

Document: EB 2013/109/R.38/Add.1
Agenda: 17
Date: 17 September 2013
Distribution: Public
Original: English

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Enabling poor rural people
to overcome poverty

IFAD's investment portfolio as at 31 August 2013

Addendum

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Executive Board — 109th Session
Rome, 17-19 September 2013

For: Information

IFAD's investment portfolio as at 31 August 2013

I. Executive summary

1. The 128th meeting of the Audit Committee, held on 6 September 2013, recommended that an addendum be included for information updating the Executive Board on recent developments pertaining to IFAD's investment portfolio.
2. As at 31 August 2013, the investment portfolio's year-to-date net rate of return was negative 1.61 per cent¹, translating into a negative investment income amount of US\$37.6 million for the eight month period.
3. Anticipating future net outflows resulting from an increased Programme of Work (PoW), and the possibility of a negative investment performance, IFAD proactively initiated an overall investment strategy review in the first half of 2013. As part of this review, an asset class study with BlackRock (an investment management and financial consulting firm) was undertaken to validate options and support decisions on any actions which could be undertaken by IFAD to protect the investment portfolio.
4. Recommendations of the strategic review are within the provisions stipulated in IFAD's Investment Policy Statement (IPS) and have been endorsed by the President for implementation by year end.

II. Performance updates as at 31 August 2013

5. As reported in the 109th session of the Executive Board², the net year-to-date performance of IFAD's investment portfolio as at 30 June 2013 was negative 1.51 per cent. Despite a positive rally in July 2013, the investment portfolio's performance continued its trend the following month and the net year-to-date performance as at 31 August 2013 remained negative at 1.61 per cent¹. As a result, the net negative investment income amounted to US\$37.6 million for the eight month period.
6. IFAD's investment portfolio has continued to remain within its approved IPS risk budget levels. As at 31 August 2013, the conditional value-at-risk (CVaR) was at 2.69 per cent, representing a slight reduction in risk from 2.85 per cent reported as at 30 June 2013 and well within the risk budget level of 6.00 per cent. This low risk level reflects IFAD's conservative approach to investments.

III. Mitigation measures

7. Following the banking crises which started in 2008 and escalated into a global sovereign crisis during 2009/2010, the uncertain economic environment favoured global government bond investors like IFAD as a safe haven for investments like United States Treasuries and core European fixed income which performed well during this period. IFAD's investment income therefore remained solid whilst maintaining a low risk profile. However with general interest rates at a historical low level after extraordinary measurements taken by monetary authorities in the wake of the financial crises, fundamentals of these investment asset classes are now deemed to present different characteristics.

¹ The August 2013 year-to-date performance for IFAD is based on final year-to-date performance data as at 31 July 2013 plus estimated August 2013 performance data. Final performance data for August 2013 was not available when this paper was prepared.

² EB 2013/109/R.38 – Report on IFAD's investment portfolio for the first and second quarters of 2013.

8. In addition, the significant increase of the PoW over the recent replenishment cycles has resulted in substantial growth of net outflows, thereby decreasing the investment portfolio's asset size. This aspect merited a review of investments to secure liquidity for disbursements and maximize investment returns within established risk parameters stipulated in IFAD's IPS.
9. To complement the overall strategy review, an asset class study was undertaken with an external advisor BlackRock, to determine what strategic action, if any, IFAD can take to preserve the investment portfolio in light of the challenging circumstances that lay ahead.
10. The outcome of the study indicated an expected rise in the interest rate environment over the next five years, meaning that cash and near cash investments are expected to outperform global government bonds. The outlook for sovereign emerging market bonds and non-government bonds remain moderately positive, although not necessarily in the short-term.

IV. Conclusion

11. Based on the results of the investment strategy review; modifications of IFAD's policy asset allocation were recommended to IFAD's two finance committees (FALCO and FISCO) and were subsequently approved. As per standard practice the Audit Committee and the Executive Board will be informed at their subsequent sessions.