finnfund

15.5.2024

Disclosure Statement

Operating Principles for Impact Management

Finnfund (the "Signatory") hereby affirms its status as a Signatory to the Operating Principles for Impact Management (the "Principles").

This Disclosure Statement applies to the following assets (the "Covered Assets"): Finnfund's total portfolio.

The total assets under management in alignment with the Principles is US$ 781.2 million as of 31 December 2023.

15 May 2024

Finnfund
Jaakko Kangasniemi
Managing Director, CEO

IMPACT STATEMENT, IMPACT MANUAL

Principle 1: Define strategic impact objective(s), consistent with the investment strategy.

The Manager shall define strategic impact objectives[1] for the portfolio or fund to achieve positive and measurable social or environmental effects, which are aligned with the Sustainable Development Goals (SDGs), or other widely accepted goals. The impact intent does not need to be shared by the investee. The Manager shall seek to ensure that the impact objectives and investment strategy are consistent; that there is a credible basis for achieving the impact objectives through the investment strategy; and that the scale and/or intensity of the intended portfolio impact is proportionate to the size of the investment portfolio.

- Finnfund was founded in 1980 to promote social and economic development in developing countries.

- Finnfund Act (291/79) reads that: “The Company (Finnfund) shall promote the economic and social development of countries which the OECD DAC has classified as developing countries by directing human and material resources to the development of the industrial and other economic corporate activity of these countries.”

- In December 2021, Finnfund’s Board of Directors approved a strategy for the company, setting operational guidelines until 2025. The strategy reconfirms that Finnfund’s mission is to build a sustainable world by investing in businesses that solve global development challenges with a vision to have people and planet at the core of every investment decision. The strategy further sets three key strategic objectives: 1) double total impact from 2020 to 2025; 2) make half of the investments with private capital by 2030; and 3) maintain a carbon net negative portfolio. The strategy defines renewable energy, sustainable forestry, sustainable agriculture, digital infrastructure and solutions as well as financial institutions as priority sectors for Finnfund due to their critical role in achieving sustainable development.

  In addition, gender equality is an important objective for Finnfund as detailed in our Gender Statement. In June 2021 Finnfund published it’s Climate and Energy Statement that, in addition to the above mentioned net carbon negative portfolio, aims to increase Finnfund’s climate finance to EUR 1 billion by 2030 and ensure that all new investments are aligned with the objectives of the Paris Agreement.

- The Finnish State owns 96.18% of Finnfund and the Ministry for Foreign Affairs of Finland is charged with steering Finnfund. The Foreign Ministry issues a *Government Ownership Steering Memorandum*, in which it sets Finnfund’s development policy and operational goals. Finnfund’s Board of Directors monitors the achievement of these objectives.

- In 2023, a new Memorandum was given for four years 2024-2027, coinciding the Government’s expected tenure. The Memorandum encourages Finnfund to prioritise digital infrastructure and solutions, sustainable forestry, and Ukraine. Finnfund is expected to strengthen its role in financing green transition and promote gender equality through its investments. The Memorandum also reinstates the Government wish that Finnfund should work more with Finnish companies.

Principle 2: Manage strategic impact on a portfolio basis

The Manager shall have a process to manage impact achievement on a portfolio basis. The objective of the process is to establish and monitor impact performance for the whole portfolio, while recognizing

[1] Impact objectives can be defined as the intended impact that contributes to financial, institutional, social, environmental, or other benefits to a society, community, or group of people via one or more investment. Adapted from OECD-DAC (www.oecd.org/dac/).

that impact may vary across individual investments in the portfolio. As part of the process, the Manager shall consider aligning staff incentive systems with the achievement of impact, as well as with financial performance.

- Strategic impact is at the core of Finnfund's incentive structure. Corporate KPIs, set by Finnfund's management, are largely based on project score of new investments. In the project score, half of the points is derived from the impact scoring, value additionality, and the strategic priorities of climate, gender, biodiversity.

- Impact scoring is done for every new investment with Finnfund's bespoke Development Effectiveness Assessment Tool (DEAT) in two occasions: first for the investment committee meeting to obtain Clearance in Principle to continue preparation of the investments; and second for the Board meeting for the approval of the investment.

- DEAT is comprised of three sections: strategic relevance (40%), market impact (40%) and additionality (20%). The first section, strategic relevance, seeks to assess the proposed investment's conformity with Finnfund's strategic objectives. The specific questions in the section relate to the ODA status of the project country, sector, inclusivity of the business model, gender, climate change, biodiversity and breadth and depth of CSR activities.

- The score for Strategic relevance represents 40% of the total development impact score and thus plays an important part in the overall ranking of the investment.

- Alignment and achievement of portfolio level strategic impact is monitored on an annual basis by the Board of Directors.

- Results for 2023 include: 95% of the value of investment decisions were made into lower middle income or poorer countries, 30% of the value of new decisions were for investments in Africa, 41% was climate financing, and 50% gender financing.

- Total portfolio allocation between geographies and different instruments is presented in the below table.

Geography	MUSD	Instrument	MUSD
Africa	397	Senior loan	257
Asia	135	Equity	230
Latin America	84	Mezzanine	137
Europe and Central Asia	38	Fund	123
Middle East	16	OP Finnfund Fund	32
International	111		

- In the Strategy of 2021, Finnfund aims to double its impact by 2025. To monitor, and manage the achievement of this objective, Finnfund has developed a bespoke summary index of its development impact. In the index, each sector is assigned a key impact indicator that captures both portfolio growth and investee level impact growth. The values in the index are attributed, take into account Finnfund's financing share of the company, and relative size of each sector in Finnfund's portfolion. The baseline is set at 2020.

- Sector specific impact key performance indicators (KPIs) are:
  - **Sustainable forestry:** Sequestrated CO2. While forestry investments have multiple impact pathways, a key reason to invest in forestry is the sequestration potential of growing forests.
  - **Renewable energy:** Avoided CO2. Energy plays a key role in helping countries to develop. Increasing energy production by investing in clean and more affordable energy production is at the heart of this development.

- **Sustainable agriculture:** Number of people fed or small-holder farmers reached. Local food production and enhancing local agriculture value chains help to increase food security and create inclusive livelihood opportunities.
- **Financial institutions**: Number of loans to micro, small and medium sized (MSME) companies. Limited access to financial services remains a fundamental constraint on development in most of Finnfund's target countries.
- **Digital infrastructure and solutions:** Number of users / beneficiaries. Access to digital services is vital for inclusive development for people especially in rural regions.
- **Other:** Number of jobs in the investee company (full time equivalent).

Principle 3: Establish the Manager's contribution to the achievement of impact

The Manager shall seek to establish and document a credible narrative on its contribution to the achievement of impact for each investment. Contributions can be made through one or more financial and/or non-financial channels.[2] *The narrative should be stated in clear terms and supported, as much as possible, by evidence.*

- In consonance with SDG 17, Finnfund's niche and task is to provide additional financing to underserved markets and companies. In many developing countries, especially in the poorest ones, small and medium-sized businesses struggle to find risk-tolerant long-term finance[3].

- All Finnfund's investments are assessed on the basis of their additionality, and additionality is one of the three sections in Finnfund's DEAT. Additionality is key in Finnfund's corporate KPI system.

- Additionality can be financial, providing financing to underserved geographies, sectors, segments, accepting higher risk and providing longer tenors. As a proxy for additionality, Finnfund uses a compilation score, an average of three indicators addressing different dimensions of additionality, or scarcity of financing. The first proxy is participation of other financiers in the deal, where highest additionality is in investments where Finnfund is the sole financier in addition to the sponsors and lowest when there are plentiful financiers, including private, willing to finance the investment. Second proxy is Domestic credit to private sector as % of GDP. This World Bank indicator refers to domestic financial resources provided to the private sector by financial corporations. The third proxy for financial additionality is country risk rating managed by Finland's export credit agency Finnvera. In addition, each investment includes consideration if Finnfund has had a catalytic role by mobilising additional financing for the project from third parties, which leads to an additional point in scoring.

- Additionality can also be qualitative, value added through Finnfund's organisational experience with respect to specific sector, country, project type that can contribute in a demonstratable and significant manner to the successful completion and realisation of the project. Examples include expertise and advice in environmental, social or corporate governance issues or in climate change mitigation and adaptation awareness and CO2 calculations and reporting. An important part of value addition is impact and job decency surveys conducted at Finnfund's expense that provide companies, and Finnfund, with first-hand information on customers, employees or value chain.

Principle 4: Assess the expected impact of each investment, based on a systematic approach

[2] For example, this may include: improving the cost of capital, active shareholder engagement, specific financial structuring, offering innovative financing instruments, assisting with further resource mobilization, creating long-term trusted partnerships, providing technical/market advice or capacity building to the investee, and/or helping the investee to meet higher operational standards.
[3] Enterprise surveys clearly show that lack finance is the biggest challenge for companies in emerging markets.

For each investment the Manager shall assess, in advance and, where possible, quantify the concrete, positive impact[4] potential deriving from the investment. The assessment should use a suitable results measurement framework that aims to answer these fundamental questions: (1) What is the intended impact? (2) Who experiences the intended impact? (3) How significant is the intended impact?[5] The Manager shall also seek to assess the likelihood of achieving the investment's expected impact. In assessing the likelihood, the Manager shall identify the significant risk factors that could result in the impact varying from ex-ante expectations.

In assessing the impact potential, the Manager shall seek evidence to assess the relative size of the challenge addressed within the targeted geographical context. The Manager shall also consider opportunities to increase the impact of the investment. Where possible and relevant for the Manager's strategic intent, the Manager may also consider indirect and systemic impacts. Indicators shall, to the extent possible, be aligned with industry standards[6] and follow best practice.[7]

- Finnfund has developed generic Theories of Change (ToC) for its priority sectors to guide its impact work. ToCs are based on existing literature of academic and non-academic research, expert opinions and analytical thinking. ToCs are causality frameworks comprising three spheres of impact (company/economy, people/society, environment/climate) and three dimensions of impact (direct, indirect, wider/systemic).

- The ToCs are used in 1) ex-ante assessment to guide the assessment of investments anticipated impact to the market and customers; 2) selecting key indicators for which baselines are established both at investee and system/national level; 3) annual monitoring and reporting (direct impacts only); and 4) impact studies for verifying indirect and system level impacts.

- Ex-ante assessments also include a summary table highlighting 1) what are the main outcomes of the investment? 2) who are the main beneficiaries of the outcomes and how are they underserved? 3) what is the scale, depth and duration of the outcome? 4) what is Finnfund's contribution to the achievement of the outcomes? and 5) what is the most important risk for the achievement of the impact, its likelihood to materialise and mitigation measures?

- In selecting suitable indicators, Finnfund uses HIPSO and EDFI harmonised indicators when applicable.

Principle 5: Assess, address, monitor, and manage potential negative impacts of each investment

For each investment the Manager shall seek, as part of a systematic and documented process, to identify and avoid, and if avoidance is not possible, mitigate and manage Environmental, Social and Governance (ESG)[8] risks. Where appropriate, the Manager shall engage with the investee to seek its commitment to take action to address potential gaps in current investee systems, processes, and

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[4] Impact is considered the material effect/s on people and the environment resulting from the investment, as outlined in Principle 1. Impacts assessed under Principle 4 may also include positive ESG effects derived from the investment.
[5] Adapted from the Impact Management Project (www.impactmanagementproject.com).
[6] Industry indicator standards include HIPSO (https://indicators.ifipartnership.org/about/); IRIS (iris.thegiin.org); GIIRS (http://b-analytics.net/giirs-funds); GRI (www.globalreporting.org/Pages/default.aspx); and SASB (www.sasb.org), among others.
[7] International best practice indicators include SMART (Specific, Measurable, Attainable, Relevant, and Timely), and SPICED (Subjective, Participatory, Interpreted & communicable, Cross-checked, Empowering, and Diverse & disaggregated), among others.
[8] The application of good ESG management will potentially have positive impacts that may or may not be the principal targeted impacts of the Manager. Positive impacts resulting from ESG matters shall be measured and managed alongside with, or directly embedded in, the impact management system referenced in Principles 4 and 6

standards, using an approach aligned with good international industry practice.[9] As part of portfolio management, the Manager shall monitor investees' ESG risk and performance, and where appropriate, engage with the investee to address gaps and unexpected events.

- Finnfund has adopted a Sustainability Policy that outlines Finnfund's commitment to sustainable development and responsible business practices. The Policy covers environmental, social and governance issues including human rights and development impact created through sustainable business practices.

- In all investments, Finnfund requires its investees to comply with applicable host country laws and regulations as well as the relevant international obligations. All Finnfund's investments associated with medium to high inherent environmental and social risks and adverse impacts are, over a reasonable period of time, required to achieve compliance with international standards on environmental and social management and performance. The project and the associated impacts and risks define the standards to be applied, but the principal environmental and social risk management framework adopted consist of the IFC Performance Standards on Environmental and Social Sustainability, and the associated WB Group general and industry specific Environmental, Health and Safety Guidelines.

- Finnfund has prepared a Human Rights Statement to actively and continuously identify, avoid, mitigate and manage potential and actual adverse human right impacts related to its transactions, and take actions to address them using the UN Guiding Principles for Business and Human Rights (UNGPs) as a practical framework.

- Finnfund has developed specific procedures for environmental, social and human rights risk due diligence, management and monitoring as well as corporate governance, corruption and taxation matters. All these are integrated into the investment process and codified in Finnfund's internal guidelines and handbooks. Different procedures are applied for direct and indirect investments as well as for different financing instruments. Finnfund focuses on the key ESG and human rights impacts, benefits, risks and opportunities relevant for each project. The higher the risks are, the more stringent the requirements become.

- Finnfund, together with the investee, often develops a project-specific Environmental and Social Action Plan (ESAP) based on the gaps identified during the environmental and social due diligence process. Finnfund supports the investees in meeting the requirements of the ESAPs and monitors compliance through regular communications and on monitoring visits.

- Finnfund identifies and analyses physical and transitional climate risks and adaptation opportunities as part of the investment process. According to Finnfund Climate and Energy Statement (2021), Finnfund investment team uses in-house climate risk assessment tool to identify location and sector specific climate hazards and exposure to these risks, and to assess the potential contribution of an economic activity to adapt to climate change and increase climate resilience. If an investee is exposed to physical climate risks based on country and sector context, further climate risk and adaptive capacity analysis is required. If the potential negative impact of climate risks can be sufficiently mitigated by applying adaptation measures, an acceptable level of residual risk may be attained.

Principle 6: Monitor the progress of each investment in achieving impact against expectations and respond appropriately

The Manager shall use the results framework (referenced in Principle 4) to monitor progress toward the achievement of positive impacts in comparison to the expected impact for each investment. Progress

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[9] Examples of good international industry practice include: IFC's Performance Standards (www.ifc.org/performancestandards); IFC's Corporate Governance Methodology (www.ifc.org/cgmethodology), the United Nations Guiding Principles for Business and Human Rights (www.unglobalcompact.org/library/2); and the OECD Guidelines for Multinational Enterprises (http://mneguidelines.oecd.org/ themes/human-rights.htm).

shall be monitored using a predefined process for sharing performance data with the investee. To the best extent possible, this shall outline how often data will be collected; the method for data collection; data sources; responsibilities for data collection; and how, and to whom, data will be reported. When monitoring indicates that the investment is no longer expected to achieve its intended impacts, the Manager shall seek to pursue appropriate action.[10] *The Manager shall also seek to use the results framework to capture investment outcomes.*[11]

- Finnfund operates a layered monitoring and evaluation system using different, quantitative and qualitative data collection and analysis methods. This system is hoped to serve as a cost-efficient method for analysing the direct, indirect and wider development impacts of the investments.

METHOD	ANNUAL SAMPLE	QUALI/QUANTI	IMPACT DIMENTION	WHO CONDUCTS?
Annual monitoring	100+	Quantitative	Direct	Self
Project Management Committees	100+	Quantitative and qualitative	Direct	Self
Client insight and impact surveys	10	Quantitative and qualitative	Direct/Indirect	Other
Job decency surveys	5	Quantitative and qualitative	Direct/Indirect	Other
Impact studies	1	Quantitative and qualitative	Indirect/wider	Other
Case studies	2-3	Qualitative	Indirect/wider	Self/other

- Investee level regular impact monitoring takes place annually. The relevant indicators and timing of the reporting are attached to the contracts. As of 2019, has Finnfund requested the data from its investee companies through an online system. The results are published annually in Finnfund's Annual Report that presents the findings at aggregate, sector and portfolio level.

- Starting in 2021, all new investments are set two specific impact key performance indicators with targets. The indicators and targets are assigned with the company with a view to drive towards more active impact management at company level.

- Annually, each investment is discussed in the Project Management Committee, that is responsible for monitoring the progress of investments against set targets: financial, environmental and social, and impact. In case deviations from the original targets or estimates are detected, the responsible portfolio manager seeks reasons for the deviation and decides on subsequent actions. Typically, the deviations are due to worse than expected business performance of the company that may be caused by internal or external (market) factors. In case the reason is deemed to be an internal management issue, corrective measures are sought. If the less-than-expected performance is due to changes in the wider market situation, then possibilities for corrective measures are limited.

- In addition to the annual monitoring, Finnfund commissions impact studies and surveys to better understand the indirect and wider impacts of its investments as well as the context where the

[10] Actions could include active engagement with the investee; early divestment; adjusting indicators/expectations due to significant, unforeseen, and changing circumstances; or other appropriate measures to improve the portfolio's expected impact performance.
[11] Outcomes are the short-term and medium-term effects of an investment's outputs, while the outputs are the products, capital goods, and services resulting from the investment. Adopted from OECD-DAC (www.oecd.org/dac/).

impact happens. Since 2021, Finnfund has commissioned regular rapid surveys to collect outcome level data on the impacts on Finnfund's investee company on its employees, clients and other stakeholders.

- Finnfund continues to commission impact and case studies on investments and themes that are deemed important for wider understanding of our impact. Commissioned studies have explored impacts of investments in energy sector, agriculture, forestry, corporate social responsibility and specifically addressed job creation, gender equality, biodiversity and food security, among others. Upcoming work will include a deep dive in better understanding Finnfund's financial and qualitative additionality.

Principle 7: Conduct exits considering the effect on sustained impact.

When conducting an exit,[12] the Manager shall, in good faith and consistent with its fiduciary concerns, consider the effect which the timing, structure, and process of its exit will have on the sustainability of the impact.

- When conducting an exit from an equity investment, the investment manager will write an exit memo based on a predefined template. In the template, the investment manager is requested to reflect on the achievements against set targets/estimates and consider future direction of the company.

- The template includes a specific section for development impact where key impacts are presented and compared to the original targets/estimates. The exit memo also encourages combining development impact with progress in environmental and social issues and possible negative impacts. The exit memo places emphasis on sustained impacts and how to best ensure sustained impact after exit. This includes analysis of the capacity and commitment of the management, exit partners' commitment and track record, and discussion on future of extension plans and commitments made to local communities or other stakeholders possibly at risk.

Principle 8: Review, document, and improve decisions and processes based on the achievement of impact and lessons learned.

The Manager shall review and document the impact performance of each investment, compare the expected and actual impact, and other positive and negative impacts, and use these findings to improve operational and strategic investment decisions, as well as management processes.

- The above-mentioned Project Management Committee system and the standardisation of impact assessment in that process is generating useful information for decision-making. The Project Management Committee systematically reviews the performance – financial, impact and E&S – of each investment every year. The impact assessment for the Committee discussion entails an assessment of project performance both on the basis of key performance indicators but also using the ex-ante assessment format that provides and up-to-date information on the investment performance as per the ex-ante assessment topics and shows discrepancies with regard to the initial assessment.

- Another highly useful tool to provide information to improve decision making has proven to be the rapid surveys that provide nearly real-time information on the company's performance from the perspective of its employees, clients and other stakeholders. Standardised surveys include sections on the respondents' socio-economic status referenced to Poverty Probability Index, the

[12] This may include debt, equity, or bond sales, and excludes self-liquidating or maturing instruments.

impact of product or service have on customers with qualitative information or perceptions on job decency, and suggestions for improvement.

Principle 9: Publicly disclose alignment with the Principles and provide regular independent verification[13] of the alignment.

The Manager shall publicly disclose, on an annual basis, the alignment of its impact management systems with the Principles and, at regular intervals, arrange for independent verification of this alignment. The conclusions of this verification report shall also be publicly disclosed. These disclosures are subject to fiduciary and regulatory concerns.

- This statement serves as Finnfund's testimony of its continued alignment to the Principles. The statement and information contained therein was independently verified in February - March 2021 by BlueMark, which is a leading provider of independent impact verification and intelligence for the impact and sustainable investing market. BlueMark is headquartered at 915 Battery Street, San Francisco, CA 84111, USA.

- The independent verification report can be found here.

- Finnfund intends to commission the next independent verification latest by 2025.

[13] The independent verification may be conducted in different ways, i.e., as part of a financial audit, by an independent internal impact assessment committee, or through a portfolio/fund performance evaluation. The frequency and complexity of the verification process should consider its cost, relative to the size of the fund or institution concerned, and appropriate confidentiality

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