Swiss Investment Fund for Emerging Markets (SIFEM AG)

Investment Guidelines

Version 2.1, as approved by the Board on 1 September 2014
(minor classifications adjustments, as approved by the Board on 4 March 2015)

1. Objectives

SIFEM shall seek to contribute to long-term economic growth in developing and transition countries by:

- investing primarily in funds managed by financial intermediaries and in other financial institutions (e.g. banks, leasing companies, investment funds, guarantee funds, securitisation notes) providing access to capital and know-how to local, growth-oriented businesses;
- investing directly in sustainable private businesses; and
- seeking to mobilize private sector resources (finance and know-how), and to channel these resources to the private sector in its target countries.

SIFEM is a key pillar of the Swiss Confederation's efforts to promote sustainable private sector-led growth in developing countries and transition economies with a view to reduce poverty and to contribute to increased living standards in these countries.

SIFEM shall invest in a commercial way, subsidiary to the market, in those companies that are most likely to be commercially viable and hence sustainable. Furthermore, SIFEM's investments shall be development-oriented and therefore aim at achieving a broad set of objectives beyond the financial rate of return. This shall require careful monitoring and evaluation of the development impact of its investments.

SIFEM's specific tasks will be to optimize the management and the efficiency of the investment activity, reinvest the reflows from investments (capital, interest, profits), and improve the transparency and visibility of the investment activity in the economic development cooperation of Switzerland

SIFEM shall be committed to co-ordinate its investment activities closely with SECO's and SDC's other complementary activities, wherever meaningful. The impact of SIFEM's activities shall be enhanced by SECO's activities in further complementary areas, such as improving the general investment environment, technical assistance to SMEs, financial sector support, trade promotion etc.

SIFEM's resources shall be fully untied and its investment guidelines do not allow for any preferential treatment of Swiss companies as regard the allocation of funds and other resources.

2. Normative framework

SIFEM shall invest in accordance with the Swiss development policy as laid out in the following documents:

- Federal Act of 19.3.1976 on international development co-operation and humanitarian aid (Art. 15), SR 974.0, version as of 28.1.1998.
- Ordinance on international development co-operation and humanitarian aid of 12.12.1977 (i.d.F. of 1.4.2010), particularly paragraph 8a: Company to support the Confederation in economic co-operation in development and transition countries, SR 974.01.
- Federal Act of 24.3.2006 on co-operation with Eastern European countries (Art. 14), SR 974.1.
- Ordinance on co-operation with Eastern European countries of 6.05.1992, SR 974.11 (version as of 1.4.2010).

SIFEM shall, in an active dialogue with its partners and stakeholders, constantly encourage high standards of corporate governance, social responsibility, occupational health and safety as well as respect for human rights and the external environment. The partners and stakeholders include the communities in which the portfolio companies are located, in addition to management, staff, investors, co-financiers and business partners.

The standard set out in this Chapter constitutes a Code of Best Practice and is designed to apply to all of SIFEM's investments. As such, SIFEM will encourage compliance by its partners and stakeholders with the business ethics and principles that underlie this Code of Best Practice. SIFEM's ability to put this into effect will vary according to the size of SIFEM's stake in the company concerned; however SIFEM may decline to invest if it considers that measures essential to achieving a necessary degree of compliance are not being taken.

In setting its standards and objectives, SIFEM shall utilize the framework established by international organizations and agreements such as (but not limited to):

- The United Nations Universal Declaration of Human Rights.
- The Council of Europe's Convention for the Protection of Human Rights and
- Fundamental Freedoms.
- The ILO Conventions Nos. 29 (Protection against forced labor), 87 (Protection of freedom of association), 98 (Protection of the right to collective bargaining), 100 (Equal remuneration for men and women), 105 (Abolition of forced labor), 111 (Non-discrimination concerning employment and occupation) and 138 and 182 (Protection against child labor).
- The OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions.

3. Scope of Activities

SIFEM shall have two main investment objectives for developing countries and countries in transition: first, investments in financial institutions and in funds, mainly private equity funds, managed by financial intermediaries, and second direct investments in sustainable private businesses.

In accordance with the investment principles and guidelines set out below for funds and direct investments, SIFEM can inter alia:

- Invest in equity and quasi equity instruments. Equity investments in private companies shall generally be of lower priority.
- Advance loans and provide other debt instruments. Loans may be secured or unsecured, subordinated, convertible or equity linked.
- In specific cases, furnish guarantees to assist borrowers in gaining access to financing in return for a fee.

When preparing investment proposals, SIFEM shall carefully explore the feasibility, workability and enforceability of the financial instruments applied.

4. General Investment Principles

The investment policy of SIFEM is based on the following broad guiding principles:

- Subsidiarity: SIFEM will provide financing which is either unavailable on the market or not available at reasonable terms and conditions, or in sufficient amounts or maturity.
- Sustainability: In its investment activity SIFEM AG will adhere to the basic principles of financial, economic, social and environmental sustainability.
- Leverage effect: SIFEM will mobilise optimum additional capital from other private and institutional investors for the target countries or the beneficiary companies. To this end, in accordance with its mandate, SIFEM will bear a portion of the political or commercial risks and

conversely will share the returns from the investments with the private and institutional investors.

- Complementarity/Additionality: SIFEM will carry out investments that not only fill a gap in financing but also include tangible value add, particularly in the form of knowhow-transfer and technical support for financial intermediaries and companies.

5. General Investment Guidelines

SIFEM shall make investments in accordance with the following guidelines:

- Investment through funds or directly in growth oriented SMEs, Micro Finance institutions, infrastructure projects, in financial institutions and in funds managed by financial intermediaries and serving the needs of SMEs, in the target countries. Investments in larger companies through funds or directly from time to time are not excluded provided they are likely to contribute to reducing the overall risk in the portfolio and are meaningful from a developmental point of view.
- Investment in economically viable businesses, reflected by a reasonable prospect of earning a positive return on the investment.
- Investment in sustainable businesses, financial institutions or funds managed by financial intermediaries perceived to possess strong management with a good reputation. They should also be prepared to work with SIFEM so that it might advise on improvements, thereby achieving its additionality objective.
- In all its investments, SIFEM shall be securing proper minority protection rights and subscription agreements, with full monitoring rights and board positions as appropriate.
- SIFEM’s primary role is to participate, directly and indirectly, in the establishment and development of sustainable enterprises, and it shall divest at the most propitious time after its objectives have been achieved

6. Specific Requirements and Terms for Investments in Funds Managed by Financial Intermediaries and in Financial Institutions

In the target countries, SIFEM shall normally make investments in funds and other financial institutions that provide medium and long-term capital with know-how transfer, to local small and medium sized companies.

SIFEM shall make investments in three categories of investments, namely:

- “Growth Investments”: the main objective of these investments is to foster economic growth, support sus-tainable job creation and the integration of target countries into world economy. The beneficiaries are the newly hired employees, both skilled and unskilled, of the portfolio companies. Indirectly, these in-vestments will benefit the all job market participants in the target countries.
- “Economic Development Investments”: the main objective of these investments is to generate broad and sustainable economic development by creating or fostering the early development of risk capital mar-kets in previously underserved countries or sectors. The direct beneficiaries are the stakeholders of the portfolio companies. Indirectly, these investments will also benefit the entire economic ecosystem of target countries by laying the groundwork for future economic growth and/or contributing to the provision of global public goods.
- “Investments in Social Impact Entities”: the main objective of these investments is to reduce inequalities and support inclusion by providing access for disadvantaged populations or social

groups to products, services and/or jobs. The key beneficiaries are the so-called "base of the pyramid".

The system, according to which fund investments are classified into the three above groups, is outlined in a separate policy.

For all investments in funds, SIFEM shall be looking for: deep markets knowledge and a high potential deal flow, sound track record in private equity of the management team or at least high potential to develop further, investment processes and back office support/good governance principles, a compelling and well articulated investment thesis, credible exit opportunities.

Funds and other financial institutions must be adequately regulated. If the local regulatory regime is unsatisfactory, SIFEM shall, in close collaboration with SECO, seek to address the shortcomings. In such cases, SIFEM shall, on the basis of a thorough analysis of potential risks, demonstrate that such risks can be managed and are therefore acceptable.

The total exposure in a single fund or financial institution shall not exceed 4% of SIFEM's total capital commitments.

7. Specific Requirements and Terms for Direct Investments

SIFEM will make investments in businesses, normally alongside co-investors of good financial standing and with sound track records, including private investors (foreign direct investors or local investors), regional development banks, national and international development finance institutions.

SIFEM shall require that the financial structure is well-balanced and will normally take less than 50% of the total investment in the portfolio company, including working capital. The strategic partners in the project must be willing to enter a long-term commitment with a relevant risk exposure.

Active local participation is desirable so that the enterprise is fully integrated into the local economy. The local partner shall have a sound knowledge of local conditions, experience of the business involved, and a material financial interest in the enterprise.

SIFEM's investments will primarily be used to finance specific projects or investment programs aiming at the modernizing and expanding the portfolio companies, or for their permanent working capital requirements.

For the selection of investment projects, key business factors considered shall include the expertise and reputation of the management team, the prospect for the industry in which the portfolio company is active, the competitive advantages (including barriers to entry) and profitability of the product range, the interest in growth and exit intentions exhibited by the owner, and sound financial controls.

The maximum exposure in a single company shall not exceed 3% of SIFEM's total capital commitments.

For its equity and quasi-equity investments, SIFEM will seek a market return. For loans, SIFEM will make best efforts to demonstrate that the interest rates charged and the terms offered do not result in a crowding out of the private sector and are adequate, provided the risk taken. Lower returns may be accepted in projects with a particular and relevant development impact. In order to mitigate interest rate fluctuations, SIFEM may use fixed for floating hard currency interest rate swap agreements.

8. Priority Countries

The investment universe of SIFEM shall encompass all transition and developing countries appearing on the OECD-DAC list, and having a GNI per habitant below the IBRD graduation threshold defined annually by the World Bank. Any (e.g. regional) investment that includes countries that do not fulfil those criteria (e.g. Costa Rica) shall be considered as sensitive and referred to the Board for decision. In its decision, the Board will take into account the recommendation of the representative of the Confederation regarding a potential waiver on the country eligibility criterion.

Certain countries shall be considered priority countries for SIFEM investments. These priority countries comprise the priority countries of SECO's economic development co-operation, as well as the priority countries of the Swiss Agency for Development and Cooperation (SDC). For the period 2010-12, the following countries shall be considered as priority countries:

- **Africa:** Benin, Burkina Faso, Chad, Egypt, Ghana, Jordan, Mali, Mozambique, Niger, South Africa and Southern Africa (SADC Region), Tanzania, Tunisia, Morocco, the Great Lakes Region (Rwanda, Burundi, Democratic Republic of Congo), Horn of Africa (Somalia, Ethiopia, Kenya), Occupied Palestinian Territory.
- **Asia:** Afghanistan, Bangladesh, Cambodia, Indonesia, Lao PDR, Mongolia, Myanmar, Nepal, Pakistan, Sri Lanka, Vietnam.
- **Latin America:** Bolivia, Colombia, Central America, Peru, Haiti, Cuba.
- **Transition Countries:** Albania, Armenia, Azerbaijan, Bosnia, Georgia, Kazakhstan[1], Kyrgyzstan, Kosovo, Macedonia, Moldova, Serbia, Tajikistan, Ukraine.

The Confederation shall have the right to revise and update this list at any time. When making investments SIFEM shall apply the following principles:

- In the context of direct investment operations (non-fund investments), SIFEM may only invest in the priority countries.
- In the context of indirect investment operations (fund investments), SIFEM shall allocate at least 60% of its investment volume to the priority countries (as they are defined at the time of making the investments), while 40% can be invested in other developing countries or countries in transition. In cases of regional or global funds, SIFEM shall consider the project as a priority country investment if, on the basis of credible evidence (due diligence, pipeline), it can reasonably be assumed that that least 50% of the commitments will be made in priority countries (in Sub-Saharan Africa, this percentage is reduced to 20%).

SIFEM shall immediately stop new investments in a country if this country is not eligible anymore for receiving public development funds of the Swiss Government. The reasons for such a situation can be (but are not limited to) an armed conflict with another country, a state of war, a serious breach of human rights issues. It should be noted that existing investments in countries falling into political disfavour, cannot be withdrawn immediately. SIFEM shall however endeavour to wind these investments down as soon as possible.

[1] Kazakhstan is not listed as a priority country in the message to Parliament, but had been added to the SIFEM list at SECO request by virtue of its belonging to the Swiss-led constituency at the World Bank.

9. Further Investment Restrictions

Except with a specific written approval of SIFEM's Board, SIFEM shall restrict its investments as follows:

- With the exception of the financial sector (investments in funds and other financial institutions) investments in any single industry shall not exceed twenty percent (20%) of SIFEM's total capital commitments.
- Investments in any country shall not exceed twenty percent (20%) of SIFEM's total capital commitments.
- SIFEM shall not be involved in hostile take-over bids.
- SIFEM shall not invest in any company, fund or other financial institution that is more than 50% (post-investment) directly or indirectly owned or controlled by one state, including its political subdivisions and agencies.
- SIFEM shall not invest in portfolio companies engaged in speculative real estate development.
- SIFEM shall not engage in speculative investment activities such as commodities, commodity contracts, forward currency contracts, except for currency contracts entered into in connection with investments in portfolio companies or the purchase of real estate to be used for the implementation of an investment project. SIFEM can only investment in derivatives, options or warrants in association with long term financing structures.
- SIFEM shall not invest in portfolio companies that are related parties of the company managing SIFEM's portfolio, and of its employees, SIFEM's Board, or its Investment Committee unless it has been fully disclosed and approved by the Board. Further details shall be regulated in a SIFEM policy on Conflict of Interest.
- SIFEM shall not invest in companies that violate its Environmental and Social Guidelines

10. Social and Environmental Guidelines

SIFEM shall adopt a Social and Environmental Risk Management System, which is in accordance with European and International best practice. Specifically, it shall adopt the investment exclusion list provided by the association of European Development Finance Institutions (EDFI) and classify projects according to their possible environmental impact according to the World Bank Environmental Guidelines.