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An example of commitment to good governance: DFIs and corporate governance support

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Good corporate governance practices have a direct impact on corporate performance and value. Moreover, they are an essential component of business ethics and, so, an integral part of "sustainable development". This is why support for the development of good practices has become an important part of the work scope of development finance institutions (DFIs).
There are development finance institutions (DFIs) in all continents. Some are multilateral, like the IFC or the IDB Invest ; others are bilateral, like Proparco, Norfund and some at a country level like Nafin in Mexico. All have the role of financing private companies in developing countries, in order to create wealth and employment, while developing good social, environmental and, of course, governance practices.

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Recognizing the convergence of their missions and their philosophy of intervention, DFIs decided to meet in the form of an informal association around a common platform, the Corporate Governance Development Framework (CGDF), signed in Washington, DC, in 2011. To date, there are 35 signatories from all over the world. Through this founding platform, DFIs commit to integrate corporate governance in its investment operations, regularly exchange information, set up a common strategy, common analysis and action tools, and develop a proactive policy for their clients to promote good corporate governance practices .

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On this common basis, each DFI develops its own programs and actions, according to its priorities or means. However, one action is common to all DFIs: the evaluation of client governance leading to the elaboration, negotiation, and implementation of improvement plans. These plans can be accompanied by technical assistance.

Governance diagnosis, action plans and technical assistance

Loans or equity investments are the occasion for an evaluation of governance and the implementation of action plans.

A DFI entering into a financial relationship with a company or a bank carries out an analysis of its governance practices, taking into consideration five parameters: the structure and functioning of the board of directors, the organisation and functioning of internal control, the quality of external control and transparency of the company, the rights of shareholders (equality between shareholders and shareholder groups), and the management of transactions between parties and conflicts of interest.

The DFIs also evaluates a major transversal aspect, “the commitment to good governance”, which groups together: the actions taken by the company demonstrating a real commitment (existence of a good governance charter, for example), the hyper-dominant situation or not of a majority shareholder, the role and possible privileges of the family when it is a family company, and the questions of succession for key positions. It is therefore a very broad vision of governance.

Of course, DFIs take into account the size of the enterprise and the cultural context in which a company operates: it will obviously not be possible to have the same expectations from a small enterprise or a multinational. Similarly, the pre-eminent role of the founder’s family in certain regions should be taken into account, including companies that have already reached international business exposure. However, the difference is only in terms of degree, not in terms of substance for the structures to be promoted. This is because the principles of corporate governance are universal: everywhere we expect governance that respects legal obligations, fair play towards stakeholders, transparency towards shareholders, a clear organization of powers between general management and governance bodies, effective control of operational and financial activity.

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The diagnosis conducted by the DFIs is undertaken by their internal teams or by external consultants. Based on the findings, recommendations are made. They may, where appropriate, take the form of an action plan to upgrade governance. Diagnosis and action plan are systematically shared with the head of the company, the main executives and the board of directors, because the real driver of change is the company itself.

Where the situation requires it and when a business owner so requests, DFIs may co-finance governance technical assistance with the partner. This is the case when the measures to be taken are particularly specific or require the recurrent presence of a specialist. This can involve training, drafting policies or internal regulations, internal organization of the company, and the setting up of procedures. Here again, it is a question of accompanying the company in its efforts, by making available not only financial resources, but also the requisite human resources.

Investment funds as intermediaries to promote good practices

DFIs can partner with investment funds by taking equity, providing debt lending or co-investing at the level of the investee company. This type of intervention is also an opportunity to promote good environmental, social and governance practices, and ideally realize a "sustainability premium " at exit. Regarding governance, DFIs encourage investment funds to apply the same rules for their underlying assets as they require for their own direct clients. Depending on the scale of investment and risk profile, some DFIs, including FMO and Obviam , even make it a contractual obligation.

Client training and awareness

Many DFIs offer group or individual training to clients or prospects. Where possible, grouped trainings are organized in partnership with representative private sector structures. . Other examples include the principle of thematic conferences on a governance topic . In addition to these actions, standard documents or examples are made available to facilitate the work of entrepreneurs and boards of directors (internal regulations of a board of directors and associated committees; family policy charter, etc.).

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Corporate governance, a real world experience feedback

The particularity of good governance practices is precisely that they are… good practices. That is to say that they are constituted and evolve essentially based on real world experience and on the interaction between companies. States legislate relatively little in this area , especially for non-listed companies. As a result, it is very often up to professional organizations to write down the recommended practices and ensure that they are applied. In this case, good practices are not mandatory; they are prepared by and for companies themselves without state intervention. However, professional groups strongly encourage their members to comply with voluntary codes of good governance or to explain the reasons why they prefer to ignore them (Comply or Explain principle). This role of reflection, code compilation, and publication of professional associations is often supplemented – when resources are available – by training and awareness-raising activities.

It is for these reasons that some DFIs, including the IFC, IDB Invest and CAF, are very active in the development of professional networks, such as institutes of corporate governance, associations of directors, associations of corporate secretaries, academic centers and in helping to publish Codes of Good Governance in emerging and developing countries. It is worth mentioning the particularly important role of institutes and associations of directors in the diffusion of good practices in the markets where they exist and at the very heart of boards of directors. Moreover, these institutes and associations are very often at the origin or closely associated with the drafting of "Codes of Good

Governance

It should also be noted that DFIs disseminate reference works and analytical tools for use by governance actors, business leaders and administrators. They, thus, complement the work of specialized networks. The aim is to offer practical, didactic books and tools that can be used directly by professionals.

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The activities of DFIs in favour of business development are multifaceted, and the offer continues to grow. In addition to business diagnostics, consulting and technical assistance, they provide training, reference works, and support to intermediary bodies involved in governance. Promoting corporate governance has become a key driver that DFIs use to fulfil their mission of providing financial and non-financial added value to developing economies.

Footnotes:

1 International Finance Corporation, a World Bank company.
2 IDB: Interamerican Development Bank.
3 Norway's development finance institution.
4 Some DFIs may have an expanded role in financing state-owned enterprise.
5 In addition, there are regional working groups to promote advanced collaborations: thus, the European institutions have grouped together in the
EDFI group (European Development Financial Institutions
6 Notwithstanding financial, social and environmental due diligence.
7 Investors are willing to pay a higher price for a company with high standards of governance. Since the 2000s, corporate governance has become
one of the building blocks of corporate value. This investor position is particularly true for companies in emerging markets.
8 FMO: Nederlandse Financierings-Maatsschappij voor Ontwikkelingslanden, the Dutch development finance company. Obviam: independent Swiss investment advisor specialised in developing and emerging countries, from the Swiss Investment Fund for Emerging Markets (SIFEM).
9 These include the training seminars organized by IDB Invest, or by CAF to local Development Banks in Latin America.
10 Such as the one organized by Proparco in the spring of 2018 in Yaoundé or the joint program to promote good practices launched in 2017 by the IFC and the Institute of Directors of Côte d'Ivoire.
11 With the exception of banking and financial activities, which are often highly regulated.