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Investing in rural people

Report on IFAD's Investment Portfolio for the Third Quarter of 2019

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For: **Information**

Report on IFAD's Investment Portfolio for the Third Quarter of 2019

I. Executive summary

1. The value of IFAD's investment portfolio in United States dollar terms decreased by US\$ 71.8 million from US\$ 1,123.8 million as of 30 June 2019 to US\$ 1,052.0 million as of 30 September 2019.¹ The main factors underlying this decrease were net outflows of US\$ 47.8 million, net investment income of US\$4.8 million and negative foreign exchange movements of US\$ 28.8 million.
2. Risk levels in the investment portfolio were stable. The conditional value at risk (CVaR) of the overall portfolio marginally increased from 0.80 to 0.82 as portfolio duration levels decreased from 0.52 to 0.39. It is worth noting that BBB-rated debt made up only 1.9 per cent of the portfolio compared to 2.4 per cent at the beginning of the quarter.
3. The size of the portfolio comfortably exceeds the minimum liquidity requirement.

Table 1

Key portfolio changes during the third quarter

	Q2 2019	Q3 2019
Portfolio size (thousands of US\$)	1 123 793	1 052 038
Net investment income (thousands of US\$)	5 678	4 799
Rate of return (%)	0.50	0.44
Duration	0.52	0.39
CVaR	0.80	0.82

¹ Note: Figures in this report have been rounded up or down. There may therefore be discrepancies between the actual totals of the individual amounts in the tables and the totals shown, as well as between the numbers in the tables and the numbers included in the corresponding analyses in the text of the annual report. All roundings, totals, percentage changes and key figures were calculated using the complete (unrounded) underlying data.

II. Market conditions

4. Government bond yields declined markedly due to increased risk aversion among investors as trade tensions escalated between the United States and China. In addition, the Federal Reserve cut interest rates twice during the quarter, further supporting government bonds.
5. The increased risk aversion, although positive for duration-sensitive assets, caused corporate bonds to underperform relative to government bonds. Therefore, returns on portfolios with greater exposure to corporate bonds, such as the asset liability portfolio, experienced only modest gains, while the global liquidity portfolio produced significant gains.

III. Portfolio allocation

6. During the third quarter of 2019, the value of IFAD's investment portfolio in United States dollar terms decreased by US\$ 71.8 million. Drawdowns of concessional partner loans led to significant cash balances.

Table 2

Movements affecting IFAD's investment portfolio during the third quarter of 2019

(Thousands of United States dollars equivalent)

	Operational cash ^a	Global strategic portfolio ^b	Global liquidity portfolio	Asset liability portfolio	Other ^c	Grand total
Opening balance (30 Jun 2019)	105 152	130 810	330 073	556 937	821	1 123 793
Net investment income	201	932	3 184	484	(2)	4 799
Net flows ^d	50 376	(131 470)	48 351	(14 824)	(207)	(47 774)
Foreign exchange movements	(5 0819)	(272)	38	(23 434)	(23)	(28 780)
Closing balance (30 Sep 2019)	150 639	-	381 646	519 163	589	1 052 038

^a Cash held with banks that is readily available for disbursing loans, grants and administrative expenses.

^b The global strategic portfolio was closed on 31/7/2019.

^c Residual cash positions of portfolios closed in 2019 and cash held in Chinese renminbi.

^d Net flows consist of outflows for portfolio transfers, disbursements for loans, grants, investment and administrative expenses, inter-fund portfolio transfers and inflows from loan reflows and encashment of Member States' contributions.

IV. Investment income

7. Gross investment income for the third quarter of 2019 amounted to US\$5.0 million, with net investment income inclusive of all investment-related fees totalling US\$4.8 million. Year-to-date net investment income amounted to US\$20.7 million. Table 2 presents a summary of the third quarter 2019 investment income broken down by portfolio.

Table 3

Breakdown of investment income by portfolio during the third quarter of 2019

(Thousands of United States dollars equivalent)

Investment income	<i>Operational cash</i>	<i>Global strategic portfolio</i>	<i>Global liquidity portfolio</i>	<i>Asset liability portfolio</i>	<i>Other</i>	<i>Total</i>
Interest and coupon income	230	253	2 416	311	0	3 210
Realized market gains/(losses)	0	675	599	(5)	()	1 268
Unrealized market gains/(losses)	-	-	234	258	0	492
Amortization*	-	8	-	-	-	8
Investment income before fees	231	935	3 249	563	0	4 978
Investment manager fees	-	-	-	-	7	7
Custody fees	(1)	(3)	(11)	(9)	(9)	(33)
Bank charges	(29)	-	-	()	-	(30)
Advisory and other investment-related fees	-	-	(54)	(69)	()	(123)
Investment income after fees	201	932	3 184	484	(2)	4 799

* A period's amortization amount represents a portion of the difference between the purchase price and the final redemption value for portfolios reported at amortized cost.

V. Rate of return

8. The rate of return on IFAD's investment portfolio is calculated in local currency terms without reflecting the impact of foreign exchange movements.
9. Excluding the asset liability portfolio, IFAD's investment portfolio generated a positive net return of 0.75 per cent during the third quarter of 2019, 32 basis points above the benchmark return for the same period. The asset liability portfolio generated a positive gross return of 0.11 per cent versus a target rate of return of 0.05 per cent for the same period. The net rate of return for the entire investment portfolio including the asset liability portfolio was 0.44 per cent.

Table 4
IFAD's portfolio performance rolling average as of September 2019
 (Percentages in local currency terms)

	Quarterly performances in 2018				Quarterly performance in 2019				
	First quarter	Second quarter	Third quarter	Fourth quarter	First quarter	Second quarter	Third quarter	Third quarter benchmark	Difference
Operational cash	0.19	0.16	0.29	0.24	0.40	0.44	0.12	0.12	0.00
Global strategic portfolio	0.53	0.55	0.56	0.57	0.59	0.61	0.00	0.00	0.00
Global liquidity portfolio	0.41	0.50	0.60	0.64	0.71	0.77	0.99	0.56	0.43
Global credit bonds	(1.03)	(0.02)	0.22	0.85	2.98	0.65	0.00	0.00	0.00
Gross rate of return excluding ALP	(0.21)	0.21	0.43	0.59	1.28	0.68	0.77	0.44	0.34
Net rate of return excluding ALP	(0.26)	0.16	0.39	0.55	1.24	0.65	0.75	0.44	0.32
Asset liability portfolio (ALP)*	(0.03)	(0.16)	0.04	(0.76)	0.77	0.36	0.11	0.05	0.07
Gross rate of return including ALP	(0.15)	0.08	0.28	0.01	1.05	0.52	0.45	n/a	n/a
Net rate of return including ALP	(0.19)	0.05	0.26	(0.02)	1.02	0.50	0.44	n/a	n/a

*The ALP benchmark is a target rate of return representing the cost of funding and does not reflect the investment universe allowed by the guidelines.

Table 5
IFAD portfolio performance rolling average as at 30 September 2019
 (Percentages in local currency terms)

	One year	Three years	Five years
Net portfolio performance (including ALP)	1.91	1.09	1.47

Table 6
Historical annual performances versus benchmarks
 (Percentages in local currency terms)

	2018		2017		2016		2015	
	Actual	Benchmark	Actual	Benchmark	Actual	Benchmark	Actual	Benchmark
Operational cash	0.88	0.88	0.79	0.79	0.30	0.30	0.13	0.13
Global strategic portfolio	2.22	1.02	1.92	0.80	1.83	0.95	1.75	1.12
ALP	(0.91)	0.21	1.39	-	0.62	-	(0.78)	0.31
Chinese RMB portfolio	1.46	0.00	3.72	-	0.48	-	-	-
Global government bonds	0.89	1.88	0.27	0.99	0.64	1.03	0.05	0.43
Global credit bonds	0.00	0.90	3.43	3.31	3.23	3.52	1.17	1.25
Global inflation-indexed bonds	0.16	0.39	1.86	1.53	4.41	4.37	(0.85)	(0.51)
RAMP portfolio	0.14	0.14	0.31	0.30	n.a.	n.a.	n.a.	n.a.
Emerging market debt bonds	(3.07)	(2.55)	8.45	7.64	6.83	6.40	(1.17)	(0.86)
Gross rate of return (excluding fees)	0.21	n.a.	2.35	n.a.	3.09	n.a.	0.13	0.35
Net rate of return (including all fees)	0.09	n.a.	2.21	n.a.	2.91	n.a.	(0.06)	0.16

VI. Composition of the portfolio by instrument

10. Table 7 shows the composition of the investment portfolio by instrument as at 30 September 2019.

Table 7
Investment portfolio by instrument as of 30 September 2019
 (Thousands of United States dollars equivalent)

	30 September 2019	
	Actual portfolio allocation (US\$)	Actual portfolio allocation (%)
Cash*	152.1	14.5
Swaps	-3.4	(0.3)
Time deposit	.0	0.0
Global government bonds/agencies	507.0	48.2
Global credit bonds	396.3	37.7
Total	1 052.0	100.0

* Includes pending trades.

VII. Risk measurements

11. The risk budgeting measures used pursuant to the Investment Policy Statement (IPS) are CVaR and the ex ante tracking error, which are reported in subsections B and C. Other risk indicators are reported in subsections A, D, E and F.

A. Market risk: duration

12. Duration is a measure of the sensitivity of the market price of a fixed-income investment to a change in interest rates. Duration is expressed as a number of years.

Table 8
Effective durations of IFAD's investment portfolio and benchmarks
 (Duration in number of years)

	30 June 2019		30 September 2019	
	Portfolio	Benchmark	Portfolio	Benchmark
Asset liability portfolio	0.51	0.50	0.52	0.60
Global liquidity portfolio	0.35	0.00	0.35	0.50
Global strategic portfolio	1.39	0.00	n/a	n/a
Total portfolio (including operational cash)	0.52	0.42	0.40	0.56

13. The overall portfolio duration was 0.40 year (1.18 years in December 2018).

B. Market risk: conditional value at risk

14. The one-year CVaR at 95 per cent is a measure of the potential average probable loss of a portfolio under extreme conditions and provides an indication of how much value a portfolio could lose over a forward-looking one-year horizon with a confidence level of 95 per cent.
15. The maximum risk budget for the overall investment portfolio is set in the IPS at a CVaR of 3.0 per cent. CVaR for the overall IFAD portfolio was 0.82 per cent, which is well below the approved risk budget. The current CVaR risk level of 0.82 per cent implies an average loss of US\$ 8.6 million under extreme market conditions.

Table 9

CVaRs of IFAD's asset classes

(95 per cent confidence level; percentages based on historical simulations over a five-year history)

	<i>Actual investment portfolio one-year CVaR</i>	
	<i>30 June 2019</i>	<i>30 September 2019</i>
Asset liability portfolio	1.37	1.30
Global liquidity portfolio	0.92	1.12
Total portfolio (including operational cash)	0.80	0.82

Note: Total portfolio CVaR is lowered by the operational cash portfolio, as cash is not subject to market fluctuations.

C. Credit risk: credit rating analysis

16. The IPS establishes a credit rating floor, in addition to investment guidelines setting out credit quality requirements. Credit risk is managed by monitoring the compliance of securities with these requirements.

Table 10

Investment portfolio composition by credit rating at 30 September 2019

(Thousands of United States dollars equivalent)

	<i>Operational cash</i>	<i>Global liquidity portfolio</i>	<i>Asset liability portfolio</i>	<i>Other</i>	<i>Total</i>	<i>Percent-age</i>
AAA	-	299 761	-	-	299 761	28.9
AA+/-	-	83 308	181 065	-	264 373	25.5
A+/-	-	-	319 482	-	319 482	30.8
BBB+/-	-	-	19 706	-	19 706	1.9
Cash ^a	150 639	18 575	2 306	590	172 110	15.0
Time deposit	-	-	-	-	-	-
Pending trades ^b	-	-19 997	-	-	-19 997	(1.9)
Swaps	-	-1	-3 396	-	-3 396	(0.3)
Total 30/09/2019	150 639	381 646	519 163	590	1 052 038	100.0

^a Consists of cash and equivalents with central banks and approved commercial banks and cash held by external portfolio managers. These amounts are not rated by credit rating agencies.

^b Pending foreign exchange purchases and sales used for hedging purposes and trades pending settlement. These amounts do not have an applicable credit rating.

E. Currency risk: currency composition analysis

17. In order to protect the short term liquidity profile from foreign currency risk fluctuations, the Fund ensures that the currency composition of projected inflows matches that of outflows over a 24-month horizon.

Table 11

Currency composition of assets and commitments as at 30/09/2019

(Thousands of United States dollars equivalent)

Category	CNY Group	EUR Group	GBP Group	JPY Group	USD Group	Grand Total
Current Liquidity						
Cash	34 996	85 510	1 087	198	28 268	150 058
Investments	577	71	12	0	381 871	382 532
Projected Inflows						
Contributions	40 532	185 163	68 580	34 986	217 721	546 981
Projected Reflows	79 807	240 633	58 622	62 624	342 826	784 512
Projected Liquidity	155 912	511 378	128 301	97 807	970 686	1 864 084
Projected Outflows						
Projected Disbursements	(86 621)	(315 776)	(63 626)	(67 970)	(988 848)	(1 522 841)
Projected Operating Expenses	0	(225 012)	0	0	(143 860)	(368 872)
Projected Outflows Total	(86 621)	(540 788)	(63 626)	(67 970)	(1 132 708)	(1 891 713)
Hedging						
Currency Forwards	0	0	0	0	0	0
Hedging Total	0	0	0	0	0	0
Projected Liquidity (Deficit)/Excess	69 292	(29 410)	64 674	29 837	(162 023)	(27 629)
(Deficit)/Excess as %of Commitments	3.66%	(1.55%)	3.42%	1.58%	(8.56%)	(1.46%)

F. Liquidity risk: minimum liquidity requirement

18. IFAD's latest financial model assumptions – incorporating 2018 resources available for commitment under the sustainable cash flow approach – calculate a minimum liquidity requirement of US\$514.0 million (60 per cent of gross annual outflows),² which is comfortably cleared by the investment portfolio balance of US\$1,052 million (see table 1).

² See EB 2018/125/R.42.