

Risk management policy

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1. Policy objectives and background

1.1 Policy background

CDC's mission is to support the building of businesses throughout Africa and South Asia, to create jobs and to make a lasting difference to people's lives in some of the world's poorest places. Risk is an inherent component of CDC's activities. The ability to effectively identify, assess, measure, respond, monitor and report on risk in activities is critical to the achievement of CDC's mission and objectives.

1.2 Policy objective

The objective of this policy is to set out the principal risk types that may face CDC group, CDC's appetite for these risks, and how CDC will manage these risks.

1.3 Policy sponsor and maintenance

The CFO is the sponsor of this policy and is responsible to review and maintain this policy and submit it to the Board Risk Committee for review and recommendation to the Board for approval at a minimum once every two years.

2. Risk types

CDC has identified six main categories of risk that it may face:

- ✦ Financial Risk
- ✦ Development Impact Risk
- ✦ Environmental and Social (E&S) Risk
- ✦ Business Integrity (BI) Risk
- ✦ Operational Risk
- ✦ Strategic and External Risk

In addition to these risk types, CDC has identified reputational risk as a risk that it faces, which could be a consequence of any of the six main risk categories. These risks are further defined and sub-categorised in a separate document, the CDC Risk Taxonomy, which sets out the risk likelihood scale and risk impact definitions for each risk category. CDC assesses individual risks based on their impact and likelihood and compares these to the risk appetite set by the Board of Directors and summarised in section 3 of this policy.

2.1 Financial risk

The financial risks at CDC are the risks of underperformance or unacceptable volatility of the investment portfolio return, as well as liquidity risks. Financial risk includes:

- ✦ Portfolio return risk
- ✦ Individual investment risk
- ✦ Liquidity risk

2.2 *Development impact risk*

Development impact risk is the risk that CDC will fail to achieve its development objective to create jobs and make a lasting difference to people's lives in some of the world's poorest places. Development impact risk includes:

- ✦ Portfolio development impact risk
- ✦ Investment development impact risk
- ✦ Credibility of CDC's methodologies risk
- ✦ Additionality risk

2.3 *Environmental and social risk*

E&S risk is the risk that a business in which CDC has invested materially damages the environment, causes death or serious injury, fails to deliver appropriate working terms and conditions, or causes social harm.

E&S risk includes:

- ✦ E&S implementation risk
- ✦ E&S residual risk

2.4 *Business integrity risk*

BI risk is the risk that CDC, or a fund manager or portfolio company in which CDC has invested is involved in fraud, corruption, money laundering, terrorist financing, breaches of international sanctions regimes or breaches of other regulatory requirements. BI risk includes:

- ✦ BI implementation risk
- ✦ BI residual risk
- ✦ Regulatory risk

2.5 *Operational risk*

Operational risk is the risk of loss or other damage to CDC resulting from inadequate or failed processes, people and systems at CDC. This includes legal risks other than those directly associated with compliance with the requirements of regulatory bodies such as the FCA. Operational risk includes:

- ✦ Operational risk
- ✦ Legal risk

2.6 Strategic and external risk

The strategic and external risks at CDC are those risks which arise from the context in which CDC is operating and the strategic decisions that CDC has made. They are often long term in nature and frequently outside CDC's direct control. Strategic and external risk includes:

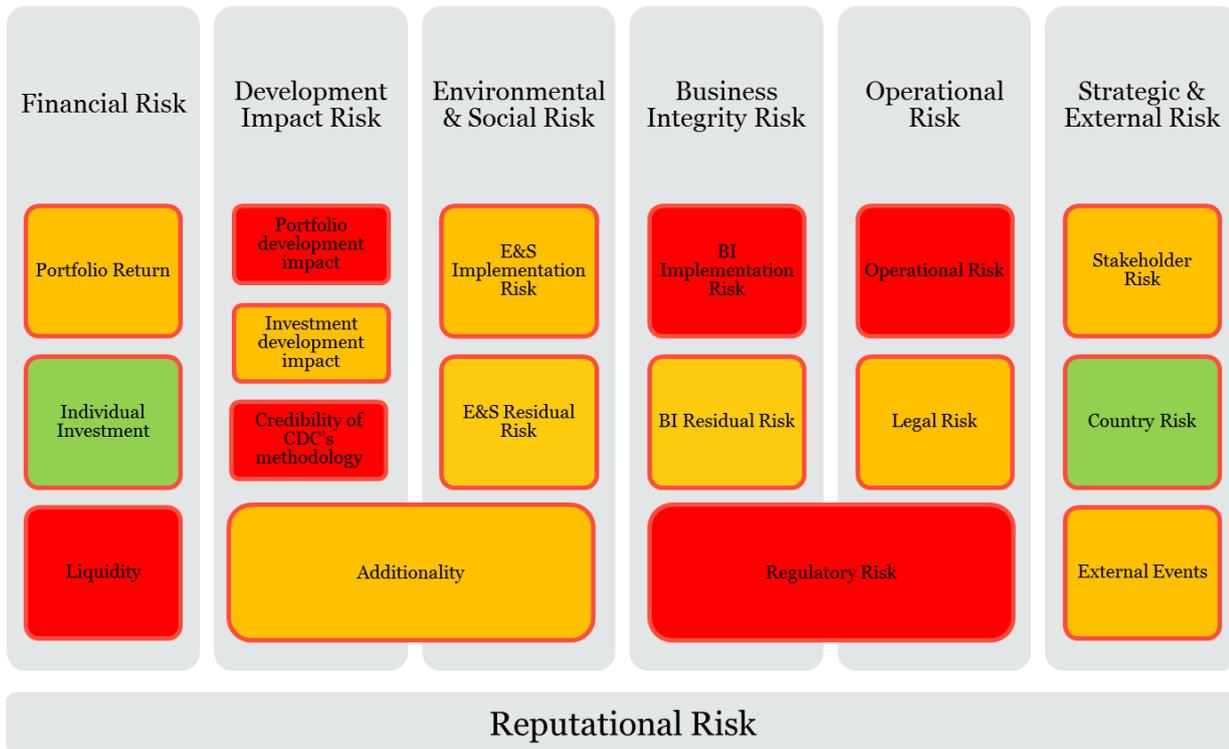
- ✦ Stakeholder risk
- ✦ Country risk
- ✦ External event risk

3. Risk appetite

Fulfilling CDC's mission requires us to take risks – some of which we actively seek out and some which arise as a result of our activities. CDC's risk appetite statement describes the types of risk that we face, the level of risk we are willing to take to achieve our mission and how we will respond to these risks. When developing our risk appetite statement, we have taken account of the following principles:

- ✦ CDC actively seeks our equity and credit risks resulting from investments in companies in developing countries in order to achieve both the targets set by its shareholder – achieving both a financial return on investment and development impact.
- ✦ Doing this business exposes us to environmental and social, business integrity and operational risks. We take active steps to understand and where appropriate mitigate or manage these risks so they do not damage our licence to operate.
- ✦ CDC's mission exposes us to high contextual risks, in particular related to investment returns, environmental and social damage and business integrity risk, which can never be fully mitigated.
- ✦ CDC's reputation is an important part of our licence to operate. We seek to manage and mitigate reputational risk by addressing the underlying causes of reputational risk and by engaging with stakeholders.

CDC's current risk appetite is summarised in the table below.



4. Behaviours and culture

The culture and behaviours of staff at CDC are critical to ensuring effective risk management. CDC encourages a culture of openness, willingness to learn and taking pride from fixing problems when they occur. CDC's policies and procedures set out expected behaviours, in particular the Business Integrity Manual and the Staff Handbook. Regarding risk management, the key requirements are:

- ✦ Risks and their management are considered in business decision making
- ✦ CDC management and staff are expected to disclose and take appropriate action to mitigate known risks

5. Governance and roles and responsibilities

5.1 Key roles and responsibilities

CDC's Board and Management are responsible for developing and implementing a risk framework which supports the identification and mitigation of risks to CDC's operations. Individual roles and responsibilities are set out below.

- ✦ **Board** – The Board is responsible for setting overall risk appetite and approving risk management policies.

- ✦ **Board Risk Committee** – The Board Risk Committee is established to oversee risk management and make recommendations to the board on risk management policy and risk appetite. The Board Risk Committee is also responsible for reviewing the principal risks facing CDC and escalating risk matters to the Board.
- ✦ **Management** – Management is responsible for implementation of the risk management policy and framework within their respective areas of responsibility. Management is responsible for monitoring levels of risk and developing action plans to reduce risks to within appetite if appropriate and escalating risk matters to the Board Risk Committee for their consideration. Management may assign responsibility for the management of specific risks to individuals within the firm, referred to as ‘Risk Owners’. Management is also responsible for setting ‘tone at the top’ in respect of risk management culture.

5.2 Three lines of defence

Within the company, CDC generally adopts a ‘three lines of defence’ model to managing risk. However, the size of the organisation means that in some cases there is overlap between the first and second lines of defence. This risk is mitigated by ensuring independent oversight from the Internal Audit function.

- ✦ 1st line – the functions that own and manage risk (Investment, Transaction Support and Corporate Functions)
- ✦ 2nd line – the functions that oversee risk (Investment Committees, Finance, OCIO, Risk Management and Compliance)
- ✦ 3rd line – functions that provide independent assurance (Internal Audit)

CDC’s Risk Management and Internal Audit functions seek to work collaboratively to ensure that risk identification and assurance work covers the full suite of risks facing CDC, while respecting the independence of the Internal Audit function.

The CEO, CFO and COO, as members of senior management with responsibility for risk management are viewed as above the three lines of defence.

6. CDC’s risk management framework

CDC’s management is responsible for developing and implementing a framework to identify, assess, measure, respond, monitor and report on risk within CDC’s activities. CDC’s risk framework consists of the following key components:

- ✦ **Establishing the context for risk management**
 - **Strategy and objectives** – CDC’s corporate objectives and individual / team objectives are defined each year. They provide the basis for determining CDC’s risk appetite.

- **Policies and procedures** – policies set the rules under which CDC will operate and procedures describe how these policies need to be implemented, including setting out the key controls in place to mitigate risk.

+ Risk assessment and risk treatment

- **Risk registers** – risk registers document the risks facing CDC, the controls in place to mitigate those risks and assess the impact and likelihood of the risk occurring. If risks are assessed as being outside appetite, mitigation plans are developed to reduce the level of risk.
- **Investment decision making and portfolio monitoring** – identification and assessment of the key risks associated with investments at the point of investment approval and during the life of CDC's investment
- **Key risk indicators** – key risk indicators are metrics used to provide an early signal of increasing risk exposures. They allow CDC to identify risk trends and take action before events occur.
- **Incident management** – incident management and analysis allows CDC to ensure appropriate action is taken when incidents occur (when risks crystallise), validate the contents of the risk registers and determine whether action is required to avoid reoccurrence of similar incidents in future.

+ Monitoring, review and communication

- **Risk reporting** – reporting on identified risks to management and the board, including emerging risks and those that require action.
- **Internal Audit monitoring** – independent monitoring of the implementation of the risk framework to ensure it is adequately designed and operating effectively.



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