CDC
Investment works

Commonwealth Development Corporation Bill
Updated January 2017

Comment from CDC's Chief Executive on the Bill

Diana Noble said: "Investment is a powerful way to deliver development and reduce poverty. A strong private sector generates the prosperity that will provide much-needed infrastructure, public services and jobs in developing nations. CDC has supported many now market-leading businesses and employers in Africa and South Asia during formative and, often, challenging periods of their early growth. And CDC's investments have generated good returns over its history, which are then recycled into further investments, making it an efficient use of UK taxpayers money.

The 1999 CDC Act set a limit on the level of financial support that the UK Government can provide to CDC. While raising the limit increases the Government's options in supporting CDC's future growth, on its own, the Bill doesn't lead to any further capital for CDC. All future decisions to invest in CDC will be supported by a robust business case."

The Bill can be found here. It receives its Third Reading on 10 January 2017.

CDC briefing on the introduction of the Bill:

The broad case for further investment in developing countries

There is now an international consensus that if we are to achieve the Global Goals for Sustainable Development by 2030, we need to mobilise the private sector to help fill the annual financing gap of $2.5 trillion every year.

No country has ever escaped poverty without its private sector playing a full role in developing a strong economy. The private sector creates the prosperity needed for countries to build infrastructure, provide much-needed public services, and create the jobs that give people the dignity and the means to help themselves.

We believe having a job is one of the best and first steps out of poverty. People living in the world's poorest countries agree: 70 per cent of respondents to the World Bank's 'Voices of the Poor' survey believed that a job was the best way to escape poverty.

The private sector needs a great deal of help in the poorest countries. Businesses lack access to finance and, because of the challenging operating environment, they also need expert advice and support to help their businesses grow. However, while there is demand, many investors and lenders are put off by the higher levels of risk. CDC is one of the few investors in the world with the skills and risk appetite to do this difficult work.

CDC's role

CDC's mission is to invest in businesses in the poorest parts of the world to help them grow and create the jobs that will make a lasting difference to people's lives. We invest in Africa and South Asia because that's where 80 per cent of the world's poorest people live. We prioritise investing where growth leads to jobs.

Investment sits alongside other development interventions, such as grant aid, and is particularly well suited to stimulating economic growth that will provide much-needed jobs and livelihoods.

CDC has a challenging dual objective to deliver development impact alongside a financial return. These go hand in hand: if a business isn't viable and profitable it won't maintain jobs and livelihoods over the long term.

In 2015, the businesses we invested in helped create over a million new direct and indirect jobs and paid $2.6 billion in local taxes. Our activity also encouraged US$832m of additional private sector investment.

We are wholly owned by the British taxpayer and our investments not only have a powerful development impact but also generate a return, which is recycled into future investments, making each pound invested go further.

This means that by 2030, the end of the period of the Sustainable Development Goals, each new pound invested in CDC will have supported two to three businesses, will have attracted further capital from private investors alongside it and will continue to grow and generate more impact in the years to come.

Our growth in context

CDC is still relatively small by comparison with our closest European peers both absolutely and relative to the annual ODA budget. [1]

	Netherlands (FMO)	**Germany (DEG)**	**France (Proparco)**	**UK (CDC)**
Portfolio size (2015, USD$ billion)	10.2	7.9	6.2	4.4
ODA 2015 (2015 USD$ billion)	6.8	21.0	10.7	19.7
DFI size as % of 5 years of 2015 ODA	30%	8%	12%	4%

A step change in investment to meet the growing need

In steady state, we are self-funding and financial returns can support steady growth. However, a step change in annual investment rate does require new capital.

Since 2012, we have been encouraged to grow and do more, under our new, highly developmental mandate. In 2012, we invested £0.2bn but we knew that this level of activity wasn't enough if we were

[1] Source - EDFI Flagship report and 2016 OECD data https://data.oecd.org/oda/net-oda.htm

FX used: €1 = $1.1

going to make a greater contribution achieving the Sustainable Development Goals. Over the past five years we have grown our capability rapidly in order to respond to the need and in 2016 invested £1.2bn. However, this level cannot be maintained without a capital injection.

We have also been exploring some innovative strategies with DFID during 2016 which are intended to generate further impact through lowering our financial return requirement. These are ready to start implementing in 2017.

The purpose of the Bill

The CDC Act 1999 limited the amount of money the Government could invest in CDC to £1.5 billion, and after 17 years this has now been reached. By raising the limit, we will have the flexibility to meet the growing demand for investment in developing countries and build on the recent success of our new strategy.

While the Bill raises the limit, it is not an approval or a commitment to provide CDC with additional funds within any set period of time. Before any amount is agreed, a robust business case will be prepared and agreed by our Board and DFID, and published for public accountability. Any business case will show how further investment will continue to achieve value for money, clear development impact and ensure we are responding to market needs.

CDC since 2012

A new development-focused strategy

- Over the past five years, we have dramatically changed how we operate incorporating recommendations from a public enquiry and an International Development Select Committee report. Under this new strategy, development is placed at the heart of what we do.
- Our mission, agreed with DFID, is to support the building of businesses throughout Africa and South Asia to create jobs and make a lasting difference to people living in the poorest parts of the world.
- To achieve this, we must generate a modest financial return: a business must be viable and profitable if it is to create jobs that will last.
- We invest responsibly, with international environmental, societal and governance standards, which gives confidence to other commercial investors to follow.

Focusing on jobs and the hardest geographies

- Since 2012, we only invest in Africa and South Asia. We target our support to countries where it is needed most and where it can have the most development impact, through job creation. The jobs challenge is significant, for example Africa needs 15 million new jobs every year to achieve the Global Goals.
- We've developed a methodology for assessing each investment opportunity for its potential to create employment and the difficulty of the geography. This maintains a focus on development impact in a way that is both objective and quantifiable.
  - 66 per cent of our disbursed investments last year went to the poorest and most difficult countries within our geographies.
  - We dedicate more of our portfolio to investments in fragile and conflict affected states than any other DFI or multilateral investment body (44 per cent of our new strategy investments

are in Fragile and Conflict Affected States compared to an est. 10-25 per cent for other International Finance Institutions and European Development Finance Institution)

- We prioritise investing in sectors where growth leads to jobs. In 2015, the businesses we invest in helped create 1.03 million new jobs in Africa and South Asia.

✚ The current strategy is showing a shift in our portfolio towards priority, job-creating sectors and more challenging geographies. We continue to divest from legacy investments, made under our old strategy. And we're conducting major evaluations about how our investments make a difference – and can be better targeted, for example our recent independent report on the link between power and jobs in Uganda recommended focussing investments on connecting mini and regional grids to national grids and trying to employ private sector capital and expertise into the transmission challenge (i.e. getting power from the generating site to sub-stations).

CDC's approach through to 2021

We are currently agreeing a new strategy with DFID for 2017-2021 listening to the feedback we've received during the passage of the Bill. It will build on the progress we've made since 2012, when we set out to focus on the most challenging countries and deliver more impact through our investments. The new strategy will continue to focus within Africa and South Asia, will challenge us to be even more developmental and transparent and will incorporate some innovative start-up strategies.

Measuring our success and development impact

✚ In 2015, the businesses we invested in raised $2.6 billion in local taxes which can be used to support public services like health and education in developing countries. The power companies we invested in generated 56,400GWh of electricity last year: enough to meet the needs of 28 million people.

✚ We aim to crowd-in private capital into the countries we invest in by demonstrating that investments in these markets can be commercially viable. In 2015, we committed $350m to investment funds, which helped bring in a further US$832m of private sector investment;

✚ Overall the businesses in our portfolio in Africa and South Asia supported 17.9 million jobs, and helped create 1.03 million new jobs. The portfolio itself directly created 25,000 new jobs.

✚ This job creation rate of 6.1 per cent appears to have exceeded the rate experienced in many larger economies. For example, Nigeria's economy-wide job creation rate was 1.5 per cent and South Africa's equivalent figure was 1.3 per cent.

✚ We clearly explain our approach in our Annual Review and we're careful to explain the difference between direct and indirect jobs.

✚ Indirect jobs are created/ supported in three different ways:

1. In supply chains. By buying more goods and services, jobs are generated within suppliers.

2. Through local wages. Workers spend their wages locally, stimulating more jobs.

3. Through better access to infrastructure and finance. Removing barriers such as no access to power, poor transport links or limited access to finance stimulates economic activity, which leads to job creation.

CDC's performance targets

DFID measures our performance against two targets set within our Investment Policy:

1. To deliver a significant development impact (above 2.4 out of 4 as measured by our investment screening tool (Development Impact Grid), which was developed by DFID and external experts to score each investment before it is made on the difficulty of the country and the propensity of the particular business sector to generate employment directly and indirectly).

2. Make a positive portfolio-wide financial return (above 3.5 per cent gross return on a ten year rolling average). Making a financial return is essential to achieve a development impact: only viable and profitable businesses will create and sustain jobs. We recycle all our returns into more promising businesses to create more impact.

   We have exceeded both targets over the last five years:

   - Our average annual return has been 7.8 per cent (target 3.5 per cent)
   - Our Development Grid score has been 3.05 out of 4 (target 2.4)

- All development impact scores are externally assured annually, with an independent Report to the Board confirming the three-year aggregate score against our target.

- We have also commissioned and published a number of evaluations that have assessed the impact of our investments in specific sectors. See http://www.cdcgroup.com/The-difference-we-make/Performance/

Transparency of our investments

- In 2011, we adopted a new Transparency and Disclosure Policy. We now disclose a wide range of corporate and institutional information, as well as information about partners, investments and development impact. The information published on our website often goes over and above the data provided by other DFIs.

- We have an online database of all our investments, which allows users to search for and discover information about each of CDC's underlying investments, including the name, description, location, sector, CDC commitment, date of first investment, fund and fund manager associated with the investment.

- In November 2011, CDC became the first DFI to sign up to International Aid Transparency Initiative (IATI). Between May 2013 and October 2014, CDC played a leading role in a working group comprising IATI, EBRD, EIB, IFC and PIDG to develop an IATI implementation standard that is appropriate for DFIs/IFIs.

Tax

- We never use off-shore financial centres to avoid tax. We use them so that we can invest alongside other international investors, which often requires the use of a third neutral nation to hold the investment. Where we can we invest directly, we do. But the reality is that many developing countries do not yet have stable administration and legal systems necessary to do this. We look forward to the time we can work through onshore financial centres in the markets where we invest.

- In 2013 we introduced a new policy on offshore financial centres ensuring we won't make new investments through jurisdictions deemed harmful by the OECD's Global Forum. Mauritius and the Cayman Islands are approved by the OECD Global Forum.

- The beneficiaries of our capital are always the businesses in the nation where we invest.