INVESTING IN UNDERSERVED MARKETS

Norfund's investments are additional, helping to fill the gap between what markets in poor countries need and what the private sector offers.

Economic growth that provides jobs is the main driver of global poverty reduction. Ninety percent of all jobs in the developing world are created by the private sector. Surveys show that access to finance is a major obstacle for business growth, and is particularly pronounced in the poorest countries. Investing in these countries is therefore important to stimulate growth and job creation.

Foreign direct investments (FDI) have grown rapidly over the past two decades and now exceed official development assistance (ODA) to low- and lower middle-income countries. However, the percentage of global foreign direct investments to low-income countries remains small. Many private investors are hesitant to invest in the poorest countries because of the high risks involved and inadequate information about these investment environments.

Financial additionality is an essential part in Norfund's investment processes. We achieve additionality by focusing strategically on countries and sectors in which capital is scarce, and scrutinise our role in each investment. A comparison of our investment activities with global FDI flows shows that Norfund takes higher risks than many other investors.

DEFINING ADDITIONALITY

An investment is said to be financially additional if it supports capital-constrained markets in which private sector partners are unable to obtain commercial financing because of the high-risk nature of investment environments. Financial additionality is characterised by an avoidance of market distortions – investors such as Norfund, for example, do not seek to compete with commercial finance providers.

An investment is said to be additional in value if it offers non-financial value that is otherwise not available and that leads to better development outcomes.

Investing in the poorest countries
The World Bank classifies countries in four income groupings: low, lower-middle, upper-middle, and high. Income is measured using gross national income (GNI) per capita, and expressed in USD. Economic growth in low-income countries, in particular, depends on private sector investments.

Norfund's performance: 85 percent of Norfund's investments in 2016 went to low- and lower middle-income countries. In 2015, the corresponding figure for FDI flows was only 7 percent.

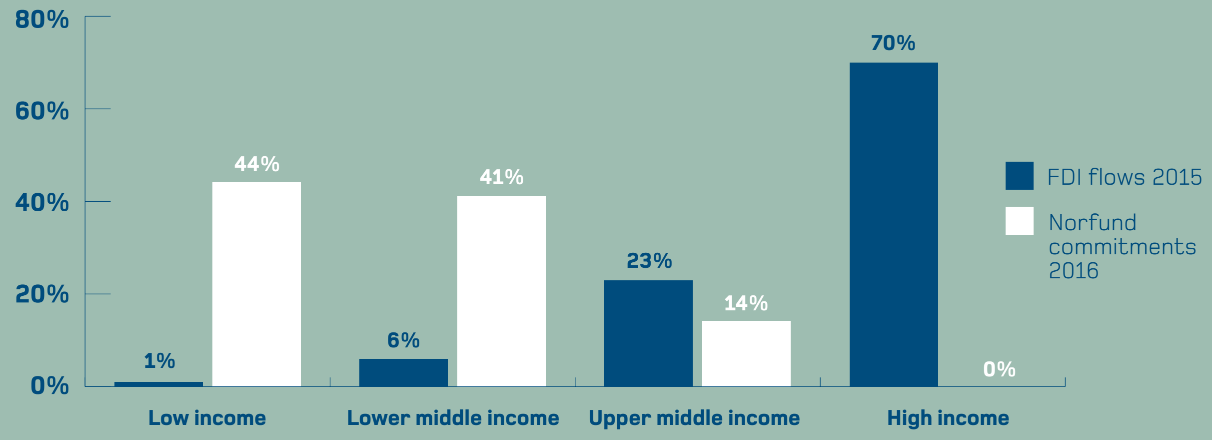
Risky markets
Sovereign credit ratings indicate the risk level of a country's investing environment. Credit rating agencies, such as Standard & Poor's, issue rating grades ranging from AAA (prime) to D (in default). Ratings below BBB- are seen as non-investment grades or "junk", and usually deter investors. A good sovereign credit rating is important for countries wanting to attract foreign direct investment and access funding in international bond markets.

Norfund's performance: 93 percent of Norfund's investments in 2016 were invested in non-investment grade countries or countries without a credit rating; the corresponding figure for FDI in 2015 was just 23 percent.

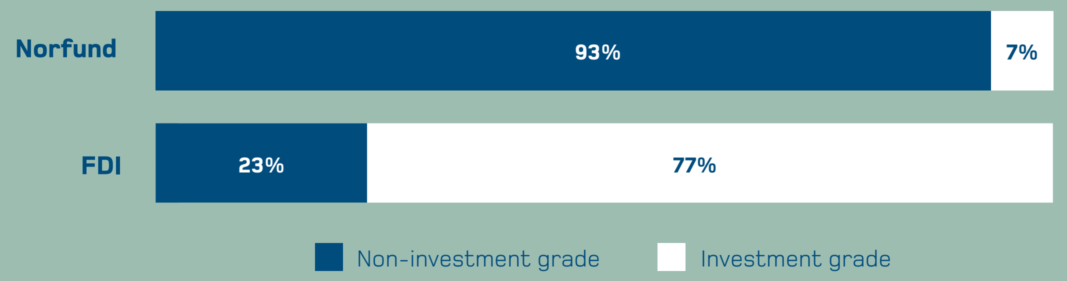
Difficult business environments
The World Bank also ranks economies according to the ease of doing business. A high ease ranking indicates that a country's regulatory environment is conducive to starting and operating local firms. High ease markets are more attractive to businesses and private investors. For the purposes of this analysis, ranked countries are divided into four quartiles, ranging from 1 (easy) to 4 (most difficult).

Norfund's performance: 86 percent of Norfund's investments in 2016 were in countries in the lower two quartiles; the corresponding figure for FDI in 2015 was 11 percent. ■

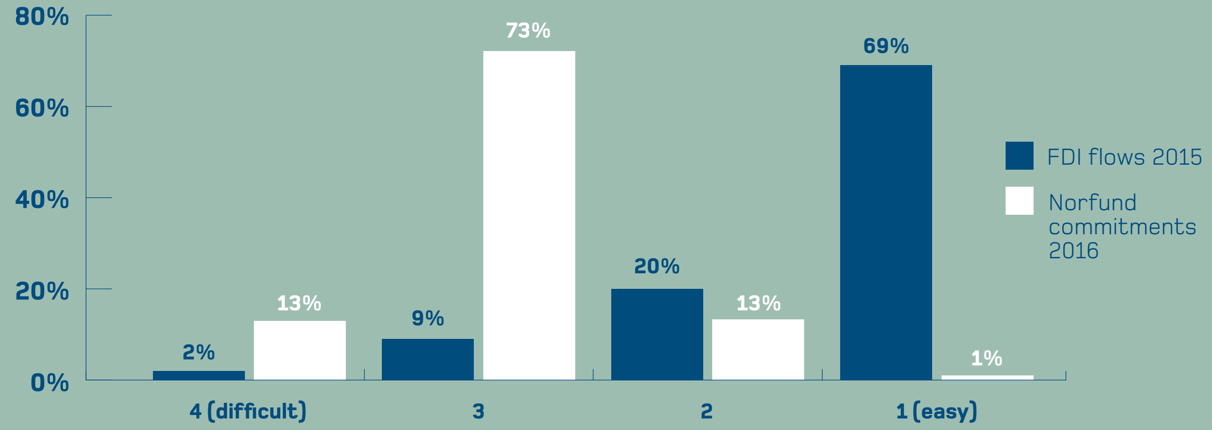
INVESTING IN THE POOREST COUNTRIES
Share of investments by income group



RISKY MARKETS
Share of investments by credit rating



DIFFICULT BUSINESS ENVIRONMENTS
Share of investments by ease of doing business quartiles



Sources: World Bank, World Development Indicators, Standard & Poor's credit ratings and World Bank, Ease of Doing Business ranking