finance institutions (DFIs) such as CDC have specific requirements for the ESG policies that they expect to see from fund managers investing their capital. CDC's Investment Code, p. 9-13, sets out CDC's ESG policies and exclusions to which all fund managers that invest CDC's capital are required to commit.

Sections 1.1-1.4 of CDC's Investment Code specify the ESG policies and guidelines that fund managers that invest CDC's capital are expected to apply. Sections 1.1-1.3 apply to their portfolio companies.

CDC's Investment Code contains references to international standards and conventions, among which some are requirements for all fund managers investing CDC's capital, some are mandatory for fund managers investing in high risk assets and some are best industry practice to be worked towards over time. The international standards and conventions referred to in CDC's Investment Code are briefly described in *Appendix 5,* along with additional useful international guidance materials that can assist fund managers to formulate their ESG policies and guidelines.

Case 4: Example of the business case for ESG improvements: Outsourcing Services Limited (OSL), Nigeria

Outsourcing Services Limited (OSL) is a security outsourcing company that supplies security guards for companies operating in Nigeria. CDC's fund manager African Capital Alliance (ACA) acquired a 40% stake in OSL in 1999. Given the difficult security situation In Nigeria, OSL was clearly a high-risk investment.

ACA was instrumental in instituting numerous improvements for OSL's employees. OSL's security guards became better trained and better paid than guards at competitor firms. With higher standards, OSL was able to charge a premium from its corporate clients and became the leading firm in the outsourced security services industry in Nigeria.

The international firm G4S bought ACA's stake in OSL for US$10m in 2009. This sale realised an IRR of 58% over 10 years, one of the most successful exits to date from CDC's fund-of-funds portfolio.

Case 5: Example of the business case for cleaner technologies: Suntech Power, China

Suntech Power is a Chinese manufacturer of crystalline silicon solar cells, modules and solar powered products which received an investment of US$12.5m from CDC's fund manager Actis in 2005. The investment proved to be a financial success. Suntech Power first floated shares on the New York stock exchange in 2005 and Actis exited fully in 2007 at a multiple of 11.9x investment cost and an IRR of 684%.

When Actis invested in Suntech Power, its investment team identified various environmental and social issues which needed careful management. These included waste water disposal, the handling of hazardous substances and the use of CFCs in refrigeration and air conditioning units. An environmental impact assessment performed in the early phase of Actis' investment showed that Suntech Power's production met all statutory standards related to water, air and noise pollution. Actis was instrumental in ensuring that Suntech Power's employees followed formal, written procedures when handling hazardous materials.

Actis was able to add substantial value to Suntech Power's operations through improvements in corporate governance. Actis assisted in Suntech Power's initial public offering (IPO) and helped recruit to a new CFO. Over Actis' investment period, Suntech's turnover increased by almost 1500%, whilst employment numbers rose by nearly 400%.

Tool 3

ESG considerations at each stage of the investment process

An effective ESG management system requires a fund manager to pay attention to ESG matters at all stages of the investment process. The actions and procedures involved are described below, with references to how the *Tools* and *Appendices* in this Toolkit can be helpful for fund managers at different stages of their investment process.

CDC's requirements on ESG management systems for fund managers that invest CDC's capital are described in CDC's Investment Code, section 1.4, p. 13. CDC's requirements are fully consistent with the actions and procedures described below.

For guidance on how to consider ways to add value from the ESG perspective at any stage in the investment process (see *Tool 1*).

For guidance on how the fund managers' internal organisation can support an effective ESG management system (see *Tool 4*).

Initial screening	Due diligence	Investment decision	Investment agreement	Investment monitoring	Exit

At the initial screening of a potential investment opportunity, fund managers need to assess whether the investment proposition is in line with their ESG policies and guidelines (see *Tool 2*), notably that the investment does not violate their exclusion list. If a potential investment includes any of the businesses or activities listed as excluded by the fund manager, the investment can normally not proceed.

Fund managers that invest CDC's capital should contact and consult with CDC if they have any doubts as to whether a potential investment would fall within CDC's exclusion list or not (see p. 12). In very rare circumstances, the fund may proceed with an investment, while not be permitted to deploy CDC's capital for that investee company.

If there are other reasons why a fund manager would question whether a potential investment is in line with its ESG policies, the fund manager would need to assess whether the operations of that company could be brought in line with those policies over a reasonable timeframe and thus whether to proceed to due diligence or not.

Identifying opportunities for improvements and rating ESG risks (see *Tools 1* and *5*) are important elements of the initial screening of potential investment opportunities. The risk rating determines how much attention a particular investment should receive during the due diligence and whether specialist assistance is required, as would normally be expected for investments in sectors with significant risks.

Initial screening	**Due diligence**	Investment decision	Investment agreement	Investment monitoring	Exit

The due diligence stage is when a fund manager can most effectively assess the ESG credentials of the potential investee company and the risks involved.

During due diligence, the fund manager should thoroughly check the company's compliance with all relevant laws and regulations and with the standards stipulated in the fund's ESG policy; for CDC's fund managers, CDC's Investment Code (see p. 9-13).

Due diligence questions on ESG matters (see *Tool 6* and *Appendices 1-2*) help fund managers to establish the key areas to focus on. Sector-specific questions (see *Appendix 2*) enhance the due diligence. If the investment involves significant risks, an environmental and social impact assessment, conducted by specialists, would normally complement the fund manager's own due diligence (see *Tool 7*).

At the due diligence stage, it is also important for fund managers to assess the quality of the potential investee company's management systems in relation to the identified ESG risks and opportunities for improvements. Questions to help fund managers with this assessment are provided in *Tool 8*.

Tool 3

ESG considerations at each stage of the investment process

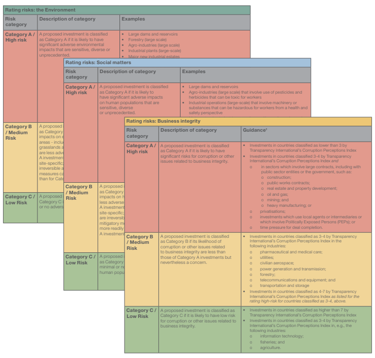
Please see below an illustration of the process involved in rating ESG risks, conducting due diligence, and assessing a company's ESG management systems, which should all contribute to formulating an action plan for improvements that may have to be undertaken during the investment duration.

1. Rate inherent ESG risks for the potential investee company, considering the sector, size of operations, country, etc (see *Tool 5*).

2. Enhance the analysis through due diligence questions (see *Tool 6* and *Appendices 1-2*) and, if the potential investment involves high risks from the environmental and / or social perspective, through an environmental and social impact assessment (see *Tool 7*).

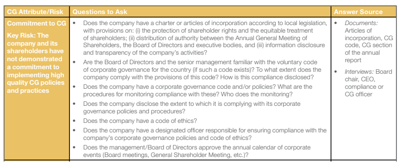
3. Assess the quality of the potential investee company's ESG management system in relation to risks and identify needs for improvements (see *Tool 8*).

1 Rating ESG risks



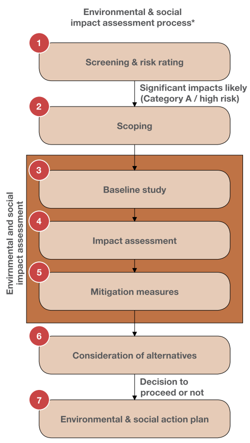
Tool 5

2 Due diligence questions



Tool 6 and Appendices 1-2

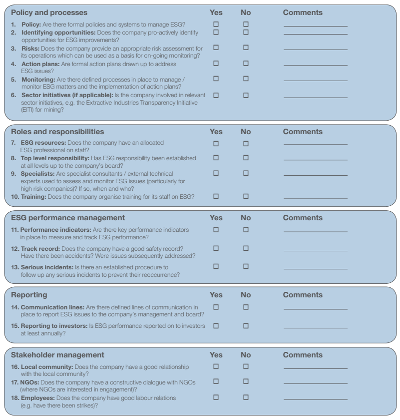
If high risks: **environmental and social impact assessment**



Tool 7

*Adapted from the IFC "A Guide to Biodiversity for the Private Sector

3 Assessment of a company's ESG management systems in relation to risk level



Tool 8

4. Formulate an action plan together with the management of the potential investee company, detailing the areas of ESG concern as identified through steps 1-3, with the risk levels, actions required, timeframe, proposed responsibilities and costs involved (see *Tool 9*).

4 Action plan for ESG improvements

Area of ESG concern as identified through DD or management systems questions or through environmental and social impact assessments	Level of ESG risk (H, M or L)	Action required	By when	Responsibility (company staff, management and board member)	Cost (US$)
X					
Y					
Z					

Tool 9

Tool 3

ESG considerations at each stage of the investment process

Initial screening | Due diligence | **Investment decision** | Investment agreement | Investment monitoring | Exit

At the time of the investment decision, the fund's investment committee needs to have the opportunity to consider all of the aspects of the ESG analysis so that these findings can be assessed in the context of the deal as a whole. The investment paper should bring out all of the relevant elements and include an action plan for necessary improvements over the investment duration, with associated timeframe and costs (see *Tool 9*).

Initial screening | Due diligence | Investment decision | **Investment agreement** | Investment monitoring | Exit

During the investment negotiations, the action plan for necessary improvements should be discussed and agreed upon between the fund manager and the management of the potential investee company.

As part of the investment negotiations, it is also important to establish that the potential investee company has ESG policies which are in line with the fund manager's ESG policies and guidelines; for CDC's fund managers CDC's Investment Code. The fund manager should present its ESG policies and guidelines (see *Tool 2*) to the management of a potential investee company at an early stage in their interactions to clarify expectations on both parts.

Before making the investment, the fund manager should seek a formal legal commitment from the potential investee company to adhere to the fund manager's ESG policies (see *Tool 10*).

ESG considerations at each stage of the investment process

Initial screening → Due diligence → Investment decision → Investment agreement → **Investment monitoring** → Exit

During the investment period, the fund manager should monitor its investment from the ESG perspective:

- to check the portfolio company's on-going compliance with all legislation relating to ESG matters and with the standards stipulated in the fund's ESG policy (see *Tool 2*);
- to ensure timely implementation of any action plan for ESG improvements (see *Tool 9*);
- to encourage the managers of the portfolio company to work towards continuous improvements (see *Tools 1* and *11*);
- to ensure that any new risks, issues or opportunities for improvement that may emerge are dealt with in an appropriate manner (see *Tools 1, 5, 6* and *11*);
- to monitor and record any serious incidents involving portfolio companies that result in loss of life, serious injury, material effect on the environment, or material breach of law, and promote appropriate corrective actions (see *Tool 12*);
- to record and report key performance indicators to the fund's investment committee, governing body, investors and the general public (see *Tool 12* and *13*); and
- to review the company's strategy in the light of changes, for example in regulation, markets and technology, over the investment duration (see *Tool 1*).

See *Tool 11* for further guidance on investment monitoring from the ESG perspective.

ESG issues should be tabled at the portfolio company's board and reported to investors at least once a year. A suggested reporting format is provided in *Tool 12*, with examples of an annual ESG report in *Appendix 7*.

The fund manager may also wish to make information about its ESG policies and the performance of portfolio companies available to the broader public through its website and annual reports. Suggestions for such disclosure are provided in *Tool 13*.

Initial screening → Due diligence → Investment decision → Investment agreement → Investment monitoring → **Exit**

At the exit, the fund manager realises the return on its investment and seeks to maximise the exit price. To generate the best outcome for society as a whole, as well as for the reputation of the fund manager, sound ESG policies and practices implemented during the investment duration should continue under the new ownership. The fund manager should take account of the future of a portfolio company under its new ownership and assume some responsibility for ensuring that sound management of ESG matters will continue. See *Tool 14* for considerations on ESG for investment exits.

Tool 4

Questions to assess a fund manager's ESG management systems

The fund manager's internal structure should be organised appropriately to support sound ESG management of its investments. For investments in sectors with significant ESG risks, fund managers would normally require specialist staff or external specialist assistance. Appropriate procedures need to be implemented to support the relevant actions at each stage of the investment process. Adequate internal reviews and controls are needed to ensure that these procedures are followed.

Partners and investment executives need to be trained and incentivised to build ESG into their investment decisions and investment management. A basic level of training can help fund managers increase their awareness of ESG issues and enhance their ability to address ESG risks and opportunities for improvements.

The following questions can be used to help assess the quality of the internal organisation of a fund manager and its ability to manage ESG in its investment activities.

Policy and processes	Yes	No	Comments
1. Policy: Are there formal policies and systems to manage ESG?	☐	☐	________
2. Identifying opportunities: Does the fund manager proactively identify opportunities for ESG improvements for its investments?	☐	☐	________
3. Risks: Are investments formally assessed for ESG risk and given an appropriate level of monitoring based upon this risk taking?	☐	☐	________
4. Critical risks: Can ESG considerations act as a block on a potential investment opportunity?	☐	☐	________
5. Action plans: Are formal action plans drawn up to address ESG deficiencies?	☐	☐	________
6. Monitoring: Are there any processes in place to manage / monitor ESG risks and to implement action plans for improvement?	☐	☐	________

Roles and responsibilities	Yes	No	Comments
7. ESG resources: Does the fund manager have a designated ESG professional?	☐	☐	________
8. Top level responsibility: Has ESG responsibility been established at all levels including the fund's investment committee and governing body?	☐	☐	________
9. Specialists: Are specialist consultants / external technical experts used to assess and monitor high risk investments? If so when and who?	☐	☐	________
10. Training: Does the fund manager provide ESG training for all relevant staff?	☐	☐	________

ESG performance management	Yes	No	Comments
11. Performance indicators: Are there key performance indicators in place to measure and track ESG performance at portfolio companies?	☐	☐	________
12. Serious incidents: Is there an established protocol for how to follow up serious incidents involving portfolio companies?	☐	☐	________

Reporting	Yes	No	Comments
13. Communication lines: Are there defined lines of communication in place to report on ESG matters, including any serious incidents, to the fund manager's investment committee and governing body?	☐	☐	________
14: Reporting to the fund's investors: Are ESG matters reported on to the fund's investors at least annually and are any serious incidents reported immediately?	☐	☐	________

Stakeholder management	Yes	No	Comments
15. Disclosure: Does the fund manager publically communicate on ESG matters through its annual report and website?	☐	☐	________
16. Media: Does the fund manager maintain a good relationship with the media on ESG aspects of their investments?	☐	☐	________

Tool 4

Questions to assess a fund manager's ESG management systems

The need for specialist staff and technical consultants depends on the risk level of the investment strategy of the fund and the types of investments made. For investments in high risk assets from the ESG perspective, specialists usually need to be involved in the due diligence and throughout the investment management process.

A fund manager that specialises in high ESG risk investments, e.g. mining in Africa, would probably hire specialist personnel for due diligence and investment management of ESG matters (see *Tool 5* for guidance on how to rate ESG risks). A fund manager that invests in multiple different high risk sectors, or that only occasionally considers investing in assets with significant ESG risks, would probably be better served by using consultants with appropriate specialist expertise for each such investment consideration.

Case 6: Responsible coal mining in India: Sainik Mining

Sainik Mining is one of the biggest coal mining contractors in India and has received an investment from CDC's Indian fund manager ICICI. Sainik Mining has demonstrated a strong commitment to addressing the environmental and social risks associated with mining. The company addressed the impact of its greenhouse gas emissions in two ways. Firstly, it uses a form of surface mining that minimises the high pollution levels associated with drilling and blasting. Secondly, Sainik Mining's sister company has developed a 'washing' process that reduces greenhouse gas emissions when coal is burned. Sainik Mining's coal washing plant in Chattisgarh is the largest such facility in the world.

While implementing these improvements, Sainik Mining has seen its turnover grow by US$21m since ICICI's investment and its profitability increase by US$8m. Sainik Mining's operations represent a good example of how a company can address the complex issues associated with mining in a responsible and financially sustainable manner.

Sainik Mining's management also finances charitable activities, including schools for girls in the local communities around its headquarters and mining operations.

5

Tool 5

Rating ESG risks

Fund managers can be well served by a systematic risk rating system for ESG matters. Such a system should rate each potential investment as high, medium or low for ESG risks. Rating ESG risks during the initial screening and fine-tuning the ratings during the due diligence, provides fund managers with an understanding of which investments that would require more thorough attention from an ESG perspective, and whether to involve specialist technical expertise to enhance the due diligence through e.g. an environmental and social impact assessment (see *Tools 6-7* and *Appendices 1-2*). The ESG management systems of portfolio companies should be proportional to their risk level (see *Tool 8*).

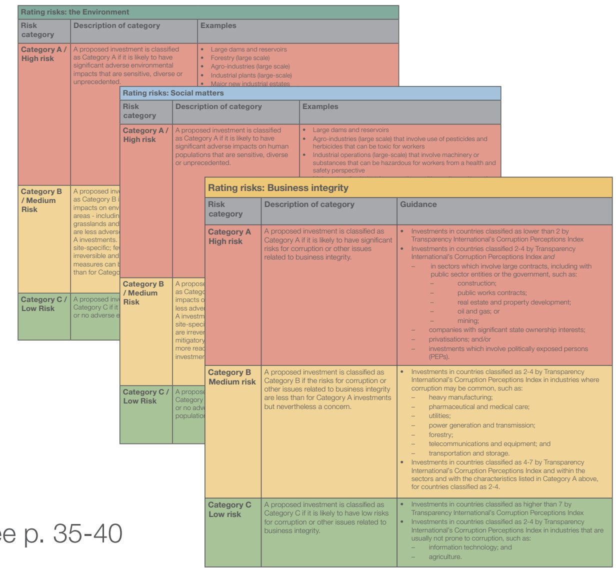
Considering risks in a systematic way enhances the investment paper and provides the fund manager's investment committee with important information upon which to base its investment decision (see *Tool 9*). The risk rating also serves as a tool to focus attention on the investments that require more attention during the fund manager's monitoring of portfolio companies, including through regular site visits (see *Tool 11*).

Examples of high ESG risks:

- highly polluting industries, such as large factories, oil and gas extraction and refineries;
- activities which affect the natural environment, for example mining, large scale agribusiness, forestry and construction of new infrastructure;
- resource intensive industries, including cement plants and aluminium smelters;
- businesses which use low skilled workers such as textile production, mining, agribusiness and forestry, in countries with weak labour legislation;
- businesses which involve workers handling hazardous substances, for example mining, large scale agribusiness and chemical factories;
- businesses which can pose health and safety dangers for consumers, such as pharmaceuticals and food producers; and
- businesses which deal with large contracts in sectors and countries that are prone to bribery, including construction, extractive industries and other public procurement contracts.

Risks are usually lower for small and medium sized enterprises (SMEs). Microfinance usually involves low environmental and social risks while governance risks may be present from the business integrity and / or corporate governance perspectives.

Rating ESG risks



See p. 35-40

Tool 5

Rating ESG risks

The following pages provide guidance on how to rate companies as high, medium or low risk from the ESG perspectives. Such risk ratings, along with the enhanced analysis provided by due diligence questions (see *Tool 6* and *Appendices 1-2*) and, if the investment is considered to involve high-risks, with the findings from an environmental and social impact assessment (see *Tool 7*), together with an assessment of the potential investee company's ESG management systems, as proportional to the risk level, (see *Tool 8*), helps the fund manager to identify and prioritise actions for improvements that may need to be undertaken during the investment period.

While risk ratings from the environmental and social perspectives are fairly well established, the proposed methodology for rating governance risks has been developed by CDC and Rosencrantz & Co, building on work by Transparency International in the area of business integrity and, for corporate governance, on the OECD Principles of Corporate Governance and material developed by the IFC and a development finance institution (DFI) working group on corporate governance.

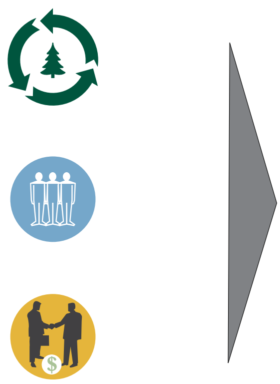
Business integrity and corporate governance risks may cut across most sectors, as governance risks are linked to inadequate company policies, deficient internal controls, unreliable reporting or other inappropriate practices. Some countries and some sectors are, however, more prone to business integrity risks than others. Corrupt practices are particularly common in sectors that involve large public sector contracts. CDC expects a zero-tolerance corruption policy from its fund managers irrespective of local laws and customs. Good corporate governance can reduce business integrity risks.

The Dutch DFI FMO has developed a microsoft excel tool to help private equity fund managers assess risks from the environmental and social perspectives. This tool is compatible with CDC's recommended risk rating system and can be downloaded from FMO's website www.fmo.nl

Some of the European DFIs use a four step rating process for environmental and social risks, which includes a B+ category. This approach is compatible with CDC's recommended three step risk rating system.

CDC's recommended ESG risk rating system is explained for each of the three environmental, social and governance parameters in the following pages.

Rating ESG risks



ESG risk ratings
Category A-C
High / medium / low

See p. 35-40

5

Tool 5

Rating ESG risks: The Environment

1. Rating environmental risks

This is an illustrative matrix for rating environmental risks. It should be stressed that each investment needs to be assessed on an individual basis. The due diligence questions in *Tool 6* and *Appendices 1-2* enhance the basic assessment of environmental risks provided by this matrix, which is based on inherent sector risks, the scale of the company's operation and whether the investment involves new or continued operations and locations.

Rating risks: the Environment		
Risk category	**Description of category**	**Examples**
Category A High risk	A proposed investment is classified as Category A if it is likely to have significant adverse environmental impacts that are sensitive, diverse or unprecedented.	• Large dams and reservoirs • Forestry (large scale) • Agro-industries (large scale) • Industrial plants (large-scale) • Major new industrial estates • Extractive industries, including mining, major oil and gas developments and major pipelines • Large ferrous and non-ferrous metal operations • Large port and harbour developments • Developments with large resettlement components • Large thermal and hydropower development • Projects that include the manufacture, use or disposal of environmentally significant quantities of pesticides or herbicides • Manufacture, transportation and use of hazardous and / or toxic materials • Domestic and hazardous waste disposal operations
Category B Medium risk	A proposed investment is classified as Category B if its potential adverse impacts on environmentally important areas including wetlands, forests, grasslands and other natural habitats are less adverse than those of Category A investments but more adverse than Category C investments. These impacts are site-specific; few if any of them are irreversible and in most cases mitigating measures can be designed more readily than for Category A investments.	• Agro-industries (small scale) • Electrical transmission • Aquaculture • Renewable energy (except large hydroelectric power projects) • Tourism (including hotel projects) • Rural water supply and sanitation • Rehabilitation, maintenance and modernisation projects (small scale) • Manufacture of construction materials • General manufacturing • Telecommunications • Greenfield projects in existing industrial estate
Category C Low risk	A proposed investment is classified as Category C if it is likely to have minimal or no adverse environmental impacts.	• Advisory assignments • Media and information technology • Life insurance companies • Securities underwriters and broker / dealers • Technical assistance

Rating ESG risks: Social matters

2. Rating social risks

Social matters include labour and working conditions, health and safety and other social aspects, including impacts on communities and consumers. This is an illustrative matrix for rating social risks. The due diligence questions in *Tool 6* and *Appendices 1-2* enhance the basic assessment of social risks provided by this matrix, which is based on inherent sector risks, the scale of the company's operations and different types of social risks.

Rating risks: Social matters		
Risk category	**Description of category**	**Examples**
Category A High risk	A proposed investment is classified as Category A if it is likely to have significant adverse impacts on human populations that are sensitive, diverse or unprecedented.	• Large dams and reservoirs • Agro-industries (large scale) that involve use of pesticides and herbicides that can be toxic for workers • Industrial operations (large-scale) that involve machinery or substances that can be hazardous for workers from a health and safety perspective • Major extractive industries operations, with on-site workers who often work on remote locations • Projects with large resettlement components and all projects with potentially major impacts on local communities • Projects affecting indigenous or tribal populations • Projects that include the manufacture, use or disposal of environmentally significant quantities of pesticides and herbicides • Manufacture, transportation and use of hazardous and / or toxic materials • Domestic and hazardous waste disposal operations • Any projects which pose serious health and safety risks • Any projects which pose serious socio-economic concerns
Category B Medium risk	A proposed investment is classified as Category B if its potential adverse impacts on human populations are less adverse than those of Category A investments but more adverse than Category C investments. These impacts are site-specific; few if any of them are irreversible; and in most cases mitigatory measures can be designed more readily than for Category A investments.	• Agro-industries (small scale) • Electrical transmission • Aquaculture • Renewable energy (except large hydroelectric power projects) • Tourism (including hotel projects) • Rural water supply and sanitation • Rehabilitation, maintenance and modernisation projects (small scale) • Manufacture of construction materials • General manufacturing • Textile plants • Greenfield projects in existing industrial estates
Category C Low risk	A proposed investment is classified as Category C if it is likely to have minimal or no adverse impacts on human populations.	• Advisory assignments • Media and information technology • Life insurance companies • Securities underwriters and broker / dealers • Technical assistance

5

Tool 5

Rating ESG risks: Governance

3. Rating governance risks: business integrity and good corporate governance

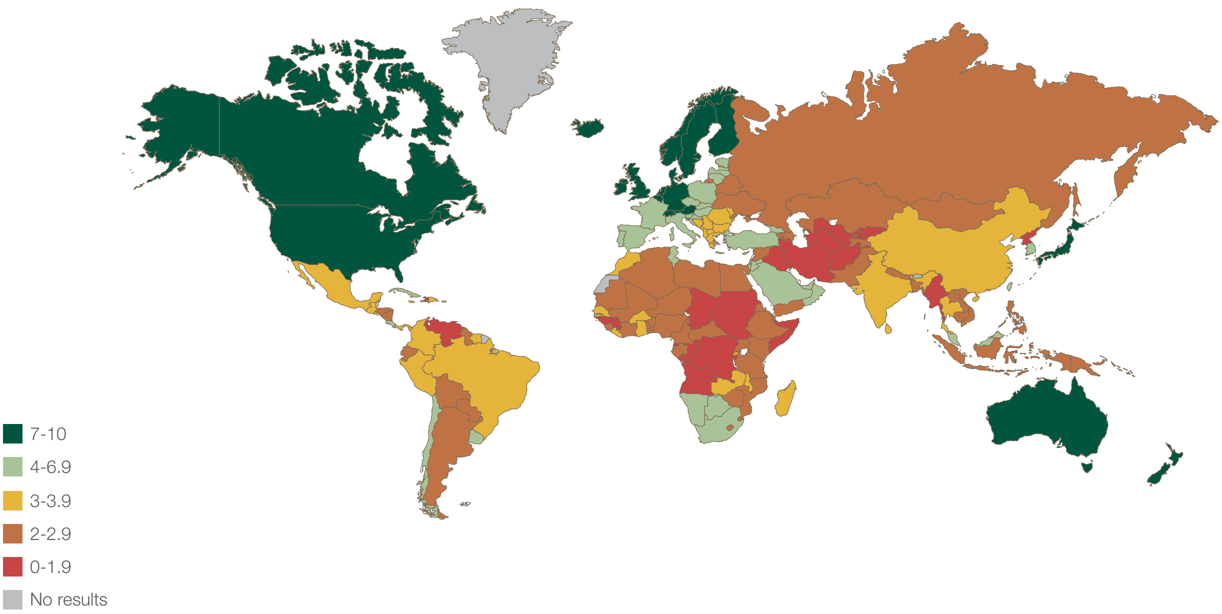
Governance includes aspects of business integrity as well as good corporate governance. The methodology for rating governance risks described below starts from the business integrity perspective, by firstly considering country risks and secondly by considering risks from certain industries and types of businesses or deals. Recognising that good corporate governance reduces business integrity risks, this methodology then proceeds to rate the potential investee company based on whether it has all, some or few basic elements of corporate governance. Finally, this risk rating methodology combines the business integrity and corporate governance risk ratings into one risk rating for governance. The due diligence questions in *Tool 6* and *Appendices 1-2* enhance the basic assessment of governance risks from following this methodology.

Business integrity risks are most pronounced in sectors which involve large public sector contracts. Certain countries and regions are more prone to corruption than others.

Fund managers that invest in countries which are ranked as prone to corruption by Transparency International's Corruption Perceptions Index (www.transparency.org), especially in sectors where corruption is common place, should rate their investments as high risk from the business integrity perspective and pay particular attention to managing business integrity risks during the investment period by instituting appropriate policies and procedures. A country ranking below 3 in Transparency International's Corruption Perceptions Index means that corruption is perceived to be endemic in that country. CDC's recommended risk rating methodology for business integrity risks rates all investments in countries classified as lower than 2 as high risk, as well as investments in certain industries and types of businesses or deals in countries classified as 2-4.

For more information about Transparency International and its work, see *Appendix 5*.

Transparency International's Corruption Perceptions Index 2009



Rating ESG risks: Governance

Rating risks: Business integrity		
Risk category	**Description of category**	**Guidance[1]**
Category A High risk	A proposed investment is classified as Category A if it is likely to have significant risks for corruption or other issues related to business integrity.	• Investments in countries classified as lower than 2 by Transparency International's Corruption Perceptions Index • Investments in countries classified 2-4 by Transparency International's Corruption Perceptions Index *and* – in sectors which involve large contracts, including with public sector entities or the government, such as: – construction; – public works contracts; – real estate and property development; – oil and gas; or – mining; – companies with significant state ownership interests; – privatisations; and / or – investments which involve politically exposed persons (PEPs).
Category B Medium risk	A proposed investment is classified as Category B if the risks for corruption or other issues related to business integrity are less than for Category A investments but nevertheless a concern.	• Investments in countries classified as 2-4 by Transparency International's Corruption Perceptions Index in industries where corruption may be common, such as: – heavy manufacturing; – pharmaceuticals and medical care; – utilities; – power generation and transmission; – telecommunications and equipment; – transportation and storage; – hotels, restaurants and leisure; and – forestry. • Investments in countries classified as 4-7 by Transparency International's Corruption Perceptions Index and within the sectors and with the characteristics listed in Category A above, for countries classified as 2-4.
Category C Low risk	A proposed investment is classified as Category C if it is likely to have low risks for corruption or other issues related to business integrity.	• Investments in countries classified as higher than 7 by Transparency International's Corruption Perceptions Index • Investments in countries classified as 2-7 by Transparency International's Corruption Perceptions Index in industries that are usually not prone to corruption, such as: – information technology; and – agriculture.

For investments in countries classified as 2-7 by Transparency International's Corruption Perceptions Index in industries other than those listed above, fund managers should use their judgement when assigning a business integrity risk rating. More guidance on business integrity risks in different countries and industries, and potential measures to counter corruption, can be found on Transparency International's website www.transparency.org

[1] Source: Transparency International Bribery Payers Survey 2008

5

Tool 5

Rating ESG risks: Governance

Business integrity risks can be mitigated by company zero-tolerance bribery policies and anti-corruption programmes, coupled with appropriate monitoring. See CDC's business integrity compliance programme and policies, p. 14-18.

Good corporate governance reduces risks overall, in particular from the business integrity perspective. The matrix below illustrates how to rate corporate governance risks, based on whether a company has established minimum elements of good corporate governance. Risks can be reduced through improvements in corporate governance, firstly by implementing all minimum elements of good corporate governance and then by moving from the minimum elements of good corporate governance to good practice towards best practice as illustrated in *Tool 1* and as appropriate for the size of the company.

Rating risks: Corporate governance

Risk category	Description of category	Minimum elements of corporate governance[1]
Category A High risk	A proposed investment is classified as Category A if the company **does not** have the minimum elements of good corporate governance.	• Basic formalities of corporate governance are in place, including: – a board of directors which meets regularly; – records of shareholders; and – annual shareholders' meetings. • A board of directors is constituted, meets regularly and deliberates independently of executive management. • Adequate internal controls and risk management systems are in place and periodically reviewed by independent external auditors[2]. • Adequate accounting and auditing systems, including: – quarterly financial reports approved by the board; and – annual financial statements audited by recognised firm. • Annual shareholders' meetings. All shareholders are provided with all material information and a detailed agenda in advance of meetings.
Category B Medium risk	A proposed investment is classified as Category B if the company **only has some** of the minimum elements of good corporate governance.	
Category C Low risk	A proposed investment is classified as Category C if the company has the minimum elements of good corporate governance.	

[1] See *Tool 1* for an illustration of elements of good corporate governance.

[2] Such a review is normally performed by certified auditors as part of their regular annual audit of a company.

Tool 5

Rating ESG risks: Combining risk ratings

Combining the risk ratings for governance: business integrity and corporate governance

Combining the business integrity risk rating with the risk rating from the corporate governance perspective gives the fund manager a complete understanding of governance risks for a potential investee company. This is illustrated by the combined risk rating matrix for governance, below.

Risk rating for corporate governance

<table>
<tr><th colspan="3">Rating risks: Corporate governance</th></tr>
<tr><th>Risk category</th><th>Description of category</th><th>Minimum elements of corporate governance[1]</th></tr>
<tr><td>Category A
High risk</td><td>A proposed investment is classified as Category A if the company does not have the minimum elements of good corporate governance.</td><td rowspan="3">• Basic formalities of corporate governance are in place, including:
– a board of directors which meets regularly;
– records of shareholders; and
– annual shareholders meetings.
• A board of directors is constituted, meets regularly and deliberates independently of executive management.
• Adequate internal controls and risk management systems are in place and periodically reviewed by independent external auditors[2].
• Adequate accounting and auditing systems, including:
– quarterly financial reports approved by the board; and
– annual financial statements audited by recognised firm.
• Annual shareholders' meetings. Shareholders provided with all material information and a detailed agenda in advance.</td></tr>
<tr><td>Category B
Medium risk</td><td>A proposed investment is classified as Category B if the company only has some of the minimum elements of good corporate governance.</td></tr>
<tr><td>Category C
Low risk</td><td>A proposed investment is classified as Category C if the company has the minimum elements of good corporate governance.</td></tr>
</table>

Risk rating for business integrity

<table>
<tr><th colspan="3">Rating risks: Business integrity</th></tr>
<tr><th>Risk category</th><th>Description of category</th><th>Guidance</th></tr>
<tr><td>Category A
High risk</td><td>A proposed investment is classified as Category A if it is likely to have significant risks for corruption or other issues related to business integrity.</td><td>• Investments in countries classified as lower than 2 by Transparency International's Corruption Perceptions Index
• Investments in countries classified 2-4 by Transparency International's Corruption Perceptions Index and
– in sectors which involve large contracts, including with public sector entities or the government, such as:
– construction;
– public works contracts;
– real estate and property development;
– oil and gas; or
– mining;
– companies with significant state ownership interests;
– privatisations; and/or
– investments which involve politically exposed persons (PEPs).</td></tr>
<tr><td>Category B
Medium risk</td><td>A proposed investment is classified as Category B if the risks for corruption or other issues related to business integrity are less than for Category A investments but nevertheless a concern.</td><td>• Investments in countries classified as 2-4 by Transparency International's Corruption Perceptions Index in industries where corruption may be common, such as:
– heavy manufacturing;
– pharmaceutical and medical care;
– utilities;
– power generation and transmission;
– forestry;
– telecommunications and equipment; and
– transportation and storage.
• Investments in countries classified as 4-7 by Transparency International's Corruption Perceptions Index and within the sectors and with the characteristics listed in Category A above, for countries classified as 2-4.</td></tr>
<tr><td>Category C
Low risk</td><td>A proposed investment is classified as Category C if it is likely to have low risks for corruption or other issues related to business integrity.</td><td>• Investments in countries classified as higher than 7 by Transparency International's Corruption Perceptions Index
• Investments in countries classified as 2-4 by Transparency International's Corruption Perceptions Index in industries that are usually not prone to corruption, such as:
– information technology; and
– agriculture.</td></tr>
</table>

Combine the risk ratings for governance: business integrity and corporate governance

Corporate Governance / Business Integrity	Category A High risk	Category B Medium risk	Category C Low risk
Category A High risk			
Category B Medium risk			
Category C Low risk			

Using the ESG risk ratings

A fund manager should use the risk ratings for a potential investee company from the ESG perspectives to determine the extent of due diligence required (see *Tool 6* and *Appendices 1-2*), whether to involve the help of specialists and whether to conduct an environmental and social impact assessment (see *Tool 7*) and / or an extended business integrity review (see p. 14-18). If a high risk investment proceeds, the fund manager would need to pay adequate attention to the ESG risks during the investment duration.

ESG risk ratings
Category A-C
High / medium / low

6

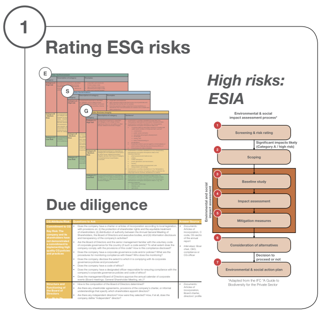
Tool 6

ESG due diligence

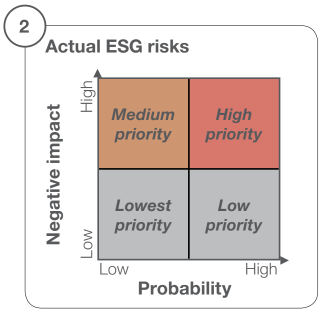
As part of its commercial due diligence, a fund manager should also pay careful attention to assess key ESG matters for a potential investee company. A mapping of opportunities for ESG improvements (see *Tool 1*) and rating ESG risks (see *Tool 5*) serve important functions in determining the depth of the required due diligence, and whether to involve specialist technical experts. For investments in sectors with significant environmental or social risks, the fund manager should normally use specialists to conduct an environmental and social impact assessment (see *Tool 7*).

The due diligence should always assess whether a potential investee company is in compliance with all relevant laws and regulations. For potential investments that involve significant risks, the IFC Performance Standards and the associated Environmental, Health and Safety (EHS) Guidelines (see *Appendix 5*) should be used as the reference standard, even where local laws fall short of these standards. The IFC's industry specific EHS Guidelines provide practical and concrete guidance to benchmark a company's environmental and health and safety performance, and to identify areas for improvements.

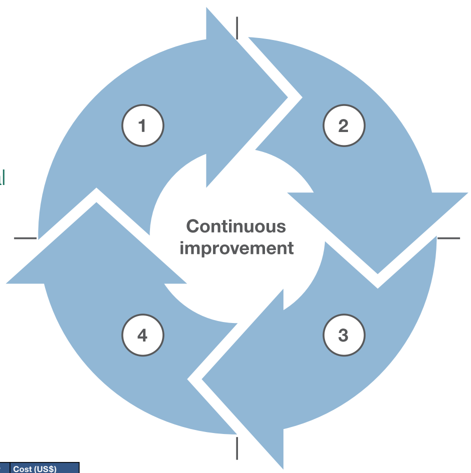
The due diligence should include a review of information in the public domain to check for any environmental, social, business integrity or legal controversy related to the potential investment. Due diligence should involve interviews with company management, employees, board members, shareholders and other stakeholders; reviews of relevant records and disclosures; and site visits, especially where there may be significant risks.



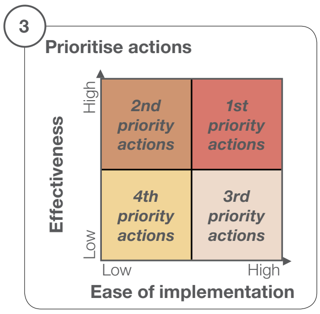
1. Identify key issues that have to be addressed: rate ESG risks (*Tool 5*); perform due diligence (*Tool 6* and *Appendices 1-2*); if significant risks, conduct an environmental and social impact assessment (*Tool 7*).



2. Rank the identified ESG issues in order of priority based on the severity and likelihood of occurrence of any potential negative impact. Prioritise mitigation measures based on a) severe negative impact and b) its probability to occur.



3. For the high priority ESG issues, identify all possible corrective actions and map them against their ease of implementation (costs etc) and likely effectiveness.



4. Formulate an action plan detailing areas of ESG concern with the risk levels, actions required, time-frame, proposed responsibilities and costs involved (*Tool 9*).

4 Action plan for ESG improvements

Area of ESG concern as identified through DD or management systems questions or through environmental and social impact assessments	Level of ESG risk (H, M or L)	Action required	By when	Responsibility (company staff, management and board member)	Cost (US$)
X					
Y					
Z					

Tool 6

ESG due diligence

The fund manager's initial due diligence determines whether a more detailed or formal investigation is warranted. Fund managers may need to develop a network of trusted specialist consultants on ESG matters in the same way as they have a network of legal, accounting and tax advisors.

Where the due diligence uncovers inadequate standards, systems and / or processes for a potential investee company, the fund manager and the management of the potential investee company, assisted by specialists as appropriate, should identify appropriate mitigating measures. In developing an action plan for improvements during the investment duration, the focus should be on addressing the most important areas of risk, and start with the highest priority risks that can be implemented swiftly.

The illustration on the left shows how the ESG risk rating, due diligence and, where there are significant risks, an environmental and social impact assessment, should provide the basis for an action plan with mitigation measures that address areas of concern.

The due diligence review can usefully be repeated as appropriate for continuous improvements during the investment duration.

ESG due diligence questions should be asked in the areas listed below. *Appendix 1* provides the actual due diligence questions for each of these areas, in a template that fund managers can use to conduct their ESG due diligence.

Appendix 2 complements the general due diligence questions with guidance on ESG risks and opportunities for different industries. *Appendix 3* describes key risks for certain regions and countries. For different types of funds (SME, microfinance and debt) see *Appendix 4. Appendix 5* provides guidance to useful international reference standards. For special considerations from the climate change and gender perspectives, see *Appendices 9* and *10*.

General questions:

- Compliance with all relevant laws, standards and regulations?
- Local law enforcement situation?
- Record keeping?
- Permits and licences: obtained and up-to-date?
- Risk management processes?
- Environmental, social and business integrity track-record?
- Certifications obtained (e.g. ISO 14001; OHSAS)? See *Appendix 5*.
- For investments with significant risks: compliance with the IFC Performance Standards and Environmental, Health and Safety Guidelines? See *Appendix 5*.
- Adherence to other relevant international standards? See *Appendix 5.*
- Supply chain practices?

The Environment

- Effluents?
- Emissions?
- Water pollution?
- Air pollution?
- Energy use?
- Natural resource use?
- Water use?
- Waste management?
- Land clearance?
- Sensitive forests or other habitats? See *Appendix 2*.
- Biodiversity loss?
- Climate change: risks and opportunities? See *Appendix 9.*
- Other environmental impacts?

Social matters

Labour and working conditions

- Local adherence to the Fundamental ILO Conventions? See *Appendix 5*.
- Local minimum working age in line with ILO Conventions 138 and 182? See *Appendix 5*. Company compliance?
- Local minimum wage levels? Company compliance?
- Discrimination? See *Appendices 5* and *10*.
- Representation and unions?
- Vulnerable labour?

Tool 6

ESG due diligence

Health and safety

- Types and level of health and safety risks?
- Protective measures, procedures and equipment?
- Safety record?
- Training?

Other social matters

- Impacts on local communities?
- Any particular local social issues?
- Community / NGO consultations?
- Relocations?
- Resettlement?
- Sensitive cultural heritage issues?
- Risk of adverse impacts for indigenous peoples?
- For remote operations: impact of company' activities on local communities? Use of non-local labour? Accommodation and other living conditions for workers and their families?
- Retrenchments?
- Corporate use of security force?

Governance: business integrity and corporate governance

Business Integrity

- Transparency International's Country Corruption Perception Ranking? See *Tool 5* and *Appendix 5*.
- Prevalence of bribery in industry sector?
- Criminal convictions?
- Code of conduct?
- Anti-bribery training for employees?
- Anti-money laundering (AML) and know-your-customer (KYC) training and procedures?
- Accounting and legal compliance?
- Political affiliations or contributions?
- Media references to illegal or disreputable activities?
- Undisclosed or unusual beneficial ownership or carried interests?
- Sudden or unexplained change of investors, shareholders, auditors, accountants, lawyers or other professional advisors?
- Tax evasion?
- Suspicious use of tax havens, off-shore companies, compensation, sources of wealth, lifestyles, fees, local costs or transfer pricing?
- Large or serious law suits?
- Reluctance to discuss business integrity issues?

Corporate governance

- Commitment to good corporate governance?
- Structured and functioning board?
- Adequate control and risk management?
- Adequate transparency and disclosure?
- Rights of minority shareholders and treatment of stakeholders?

The matrix opposite provides guidance to the types of ESG risks and opportunities for improvements that are the most prevalent in different industry sectors. See *Appendix 2* for detailed guidance. Further information on specific industry sectors can be found in the IFC EHS Guidelines, as described briefly in *Appendix 5* of this Toolkit.

Tool 6

ESG due diligence

6

ESG due diligence

Appendix 2 **provides guidance on key ESG risks and opportunities for specific industries**

ESG aspect	Issue	Relevant issues / Activity	Construction	Food	Fishery	Retail	Tourism	Telecommunications	Mining	Pharmaceuticals	Healthcare	Manufacturing	Painting and printing	Garments production	Agriculture	Forestry	Infrastructure	Energy and utilities
Environment	Waste management	Paper / plastics general disposal	0	#	0	#	0	0	0	0	0	0	#	0	0	0	0	0
		Industry / chemical waste disposal	0	0				0	#	0	0	#	#	0	0	0	#	0
		Organic waste contamination		#	0	0				0	0				#			
	Effluents	Effluent monitoring and control	#	0		0			#	0	0	0	#		0		#	0
	Emissions	Toxic materials emissions	0	0					#	0	#	0	#		0		0	
		Dust	#						#			0	0		0	0	#	0
	Water pollution	Unsafe / contaminated water	0	0					#	0	0	#	0		0		#	0
	Energy use	Fossil fuels usage	0					0	0			0			0		#	#
	Water use	Threat of water shortages	0	#			0		#	0	0	#	0		#	0	0	0
	Natural resources use	Deforestation	0				0	0	#						#	#	#	0
		Fish decline		0	#													
		Land erosion	0					0	#						#	#	#	0
	Climate change	Carbon-intensive industry	0	0					#			0			0		#	#
		Greenhouse gas emissions	0						#			#			0		#	#
	Biodiversity	Loss of habitat	0		#		0		#						#	#	#	0
Social matters	Labour and working conditions	Forced or child labour	#						#			0		#	#	0	0	
		Minimum wages	#	0	0	0	0		#			#		#	#	#	#	0
		Discrimination in the workplace	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
		Lack of work-place representation associations	#	0	0	0	0	0	0	0	0	0	0	0	#	#	#	0
	Health and safety	Work safety risks	#	0	0		0	0	#	0	0	#	0		0	0	#	0
		Unsafe pesticides use and storage													#	#		
		Unsafe chemicals use and storage	0	0					0	#	#	#	#		#	0	#	0
		Poor sanitation / living conditions	#						#			0		0	#	0	#	0
	Other social matters	Risks to cultural heritage or indigenous peoples or non-local labour	#					0	#						#	#	#	0
Governance	Business integrity	Risks related to business integrity (e.g. transparency, bribery, money-laundering etc)	#		0	0	0	0	#	0	0	0	0		0	0	#	#
	Corporate governance	Risks of poor corporate governance (e.g. board construction, political connections, shareholder rights)	0	0	0	0	0	0	#	0	0	0	0	0	0	0	0	0

most significant risk

0 risk

Source: *IFC Activity Assessment Tool*, adapted by CDC and Rosencrantz and Co.

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Tool 7

Environmental and social impact assessments

An environmental and social impact assessment is a formal, in-depth study by technical specialists to consider thoroughly the potential and actual negative impacts of a new or expanded business operation on the environment and local communities, and how any negative impacts can be mitigated. As a general rule, environmental and social impact assessments should be commissioned by a company before initiating a new or expanded high risk business operation and by a fund manager before making an investment in assets that involve significant risks (i.e. ranked as high-risk from an environmental and / or social perspective as per *Tool 5*).

CDC's Investment Code, see p. 9-13, specifically requires environmental and social impact assessments to be carried out when business activities could involve:

Environmental impacts:

- loss of biodiversity or habitat;
- emission of significant quantities of greenhouse gases;
- severe degradation of water or air quality;
- substantial solid waste; and
- other significant negative environmental impacts.

Social impacts:

- resettlement;
- critical cultural heritage;
- indigenous peoples;
- non-local labour; and
- other issues where the negative social impact could be significant.

The environmental and social impact assessment should focus on the potential and actual impacts that are deemed to be significant from an initial scoping. A first point of reference is always compliance with local laws, standards and regulations. Where local laws and / or local law enforcement fall short of the IFC's Performance Standards (see *Appendix 5*), the IFC Performance Standards should serve as the reference benchmark for the impact assessment. The IFC's industry specific Environmental, Health and Safety Guidelines are also helpful as concrete reference standards for the impact assessment, with possible mitigating measures for any issues (see *Appendix 5*).

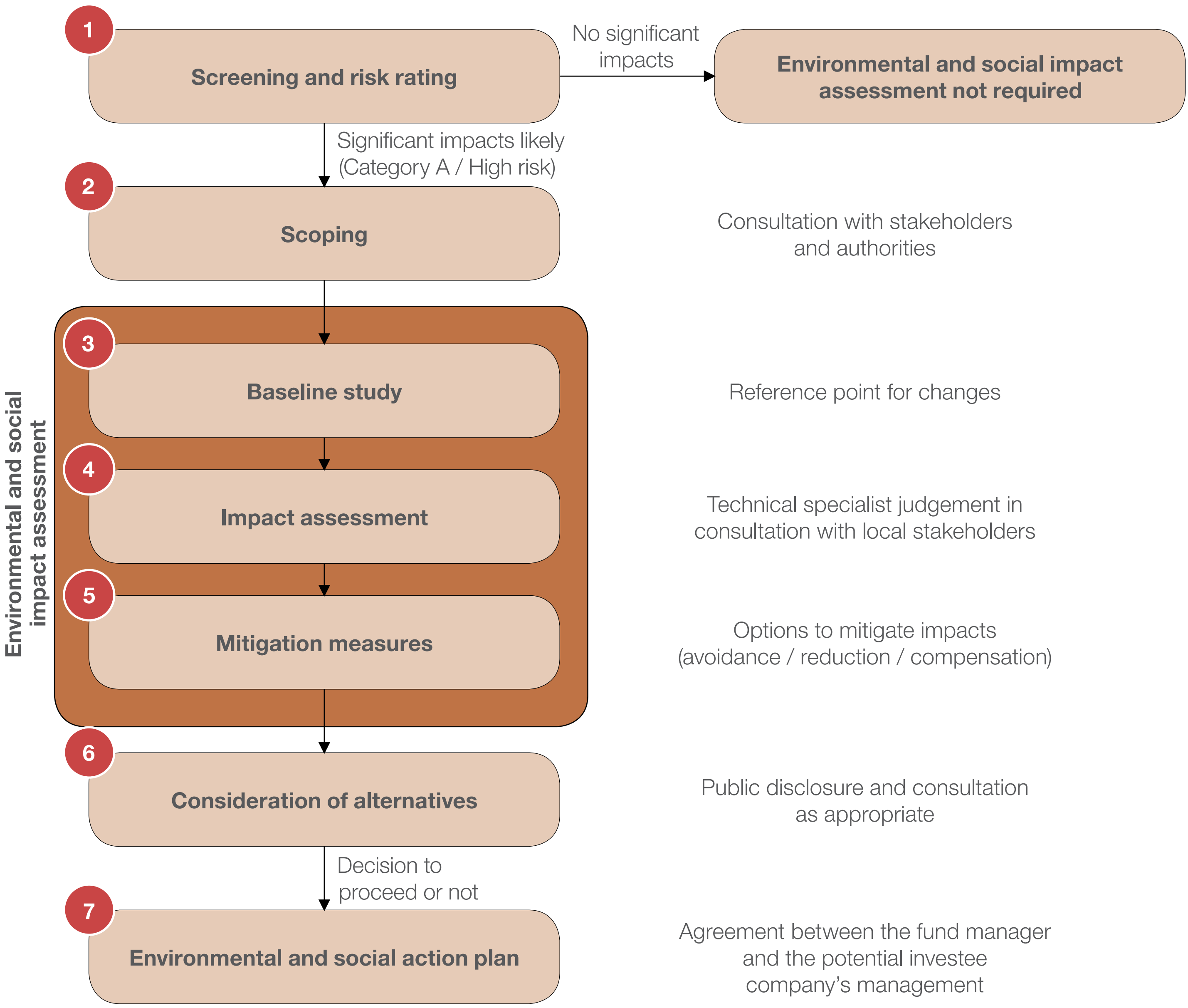
A baseline study is particularly useful for green-field operations as a reference for impacts associated with future operations. Consultation with local communities and authorities is of key importance during the impact assessment. Once the actual and potential impacts are fully understood, it is necessary to judge whether they are acceptable, require mitigation or are unacceptable. Appropriate mitigation measures should then be identified, with cost estimates, and compared.

The fund manager should use the environmental and social impact assessment as a basis for discussions with the management of the potential investee company to reach a clear agreement on expected actions during the investment duration, based on the identified mitigation measures. These measures should be specified in an action plan, which should be agreed upon as part of the investment agreement (see *Tools 9* and *10*).

Tool 7

Environmental and social impact assessments

Environmental and social impact assessment[1]



[1] Adapted from the *IFC A Guide to Biodiversity for the Private Sector* by CDC and Rosencrantz & Co.

Tool 8

Questions to assess a company's ESG management systems

The management systems of companies should be proportional to the level of ESG risks that their operations involve (see *Tool 5*). The questions provided opposite can be used to help a fund manager assess the quality of a potential investee company's management systems to integrate ESG matters into its operations in a systematic manner.

Using the answers to these questions, the fund manager can decide whether the current ESG management systems of a potential investee company merit a good, moderate or poor rating.

Many companies, most particularly small and medium-sized enterprises (SMEs), may not have sophisticated ESG management systems. If they are not operating in a high risk sector, they may not need to. It is nevertheless useful for a fund manager to obtain a sense of the ESG management systems of any potential investee company, and the willingness of company management to improve matters by raising these questions.

Where the current ESG management systems of a potential investee company are deemed by a fund manager to be less than good, the fund manager should consider how these management systems could be improved and add such improvements to the action plan to be discussed and agreed with the company's management (see *Tool 9*).

Case 7: Effective management of ESG risks and opportunities: Compagnie Hévéicole de Cavally, Côte d'Ivoire

In 1996, CDC invested in Compagnie Hévéicole de Cavally, a company with 2,000 hectares of rubber plantation located in the Moyen Cavally region of Côte d'Ivoire. Investing in expansion of a rubber plantation in a post-conflict country had high risks as well as exciting opportunities from the ESG perspectives, and required careful management. At exit in 2007, Compagnie Hévéicole de Cavally employed over 1,020 permanent staff and 300 contractors. 600 further people gained their livelihood through Cavally's smallholder programme. These jobs have been important for stabilising the surrounding communities after the country's destructive civil war.

Over CDC's eleven year investment period, Compagnie Hévéicole de Cavally developed into one of the most productive rubber plantations in West Africa and launched a premium export product. In 2006, the company produced 14,000 tonnes of rubber for export to customers such as Michelin and Goodyear, generating US$20m in export revenues. These foreign currency earnings provided much needed hard currency for the Ivorian economy. The Cavally plantation was sold by CDC's fund manager Actis to a well-established tropical plantation business. The sale received a 2.5 times investment cost exit multiple and an IRR of 11%.

Tool 8

Questions to assess a company's ESG management systems

Policy and processes	Yes	No	Comments
1. **Policy:** Are there formal policies and systems to manage ESG?	☐	☐	________
2. **Identifying opportunities:** Does the company pro-actively identify opportunities for ESG improvements?	☐	☐	________
3. **Risks:** Does the company provide an appropriate risk assessment for its operations which can be used as a basis for on-going monitoring?	☐	☐	________
4. **Action plans:** Are formal action plans drawn up to address ESG issues?	☐	☐	________
5. **Monitoring:** Are there defined processes in place to manage / monitor ESG matters and the implementation of action plans?	☐	☐	________
6. **Sector initiatives (if applicable):** Is the company involved in relevant sector initiatives, e.g. the Extractive Industries Transparency Initiative (EITI) for mining?	☐	☐	________

Roles and responsibilities	Yes	No	Comments
7. **ESG resources:** Does the company have an allocated ESG professional on staff?	☐	☐	________
8. **Top level responsibility:** Has ESG responsibility been established at all levels up to the company's board?	☐	☐	________
9. **Specialists:** Are specialist consultants / external technical experts used to assess and monitor ESG issues (particularly for high risk companies)? If so, when and who?	☐	☐	________
10. **Training:** Does the company organise training for its staff on ESG?	☐	☐	________

ESG performance management	Yes	No	Comments
11. **Performance indicators:** Are there key performance indicators in place to measure and track ESG performance?	☐	☐	________
12. **Track record:** Does the company have a good safety record? Have there been accidents? Were issues subsequently addressed?	☐	☐	________
13. **Serious incidents:** Is there an established procedure to follow up any serious incidents to prevent their reoccurrence?	☐	☐	________

Reporting	Yes	No	Comments
14. **Communication lines:** Are there defined lines of communication in place to report ESG issues to the company's management and board?	☐	☐	________
15. **Reporting to investors:** Is ESG performance reported on to investors at least annually?	☐	☐	________

Stakeholder management	Yes	No	Comments
16. **Local community:** Does the company have a good relationship with the local community?	☐	☐	________
17. **NGOs:** Does the company have a constructive dialogue with NGOs (where NGOs are interested in engagement)?	☐	☐	________
18. **Employees:** Does the company have good labour relations (e.g. have there been strikes)?	☐	☐	________

Tool 9

Investment paper and action plan for ESG improvements

9

Investment paper

The investment paper's standard business assessment can be augmented by an integrated ESG analysis, using *Tool 1* to identify key ESG drivers for the business success. It could, for example, highlight how improved ESG practices could provide access to a wider range of customers in new markets and how future ESG trends may affect supply or demand for the goods or services provided by the potential investee company.

The investment paper should include the conclusions derived from the ESG risk rating (*Tool 5*), due diligence questions (*Tool 6* and *Appendices 1-2*), including an environmental and social impact assessment for high risk investments (*Tool 7*), and an assessment of the potential investee company's ESG management systems (*Tool 8*) and clearly articulate whether the proposed investment complies with the fund manager's ESG standards or whether improvements are required over the investment period.

Furthermore, the investment paper should outline the potential reputational risks to the fund manager (and its investors) of investing in a company which has certain ESG issues.

Consideration of key positive and / or negative ESG matters for a proposed investment in the investment paper fulfils several functions:

- ensures that opportunities to add value to a business from the ESG perspectives are understood and captured;
- ensures that key ESG risks are factored into the decision on whether to invest and at what price; and
- highlights actions to bring about ESG improvements which may need to be taken during the investment period and the timeframe and costs involved.

Case 8: ESG management for a high-risk investment: Banro Corporation, DR Congo

Banro is a gold exploration company focused on exploring and developing mining rights in the gold belt of eastern DR Congo assisted by an investment from CDC's fund manager Actis. Mining operations in DR Congo are high risk from all ESG perspectives. During its start-up phase, Banro had to pay thorough attention to minimise adverse environmental and social impacts. Having conducted an environmental and social impact assessment, Banro implemented a resettlement action plan for the local community that lived on the site to be mined. The resettlement action plan, drawn up according to IFC standards, included 150% compensation for all property lost and relocation assistance for everyone affected.

For all of its operations, Banro aims to be a model for corporate and social responsibility by showing a long-term commitment to the local communities where it operates. Although Banro's mining operations are not yet revenue generating, the company has set up the Banro Foundation to help local communities improve their economic situation. The Banro Foundation spent US$0.8m in 2008 on projects to benefit local communities including schools, a clinic and a water distribution system. The Banro Foundation has created panels of community members that decide, at a local level, which projects to be financed.

Investment paper and action plan for ESG improvements

Action plan for ESG improvements

Where the fund manager has concerns about certain ESG issues, identified through the due diligence questions posed to the potential investee company and, for high risk investments, through an environmental and social impact assessment, an action plan for improvements during the investment duration should be prepared in collaboration with the management of the potential investee company and included in the investment paper.

Depending on the risks involved, specialist help may be needed to ensure that the mitigating actions, timeframe and costs are appropriate. The action plan should be prepared together with the management of the potential investee company and agreed upon as part of the legal investment agreement. Appropriate funding should be set aside to ensure proper implementation during the investment period.

Where the potential investee company does not accept the need for actions for improvements of the kind identified, or over the suggested timeframe, the fund manager needs to have discussions with the company managers to understand whether interests can be aligned. If not, the fund manager may decide not to proceed with the investment.

In case the fund manager has little or no influence over a potential investee company, this should be highlighted to the fund manager's investment committee in the investment paper, and the option to invest or not considered carefully (including not to pursue the investment opportunity where risks are high).

Action plan template

Area of ESG concern as identified through due diligence and management systems questions	Level of ESG risk (high, medium or low)	Action required	By when	Responsibility (company staff, management and board member)	Cost (US$)
X					
Y					
Z					

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Tool 10

Investment agreement

Clauses should be included in legal investment agreements to ensure that each portfolio company is fully committed to incorporate good ESG practices into its activities. CDC's fund managers are typically required to obtain written investment undertakings from their portfolio companies in line with CDC's Investment Code where a fund manager has effective control or significant influence over a portfolio company.[1] (See sections 1.1-1.3 of CDC's Investment Code, p. 9-13.) For a suggested template for a portfolio company investment undertaking, see below.

If a fund manager proposes an alternative text for the written investment undertakings for their portfolio companies, CDC may agree to such alternative text. This would typically be the case for funds with other development finance institutions (DFIs) as investors. As a general rule, CDC will normally agree to language approved by other DFIs. See *Appendix 8* for guidance on standards and procedures from different DFIs.

[Letterhead of Portfolio Company]

[Date]

[Fund]

[Fund Address]

Subscription of Shares by [Fund] – Undertaking by [Portfolio Company] ('Company') to comply with [CDC's Investment Code] [the Fund's Investment Code][2]

Dear Sirs,

We refer to your agreement to subscribe for shares in the Company set forth in that certain Subscription Agreement dated [date]. We acknowledge that a condition precedent to your obligation to complete and fund your subscription of shares is that we deliver to you a signed undertaking regarding [CDC's Investment Code] [the Fund's Investment Code].

Therefore, by this letter we undertake at all times until [the Fund] ceases to be a shareholder of the Company to operate our business in line with [Sections 1 - 3 of CDC's Investment Code] [Sections ____ of the Fund's Investment Code] which is set forth in the attachment to this letter.

We further agree that you may send a copy of this undertaking to CDC.

Yours sincerely,

[Portfolio Company]

By: ___________________________

Name: _______________________

Title: ________________________

Attachment

[Attach CDC's Investment Code or the Fund's Investment Code, as relevant.]

[1] A fund manager is deemed to have significant influence over a portfolio company where its fund has (i) an ownership interest in the portfolio company in excess of 20%, which is presumed to be a level that allows for participation in the financial and operating policies of a portfolio company (if the percentage is lower but gives rise to the same participation, this will also meet the definition of significant influence); or (ii) board representation to a level that allows for participation in determining the financial and operating policies of the portfolio company; or (iii) rights to influence the financial and operating policy decisions of the portfolio company pursuant to a shareholders' or similar agreement.

[2] The Fund's Investment Code must be identical to or substantially similar to CDC's Investment Code.

Investment agreement

Case 9: Business opportunities from cleaner technologies: Duoyuan Global Water, China

CDC is invested in Duoyuan Global Water through its fund manager Global Environment Fund (GEF). Duoyuan Global Water is one of China's leading water treatment equipment suppliers, offering more than 80 products including water treatment, water purification and waste-water treatment. Duoyuan Global Water is working towards solutions for China's challenges in maintaining its water supply and improving its water quality. GEF has worked with Duoyuan Global Water to improve health and safety practices. An environmental action plan was agreed to and documented when GEF invested.

Duoyuan was listed on the New York stock exchange in June 2009. The initial public offering (IPO) was over-subscribed; evidence of strong investor appetite for well-run emerging market companies with strong management, sound environmental and social practices and clear earnings growth potential. By year-end, Duoyuan's stock traded at a significant premium to the IPO price. In January 2010, Duoyuan raised an additional US$76.8m through a follow-on public offering to finance the expansion of its manufacturing facilities and thereby increase in-house production of key components.

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Tool 11

Investment monitoring

Fund managers must ensure that ESG matters are not only considered during the due diligence and investment decision phase but also that they monitor, record and manage all important ESG aspects once an investment has been made. Active monitoring is key to reduce risks and realise opportunities to add value to investments through continuous improvements. During the investment period, the fund manager should monitor its investment from an ESG perspective:

- to check the company's on-going compliance with all relevant laws, standards and regulations relating to ESG matters and with the standards stipulated in the fund's ESG policy; for CDC's fund managers the Investment Code, p. 9-13;
- to ensure timely implementation of action plans for ESG improvements;
- to encourage the managers of portfolio companies to work towards continuous improvements;
- to ensure that any new risks, issues or opportunities for improvement that may emerge are dealt with in an appropriate manner;
- to monitor and record serious incidents involving portfolio companies that result in loss of life, serious injury, material effect on the environment, or material breach of law, and promote appropriate corrective actions;
- to record and report key performance indicators to the fund's investment committee, governing body, investors and the general public; and
- to review the company's strategy in the light of changes, e.g. in regulation, markets and technology, over the investment duration.

Investment monitoring would normally be done by the fund manager as described below.

Regular interactive reviews of progress towards ESG action plans should be undertaken between the fund manager's investment executive responsible for a deal and the portfolio company's management. These reviews should cover the planned actions that should have been achieved since the last meeting. Any shortcomings should be discussed and resolved, and adjustments made as necessary to the action plan based on any shortcomings and new opportunities for improvements.

Board membership The fund manager would often appoint the investment executive responsible for a deal to be a non-executive director at the portfolio company's board. Board participation is an effective way for fund managers to gain influence on an on-going basis over portfolio companies and to bring about improvements in corporate governance as illustrated in *Tool 1*.

Site visits should be undertaken on a regular basis to all investments that are rated as high risk from the ESG perspective by the fund manager's investment executive responsible for the deal and, as appropriate, by specialist advisors. Occasional visits to lower risk investments are also appropriate. There may be specific issues that warrant an immediate site visit to a specific investment, notably after the occurrence of a serious incident.

Progress towards ESG action plans and status checks should be carried out during the site visits through interviews with management, employees, contractors and affected communities; through relevant environmental checks; and reviews of company records. Specialist advisors would normally assist the fund manager to carry out ESG status checks to identify any issues and appropriate mitigating actions during site visits to high risk portfolio companies as a follow-up to the environmental and social impact assessments conducted prior to the investment.

Investment monitoring

Record keeping and formal reports should be the responsibility of the portfolio company's management to its board and investors, including on key performance indicators. The fund manager may wish to check on an ad-hoc basis that its portfolio companies keeps all required permits, records, etc up-to-date and in good order. The portfolio companies' management should prepare regular reports, at least on an annual basis, to their boards and investors, which include progress towards action plans, any new issues or opportunities and any changes in ESG risks. The reports should also describe any changes in corporate governance practices or ESG management systems. Any serious issue that may occur should be reported immediately to the company's board and investors, with the results of any investigation and the corrective measures to be introduced in order to prevent any reoccurrence. See *Tool 12* for further guidance on ESG reporting to investors.

Investment reviews by the fund manager's investment committee are normally held quarterly or twice per year. The investment executive responsible for the monitoring of a portfolio company should report regularly to the fund manager's investment committee on that company's progress towards action plans, any issues or new opportunities to add value (to be added to existing action plans) and updated key performance indicators. The investment review is an appropriate forum to discuss new opportunities that may arise from changes in e.g. regulations, markets and technology as well as further improvements in corporate governance and ESG management systems. The investment review is also an appropriate forum to discuss the fund manager's ability to influence the portfolio company and assist with improvements.

Independent verifications It is considered to be best practice to select a sample of deals for annual independent verifications of portfolio companies' adherence to the fund manager's ESG policies and guidelines; for CDC's fund managers the Investment Code. Such independent verifications are performed by specialist consultants and always involve site visits to portfolio companies that are considered to be high risk from the ESG perspectives.

Case 10: Innovative sales expansion through partnership with a NGO for social and commercial benefits: Deacons, Kenya

Deacons is a Kenyan retailer which sells clothing, footwear, accessories and home-wares. Assisted by an investment from CDC's fund manager Aureos, Deacons has expanded exponentially and now has 19 stores across Kenya, Tanzania and Uganda. At the end of 2008, Deacons had 210 permanent staff and 77 contract staff who were all paid at least double the national minimum wage.

Deacons has pioneered an innovative marketing practice by partnering with a breast cancer awareness NGO. By introducing breast cancer screening services alongside the female underwear departments of its retail stores, Deacons raised awareness of breast cancer, and achieved a huge surge in its sales of brassieres. Deacons now has 80% of the Kenyan formal market for female underwear.

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Tool 12

ESG reporting

ESG matters should be reported to the fund's governing body as relevant and as requested by directors. They should feature in board deliberations at the very least once per year.

The fund manager also reports regularly (usually quarterly and annually) to investors. The fund manager should consider whether it would be interesting, useful or a requirement from the fund's investors to learn about the ESG aspects of investments at least on an annual basis.

Development finance institutions (DFIs) such as CDC, the other European DFIs and the IFC require annual ESG reports. There are also growing numbers of private sector investors who want to ensure that their money is being used to generate and grow sustainable businesses and who stress the importance of regular ESG reports. Many pension fund trustees are required by law to disclose whether and to what extent ESG matters are taken into account in their decision-making on investments and who would welcome regular ESG reports from their fund managers. It is highly likely that the demand for ESG reports from fund managers will continue to grow.

Care needs to be taken in designing the reporting format and contents to ensure that the information is presented in an understandable and meaningful way. Reports should be representative and comprehensive for the fund's portfolio companies rather than just show-casing successes. The reports should be sufficiently robust to provide assurances to investors, while sufficiently streamlined to ensure that reporting is not unnecessarily onerous for fund managers.

CDC's reporting requirements from its fund managers are specified on p. 19-20. The information required by CDC is typical of the type of information that investors with an interest in ESG wish to see. The European DFIs try to ask for the same ESG report where they are jointly invested.

ESG and economic data: annual report for [name of fund]

Country[1]	Sector	Rating of ESG risks & opportunities for improvements[2]			Quality of ESG management systems[3]
		Environment	Social matters	Governance	
Reporting period for data	**Employee numbers (full time equivalents)**	**Currency of data**	**Taxes paid[4]**	**Turnover**	**EBITDA**
ESG issues / opportunities for improvements at the time of investment:					
ESG improvements achieved:					
Status / further actions to be undertaken, with timeframe:					
Other information:					

[1] Country or countries of operation.

[2] High, medium or low. See *Tool 5*.

[3] Good, moderate or poor. See *Tool 8*.

[4] Taxes paid for last year as shown in the cash flow statement, not taxes payable in the profit and loss (P&L) statement.

ESG reporting

Fund managers can use CDC's recommended reporting template, left, to report annually to CDC and other investors. The submission includes a brief section with key information for each portfolio company, with more extensive information reported where there have been issues or improvements made. An example of a completed report is provided in *Appendix 7*.

ESG risk ratings for each portfolio company, along with an assessment of the quality of their ESG management systems, provide investors in a fund with insights into the capacity of the fund manager to analyse ESG matters. The assessment of issues and value adding opportunities at the time of investment, or as may subsequently emerge, provide assurances to investors and showcase the initiatives taken by the portfolio companies and the fund manager. The narrative on ESG improvements achieved, along with the description of plans for further actions with timeframe and cost estimates, gives investors in the fund an indication of how / whether the fund manager is resolving any issues and adding value to its investments.

The number of employees, taxes paid, turnover and profitability (EBITDA) data for the portfolio companies provide investors with an estimate of the company's commercial success and broader economic benefits from the business. The fund manager may also wish to add other relevant, interesting and useful information in its annual report, for example if a portfolio company is contributing towards charitable activities, has introduced new technologies or innovations, or has demonstrated successful contributions to expand the availability of goods, services or infrastructure to the benefit of local communities.

Fund managers must immediately report to their governing body and investors any serious incidents involving portfolio companies that result in loss of life, material effect on the environment, or material breach of law. Such serious incidents can have severe reputational implications for the fund manager and its investors. Fund managers must follow-up on serious incidents as a matter of priority to investigate the cause and the need for mitigating actions to avoid reoccurrence.

A report about a serious incident to the fund's governing body and its investors should contain the elements specified below.

- Name of the portfolio company involved.
- Date and amount invested by the fund.
- Date and time of incident.
- Type of incident: environmental issue, fatality, alleged fraud or other.
- Name of person/s involved / injured / deceased, if applicable.
- Narrative and contextual information.
- Whether the incident was work or non-work related.
- Cause of the incident.
- Status of investigation.
- Listing of parties involved in the investigation (witnesses and staff, unions, police, other authorities and other parties).
- Fund manager's view of the incident: degree of severity, possible uncertainties or disputed facts to be investigated.
- Reports received (and outstanding, if any).
- Immediate actions taken by the portfolio company, fund manager and other parties.
- Further actions to prevent reoccurrence of incident.
- Monitoring / reporting arrangements to follow up on the efficacy of the corrective actions taken.
- Results to-date of the corrective actions taken and plans for follow-up actions.

CDC's recommended template for serious incident reporting is provided in *Appendix 7*.

While reporting provides important insights, meeting portfolio company management face-to-face and visits to their business locations are the best way to give investors a proper understanding of ESG issues. Fund managers should organise investor days where such interactions can be realised.

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Tool 13

Information for the public: annual reports and websites

The general public sometimes perceives that private equity fund managers' success arises from structuring investments so that their investors make quick returns with substantial 'carry' payments for the fund managers without regard for the well-being of the underlying portfolio company, its employees and other stakeholders. Public transparency serves to strengthen a fund manager's reputation. In the long term, public disclosure by fund managers of ESG policies and the ESG performance of portfolio companies could also help the private equity industry avoid excessive regulation.

CDC encourages its fund managers and their portfolio companies to be transparent about their businesses to help broaden the public understanding of their activities and how investments in emerging markets promote private sector development and economic growth. CDC also believes that enhanced public transparency and accountability will help attract further investors to the emerging markets of developing countries.

Information for the public is most easily accessed through annual reports and websites. Examples of information that is useful to report to the general public include the elements listed overleaf:

- ESG policies and guidelines of the fund and its portfolio companies;
- examples of improvements made to portfolio companies during the investment period;
- examples of issues encountered;
- examples illustrating the business case for ESG, e.g. cost savings, revenue increases, new investors, licences to operate / IPO, etc;
- any serious incidents and corrective actions undertaken or underway;
- number of employees and taxes paid to local governments to illustrate the broader economic benefits of investments and business activities; and
- case examples illustrating how portfolio companies provide increased access to goods, services, technology or infrastructure for local populations, with comments about any improvements to quality or lower prices.

Reports should provide a balanced and complete picture of the fund manager's investments rather than only show-casing a few success cases.

Tool 13

Information for the public: annual reports and websites

CDC prepares case studies based on its portfolio companies in emerging markets to illustrate the broader benefits of private sector development from successful business activities. This includes greater access for local communities to better quality goods, services, technology and infrastructure, often at lower prices and of better quality as a result of increased competition and new retail outlets. Case studies from the geographic regions of investments and for most industry sectors are included in CDC's annual reports. The first such report to include the development effects of CDC's investments, *Growth for Development*, was published in 2009. A subsequent report was published by CDC in 2010. Additional case studies are published regularly on CDC's website www.cdcgroup.com

Tool 14

ESG considerations at exit

When an investment is exited, it is highly desirable that the sound ESG practices and improvements undertaken in a portfolio company continue under the new management. This is not least important from a reputational perspective for the fund manager and its investors.

While it is not possible to predict the future with absolute certainty and the fund manager can not be expected to be responsible for practices in an exited portfolio company, suitable care should be taken during the exit screening to assess how the new ownership may affect ESG matters. Such an exit review should involve consideration of the impact that the exited portfolio company will have going forward on employees, local communities and the local environment.

For a trade sale to a company or for an exit to another investor, the fund manager is expected to check the reputation and track-record of potential purchasers and to interview them on their intentions in relation to responsible ESG practices.

Checks on real or perceived conflicts of interest and money laundering checks also have to be undertaken as part of the exit review. A key part of this process is to verify, through auditors or specialist advisors, the identity of the person or entity aspiring to make the acquisition and that the funds were not derived from criminal activities. For further guidance, see CDC's business integrity compliance programme and policies, p. 14-18.

Examples of key questions to ask for at exit are provided below.

The potential buyer: What is the ESG track-record of the potential buyer? Any issues with previous or current operations or investments? Adherence to and awareness of relevant local and international ESG standards? Formal policies and ESG management systems? Any concerns about the integrity of the potential buyer? Any legal issues? Money laundering?

Continued ESG practices: Are there any reasons to believe that the potential buyer will change the current ESG practices in the portfolio company? Would the potential buyer commit to continue responsible business practices in line with the fund manager's ESG policies and guidelines; for CDC's fund managers the Investment Code (see p. 9-13 and *Tool 2*)?

Redundancies: Is there a likelihood of significant job cuts after the exit? How has the potential buyer dealt with redundancies in the past?

Media coverage / NGO attention: Are there reasons to believe that the exit will give rise to media coverage or NGO attention? How is the potential buyer perceived by media and NGOs?

Conflicts of interests: Are there any potential or perceived conflicts of interest from the exit?

If the answer to one or more of these questions is yes, the fund manager should consider mitigating measures and manage risks before the exit.

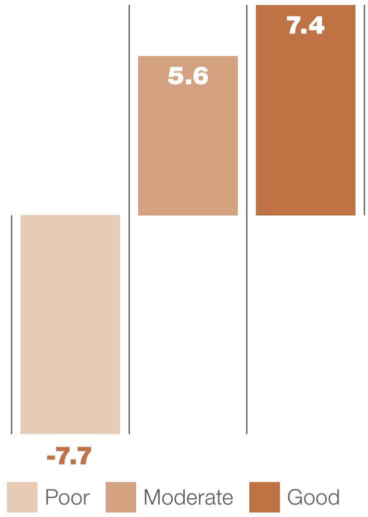
ESG considerations at exit

Case 11: CDC portfolio findings in 2010: Correlation between IRRs and quality of ESG management systems

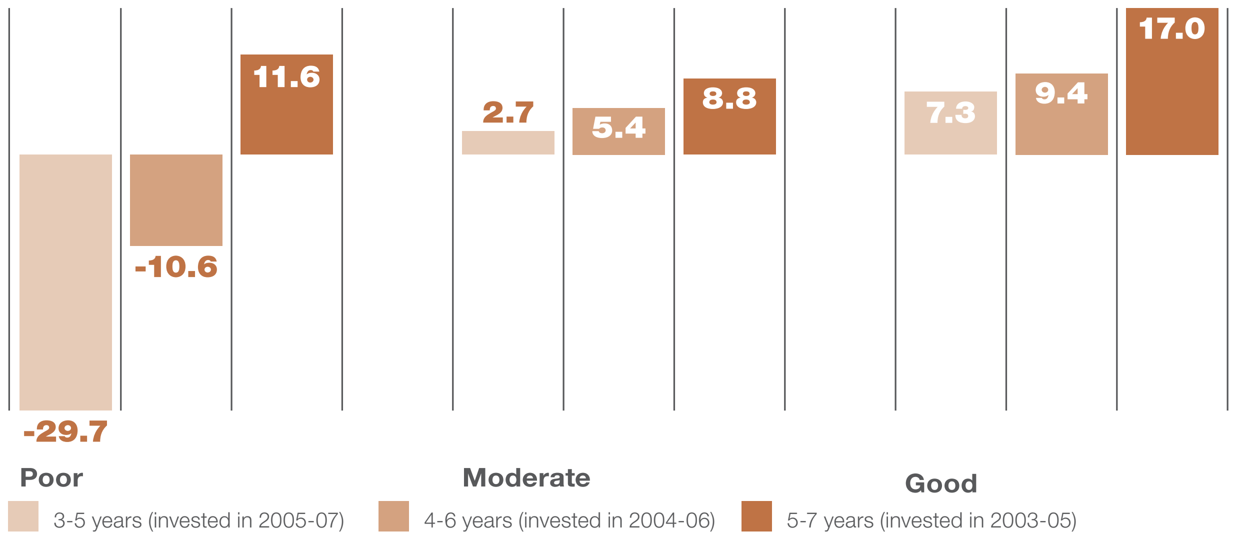
An analysis of CDC's portfolio companies suggests that there is a correlation between companies with higher financial returns and companies with relatively good ESG management systems.[1] The analysis shows that companies with good ESG management systems outperform those with poor systems by 15% in IRR. When controlling for average income levels in different countries, the correlation remains between companies with good and poor ESG management systems, respectively, and the financial returns that they generated. One possible explanation might be that more financially successful companies are better managed. These companies could for example also have rigorous and comprehensive management systems for operational performance, customer relations, staff training and other areas. The attribution to these various aspects of good corporate management systems, including for ESG matters, would require a more comprehensive sample of data and further analysis.

These analyses constitute a first attempt at building a better and more quantitative understanding of the ESG management systems of CDC's portfolio companies and their financial performance. CDC will progress to improve the analysis of the relation between financial performance and good ESG management over the next few years. Priorities for this work include expanding the number of companies in the analysis, increasing the amount of data collected and strengthening the consistency of the quality rating for ESG managerial systems.

Quality of ESG management systems and portfolio company returns (mean IRR, %)



Quality of ESG management systems and portfolio company returns for investments of different vintages (mean IRR, %)



[1] This analysis is based upon 345 companies in which CDC's fund managers invested during the period 2003-07.

Appendices

Toolkit on ESG for fund managers

Contents

Appendices

Appendix 1

ESG due diligence questions
The Environment

The following tables provide due diligence questions that can be asked to assess environmental, social, business integrity and corporate governance aspects of a potential investment.[1] These general questions should be supplemented as relevant with questions specifically related to the ESG risks and opportunities for the industry sector in which the potential investee company operates. See *Appendix 2*. If the company operates in a sector with significant risks, the relevant industry specific IFC Environmental, Health and Safety (EHS) Guidelines should be used as a reference. See *Appendix 5* and www.ifc.org

	Due diligence on environmental matters	**Tick Yes / No**		**Comments / action required**	**Answer source**
Key due diligence areas	**Questions to ask**	**Yes**	**No**		
Compliance with local laws	What are the local environmental laws, standards and regulations of relevance for the company's operations?				*Documents:* Company environmental policies, permits, certifications; environmental sign-offs or audits performed; effluent and emission records; energy and resource consumption records; recycling contracts; waste treatment contracts; environmental impact assessments.
	Are local environmental laws, standards and regulations effectively enforced by the local authorities?				
	Does the company comply with all relevant local environmental laws, standards and regulations?				
	What environmental permits or certifications for the company's operations are required by the local environmental authorities?				
	Has the company obtained all relevant environmental permits and certifications and are they up to date? Request copies as part of the due diligence.				
	Are there any environmental sign-offs, checks or audits required by the local environmental authorities?				
	Has the company successfully complied with all locally required environmental sign-offs, checks and / or audits? Request copies of any relevant records as part of the due diligence.				
International environmental conventions and standards	Are there any international environmental conventions or standards of particular relevance to the operations of the company? Examples include hazardous wastes, ozone depleting substances, herbicides and pesticides, timber, desertification, etc. See *Appendix 5*.				
IFC Performance Standards & industry specific environmental guidelines	Does the company operate in a sector for which the IFC has issued industry specific Environmental, Health and Safety (EHS) Guidelines? See *Appendix 2, 5* and www.ifc.org If so, use the industry specific environmental guidelines as reference for the due diligence.				
Risk management	What processes does the company have to assess the environmental risks arising from its operations?				
	What processes does the company have to ensure that protective measures are put in place and enforced?				

[1] Several of these due diligence questions were inspired by materials from the IFC and Transparency International.

ESG due diligence questions
The Environment

Key due diligence areas	Due diligence on environmental matters – Questions to ask	Tick Yes / No – Yes	No	Comments / action required	Answer source
Environmental track record	Have there been any serious environmental incidents in the last five years?				*Interviews:* CEO, operations and plant managers, workers responsible for effluent and emission monitoring, workers dealing with any hazardous substances and wastes, specialist consultants, local authorities, local community representatives.
	Does the company record all serious environmental incidents and conduct full investigations?				
	Had the company paid charges, fines or penalties for non-compliance with environmental regulations and standards in the last two years? Request to see copies of records as part of the due diligence.				
	Is the company exposed to potentially significant environmental liabilities, such as those arising from land or ground water contamination, related to the company's past or ongoing operations? If yes, specify magnitude.				
	If the company is not materially in compliance with environmental regulations and standards, or if there are potentially significant environmental liabilities, please describe further actions required by the authorities and / or planned by the company to address these issues satisfactory and to achieve regulatory compliance.				
Effluents	Does the company generate waste water or other effluents? What types, qualities and quantities?				
	Are any of the effluents hazardous or toxic? How are these dealt with?				
	Where are effluents released?				
	Are effluents treated before release?				
	Is there an effluent treatment plant?				
	Are effluent quantity and quality monitored regularly and effectively?				
	Are company effluents (quality and quantity) and pollution prevention measures in line with local laws, standards and regulations?				
	Are company effluents and pollution prevention measures in line with IFC industry specific environmental guidelines? (If applicable – see *Appendix 5* for a list of IFC industry specific Environmental, Health and Safety (EHS) guidelines).				
Emissions	Does the company generate air emissions? What types, qualities and quantities?				
	Are any of the emissions hazardous? How are these dealt with?				
	Does the company take measures to reduce emissions?				
	Are emissions quantity and quality monitored regularly and effectively?				
	Are company emissions (quality and quantity) and pollution prevention measures in line with local laws, standards and regulations?				
	Are company emissions and pollution prevention measures in line with IFC industry specific environmental guidelines? (If applicable – see *Appendix 5* for a list of IFC industry specific Environmental, Health and Safety (EHS) guidelines).				

Appendix 1

ESG due diligence questions
The Environment

	Due diligence on environmental matters	Tick Yes / No		Comments / action required	Answer source
Key due diligence areas	**Questions to ask**	**Yes**	**No**		
Resource conservation	Does the company keep records of and monitor its use of energy and other resources?				See p. 63-64
	Could use of energy and / or other resources be reduced with more efficient processes and controls or different technologies?				
Waste management	What wastes does the company generate (types, quantities)?				
	Are any of the wastes hazardous? How are these dealt with?				
	How is the waste managed?				
	Are wastes recycled?				
	Could wastes be reduced? If so, how?				
	Does the company produce a significant amount of packaging which creates substantial solid waste elsewhere?				
Water use	Does the company use large quantities of water?				
	Might water supply for the company be under threat of shortages?				
	Does the company's use of water reduce the supply available to other users?				
International certifications	Does the company have ISO 14000 certification(s), including ISO 14001 for its environmental management systems? See *Appendix 5*.				
	Does the company have any relevant industry specific certifications, e.g. from the Forestry Stewardship Council (FSC) or other relevant industry bodies? See *Appendix 2*.				
	If relevant, does the company qualify for 'organic' certification of its products, which could command a premium price in international markets?				
Land clearance	Do the company's activities involve land clearance?				
	Are any land clearances well managed, including thorough consultations with local authorities and affected communities?				
Biodiversity	Are there any risks for negative impacts on local flora or fauna from the company's operations?				
	Are there any risks for biodiversity loss from the company's operations? See IFC Performance Standard 6, *Appendix 5*.				
	Has the company identified and addressed all biodiversity impacts of its operations if it operates within an industry with significant risks through an environmental impact assessment? See *Tool 7* and *Appendix 2* for industries with risks for biodiversity loss.				
Sensitive forests	Does the company source materials from sensitive forests or use inputs in its production process which could contribute to loss of sensitive forests? See *Appendix 2*.				
Climate change ***See Appendix 9***	Does the company operate in a carbon-intensive industry, e.g. cement, aviation, power generation?				
	Has the company taken measures to reduce greenhouse gas emissions?				
	Could greenhouse gas emissions be reduced further through use of different technologies?				
	Do the company's activities include significant use of transportation? See *Appendix 2*.				

ESG due diligence questions
The Environment

	Due diligence on environmental matters	Tick Yes / No		Comments / action required	Answer source
Key due diligence areas	Questions to ask	Yes	No		
Climate change (continued) ***See Appendix 9***	In what ways could carbon emissions from transportation be reduced?				See p. 63-64
	Can the company certify its reductions in green house gas emissions and thereby augment cash flows under the Clean Development Mechanism?				
Supply chain	Is the company aware of the environmental practices of its sub-contractors and / or of other companies from which it sources significant inputs?				
	Are the environmental practices of sub-contractors and / or of other companies from which the company sources significant inputs as sound as those deployed by the company?				
	If not, can the company influence its major sub-contractors and / or suppliers to improve their environmental practices, potentially by making improved practices a condition for continued business?				

Appendix 1

ESG due diligence questions
Social matters

Key due diligence areas	Due diligence on social matters: labour and working conditions Questions to ask	Tick Yes / No Yes	No	Comments / action required	Answer source
Compliance with local laws	What are the local labour laws, standards and regulations of relevance for the company's operations?				*Documents:* Company human resource policies, including on wages, non-discrimination, representation, grievance mechanism, etc; contracts for different types of employees and seasonal / temporary workers if applicable; other labour records as relevant. *Interviews:* CEO, company managers, human resource manager, workers (of different gender), seniority and pay levels, representatives of minority groups, union representatives.
	Has the country ratified the ILO's Fundamental Conventions and are these reflected in local laws? See *Appendix 5*.				
	Are local labour laws, standards and regulations effectively enforced by the local authorities?				
	Does the company comply with all relevant local labour laws, standards and regulations?				
	What labour records are the company required to keep according to local laws and regulations?				
	Are all of the company's labour records and contracts properly kept and up to date?				
Child labour	Is the company operating in a country or sector where child labour is common? See *Appendix 2, 3* and *5*.				
	What is the local minimum working age?				
	Is the local minimum working age consistent with ILO Conventions 138 and 182? See *Appendix 5*.				
Minimum wage	Does the company adhere to local and / or industry minimum wage standards?				
	Are local minimum wage standards consistent with decent living wages?				
	Is the company operating in a sector where competitive advantage arises from paying low wages? See *Appendix 2*.				
	If so, what systems are in place to ensure that the legal minimum wage is adhered to?				
	Is the company operating in a country where the cost of living has increased substantially (e.g. because of inflation or drought)?				
	If so, have wages kept up with increases in living costs?				
Discrimination	Does the workforce appear to be representative of the local population with respect to gender, race, religion, etc?				
	Are any local customs likely to result in discriminatory practices?				
	What are local norms regarding the employment of women?				
	Does the company have a non-discriminatory policy with respect to gender, race, colour, disability, political opinion, sexual orientation, age, religion, social or ethnic origin, or HIV status?				
	Is such a policy adhered to?				
	Does the company adhere to good gender practices? See *Appendix 10*.				
	Does the company improperly conduct non-confidential or mandatory HIV tests for its workers?				
Representation	What systems does the company have in place to enable workers to present and argue their views to management?				
	Is the workforce unionised?				
	If so, is the union representative of all workers including minority groups?				

ESG due diligence questions
Social matters

	Due diligence on social matters: labour and working conditions	Tick Yes / No		Comments / action required	Answer source
Key due diligence areas	**Questions to ask**	**Yes**	**No**		
Vulnerable labour	Does the company employ migrant labour, non-local workers or other workers which are likely to be particularly vulnerable? If so, how are their interests looked after?				See p. 67
Human resources	Does the company have a human resource policy which informs workers of their rights and conditions of employment?				
	Are workers aware of their rights?				
	Are proper labour contracts in place for all staff, including for temporary and seasonal workers?				
	Does the company have policies in place for overtime, maternity leave, sick leave and disability?				
	Does the company have a grievance mechanism for staff to make formal complaints to human resources?				
Supply chain	Is the company aware of the labour practices of its sub-contractors and / or of other companies from which it sources significant inputs?				
	Are the labour practices of sub-contractors and / or of other companies from which the company sources significant inputs as sound as those deployed by the company?				
	If not, can the company influence its major sub-contractors and / or suppliers to improve their labour practices, potentially by making improved practices a condition for continued business?				

	Due diligence on social matters: health and safety	Tick Yes / No		Comments / action required	Answer source
Key due diligence areas	**Questions to ask**	**Yes**	**No**		
Local laws	What are the local health and safety laws, standards and regulations of relevance for the company's operations?				*Documents:* Health and safety policy; health and safety records; documentation of any accidents; any relevant permits and certifications; records of any health and safety checks or audits performed.
	Are local health and safety laws, standards and regulations effectively enforced by the local authorities?				
	Does the company comply with all relevant local health and safety laws, standards and regulations?				
	What permits or certifications on health and safety are required by the local authorities for the company's operations?				
	Has the company obtained all relevant health and safety permits and certifications? Request copies as part of the due diligence.				
	Are there any health and safety checks or audits required by the local authorities?				
	Has the company successfully complied with any locally required health and safety checks or audits?				

Appendix 1

ESG due diligence questions
Social matters

Key due diligence areas	Due diligence on social matters: health and safety Questions to ask	Tick Yes / No Yes	No	Comments / action required	Answer source
IFC Performance Standards & industry specific health and safety guidelines	Does the company operate in a sector for which the IFC has issued industry specific Environmental, Health and Safety (EHS) Guidelines? See *Appendix 2, 5* and www.ifc.org If so, use the industry specific health and safety guidelines as reference for the due diligence.				*Interviews:* CEO, company management, HR manager, operations and plant managers, workers, especially any worker that has been exposed to a serious health and safety incident, specialist consultants (where relevant), local authorities (where relevant), local community representatives (where relevant).
Risk management	Does the company have an appropriate health and safety policy for the health and safety risks of its operations?				
	What processes does the company have in place to assess the health and safety risks arising from its activities? (e.g. hazardous chemicals, machinery, dust, noise, odours, fumes, vibrations)				
	What processes does the company have to ensure that appropriate protective health and safety measures are put in place?				
	What processes does the company follow to ensure that workers use protective equipment (e.g. hats, goggles, gloves) when dealing with hazards (e.g. handling chemicals, machinery)?				
	Does the company have regular training programmes for all relevant staff on occupational health and safety?				
	Does the company have an emergency plan in place, if relevant including provisions for fires, leakage of hazardous chemicals or explosions?				
	Does the company conduct regular and effective inspections and compliance checks on health and safety?				
Health and safety track-record	Has the company paid charges, fines or penalties for non-compliance with health and safety regulations and standards in the last two years? Request to see copies of records as part of the due diligence.				
	Is the company exposed to potentially significant health and safety liabilities, such as those from ongoing or future claims from negatively affected workers and / or communities, related to the company's past or ongoing operations? If yes, specify magnitude.				
	If the company is not materially in compliance with local health and safety laws, regulations and standards, or if there are potentially significant health and safety liabilities, please describe further actions required by the authorities and / or planned by the company to address these issues satisfactorily and to achieve regulatory compliance.				
	Does the company record accidents and conduct full investigations of any serious incidents?				
	Has there been any accidents in the last five years?				
	What is the company's health and safety record (ask to see the accident record book)?				
	On a tour of the factory or other site of operations (if applicable), keep an eye out for obvious areas of health and safety risks and ask for management's and workers' views. Any issues?				

ESG due diligence questions
Social matters

Due diligence on social matters: health and safety		Tick Yes / No		Comments / action required	Answer source
Key due diligence areas	**Questions to ask**	**Yes**	**No**		
Community health and safety	Are there any health and safety risks for local communities or consumers associated with the company's operations or products?				See p. 68-69
	Are any health and safety risks for local communities or consumers managed in a satisfactory manner? Refer to the IFC Performance Standards and any relevant industry specific health and safety guidelines. See *Appendix 5*.				
International certifications	Does the company have OHSAS certification? See *Appendix 5*.				
Supply chain	Is the company aware of the health and safety practices of its sub-contractors and / or of other companies from which it sources significant inputs?				
	Are the health and safety practices of sub-contractors and / or of other companies from which the company sources significant inputs as sound as those deployed by the company?				
	If not, can the company influence its major sub-contractors and / or suppliers to improve their health and safety practices, potentially by making improved practices a condition for continued business?				

Due diligence on social matters: other social matters		Tick Yes / No		Comments / action required	Answer source
Key due diligence areas	**Questions to ask**	**Yes**	**No**		
Local communities	What impacts may the company's activities have on local communities and other stakeholders?				*Documents:* Company community consultation policy, records of consultations, retrenchment policy, social impact assessments.
	If there could be significant adverse impacts, has the company conducted a social impact assessment and followed up on its findings and recommendations with mitigating measures?				
	Does the company have good relations with the local communities and NGOs?				
	Does the company employ local workers? If not, why not?				
	Do the company's activities have a direct or indirect impact on marginal or vulnerable social groups with identities distinct from the dominant groups on the basis of race, religion, HIV status or other potential basis for discrimination?				
	Does the company contribute to any community development programmes through financial donations or in other ways?				
Consultations	What systems does the company have in place to consult with persons and groups affected by its operations and / or products?				
Adverse effects and mitigation	If there are any adverse effects on local communities or other stakeholders from the company's operations, how are such effects minimised, reduced or compensated for?				

Appendix 1

ESG due diligence questions
Social matters

	Due diligence on social matters: other social matters	Tick Yes / No		Comments / action required	Answer source
Key due diligence areas	**Questions to ask**	**Yes**	**No**		
Relocation	Are persons being moved as a result of the company's new or expanded operations? See IFC Performance Standards, *Appendix 5*.				*Interviews:* CEO, company management, operation and plant managers, workers, representatives from local communities, NGOs, local authorities.
	Even if persons are not being moved, might their livelihoods be affected because of a change in land use as a result of the company's operations?				
	If persons are being moved or otherwise negatively affected as a result of company operations, are they adequately compensated by the company, including through provision of new housing and / or financial compensation?				
Particular social issues	Are there any particular sensitive social issues to consider for the country of company operations, such as a high HIV / AIDS prevalence rate, civil conflict or discrimination against indigenous, religious or other minority groups? See IFC Performance Standard 7, *Appendix 5* if any issues concerning indigenous peoples.				
	If so, does the company have appropriate policies and procedures to address such sensitive social issues?				
Cultural matters	Do the company's operations have an impact on a natural or historical location with a local cultural significance? This is particularly relevant for new or expanded operations. See IFC Performance Standard 8, *Appendix 5*.				
Non-local workers and remote locations	Does the establishment or expansion of the company's operations require the import of non-local labour to the region, either for construction or for longer-term employment?				
	Why is it appropriate or necessary to use non-local labour?				
	What are the company's measures to ensure that non-local labour has no or insignificant negative impact on the local communities? Note the risk of an increase in prostitution as a frequent result of the import of non-local male workers, with subsequent increases in HIV / AIDS prevalence.				
	Have the local communities and NGOs been consulted as relevant?				
	How are non-local workers accommodated? Do they have decent housing conditions and other adequate facilities, including health care and other provisions for remote locations?				
	What are the plans for non-local labour to return to their destination of origin?				
	Are the families of non-local workers also relocated by the company?				
	Are they, in that case, adequately provided for (schools, health centres, family housing, etc).				
Retrenchment	Are substantial job losses expected as a result of this investment or the company's future strategy?				
	What is the company's retrenchment policy (who would be affected by job losses, what compensation is provided, etc)?				
	How has the company dealt with any major retrenchments in the past? Impressions from workers and unions?				
	What has the company done to ensure that any retrenchment is managed fairly?				
Use of security force	Will / does the company employ its own security force?				
	How are company security guards trained?				

ESG due diligence questions
Social matters

Key due diligence areas	Due diligence on social matters: other social matters Questions to ask	Tick Yes / No Yes	No	Comments / action required	Answer source
Use of security force (continued)	Are proper mental health and criminal record checks carried out for all security guards prior to contracting?				See p. 70-71
	What weapon will / do the guards use?				
	Have there been any complaints about the corporate security guards, e.g. for use of force, from local communities?				
	Have there been any accidents and / or fatalities associated with the company's security guards during the last five years?				
Road safety	What is the company's road safety record?				
	Have there been any accidents and / or fatalities in the last five years?				
	What road safety measures does the company follow?				

Appendix 1

ESG due diligence questions

Governance: business integrity

	Due diligence on business integrity matters	Tick Yes / No		Comments / action required	Answer source
Key due diligence areas	**Questions to ask**	**Yes**	**No**		
Country corruption situation	How does the country rank in Transparency International's Corruption Perceptions Index?				*Documents:* Code of ethics, code of conduct, legal records, accounting records, compliance policy, audit statements, relevant legal records. *Interviews:* Board chair, board directors, CEO, company management, CFO, controller, staff members, compliance or risk officer, legal counsel, auditors, specialist consultants.
	How are business integrity issues dealt with locally?				
	Is the financial regulatory system of the country operating in line with high international standards?				
Business integrity of company	Is there a designated person at the company with responsibility for managing compliance issues, ethics and potential conflicts of interest?				
	Any criminal convictions amongst the company management, staff or board members?				
	Has any management person, staff or board member been, or is, under investigation by law enforcement or regulatory authorities?				
	Evidence or suspicion of company management criminal activity: e.g. intimidation, blackmail, etc?				
	Involvement or association with criminals?				
	Involvement or association with money laundering?				
	Does anyone connected with the company appear on any UN list of persons suspected of involvement in terrorist activities or any other relevant national or international blacklists? The response should include the results of enquiries in Complinet, World-Check or other comparable systems. If not accessible or available, this should be noted here.				
Code of conduct	Does the company have a code of conduct for employees prohibiting bribery?				
Anti-bribery	How are employees made aware that the company does not condone bribery?				
	Is there regular anti-bribery training for employees?				
	Does the company operate in a sector where bribery is prevalent? See *Appendix 2*.				
	Does the company have a policy on gifts, entertainment and other potential sources of conflict of interest?				
Anti-money laundering	Does the company have appropriate anti-money-laundering training and procedures in place?				
	Have background searches been performed on beneficial owners and others with a significant relationship to the company?				
Accounting and compliance	Are the accounting records fully up to date and complete?				
	Does the company send regular and complete information to the tax authorities?				
Dealings with government	Evidence of company involvement in misuse or misappropriation of public property?				
	Evidence of bribing public officials or use of inappropriate means to influence public decisions or processes?				
	Evidence of major political affiliations or contributions?				
	Evidence of politician or government official involvement in the company? (e.g. beneficial owners, on board of directors, etc).				

ESG due diligence questions
Governance: business integrity

	Due diligence on business integrity matters	Tick Yes / No		Comments / action required	Answer source
Key due diligence areas	**Questions to ask**	**Yes**	**No**		
Corporate affairs	Media references to illegal or disreputable activities?				See p. 73
	Persistent rumours of illegal or disreputable activities?				
	Requests for or suggestions of illegal or disreputable actions (e.g. falsification of document, bribes, etc)?				
	Misappropriation, fraud or other crimes against the company or its owners or stakeholders?				
	Any undisclosed or unusual beneficial ownership or carried interests?				
	Sudden or unexplained withdrawal of potential customers, investors or other affiliates to the company?				
	Sudden or unexplained change of shareholders, auditors, accountants, lawyers or other professional advisors?				
	Unnecessarily complex ownership structures?				
	Evidence of tax evasion?				
	Evidence of suspicious use of tax havens?				
	Evidence of suspicious use of offshore companies?				
	Evidence of suspicions use of transfer pricing?				
	Are there pools of unexplained cash or near cash investments (e.g. slush funds)?				
	Large or serious law suits for which there is not a satisfactory explanation?				
	Inappropriate or above-market costs, fees or other company expenses?				
	Non-market compensation of key staff, management or company shareholders?				
	Unknown or suspicious sources of wealth for company staff, management and / or shareholders?				
	Ostentatious lifestyle inappropriate to the financial situation of the company of company staff, management and / or shareholders?				
	Reluctance to discuss integrity or corruption issues from company staff, management and / or shareholders?				
More detailed or formal investigation	Is a more detailed or formal investigation warranted?				
	Why or why not?				

Appendix 1

ESG due diligence questions

Governance: corporate governance

	Due diligence on corporate governance matters[2]	Tick Yes / No		Comments / action required	Answer source
Key due diligence areas	**Questions to ask**	**Yes**	**No**		
Commitment to good corporate governance	Does the company have a charter or articles of incorporation according to local legislation, with provisions on: (i) the protection of shareholder rights and the equitable treatment of shareholders;				*Documents:* Articles of incorporation, corporate governance code, corporate governance section of the annual report, code of ethics, whistleblower policy, minutes of board meetings. *Interviews:* Board chair and other board members, CEO, compliance or corporate governance officer.
	(ii) distribution of authority between the annual general meeting of shareholders, the board of directors and executive bodies, and				
	(iii) information disclosure and transparency of the company's activities?				
	Are the board of directors and the senior management familiar with the voluntary code of corporate governance for the country (if such a code exists)?				
	To what extent does the company comply with the provisions of this code? How is this compliance disclosed?				
	Does the company have a code of ethics?				
	Does the company have a corporate governance code and / or policies?				
	What are the procedures for monitoring compliance with these? Who does the monitoring?				
	Does the company have a whistleblower policy and procedures?				
	Does the company disclose the extent to which it is complying with its corporate governance policies and procedures?				
	Does the company have a designated officer responsible for ensuring compliance with the company's corporate governance policies?				
	Does the management / board of directors approve the annual calendar of corporate events (board meetings, general shareholder meeting, etc)?				
Structure and functioning of the board of directors	How is the composition of the board of directors determined?				*Documents:* Articles of incorporation, board charter, directors' profiles, calendar of board meetings, minutes of board meetings, related party transactions table.
	Are there any shareholder agreements, provisions of the company's charter, or informal understandings that specify which shareholders appoint directors?				
	Are there any independent directors?				
	How were they selected? How, if at all, does the company define 'independent' director?				
	Does the company have board committees? Which functions?				
	If so, how are board committees established, who sits on them, and how do they function?				
	How often does the board of directors meet?				
	Is an agenda prepared and distributed in advance of board meetings?				
	Are minutes prepared and approved after board meetings?				
	Does the company have a corporate secretary? If not, who organises board meetings?				

[2] Adapted by CDC and Rosencrantz & Co from the Toolkit on Corporate Governance developed by a development finance institution (DFI) working group, which is based on IFC materials and consistent with the OECD Principles of Corporate Governance. See *Appendix 5*.

ESG due diligence questions
Governance: corporate governance

	Due diligence on corporate governance matters	Tick Yes / No		Comments / action required	Answer source
Key due diligence areas	Questions to ask	Yes	No		
Structure and functioning of the board of directors (continued)	What is understood as the role of the board of directors vis-à-vis management, particularly with respect to the following: (i) setting strategy and vision of the company; (ii) selection and compensation of the CEO and senior management; (iii) risk management, oversight of internal controls, external audit and preparation of financial statements; and (iv) major capital expenditures and large-value transactions?				*Interviews:* Board chair, corporate secretary, board committee chairmen, CEO, CFO.
	How does the current mix of skills / experience on the board of directors serve the company's interests?				
	Are directors appointed on the basis of a clear job description which identifies the required directors' background and expertise?				
	Does the board of directors review material transactions that involve conflicts of interest and related parties?				
	Does the board of directors conduct self-evaluations or other reviews of its effectiveness?				
	How and when are such reviews conducted and with whom are the results shared?				
	Do all board directors have a clean record when it comes to sanctions for violating any of his / her duties?				
	How often are board directors re-elected?				
	Is there a maximum number of terms that a director can serve?				
	Does the company have a formal or informal succession plan for its current CEO?				
	How much longer does the current CEO intend to remain in this position?				
	Is the effectiveness of the board and its directors regularly evaluated by an independent third party?				
Control and risk management	Does the company have adequate internal controls in place?				*Documents:* Audit committee charter, internal control and risk management policies, management letters, compliance programme.
	Are internal controls properly documented and periodically reviewed?				
	Does the company have an audit committee?				
	What is the role of the audit committee and the board of directors in ensuring that proper internal controls are maintained, risks are managed and that the company is in compliance with all relevant laws and regulations?				
	Does the board of directors set the company's risk profile and periodically review the company's risk management system?				
	Does the company have an internal audit (IA) function?				
	Does the IA function have a charter that is approved by the audit committee or board of directors?				
	Does the IA function have full access to records, property and personnel relevant to their audit?				

Appendix 1

ESG due diligence questions

Governance: corporate governance

Key due diligence areas	Due diligence on corporate governance matters Questions to ask	Tick Yes / No Yes	No	Comments / action required	Answer source
Control and risk management (continued)	To whom does the IA function report?				*Interviews:* Board chair, audit committee chair, CFO, controller, internal audit responsible risk officer, compliance officer, external auditor.
	Is the IA chief independently hired and dismissed with the consent of the board of directors?				
	Does the board of directors monitor management's response to deficiencies and weaknesses identified by the IA function and / or external auditors?				
	Does the company have a risk management system including ESG matters?				
	Who is responsible for developing the company's risk management system?				
	How are the risks identified and compared with industry standards?				
	Does the company have a compliance programme or procedures that include the training of employees, auditing and monitoring systems, and a company 'hotline' for reporting any violations?				
	Have internal controls, risk management and compliance in the past 5 years operated without any significant problems being reported?				
	Is the company's external audit in line with international standards on auditing (ISA)?				
	Who, formally and in practice, selects the external auditors and to whom are they accountable?				
	Is there a policy to rotate the external auditors or the engagement audit partner?				
	Does the company have a history of there being no qualified, adverse, or disclaimer of opinion/s on the financial statements issued by external auditor?				
	If no (i.e. if the external auditor has issued qualified, adverse, or disclaimer of opinion/s on financial statements): why?				
Transparency and disclosure	Are the financial statements prepared in keeping with internationally recognised accounting standards (e.g., IFRS or U.S. GAAP)?				*Documents:* Financial statements, information disclosure policy. *Interviews:* Audit committee chair, CFO, controller, external auditor, chief of investor relations.
	Have the company's financial statements in the past 5 years been re-statements in a material way?				
	If re-statements have been made: please specify.				
	Does the company disclose major transactions, related party transactions, off-balance sheet activities, and other material events?				
	How (e.g. annual report, website)?				
	Does the board of directors / audit committee review key elements of the company's financial statements?				
	How often?				
	Does the company have a written information disclosure policy that seeks to make all material information (financial and non-financial) fully, timely and equally available to all stakeholders?				
	Is the company publicly listed? If the company is publicly listed: on what exchange?				
	Are periodic meetings with securities analysts held? Who participates in such meetings?				

ESG due diligence questions
Governance: corporate governance

Key due diligence areas	Due diligence on corporate governance matters – Questions to ask	Tick Yes / No – Yes	Tick Yes / No – No	Comments / action required	Answer source
Transparency and disclosure (continued)	Has the regulator or the exchange required the company to provide additional information or clarification to the annual report, financial statements or other disclosures?				
	If the regulator has required additional information: on what elements?				
	Has the company ever been sanctioned or censured by the regulator or the exchange for any failure or delay in disclosing required information to the public?				
Rights of minority shareholders and treatment of stakeholders	Is there equality between the voting rights and the cash flow rights of the company's various classes of equity and quasi-equity securities (the 'one share, one vote' principle)?				*Documents:* Articles of association, annual report, by-laws on shareholders' meeting, minutes of shareholders' meeting. *Interviews:* Controlling shareholders, minority shareholders, board chair, corporate secretary.
	Do minority shareholders have any mechanism to nominate members of the board of directors (e.g. cumulative voting, block voting, etc)?				
	Have such rights been exercised?				
	Is ultimate beneficial ownership of shares disclosed by controlling shareholders and management?				
	Are there any minority shareholders protection mechanisms in place?				
	How will minority shareholders be treated in the event of a change of control of the company (e.g. tag-along rights)?				
	Does the preparation and calling of annual and extraordinary shareholders meetings enable the participation of all shareholders (sufficient notice; agenda and supporting materials; proposing agenda items; participation personally or through proxy; the right to ask questions; dissemination of the results of the meetings)?				
	Has the company a clean history when it comes to investigation into its treatment of shareholders, i.e. never having undergone such an investigation?				
	How have any shareholder disputes been resolved?				
	Does the company regularly consult with local communities, NGOs and other relevant stakeholders?				
	Has there been negative media coverage about the company or its staff / management / board directors?				
	How is the company perceived by media and NGOs?				

Appendix 2

Sector-specific ESG risks and opportunities for improvements

Investments in companies in different sectors require a fund manager to consider different sector specific risks and opportunities from the environmental, social and governance (ESG) perspectives. Some sectors involve significant risks from one or more ESG perspectives. Where significant risks are involved, fund managers should always use specialists for due diligence, which would often require an environmental and social impact assessment (see *Tool 7*). Specialists may also need to be involved during the investment period, especially if the assets have significant risks and / or if there are ESG issues at the time of investment and improvements to be undertaken during the investment duration.

Different international reference standards may also need to be considered, in addition to local laws, for investments in various industry sectors. For investments in sectors with significant risks, fund managers investing CDC's capital have to apply the IFC's Performance Standards and the associated Environmental, Health and Safety (EHS) Guidelines for specific industries as the reference standards for improvements to the company's operations over the investment duration, if these standards are not met at the time of the investment (see *Appendix 5*). The ILO core labour standards should always be met for all portfolio companies by fund managers investing CDC's capital (see *Appendix 5*). For some industries, the risk of companies not complying with the ILO core labour standards is higher. Other international conventions may also need to be considered, as per CDC's Investment Code (see p. 9-13, each industry sector presented in this appendix and *Appendix 5*).

Some industry sectors have key business opportunities related to ESG improvements.

By factoring into the due diligence sector relevant ESG issues and opportunities for each potential investment, particularly for companies in sectors with significant risks, a fund manager will obtain an enhanced picture of the risk level and opportunities for improvements. Face-to-face discussions with management and site visits are usually required, since the reaction of the company management to the questions asked sometimes reveals as much about the company as the answer itself and site visits provide a more complete understanding of the issues and risks involved.

The section below highlights key issues and opportunities that fund managers need to consider for selected industry sectors including construction, food and beverages, retail, telecommunications, mining, pharmaceuticals, manufacturing, agriculture, forestry, infrastructure and energy and utilities. These issues and opportunities should be explored during a fund manager's due diligence.

1 Construction

Key ESG risks and opportunities for improvements in the construction sector are highlighted below.

Environmental risks:

- risks for alterations to the natural habitat, with negative impacts for local communities, flora and fauna;
- waste management, including general wastes and hazardous wastes;
- effluent monitoring and controls;
- water pollution;
- energy use; and
- non-compliance with local environmental laws and regulations.

Social risks:

- non-payment of minimum wages;
- lack of proper labour contracts;
- lack of workplace associations / unions;

- elevated working conditions with risks for accidents;
- fire safety;
- worker exposure to hazardous building materials;
- non-compliance with local health and safety laws and regulations;
- community exposure to dust, noise and vibrations; and
- lack of community involvement in planning of new constructions on previously unused land.

Governance risks:

- risk of corrupt payments for access to planning permissions from the local or national government, certifications and new property development contracts;
- risk of corrupt business practices, with non-registered and improper payments to sub-contractors;
- avoidance of tax payments;
- poor corporate governance; and
- management of challenging or controversial projects from a regulatory perspective.

ESG business opportunities:

- increased demand for energy efficient buildings;
- good relationships with local communities and NGOs to avoid potential unrest, project delays and associated extra costs;
- cost effectiveness from efficient use of building materials;
- purchases from local suppliers, which can improve the company's relations with the local communities;
- decent labour practices, notably payment of minimum wages, non-discriminatory practices and proper contracts for workers to improve worker satisfaction and retention;
- zero corruption tolerance; and
- improvements in corporate governance.

International standards of particular importance in the construction sector:

- IFC Performance Standards (see p. 105)
- The Rotterdam Convention (see p. 121)
- The Basel Convention (see p. 122)
- The ISO 9000 and 14000 standards (see p. 124)
- The ILO Fundamental Conventions (see p. 125)
- The ISO 26000 standards (see p. 133)
- The OHSAS 18000 series (see p. 133)
- The Construction Sector Transparency Initiative (see www.constructiontransparency.org)
- All conventions, standards and guidelines related to governance (see p. 135)

2 Food and beverages

Key ESG risks and opportunities for improvements in the food and beverages sector are highlighted below.

Environmental risks:

- waste management, including general wastes, chemical wastes and biological wastes;

Appendix 2

Sector-specific ESG risks and opportunities for improvements

- effluent monitoring and controls;
- air emissions;
- contamination of waste water;
- reduction in local water supply from overuse;
- energy use;
- dependence on raw materials that may become scarce; and
- non-compliance with local environmental laws and regulations.

Social risks:

- adherence to food safety standards;
- contamination of products;
- non-payment of minimum wages;
- exposure of workers to hazardous substances;
- lack of proper training and protective equipment for workers; and
- non-compliance with local health and safety laws and regulations.

Governance risks:

- risk of corrupt payments to obtain permits, certifications, sanitary controls or similar; and
- poor corporate governance.

ESG business opportunities:

- capitalisation on higher margins and sales growth from specialist markets such as organic food, health food, 'fair-trade' products or products for minority groups;
- international certifications to support such sales to specialist markets and / or to sustainability concious consumers
- non-use of genetically-modified crops where consumer preferences are against such usage;
- new potential market segments, including food and beverages for poor populations;
- decent labour practices, notably payment of minimum wages, non-discriminatory practices and proper contracts for workers to improve worker satisfaction and retention;
- zero corruption tolerance; and
- improvements to corporate governance.

International standards of particular importance in the food and beverages sector:

- IFC Performance Standards (see p. 105)
- IFC EHS Guidelines for agribusiness / food production (multiple) (see p. 109)
- The Montreal Protocol (see p. 117)
- The Stockholm Convention (see p. 119)
- The Rotterdam Convention (see p. 121)
- The Basel Convention (see p. 122)
- The ISO 9000 and 14000 standards (see p. 124)
- The ILO Fundamental Conventions (see p. 125)
- The ISO 26000 standards (see p. 133)
- The OHSAS 18000 series (see p. 133)
- The Good Manufacturing Practices (GMP) in the production of food and pharmaceuticals (see p. 134)
- The Food and Agricultural Organization's (FAO) guidelines (see www.fao.org)
- All conventions, standards and guidelines related to governance (see p. 135)

Sector-specific ESG risks and opportunities for improvements

3 Retail

Key ESG risks and opportunities for improvements in the retail sector are highlighted below.

Environmental risks:

- waste management, including general wastes and hazardous wastes;
- contamination of waste water;
- energy use; and
- non-compliance with local environmental laws and regulations.

Social risks:

- non-payment of minimum wages;
- non-compliance with local health and safety laws and regulations.

Governance risks:

- risk of corrupt payments to obtain permits, certifications, controls or similar;
- risk of corrupt payments for expansions (e.g. to obtain planning permissions for new sites); and
- poor corporate governance.

ESG business opportunities:

- responsible sourcing;
- new market segments, including poor populations;
- purchases from local suppliers, which may improve relations with local communities and the retail chain's reputation;
- decent labour practices, notably payment of minimum wages, non-discriminatory practices and proper contracts for workers to improve worker satisfaction and retention;
- alternative opening hours or flexible working hours offered to staff;
- zero corruption tolerance; and
- improvements in corporate governance.

International standards of particular importance in the retail sector:

- IFC Performance Standards (see p. 105)
- The Rotterdam Convention (see p. 121)
- The Basel Convention (see p. 122)
- The Convention on International Trade in Endangered Species of Wild Flora and Fauna (CITES) (see p. 123)
- The ISO 9000 and 14000 standards (see p. 124)
- The ILO Fundamental Conventions (see p. 125)
- The ISO 26000 standards (see p. 133)
- The OHSAS 18000 series (see p. 133)
- The Good Manufacturing Practices (GMP) in the production of food and pharmaceuticals (see p. 134)
- All conventions, standards and guidelines related to governance (see p. 135)

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Sector-specific ESG risks and opportunities for improvements

4 Telecommunications

Key ESG risks and opportunities for improvements in the telecommunications sector are highlighted below.

Environmental risks:

- habitat alternations, with adverse impacts on local communities, flora and fauna;
- waste management, including general wastes and hazardous wastes;
- energy use; and
- non-compliance with local environmental laws and regulations.

Social risks:

- worker exposure to hazardous materials;
- safety issues concerning electric and magnetic fields for workers and local communities;
- elevated working conditions;
- lack of proper training and protective equipment for workers;
- community concerns over the siting of masts or other new telecommunications infrastructure on previously unused or otherwise occupied lands; and
- non-compliance with local health and safety laws and regulations.

Governance risks:

- risk of corrupt payments to obtain mobile network concessions, licences, permits for new telecommunications infrastructure, certifications, controls or similar; and
- poor corporate governance.

ESG business opportunities:

- adaption of telephony service offerings to new markets, including poor populations;
- generation of additional revenues through re-sale or re-use of materials from disassembled returned handsets;
- cost savings from the new generation of base stations with lower energy consumption;
- decent labour practices, notably payment of minimum wages and proper contracts for workers to improve worker satisfaction and retention;
- zero corruption tolerance; and
- improvements in good corporate governance.

International standards of particular importance in the telecommunications sector:

- IFC Performance Standards (see p. 105)
- IFC EHS Guidelines for telecommunications (see p. 109)
- The Rotterdam Convention (see p. 121)
- The Basel Convention (see p. 122)
- The ISO 9000 and 14000 standards (see p. 124)
- The ILO Fundamental Conventions (see p. 125)
- The ISO 26000 standards (see p. 133)
- The OHSAS 18000 series (see p. 133)
- All conventions, standards and guidelines related to governance (see p. 135)

Sector-specific ESG risks and opportunities for improvements

5 Mining

Key ESG risks and opportunities for improvements in the mining sector are highlighted below.

Environmental risks:

- habitat alternations, with adverse impacts for local communities, flora and fauna;
- waste management, including general wastes and hazardous wastes;
- gaseous emissions;
- hazardous effluents;
- use of explosives;
- specific hazards in underground mining (fires, explosions);
- water contamination;
- reduction in local water supply from overuse;
- energy use; and
- non-compliance with local environmental laws and regulations.

Social risks:

- child labour;
- forced labour;
- worker exposure to hazardous materials;
- use of explosives;
- physical hazards, notably from underground mining (fires, explosions, confined spaces);
- non-payment of minimum wages;
- lack of proper labour contracts;
- lack of workplace associations / unions;
- lack of proper training and protective equipment for workers;
- community concerns over land alternations from mining;
- resettlement of local communities from new or expanded mining operations;
- inflow of non-local workers to new or expanded mining sites, with potential adverse impacts for local communities such as an increase in prostitution and HIV / AIDS prevalence, especially if new non-local male workers are not bringing their families;
- impacts on indigenous populations;
- impacts on cultural heritage;
- if the mining site is remotely located, risks for improper living conditions for workers and their families;
- risks associated with the use of a company security force; and
- non-compliance with local health and safety laws and regulations.

Governance risks:

- risk of corrupt payments to obtain mining concessions, licences, permits, certifications, controls or similar;
- risk of corrupt business practices, with non-registered and improper payments to subcontractors;
- avoidance of tax payments;
- poor corporate governance; and
- management of challenging or controversial projects from a regulatory perspective.

ESG business opportunities:

- decent labour practices, notably payment of minimum wages and proper contracts for workers to improve worker satisfaction and retention;
- positive relations with local communities, NGOs and indigenous populations to reduce risk of issues and improve the corporate brand;

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Sector-specific ESG risks and opportunities for improvements

- consultations with local communities and NGOs throughout the development of any new or expanded infrastructure project;
- proper resettlement programmes with fair compensation and consultations for persons affected by new or expanded mining operations, to avoid local resentment, disruptions, extra costs and brand damage;
- support to local communities that are affected by any new or expanded infrastructure project, and / or to the inflow of non-local workers and their families;
- proper attention to the rights of local indigenous populations;
- proper attention to cultural heritage matters;
- employment of local workers;
- proactive safety measures;
- if non-local workers are used, relocation of their families to the site of the operations if so desired for improved worker satisfaction and retention as well as reduced risk of issues with local communities;
- if the mining site is remotely located, construction of proper housing, health care centres, educational facilities for children, etc, for improved worker satisfaction and retention;
- cost effectiveness from efficient use of energy and materials;
- zero corruption tolerance;
- application of the Extractive Industries Transparency Initiative, with transparent publishing of all payments to local and national governments and public officials to reduce risk of costly corrupt payments; and
- improvements in corporate governance.

Mining is an especially high risk sector. The fund manager should therefore contract or employ specialists to help with due diligence and on-going operations.

International standards of particular importance in the mining sector:

- IFC Performance Standards (see p. 105)
- IFC EHS Guidelines for mining (see p. 109)
- The Rotterdam Convention (see p. 121)
- The Basel Convention (see p. 122)
- The ISO 9000 and 14000 standards (see p. 124)
- The ILO Fundamental Conventions (see p. 125)
- The ISO 26000 standards (see p. 133)
- The OHSAS 18000 series (see p. 133)
- All conventions, standards and guidelines related to governance (see p. 134)
- The Extractive Industries Transparency Initiative (see p. 139)

Sector-specific ESG risks and opportunities for improvements

6 Pharmaceuticals

Key ESG risks and opportunities for improvements in the pharmaceuticals sector are highlighted below.

Environmental risks:

- waste management, including general wastes and hazardous wastes from manufacturing and usage;
- lack of clearly defined, safe and controlled manufacturing processes;
- contamination of waste water;
- reduction in local water supply from overuse;
- energy use;
- hazardous effluents;
- air emissions; and
- non-compliance with local environmental laws and regulations.

Social risks:

- adherence to safe drug standards;
- unsafe distribution of products to end users;
- exposure of workers to hazardous substances;
- lack of proper training and protective equipment for workers; and
- non-compliance with local health and safety laws and regulations.

Governance risks:

- risk of corrupt payments to obtain licences, permits, certifications or similar;
- patent infringement; and
- poor corporate governance.

ESG business opportunities:

- improving research and development (R&D) procedures and standards towards good and best international practices (WHO GMP, US FDA, EU GMP);
- new potential market segments, including poor populations;
- decent labour practices, notably payment of minimum wages and proper contracts for workers to improve worker satisfaction and retention;
- zero corruption tolerance; and
- improvements in corporate governance.

International standards of particular importance in the pharmaceuticals sector:

- IFC Performance Standards (see p. 105)
- IFC EHS Guidelines for pharmaceuticals (see p. 109)
- The Rotterdam Convention (see p. 121)
- The Basel Convention (see p. 122)
- The ISO 9000 and 14000 standards (see p. 124)
- The ILO Fundamental Conventions (see p. 125)
- The ISO 26000 standards (see p. 133)
- The OHSAS 18000 series (see p. 133)
- The Good Manufacturing Practices (GMP) in the production of food and pharmaceuticals (see p. 134)
- The Medicines Transparency Alliance (see www.medicinestransparency.org)
- All conventions, standards and guidelines related to governance (see p. 135)

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Sector-specific ESG risks and opportunities for improvements

7 Manufacturing

Key ESG risks and opportunities for improvements in the manufacturing sector are highlighted below:

Environmental risks:

- waste management, including general wastes, chemical wastes and other hazardous wastes;
- hazardous emissions;
- emissions of dust;
- hazardous effluents;
- water contamination;
- reductions in local water supply from overuse;
- fires and explosives;
- energy use; and
- non-compliance with local environmental laws and regulations.

Social risks:

- child labour;
- worker exposure to hazardous materials, substances, and machinery;
- non-payment of minimum wages;
- lack of proper labour contracts;
- lack of workplace associations / unions;
- lack of proper training and protective equipment for workers;
- chemical and physical hazards for workers;
- fires and explosives;
- workers' use of unsafe machinery; and
- non-compliance with local health and safety laws and regulations.

Governance risks:

- risk of corrupt payments to obtain licences, permits, certifications or similar;
- risk of corrupt business practices, with non-registered or improper payments to subcontractors;
- patent infringement; and
- poor corporate governance.

ESG business opportunities:

- new market segments for manufacturing products, including poor populations;
- new products (e.g., cleaner technologies, re-usable products);
- use of recycled materials in the production process;
- decent labour practices, notably payment of minimum wages, non-discriminatory practices and proper contracts for workers to improve worker satisfaction and retention;
- proactive safety measures;
- programmes that enable workers to combine a family and work (e.g., flexible working hours, child care for working mothers);
- zero corruption tolerance; and
- improvements in corporate governance.

Sector-specific ESG risks and opportunities for improvements

International standards of particular importance in the manufacturing sector:

- IFC Performance Standards (see p. 105)
- IFC EHS Guidelines for general manufacturing (multiple) and chemicals (multiple) (see p. 108-109)
- The Stockholm Convention (see p. 119)
- The Rotterdam Convention (see p. 121)
- The Basel Convention (see p. 122)
- The ISO 9000 and 14000 standards (see p. 124)
- The ILO Fundamental Conventions (see p. 125)
- The ISO 26000 standards (see p. 133)
- The OHSAS 18000 series (see p. 133)
- All conventions, standards and guidelines related to governance (see p. 135)

8 Agriculture

Key ESG risks and opportunities for improvements in the agriculture sector are highlighted below:

Environmental risks:

- habitat alternations, with adverse impacts on local communities, local flora and / or fauna;
- unsafe genetically modified crops
- unsustainable farming methods with subsequent soil erosion and loss of productive capacity;
- changes to local flora and fauna from introduction of new crops, herbicides or pesticides;
- waste management, including chemical wastes and biological wastes;
- hazardous effluents;
- water contamination;
- reductions in local water supply from overuse;
- use of unsafe and / or prohibited herbicides and pesticides;
- energy use; and
- non-compliance with local environmental laws and regulations.

Social risks:

- child labour;
- forced labour;
- chemical hazards for workers and local communities from pesticides and herbicides;
- worker use of unsafe machinery;
- non-payment of minimum wages;
- lack of proper labour contracts;
- lack of workplace associations / unions;
- inflow of seasonal / migrant workers, with potential adverse impacts for local communities including prostitution, increased HIV / AIDS prevalence and / or other negative impacts, especially if the non-local workers are not bringing their families;
- lack of proper training and protective equipment for workers;
- community concerns over land alternations from farming;

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Sector-specific ESG risks and opportunities for improvements

- resettlement of local communities from new or expanded agricultural operations;
- if the farming site is remotely located, risks for improper living conditions for workers and their families;
- impacts on local indigenous populations;
- impact on cultural heritage; and
- non-compliance with local health and safety laws and regulations.

Governance risks:

- risk of corrupt payments to obtain farming concessions, permits, certifications or similar;
- risk of corrupt business practices, with non-registered and improper payments to subcontractors; and
- poor corporate governance.

ESG business opportunities:

- decent labour practices, notably payment of minimum wages, non-discriminatory practices and proper contracts for workers for improved worker satisfaction and retention;
- proactive safety measures;
- positive relations with local communities, NGOs and indigenous populations to reduce risk of issues and improve the company's brand;
- consultations with local communities and NGOs throughout the development of any new or expanded agricultural operations;
- proper resettlement programmes with fair compensation and consultations for persons affected by new or expanded agriculture operations to avoid local resentment, disruptions, extra costs and brand damage;
- support to local communities that are affected by any new or expanded agricultural operations, and / or to the inflow of non-local workers and their families;
- proper attention to the rights of local indigenous populations;
- proper attention to cultural heritage matters;
- if non-local workers are used, relocation of families to the site of the operations if so desired for improved worker satisfaction and retention as well as reduced risk of issues with local communities;
- higher margins and sales growth from specialist markets such as organic food or fair trade products, with the relevant international certifications;
- restitution of previously depleted land for renewed agricultural use;
- programmes that enable workers to combine a family and work (e.g., through flexible working hours and child care facilities for working mothers);
- efficient use of energy, water, and other resources used;
- sustainable farming practices to ensure that the soil is not eroded and the farming land maintains its productivity;
- zero corruption tolerance; and
- improvements in good corporate governance.

International standards of particular importance in the agricultural sector:

- IFC EHS Guidelines for agribusiness / food production (multiple) (see p. 108)
- The Montreal Protocol (see p. 117)
- The Stockholm Convention (see p. 119)
- The Rotterdam Convention (see p. 121)
- The Basel Convention (see p. 122)
- The Convention on International Trade in Endangered Species of Wild Flora and Fauna (CITES) (see p. 123)
- The ISO 9000 and 14000 standards (see p. 124)
- The ILO Fundamental Conventions (see p. 125)
- The ISO 26000 standards (see p. 133)
- The OHSAS 18000 series (see p. 133)
- The Food and Agricultural Organization's (FAO) guidelines (see www.fao.org)
- All conventions, standards and guidelines related to governance (see p. 135)

Sector-specific ESG risks and opportunities for improvements

9 Forestry

Key ESG risks and opportunities for improvements in the forestry sector are highlighted below:

Environmental risks:

- habitat alternations, with adverse impacts for local communities, flora and fauna;
- unsustainable harvesting;
- deforestation;
- soil erosion;
- use of unsafe and / or prohibited herbicides and pesticides;
- changes to local flora and fauna;
- impacts on biodiversity;
- waste management, including chemical wastes;
- emissions of dust from saw mills;
- water contamination;
- reductions in local water supply from overuse; and
- non-compliance with local environmental laws and regulations.

Social risks:

- child labour;
- forced labour;
- non-payment of minimum wages;
- lack of proper labour contracts;
- physical hazards for workers from use of unsafe machinery, saws and from falling trees;
- chemical hazards for workers and local communities from pesticides and herbicides;
- lack of workplace associations / unions;
- lack of proper training and protective equipment for workers;
- community concerns over land alternations from forestry;
- inflow of seasonal / migrant workers, with potential adverse impacts for local communities including prostitution, increased HIV / AIDS prevalence and / or other negative impacts, especially if the non-local workers are not bringing their families;
- lack of proper training and protective equipment for workers;
- community concerns over land alternations from farming;
- resettlement of local communities from new or expanded forestry operations;
- if the farming site is remotely located, risks for improper living conditions for workers and their families;
- impacts on local indigenous populations;
- impact on cultural heritage; and
- non-compliance with local health and safety laws and regulations.

Governance risks:

- risk of corrupt payments to obtain forestry concessions, permits, certifications or similar;
- risk of corrupt business practices, with non-registered and improper payments to subcontractors; and
- poor corporate governance.

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Sector-specific ESG risks and opportunities for improvements

ESG business opportunities:

- decent labour practices, notably payment of minimum wages, non-discriminatory practices and proper contracts for workers to improve worker satisfaction and retention;
- adherence to the Forestry Stewardship Council (FSC) principles and certification, which could lead to premium pricing for conscious buyers;
- Carbon markets opportunities, including Verified Emissions Reductions (VERs) and the opportunities provided by REDD+ as per the Copenhagen Accord;
- positive relations with local communities, NGOs and indigenous populations to reduce risk of issues and improve the corporate brand;
- consultations with local communities and NGOs throughout the development of any new or expanded forestry operations;
- proper resettlement programmes with fair compensation for persons affected by new or expanded operations to avoid local resentment, disruptions, extra costs and brand damage;
- support to local communities that are affected by any new or expanded forestry operations, and / or to the inflow of non-local workers and their families;
- proper attention to the rights of local indigenous populations;
- proper attention to cultural heritage matters;
- proactive safety measures;
- efficient use of energy, water and other resources;
- sustainable harvesting to reduce risks of soil erosion and deforestation;
- zero corruption tolerance; and
- improvements in corporate governance.

International standards of particular importance in the forestry sector:

- IFC Performance Standards (see p. 105)
- IFC EHS Guidelines for forestry (multiple) (see p. 108)
- The Montreal Protocol (see p. 117)
- The Stockholm Convention (see p. 119)
- The Rotterdam Convention (see p. 121)
- The Basel Convention (see p. 122)
- The Convention on International Trade in Endangered Species of Wild Flora and Fauna (CITES) (see p. 122)
- The Forestry Stewardship Council (FSC) principles (see www.fsc.org)
- The Copenhagen Accord (see p. 118 and *Appendix 9*)
- The ISO 9000 and 14000 standards (see p. 124)
- The ILO Fundamental Conventions (see p. 125)
- The ISO 26000 standards (see p. 133)
- The OHSAS 18000 series (see p. 133)
- All conventions, standards and guidelines related to governance (see p. 135)

10 Infrastructure

Key ESG risks and opportunities for improvements in the infrastructure sector are highlighted below:

Environmental risks:

- habitat alternations, with adverse impacts for local communities; flora and fauna;
- impact on biodiversity;
- waste management, including general wastes, chemical wastes and other hazardous wastes;
- gaseous emissions;
- unsustainable land use with resulting damage;
- emissions of dust;
- hazardous effluents;
- water contamination;
- reduction in local water supply from overuse;
- energy use; and
- non-compliance with local environmental laws and regulations.

Social risks:

- forced labour;
- non-payment of minimum wages;
- lack of proper labour contracts;
- worker exposure to hazardous substances;
- worker use of unsafe machinery;
- use of explosives;
- inflow of non-local labour, with impacts on local communities including increase in prostitution, HIV / AIDS prevalence and / or other negative impacts, especially if the non-local workers are not bringing their families;
- impacts on indigenous populations;
- impacts on cultural heritage;
- resettlement of local communities from sites of new or expanded infrastructure developments;
- lack of workplace associations / unions;
- lack of proper training and protective equipment for workers;
- community concerns over land alternations from new or expanded infrastructure developments;
- visual impacts that could impede tourism or recreation;
- if the new or expanded infrastructure development is remotely located, risks for improper living conditions for workers and their families;
- risks associated with the use of a company security force; and
- non-compliance with local health and safety laws and regulations.

Governance risks:

- risk of corrupt payments to obtain concessions, permits, certifications or similar;
- risk for corrupt business practices, with non-registered and improper payments to subcontractors; and
- poor corporate governance.

ESG business opportunities:

- decent labour practices, notably payment of minimum wages, non-discriminatory practices and proper contracts for workers, to improve worker satisfaction and retention;
- proactive safety measures;
- consultations with local communities and NGOs throughout the development of any new or expanded infrastructure project;

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Sector-specific ESG risks and opportunities for improvements

- proper resettlement programmes with fair compensation for persons affected by new or expanded infrastructure to avoid local resentment, disruptions, extra costs and brand damage;
- support to local communities that are affected by any new or expanded infrastructure project, and / or to the inflow of non-local workers and their families;
- proper attention to the rights of local indigenous populations;
- proper attention to cultural heritage matters;
- proper training of any corporate security personnel;
- zero corruption tolerance;
- transparency of all payments to local and national government representatives; and
- improvements in corporate governance.

International standards of particular importance in the infrastructure sector:

- IFC Performance Standards (see p. 105)
- IFC EHS Guidelines for infrastructure (multiple) (see p. 108)
- The Rotterdam Convention (see p. 121)
- The Basel Convention (see p. 122)
- The ISO 9000 and 14000 standards (see p. 124)
- The ILO Fundamental Conventions (see p. 125)
- The ISO 26000 standards (see p. 133)
- The OHSAS 18000 series (see p. 133)
- All conventions, standards and guidelines related to governance (see p. 135)

11 Energy and utilities

Key ESG risks and opportunities for improvements in the energy and utilities sector are highlighted below:

Environmental risks:

- habitat alternations, with adverse impacts on local communities, flora and / or fauna;
- impacts on biodiversity;
- waste management, including general wastes and chemical wastes;
- hazardous emissions;
- hazardous effluents;
- damage to land from new developments;
- energy use; and
- non-compliance with local environmental laws and regulations.

Social risks:

- non-payment of minimum wages;
- lack of proper labour contracts;
- resettlement of local communities for new or expanded facilities;
- safety issues concerning electric currents, and electric and magnetic fields for workers and local communities;

- worker exposure to hazardous substances;
- lack of workplace associations / unions;
- lack of proper training and protective equipment for workers;
- inflow of non-local labour, with impacts on local communities including increase in prostitution, HIV / AIDS prevalence and / or other negative impacts, especially if the non-local workers are not permitted to bring their families;
- impact on local indigenous populations;
- impacts on cultural heritage;
- risks associated with use of corporate security forces;
- delays or disruption caused by community alienation to new or expanded facilities;
- if the site is remotely located, risks for improper living conditions for workers and their families; and
- non-compliance with local health and safety laws and regulations.

Governance risks:

- risk of corrupt payments to obtain concessions, permits, certifications or similar;
- risk of corrupt business practices, with non-registered and improper payments to subcontractors; and
- poor corporate governance.

ESG business opportunities:

- efficient and safe distribution to local communities, with minimum electricity wasted;
- provision of electricity to new market segments, including poor populations;
- decent labour practices, notably payment of minimum wages, non-discriminatory practices and proper contracts for workers for improved worker satisfaction and retention;
- proactive safety measures;
- consultations with local communities and NGOs throughout the development of new or expanded facilities;
- proper resettlement programmes with fair compensations for persons affected by new or expanded infrastructure to avoid local resentment, disruptions, extra costs and brand damage;
- support to local communities that are affected by any new or expanded facilities, and / or to the inflow of non-local workers and their families;
- proper attention to the rights of local indigenous populations;
- proper attention to cultural heritage matters;
- proper training of any corporate security personnel;
- zero corruption tolerance;
- transparency of all payments to local and national government representatives to reduce the risk of costly corrupt payments; and
- improvements in corporate governance.

International standards of particular importance in the energy and utilities sector:

- IFC Performance Standards (see p. 105)
- IFC EHS Guidelines for power (multiple) (see p. 109)
- The Basel Convention (see p. 122)
- The ISO 9000 and 14000 standards (see p. 124)
- The ILO Fundamental Conventions (see p. 125)
- The ISO 26000 standards (see p. 133)
- The OHSAS 18000 series (see p. 133)
- All conventions, standards and guidelines related to governance (see p. 135)

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Sector-specific ESG risks and opportunities for improvements

International Reference Standards and Conventions	Page	Construction	Food and beverages	Retail	Telecommunications	Mining	Pharmaceuticals	Manufacturing	Agriculture	Forestry	Infrastructure	Energy and utilities
IFC Performance Standards	105	X	X	X	X	X	X	X	X	X	X	X
IFC EHS Guidelines	108		X		X	X	X	X	X	X	X	X
IFC Environmental and Social Management Toolkit for Private Equity Funds	109	X	X	X	X	X	X	X	X	X	X	X
The Environment												
The Montreal Protocol	117		X					X	X	X		
The UN Framework Convention on Climate Change, the Kyoto Protocol and the Copenhagen Accord	118	X	X	X		X	X	X	X	X	X	X
The Stockholm Convention	119		X				X	X	X	X		
The Rotterdam Convention	121							X	X	X		
The Basel Convention	122	X	X		X	X	X	X	X	X	X	X
The Convention on International Trade in Endangered Species of Wild Flora and Fauna	123			X					X	X		
ISO 9000 and 14000	124	X	X	X	X	X	X	X	X	X	X	X
Social matters												
The ILO Fundamental Conventions	125	X	X	X	X	X	X	X	X	X	X	X
ISO 26000	133	X	X	X	X	X	X	X	X	X	X	X
The Occupational Health and Safety Assessment Series 18000	133	X	X	X	X	X	X	X	X	X	X	X
Good manufacturing practices in the production of food and pharmaceuticals	134		X	X			X					

Sector-specific ESG risks and opportunities for improvements

International Reference Standards and Conventions	Page	Construction	Food and beverages	Retail	Telecommunications	Mining	Pharmaceuticals	Manufacturing	Agriculture	Forestry	Infrastructure	Energy and utilities
Governance												
The UN Convention against Corruption	135	X	X	X	X	X	X	X	X	X	X	X
The UN Anti-Corruption Toolkit	136	X	X	X	X	X	X	X	X	X	X	X
The OECD Anti-Bribery Convention	137	X	X	X	X	X	X	X	X	X	X	X
Transparency International's Corruption Perceptions Index	138	X	X	X	X	X	X	X	X	X	X	X
The Extractive Industries Transparency Initiative	139					X						
The Financial Action Task Force	139	X	X	X	X	X	X	X	X	X	X	X
The UK Proceeds of Crime Act and the UK Bribery Act	140	X	X	X	X	X	X	X	X	X	X	X
The UK Money Laundering Regulations	140	X	X	X	X	X	X	X	X	X	X	X
The US Foreign Corrupt Practices Act	140	X	X	X	X	X	X	X	X	X	X	X
The Business Anti-Corruption Portal	141	X	X	X	X	X	X	X	X	X	X	X
The OECD Principles of Corporate Governance	142	X	X	X	X	X	X	X	X	X	X	X
The International Financial Reporting Standards	143	X	X	X	X	X	X	X	X	X	X	X
The DFI Toolkit on Corporate Governance	144	X	X	X	X	X	X	X	X	X	X	X

Appendix 3

ESG risks in different regions and selected countries

ESG risks are usually higher in emerging markets than in more developed countries as local laws and regulations are sometimes weak and often poorly enforced. While similar ESG analyses apply across many low income markets, it is useful to be aware of risks that are more pronounced in certain countries and regions. Understanding local laws and how they relate to international standards and conventions is one step towards identifying country specific ESG risks. However, as international standards and conventions often are poorly enforced even if they have been ratified by a particular country and thereby become part of local law, it is critical for a fund manager to gain a more thorough understanding of the local situation in each country where investments are considered. The best way to do so is usually to establish a local presence, ideally through a country office or at least through a network of trusted specialist local advisors.

To facilitate a basic understanding of ESG risks for different regions and a few selected large countries, the table below presents a very basic overview of:

- some of the most pertinent ESG risks by region;
- some specific risks in a number of selected large countries; and
- ratification / signatory status for each of the select countries for some of the most important international standards and conventions related to ESG (see *Appendix 5*).

While ratification / signatory status means that a particular international standard or convention should have become part of local law, it has to be stressed that this is by no means an indication that fund managers should rely on the enforcement of such laws in many poor countries. Thorough due diligence and investment monitoring are always required, especially for investments in high risk sectors.

For other countries and their ratification / signatory status for key international ESG standards and conventions, see Appendix 5 as per the page indicated in the table below for each of these international standards.

Case 12: Energy efficiency delivers reduction of emissions and cost savings: Dalmia Cement, India

India is the second largest producer of cement in the world after China. Cement production is an energy intensive process and contributes to 5% of global greenhouse gas emissions. The cement sectors in China and India are growing at a rapid rate and greenhouse gas emissions from cement production are predicted to rise even further, posing a major climate change risk. Dalmia Cement is a leading cement producer in south India, with a total production capacity of 6.5 million tonnes of cement per year. In order to drive down emissions from its operations, Dalmia Cement has worked to improve the energy efficiency of its production processes.

- In 2009, Dalmia Cement's Dalmiapuram unit became self reliant in power, with 25% of the energy (16.5 MW) used by the plant sourced from a wind farm.
- Across its operations, Dalmia Cement has reduced power consumption per tonne of cement produced.

These initiatives have led to lower costs, whilst making Dalmia Cement one of the cleanest cement producers in India when measured by emissions per tonne of production. Dalmia Cement was the recipient of the Greentech Environmental Excellence Award in 2008 in recognition of these achievements.

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ESG risks in different regions and selected countries

Environment		Sub-Saharan Africa				Asia			Latin America	
General risks in each region		• Weak enforcement of local environmental laws and standards in many countries in sub-Saharan Africa. • Soil erosion and desertification caused by over-grazing and unsustainable agricultural practices. • Air and water pollution due to lack of enforcement of pollution controls, lack of clean energy sources, and rapid urban growth. • Loss of biodiversity, often connected to deforestation and changes in land use. • Threat of drought from climate change, with risks to local agribusiness, tourism and other industries.				• Rapid urbanisation has led to over-crowding, increased pollution and poor water, air and soil quality in many areas. • Deforestation from unsustainable forestry practices, especially in South East Asia. • Vulnerability to flooding and storms as a result of climate change. • Important improvements in environmental legislation and enforcement in recent years.			• Deforestation caused by over-grazing, unsustainable agriculture and forestry, and changes in land use to farming. • Water and air quality poor in large cities.	
		DR Congo	**Kenya**	**Nigeria**	**South Africa**	**China**	**India**	**Indo-nesia**	**Brazil**	**Mexico**
General risks in each country		Abundance of natural resources and related industries. Often unsustainable practices for mining and extraction of other local natural resources.	Threat of drought from climate change. Loss of biodiversity from unsustainable agriculture, tourism and industry practices.	Poor water quality and waste disposal. Threat of drought. Extensive environmental damage to the Niger delta due to unsustainable oil and gas extraction.	Reduction in water reserves and loss of natural habitat from industrialisation.	Extensive air and water pollution from growing cities and industrial zones. Flooding. Overfishing and soil erosion from unsustainable agricultural practices.	Imminent water crisis. Water and air pollution from growing cities and increasing numbers of vehicles and industries. Lack of major energy sources other than highly polluting coal.	Deforestation. Loss of habitat and biodiversity. Water and air pollution in heavily populated Jakarta and Java.	Deforestation. Loss of habitat and biodiversity. Positive use of clean alternative biofuels.	Water scarcity. Pollution, Soil erosion and desertification.
International standard / convention	**Page**									
The UN Framework Convention on Climate Change	118	Ratified	Ratified	Ratified	Ratified	Only ratified for Hong Kong	Ratified	Ratified	Ratified	Ratified
The Kyoto Protocol	118	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified
The Stockholm Convention	119	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified	Signed but not ratified	Ratified	Ratified
The Rotterdam Convention	121	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified	Signed but not ratified	Ratified	Ratified
The Basel Convention	122	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified
The Convention on International Trade in Endangered Species	123	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified

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Appendix 3

ESG risks in different regions and selected countries

Social matters		Sub-Saharan Africa				Asia			Latin America	
General risks in each region		• Weak enforcement of local social protection laws and regulations, and the underlying international standards and conventions, in many countries in sub-Saharan Africa. • Widespread poverty. • Lack of formal labour markets, income protection, social security and union protection in sub-Saharan Africa. • High HIV / AIDS prevalence. • Risks for child and forced labour, particularly in certain industries (see *Appendix 2*).				• Rural-urban inequalities • Extensive migration from rural to urban areas, with difficulties for migrant workers to assert their rights. • Lack of income protection and social security. • Risks for child and forced labour, particularly in certain industries (see *Appendix 2*).			• Lack of income security and social protection for migrant and seasonal workers. • Indigenous populations' rights. • Large income inequality and high levels of unemployment.	
		DR Congo	**Kenya**	**Nigeria**	**South Africa**	**China**	**India**	**Indonesia**	**Brazil**	**Mexico**
General risks in each country		Lack of representative democracy. Poor basic infrastructure and social services. Frequent violence and general lack of security. Tensions between different ethnic groups and with neighbouring countries. Risks of forced and child labour.	Tensions between tribal groups and regions.	Tensions over resources in the Niger delta. Lack of protection of workers rights. High levels of crime and violence.	HIV / AIDS prevalence ~ 20%. Widespread crime and lack of security. High levels of income inequality. Positive black empowerment programmes.	Risks of forced labour (prison populations) and forced migration. Non-state unions not permitted. Lack of enforcement of health and safety standards and regulations.	No national minimum age or minimum wage legislation, and risks for child labour. Widespread rural and urban poverty. Lack of social protection. Risks for discrimination based on race and the cast system.	Social unrest between different ethnic groups. Overcrowding in Jakarta and Java.	Indigenous populations in the Amazon region are threatened by new land uses for agriculture and forestry. Widespread income inequalities.	Risks of discrimination against indigenous populations. Drug trafficking, crime and kidnappings.
International standard / convention	**Page**									
The ILO Fundamental Conventions:										
29 and 105: Abolition of forced labour	125	Ratified	Ratified	Ratified	Ratified	Not ratified	Ratified	Ratified	Ratified	Ratified
138: Minimum employment age	127	Ratified	Ratified	Ratified	Ratified	Ratified	Not ratified	Ratified	Ratified	Not ratified
182: Worst forms of child labour	127	Ratified	Ratified	Ratified	Ratified	Ratified	Not ratified	Ratified	Ratified	Ratified
100: Equal remuneration	129	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified
111: Elimination of discrimination	130	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified
87: Freedom of association	131	Ratified	Not ratified	Ratified	Not ratified	Not ratified	Ratified	Not ratified	Ratified	Ratified
98: Right to organise and collective bargaining	131	Ratified	Ratified	Ratified	Ratified	Not ratified	Not ratified	Ratified	Ratified	Not ratified

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ESG risks in different regions and selected countries

Governance		Sub-Saharan Africa				Asia			Latin America	
General risks in each region		• Corruption remains endemic across most of the region, as illustrated by the low country rankings in Transparency International's Corruption Perceptions Index. • Bribery of public officials frequent. • Lack of transparency and accountability, particularly in transactions involving natural resources and public contracts. • Rudimentary company corporate governance regulations and resulting poor company disclosure of financial statements and other company information and records.				• Corporate governance standards and transparency lag behind more developed markets. • Bribery remains a significant regional problem. • Frequent issues with protection of minority shareholders' rights. • Lengthy court procedures make contract enforcement difficult. • Businesses are often family run and would benefit from improvements in corporate governance.			• Businesses are often family run and would benefit from improvements in good corporate governance. • Bribery of public officials remains frequent.	
		DR Congo	**Kenya**	**Nigeria**	**South Africa**	**China**	**India**	**Indo-nesia**	**Brazil**	**Mexico**
General risks in each country		Extensive corruption across all sectors, especially in extractive industries. Wide-spread bribery.	Frequent corruption and bribery, especially for public contracts.	Corruption and governance issues across sectors. Endemic corruption in some sectors, including construction, public contracts and extractive industries.	Relatively lower levels of corruption than in other countries in sub-Saharan Africa.	Privatisation of state owned enterprises with need for improvements in corporate governance standards. Inconsistent protection of shareholder rights.	Inconsistent implementation of good corporate governance standards and shareholder rights. Low level corruption and bribery.	Frequent corruption and bribery.	Positive new corporate governance standards for listed companies.	Risks of money laundering from drug related businesses. Low level corruption and bribery.
International standard / convention	Page									
The UN Convention against Corruption	135	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified	Ratified
The OECD Anti-Bribery Convention	137	Not ratified	Not ratified	Not ratified	Ratified	Not ratified	Not ratified	Not ratified	Ratified	Ratified
Transparency International's Corruption Perceptions Index (2009)	138	1.0	2.2	2.5	4.7	3.6	3.4	2.8	3.7	3.3
The Extractive Industries Transparency Initiative	139	Candidate country (not yet compliant)	No intent signalled, not in validation process	Candidate country (not yet compliant)	No intent signalled, not in validation process	No intent signalled, not in validation process	No intent signalled, not in validation process	Intent signalled to implement the EITI	No intent signalled, not in validation process	No intent signalled, not in validation process

Appendix 4

ESG management for different types of funds: SME, microfinance and debt funds

This Toolkit on ESG for fund managers is particularly designed for private equity fund managers. Fund managers of other types of funds, including debt funds and microfinance funds should also find the Toolkit useful, even though some *Tools* are less applicable. For debt funds, fund managers do not have the same level of influence over companies receiving credit as do equity investors. Microfinance funds provide very small amounts of finance, often to poor individual entrepreneurs, and the ESG risks they face are lower than for investors in companies. Fund managers investing in small and medium size enterprises (SMEs) usually face lower ESG risks than investors in larger companies, due to the sheer magnitude of their portfolio companies' operations and impacts.

The sections below provide brief guidance for SME fund managers, microfinance fund managers and debt fund managers on ESG matters and CDC's expectations.

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SMEs

Small and medium size enterprises (SMEs) have different definitions in different countries, usually limited by the number of employees, assets and / or turnover / sales. CDC uses the official World Bank and IFC definition for SMEs, which defines a company as an SME if at least two of the following three conditions are met:

- employees: < 300 persons
- total assets: < $15m
- turnover / annual sales: < $15m

As per CDC's and the IFC's definition, an SME fund is a fund where the fund manager credibly expects at least 50% of portfolio companies to qualify as SMEs at the time of investment.

Due to the smaller magnitude of their operations, SMEs usually involve lower ESG risks than large companies. SMEs are also rarer in some of the industries with the highest ESG risks, including mining, heavy industry and oil and gas. From the environmental perspective, SMEs usually generate lower levels of wastes, effluents and emissions, generating therefore more limited adverse environmental impacts than large companies can have. SMEs also employ fewer workers and therefore usually have more limited potential for adverse social impacts. From the governance perspective, SMEs can be prone to corruption and bribery, just like large companies, although at a smaller scale. SMEs usually require substantial improvements in corporate governance as they grow into larger corporations.

SMEs have limited staff and resources. ESG improvements can therefore be proportionally more costly for them to implement than for larger companies. Small SMEs would find it particularly challenging to develop, implement and continuously manage extensive management systems and processes for ESG. SME investors should therefore use their judgement as to which of the key questions listed in *Tool 8* that are relevant to assess the ESG management systems of a potential investee company.

While CDC expects fund managers investing in SMEs to fully apply its Investment Code (see p. 9-13) and to find the *Tools* in this Toolkit applicable for their operations, CDC appreciates that ESG improvements may be gradually implemented over time. Some development finance institutions (DFIs), including the IFC, have grant funding that can be made available for SMEs seeking to make ESG improvements.

Case 13: Successful SME investments in emerging markets: Aureos

Aureos is a specialist emerging markets private equity firm providing growth capital and expertise to help build and transform small and medium sized enterprises (SME).

From small beginnings in 2001, Aureos has raised over 16 regional SME funds with a total of US$1.3 billion in capital under management. Aureos has 25 local offices spread throughout Africa, Asia and Latin America, its principal investment destinations.

Aureos has integrated environmental and social criteria throughout its investment process, from due diligence to monitoring and reporting. Investment professionals are trained in responsible investment practice, using standards derived from CDC and the IFC. Aureos considers sound ESG management to be critical and integral part of its investment activities.

In the challenging field of SME investing in emerging markets, the establishment of a large and successful private equity fund manager in such a relatively short time is impressive.

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ESG management for different types of funds: SME, microfinance and debt funds

Microfinance

Microfinance institutions provide access to small amounts of credit and other financial services, most often to those segments of the population in emerging markets that previously did not have access to banking services. Microfinance promotes social entrepreneurship and the ability to develop sustainable small-scale businesses for poor people, the so-called 'bottom of the pyramid.'

Due to the very small scale of the activities funded through the provision of microfinance, environmental and social risks are low. Many of the *Tools* in this Toolkit would not be directly applicable to a microfinance institution's investment management processes. Business integrity risks could be high for microfinance, as for any institution dealing with the provision of finance. It is critical for the microfinance institution to ensure good corporate governance. The standards and *Tools* in this Toolkit which relates to governance should be particularly relevant.

The Dutch development finance institution, FMO, has developed a useful Toolkit for microfinance which can be downloaded from www.fmo.nl

CDC and other investors in microfinance institutions are keen to receive more accurate data on numbers of borrowers, the percentage of these borrowers that are women and whether these borrowers live in rural areas that are traditionally under-served by financial institutions.

CDC tracks the following indicators for its investments in microfinance funds, and requests its microfinance fund managers to report accordingly:

- taxes paid;
- portfolio at risk (30 days);
- growth of the loan portfolio;
- total number of borrowers;
- number of rural borrowers as a % of total;
- number of women borrowers as a % of total;
- number of employees; and
- individual ESG ratings per entity.

Debt funds

Debt fund managers in general have more limited ability to influence companies that receive credit from them or their underlying institutions than equity investors. Therefore, it is particularly important for debt fund managers to fully understand the ESG risks of the companies receiving financing from them before such credit is extended.

The Equator Principles, which incorporates the IFC's Performance Standards and which are consistent with CDC's Investment Code, are widely accepted by banks and other financial institutions that provide project finance in emerging markets (see *Appendix 5*). Debt fund managers are encouraged to become signatories to the Equator Principles and to apply them for their financing activities.

CDC expects debt fund managers with capital from CDC to fully apply CDC's Exclusion List and all relevant sections of the Investment Code (see p. 9-13). CDC also expects debt fund managers with capital from CDC to apply all relevant anti-money laundering (AML) and know-your-customer (KYC) checks (see p. 14-18).

Case 14: Successful expansion of microfinance to poor women: Sathapana, Cambodia

Sathapana, formerly known as Cambodian Entrepreneur Building, is a microfinance organisation in Cambodia with an investment from CDC's fund manager ShoreCap International. Since starting operations in 1996, Sathapana has provided 315,000 loans with a total value of US$126m to over 108,000 Cambodian households. With each loan benefiting several family members, Sathpana's lending has had a positive impact for an estimated 700,000 people.

ShoreCap International has provided Sathapana with technical assistance to improve its financial, audit and information systems.

In addition to the provision of finance, Sathapana is focused on helping entrepreneurial poor people, especially women, to develop micro-enterprises. Women run more than 60% of all micro-enterprises in Cambodia. Despite a strong entrepreneurial culture, women in Cambodia face socio-cultural and political discrimination, and have limited opportunities for formal employment. Approximately 70% of the loans made by Sathapana are to women. Higher income for women tends to result in better nutrition, welfare, and education for their children and other dependants.

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International ESG reference standards and conventions

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International ESG reference standards and conventions:
5.1 General

5.1.1 The IFC Performance Standards
(2006 with updates planned for 2011)

The International Finance Corporation (IFC) is the private sector arm of the World Bank group and the world's largest development finance institution (DFI). The IFC provides debt and equity capital for businesses throughout the emerging markets. A sizeable part of IFC's portfolio is invested through financial intermediaries, including private equity funds.

In 2006, the IFC launched its Policy and Performance Standards on Social and Environmental Sustainability (IFC Performance Standards). The purpose of IFC's Performance Standards is to provide a reference for businesses in emerging markets for environmental and social standards. It also includes a section on appropriate assessments and management systems to identify and address social and environmental risks with a view to ensure the continuous improvement of the sustainability performance of a business within the limits of its resources. IFC's Performance Standards have been adopted by most DFIs as well as by many commercial investors in emerging markets and are an underlying reference standard for the Equator Principles for project finance to emerging markets.

IFC Performance Standards from 2006 consist of the following:

Performance Standard 1	Social and Environmental Assessment and Management System
Performance Standard 2	Labour and Working Conditions
Performance Standard 3	Pollution Prevention and Abatement
Performance Standard 4	Community Health, Safety and Security
Performance Standard 5	Land Acquisition and Involuntary Resettlement
Performance Standard 6	Biodiversity Conservation and Sustainable Natural Resource Management
Performance Standard 7	Indigenous Peoples
Performance Standard 8	Cultural Heritage

The IFC intends to issue revised and updated Performance Standards in 2011. The drafting process is well underway.

Specific themes for further clarification in the proposed updates for 2011 include among others, climate change, ecosystem services, gender considerations and human rights. Operational topics that would receive additional clarification in the updated Performance Standards include consultation when working with indigenous peoples; clearer categorisation of risk and impact magnitudes; and guidance on governance and disclosure.

Links to the full text of the IFC Performance Standards can be found on IFC's website www.ifc.org

IFC categorisation of investments (projects)

The IFC classifies investments (projects) by the level of social and environmental impacts involved as per below. This is similar to the risk rating system described in *Tool 5* of this Toolkit.

- **Category A (high risk)**
  Projects with potential significant adverse social or environmental impacts that are diverse, irreversible or unprecedented.
- **Category B (medium risk)**
  Projects with potential limited adverse social or environmental impacts that are few in number, generally site-specific, largely reversible and readily addressed through mitigation measures.
- **Category C (low risk)**
  Projects with minimal or no adverse social or environmental impacts, including certain financial intermediary projects with minimal or no adverse risks.
- **Financial intermediary (FI)**
  All investments made through financial intermediaries excluding those that are Category C. Under the proposed updates, IFC is proposing to divide the current financial intermediary category into FI-High, FI-Medium and FI-Low to provide a greater indication of the risks involved when investing through financial intermediaries.

Financial intermediaries

As per the Performance Standards from 2006, the IFC ranks investments through financial intermediaries by assessing their entire investment portfolio to assess the level of risks. All financial intermediaries that receive capital from the IFC must adhere to IFC's exclusion list

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International ESG reference standards and conventions: 5.1 General

and national laws (see *Appendix 8*). In addition, financial intermediaries are required to apply the Performance Standards for investments in assets with significant risks (Category A / high risk).

Extractive industries and infrastructure projects

Specific requirements are applied to these industry sectors. See 5.1.2 IFC Environmental, Health and Safety (EHS) Guidelines.

The IFC Performance Standards

Summary

Performance Standard 1 covers: (i) integrated assessments to identify the social and environmental impacts, risks and opportunities of investments; (ii) community engagement through disclosure of investment-related information and consultation on matters that directly affect local communities; and (iii) management of social and environmental performance throughout the investment duration.

Performance Standards 2 to 8 establish requirements to avoid, reduce, mitigate or compensate for impacts on people and the environment from investments and to improve conditions where appropriate.

Performance Standard 1

Social and Environmental Assessment and Management System

Performance Standard 1 covers social and environmental assessments and appropriate management systems.

Its objectives are to:

- identify and assess the social and environmental impacts, both adverse and beneficial, of any potential investment (project);
- avoid, or where avoidance is not possible, minimise, mitigate, or compensate the adverse impacts on workers, affected communities and the environment;
- ensure that affected communities are appropriately engaged on issues that could potentially affect them; and
- promote improved social and environmental performance of companies through effective management systems.

Performance Standard 2

Labour and Working Conditions

Performance Standard 2 covers worker-management relationships.

Its objectives are to:

- establish, maintain and improve worker-management relationships;
- promote fair treatment, non-discrimination and equal opportunity of workers in compliance with national labour and employment laws;
- prohibit child labour and forced labour; and
- promote safe and healthy working conditions and protect and promote the health of workers.

Performance Standard 3

Pollution Prevention and Abatement

Performance Standard 3 covers business activities that lead to pollution of air, water and land that affect people and the environment at the local, regional and / or global level.

Its objectives are to:

- avoid or minimise adverse impacts on human health and the environment by avoiding or minimising pollution from business activities; and
- promote the reduction of emissions that contribute to climate change.

Performance Standard 4

Community Health, Safety and Security

Performance Standard 4 addresses a company's responsibility to avoid or minimise the risks and impacts to community health, safety and security that may arise from its activities.

Its objectives are to:

- avoid or minimise risks to and impacts on the health and safety of the local community from business activities; and
- ensure that the safeguarding of personnel and property is carried out in a legitimate manner that avoids or minimises risks to the local community's safety and security.

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Performance Standard 5

Land Acquisition and Involuntary Resettlement

Performance Standard 5 covers involuntary resettlement, which may result in long-term hardship and impoverishment for affected persons and communities, and cause environmental damage and social stress in areas to which they have been displaced.

Its objectives are to:

- avoid or at least minimise involuntary resettlement wherever feasible;
- mitigate adverse social and economic impacts from land acquisition or restrictions on affected persons' use of land by: (i) providing compensation for loss of assets at replacement cost; and (ii) ensuring that resettlement activities are implemented with appropriate disclosure of information, consultation and the informed participation of those affected;
- improve or at least restore the livelihoods and standards of living of displaced persons; and
- improve living conditions among displaced persons through provision of adequate housing with security of tenure at resettlement sites.

Performance Standard 6

Biodiversity Conservation and Sustainable Natural Resource Management

Performance Standard 6 covers the protection and conservation of biodiversity.

Its objectives are to:

- protect and conserve biodiversity; and
- promote the sustainable management and use of natural resources through the adoption of practices that integrate conservation needs and development priorities.

Performance Standard 7

Indigenous Peoples

Performance Standard 7 addresses the interests of indigenous peoples; social groups with identities that are distinct from the dominant groups in national societies who are often among the most marginalised and vulnerable segments of the population.

Its objectives are to:

- ensure that the development process fosters full respect for the dignity, human rights, aspirations, cultures and natural resource-based livelihoods of indigenous peoples;
- avoid adverse impacts of projects on communities of indigenous peoples, or when avoidance is not feasible, to minimise, mitigate, or compensate for such impacts, and to provide opportunities for development benefits, in a culturally appropriate manner;
- establish and maintain an on-going relationship with the indigenous people affected by business operations;
- foster good faith negotiation with and informed participation of indigenous peoples when projects are to be located on traditional or customary lands under use by the indigenous peoples; and
- respect and preserve the culture, knowledge and practices of indigenous peoples.

Performance Standard 8

Cultural Heritage

Performance Standard 8 covers cultural heritage matters.

Its objectives are to:

- protect cultural heritage from the adverse impacts of business activities and support its preservation; and
- promote the equitable sharing of benefits from the use of cultural heritage.

For the complete Performance Standards document, updates and news: www.ifc.org

IFC Performance Standards vs. local legislation

The IFC and the rest of the World Bank group have conducted studies to assess whether compliance with local legislation would result in lower standards than compliance with the IFC Performance Standards and other World Bank guidelines in various emerging market countries.

See www.worldbank.org and www.ifc.org

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International ESG reference standards and conventions:
5.1 General

Implications for fund managers

Fund managers that invest in assets with significant environmental and / or social risks have to be aware of differences between local legislation and the IFC Performance Standards and ensure that portfolio companies adhere to the higher standards or that improvements towards the high standards are made during the investment period.

Implications for companies

Companies with significant environmental and / or social risks should apply or work towards the IFC Performance Standards.

5.1.2 The IFC Environmental, Health and Safety Guidelines (2007)

Associated with the IFC Performance Standards are the World bank Group's general and industry specific Environmental, Health and Safety (EHS) Guidelines.

The EHS Guidelines are technical reference documents with general and industry-specific examples of good international industry practice.

Implications for fund managers

The industry-specific EHS Guidelines can be particularly useful as practical reference standards for fund managers, who may not have technical industry-specific expertise in-house, to understand how investee companies perform and what measures could be undertaken to improve environmental, health and safety matters.

Implications for companies

Companies in the industry sectors listed below should use the EHS Guidelines as reference standards for their operations.

The EHS Guidelines include the following industry sectors:

Forestry

- Board and particle-based products
- Sawmilling and wood-based products
- Forest harvesting operations
- Pulp and paper mills

Agribusiness / food production

- Mammalian livestock production
- Poultry production
- Plantation crop production
- Annual crop production
- Aquaculture
- Sugar manufacturing
- Vegetable oil processing
- Dairy processing
- Fish processing
- Meat processing
- Poultry processing
- Breweries
- Food and beverages processing

General manufacturing

- Cement and lime manufacturing
- Ceramic tile and sanitary ware manufacturing
- Glass manufacturing
- Construction materials manufacturing
- Textiles manufacturing
- Tanning and leather finishing
- Semiconductors and electronics manufacturing
- Printing
- Foundries
- Integrated steel mills
- Base metal smelting and refining
- Metal, plastic, rubber products manufacturing

Oil and gas

- Onshore oil and gas development
- Offshore oil and gas development
- Liquefied natural gas (LNG) facilities

Infrastructure

- Tourism and hospitality development
- Railways
- Ports, harbours and terminals
- Airports
- Airlines
- Shipping
- Gas distribution systems
- Toll roads
- Telecommunications

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- Crude oil and petroleum product terminals
- Retail petroleum networks
- Healthcare facilities
- Waste management facilities
- Water and sanitation

Chemicals

- Pharmaceuticals and biotechnology management
- Coal processing
- Natural gas processing
- Oleochemicals manufacturing
- Nitrogenous fertiliser manufacturing
- Phosphate fertiliser manufacturing
- Pesticides formulation, manufacturing and packaging
- Petroleum-based polymers manufacturing
- Petroleum refining
- Large volume petroleum based organic chemicals manufacturing
- Large volume inorganic compounds manufacturing and coal tar distillation

Mining Power

- Wind energy
- Geothermal power generation
- Electric power generation
- Thermal power

Within each of these sectors there are specific guidelines with relevant advice for each industry.

The full text of the IFC EHS Guidelines is provided at IFC's website: www.ifc.org

5.1.3 The IFC Environmental and Social Management Toolkit for Private Equity Funds (2010)

In 2010, the IFC issued an Environmental and Social Toolkit to assist managers of private equity funds in assessing and managing the environmental and social risks and opportunities associated with their investments. This Toolkit is consistent with *CDC's Toolkit on ESG for Fund Managers*.

Similarly to CDC's Toolkit, the IFC's Environmental and Social Toolkit is organised according to the stages of private equity investment (screening, appraisal of risk / opportunity, management and exit). It guides users through environmental and social considerations for each phase.

An on-line assessment engine allows users to generate project types appropriate to their requirements and pipeline. At each investment stage, the Toolkit generates a description of the matters to be addressed and provides relevant resources and document templates. The templates can be downloaded and are adaptable to allow the integration of different requirements.

The Toolkit is in a state of evolution. Industry sectors covered in 2010 by the assessment engine include agribusiness, chemicals, general manufacturing, infrastructure, mining, oil and gas, power and retail. For industry sectors with significant risks, specialist environmental and social impact assessments are required.

Implications for fund managers

The IFC's Toolkit provides resources for different industry types and investment / project phases, which can be downloaded as appropriate for a fund manager. This Toolkit can be used to complement *CDC's Toolkit on ESG for Fund Managers.*

Implications for companies

The environmental and social assessment engine provides guidelines on standards and reporting requirements.

For more information: www.estoolkit.com

International ESG reference standards and conventions: 5.1 General

5.1.4 The Equator Principles (2006)

The Equator Principles are a widely adopted financial industry benchmark for determining, assessing and managing social and environmental risks in project finance for emerging markets.

The Equator Principles build on and incorporate the IFC Performance Standards and the associated Environmental, Health and Safety (EHS) Guidelines.

Signatory institutions include global and local banks and other financial institutions which provide project finance to companies in emerging markets.

Implications for fund managers

Companies which have received project finance from banks that are signatories to the Equator Principles should have had these projects assessed for environmental and social risks. Projects receiving finance from these banks would need to adhere to the Equator Principles and the IFC Performance Standards if classified as high risk (A) or, as appropriate, medium risk (B).

Implications for companies

Companies backed by financial institutions that have signed up to the Equator Principles should adhere to the IFC Performance Standards, as relevant.

The Equator Principles (summary)

- **Principle 1** Review and categorisation

  To categorise projects for magnitude of potential environmental and social risks (using the IFC Performance Standards).

- **Principle 2** Social and environmental assessment

  To conduct an appropriate risk assessment and propose mitigation and management strategies.

- **Principle 3** Applicable social and environmental standard

  To ensure this assessment complies with the relevant IFC Performance Standards and associated EHS Guidelines.

- **Principle 4** Action plan and management system

  To prepare an action plan which addresses, describes and prioritises the findings from the assessment.

- **Principle 5** Consultation and disclosure

  To ensure appropriate consultation with affected communities and the release of appropriate information to the public.

- **Principle 6** Grievance mechanism

  To set up a system to facilitate resolution of concerns and grievances for local communities and other stakeholders.

- **Principle 7** Independent review

  To have an independent reviewer assess the project.

- **Principle 8** Covenants

  For all higher risk projects, the borrower will covenant:

  - to comply with host countries' environmental and social laws;
  - to comply with the action plan for the length of the project;
  - to provide reports on compliance on at least an annual basis; and
  - to decommission the facilities, if applicable, in accordance with an agreed plan.

- **Principle 9** Independent monitoring and reporting

  To appoint / retain external experts to verify projects information on a regular basis.

- **Principle 10** Reporting

  Each financial institution that is a signatory to the Equator Principles is to report publicly on its implementation of the Equator Principles at least annually.

For more information and a list of signatories: www.equator-principles.com

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International ESG reference standards and conventions: 5.1 General

5.1.5 The UN Global Compact (2000)

The UN Global Compact is a voluntary policy initiative based around ten principles in the areas of human rights, labour standards, the environment and anti-corruption. The UN Global Compact principles are derived from several core UN conventions:

- the Universal Declaration of Human Rights;
- the International Labour Organisation's Declaration on Fundamental Principles and Rights at Work;
- the Rio Declaration on Environment and Development; and
- the United Nations Convention against Corruption.

The UN Global Compact requests companies to embrace, support and enact a set of core values within their sphere of influence. By doing so, companies can help ensure that markets, commerce, technology and finance benefit economies and societies.

The UN Global Compact is a voluntary initiative. A participating company is expected to make the principles part of its strategy, culture and daily operations. In addition, the company is expected to advocate the UN Global Compact's principles publicly and to report annually to stakeholders on its progress in advancing them.

5

Implications for fund managers and companies

The UN Global Compact is the most widely recognised international principles for responsible and sustainable business practices and is fully consistent with CDC's Investment Code. Fund managers and `companies are encouraged to become signatories.

For more information: www.unglobalcompact.org

The UN Global Compact Principles

Human Rights

Principle 1 Businesses should support and respect the protection of internationally proclaimed human rights; and

Principle 2 make sure that they are not complicit in human rights abuses.

Labour Standards

Principle 3 Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining;

Principle 4 the elimination of all forms of forced; and compulsory labour;

Principle 5 the effective abolition of child labour; and

Principle 6 the elimination of discrimination in respect of employment and occupation.

Environment

Principle 7 Businesses should support a precautionary approach to environmental challenges;

Principle 8 undertake initiatives to promote greater environmental responsibility; and

Principle 9 encourage the development and diffusion of environmentally friendly technologies.

Anti-Corruption

Principle 10 Businesses should work against corruption in all its forms, including extortion and bribery.

For more information: www.unglobalcompact.org

5.1.6 The UN Global Reporting Initiative (2006)

The UN Global Reporting Initiative (GRI) is closely associated with the UN Global Compact. Its vision is to make disclosure on sustainability performance as comparable and commonplace as financial reporting and of comparable importance to an organisation's measure of success.

The GRI aims to provide a framework for transparent and accurate disclosure of sustainability information for any type of organisation or business.

The GRI reporting framework was developed after extensive consultations with businesses, civil society, labour organisations and professional institutions.

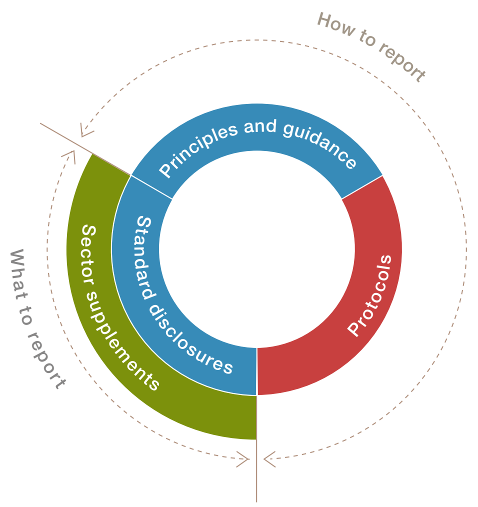
Sustainability reports based on the GRI framework can be used to benchmark organisational performance with respect to laws, norms, codes, performance standards and voluntary initiatives; demonstrate organisational commitment to sustainable development; and compare organisational performance over time.

The GRI reporting framework provides sustainability reporting guidelines and sets out principles and indicators that organisations and companies can use as relevant to measure and report on their performance from a sustainability perspective.

International ESG reference standards and conventions: 5.1 General

The GRI reporting framework also includes industry sector supplements and national annexes with country-level information.

GRI reporting framework



Implications for fund managers and companies

The UN GRI is the most widely recognised international sustainability reporting framework for businesses, and fully consistent with CDC's recommended reporting from fund managers. Fund managers and companies are encouraged to use it for their sustainability reporting.

For more information, including the GRI sustainability reporting guidelines, sector supplement and national annexes: www.globalreporting.org

5.1.7 The UN Principles for Responsible Investment (2006)

The UNPRI are voluntary and aspirational principles for actions to incorporate ESG issues into mainstream investment decision-making and investment management.

In 2010, UNPRI had almost 600 signatories representing asset owners, investment managers and professional services providers. Signatories to the UNPRI can access UNPRI guidance documents, share resources and consult with each other on the best solutions to particular ESG matters.

UNPRI Principles

1. We will incorporate ESG issues into investment analysis and decision-making processes.
2. We will be active owners and incorporate ESG issues into our ownership policies and practices.
3. We will seek appropriate disclosure on ESG issues by the entities in which we invest.
4. We will promote acceptance and implementation of the Principles within the investment industry.
5. We will work together to enhance our effectiveness in implementing the Principles.
6. We will report on our activities and progress towards implementing the Principles.

Implications for fund managers

Fund managers are encouraged to sign up to the UNPRI. UNPRI is complementary to CDC's Investment Code and the IFC Performance Standards, which provide specific ESG standards for implementing the high-level and aspirational UNPRI principles.

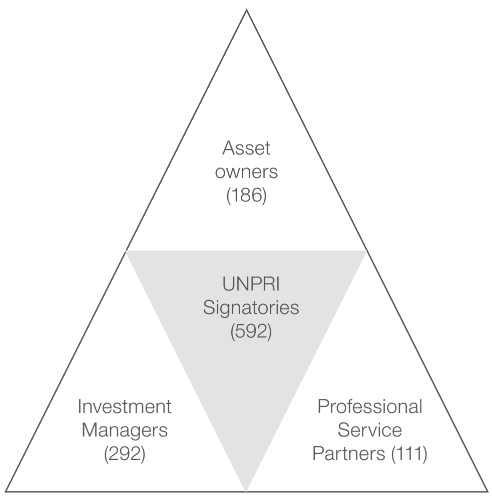
Implications for companies

Investors signed up to the UNPRI are committed to promote responsible ESG practices for their portfolio companies.

CDC became a signatory to UNPRI in 2009. Some of CDC's fund managers are also signatories.

For more information and a complete list of signatories: www.unpri.org

As per 2010, number of UNPRI signatories



Appendix 5

International ESG reference standards and conventions: 5.1 General

5.1.8 The US Private Equity Council Responsible Investment Guidelines (2009)

The US Private Equity Council provides responsible investment guidelines for its members to apply prior to making investments and during their period of ownership. The guidelines cover environmental, social and governance matters.

Implications for fund managers

The US Private Equity Council's Responsible Investment Guidelines have signatories including many of the world's largest and most reputable private equity fund managers. These guidelines are fully consistent with CDC's Investment Code. Fund managers are encouraged to apply these guidelines if they are members of the US Private Equity Council.

For more information: www.privateequitycouncil.org

The US Private Equity Council Responsible Investment Guidelines

1. Consider environmental, public health, safety and social issues associated with target companies when evaluating whether to invest in a particular company or entity, as well as during the period of ownership.
2. Seek to be accessible to, and engage with, relevant stakeholders either directly or through representatives of portfolio companies, as appropriate.
3. Seek to grow and improve upon portfolio companies for long-term sustainability and to benefit multiple stakeholders, including on environmental, social and governance issues. To that end, Private Equity Council members will work through appropriate governance structures (e.g. board of directors) with portfolio companies with respect to environmental, public health, safety and social issues, with the goal of improving performance and minimising adverse impacts in these areas.
4. Seek to use governance structures that provide appropriate levels of oversight in the areas of audit, risk management and potential conflicts of interest and to implement compensation and other policies that align the interests of owners and management.
5. Remain committed to compliance with applicable national, state, and local labour laws; support the payment of competitive wages and benefits to employees; provide a safe and healthy workplace in conformance with national and local law; and consistent with applicable law, respect the rights of employees to decide whether or not to join a union and engage in collective bargaining.
6. Maintain strict policies that prohibit bribery and other improper payments to public officials consistent with the U.S. Foreign Corrupt Practices Act, similar laws in other countries, and the OECD Anti-Bribery Convention.
7. Respect the human rights of those affected by investment activities and seek to confirm that investments do not flow to companies that utilise child or forced labour or maintain discriminatory policies.
8. Provide timely information to limited partners on the matters addressed herein, and work to foster transparency.
9. Encourage portfolio companies to advance these principles in a way which is consistent with fiduciary duties.

International ESG reference standards and conventions:
5.1 General

5.1.9 The EDFI Principles for Responsible Financing (2009)

EDFI is the association of the European Development Finance Institutions (EDFIs), a group of 16 bilateral investment organisations which provide finance to private sector companies in developing economies.

Below follows the full text of the EDFI Principles for Responsible Financing.

'Our aim is to have a positive impact on the local communities where we invest. We also strive to ensure respect for human rights and environmental sustainability. Responsibly managed companies, supported by EDFI members, play a vital part in environmental, social and economic development: they employ and train people, pay taxes, and build and operate infrastructure and services. Such businesses set an example for other companies. They also generate sustainable economic growth, which benefits the poor.

Our collaboration includes EDFI's harmonised ESG standards in relation to the environment, social matters and governance (ESG) in investment activities.[1,2]

The EDFI institutions[3]:

- Require that all our investee companies comply with the legal and regulatory requirements in the jurisdictions where they operate.
- Require high standards of business integrity and corporate governance[2] in our investee companies.
- Recognise that our decisions and activities may have environmental and social consequences and require our investee companies to work over time towards relevant international best practice norms and standards.[4] We aim to achieve full compliance with such norms and standards within the duration of our investments. We encourage our investee companies to promote the same standards throughout their supply chains, e.g. with their contractors.
- Ensure a preventative and precautionary approach with respect to the environmental and social impacts of our investee companies, giving high attention to the interests of affected people. If negative environmental or social impacts are unavoidable, they must be appropriately mitigated or compensated for.
- Encourage investee companies to establish an open dialogue with their stakeholders on the environmental and social impacts of their business activities.
- Commit to continuous improvements in the management of ESG matters. Our aim is always to enhance positive effects in relation to the environment, workers and all stakeholders.
- Provide transparent and accountable information on investment activities, while observing normal commercial confidentiality.'

For more information: www.edfi.eu

[1] Harmonised EDFI environmental and social standards encompass (a) environmental and social category definitions, (b) requirements for environmental and social due diligence, environmental and social contractual requirements and monitoring and (c) an exclusion list, all of which will be reviewed regularly.

[2] Governance standards such as stated in the DFI approach statement on good corporate governance adopted in 2007, refer to the structure and processes for the direction and control of companies.

[3] When investing through intermediaries such as financial institutions or funds, we require the intermediaries to implement systems to ensure adherence to our standards.

[4] Our benchmarks are the UN Declaration of Human Rights, the ILO Core Conventions and the IFC Performance Standards on Economic and Social Sustainability and associated Environmental, Health and Safety Guidelines.

Appendix 5

International ESG reference standards and conventions:
5.1 General

EDFI Environmental & Social (E&S) Guidelines for Fund Investments[1]

Objectives:	Funds where EDFI capital is invested should employ management systems which effectively address environmental and social (E&S) risks in portfolio companies and realise opportunities for improvements over the investment period as a fundamental part of a portfolio company's value. Special attention from the E&S perspective is required for funds that invest in companies in high risk sectors like (large scale) agribusiness, infrastructure (ports, large scale housing development), energy (including oil & gas exploitation), heavy industry or mining.[2]
EDFI practices: Assessment	As part of due diligence, the EDFI investment professional, if necessary assisted by a qualified expert, will assess the E&S management systems of a fund manager in relation to the risk level of the investment strategy. This assessment should review the E&S risk level of focus sectors, if any, the E&S risks and performance of existing portfolio companies, the portfolio of previous funds of the same manager with a similar investment strategy and/or the investment pipeline, and the capability of the fund manager to address adequately such risks and impacts.
Assistance	Where a fund manager's E&S management systems are assessed to be inadequate or not (yet) in place, EDFIs will assist the fund manager with advice, support and/or training.[3]
Monitoring	EDFIs will monitor the E&S performance of fund managers and their portfolio companies through reports, dialogue and visits.
E&S requirements for funds:[4]	1. Commit to an Investment Code on E&S prior to the first investment from an EDFI member. This Investment Code defines the principles, objectives, policies and management systems to be deployed by the fund manager.
Investment Code & Exclusion List	2. Apply EDFI's Exclusion List in selecting investees.
	3. Implement and maintain appropriate E&S management systems and assign E&S responsibilities to a designated representative of senior management and, where appropriate, to a suitably trained E&S officer.[5, 6]
Responsibilities	4. Assess the E&S impacts of all new investments as an integral part of the investment appraisal process, with reference to relevant laws and regulations and international standards, including the ILO Core Conventions and the IFC Performance Standards and IFC EHS Guidelines. For high risk investees, the IFC Performance Standards and IFC EHS Guidelines are the appropriate benchmark.
Assessment & risk rating	5. Categorise (potential) investees as high, medium or low risk using adequate instruments to determine the appropriate level of management and monitoring.
	6. For high risk investees, use a suitably qualified expert for the environmental and social assessment (impact assessment or audit with reference to IFC's Performance Standards and IFC EHS Guidelines).

[1] These guidelines reflect EDFI's harmonized environmental and social requirements for fund investments. EDFI members also integrate governance into their investment standards, guidelines and tools alongside environmental and social matters. Harmonized practice in this field is still evolving.

[2] EDFI will provide a harmonized list of high risk sectors (to be finalized).

[3] Many EDFI members have technical assistance facilities that can be used to support training and E&S management systems (ESMS) implementation.

[4] Guidance notes with suggestions on tools for and implementation of the EDFI E&S Guidelines for Fund Investments can be found at www.edfi.eu

[5] Suggestions for training can be found at www.edfi.eu

[6] If there is no suitable trained officer within the team, a fund manager can also mandate an external consultant or expert to take this role as long as there is a designated E&S representative of senior management of the fund manager. This representative is responsible for E&S aspects for the fund and for the assignment of any external consultant.

App 5

International ESG reference standards and conventions: 5.1 General

Improvements over time	7.	Agree with the investee on corrective action plans to address any identified shortcomings in relation to E&S matters.
Investment undertaking	8.	A fund manager shall not invest in a company if it has high E&S risks and/or significant E&S shortcomings if the fund manager cannot contractually bind or in other way demonstrate robust evidence that E&S risks are or will be addressed in an appropriate way. Where the fund manager has effective control or significant influence,[7] the fund manager shall contractually bind investees to comply with EDFI's E&S requirements[8] for investees and set up a monitoring system to ensure compliance.
Climate change	9.	Assess and support the reduction of carbon emissions for investees with significant CO_2 equivalent emissions (according to IFC Performance Standard 3, Pollution Prevention and Abatement).
Monitoring	10.	Monitor investees performance on environmental and social matters including their progress towards action plans and targets for improvements as well as any serious incidents. For high risk investees external monitoring is recommended.
Reporting	11.	Submit an annual E&S monitoring report in a format acceptable to EDFI members, including risk ratings for investees, issues, improvements and future targets.
	12.	Report serious incidents immediately, with plans for corrective actions and follow-up.
	13.	Make relevant E&S information available for EDFI members and assist with site visits upon request, e.g., for evaluation purposes.
E&S requirements for investees:	1.	Comply with all applicable local environmental, health & safety and labour laws and regulations.
	2.	Work over time to comply with relevant international standards, including the ILO Core Conventions and, for high-risk investees, the IFC Performance Standards and IFC EHS Guidelines.
	3.	In case of non-compliances with these requirements, commit to an action plan to address issues, with appropriate targets, responsibilities and timetable for improvements.
	4.	Adopt policies and commit to continuous improvements on E&S matters.
	5.	Report annually on E&S matters to the fund managers.
	6.	Report serious incidents immediately, with plans for corrective actions and follow-up.

Guidance notes

Please refer to the following documents for guidance and tools to implement the EDFI E&S Guidelines for Fund Investments:

CDC's Toolkit on ESG for Fund Managers 2010 www.cdcgroup.com

FMO's Private Equity Toolkit for Investment Funds www.fmo.nl

Guidance on how to assess carbon emission is given in IFC Guidance Notes. A practical tool for evaluating carbon emissions can be found on the website of AFD http://climatechange.afd.fr. Guidance for fund managers on how to manage risks associated with climate change is also available on CDC's website www.cdcgroup.com

For further information: www.edfi.eu

[7] A fund manager will be deemed to have significant influence over a portfolio company where its fund has (i) an ownership interest in the portfolio company in excess of 20%, which is presumed to be a level that allows for participation in the financial and operating policies of a portfolio company (if the percentage is lower but gives rise to the same participation, this will also meet the definition of significant influence); or (ii) board representation to a level that allows for participation in determining the financial and operating policies of the portfolio company; or (iii) rights to influence the financial and operating policy decisions of the portfolio company pursuant to a shareholders' or similar agreement.

[8] For funds with a portfolio of SMEs (low risks), compliance with local laws could be sufficient if these are satisfying for the EDFI investor.

Appendix 5

International ESG reference standards and conventions: 5.2 The Environment

5.2.1 The Montreal Protocol (1999)

The Montreal Protocol was designed to protect the ozone layer by banning and phasing out the production and use of substances that are harmful to it. It has been ratified by almost every country in the world.

Developed and developing nations have different bans, phase-out and reduction requirements.

Substances covered by the Montreal Protocol, their uses, applicable industry sectors, and the timeframe for phase out for developed and developing countries are outlined in the table below.

Implications for fund managers

CDC's exclusion list prohibits fund managers that invest CDC's capital from investing in businesses that produce or use ozone depleting substances as covered by the Montreal Protocol.

Implications for companies

Companies with capital from CDC are prohibited from production or use of ozone depleting substances banned by the Montreal Protocol.

For more information: www.ozone.unep.org

Substance	Uses	Reduction requirements: developed countries	Reduction requirements: developing countries
Chloroflurocarbons (CFCs)	Food packaging Refrigerant Aerosol propellant	Phased-out 1995	Phase-out 2010
Halons	Fire fighting agents	Phased-out 1993	Phase-out 2010
Carbon tetrachloride	Dry cleaning agent Fire fighting equipment Refrigerant	Phased-out 1995	Phase-out 2010
Methyl chloroform	Solvent (metal cleaning) Photographic film cleaning Aerosol propellant	Phased-out 1995	Phase-out by 2015
Hydrochloroflurocar-bons (HCSCs)	Refrigerant	Begin phase-out by 1996, 75% reduction by 2010, 90% reduction by 2015, total phase-out by 2020	Freeze starting 2013: base level calculated as 2009 levels, 10% reduction by 2015, 35% reduction by 2020, 67.5% reduction by 2025, total phase-out by 2030.
Methyl bromide	Pesticide	Phased-out 2005	Freeze in 2002 at 1995-1998 levels, 20% reduction by 2005, total phase-out by 2015
Bromochloromethane	Aerosol propellant	Phased-out 2002	Phased-out 2002

International ESG reference standards and conventions: 5.2 The Environment

5.2.2 The UN Framework Convention on Climate Change (1994)

Over a decade ago, most countries joined the United Nations Framework Convention on Climate Change to begin to consider what can be done to reduce global warming. In 2005, a number of countries adopted more powerful and legally binding measures through the Kyoto Protocol.

5.2.2.a The Kyoto Protocol (2005)

The Kyoto Protocol on the reduction of carbon emissions sets binding commitments for 37 industrialised nations and the European Union for reducing greenhouse gas (GHG) emissions. The agreed reductions amount to an average of five percent compared to 1990 levels to be achieved over the period 2008 to 2012.

The Kyoto Protocol offers three means of meeting reduction targets: emissions trading, the clean development mechanism (CDM) and joint implementation.

5.2.2.b The Copenhagen Accord (2009)

In December 2009, the Copenhagen Summit on Climate Change was held with the objective for countries to reach agreements on climate change mitigation. No legally binding outcome was agreed at the summit, nor were new global GHG emission reduction targets established. However, several important issues were 'taken note of' by participants. These included:

- a recognition of the scientific case for keeping global temperature rises beneath 2°C with a review in 2015;
- a pledge of funding of US$30 billion to developing countries to help mitigate climate change over the 2010 – 2013 period, with the goal of mobilising US$100 billion by 2020;
- new market incentives from developed countries to developing countries to reduce emissions from deforestation and degradation (REDD+); and
- the establishment of the Copenhagen Green Finance Fund to promote emission reductions.

Implications for fund managers

Fund managers should assess, monitor and seek to reduce GHG emission from their portfolio companies. See *Appendix 9* for further guidance.

Implications for companies

Companies should develop strategies to reduce their GHG emissions. See *Appendix 9* for further guidance.

For more information: www.unfccc.int

Appendix 5

International ESG reference standards and conventions: 5.2 The Environment

5.2.3 The Stockholm Convention (2004)

Persistent organic pollutants (POPs) are chemicals that do not degrade easily and whose residue can remain in soil, water and plants for decades after initial use. In humans, POPs are known to cause cancers, birth defects and reproductive problems. A list of the chemicals classified as POPs is provided below.

The Stockholm Convention commits ratifying governments to protect human health and the environment by reducing and where feasible, eliminating the production and environmental release of POPs. Stockpiles must be disposed of in an appropriate and environmentally sound manner.

Type	Fungicides, herbicides, insecticides and pesticides	Industrial chemicals	Bi-products of other processes
Names	Aldrin Dieldrin Chloradane Endrin Heptachlor Toxaphene DDT[1] Hexachlorobenzene Mirex Chlordecone Alpha hexachlorocyclohexane Beta hexachlorocyclohexane Lindane Pentachlorobenzene	Polychlorinated biphenyls (PCBs)[2] Hexachlorobenzene Hexabromodiphenyl Hexabromodiphenyl ether Heptabromodiphenyl ether Pentachlorobenzene Perfluorooctanesulfonic acid and its salts Perfluorooctane sulfonyl fluoride Tetrabromodiphenyl ether Pentabromodiphenyl ether	Polychlorinated biphenyls (PCBs)[2] PCDD/PCDF Alpha hexachlorocyclohexane Beta hexachlorocyclohexane Pentachlorobenzene
Uses	Agriculture	Electrical transformers	Waste incineration Chemical and fertiliser manufacture

Implications for fund managers

CDC's exclusion list prohibits fund managers from investing CDC's capital in businesses that produce or use products containing POPs. The risks are greater in countries that have not ratified the Stockholm Convention as per the map overleaf.

Implications for companies

Companies with capital from CDC are prohibited from production or use of POPs.

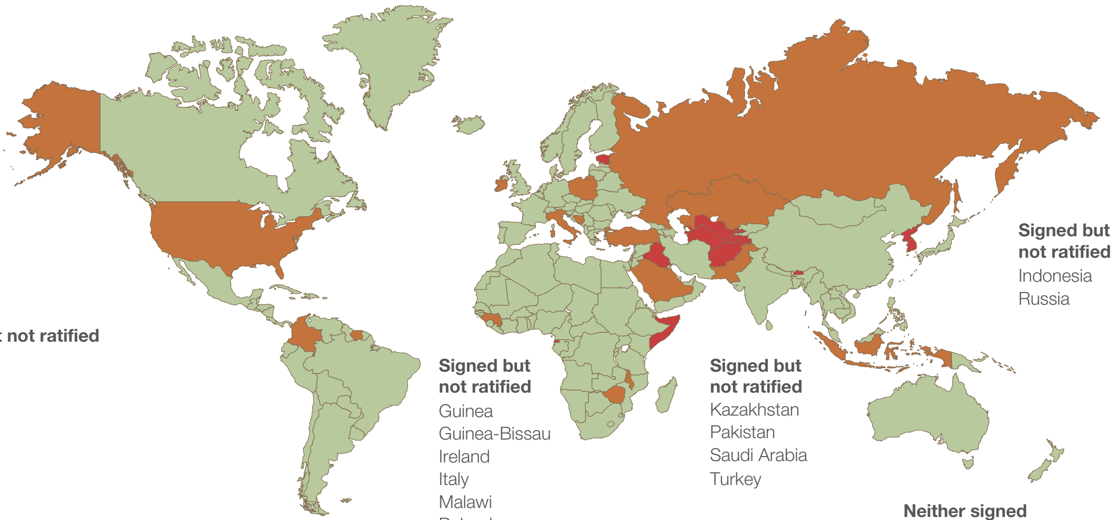
For more information: www.pops.int

[1] DDT may be used with WHO approval to combat malaria with limited and restricted interior spraying until DDT can be replaced with better alternatives.

[2] Any electrical transformers in use which contain PCBs must be phased out by 2025.

International ESG reference standards and conventions: 5.2 The Environment

Ratifications to the Stockholm Convention on persistent organic pollutants



Signed but not ratified
Colombia
Suriname
Tonga
USA

Signed but not ratified
Guinea
Guinea-Bissau
Ireland
Italy
Malawi
Poland
Serbia
Zimbabwe

Neither signed nor ratified
Equatorial Guinea
Estonia
Somalia

Signed but not ratified
Kazakhstan
Pakistan
Saudi Arabia
Turkey

Neither signed nor ratified
Afghanistan
Bhutan
Iraq

Signed but not ratified
Indonesia
Russia

Neither signed nor ratified
North Korea
Timor Leste
Turkmenistan
Uzbekistan

- Neither signed nor ratified
- Signed but not ratified
- Signed and ratified

Appendix 5

International ESG reference standards and conventions: 5.2 The Environment

5.2.4 The Rotterdam Convention (2004)

The Rotterdam Convention on the prior informed consent procedure for hazardous chemicals in international trade deals with information sharing for hazardous chemicals during international trade, including appropriate labelling and handling. The process covered by the Rotterdam Convention is called a prior informed consent mechanism. In 2010, the Rotterdam Convention specified 40 chemicals as hazardous, the bulk of which are subject to bans in a number of countries on health and environmental grounds. This list included 29 pesticides (including 4 severely hazardous pesticides) and 11 industrial chemicals.

Implications for fund managers

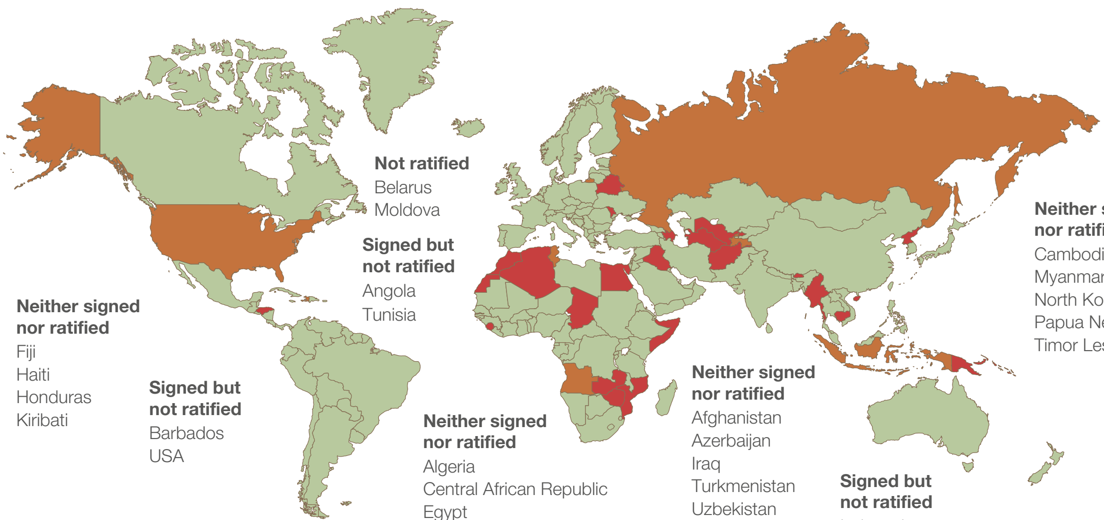
CDC's exclusion list does not permit investment in business or activities that do not adhere to the Rotterdam Convention. Fund managers that invest in sectors that make use of chemicals covered by the Rotterdam Convention should watch for inappropriate use and ensure that the prior informed consent mechanism specified by the Rotterdam Convention is adhered to. This is particularly important for investments in countries that have not ratified the Rotterdam Convention.

Implications for companies

Companies should ensure that chemicals listed under the Rotterdam Convention are traded according to its specifications.

For more information and a list of all chemicals covered by the Rotterdam Convention: www.pic.int

Ratifications to the Rotterdam Convention on the prior informed consent procedure for hazardous chemicals in international trade



International ESG reference standards and conventions: 5.2 The Environment

5.2.5 The Basel Convention (1992)

The Basel Convention on the control of trans-boundary movements of hazardous wastes aims to ensure that any hazardous wastes produced or generated are disposed of in a transparent and environmentally sound manner, as close as possible to the source of waste generation. The Basel Convention is intended to prevent the dumping of hazardous wastes in countries with lower environmental standards, notably many developing countries. The Basel Convention also calls for production of hazardous wastes to be kept to a minimum.

Hazardous wastes are defined by the Basel Convention as wastes which are explosive, flammable, toxic or corrosive. Also covered by the Basel Convention are those substances that are proscribed as hazardous by the laws of either the importing or the exporting country.

Implications for fund managers

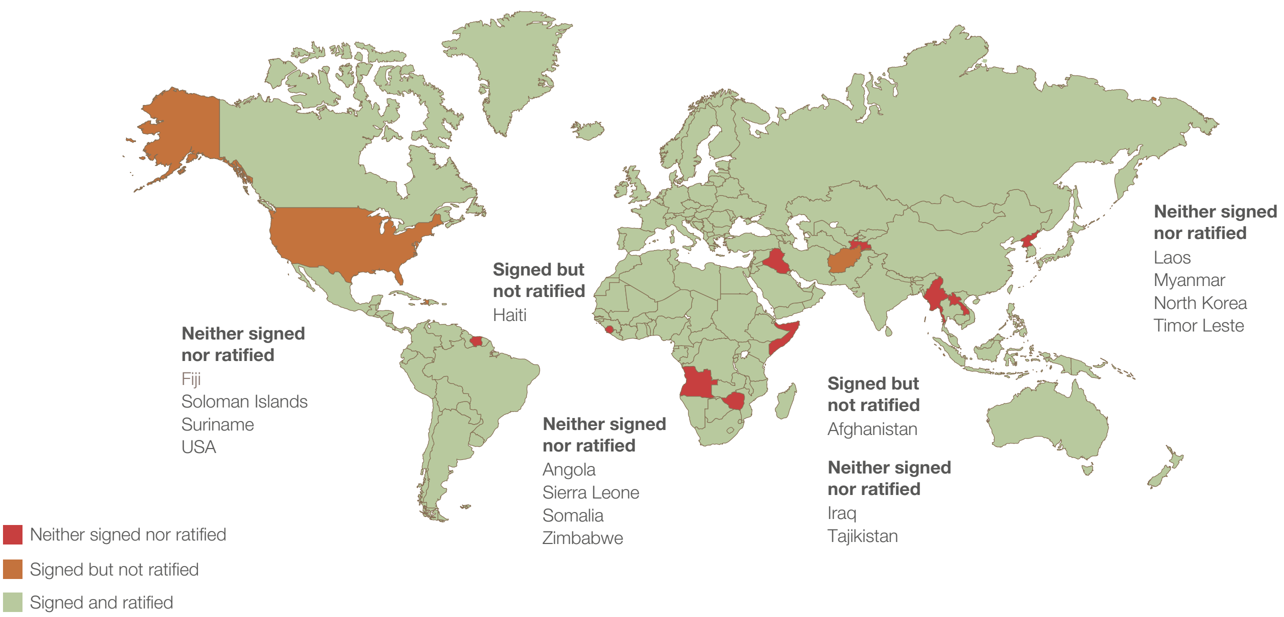
CDC's exclusion list does not permit investment in business or activities that do not adhere to the Basel Convention. It is the responsibility of the fund managers to ensure that any portfolio company whose operations involve hazardous wastes dispose of these in a safe manner, in accordance with the Basel Convention.

Implications for companies

Companies should ensure that they develop procedures and means for the safe disposal of hazardous waste.

For more information: www.basel.int

Ratifications to the Basel Convention on the control of trans-boundary movements of hazardous waste



Appendix 5

International ESG reference standards and conventions: 5.2 The Environment

5.2.6 The Convention on International Trade in Endangered Species of Wild Flora and Fauna (1973)

The Convention on International Trade in Endangered Species of Wild Flora and Fauna (CITES) is designed to ensure that international trade in specimens of wild animals and plants does not threaten their survival. Over 25,000 plants and 5,000 animals, that are considered to be threatened, were covered by CITES in 2010.

Trade in species threatened with extinction is prohibited by CITES. This includes trade in furs and dried plants.

Trade in species near extinction is regulated by CITES. Certificates and / or permits are required for the import, export and re-export of species listed as near extinction by CITES.

Implications for fund managers

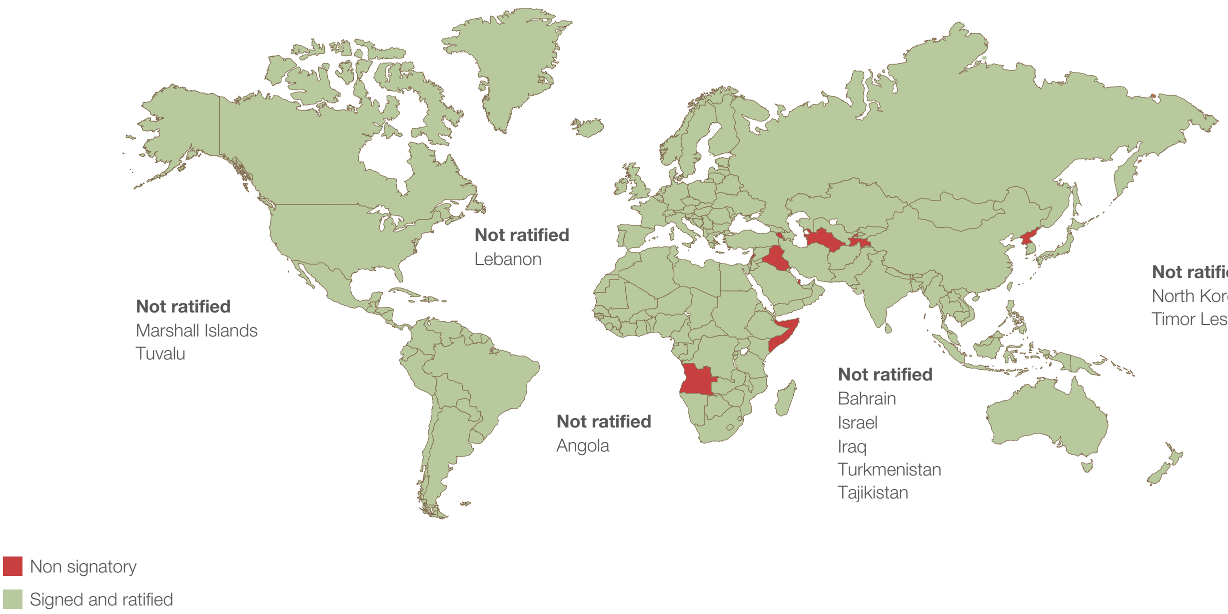
As per CDC's exclusion list, fund managers are not permitted to invest CDC's capital in any business that trade in species listed under CITES.

Implications for companies

Companies should ensure that their business does not involve any international trade in species listed under CITES.

For more information: www.cites.org

Ratifications to the Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES)



International ESG reference standards and conventions: 5.2 The Environment

5.2.7 The International Standards Organisation Standards

The International Standards Organisation (ISO) is the world's largest developer and publisher of standards. It is a non-governmental organisation with 162 members worldwide, including most countries.

ISO has published numerous standards including the following:

- **themes:** product quality, environment, safety, reliability, efficiency, interchangeability, distribution, transport, good management practice and services; and
- **sectors:** agriculture, construction, mechanical engineering, manufacturing, medical devices, information and communication technologies. good management practices and services.

ISO standards are developed on a consensus basis by panels and consultative groups composed of international experts. They are reviewed for relevance every 5 years. The ISO standards are voluntary, but can be integrated into national law or become a market requirement.

Implications for fund managers and companies

Relevant ISO standards can be used as a guide to good international practice. Certain key ISO standards are described below.

5.2.7.a ISO 9000

ISO 9000 are international standards for quality management systems covering the key processes of a business including:

- monitoring to ensure processes are effective;
- adequate record keeping;
- checking output for defectives and taking corrective action where necessary; and
- regular reviews of processes for effectiveness and to identify areas for improvement.

5.2.7.b ISO 14000

ISO 14000 are international standards for environmental management.

ISO 14001 specifies guidelines and standards for environmental management systems for businesses. ISO 14001 is designed to target those environmental impacts which the company can control. The ISO 14001 management system includes guidance on how to formulate a policy, the implementation and operation of such a policy, assessments and the formulation of corrective action plans and periodic management reviews.

ISO 14064 on greenhouse gas emissions (GHG) specifies principles and requirements at company level for quantifying and reporting on GHG emissions.

ISO 14065 specifies the accreditation requirements for organisations that validate GHG emission declarations made under IS0 14064.

Implication for fund managers and companies

Fund managers and companies should consider implementing the ISO standards for their operations, both in terms of quality management (ISO 9000) and environmental management (ISO 14001), as well as for their greenhouse gas emissions (ISO 14064-65).

For more information: www.iso.org

Appendix 5

International ESG reference standards and conventions: 5.3 Social matters

5.3.1 ILO Fundamental Conventions

The most basic labour rights have been codified by the International Labour Organization (ILO) in the 1998 Declaration on Fundamental Principles and Rights at Work. The declaration identified eight ILO conventions as fundamental to the rights of persons at work, irrespective of the level of development of a country. These 'core labour standards' cover four main areas, with two ILO conventions associated with each one:

- the elimination of all forms of forced or compulsory labour;
- the effective abolition of child labour;
- the elimination of discrimination in respect of employment and occupation; and
- the freedom of association and the effective recognition of the right to collective bargaining.

The ILO Declaration on Fundamental Principles and Rights at Work declares that all ILO member states, whether they have ratified the relevant conventions or not, have an obligation due to their membership in the ILO to respect, promote and realise the fundamental rights which are the subject of those conventions.

Implications for fund managers and companies

The ILO core labour standards have to be applied by all fund managers investing CDC's capital and by all portfolio companies.

5.3.1.a The elimination of all forms of forced or compulsory labour: ILO Conventions 29 and 105

ILO Conventions 29 and 105 concern abolishing the use of forced or compulsory labour in all its forms. Convention 105 clarifies Convention 29 and applies it to specific defined acts of forced labour.

ILO Convention 29: Forced or compulsory labour (1930)

The aim of ILO Convention 29 is to abolish the use of forced or compulsory labour in all forms. Compulsory labour is defined as labour that is non voluntary and exacted under the threat of penalty.

Exclusions may be possible in certain limited circumstances: compulsory military service, civic obligations (e.g. jury service), community work or work under the public authority resulting from a court conviction or emergency labour in the event of natural disaster.

ILO Convention 105: Abolition of forced labour (1957)

ILO Convention 105 prohibits any form of forced or compulsory labour (defined under ILO Convention 29) as a means of:

- political coercion, education or punishment or discrimination against those opposed to the political or economic system;
- mobilising labour for economic development; or
- as punishment for participating in strikes.

Implications for fund managers

Watch for the use of any form of forced labour in portfolio companies. Any form of forced labour, apart from the exceptions listed in ILO Convention 29, is prohibited. Particular care should be taken if a company employs migrant labour, especially if the practice is to store such workers' identification papers during the work period. Fund managers should monitor these conventions with particular care in China, Afghanistan, Laos, Malaysia and Vietnam, as these countries have not signed either convention, as well as in countries which have ratified the conventions but where local law enforcement is weak.

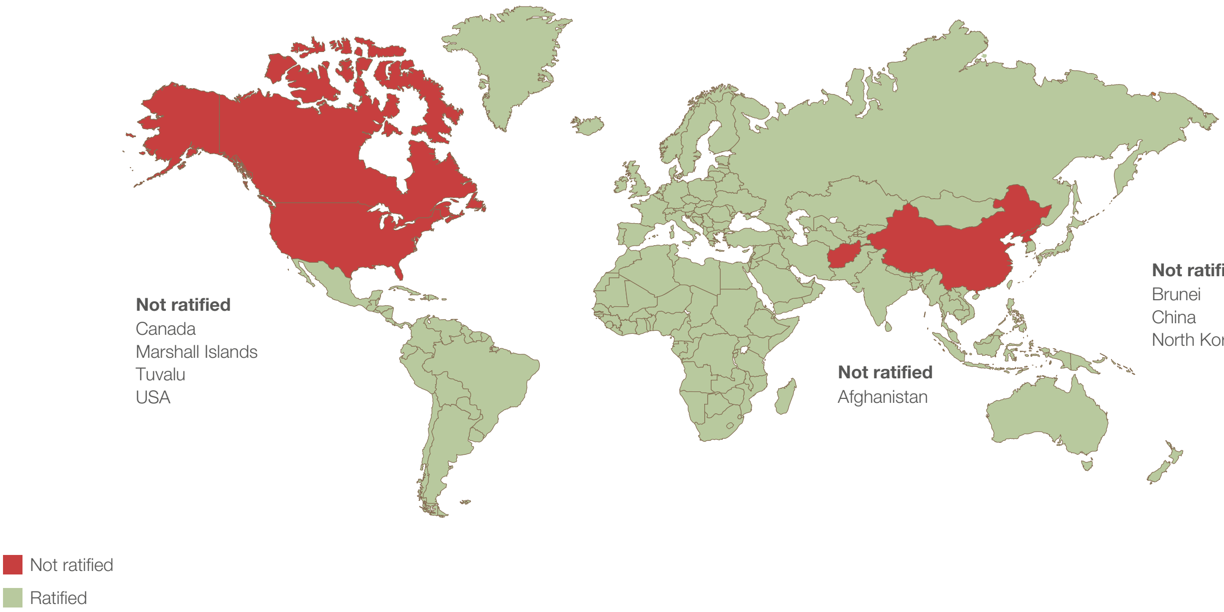
Implications for companies

Companies should ensure that their business operations do not use workers under conditions that could be defined as forced labour, and ensure that any use of prison labour does not constitute forced labour.

For more information: www.ilo.org

International ESG reference standards and conventions:
5.3 Social matters

Countries that have ratified ILO Convention 29: Forced or compulsory labour



Countries that have ratified ILO Convention 105: Abolition of forced labour

Appendix 5

International ESG reference standards and conventions: 5.3 Social matters

5.3.1.b Abolition of child labour: ILO Conventions 138 and 182

ILO Conventions 138 and 182 aim to establish a minimum age for employment and to protect children and young persons from inappropriate and harmful work.

ILO Convention 138: Minimum age for admission to employment (1973)

ILO Convention 138 aims to raise the minimum age for employment to a level consistent with the full physical and mental development of young persons.

The minimum age for entry into the workforce is defined as 15 years. This can be 14 years as a transitional measure in countries where educational facilities and the economy are significantly underdeveloped.

For work that may jeopardise the health, safety or morals of employees, the minimum working age is 18 years.

ILO Convention 182: Prohibiting the worst forms of child labour (1999)

ILO Convention 182 defines a child as a person under the age of 18 and prohibits activities deemed as the 'worst forms of child labour'.

The 'worst forms of child labour' are defined as:

- slavery, including the sale or trafficking of children, debt bondage, serfdom, forced or compulsory labour including armed conflict;
- prostitution or pornography;
- drug production and trafficking; or
- any work likely to harm the health, safety or morals of a child as set out by national laws and regulations.

Implications for fund managers

Watch for the use of any child labour in portfolio companies. In non-ratifying countries, where there may not be a legal national minimum working age, the age limits set by ILO Convention 138 must nevertheless be respected. Be aware also that ratifying countries may not enforce minimum working age laws. Be particularly mindful of the worst forms of child labour and risks for child labour in low skilled / low wage sectors such as agriculture, textiles, mining and some manufacturing.

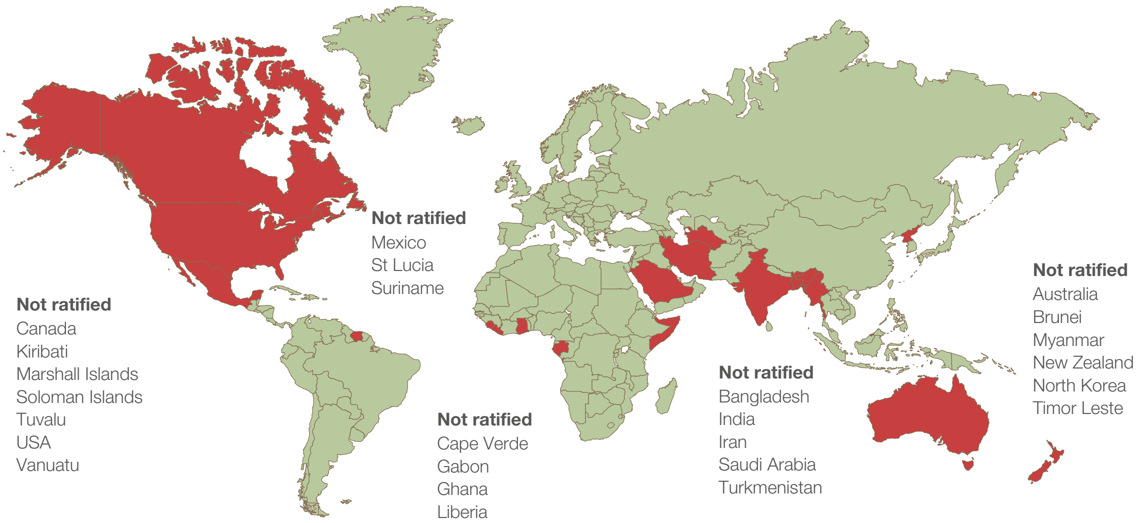
Implications for companies

Companies should ensure that the business does not employ workers under the age specified by ILO Convention 138.

For more information: www.ilo.org

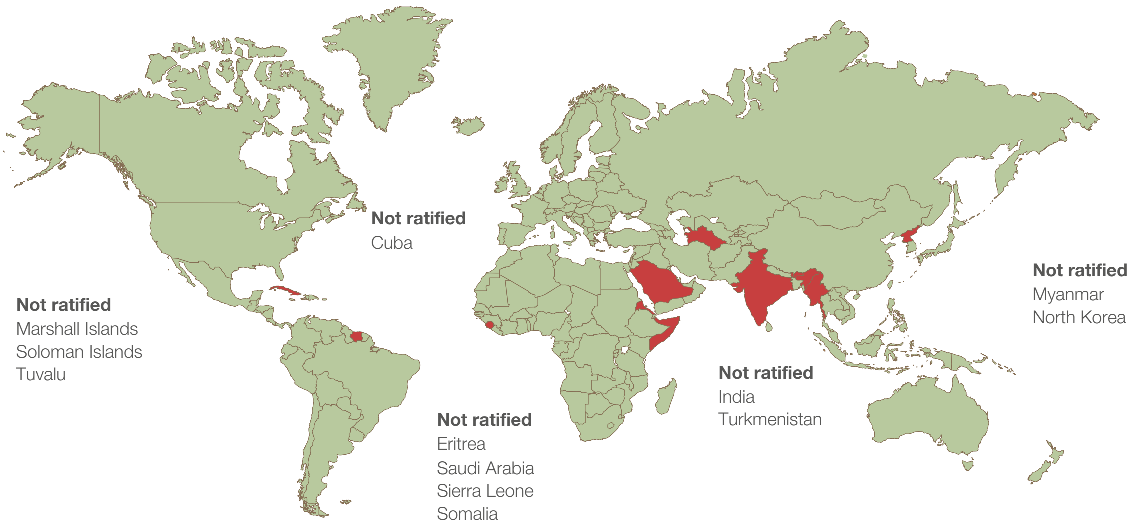
International ESG reference standards and conventions:
5.3 Social matters

Countries that have ratified ILO Convention 138: The minimum age for work



Not ratified
Ratified

Countries that have ratified ILO Convention 182: The worst forms of child labour



Not ratified
Ratified

Appendix 5

International ESG reference standards and conventions: 5.3 Social matters

5.3.1.c Elimination of discrimination in respect of employment and occupation: ILO Conventions 100 and 111

ILO Conventions 100 and 111 concern workers' rights to equal treatment in the workplace. Convention 100 aims to ensure equal pay for work of equal value. Convention 111 aims to eliminate discrimination on any grounds in the workplace.

ILO Convention 100: Equal remuneration (1951)

ILO Convention 100 aims to ensure the application of the principle of equal pay for women and men for work of equal value.

Remuneration is defined within the convention as ordinary, basic or minimum wage or salary and additional compensation arising out of employment.

Implications for fund managers

Watch for pay inequalities and indirect forms of discrimination against women in particular in portfolio companies, which should not be permitted. Job evaluations may be needed.

Implications for companies

Companies have to remunerate all men and women equally for work of equal value.

For more information: www.ilo.org

5

Countries that have ratified ILO Convention 100: Equal remuneration

International ESG reference standards and conventions:
5.3 Social matters

ILO Convention 111: Elimination of discrimination in respect of employment and occupation (1958)

ILO Convention 111 aims to ensure equality of opportunity and treatment and to eliminate discrimination in employment and occupation. Employment includes vocational training.

Discrimination is defined as distinction, exclusion or preference made on the basis of race, colour, sex, religion, political opinion, or social origin. Discrimination based on job requirements or on skills and competencies are not regarded as prohibited discrimination. The principle of non-discrimination applies to recruitment, retention, job assignment, promotion, training, pay, benefits and social protection.

Implications for fund managers

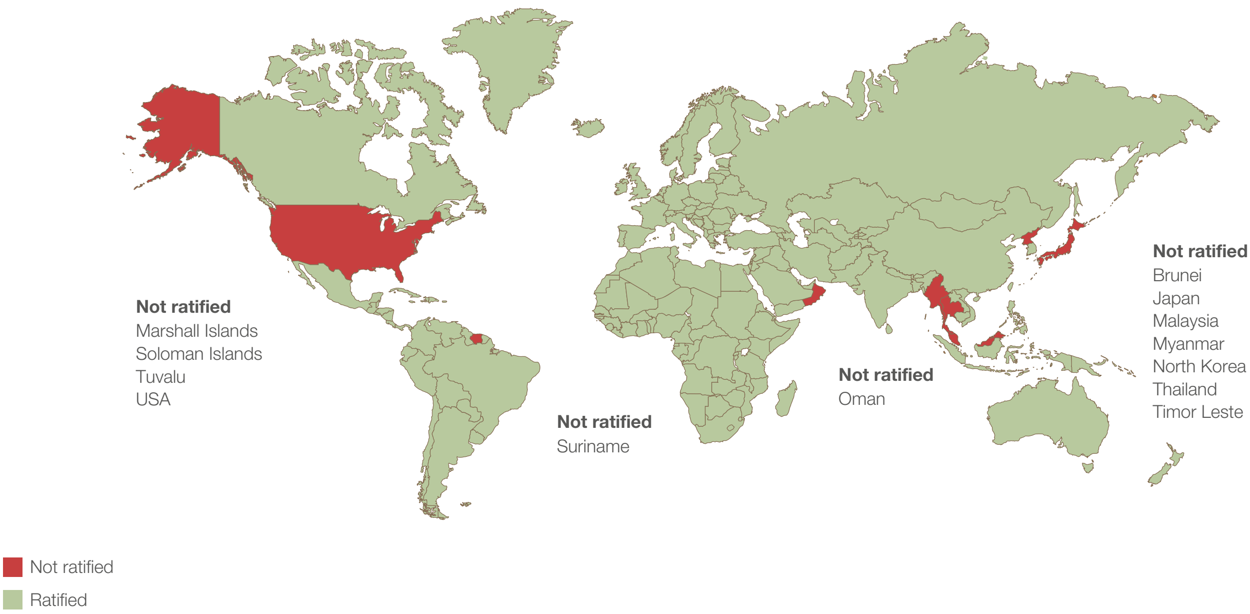
Watch for inequality and discrimination in portfolio companies on grounds of race, colour, sex, religion, political opinion, social origin, or any basis other than skills and competencies, which should not be permitted.

Implications for companies

Companies should not be permitted to discriminate between any workers on grounds other than skills and competencies. Allowable distinctions should be carefully circumscribed.

For more information: www.ilo.org

Countries that have ratified ILO Convention 111: Elimination of discrimination in respect to employment and occupation



Appendix 5

International ESG reference standards and conventions: 5.3 Social matters

5.3.1.d Freedom of association and the right to collective bargaining: ILO Conventions 87 and 98

ILO Conventions 87 and 98 concern the right of a workforce to organise and establish vehicles for collective rights (unions). ILO Convention 87 establishes the right of employees to form collective groups whilst ILO Convention 98 protects these groups from discrimination.

ILO Convention 87: Freedom of association and the protection of the right to organise (1948)

Under ILO Convention 87, workers and employers have the right to establish organisations of their choosing without prior authorisation and to run such organisations without external interference.

'Organisation' for the purpose of this convention is defined as a group of workers or employers collaborating to further and defend their respective interests.

ILO Convention 98: Right to organise and collective bargaining (1949)

ILO Convention 98 protects workers against acts of anti-union discrimination. It encourages the development and utilisation of collective bargaining mechanisms and consultative structures for the terms and conditions of employment.

Implications for fund managers

Watch for businesses not accepting workers' right to organise themselves independently of management. In some countries, which have not ratified ILO Conventions 87 and 98, non-state sanctioned unions may be illegal. Also in countries that have ratified ILO Conventions 87 and 98, unions may be discouraged or even prohibited. Fund managers must ensure that the workers in their portfolio companies have means to be able to express their views to management collectively.

Implications for companies

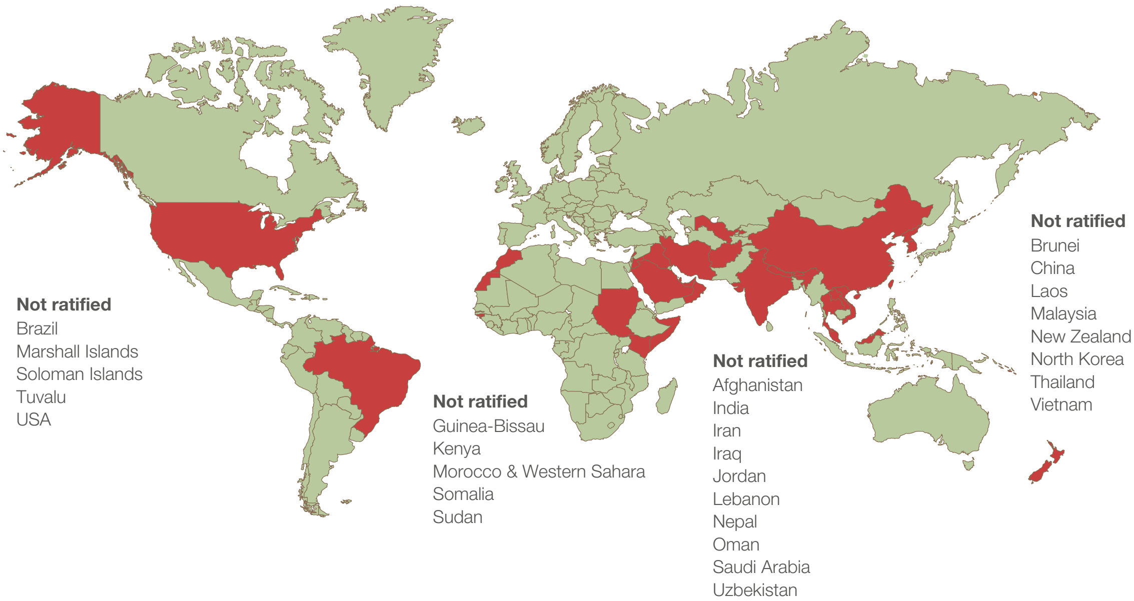
The representatives of workers should be chosen by them alone, accountable only to their members and free from any interference. Companies should be aware of workers' rights to form employee organisations and not interfere with such processes. Companies should provide facilities for workers to organise themselves (e.g. access for union representatives, office space and reasonable time to organise) but refrain from any active or participatory role in the formation or running of worker organisations.

For more information: www.ilo.org

International ESG reference standards and conventions:

5.3 Social matters

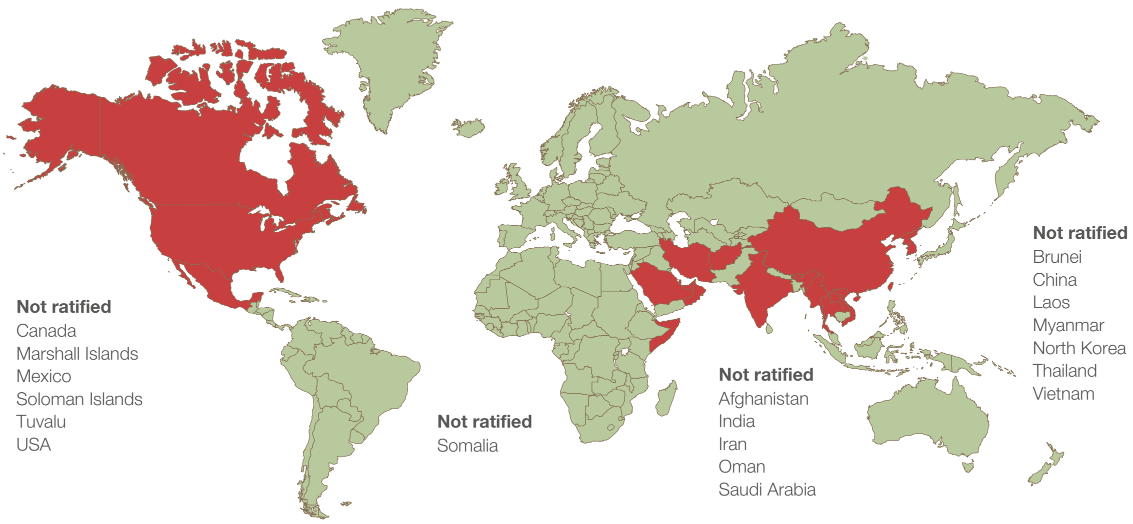
Countries that have ratified ILO Convention 87: Freedom of association and protection of the right to organise



Not ratified

Ratified

Countries that have ratified ILO Convention 98: Right to organise and collective bargaining



Not ratified

Ratified

Appendix 5

International ESG reference standards and conventions: 5.3 Social matters

5.3.2 ISO 26000 (2010)

The new ISO 26000 standard provides guidance on social responsibility and on ways of integrating socially responsible behaviour into existing organisational strategies, systems, practices and processes. ISO 26000 emphasises the importance of results and improvements in social responsibility performance.

ISO 26000 provides guidance to both public and private organisations on issues including:

- concepts, terms, core definitions and issues related to social responsibility;
- principles and practices relating to social responsibility;
- integrating, implementing and promoting socially responsible behaviour throughout an organisation and through its policies and practices within its sphere of influence;
- identifying and engaging with stakeholders; and
- communicating information, commitments and performance related to social responsibility.

ISO 26000 does not proscribe requirements for a management system although it can be incorporated into existing management systems. ISO 26000 is not intended for certification purposes or regulatory or contractual use.

Implications for fund managers

ISO 26000 can be used to guide and augment a fund manager's existing understanding and management systems which address corporate social responsibility.

Implications for companies

ISO 26000 can be used by companies of all sizes as a guide to good industry practice with respect to corporate social responsibility. Guidance is also provided in ISO 26000 on how best to identify and communicate with stakeholders.

For more information: www.iso.org

5.3.3 The Occupational Health and Safety Assessment Series (OHSAS) 18000

The OHSAS 18000 series is the most widely used standard for occupational health and safety management. It was first developed in 1999 as a result of consultations between 42 different organisations from 28 countries.

OHSAS 18001 has been developed by the British Standards Institution in response to consumer demand for a recognised, assessable and certifiable management system for health and safety. The OHSAS 18001 specifies key elements for management systems: policy, planning, implementation and operation, assessments, development of corrective action plans and management reviews. OHSAS 18001 is currently used in over 82 countries and by 16,000 organisations.

The purpose of OHSAS 18001 is to help organisations manage and control their occupational health and safety issues by providing a framework to implement an occupational health and safety management system. OHSAS 18001 requires a company to:

- investigate the health and safety risks related to its activities, products and services;
- evaluate and control those risks; and
- continually seek to improve its OHS performance.

Implications for fund managers and companies

The OHSAS 18001 management system can be implemented by fund managers and companies as an internationally recognised management system on occupational health and safety. OHSAS 18001 is compatible with both ISO 9001 (quality) and ISO 14001 (environmental management systems) and is closely modelled upon ISO 14001.

International ESG reference standards and conventions: 5.3 Social matters

5.3.4 Good manufacturing practices in the production of food and pharmaceuticals

Good manufacturing practices (GMP) for the production of pharmaceuticals are devised by the World Health Organization (WHO) through expert panels and working groups composed of WHO member states' representatives. GMP standards for food products and pharmaceuticals are also developed by the United States Food and Drug Administration (FDA) and collectively through collaboration by the relevant authorities from the European Union's member countries. The US and EU GMP standards have the power of law for production and sales in these countries.

GMP regulations require a safe approach to manufacturing, whereby companies minimise or eliminate instances of contamination, mix-ups, and errors. The consumer is thus protected from purchasing a product which is not effective or even dangerous. Failure of firms to comply with GMP regulations, where these are required, can result in very serious consequences for companies including recall, seizure, fines, and imprisonment of management. Adherence to WHO GMP and / or the stricter standards of US FDA or EU GMP, on the other hand, for production in countries where such standards are not required can allow manufacturers in emerging markets expanded access to sell their products in other countries, at higher prices.

The philosophy underlying the GMP standards is that they make business sense. By guaranteeing the manufacturing standards of a product, its attractiveness is increased to a broader range of markets and customers than before. This is particularly true in the pharmaceuticals industry due to the sensitive nature of the products.

Implications for fund managers and companies

Where relevant, companies can seek WHO GMP and / or US FDA and / or EU GMP accreditation for their products in order to obtain quality assurance that their production is consistent with good or best international industry practice. Fund managers have an important opportunity to add value to their portfolio companies from encouraging improvements towards such standards.

For more information: www.gmp1st.com

Appendix 5

International ESG reference standards and conventions:
5.4 Governance: business integrity

5.4.1 The UN Convention against Corruption (2005)

Entered into force in 2005, the UN Convention against Corruption aims to promote and strengthen international measures to prevent and combat corruption. It aims to facilitate international cooperation in the prevention and criminalisation of corruption as well as for asset recovery where corruption or bribery has been discovered.

The convention covers the following main areas:

- prevention, criminalisation and law enforcement;
- international cooperation;
- asset recovery; and
- technical assistance.

Activities prohibited under the convention include:

- active and passive bribery;
- obstruction of justice;
- embezzlement of public funds; and
- transfer of criminal proceeds.

Implications for fund managers and companies

The UN Convention against Corruption is an important vehicle against corrupt practices. However, corruption is still widespread in emerging markets. Fund managers investing CDC's capital and their portfolio companies should follow CDC's business integrity and compliance programme, see p. 14-18. Companies should enforce a zero corruption tolerance for their operations.

For more information: www.unodc.org

Ratifications to the United Nations Convention against Corruption

Not ratified
Ratified

International ESG reference standards and conventions: 5.4 Governance: business integrity

5.4.2 The UN Anti-Corruption Toolkit (2010)

This UN Anti-Corruption Toolkit was developed in response to an increasing recognition of the serious obstacles corruption poses for both public and private sector entities. It includes 41 tools and 30 case studies, which can be important resources for fund managers and companies seeking to address business integrity issues in their investments and business operations.

The UN Anti-Corruption Toolkit covers the following aspects:

- prevention;
- legal cooperation;
- enforcement;
- awareness raising;
- empowerment;
- anti-corruption legislation; and
- monitoring.

The headings of the 41 Tools listed below inform fund managers and companies of which Tools could serve their needs.

The Toolkit also presents 30 detailed case studies to illustrate the Tools.

Implications for fund managers

The UN Anti-Corruption Toolkit can be used to guide and augment anti-corruption strategies in conjunction with a fund manager's own policy. It may be useful to seek external advice over which Tools work best to address particular matters.

Implications for companies

The Tools, particularly from Chapter IV onwards, can be incorporated in company policies against corruption and to guide their interactions with public bodies.

For the complete UN Anti-Corruption Toolkit: www.unodc.org

UN Anti-Corruption Toolkit: The Tools

	ASSESSMENTS
TOOL 1	Assessment of the nature and extent of corruption
TOOL 2	Assessment of institutional capabilities and responses to corruption
	INSTITUTION BUILDING
TOOL 3	Specialised anti-corruption agencies
TOOL 4	Ombudsman
TOOL 5	Auditors and audit institutions
TOOL 6	Strengthen judicial institutions
TOOL 7	Civil service reform
TOOL 8	Codes and standards of conduct
TOOL 9	National anti-corruption commissions and similar bodies
TOOL 10	National integrity and action-planning meetings
TOOL 11	Anti-corruption action plans
TOOL 12	Strengthen local governments
	Legislatures and their efforts against corruption
	SITUATIONAL PREVENTION
TOOL 13	Disclosure of assets and liabilities by public officials
TOOL 14	Authority to monitor public sector contracts
TOOL 15	Curbing corruption in the procurement process
TOOL 16	Integrity pacts
TOOL 17	Result orientated management
TOOL 18	Using positive incentives to improve employee culture and motivation
	SOCIAL PREVENTION
TOOL 19	Access to information
TOOL 20	Public awareness raising and empowerment
TOOL 21	Media training and investigative journalism
TOOL 22	Joint government and civil society bodies
TOOL 23	Public complaints mechanisms
TOOL 24	Citizens' charters
	ENFORCEMENT
TOOL 25	Guidelines for successful investigation into corruption
TOOL 26	Financial investigations and the monitoring of assets
TOOL 27	Integrity testing
TOOL 28	Electronic surveillance operations
TOOL 29	International and regional legal instruments
TOOL 30	National legal instruments
TOOL 31	Amnesty, immunity and mitigation of punishment
TOOL 32	Standards to prevent and control the laundering of corruption proceeds
TOOL 33	Whistleblowers: Protection of persons who report corruption
TOOL 34	Meeting the burden of proof in corruption-related legal proceedings
	MONITORING AND EVALUATION
TOOL 35	Service delivery survey (SDS)
TOOL 36	United Nations country assessment
TOOL 37	Mirror statistics as an investigative and preventative tool
TOOL 38	Measurable Performance Indicators for the jury
	INTERNATIONAL LEGAL COOPERATION
TOOL 39	Extradition
TOOL 40	Mutual legal assistance
	RECOVERY AND RETURN OF PROCEEDS OF CORRUPTION
TOOL 41	Recovery of illegal funds

Appendix 5

International ESG reference standards and conventions:
5.4 Governance: business integrity

5.4.3 The OECD Anti-Bribery Convention (2009)

The OECD Anti-Bribery Convention aims to reduce corruption by criminalising bribery of foreign public officials in international business transactions for companies based in OECD member states. Some non-OECD countries have also signed this convention.

Signatory countries are required to introduce legislation criminalising companies and individuals that bribe public officials in any country. The convention makes OECD countries responsible for implementing laws and regulations that conform to the convention. The aim is a level playing field in international business.

OECD good practice guidance on internal controls, ethics and compliance

A good practice guidance note for implementing the OECD Anti-Bribery Convention was adopted in 2010. It is designed to help companies establish and ensure the effectiveness of internal controls, ethics, and compliance programmes and measures for preventing and detecting the bribery of foreign public officials in their international business transactions. It also provides guidance for business organisations and professional associations, which play an important role in assisting companies in these efforts. To be effective, the measures recommended in this good practice guidance document should be interconnected with a company's overall compliance framework.

Implications for fund managers and companies

The OECD good practice guidance on internal controls, ethics and compliance can be of assistance in designing effective internal control systems and ethics policies, including for operations in non-OECD countries. For companies that are based in OECD countries or other signatory countries to the OECD convention, bribery of public officials in all countries is a criminal act.

For more information: www.oecd.org

Ratifications to the OECD Convention on combating bribery of foreign public officials in international business transactions

Not ratified
Ratified

International ESG reference standards and conventions: 5.4 Governance: business integrity

5.4.4 Transparency International's Corruption Perceptions Index

Every year Transparency International ranks 180 countries in terms of perceptions of public sector corruption. This is scored on a basis of 0-10 for corruption (0 being highly corrupt; 10 not corrupt at all). A ranking below three indicates that corruption is perceived to be endemic in that country.

The vast majority of the 180 countries included in Transparency International's Corruption Perceptions Index score below 5. 100% of low income countries score four or less.

The bottom half of Transparency International's Corruption Perceptions Index rankings are predominantly made up of emerging markets countries, particularly those in Africa and South Asia. Only three sub-Saharan African countries score over four: Botswana, Namibia and South Africa. In Asia, India scores 3.4 and China 3.6.

Transparency International also publishes resources which can be helpful to fund managers and companies. These include:

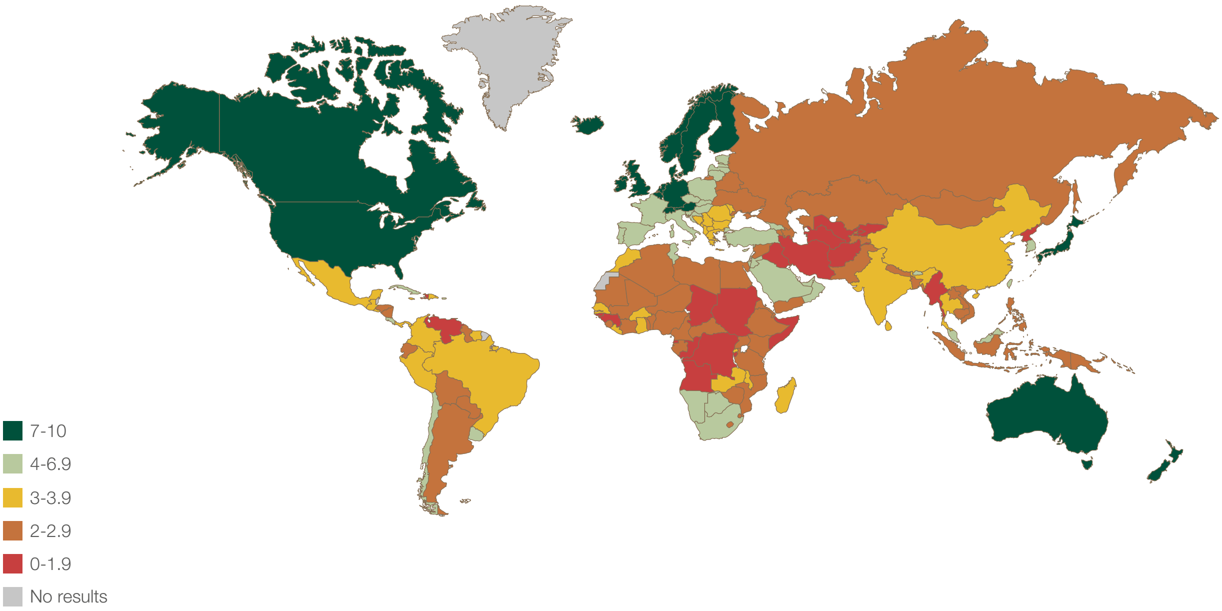
- a global corruption barometer on perceptions of corruption by region;
- a bribe payer's index evaluating the 'supply side of corruption' (ie the likelihood of firms from industrialised countries to bribe abroad); and
- an assessment of the transparency reporting of 500 of the world's largest companies.

Implications for fund managers

Transparency International's Corruption Perceptions Index gives an indication of the level of corruption in different countries. It should be used as a guide to understand potential business integrity risks (see *Tool 5c*). As this is an annually published index, fund managers could use updated country rankings to update their risk ratings for portfolio companies annually as well.

For more information: www.transparency.org

Transparency International's Corruption Perceptions Index 2009



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International ESG reference standards and conventions: 5.4 Governance: business integrity

5.4.5 The Extractive Industries Transparency Initiative (2003)

The Extractive Industries Transparency Initiative (EITI) aims to strengthen governance and reduce corruption in extractive industries, including oil, gas and mining. Such industries are often prone to corrupt practices in emerging markets.

The EITI focuses on improving transparency in payments between an extractive industry company and governments. For EITI compliant governments and companies, all payments made and revenues received must be disclosed and published regularly.

Countries must pass through an EITI validation before being recognised as a compliant country. A country must complete an EITI validation within two years of becoming an EITI candidate country, and subsequently undergo validation every five years or upon request from the EITI international board.

The EITI is supported by the European Union, the G8 countries, the G20 countries, oil, gas and mining companies and by several governments of resource rich countries in emerging markets including DR Congo, Nigeria and Tanzania. Companies signed up to the EITI include Anvil Mining, BP, Katanga, Lonmin and Shell.

Implementing the EITI

1) If the extractive industry company is in an EITI signatory country, an EITI auditor will contact the company to help control all payments made to the local government and reconcile these with government receipts. When there are gaps between the amount claimed to have been paid by the company and the amount claimed to have been received by the government, money could have been exchanged in a corrupt manner. An EITI report can identify such gaps.

2) An extractive industry company located in a non-EITI signatory country can still pledge its support to the EITI.

3) Extractive industry companies supporting EITI make voluntary donations to the EITI secretariat based on their market capitalisation.

For more information and suggested reporting guidance: www.eitransparency.org

Implications for fund managers

Fund managers should be aware of the high risks of corruption in extractive industries. CDC encourages fund managers that invest in extractive industries to encourage their portfolio companies to become EITI signatories.

Implications for companies

Companies in extractive industries should develop processes to improve transparency, accountability and their procedures to avoid corruption. Companies should consider becoming signatories to the EITI.

For more information: www.eitransparency.org

5.4.6 The Financial Action Task Force

The Financial Action Task Force (FATF) is an intergovernmental body whose purpose is to develop and promote national and international policies to combat money laundering and terrorist financing. The FATF is therefore a policy-making body which aims to generate the necessary political will to bring about legislative and regulatory reforms in these areas.

The FATF monitors member countries' progress in implementing necessary measures, reviews money laundering and terrorist financing techniques and countermeasures, and promotes the adoption and implementation of appropriate measures. In performing these activities, the FATF collaborates with other international bodies involved in combating money laundering and the financing of terrorism.

The FATF has published a number of recommendations, providing a complete set of countermeasures against money laundering. It has also adopted nine so-called 'special recommendations' to combat the financing of terrorism and the prevention of terrorist acts. These special recommendations are available on-line.

Implications for fund managers

Fund managers investing CDC's capital should be aware of the absolute prohibition of being involved in any type of money laundering or terrorist financing activities. They may refer to the FATF's recommendations as appropriate.

For more information: www.fatf-gafi.org

International ESG reference standards and conventions: 5.4 Governance: business integrity

5.4.7 The UK Proceeds of Crime Act (2002) and the UK Bribery Act (2010)

5.4.7.a The UK Proceeds of Crime Act (2002)

The UK Proceeds of Crime Act created wide and new powers for confiscation orders in relation to persons who or companies which benefit from criminal conduct. It also consolidated laws relating to money laundering in the United Kingdom. It is an offence under this act to enter into any arrangements which facilitate the use of criminal property. It is also an offence under this act not to report knowledge or suspicion of money laundering.

For more information: www.opsi.gov.uk

For amendments: www.barcouncil.org.uk

5.4.7.b The UK Bribery Act (2011)

A new UK Bribery Act will replace and enhance the United Kingdom's legislation relating to bribery and corruption and is expected to come into force in 2011. The act sets out four general offences: (i) bribing another person; (ii) accepting a bribe; (iii) bribing a foreign public official; and (iv) the failure of a 'relevant commercial organisation' to prevent bribery.

'Relevant commercial organisation' refers to a company or partnership incorporated or formed in the United Kingdom. Offences under the UK Bribery Act can be prosecuted in the United Kingdom not only when they are committed in the United Kingdom but also when they are committed in other countries by a person or company with a close connection with the United Kingdom, for example by British citizens or residents.

The corporate offence of failure to prevent bribery is a strict liability offence; meaning that a company will be guilty if a person associated with the company is guilty of an offence under the act. The company may claim a defence if it can prove that it had 'adequate procedures' in place to prevent unlawful conduct.

Note: Unlike the US Foreign Corrupt Practices Act of 1977, there is no exception for facilitation payments. These are prohibited by the UK Bribery Act.

Implications for fund managers and companies

Fund managers and companies should be aware of the possible criminal implications of any breaches of the UK Bribery Act.

For more information: www.justice.gov.uk and www.services.parliament.uk

5.4.8 The UK Money Laundering Regulations (2007)

The UK Money Laundering Regulations provide for various steps to be taken by the financial services sector and other persons to detect and prevent money laundering and terrorist financing. Obligations are imposed on 'relevant persons' (defined in regulation 3 and subject to the exclusions in regulation 4), which are credit and financial institutions, auditors, accountants, tax advisers and insolvency practitioners, independent legal professionals, trust or company service providers, estate agents, high value dealers and casinos.

Relevant persons are required, when undertaking certain activities in the course of business, to apply customer due diligence measures where they establish a business relationship, carry out an occasional transaction, suspect money laundering or terrorist finance or doubt the accuracy of customer identification information (regulation 7). Customer due diligence measures are defined in regulation 5.

Implications for fund managers and companies

Fund managers and companies should be aware of the possible criminal implications of any breaches of the UK Money Laundering Regulations.

For more information: www.opsi.gov.uk

5.4.9 The US Foreign Corrupt Practices Act (1977)

The US Foreign Corrupt Practices Act controls bribery in two ways: by prohibiting the bribery of foreign officials and by mandating record-keeping standards for companies registered under the US securities laws. The record keeping provisions require US listed companies to 'make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer'. They also require a system of internal controls to be created which provide 'reasonable assurance' that transactions are properly authorised. The anti-bribery provisions (i) prohibit all US persons from directly or indirectly bribing a foreign public official in order to obtain or retain business; and (ii) prohibit any person from using the US mail or interstate commerce 'corruptly in furtherance of an offer or payment of money or anything of value to a foreign official.'

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International ESG reference standards and conventions: 5.4 Governance: business integrity

The jurisdictional reach of the US Foreign Corrupt Practices Act's anti-bribery provisions is broad, as any currency or wire transfer connected in anyway to the United States is caught by the act.

Implications for fund managers and companies

Fund managers and companies should be aware of the possible criminal implications of any breaches of the US Foreign Corrupt Practices Act.

For more information: www.justice.gov

5.4.10 The Business Anti-Corruption Portal (2010)

The Business Anti-Corruption Portal was developed as a joint initiative between ministries from the Austrian, British, Dutch, German, Norwegian and Swedish governments. The portal focuses on corporate integrity issues with special services to assist companies on anti-corruption, anti-fraud, sustainability and business development.

The Business Anti-Corruption Portal is particularly designed to support small and medium-sized enterprises (SMEs) which operate in emerging markets and developing countries. The purpose of the portal is to counter corruption in order to facilitate a more productive business environment.

Based on public, international and local sources verified through the Global Advice Network, the Business Anti-Corruption Portal offers in-depth descriptions of the state of corruption in specific countries, with references to local authorities, NGOs, legislation and case studies. Training is also offered through the Global Advice Network.

60 countries have complete profiles on the Business Anti-Corruption Portal. The country profiles assess corruption risks between individuals, businesses and public sector representatives. Countries surveyed include China, India, Indonesia, Nigeria, South Africa and Tanzania.

Implications for fund managers

The Business Anti-Corruption Portal can be used by fund managers to understand the risks of corruption for companies in over 60 countries. The portal provides advice, tools to create sound anti-corruption policies, risk assessment criteria and due diligence tools.

Implications for companies

The portal provides free country-level corruption risk information aimed, in particular, at SMEs. It also provides practical operational assistance with sample policy documents, which can be easily modified to suit specific company needs.

For more information: www.business-anti-corruption.com

International ESG reference standards and conventions:
5.4 Governance: corporate governance

5.4.11 The OECD Principles of Corporate Governance (1999, 2004)

The OECD Principles of Corporate Governance provide an international good practice framework on corporate governance. They identify key elements of good governance, including:

- the basis for an effective corporate governance framework;
- the rights of shareholders and key ownership functions;
- equitable treatment of shareholders;
- the role of stakeholders;
- disclosure and transparency; and
- the responsibilities of the board of directors.

The OECD Principles of Corporate Governance have gained acceptance throughout much of the world and have gained worldwide recognition as an international benchmark for good corporate governance.

These principles can be used as a framework for analysing the corporate governance environment in different countries, and for improving the corporate governance of individual companies.

Implication for fund managers and companies

The OECD Principles of Corporate Governance provide internationally recognised good practice standards on corporate governance that can be used as a reference for fund managers and companies.

For more information: www.oecd.org

5.4.12 The Walker Report (2009)

The Walker Report is based on a review of corporate governance practices in the banking industry in the United Kingdom with recommendations in the following areas:

- the effectiveness of risk management at board level, including incentives in remuneration policies to manage risk effectively;
- the balance of skills, experience and independence required for board members of UK banking institutions;
- the effectiveness of board practices and the performance of audit, risk, remuneration and nomination committees;
- the role of institutional shareholders in engaging effectively with companies and in the monitoring of boards; and
- whether the UK approach is consistent with international best practices and how national and international best practices can be promulgated.

Implications for fund managers and financial institutions

Fund managers and financial institutions should be aware of the recommendations in the Walker Report and should consider adhering to them.

For more information: www.hm-treasury.gov.uk

5.4.13 The International Private Equity and Venture Capital Valuation Guidelines

The International Private Equity and Venture Capital Valuation Guidelines reflect the need for greater comparability across the private equity industry and for consistency with International Financial Reporting Standards (IFRS) and the US Generally Accepted Accounting Principles (GAAP).

Valuation guidelines are used by the private equity and venture capital industry for valuing investments. These guidelines provide a framework for fund managers and their investors to monitor the value of their investments. The guidelines are based on the principle of 'fair value' to be consistent with the IFRS and US GAAP. The guidelines have gained approval from 37 regional and national associations including L'Association Française des Investisseurs en Capital (AFIC), the British Private Equity and Venture Capital Association (BVCA), the Emerging Markets Private Equity Association (EMPEA), the Russian Private Equity and Venture Capital Association (RVCA) and the European Venture Capital Association (EVCA). They include specific guidance for fund-of-funds. AFIC, BVCA and EVCA have created an independent board accountable to a general assembly composed of all the endorsing associations to manage the evolution of the Guidelines.

Implications for fund managers

These guidelines represent industry best practice which fund managers should apply or work towards.

For more information: www.privateequityvaluation.com

Appendix 5

International ESG reference standards and conventions: 5.4 Governance: corporate governance

5.4.14 The International Accounting Standards Board and the International Financial Reporting Standards

The goal of the International Accounting Standards Board (IASB) is to develop a single set of high quality, understandable and enforceable global accounting standards to help participants in the world's capital markets and other users to make economic decisions.

Additionally, the IASB also aims to:

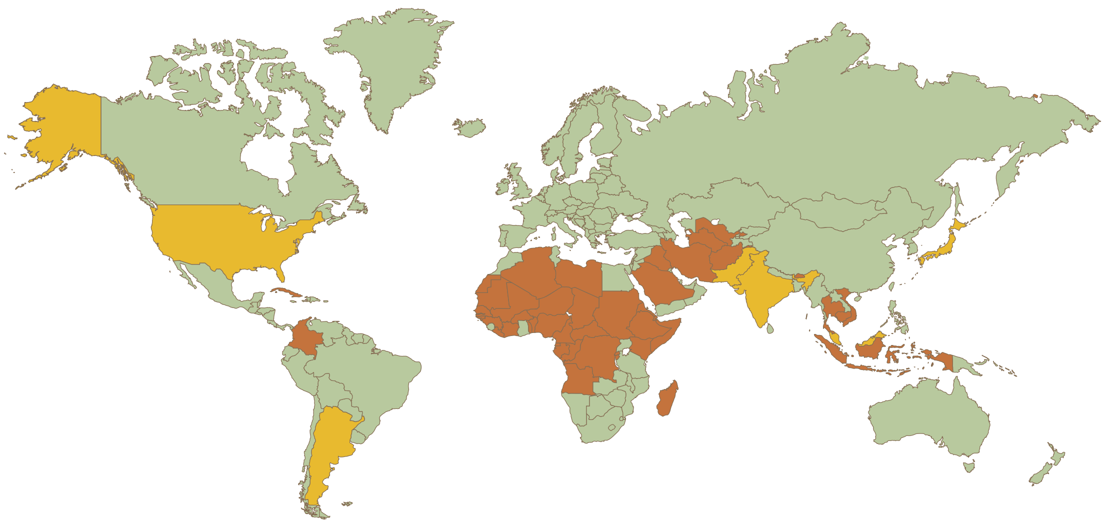
- promote the use and rigorous application of those standards;
- take account of the financial reporting needs of emerging economies and small and medium-sized enterprises (SMEs); and
- bring about the convergence of national accounting standards and International Financial Reporting Standards (IFRS) to obtain high quality accounting practices.

Implications for fund managers and companies

The IFRS, along with US Generally Accepted Accounting Principles (GAAP), are the international reference standards for accounting, which are strongly recommended for all companies.

For more information: www.iasb.org

Since 2001, over 100 countries have required or permitted the use of the International Financial Reporting Standards (IFRS)



Countries that require or permit IFRS for domestic entities

Countries seeking convergence with, or pursuing adoption of, IFRS

No current convergence

International ESG reference standards and conventions: 5.4 Governance: corporate governance

5.4.15 The DFI Toolkit on Corporate Governance (2010)[1]

A number of development finance institutions (DFI) jointly developed a corporate governance toolkit in 2010. This toolkit includes the tools listed below for analysing the corporate governance of DFIs' investee companies.

Instruction sheet

The purpose of the instruction sheet is to introduce the concept of corporate governance; the value of good corporate governance for investee companies and DFIs; and to describe each of the corporate governance tools, how they should be used, and who should be interviewed in the course of a corporate governance review.

Corporate governance progression matrix

The progression matrix relates the five areas of governance (commitment to corporate governance, structure and functioning of the board of directors, control environment and processes, transparency and disclosure and rights of minority shareholders) to four levels of achievement. The use of a matrix framework emphasises the importance of ongoing improvements in the governance practices of investee companies, rather than trying to apply rigid and static minimum standards. The first level of the matrix represents the basic governance practices that investee companies might have in place. The next three levels describe more advanced practices towards which investee companies should gradually progress. In addition, the progression matrix allows investee companies to self-assess their governance. The progression matrix should be distributed to the investee company at the earliest opportunity.[2]

Corporate governance questionnaire

This list of questions establishes the basis for a corporate governance review of an investee company. This questionnaire is organised to correspond to the five areas of governance in the progression matrix. DFI investment staff should answer this questionnaire by collecting the relevant information from the investee company and from interviews during the appraisal of the investment opportunity.[3]

In addition to these three tools, the following sample and supportive documents can be used by DFI investment staff as needed:

Sample corporate governance improvement programme

After completing a corporate governance review, DFI investment staff should summarise their key findings in the form of a corporate governance improvement programme. This document will describe the main governance risks and opportunities of the investee company and suggest recommendations for improvement.

Sample corporate governance section in the investment approval documents

This sample PowerPoint slide can be used by DFI investment staff as a platform for addressing the key corporate governance risks and opportunities when deciding on a specific investment opportunity. The level of risk (low/medium/high) is decided by DFI investment staff based on the findings of the corporate governance review.

List of key corporate governance terms

The purpose of this document is to provide definitions of key corporate governance terms from the progression matrix and the questionnaire.

For the complete DFI Toolkit on Corporate Governance, see CDC's website www.cdcgroup.com More extensive guidance is available from the IFC's website www.ifc.org

[1] Adapted by a DFI working group on corporate governance from the IFC's corporate governance methodology, which is based on the OECD Principles of Corporate Governance. Good corporate governance for some DFIs also includes business integrity issues which are not addressed in these materials.

[2] The corporate governance matrix included in Tool 1 of CDC's Toolkit on ESG for fund managers builds on, while is not identical to, the matrix included in the joint DFI Toolkit on Corporate Governance.

[3] The corporate governance due diligence questions included in Appendix 1 of CDC's Toolkit on ESG for fund managers builds on, while is not identical to, the questionnaire included in the joint DFI Toolkit on Corporate Governance.

Appendix 6

CDC's monitoring and evaluation system

6.1 Overview

Development finance institutions (DFIs) like CDC, and increasingly also private sector investors and large companies, seek to demonstrate the development benefits of their investments in emerging markets for local populations and economies. Key performance indicators to measure development effects are usually measured according to an inputs-outputs-outcomes-impact framework, as illustrated for fund investments in the graph below.

CDC's fund managers need to collect, record, report and act upon key performance indicators at different points in time. Key performance indicators should be systematically used to assess investments prior to the investments decision, to monitor investments during the investment period, and for periodic evaluations.

The development effects of CDC's investments have to be captured at different levels

Key objectives for CDC:

- Demonstrate whether CDC's investments are good for development
- Use information as a management tool to improve investment and business practices

Inputs

- CDC invests capital with fund managers
- Third party capital

Outputs

- Fund managers invest in commercially viable and responsibly managed companies in developing countries

Outcomes

- Growing and profitable businesses
- Jobs and tax revenues
- Increased availability of products and services
- Increased availability of commercial finance in developing countries

Impact

- Poverty alleviation
- Economic growth
- Efficient capital markets in developing countries

Assessments: Prior to investments

Monitoring: Quarterly, bi-annual and / or annual reviews of key performance indicators: qualitatively and quantitatively

Evaluations: Verification of existing performance information, further qualitative and quantitative data and contextual considerations: performed by CDC and external consultants

CDC's monitoring and evaluation system

CDC introduced a framework and processes for monitoring and evaluating the development effects of its fund investments in 2008 after benchmarking extensively with other DFIs. CDC's framework for measuring development effects is similar but not identical to the Development Outcome Tracking System (DOTS) used by the International Finance Corporation (IFC), as it was streamlined to focus on key parameters for ease of use for fund managers. The framework used by CDC is well suited for investments through funds, and can also be readily applied to direct investments.

CDC's framework for measuring development effects includes four key parameters to assess the overall development outcome for each fund investment, based on the performance of a fund as well as of its underlying portfolio companies.

CDC measures the Development Outcome of its investments along four parameters

Development Outcome	**Financial performance**	Fund managers' ability to attract commercial capital to developing country markets • Financial return to investors (net IRR %)
	Economic performance	Contributions to economic growth • Commercially viable and growing businesses that generate employment and pay taxes (EBITDA, turnover, employment, taxes) • Special consideration for SMEs and special indicators for microfinance
	ESG performance	Responsible investment and business practices with respect to the environment, social matters and governance (ESG) • Fund managers' ESG management systems and the ESG performance of portfolio companies against CDC's Investment Code (issues / opportunities at investment and improvements over time)
	Private sector development	• Third party capital (DFI / non-DFI, successor fund?) • More efficient capital markets (pioneering / local fund managers?) • Regulatory improvements • Multi-country investments (low income countries, sub-Sahara Africa and poor regions within large countries) • Benefits to customers from more efficient provision of goods, services and infrastructure, e.g., increased telecom penetration, extended and improved transportation systems, lower prices through local suppliers, new technologies
CDC Effectiveness	**Catalytic**	• CDC's direct role, if any, in bringing in other investors
	Added value	• CDC's direct contributions, if any, to improve the way fund managers invest CDC's capital e.g: • to shape a fund's investment thesis or terms • to improve the fund manager's ESG management systems • to recruit or contract key technical expertise for responsible investment management

Appendix 6

CDC's monitoring and evaluation system

CDC's development indicators for fund investments

As relevant/appropriate | Always

	Performance area	Concept	Indicator	When to record: At invest-ment	When to record: Annual moni-toring	Evaluations: Mid	Evaluations: Final
1 Development Outcome	**Financial performance** Fund level	Fund managers' ability to attract commercial capital to poor country markets > financial return to investors	Net IRR of fund[1]	Target			
			IRR for each realised exit (%)				
			Total investment ($)				
			Total commitment ($)				
			Investment period (yrs)	Target			
	Economic performance Investee company level	Contributions to economic growth > commercially viable and growing businesses that generate employment and pay taxes	% of portfolio companies with increase in EBITDA				
			% of portfolio companies with increase in turnover				
			% of portfolio companies with increase in employment				
			% of portfolio companies with increase in taxes paid				
			% total portfolio increase: EBITDA				
			% total portfolio increase: turnover				
			% total portfolio increase: employment				
			% total portfolio increase: taxes paid				
			% of portfolio companies with SME classification at time of acquisition (if relevant)	Target?			
			% of portfolio companies which serve low-income markets / populations (if relevant)	Target?			
	ESG performance Investee company level[2]	Responsible investment and business practices with respect to the environment, social matters and governance (ESG) > fund managers' ESG management systems and the ESG performance of portfolio companies	Environment: portfolio companies addressing environmental and climate related risks and opportunities	Risks & targets			
			Social: labour and working conditions, health and safety performance record and other social matters	Risks & targets			
			Governance: quality of portfolio companies' governance structure, track record of governance issues	Risks & targets			
	For fund manager		ESG serious incidents performance record				
			Quality of and improvements to the GP's ESG management system	Quality			
	Private sector development	Broader private sector development effects > more efficient capital markets > regulatory improvements > benefits to customers from increased availability of goods, services and infrastructure	Third party capital from DFIs and / or non-DFIs in the fund				
			Local capacity building				
			Frontier fund manager (Y / N; change in status)	Rating			
			Local fund manager (Y / N; change in status)	Local?			
			Debt or other external financing raised by investee companies ($)				
			Average holding period for investee companies (yrs)				
			Multi-country investments / operations (LICs, SSA; % capital)	Target?			
			Type of investment (growth, privatisation; expansion; VC; etc)	Target?			
			Type of realised exits (IPO, trade sale, MBO, sale to investor(s))				
			Raising of successor fund				
			Non-DFI financing in successor fund ($; %)				
	Investment context		Change in the number of PE firms in the market				
			% increase in PE investment as share of GDP				
	Contextual or directly related		Enhancements to investment environment (regulations, etc)	Target?			
			Enhancements to sectors where portfolio companies operate (if available)[3]	Target?			

Note: ESG management systems and performance will be assessed relative to CDC's Investment Code and the risk level of portfolio companies.

Improvements over time will be valued in the evaluation. The investment portfolio of each fund manager will be risk rated based on its portfolio companies and the inherent risk levels of the sectors / geographies where they operate.

1 For that asset class, type of fund manager, and / or geography.

2 ESG issues and improvements should be reviewed for all portfolio companies in high-risk sectors and for others as appropriate. The mid-point evaluation covers available information at that time.

3 If any and as per available information, e.g. infrastructure development (e.g. power, roads, water); availability of products or services (e.g. telecom penetration); new technologies or other inventions.

CDC's monitoring and evaluation system

	Performance area	Concept	Indicator	When to record: At invest-ment	Annual moni-toring	Evaluations: Mid	Final
2 CDC Effectiveness	Catalytic effects	CDC's direct role in bringing in other investors > focus on commercial capital	Third party capital from DFIs and / or non-DFIs in the fund, with evidence of attribution to CDC				
			Frontier fund manager whose establishment can be attributed with evidence to CDC (Y / N; change in status)	Rating			
			Local fund manager whose establishment can be attributed with evidence to CDC (Y / N; change in status)	Local?			
			Raising of successor fund, with evidence of attribution to CDC				
			Other positive factors that can be attributed to CDC, e.g. increase in market liquidity for distressed assets funds				
			Examples of CDC helping the fund manager with fund raising (qualitative; $)	Target?			
	Added value	CDC's direct contributions to improve the way fund managers invest CDC's capital, for example: > to shape a fund's investment thesis or terms > to improve fund managers' ESG management systems > to recruit or contract key technical expertise for responsible and successful investment management	Examples of CDC qualitative assistance to GP (e.g. shaping terms, fostering alignment, improving strategy, enhancing carry structure or other matters)	Target?			
			CDC support to improve fund ESG performance (e.g. ESG management systems, corporate governance structure or other matters)				

If there is an instance involving a portfolio company that results in loss of life, material effect on the environment, or material breach of law, CDC expects to learn about this immediately from the fund manager. CDC takes any such notification very seriously. CDC's portfolio director responsible for that fund follows up with the fund manager as corrective actions are undertaken to ensure that adequate measures are being implemented in a timely manner. CDC will follow up with the fund manager until there are sufficient assurances that the situation has been dealt with in a satisfactory manner to minimise risks for the future.

6.2 CDC's monitoring of its fund investments

CDC monitors improvements in business practices across its portfolio, as a key aspect of the development impact of investments. Information on improvements made is primarily collected from the annual ESG reports from fund managers. CDC's investment team compiles case studies to illustrate best practices. Case studies which highlight how sound ESG management has contributed to business success are particularly sought out and documented. These case studies are used by CDC to inspire other fund managers and their portfolio companies to make similar improvements.

6.3 Evaluations of fund investments by CDC

CDC and other DFI's periodically perform in-depth evaluations of their investments through funds. This is also the practice of some private sector investors. CDC's evaluations use the development indicators in the table on p. 153 and the template on p. 156-162. The evaluations can either be performed by CDC's investment professionals, assisted by ESG specialists, or by external consultants.

Since 2008, all of CDC's fund investments are evaluated:

- at the end of a fund's investment period or the half-way point of the duration of a fund, which would typically be 5 years after a standard fund has commenced; and
- at the end of the duration of a fund, which would typically be 10 years after a standard fund has commenced.

Mid-point evaluations

The mid-point evaluation is intended to take stock of how well a fund has performed to-date, including on ESG matters, and to identify any shortcomings and areas for improvements. CDC would then expect to work with the fund manager to bring about improvements as

Appendix 6

CDC's monitoring and evaluation system

appropriate for the remainder of the duration of the fund as well as for successor funds. The mid-point evaluation is usually conducted at the end of the fund's investment period which usually concurs with the half-way point of the duration of a fund, typically 5 years after first closing.

The evaluation of ESG performance is a key part of CDC's broader evaluation of the development impact of a fund. The mid-point evaluation includes a review of the ESG management systems of the fund manager, with its internal responsibilities, processes and controls, as well as any specialised external technical support used by the fund manager to identify and mitigate ESG risks and bring about improvements. The mid-point evaluation also reviews how well fund managers' ESG management systems have worked in practice for their due diligence and monitoring of portfolio companies. It includes a review of portfolio companies in high-risk sectors and companies where issues have been identified and / or where substantial improvements have been initiated or completed for other reasons. Meetings with the management of such portfolio companies and site visits are used to verify and complement the information received from the fund manager.

The mid-point evaluation feeds into CDC's due diligence work for any successor funds and thus supports CDC's investment decisions for new fund investments with existing fund managers. It is also used for a dialogue with fund managers about any issues identified or opportunities for improvements.

Fund investment monitoring post a mid-term evaluation

CDC's monitoring after a mid-point evaluation uses the findings from the mid-point evaluation report regarding improvements that may need to be undertaken during the remainder of the fund's duration. Any follow-up actions should be noted in the fund managers' annual ESG reports.

Final evaluations

At the end of a fund's life, a final evaluation is undertaken by CDC or its consultant(s) on how the fund has performed as compared to expectations and targets at the time of investment. This would typically be done 10 years after the first closing of a fund. The ESG performance is one of the key dimensions evaluated as part of CDC's broader framework for evaluating the development impact of its investments.

The findings from the mid-term evaluation are followed-up in the final evaluation. Improvements in ESG performance over the investment period are noted in the evaluation, as well as any issues that occurred and how the fund manager and portfolio companies addressed such issues. Particular attention is given to portfolio companies in high-risk sectors, particularly where there have been issues of substance and / or where substantial ESG improvements have been made during the duration of the investment.

The findings from final evaluations, like the findings from mid-point evaluations, are used for CDC's due diligence and investment decision for follow-up funds.

6.4 Evaluation ratings

In the mid-point and final evaluation reports, the fund is given an evaluation rating for each performance category on a six-scale rating from excellent to poor. Such a six-scale rating forces a judgment of performance and introduces nuances to the performance assessment. The aggregate rating of financial performance, economic performance, ESG performance and private sector development makes up an overall rating of the development outcome of each fund investment. The evaluation rating for ESG performance is based on how well the underlying portfolio companies have performed on ESG, as well as on the quality of the fund managers ESG management systems. A guidance to CDC's rating system is provided in the table opposite:

CDC's monitoring and evaluation system

Evaluation rating						
	Excellent	Successful	Satisfactory	Below expectations	Unsatisfactory	Poor
Development outcome	Judgement-based aggregate rating based on the four performance categories below.					
Financial performance	CDC has a target net IRR range for its fund investments for three different types of funds, e.g. from 20%+ to <0% for growth capital.					
Economic performance	EBITDA, turnover, employment and taxes paid are rated as high, medium or low based on what % of portfolio companies have achieved increases. Aggregate targets for each rating category. SMEs upped one rating.					
ESG performance	Improvements in ESG performance of portfolio companies and quality of the fund manager's ESG management system relative to the risk level of portfolio.					
Private sector development	Judgement-based rating based on key indicators (successor fund; investments in multiple low income countries; enhancements to the investment environment, enhancements to sectors with increased availability of products, services and infrastructure).					

6.5 **CDC's evaluation template** is provided in the pages that follow for fund managers to understand the information that CDC or its consultant(s) seek to assemble and assess as part of an evaluation. The evaluations are based on the regular reports provided by fund managers (see *Tool 12*), interviews with the fund manager and their portfolio companies, records of site visits and new site visits with a focus on high-risk assets from the ESG perspective.

The fund managers is expected to collaborate with CDC in assembling the relevant information and in identifying relevant persons for interviews. Usually, the fund manager would accompany CDC or CDC's consultant(s) during visits to the portfolio companies as part of the evaluation work but may not be present during all interviews.

Appendix 6

CDC's evaluation template

[FUND NAME]	
EXECUTIVE SUMMARY:	
KEY DATA FOR FUND:	
NET IRR:	CDC INVESTMENT:
IRR TARGET:	YEAR OF CDC INVESTMENT:
COMMITTED CAPITAL:	COUNTRIES:
INVESTED CAPITAL:	SECTOR(S):
NON-DFI INVESTORS:	FUND MANAGER:
OTHER DFI INVESTORS:	SUCCESSOR FUND:
QUALITY OF GP'S ESG MANAGEMENT SYSTEMS:	
KEY DATA FOR PORTFOLIO:	NUMBER OF COMPANIES:
EMPLOYMENT:	EBITDA:
EMPLOYMENT GROWTH:	EBITDA GROWTH:
TURNOVER GROWTH:	TAXES PAID:
SMEs OR MICROFINANCE:	REALISED EXITS:

EVALUATION RATING						
	Excellent	Successful	Satisfactory	Below expectations	Unsatisfac-tory	Poor
Development outcome						
Financial performance						
Economic performance						
ESG performance						
Private sector development						
CDC effectiveness						
Added value						
Catalytic						

6

CDC's evaluation template

1. BACKGROUND

2. FUND SUMMARY

2.A. Fund description

2.B. CDC investment rationale

2.C. What would have happened without CDC's investment?

3. EXPLANATION OF EACH EVALUATION RATING

3.A. Development outcome

3.A.1 Financial performance

3.A.2 Economic performance

3.A.3 ESG performance

Appendix 6

CDC's evaluation template

3.A.4 Private sector development

3.B. CDC effectiveness

3.B.1 Added value

3.B.2 Catalytic effects

3.C. Influence of the investment environment

4. LESSONS LEARNED

4.1 What did CDC expect at the time of the commitment?

4.2 What actually happened?

4.3 Lessons for future operations

5. FOLLOW-UP ACTIONS

App 6

CDC's evaluation template

Appendix A

[Name of fund] Portfolio summary

Company	Country	Sector	Date of investment	Deal type[1]	Share-holding %	Amount invested	Amount realised	Gross IRR	Exit type[2]
					Total				
							Net IRR for Fund		

Appendix A

[Name of fund] Portfolio summary

Company	EBITDA at investment	EBITDA last year (or exit if applicable)	Turnover at investment	Turnover last year (or exit if applicable)	Debt or other external finance[3]	Beginning employment	Employment currently / at exit	Taxes paid over holding period
Total								

[1] Management buy-out (MBO), expansion / growth capital, placement, venture capital (VC), privatisation of state owned enterprise (SOE), etc.
[2] IPO, trade sale, MBO, sale to investor(s), etc.
[3] If available and where appropriate: amount of new debt or other external finance for portfolio companies during the holding period.

Appendix 6

CDC's evaluation template

Appendix B

[Name of fund] ESG performance of portfolio companies

Company	Country	Sector	Rating of ESG risks and / or opportunities for improvements[4]			Quality of ESG management systems[7]
			Environment	Social matters[5]	Governance[6]	
ESG issues / opportunities:						
ESG improvements:						
Status / further actions recommended:						
ESG issues / opportunities:						
ESG improvements:						
Status / further actions recommended:						
ESG issues / opportunities:						
ESG improvements:						
Status / further actions recommended:						
ESG issues / opportunities:						
ESG improvements:						
Status / further actions recommended:						
ESG issues / opportunities:						
ESG improvements:						
Status / further actions recommended:						
ESG issues / opportunities:						
ESG improvements:						
Status / further actions recommended:						
ESG issues / opportunities:						
ESG improvements:						
Status / further actions recommended:						

[4] High, medium, low. See *Tool 5*.

[5] Labour and working conditions, health and safety, and / or other social matters.

[6] The local environment can pose business integrity issues; firms that were previously fully owned and run by the founder / the founder's family often need corporate governance improvements; reporting / transparency standards are often weak in non-publicly traded firms; etc.

[7] Good, medium or poor. Proportional to ESG risk rating. See *Tool 8*.

CDC's evaluation template

Appendix C

[Name of fund] Investors

[Name of fund]	
Investors[8]	**Amount**
DFIs	
Non-DFIs	

[Name of successor fund, if any]	
Investors[8]	**Amount**
DFIs	
Non-DFIs	

[8] Note if the investor is a multilateral or bilateral development finance institution (DFI). The multilateral DFIs include e.g. IFC, AsDB, IADB, EBRD, AfDB. The bilateral DFIs include e.g. OPIC and the European DFIs.

Appendix D

[Name of fund] Portfolio summary

Company name	Company website

Appendix 7

CDC's reporting templates:
Template for an annual non-financial report

ESG and economic data: annual report for [name of fund]

[Name of portfolio company]

Country[1]	Sector	Rating of ESG risks & opportunities for improvements[2]			Quality of ESG management systems[3]
		Environment	Social matters	Governance	
Reporting period for data	**Employee numbers (full time equivalents)**	**Currency of data**	**Taxes paid[4]**	**Turnover**	**EBITDA**
ESG issues / opportunities for improvements at the time of investment:					
ESG improvements achieved:					
Status / further actions to be undertaken, with timeframe:					
Other information:					

7

[1] Country or countries of operation.
[2] High, medium or low. See *Tool 5*.
[3] Good, moderate or poor. See *Tool 8*.
[4] Taxes paid for last year as shown in the cash flow statement, not taxes payable in the profit and loss (P&L) statement.

CDC's reporting templates: Template for a serious incident report

Report on ESG issue / incident in portfolio company	
Date of report	
Fund manager	
Fund	
Fund manager contact person	
Name of portfolio company involved	
Date of investment	
Amount invested	
Total portfolio investments (cost)	
Description of issue	• Date and time of incident • Type of incident: environmental issue, fatality, alleged fraud or other • Name of person/s involved / injured / deceased, if applicable • Narrative and contextual information • Whether incident was work or non-work related • Causes of incident • Status of investigation • Listing of parties involved in investigation (witnesses and staff, unions, police, other authorities and other parties
Follow-up by fund manager	• Fund manager's view of incident: degree of severity, possible uncertainties or disputed facts to be investigated • Status of investigation • Reports received (and outstanding, if any) • Immediate actions taken by the fund manager and other parties • Further actions to prevent re-occurrence of incident • Monitoring / reporting arrangements to follow up on efficacy of actions taken • Results to date of actions taken
Conclusion	• Next steps: whether to close the case, or proceed with investigations, how to do so, and the rationale for it

Appendix 7

Example of an ESG report

[Company A]

<table>
<tr><th rowspan="2">Country[1]</th><th rowspan="2">Sector</th><th colspan="3">Rating of ESG risks & opportunities for improvements[2]</th><th rowspan="2">Quality of ESG management systems[3]</th></tr>
<tr><th>Environment</th><th>Social matters</th><th>Governance</th></tr>
<tr><td>India</td><td>Manufacturing</td><td>High</td><td>High</td><td>Medium</td><td>Low</td></tr>
<tr><th>Reporting period for data</th><th>Employee numbers (full time equivalents)</th><th>Currency of data</th><th>Taxes paid[4]</th><th>Turnover</th><th>EBITDA</th></tr>
<tr><td>2009</td><td>560</td><td>US$</td><td>US$0.9m</td><td>US$7.4m</td><td>US$2.9m
(up 21% on 2008)</td></tr>
<tr><th>ESG issues / opportunities for improvements at the time of investment:</th><td colspan="5">• Environmental risks from smoke and particle emissions and waste products generated.
• Moderate climate change risk.
• Health and safety risks from equipment used, noise, smoke particle emissions and open fire pits in the plant.</td></tr>
<tr><th>ESG improvements achieved:</th><td colspan="5">• Has applied to local authorities to operate a waste treatment plant to ensure that waste produced is adequately disposed of.
• The fund manager receives quarterly reports (March, June, September and December) from Company A. The ESG manager participated in training with the IFC in November 2009.
• ESG risks are carefully monitored. Regular (monthly) reporting to board. Mr C was given board responsibility for ESG from June 2008.</td></tr>
<tr><th>Status / further actions to be undertaken, with timeframe:</th><td colspan="5">• Contract a specialist to conduct a review of health and safety risks and recommend improvements. Report on improvements in next ESG report.
• Full report on estimated savings produced by waste treatment plant to be produced. Initial estimates (based on internal review): US$0.2m p.a.
• Intends to implement an air pollution control device to minimise smoke and particles emitted.
• Grant of US$0.4m from XYZ underway to finance these improvements.
• Greenhouse gas emission reduction plan to be developed in 2010.</td></tr>
<tr><th>Other information:</th><td colspan="5">• Business model of sourcing local scrap metals for high quality new steel products proved a success with Indian steel purchasers.
• Company A estimates that there are upwards of 150,000 people throughout the region of Company A's operators who obtain income from sales of scrap metal to scrap metal dealers who sell to Company A.</td></tr>
</table>

[1] Country or countries of operation.
[2] High, medium or low. See *Tool 5*.
[3] Good, moderate or poor. See *Tool 8*.
[4] Taxes paid for last year as shown in the cash flow statement, not taxes payable in the profit and loss (P&L) statement.

App 7

Example of an ESG report

[Company B]

Country[1]	Sector	Rating of ESG risks & opportunities for improvements[2]			Quality of ESG management systems[3]
		Environment	Social matters	Governance	
South Africa	Mining	High	High	High	Good
Reporting period for data	**Employee numbers (full time equivalents)**	**Currency of data**	**Taxes paid[4]**	**Turnover**	**EBITDA**
2009	100	US$	0	Start-up	– US$0.3m

ESG issues / opportunities for improvements at the time of investment:	• Project located near a game park and migratory path for animals. • Long approval process to ensure development adhered to strict environmental regulations and did not impact on game park / migratory path. • Potentially high-risk for greenhouse gas emissions when the mine enters operations.
ESG improvements achieved:	• Discussions with multiple communities to obtain licence to develop mine. Mr J S leading discussions and reporting to Mr R T. • Wide ranging Black Economic Empowerment (BEE) partnerships established giving multiple local villages direct equity interest in project / company. XY consultancy commissioned to investigate mitigation possibilities. • Completed initial EITI reporting requirements on time and on budget. Sign off by ESG manager and by board. Audited by XYZ international auditors.
Status / further actions to be undertaken, with timeframe:	• Currently constructing mine. Estimated completion date is year-end 2011. • Consultation with local communities to be continued as necessary. IFC Performance Standard 5 used to influence actions undertaken.
Other information:	• The fund manager worked closely with Company B to help with a potential IPO. Investigations ongoing for follow-up mining operations in the area.

[1] Country or countries of operation.

[2] High, medium or low. See *Tool 5*.

[3] Good, moderate or poor. See *Tool 8*.

[4] Taxes paid for last year as shown in the cash flow statement, not taxes payable in the profit and loss (P&L) statement.

Appendix 7

Example of an ESG report

[Company C]

Country[1]	Sector	Rating of ESG risks & opportunities for improvements[2]			Quality of ESG management systems[3]
		Environment	Social matters	Governance	
Mozambique	Agribusiness	Medium	High	Low	Good
Reporting period for data	**Employee numbers (full time equivalents)**	**Currency of data**	**Taxes paid[4]**	**Turnover**	**EBITDA**
2009	120	US$	US$0.4m	US$6.1m	US$1.9m (up 71% on 2008)

ESG issues / opportunities for improvements at the time of investment:	• Health and safety risks associated with poultry farming. Company C produces and distributes chicken eggs over an area of 300 square kilometres around Maputo. • Due diligence identified poor record keeping on accidents and that Company C had no code of ethics. This has now been rectified. Mrs Y is now responsible for ESG for operations with Mr X taking board responsibility. The fund manager has one seat on the company's board. • Social risks as the firm employs a number of low-skilled, low-paid workers.
ESG improvements achieved:	• Female workforce is at 10%, up from zero at the time of investment. • Provision of in-house training and recruitment of more technically qualified staff. Recruitment programme in conjunction with local university. • Improved sanitation of staff living quarters, with running water and new toilets and separate facilities for men and women. Total cost US$30,000. • Establishment of an HIV / AIDS programme, paid for with funds from XYZ. This has attracted positive media interest. See reports in X paper.
Status / further actions to be undertaken, with timeframe:	• A recent outbreak of Gumboro disease killed over 50% of the chickens on the farm. A fumigation chamber has been installed at the entrance to the farm to reduce disease risk. Future outbreaks will be monitored and staff will be trained to identify symptoms of the disease. • Organic waste is currently sold to neighbouring farmers as manure. This is generating US$12,000 in additional revenues per year. As Company C grows, the levels of waste may exceed local demand. A review of waste management is therefore required in the short to medium term for further alternatives.
Other information:	• Company C is the largest regional table egg producer, accounting for 11% of the market. • Mozambique has one of the highest HIV / AIDS prevalence rates in sub-Saharan Africa, with 15% of the adult population infected.

[1] Country or countries of operation.

[2] High, medium or low. See *Tool 5*.

[3] Good, moderate or poor. See *Tool 8*.

[4] Taxes paid for last year as shown in the cash flow statement, not taxes payable in the profit and loss (P&L) statement.

Example of an ESG report

[Company D]

Country[1]	Sector	Rating of ESG risks & opportunities for improvements[2]			Quality of ESG management systems[3]
		Environment	Social matters	Governance	
Tanzania	Financial services	Low	Medium	Medium	Good
Reporting period for data	**Employee numbers (full time equivalents)**	**Currency of data**	**Taxes paid[4]**	**Turnover**	**EBITDA**
2009	2817	US$	US$14.2m	US$175.8m	US$65.1m (up 12% on 2008)

ESG issues / opportunities for improvements at the time of investment:	• Due to the indirect nature of banking, the environmental and social risks of Company D's operations are considered to be low. • The inherent ESG risks are mostly related to governance and management of related risks, e.g. having the correct credit screening procedures in place and monitoring the business integrity of loan customers.
ESG improvements achieved:	• Continued expansion of business lines for low income populations previously under-served by financial institutions in Kenya, Tanzania, Uganda and Sudan provide them with access to banking products. Company D currently opens 5,000 new bank accounts daily. The average size of new accounts is US$150. • The fund manager has helped Company D to revamp the directors' code of conduct and introduced an insider trading policy. Whistleblower and information sharing policies have also been substantially upgraded. • Company D has embedded Corporate Social Responsibility (CSR) within the way it does business and sponsors numerous programmes for education, health and gender equality that benefit employees as well as the wider community. Results from the CSR programmes are reported at monthly board meetings.
Status / further actions to be undertaken, with timeframe:	• A clear ESG policy for extension of credit lines, with guidelines for departments and individuals. XY consultancy company has been contacted to provide assistance. • Adjustment of the loan application documentation to include a declaration that potential ESG issues were considered during the loan review process. • Annual ESG training for all staff, with materials that cover ESG issues and explicitly including training on the bank's credit policy on exclusions and restrictions. • Provide more guidance to customers on ESG matters. A review has indicated that improved ESG management has reduced the risk of defaults by 11% for the 350 clients surveyed in 2009. • Monitoring of ESG risks of loan applicants (on-site visits). Budget is US$200k for 2010 for this activity.
Other information:	• Many individuals and SMEs would either not qualify for banking services with other Tanzanian banks or would not be able to afford the charges and interest imposed by other banks.

[1] Country or countries of operation.

[2] High, medium or low. See *Tool 5*.

[3] Good, moderate or poor. See *Tool 8*.

[4] Taxes paid for last year as shown in the cash flow statement, not taxes payable in the profit and loss (P&L) statement.

Appendix 8

Investments from different development finance institutions (DFIs): comparing standards and procedures

8.1 Introduction

CDC requires all fund managers that invest its capital to adhere to CDC's Investment Code on ESG, p. 9-13. The Investment Code includes an exclusion list on business and activities where CDC's capital will not be invested and principles, objectives and policies for ESG. Fund managers are required to produce an annual ESG report in a format satisfactory to CDC and to inform CDC as soon as possible about incidents which result in loss of life, serious injury, material effect on the environment or material breach of law.

Other development finance institutions (DFIs) have similar and compatible, while not always identical requirements, as CDC. This appendix compares CDC's exclusion list, local investment agreement for fund managers, reporting requirements and CDC's framework and process for evaluating development impact with those of other selected DFIs. The purpose is not to be comprehensive but to inform fund managers of what they can expect from different DFI investors.

8.2 Exclusion lists

DFIs have exclusion lists of business activities in which their capital can not be invested. CDC's exclusion list, see p.12, is compatible with those of the other European DFIs (EDFIs), the International Finance Corporation (IFC), the Asian Development Bank (AsDB) and the European Bank for Reconstruction and Development (EBRD), though CDC's exclusion list is shorter and does not include e.g. alcohol.

In 2007, many EDFIs agreed on an exclusion list for joint investments (the Rome Consensus). This agreement also covered definitions for environmental and social risk rating categories and due diligence procedures. When CDC updated its own exclusion list in 2008, the EDFI agreement and the exclusion lists of other DFIs were used for inspiration.

A comparison of the exclusion lists of some major DFIs is given in the table that follows. CDC's exclusion list is compatible with those of the other EDFIs, the IFC, the AsDB and the EBRD, though CDC's exclusion list is shorter and does not include e.g. alcohol.

Investments from different development finance institutions (DFIs): comparing standards and procedures

Exclusions	CDC	EDFI	IFC	AsDB	EBRD
1. Local law and regulations and international conventions and agreements	Production or trade in any product or activity deemed illegal under local laws or regulations or banned as per global conventions and agreements, such as certain pesticides, chemicals, wastes, ozone depleting substances, and wildlife or wildlife products.	Production or trade in any product or activity deemed illegal under host country laws or regulations or international conventions and agreements. Production, use of or trade in hazardous substances subject to international phase-outs or bans.	Production or trade in any product or activity deemed illegal under host country laws or regulations or international conventions and agreements, or subject to international bans.	Production or trade in any product or activity deemed illegal under host country laws or regulations or that contravenes any international conventions and agreements to which the host country is a party, and which have the force of law in the host country.	Activities prohibited by host country legislation or international conventions relating to the protection of biodiversity resources or cultural heritage. Other activity in violation of host country (i.e. national) health, safety and environmental laws or regulations. Other activity in violation of host country (i.e. national) health, safety and environmental laws or regulations. Products prohibited for import to, or exports from, the relevant countries by applicable law or international convention.
2. Weapons and munitions	Manufacturing of equipment (including nuclear products) primarily designed or primarily designated for military purposes.	When a substantial part of primary operations: production or trade in weapons and munitions. (defined as 5-10% of the balance sheet).	Production or trade in weapons and munitions.	Production or trade in weapons and munitions.	Armaments and munitions.
3. Forced labour and child labour	Covered in CDC's Investment Code in section on social matters; labour and working conditions.	Production or activities involving forced labour or child labour.	Production or activities involving harmful or exploitative forms of forced labour / harmful child labour is explicitly excluded for all investments by financial intermediaries (FIs).	Production or activities involving harmful or forms of forced labour / child labour.	Activities involving harmful or exploitative forms of forced labour / harmful child labour, discriminatory practices, or practices which prevent employees from lawfully exercising their rights of association and collective bargaining.
4. Unbonded asbestos fibres	Production, use of, or trade in unbonded asbestos fibres, excluding cement sheeting where the asbestos content is less than 20%.	Production or use of or trade in hazardous materials such as unbonded asbestos fibres.	Production or trade in unbonded asbestos fibres, not applicable to purchase and use of cement sheeting where the asbestos content is less than 20%.	Production of or trade in or use of unbonded asbestos fibres.	Production, use or trade in unbonded asbestos fibres and asbestos containing products excluding asbestos cement sheeting where the asbestos content is less than 20 per cent.

Note: Unbounded asbestos fibres were once widely used in construction, primarily for insulation, but have now been banned in many countries as asbestos can cause lung cancer when inhaled. Cross-boundary movements of asbestos are covered by the Basel Convention on hazardous wastes. Trade in asbestos is covered by the Rotterdam Convention. Production or use of asbestos is not covered by comprehensive global agreements and is therefore explicitly covered by DFI exclusion lists. See *Appendix 5*.

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Investments from different development finance institutions (DFIs): comparing standards and procedures

Exclusions	CDC	EDFI	IFC	AsDB	EBRD
5. Gambling	When a significant source of revenue: the establishment or operation of casinos or any form of gambling.	When a substantial part of primary operations: gambling, casinos and equivalent enterprises. (Defined as 5-10% of the balance sheet).	Gambling, casinos and equivalent enterprises.	Gambling, casinos, and equivalent enterprises.	
6. Pornography and prostitution	When a significant source of revenue: pornography or the provision of products or services of a substantially similar nature.	Any business relating to pornography or prostitution.			
7. Tobacco	When a significant source of revenue: manufacture or distribution of tobacco or tobacco related products (unless phase-out plan in place).	When a substantial part of primary operations: production or trade in tobacco.	Production or trade in tobacco.	Production of or trade in tobacco.	Tobacco and tobacco products.
8. PCBs	Production, use of or trade in PCBs is covered in CDC's exclusion list as per the reference to global conventions and agreements.	Production or use of or trade in hazardous materials such as PCBs.	Production or trade in any product or activity deemed illegal under international conventions and agreements or subject to international bans – explicitly including PCBs.	Production, commercial-scale use, trade, storage, or transport of products containing PCBs.	Production or trade in products containing PCBs.
Note: PCBs are polychlorinated biphenyls, highly toxic chemicals found in e.g. oil-filled electrical transformers, capacitors and switchgear from 1950-1985. PCBs are subject to international bans along with 11 other persistent organic pollutants (POPs), 'the dirty dozen' as per the 2001 Stockholm Convention. See *Appendix 5*.					
9. Ozone depleting substances	Production, use of or trade in ozone depleting substances banned under the Montreal Protocol is covered in CDC's exclusion list.	Production, use of or trade in hazardous substances which are subject to international phase-outs or bans: explicitly including ozone depleting substances.	Production or trade in any product or activity deemed illegal under international conventions and agreements or subject to international bans: explicitly including ozone depleting substances.	Production or trade in ozone depleting substances subject to international phase outs or bans.	Production, use or trade in CFCs, halons and other ozone depleting substances subject to international phase-out.
10. Hazardous wastes	Unsafe transport of hazardous wastes is regulated under the Basel Convention and covered in CDC's exclusion list.	Cross-border trade in waste and waste products unless compliant to the Basel Convention and the underlying regulations.	No direct reference, but covered under general ban of illegal activities as covered by international conventions.	Trans-boundary trade in waste or waste products, except for non-hazardous waste destined for recycling.	Trans-boundary trade in waste or waste products.

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Investments from different development finance institutions (DFIs): comparing standards and procedures

Exclusions	CDC	EDFI	IFC	AsDB	EBRD
11. Hazardous chemicals	Production, use of or trade in hazardous chemicals subject to global conventions and agreements is covered in CDC's exclusion list.	Production, use of or trade in hazardous materials such as chemicals subject to international phase-outs or bans.	Production or trade in any product or activity deemed illegal under international conventions and agreements or subject to international bans. For microfinance activities, production, trade, storage, or transport of significant volumes of hazardous chemicals, or commercial scale usage of hazardous chemicals is explicitly prohibited.	Production, commercial-scale use, trade, storage, or transport of products containing hazardous chemicals.	
Note: Hazardous chemicals are covered by the Stockholm Convention and the Rotterdam Convention. See *Appendix 5.*					
12. Hazardous pesticides	Production or trade in hazardous pesticides subject to global conventions and agreements is covered in CDC's exclusion list.	Production, use of or trade in hazardous substances which are subject to international phase-outs or bans: explicitly including pesticides / herbicides.	Production or trade in any product or activity deemed illegal under international conventions and agreements or subject to international bans: explicitly including pesticides / herbicides.	Production or trade in pesticides / herbicides subject to international phase-outs or bans.	Production, distribution, sale and trade in pesticides / herbicides subject to international phase-outs or bans.
Note: Hazardous pesticides are covered by the Stockholm Convention and the Rotterdam Convention. Hazardous pesticides are also covered by the FAOs international code of conduct on the distribution and use of pesticides, and the WHO recommended classification of pesticides. Pesticides are also explicitly treated in IFC's Performance Standard 3 and in relevant industry guidelines. See *Appendix 5.*					
13. Wildlife and wildlife products	International trade in wildlife and wildlife products banned by CITES is covered in CDC's exclusion list.	Trade in wildlife or wildlife products regulated under CITES.	Trade in wildlife or wildlife products regulated under CITES.	Trade in wildlife or wildlife products regulated under CITES.	Trade in wildlife or wildlife products regulated under CITES.
14. Hazardous pharmaceu-ticals	Indirectly covered with a specific reference in CDC's Investment Code, section on Social Matters, Health & Safety, rather than in the exclusion list.	Production, use of or trade in hazardous substances which are subject to international phase-outs or bans: explicitly including hazardous pharmaceuticals.	Production or trade in any product or activity deemed illegal under international conventions and agreements or subject to international bans: explicitly including pharmaceuticals.	Production or trade in pharmaceuticals subject to international phase-outs or bans.	Production, distribution, sale or trade in pharmaceuticals subject to international phase-outs or bans.
Note: Unlike the hazardous products referred to in the previous sections, it is not as straightforward to obtain information from the WHO or UN on banned pharmaceuticals. ECOSOC of the UN issues a bi-annual list of pharmaceutical products that have been banned / withdrawn by any member country, but that does not make this list binding on other countries. The WHO hosts an annual conference on drug regulation, but this is more a way for regulators to meet and discuss collaboration. Pharmaceuticals are therefore covered in CDC's Investment Code instead of included in the exclusion list, with references to the IFC EHS Guidelines / WHO GMP standards that specifically deal with pharmaceuticals. See *Appendix 5.*					

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Investments from different development finance institutions (DFIs): comparing standards and procedures

Exclusions	CDC	EDFI	IFC	AsDB	EBRD
15. Radioactive materials	Not covered	Production or use of or trade in hazardous materials such as radioactive materials.	Production or trade in radioactive materials. This does not apply to the purchase of medical equipment, quality control equipment and any equipment where the radioactive source is considered to be trivial and / or adequately shielded.	Production or trade in radioactive materials, including nuclear reactors and components thereof.	Production, storage, treatment disposal or trade in radioactive materials and radioactive wastes. This does not apply to the purchase of medical equipment, quality control equipment and any equipment where the radioactive source is considered to be trivial and / or adequately shielded.
Note: Nuclear materials for military use are covered in CDC's exclusion list. Radioactive materials for civilian use are not banned by CDC, provided that adequate safety measures are taken.					
16. Alcohol	Not covered	When a substantial part of primary operations: production or trade in hard liquor. (Defined as 5-10% of the balance sheet).	Production or trade in alcoholic beverages (excluding beer and wine).	Production of or trade in alcoholic beverages (excluding beer and wine).	Hard liquor (over 12% alcohol volume).
17. Drift net fishing	Not covered	Drift net fishing in the marine environment using nets in excess of 2.5 km in length.	Drift net fishing in the marine environment using nets in excess of 2.5 km in length.	Marine and costal fishing practices, such as large scale drift net fishing and fine mesh net fishing, harmful to unwanted vulnerable and protected species in large numbers and damaging to the marine biodiversity and habitats.	Drift net fishing in the marine environment using nets in excess of 2.5 km in length.
Note: Large-scale fishing is covered by CDC's Investment Code as an area that warrants an Environmental Impact Assessment, with reference to IFC's EHS Guidelines for fisheries. See *Appendix 5.*					
18. Critical habitat	Indirectly covered: critical habitats are mentioned in CDC's Investment Code as an area that warrants an Environmental Impact Assessment, with reference to the relevant IFC Performance Standard and EHS Guidelines. See *Appendix 5.*	Destruction of critical habitat, defined as areas of high biodiversity value, habitat of endangered species, primary forests, forests of high conservation value, etc.	For investments by financial intermediaries (FIs), production or trade in wood or other forestry products other than from sustainably managed forests is excluded. Commercial logging operations for use in primary tropical moist forest is also excluded for FIs.		
19. Other references in exclusion lists		Production and distribution of racist, anti-democratic and / or neo-nazi media.			

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Investments from different development finance institutions (DFIs): comparing standards and procedures

Case 15: ESG improvements during the investment duration: Brookside Dairy, Kenya

CDC first invested US$1.2m in Brookside Dairy in Kenya in 1998 to finance the expansion of Brookside Dairy's capacity and to help the business diversify into the production of dairy products such as yoghurt and butter. In 2004, Brookside Dairy sourced its milk supply from over 65,000 farmers, the majority of which were otherwise only producing for family and community consumption. The investment in Brookside Dairy proved successful and generated a 21% IRR on exit for CDC.

Brookside Dairy has gained internationally recognised ISO 9000 certification. The company also worked closely with the Kenyan authorities to establish new environmental standards for the Kenyan dairy industry. An important consequence of the new improved Kenyan dairy standards has been the increasing ability for Brookside Dairy to expand its sales and operations internationally. Brookside Dairy currently has fully-fledged operations also in Tanzania and Uganda and exports as far afield as the Middle East.

Brookside Dairy has invested in an educational campaign on improved nutrition and the benefits of milk for a balanced diet. Through such initiatives, the company seeks to promote its positive brand image and increase awareness of its products.

Appendix 8

Investments from different development finance institutions (DFIs): comparing standards and procedures

8.3 Legal agreements

CDC

As part of the investment agreement with CDC, fund managers are required to commit to CDC's Investment Code, see p. 9-13. This is normally accomplished through CDC's standard side letter. Fund managers are expected to implement management systems which effectively identify and address ESG risks in their portfolio companies, and to work with portfolio companies to manage such risks and bring about improvements in business practices during the investment period.

[LETTERHEAD OF PORTFOLIO COMPANY]

[DATE]

FUND LIMITED

Subscription of shares by Fund Limited: Undertaking to comply with CDC's Investment Code

Dear Sirs,

We refer to your agreement to subscribe to shares in our company, set forth in that certain Subscription Agreement dated (date). We acknowledge that a condition precedent to your obligation to complete and fund your subscription of shares is that we deliver to you a signed undertaking regarding CDC's Investment Code.

If a fund manager proposes an alternative agreement that satisfies CDC's requirements, CDC may agree to such an agreement. This would typically be expected from funds with other DFI investors. As a general rule, CDC will normally agree to language approved by other DFIs, as long as the agreement explicitly refers to:

- responsible investment practices for the fund managers (in line with CDC's Investment Code);
- responsible business practices for portfolio companies (in line with CDC's Investment Code; see *Tool 10* for CDC's recommended investment undertaking); and
- improvements over time with targets and time frames, with the IFC's Performance Standards and EHS Guidelines as benchmarks for portfolio companies in high-risk sectors. See *Appendix 5*.

The investment agreement should also include:

- an exclusion list which covers the areas where CDC's capital will not be invested;
- an annual ESG reporting requirement in a format satisfactory to CDC; and
- a requirement to inform CDC as soon as possible about any instance involving portfolio companies which result in loss of life, material effect on the environment or material breach of law.

EDFIs

Most European DFIs typically require adherence to the IFC Performance Standards and EHS Guidelines as a core part of their investment agreements with fund managers.

IFC

The IFC requires a side letter legal agreement with fund managers that invest its capital. Requirements in IFC's side letter include:

- adherence to IFC Performance Standards and EHS Guidelines;
- right to visit, upon reasonable notice, the premises of fund portfolio companies;
- a seat on the fund advisory committee;
- the right to opt out of participating in an investment holding vehicle; and
- an acknowledgement of the IFC's interest in potential co-investment opportunities.

8.4 Reporting

DFI investors typically require fund managers to produce an annual ESG report for their investments. CDC's reporting requirements and recommended reporting template are comparatively simple, as described on p. 19-20, in *Tool 12* and *Appendix 7*. Other DFIs request similar information. CDC will accept reporting in the format used by other DFIs if CDC's core reporting requirements are covered.

Investments from different development finance institutions (DFIs): comparing standards and procedures

IFC

The IFC requires reporting on the same annual economic data for portfolio companies as does CDC (turnover, EBITDA, taxes and employee numbers), with the additional requirements to report the number of female employees and whether the fund manager has a board seat in each company in which they are invested.

Annual environmental and social report for financial intermediary clients

Please provide responses to the questions below. Please include additional sheets or attachments as required to provide details on questions that have been answered Yes.

Organisation			
Completed by (name)			
Position and contact information		Date	

Portfolio information

Report covering period:	
From	To

Fund business lines and portfolio type

For the reporting period, please provide the following (as applicable)

Product line	Expected holding period	Total exposure (US$m)	Average transaction size (US$m)	Maximum transaction size (US$m)
Listed equity				
Private equity				
Market debt instruments				
Private placed debt				
Other (please describe)				

Exposure by industry sectors

Please completely list the sectors where the fund invests and provide an indicative % of portfolio.

Industrial sector	Indicative % of portfolio
Animal production	
Apparel	
Chemicals	
Collective investment vehicles	
Common carriers	

In addition, the IFC requires an annual 'Environmental and Social Report for Financial Intermediary Clients' to be completed. This report covers the industry sectors of the fund's investments as well as a description of environmental and social risks and 'compliance status' (see 8.3 *Legal agreements* and *Appendix 5*). Where action plans are necessary for improvements for a portfolio company, these are requested as attachments. In addition, a report is required about the environmental and social management system for the fund. IFC's questionnaire seeks information about policy and processes, staffing capacity and monitoring and reporting on environmental and social issues.

For more information: www.ifc.org

DEG

The German DFI DEG has developed a comprehensive excel-based tool to assist its environmental and social risk management, called the Environmental and Social Risk Indicator (EaSI). Based on a series of interactive drop-down questions characterising a given investment opportunity, EaSI provides an assessment of the potential impacts of an investment by means of an environmental and social categorisation. It assesses an investee company's environmental and social performance, i.e. its capacity to manage these impacts. Based on these, the EaSI tool provides a detailed understanding of the scale and significance of the actual environment and social risk encountered for an investment. DEG uses this tool for single investment assessments and for portfolio-wide risk management throughout the investment cycle, as it allows for comparison between investments in different sectors. Two versions exist of EaSI: for financial institutions and for direct investments. Fund managers can use EaSI for their environmental and social risk management purposes. The EaSI tool can be purchased from DEG.

The EaSI tool enables the user to quantify and evaluate environmental and social risks. Basic inputs are the sector, the location and the type of investments as well as the number of employees. EaSI also covers the risk management systems employed and whether standards agreed upon are met or not. For financial institutions, the portfolio risk of investee companies is assessed along with the risk management system used by the institution.

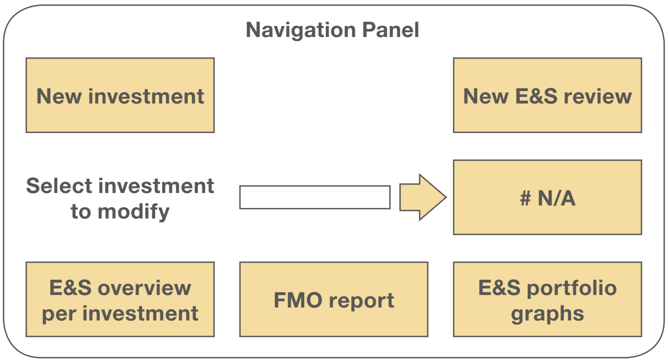
For more information: www.deginvest.de

Appendix 8

Investments from different development finance institutions (DFIs): comparing standards and procedures

FMO

The Dutch DFI, FMO, has developed an excel based assessment and reporting tool which is intended to provide a structured approach to environmental and social due diligence, reviews and management. At the level of the investment portfolio, FMO's tool can provide graphical overviews of the aggregated environmental and social situation of the entire investment fund. This overview can also be used for reporting purposes from the fund manager to FMO. The data input into FMO's tool is designed to be limited to make it as easy to complete as possible. The purpose is not to provide every possible answer but to offer a structured approach to assessing and reporting on the environmental and social aspects of investments.



FMO's tool is accompanied by a separate data sheet that supplies information specific to different industry sectors and country specific risks.

The three main categories of FMO's tool are risks, risk management and opportunities for improvement. Based on a number of characteristics of an investment, FMO's tool provides an overview of the most relevant environmental and social risks, a score on the effectiveness of the risk management and the main environmental and social opportunities. FMO's tool is based on the IFC Performance Standards. The outputs of FMO's tool provide detailed information for fund managers and FMO and identify opportunities for improvements for portfolio companies.

For more information: www.fmo.nl

8.5 Evaluations

CDC

Many DFIs, including CDC, perform evaluations of their fund investments to understand the development effects of these investments over a longer period of time. Evaluations provide an understanding of the development impact of investments in emerging markets across a spectrum of sectors and regions. Many of CDC's evaluations are conducted by consultants to lend objectivity and transparency to the evaluation process as well as to gain insights on CDC's performance from an external source. Other evaluations are conducted by CDC's investment team, assisted by ESG specialists.

Midpoint evaluations are conducted by CDC at the end of the fund's investment period, typically five years into the life of the fund. Final evaluations are conducted at the end of the duration of the fund, typically after 10 years. See *Appendix 6* for a more complete description of CDC's monitoring and evaluation system.

Investments from different development finance institutions (DFIs): comparing standards and procedures

IFC

The IFC assesses the development results of its investments, including through funds, according to a system called development outcome tracking system (DOTS). DOTS assesses each investment according to key performance areas, including indicators and benchmarks for financial performance, economic performance, environmental and social performance and private sector development impact. The key performance indicators are very similar to CDC's monitoring and evaluation framework and were an inspiration behind it. An important difference is that CDC's framework for ESG performance also includes governance, as per CDC's Investment Code, which covers business integrity as well as corporate governance, while corporate governance is part of the private sector development impact in IFC DOTS.

Professional judgement is used by IFC's staff when rating investment performance as certain effects are more important than others for some investments.

DOTS provides the IFC with an on-going assessment of the development effects of investments throughout IFC's project cycle, which is used for monitoring purposes in the same way as CDC uses annual reports from its fund managers for its monitoring and management purposes.

IFC employs a series of industry specific 'reach' indicators that provide additional information on the development reach of its investments. 'Reach' indicators are used by IFC to complement its assessment of development effects for both its investment projects and advisory services.

IFC DOTS indicators for fund investments

Financial performance	• Funds disbursed (%, US$): to be used until 3 years after first closing • Net IRR (%): to be used beyond 3 years from first closing
Economic performance	• Total and new jobs at investee level (#) • Total and new female jobs at investee level (#) • Taxes paid (US$) • Investees that are SMEs at the time of investment (#, % of investees) • Investees with positive growth in sales (% of investees, US$). Optional: high growth investees (>20% in sales growth) • Investee companies with positive labour productivity (%)
Environmental & social effects	• E&S management system of the fund
Private sector developments	• Investees in IDA countries (#, %) • Investees where the fund manager has a board seat (#, % of investees) • Emerging fund manager (Y / N) • Local fund manager (Y / N) • Corporate governance: improved governance at the fund level (Y / N) • Ability to raise a follow on fund (Y / N) • Non-DFI funding in follow-on fund (US$, %)

For more information: www.ifc.org

Appendix 8

Investments from different development finance institutions (DFIs): comparing standards and procedures

DEG

The German DFI, DEG, has developed a system of internal portfolio assessment during due diligence and portfolio reviews called the corporate policy project rating (GPR), which has been in use since 2002. DEG uses its GPR to assess the quality of its investments, including its investments through funds. GPR appraisals take place before an investment is made to set targets for that investment as well as during and after an investment to measure actual performance. GPR has specific information requirements for different sectors including infrastructure, the financial sector, manufacturing and private equity funds.

The GPR has an index point ranking system that combines four benchmarks:

- the long-term profitability of a project;
- development effects and sustainability;
- the special role of DEG; and
- return on the equity of DEG.

The GPR framework is quite similar in substance to that used by CDC and the IFC. As with CDC's monitoring and evaluation framework and IFC's DOTS, specific GPR indicators are monitored annually and used for evaluations. Each indicator is weighted by DEG, which gives each investment scores out of 500 points. Investments that score more than 320 points are categorised as 'very good'. Scores for specific indicators are also used to map out a GPR profile for an investment to demonstrate a project's strengths and weaknesses.

In order to facilitate an understanding of how the GPR works in practice, DEG gives examples on its website of completed GPR evaluations. The GPR can be purchased from DEG. Several other DFIs currently use the GPR.

For more information: www.deginvest.de

Investments from different development finance institutions (DFIs): comparing standards and procedures

FMO

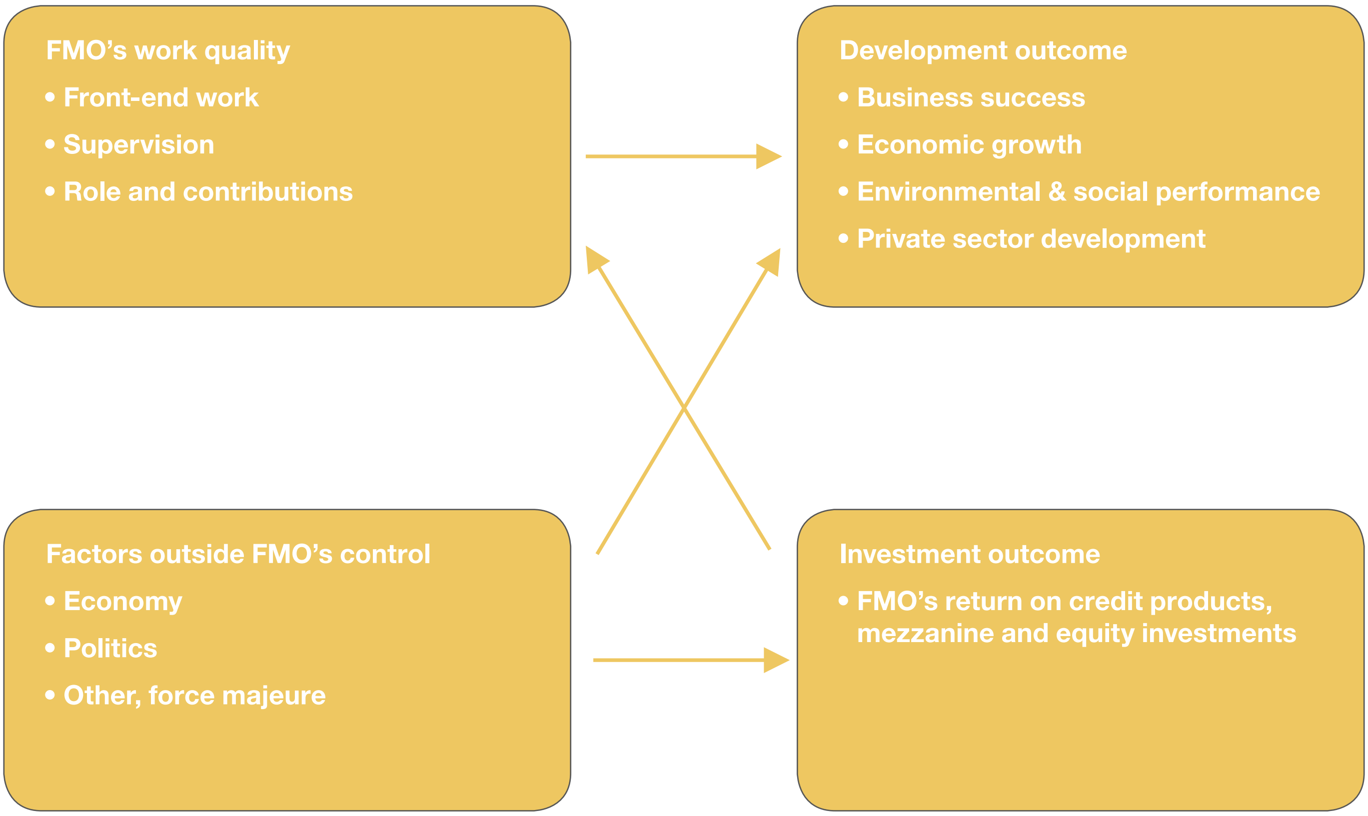
The Dutch DFI, FMO, evaluates the development effects of its investments by using its development impact indicator (DII) which is applied to every investment. FMO uses its DII to assess the expected development impact of an investment and the actual development effects during and after the investment duration. FMO has an internal evaluation unit.

FMO's evaluations assess three key categories of indicators:

- an investment's development outcome;
- FMO's investment outcome; and
- the quality of FMO's work in relation to the project.

The substance of the information that FMO monitors and evaluates is similar to that which CDC, IFC and DEG cover. FMO publishes yearly evaluation reports on the development effects of its investments on its website.

For more information: www.fmo.nl



Appendix 9

Climate change considerations: risks and opportunities

9.1 Introduction

Below is a summarised version of a guidance note prepared for CDC and CDC's fund managers by Forum for the Future. The full document can be downloaded from CDC's website www.cdcgroup.com.

This guidance note sets out the risks associated with climate change for fund managers and opportunities for them and their portfolio companies.

9.2 The significance of climate change to fund managers

Climate change is altering the competitive environment in which companies operate. A Carbon Disclosure Project (CDP) report surveying 500 leading firms across a range of industries has found that over 80% of these companies believe that climate change will present some sort of commercial risk. Firms that recognise the challenges posed by climate change and respond imaginatively will prosper more than those that do not. Present evidence indicates that climate change is likely to impose a slow but inexorable force on businesses. Fund managers should be aware of this and act now to reduce the risks and maximise the opportunities that climate change presents.

9.3 Risks resulting from climate change

Fund managers are faced with various risks to their portfolio companies as a consequence of climate change. These risks vary significantly between different industry sectors and country locations. Certain themes can be highlighted to suggest how climate change can impact emerging markets.

Physical risks

The most frequently stated risk is that of extreme weather. The World Bank has produced a list of countries most at risk of climate change driven disasters. Particular threats most likely to affect particular countries include:

- *drought*: Malawi, Ethiopia, Bangladesh;
- *flooding*: Bangladesh, China, India;
- *storm*: Philippines, Bangladesh, Madagascar;
- *coastal flooding*: low-lying islands, Vietnam, Egypt; and
- *agriculture*: Sudan, Senegal, Zimbabwe

All of the countries listed here except for China, Egypt and the Philippines are classified as low income countries by the World Bank, which makes them especially vulnerable given a lack of a budgetary capacity to respond to extreme weathers.

These physical risks can have an impact on operating costs for a business, either directly or through their supply chains. The physical impacts could affect access to raw materials, water or infrastructure (e.g. energy or transport) that the business depends on.

Regulatory risks

New regulations are likely to have an impact on businesses. Future regulations will be influenced by public and political pressure. The role of regulation in trying to prevent the worst effects of climate change means that businesses will experience short-term impacts on the cost of inputs before the physical impacts are fully felt. There will also likely be new regulations to apply industry standards to certain carbon-intensive products (e.g. boilers, light bulbs, engines). While these regulations may not come into force in the emerging markets for some time, they will have an immediate impact through supply chains.

Changes to the competitive environment

Even without new regulations, awareness of climate change is leading to a shift in consumers' demands for innovation and new products. Companies that respond to these new demands will be in a stronger position to succeed in the future.

Embedded carbon: Why it will impact companies in low-income countries

While the long-term ambition of companies such as Wal-Mart and Tesco to put carbon labels on the products they sell might seem somewhat divorced from the day-to-day concerns of businesses in low-income countries, the potential impacts could be huge over time.

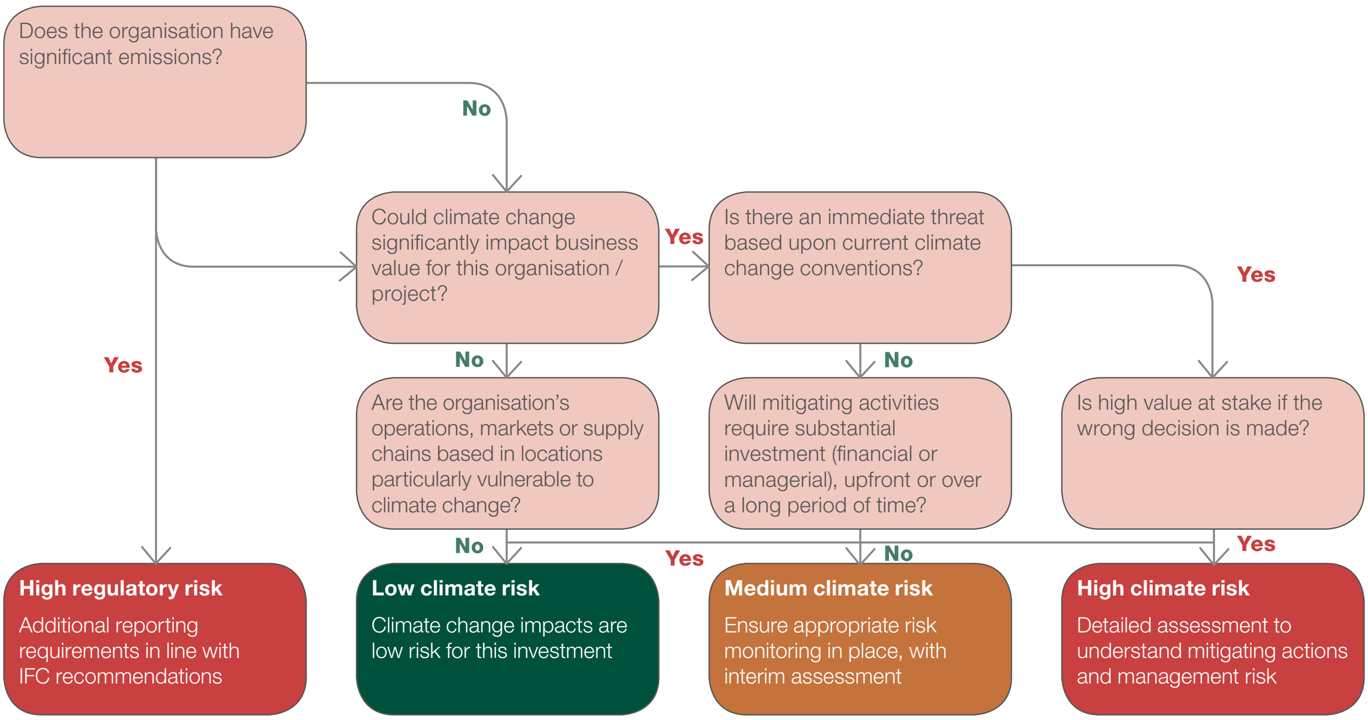
If a company in a low-income country does not invest now to improve its energy efficiency, or finds itself dependent on diesel- or coal-based electricity generation or carbon-intensive shipping processes, it may lose market share to companies that have improved their processes or found ways to meet their energy and shipping needs through low- or zero-carbon sources.

App 9

Climate change considerations: risks and opportunities

Risks and opportunities	Impacts on the corporate business model		
	Input costs	**Assets & operating costs**	**Income & revenue**
Physical	• Damage to public infrastructure on which the company depends. • Disruption to supply-chains, especially agricultural supply chains. • Water scarcity.	• Damage to corporate-owned infrastructure.	• Impacts on agricultural yields. • Impacts on product demand. • New product opportunities from new customer demands.
Regulatory	• Effects of regulation on energy / transportation costs.	• Future 'direct' climate regulation. • Potential legal costs.	• Future product standards. • Carbon markets.
Changes to the competitive environment	• Impacts of changes in the competitive landscape on suppliers.	• Impacts on insurance costs.	• Reputational impacts. • Changes in corporate procurement standards. • New low-carbon products and business models.

9.4 Process to assess climate change risk



Appendix 9

Climate change considerations: risks and opportunities

9.5 Opportunities arising out of climate change

Climate change does not just present risks to businesses. Proactive corporate management can also realise opportunities for sales growth and increased profits and valuations arising from the climate change driven circumstances. Potential opportunities include the areas listed below:

Innovative product design

Opportunities will arise for new products that take advantage of a changed competitive environment and new consumer preferences. Consumer preferences are likely to increasingly switch to low carbon products.

New markets

New markets can open up as a result of climate change. One example is the clean energy market which is expected to grow from US$77 billion in 2007 to over US$254 billion in 2017.[1]

Carbon credits

Carbon markets may also provide potential savings for companies whose products can result in greenhouse gas reductions. Under the Clean Development Mechanism (CDM), countries can meet emissions reductions targets by trading credits. These credits are called Certified Emissions Reductions (CERs).

Further information about carbon credits is contained in the full text of this guidance note.

9.6 Tools included in CDC's guidance note on climate change for fund managers:

The guidance note provides five tools for fund managers to manage the risks and opportunities from climate change. By following analyses of this type, fund managers will be able to assess and implement suitable reduction of emissions of greenhouse gases from the operations of their portfolio companies.

Tool 1

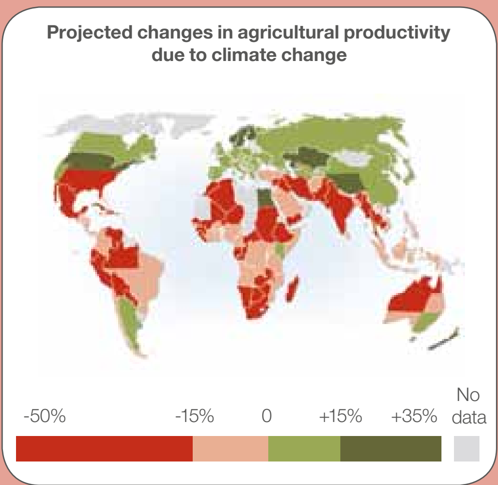
Questions for fund managers to ask portfolio companies This Tool is designed to help fund managers consider the risks and opportunities that may impact on a particular company as a result of climate change. It also considers whether a company should report to investors on the nature of applicable climate change risks.

Tool 2

Monitoring and reporting This Tool shows how a fund manager can report the risks of climate change to its investors. Emissions above 100,000 tonnes of greenhouse gases equivalent per year from a company is regarded as high and should be closely monitored and reported on. This Tool also suggests further tools

Case 16: The effects on agriculture from climate change

Agriculture is extremely vulnerable to climate change. A 2008 study by Stanford University looking into the potential impacts of climate change on agricultural production concluded that, 'the crop with the single largest projected impacts is maize in Southern Africa, currently the most important source of calories for the poor in this region. Losses by 2030 are expected to be a remarkable 30%, relative to production in 1990.'



Climate change is likely to result in gains for some crops in some regions of the world. A number of climate models have predicted that East Africa is likely to become wetter as a result of climate change, for example. This has led to hope that countries such as Kenya and Uganda might benefit (see map). However, a 2008 report looking at the impacts of climate change on Uganda concluded that 'there can be more rain and yet also more drought; what matters for farmers is the effectiveness, timing and distribution of rain throughout the crucial growing seasons.' Thus far, rains in East Africa have become less reliable, with negative impacts on agriculture.

Source: Center for Global Development and Peterson Institute for International Economics (2007), *Global Warming and Agriculture: Impact Estimates by Country.*

[1] 'Clean Energy Trends 2008'; Clean Edge www.cleanedge.com

Climate change considerations: risks and opportunities

that a fund manager can use to calculate a company's emissions in tonnes of carbon per year, including the Greenhouse Gas Protocol, the Carbon Disclosure Project and the Carbon Trust.

CDC also encourages fund managers to use the French aid agency AFD's and the French development finance institution Proparco's practical tool for assessing carbon emissions. See AFD's website http://climatechange.afd.fr

Reporting from fund managers to CDC on climate change could include:

- key areas of risk for portfolio companies and actions being taken by them;
- portfolio companies with greenhouse gas emissions above 100,000 tonnes equivalent per year with targets and action plans for reductions; and
- ways in which the investment strategy of the fund is influenced by climate change considerations.

Tool 3

Sector risks and opportunities Whilst all sectors are at risk from climate change, some sectors are more vulnerable than others. Different opportunities for business development are present for different industry sectors. This Tool presents individual industry sectors by the type of climate change risks and opportunities arising in each sector.

Tool 4

Assessing location risk and opportunity Similar to industry sectors, different regions and countries are affected by climate change in different ways. This Tool guides a fund manager towards thinking through the potential impacts of geography on both the company and its supply chain.

Tool 5

Creating opportunities through the carbon market This Tool explores how companies and fund managers can tap into the carbon market, explaining how the carbon market currently works and how to seek funding.

Case 17: New, profitable investments driven by climate change: E+Co[2]

E+Co makes clean energy investments in over 20 developing countries by identifying and supporting entrepreneurs through locally-based investment officers. E+Co has invested more than US$32m of seed and growth capital over 15 years in more than 200 companies, typically in small and medium sized enterprises (SMEs). E+Co's portfolio includes both debt and equity investments, with a projected weighted average IRR of 8.4%. With 1.6 billion people worldwide living without electricity and more than 2 billion people cooking with firewood and charcoal, innovations are needed to help provide energy for the poorest people in the world as the global energy sector becomes increasingly competitive, while recognising the climate change risks that follow from increased global energy use.

E+Co has invested in companies manufacturing and selling energy-efficient cooking stoves. Among these are Kunming Rongxia Stove Co. in China and Sodigaz, a business supplying cooking fuel to more than 21,000 households in rural Mali. Inefficient cooking stoves cause indoor pollution and are often powered by burning coal, charcoal, or wood. As coal burning emits greenhouse gases, there is demand both for efficient fuels and for the efficient use of such fuels. A major obstacle is that energy-efficient cooking stoves are often unaffordable for poor people in developing countries.

Through carbon credits, E+Co has managed to provide energy-efficient solutions for household cooking in a manner that is also profitable for entrepreneurs and investors. The stoves that E+Co's portfolio company sells in Ghana cost between US$5 and US$27 (the US$27 stove is mainly used by restaurants). In Mali, the cost is between US$5 and US$8. On average, entrepreneurs selling these stoves get about US$10 per stove in carbon credit. The carbon credits system thus provides a critical lever to lower the price of products for consumers while also sustaining profitability.

[2] www.eandco.net

Appendix 10

Gender considerations: good practices for investors and businesses

It is important for all companies to consider how business operations may impact men and women differently. Gender considerations are particularly important for women of child bearing age and from a non-discriminatory / non-harassment perspective.

The purpose of the table opposite is to show companies and investors how they can implement policies and practices that benefit women in the workplace. The extent to which best practices can be implemented varies depending on local and regional customs and cultures amongst other influencing factors. Investors and companies would therefore need to apply sound judgement in deciding what policies would be appropriate.

Other sources for guidance on how to address gender matters for companies in developing companies include IFC's Women in Business Program, see www.ifc.org, and the United Nations Development Fund for Women (UNIFEM), see www.unifem.org.

Case 18: Good gender practices in agriculture: a tea farm in Malawi[1]

Since a fund manager invested in a medium-sized tea farm in Malawi, production capacity has increased two-fold in two years. Staff numbers have also risen by 120 to a total of 280 employees. Most workers migrate to the tea farm during harvest season and 40% of the workforce is female. The fund manager has introduced best-in-class facilities to cater for this increase in employment numbers, with due considerations from the gender perspective and in respect to the non-local nature of the workforce.

In particular, new staff houses have been built, providing top quality on-site housing for 45% of employees and their families. The housing facilities provide separate living areas for male and female employees, with separate accommodation for families and segregated sanitary facilities. The compound has been electrified to improve the quality of accommodation for employees and their families. A school and a healthcare clinic are operated by the tea farm for employees and their families.

Moreover, with assistance from the fund manager, grant funding has been secured for the development of a HIV / AIDS management programme. Under this programme, education and awareness of HIV / AIDS has improved dramatically. A new clinic has provided access to voluntary testing and anti-retroviral drugs for employees and their families. It is estimated that the programme could reduce company healthcare costs by 45% through HIV prevention.

[1] This inspirational good-practice case draws upon the experiences of more than one company.

Gender considerations: good practices for investors and businesses

	Gender equality in corporate governance	Gender equality in the workplace
Best practice	The company has a gender policy with measurable targets for recruitment, and a timetable and procedures for monitoring its implementation. Gender equality is included as a company performance indicator. A budget exists for gender equality initiatives at the organisational level. The company monitors and reports on measurable targets for gender equality improvements connected to its operations, reports results regularly and makes this data available to the public. The company has at least one female board member.	The company provides maternity benefits which include leave in excess of 6 months in connection with childbirth and an excess of 75% reimbursement of salary during that time. The company provides child care support for employees. Paternity leave is given in connection with childbirth.
Good practice	The company has a gender policy with an organisational plan on how to achieve this policy.	The company provides maternity benefits including leave of at least 3 months in connection with childbirth and partial reimbursement of up to 75% of salary during that time. The company's recruitment panels include both men and women. The company implements actions to encourage work-life balance such as flexible work hour options. The company conducts regular fair pay reviews.
Minimum	The company's policies state a clear commitment to gender equality and condemns gender based discrimination and sexual harassment. The company has assigned responsibility and accountability for gender matters.	The company allows employees to take time off work for childbirth and family-related responsibilities. The company practices non-discrimination in recruitment. Contract conditions for men and women are equal and non-discriminatory. The company pays equal wages and provides equal benefits to men and women for equal work. Men and women are promoted equally. Workers group / collective / union represents women's interests as well as men's and include female representation. The company's employment and promotion policies do not discriminate based on marital or reproductive status. The company's retrenchment policy is not biased against women. The company provides maternity benefits including leave of a minimum of 6 weeks in connection with childbirth and ensures retention of the same or an equivalent job with no substantial change in contractual or other relevant terms. The company provides adequate sanitary facilities for women, which are separated from male facilities. The company provides separate housing for men and women for operations in remote locations.
Unacceptable	The company is silent on gender equality in its policies, procedures and corporate communication. The company violates legislation and standards which adversely impacts their female employees (e.g. involuntary or mandatory pregnancy testing) and / or; the company violates the ILO's core labour standards with adverse impacts for the female workforce (e.g. discrimination based on gender grounds or preventing women from organising in trade unions or workers councils). See *Appendix 5*.	No time off for childbirth is granted for female employees. Incidences of sexual harassment, physical and / or psychological abuse of women. Exposure of women to detrimental substances or working conditions. Forced female labour or trade in women. Incidences of intimidation of women to prevent them from participating in decision-making processes.

Appendix 10

Gender considerations: good practices for investors and businesses

Case 19: Good gender practices in retail: Best Buy's 'results only work environment'

Best Buy's 'results only work environment' initially started as an experiment to stem attrition in two departments at the corporate headquarters but after its initial success, began to be implemented more widely. The basic premise of the programme was that work meant the achievement of results and not presence at the workplace. Accordingly, employees working under the programme were allowed to work when they wanted and where they wanted, as long as they achieved their targets. As of late 2006, more than 50% of the employees at Best Buy's headquarters were involved in the programme.

In late 2006, Best Buy announced that it was working on a project that would allow the 'results only work environment' to be implemented in a modified form in the company's retail stores, which employed almost 120,000 people. The company believed that an employee-friendly work environment could provide a solution to the problem of high attrition in the stores. Best Buy's voluntary attrition in its retail stores was around 65% in 2006. It is well-known that it is difficult to keep people working in retail because of the hours and the stress.

'Results only work environment' teams report an average of 3.2% lower voluntary turnover than other teams. Average productivity of 'results only work environment' teams had also increased by 35%. Employee engagement, which was a measure of job satisfaction and hence an important factor in retention, was also reported to be significantly higher in teams involved in the programme. Best Buy reportedly witnessed several non-quantifiable benefits as well. For instance, managers at the company said that the programme made their work easier. They admitted that, despite their previous misgivings, performance was actually easier to track under the programme than under conventional systems. Similarly, problems were also easier to identify and correct.

Gender considerations: good practices for investors and businesses

Case 20: Good gender practices in mining: a gold mine in Ghana[2]

Due to the remote location and greenfield characteristics of a gold mining investment in Ghana, the fund manager investing in this asset realised the importance of conducting a comprehensive environmental and social impact assessment and implementing international best practice standards prior to commencing mining operations.

Recognising the necessity of relocating workers to the mine site, the importance of ensuring that the existing local community would not be adversely affected by the influx of mostly male mine workers was immediately identified. This was deemed especially important to prevent an increase in prostitution and HIV / AIDS prevalence that might otherwise have affected the local vicinity. As a consequence, mine workers were encouraged to bring their families and housing was provided to accommodate them. The company set up school facilities for children as well as free access to a healthcare clinic.

Moreover, the company felt it essential to be a role model for corporate social responsibility and to demonstrate long-term commitment to the local communities. The company thus set up a foundation to help direct funding to develop programmes selected by the local communities. The foundation has spent approximately US$0.4m in the past two years on projects including funding of local schools and a water distribution system. The foundation uses panels of local community members to decide which projects are the most important to finance.

[2] This inspirational good-practice case draws upon the experiences of more than one company.

CDC would like to express its gratitude to the following organisations, initiatives and companies for content and / or advice that has been used for this Toolkit on ESG for fund managers. Summaries, interpretations and other adaptations of the original materials have been done by CDC and Rosencrantz & Co.

Actis

The Asian Development Bank

Aureos

The Boston College Center for Corporate Citizenship

The Boston Consulting Group

The Business Anti-Corruption Portal

The Centre for Financial Market Integrity CFA Institute

DEG

The Carbon Disclosure Project

The Equator Principles

The European Development Finance Institutions

The European Bank for Reconstruction and Development

The Extractive Industries Transparency Initiative

The Financial Action Task Force

Forum for the Future

FMO

Global Advice Network

Hystra

The International Accounting Standards Board

IFU

The International Finance Corporation

The International Labour Organization

The International Organization for Standardization

The International Private Equity and Venture Capital Guidelines

McKinsey & Company

Norfund

The Occupational Health and Safety Advisory Services

The Organisation for Economic Co-operation and Development

PricewaterhouseCoopers

Proparco

SIFEM

SustainAbility

Swedfund

Transparency International

The United Nations

The United Nations Environment Program, its associated Conventions and its Financial Initiative

The UN Global Compact

The UN Global Reporting Initiative

The UN Principles for Responsible Investment

UNIFEM

The United States Private Equity Council

The World Bank

The World Health Organization

The DFI working group on corporate governance, which includes the BSTDB, CAF, CDC, EBRD, FMO, IFC and IsDB

The EDFI working group on funds, which includes the BSTDB, CDC, DEG, FMO, Norfund, Proparco and SIFEM

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Actis

Aureos

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Best Buy

Bextex

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CDH

Compagnie Hévéicole de Cavally

Dalmia Cement

Deacons

Duoyuan Global Water

E+Co

Global Environment Fund

Himin

ICICI

Outsourcing Services Limited

Permira

Sainik Mining

Sathapana

Shelys Pharmaceuticals

ShoreCap International

Suntech Power

This Toolkit on ESG for fund managers was developed for CDC by Rosencrantz & Co in 2010. It builds on the Toolkit developed for CDC by Forum for the Future in 2006, with updates and extensive additions in line with CDC's new Investment Code, requests from fund managers and other stakeholders and recent developments in international best practices and standards, as well as feedback and lessons learnt.

CDC is the UK's development finance institution. Owned by the UK government's Department for International Development, CDC provides capital to invest in promising businesses, with a particular focus on sub-Saharan Africa and South Asia. By supporting the private sector, CDC contributes to long-term poverty reduction in developing countries.

www.cdcgroup.com

Forum for the Future
This sustainable development charity works in partnership with leading organisations in business and the public sector to identify practical ways that they can deliver a sustainable future through new products, services or processes. Forum for the Future believes that a sustainable future can be achieved, but that we need bold action now to make it happen.

www.forumforthefuture.org

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