Industrial Development Corporation

Responsible Investment Policy

November 2014

1. INTRODUCTION

This policy identifies activities that the IDC will not finance as a result of ethical considerations. The policy reflects the values of the IDC, and clarifies these through clearly articulating an Exclusions List. Implementation should contribute to the prevention of long-term financial, social or reputation risks to the IDC. The adoption of a Responsible Investment Policy is in line with the global move to incorporate sustainable financing into conventional business agendas.

2. BACKGROUND

Funding decisions taken by the IDC with respect to business partners are based on factual information afforded by the due diligence exercise. Ethical concerns should form a part of the larger consideration process. Given that the IDC already has a positive focus to project selection, a negative screening process is the most appropriate mechanism to ensure responsible investment. This is done through the adoption of an IDC Exclusions List. Using the negative screening methodology and incorporating international precedent, a list was identified that categorises the types of activities that the IDC will not finance.

3. SOCIALLY RESPONSIBLE INVESTMENTS/ETHICAL INVESTMENTS

There is a growing international movement that supports socially responsible investment (SRI) and ethical investment in response to shareholder and stakeholder requirements, evolving consumer demand and media interest in corporate behaviour. Ethical investment combines the ethical, social and environmental considerations of investors with their financial objectives. For businesses this implies that they must take responsibility for the effect of their investments on humans and the environment. This approach enables business to use monetary power to bring about positive social and environmental change whilst still enjoying competitive returns.

3.1 South African context

Ethical and responsible investments in the South African financial milieu are primarily guided by the Financial Services Charter and the JSE's Socially Responsible Investment (SRI) Index. The JSE's SRI index was launched in May 2004 in response to the growing debate around sustainability globally and particularly in the South African context. The criteria used for the SRI Index retains the triple bottom line philosophy, but the indicators are structured along ESG groupings (Environment, Society, and Governance), in line with the framework promoted by the UN Principles for Responsible Investment. In keeping with the Index's developmental approach, it is foreseen that more detailed criteria will be introduced in due course for areas such as climate change, bribery and corruption, human rights and supply chain management.

3.2 International precedent

Initially SRI focused on business sectors considered ‘unacceptable’ (tobacco, alcohol and weapons) and these were excluded on moral grounds. Other types of exclusions aimed at safeguarding the reputation of major institutional investors, and at avoiding them being linked with controversial issues that affect the companies they invest in, have since been developed. These exclusions usually involve violations of human rights or environmental protection norms.

The norm-based exclusions (negative screening or ‘exclusions of worst practices’) that are most commonly adopted serve to shield investors against criticism of their legitimacy and social usefulness. Even if companies do not face the same legal requirements regarding environmental, social or governance issues between one country and another, they must be in a position to comply with a certain number of fundamental international norms in order to meet the requirements of responsible investors, regardless of the business involved or the country in which they operate. It aims to be more “all-encompassing” by establishing minimum ESG norms.

Among the international norms used by investors, the International Labour Organisation’s conventions are the most specific, while the Global Compact Principles provides a framework for the interpretation of underlying norms. The OECD Guidelines, Anti-Corruption Conventions, Universal Declaration of Human Rights, RIO Declaration and Convention on Biological Diversity (1993) are also frequently used.

The World Bank and its subsidiary, the International Finance Corporation (IFC), both have standards on environmental and social investment with accompanying exclusion lists. The African Development Bank follows the standards outlined by the World Bank, while the European Investment Bank (EIB), Kfw, Agence Française de Developpement (AFD), the Banco Nacional Do Desenvolvimento Econômico e Social (BNDES), and the Asia Development Bank all have standards that have been derived according to their specific needs. A number of commercial banks and financial institutions globally also have standards with regard to exclusions, as well as best practice notes on certain sub-sectors.

4. DISCUSSION

4.1 Purpose of a Responsible Investment Policy

The extent to which a company is ethical is a matter of careful consideration. All companies operate within an intricate framework of relationships with suppliers, customers, government authorities and other stakeholders. However, trends in law (e.g. environmental legislation), corporate governance (e.g. King III), as well as shareholder and community activism are increasingly holding companies accountable for the impact they have on communities and society generally. This requires companies to demonstrate accountability through an ethical approach to its activities. As a DFI, it is important for the IDC to clearly articulate those areas of activity which should be treated as exclusions so as to ensure its adherence to best practice in ethical investing. As a development oriented institution, the IDC should be leading and not following the business mainstream.

4.2 Rationale for an IDC Exclusions List

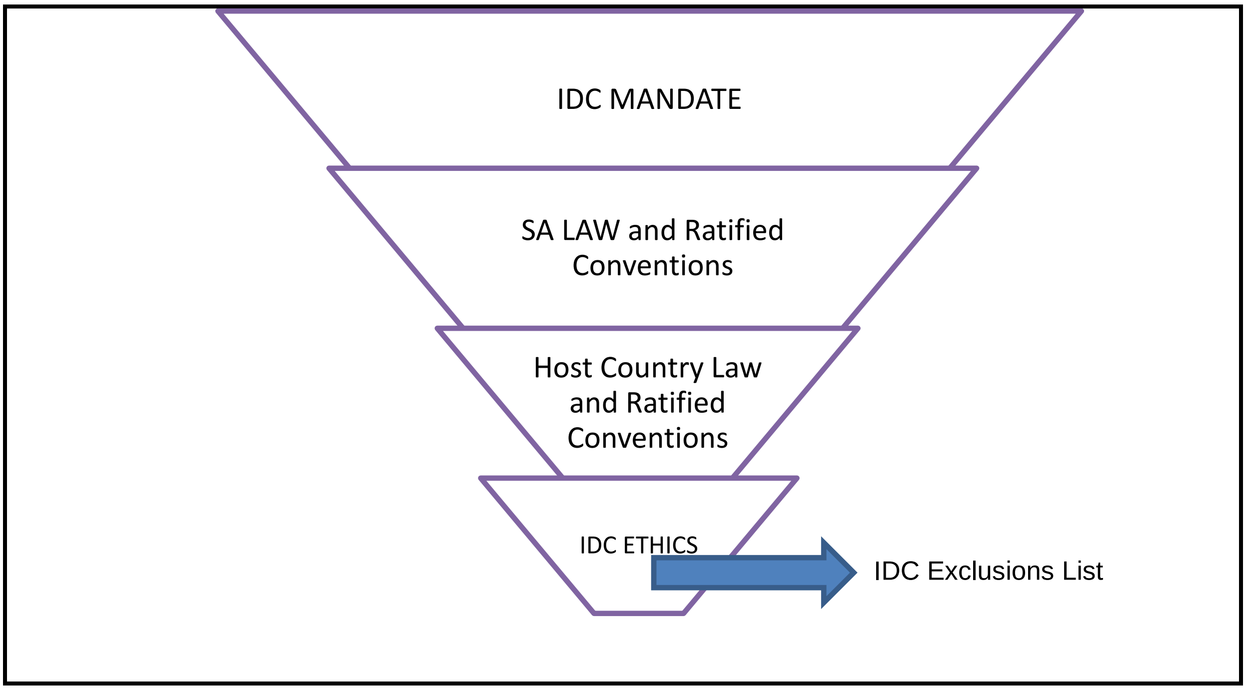
The current approach of IDC can be characterised as a pro-active approach that identifies activities that are deemed desirable. In the absence of a formal approved policy, IDC has in practice been applying elements of socially responsible investing by avoiding investments in the following, amongst others:

- casino’s and gambling facilities;
- hard liquor (any drink with the proportion of alcohol exceeding 12%);
- any tobacco and tobacco products;
- the production and trade in weapons and ammunition;
- pornography;
- projects if the required licenses have not been granted, unless these form part of the feasibility study or CP’s;
- environmental impact assessments have not been conducted or geological reports are not available, unless these form part of the feasibility study or CP’s;

Funding from the ADB and AFD is subject to minimum criteria that the IDC apply with regard to the distribution of funds. Investments outside South Africa are subject to World Bank Guidelines. The IDC is a signatory to the United Nations Environment Programme (UNEP) statement by financial institutions on the environment and sustainable operations.

IDC, as one of the world's leading and oldest DFI's, and certainly one that aims to lead rather than follow its peers, should formalise these nascent initiatives and formalise a Responsible Investment Policy into its operations.

Diagram 1: Filter for IDC Funding Decisions



All IDC operations need to comply with the applicable rules and regulations within countries it invests in. The implementation of the Responsible Investment Policy and the use of an Exclusions List will:

- Position the IDC as an ethical investor in line with its development mandate
- Unify and simplify the policy regarding exclusions
- Support management of project and reputational risks
- Harmonise IDC's investment approach with best practice of other DFI's

5. IDC EXCLUSIONS LIST

The IDC will not finance:

1.	Production or trade in any product or activity deemed illegal under South African, or host country laws or regulations, including interventions conventions ratified in either country.[1]
2.	Production/ or trade in weapons and munitions and military equipment and components specifically intended for military purposes
3.	Pornography[2]
4.	Production or trade in tobacco
5.	Gambling and casinos
6.	Projects if the required licences have not been granted, unless part of the feasibility study or CP's;
7.	Environmental impact assessments have not been conducted or geological reports are not available, unless part of the feasibility study or CP's.

6. SCOPE AND APPLICATION

The Exclusions List identifies activities that the IDC will not invest in. Funding can be considered for a company involved in any of the excluded areas as long as the planned project is unrelated, and is not a portion of a main business that is excluded, the project is clearly ring-fenced and no portion of the IDC's funding will be utilised to support the excluded areas of operation.

In all agreements it will be stipulated that, should the IDC believe that its funds are being used in a manner that is contrary to the Corporation's Responsible Investment Policy, the IDC has the right to withdraw from the transaction. All new agreements will include a signed acknowledgement from business partners to indicate their understanding and commitment to the IDC's Responsible Investment Policy and the requirement to notify the IDC if they are contemplating any of the activities captured in the Policy's Exclusion List.

[1] SA law will be applied, excluding those specific to the South African context and addressing unique social challenges such as skills shortages. It is recognised that in host countries no equivalent legislative structure might exist, for example BBBEE legislation.

[2] All the activities in which people pay money in order to have sex or see graphic representations of sex.