



RIKSREVISIONEN  
*The Swedish National Audit Office*

## RiR 2009:4 Summary

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Swedfund International AB and its commission to  
society

# Summary

The Swedish National Audit Office (SNAO) has audited Swedfund International AB, which is a fully state-owned enterprise with social commissions. Swedfund shall contribute to the goals of Sweden's policies for global development and Swedish development work through investments that contribute to sustainable economic development in those countries where investments are made.

SNAO has examined how Swedfund carries out its commissions and how the government has managed the company's activities through decisions by the Riksdag.

## **Government manages Swedfund in line with Riksdag decisions for global development**

SNAO's assessment is that the government has adapted the management of Swedfund to Riksdag decisions regarding policies for global development.

In its Articles of Association, Swedfund states that its activities will be to develop and administrate an investment portfolio consisting of shares, loans and guarantees.

Swedfund shall invest in companies in developing countries and Eastern European countries outside the EU. It is also clear from the Articles of Association that activities, on the basis of the overall objectives, shall be carried out in a businesslike fashion.

Swedfund has also received an owner's directive with guidelines for the company's activities. In the owner's directive from 2007, the owner detailed the goals of the company by stating an order of priority:

1. Development goals
2. Profitability goals
3. Cooperation with trade and industry

Through the owner's directive of 2008 the company was given the commission to report on the development effects of its activities in the annual report, divided into ongoing and completed investments.

The expected development effects will be decisive in the treatment of possible investments and decisions regarding them. According to the board and the owner, the company shall not invest in projects that are not profitable, irrespective of the development effects.

## **Need for clarifications in the governing documents**

SNAO considers that certain formulations in the list of activities in the Articles of Association, and in the owner's directive, are unclear and may be interpreted in different ways. In conjunction with interviews with the board of Swedfund, some doubt was also apparent regarding the interpretation of certain concepts in the Articles of Association.

For example, the Riksdag has underlined the importance of a three-dimensional view of sustainable development that includes social, economic and environmental aspects. SNAO thus asks why the Articles of Association state the more limited concept of sustainable development as a goal for the company's investments.

SNAO also points out that the goal for Swedfund to cooperate with Swedish trade and industry in its investments must be seen in the light of the Swedish principle of independent aid. This is not made clear in the text in the owner's directive.

SNAO consider that there is reason to review the Articles of Association and the owner's directive. Formulations can be clarified and concepts refined.

### **The supplementary role to the market should be reviewed**

According to the owner's directive, Swedfund shall avoid competition with commercial and financial players, i.e. be market supplementary. Investment projects shall be of the type for which there are not judged to be financiers on the private market.

However, before making an investment Swedfund seldom carries out an evaluation of whether the project could be financed by any other party. At the same time it may be questioned whether and how it would be possible to ascertain if there were alternative financiers for investments in developing countries. The requirement that the company shall avoid competition with commercial financial players can therefore be questioned, and should be reviewed.

### **Development goal overshadowed by profitability**

The owner has decided that development effects shall be decisive for the choice of investments, and during recent years the company has endeavoured to fulfil this. Swedfund's investment process and follow-up work has been developed and the company has worked to structure supporting information for decisions. Among other things, a quality assurance process has been introduced. This means that more employees assess projects on the basis of profitability and Swedfund International AB and society commission 9 SNAO potential development effects, not only the person responsible for investments himself. But the board, however, is of the opinion that the company needs to do more in this area since the quality of supporting information still varies considerably.

Swedfund's investments have primarily been motivated from an economic perspective. The financial development and profits of the investments is followed up thoroughly and regularly.

The expected development effects, though, have often been formulated in general terms in the investment decisions. Follow-up work has also been limited and general.

SNAO considers that the company should continue its improvements in work with projects' development effects and formulate measurable development goals to a greater extent.

## **Swedfund invests in venture capital funds**

The emphasis that has been put on projects' financial results is also indicated by the fact that Swedfund invests in venture capital funds which, for reasons of taxation among others, are located in countries and regions that the OECD describes as tax havens. It may be questioned whether this is in line with Swedfund's commission to contribute to development effects.

Venture capital funds are funds which in turn purchase shares in different companies. The funds are often geographically focused or aimed at particular industries. Swedfund's commitments to venture capital funds have increased.

There is a risk that Swedfund's public control is limited with respect to investments in venture capital funds, as are its possibilities of influencing the companies in which the funds invest.

SNAO judges that Swedfund's commitment to venture capital funds should be reviewed in the light of the company's commission.

## **Further capital contributions require analysis**

The financial goal that the owner has set for Swedfund's activities is that average returns on equity before tax shall equal the average national debt interest over one year. The level of the returns target has not been adjusted since it was introduced in 2002. Swedfund has achieved its financial goal with a wide margin during the last five-year period.

Swedfund has a total equity of approximately SEK 2 billion.

The company has received capital contributions decided by the Riksdag on a number of occasions, and during 2008 and 2009 has requested further capital contributions from the state. However, the owner has not carried out a financial analysis of the company's real requirements of capital, which is motivated before further capital contributions. In this context the government should also report to the Riksdag on the company's future direction, scope and role in Swedish development cooperation. There is also a reason to review the company's target for returns.

## **Increased investment volume**

Swedfund's investment volume has increased dramatically in recent years. Investments through loans have increased in relation to the proportion of equity. The proportion of investments in venture capital funds has also increased. Loans may be seen as a safer form of investment with annual interest revenue and require considerably less involvement by Swedfund, as opposed to direct investments through share capital. Investments made in venture capital funds also require less involvement by Swedfund.

SNAO emphasizes that investments through venture capital funds, and also loans, cannot be influenced and followed up to the same extent as direct investments in share capital. When making direct investments in companies, Swedfund is generally entitled to a place on the board. Opportunities for following up the development effects of projects are more limited when investments are through loans and venture capital funds.

## **High administration and management costs**

An analysis of the returns on share and loan portfolios shows that Swedfund has relatively high administration and management costs. The audit shows that these costs reduce share and loan portfolio returns by an average of 6.5 percentage units.

After deduction of costs, and loan portfolio average returns are negative. The share portfolio returns, i.e. profits on sales of shares, are still relatively good in relation to the selected index.

SNAO judges that there is reason to carry out a thorough screening of Swedfund's administration and management costs for its investments.

## **Deficiencies in capital management**

Swedfund's investment policy is decided by the board. Nevertheless it is deficient, with vague target formulations among other things. A number of terms in the policy are not defined at all, and certain guidelines are contradictory.

The current management and borrowing agreements have not been subject to procurement procedures or negotiations for 11 and 13 years respectively, and conditions have changed since then.

SNAO's assessment is that the policy can be considerably improved and that the board has been passive in the case of capital management.

## **Recommendations**

SNAO's assessment is that the government has adapted the control of Swedfund International AB to the decision by the Riksdag regarding policies for global development.

The company has strived to comply with the government's control and demands. The audit gives SNAO reason to submit the following recommendations, however.

SNAO recommends that the government

- clarifies Swedfund's Articles of Association and owner directive,
- reviews the requirement on Swedfund's market supplementing role,
- evaluates Swedfund's real capital requirements and adapts the target for returns to Swedfund's prevailing conditions,
- draws up guidelines for the involvement of state-owned enterprises in so-called tax havens.

SNAO recommends that Swedfund International AB

- details the development effects of investments and improves follow-up in line with the government's owner directive,
- considers to what extent Swedfund shall act through venture capital funds,
- reviews costs for share and loan portfolios,
- makes an inspection of the company's capital management.