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Investing in rural people

IFAD's Investment Policy Statement 2022

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Preamble

1. The Investment Policy Statement (IPS) is designed to establish fundamental directives for the placement of IFAD funds. While the Liquidity Policy lays down the directives for the amount of liquidity required, the IPS focuses on the composition of the investments made to meet the requirements. The IPS also aims at ensuring that financial counterparts abide, with utmost diligence and within the objective and functions set forth in the Agreement Establishing IFAD, by the Ten Principles of the United Nations Global Compact.

2. The responsibility to set the IPS rests with the Executive Board, within the parameters established by the Governing Council, whereas the President remains responsible for ensuring implementation of the IPS.

Recommendation for approval

The Executive Board is invited to approve IFAD's Investment Policy Statement, as contained in this document.

I. Scope and purpose

1. The Investment Policy Statement (IPS) provides a framework for the management of IFAD's investments. The purpose of the IPS is to:

   (i) Identify key roles and responsibilities related to the governance of IFAD's investment portfolio (section II);

   (ii) Set forth IFAD's investment objectives for risk and return, including eligible asset classes (section III);

   (iii) Establish a risk management framework (section IV); and

   (iv) Define the approach to asset allocation and tranching of the investment portfolio (section V).

A. Definition of investor and assets

2. IFAD is a specialized agency of the United Nations. It came into existence on 30 November 1977, when the Agreement Establishing IFAD entered into force. Membership in the Fund is open to any Member State of the United Nations – or any of its specialized agencies – or the International Atomic Energy Agency.

3. This IPS governs the investments of the Fund's resources that are derived from regular replenishments, borrowed funds or loan reflows, and that are used for commitments of loans and grants under IFAD's regular programme. It also serves as a framework for investments of other cash funds entrusted to and managed by the Fund, and will complement any gaps left uncovered by separate policies and guidelines established to govern such other assets.

B. Actors and their roles

Governing Council

4. The Governing Council is IFAD's main decision-making body. Each Member State is represented in the Governing Council and all the powers of the Fund are vested in the Governing Council. Subject to the limitations stated in the Agreement Establishing IFAD, the Governing Council may delegate powers to the Executive Board.

Executive Board

5. The Executive Board is responsible for overseeing the general operations of the Fund and exercises the powers given to it by the Agreement Establishing IFAD or delegated to it by the Governing Council.

Audit Committee

6. The Executive Board has established a subsidiary body, the Audit Committee, to which it refers, among other matters, questions concerning the investment of IFAD's resources in preparation for decisions by the Executive Board.

The President

7. The President is the legal representative of IFAD. Under the direction of the Governing Council and the Executive Board, the President heads, organizes, appoints and manages the Fund's staff, and is responsible for conducting the business of the Fund. Based on his or her authority to organize staff, the President may reconfigure IFAD's organizational structure. The President may place or invest cash funds not needed immediately for the Fund's operations or administrative expenditures.

(i) In order to discharge functions related to financial management and investments, the President has established a management committee to provide investment and financial advice.

II. Governance

A. Responsibilities for determining, executing and monitoring the investment policy

8. The President will ensure implementation and monitoring of all aspects of the investment policy.

B. Process for reviewing and updating the investment policy

9. The appropriateness of the investment policy will be reviewed annually by the Executive Board at the last session of each calendar year on the basis of a report submitted to it by the President. Having considered the report, the Executive Board may amend and update the IPS accordingly.

C. Responsibilities for approving investment guidelines and changes

10. Acting under regulation XIV of the Financial Regulations of IFAD and in implementation of regulation VIII, the President shall approve and adopt investment guidelines for managing each investment portfolio within the limits defined in the IPS.

D. Responsibilities for engaging and discharging external investment managers, the custodian bank(s) and other financial advisers

11. The President is responsible for the appointment and dismissal of external investment managers, the custodian bank(s) and other financial advisers required to execute the Fund's investments.

12. External investment managers must fulfil the following initial requirements in order to be considered for the selection process:

    (i) Investment managers must clearly articulate the investment strategy that they will follow and document that such strategy has been adhered to over time;

    (ii) Investment managers must, in all countries in which they operate, adhere to the governing legislation and regulations concerning financial services, including the authority of the competent regulatory bodies;

    (iii) Investment managers should endeavour to comply with the Global Investment Performance Standards[1] and to provide at least historical quarterly performance data calculated on a time-weighted basis, based on a composite of fully discretionary accounts or similar investment style, and reported net and gross of fees; and

    (iv) Investment managers must provide detailed information on the history of the firm, key personnel, key clients, fee schedule and support personnel.

13. External investment managers are formally appointed through the signing of an investment management agreement by the President. The agreements outline in detail the responsibilities of the managers.

[1] Global Investment Performance Standards (GIPS) are a set of voluntary standards used by investment managers throughout the world to ensure the full disclosure and fair representation of their investment performance. The GIPS were created by the Chartered Financial Analyst Institute, a global association for investment management professionals.

14. A copy of this IPS, as updated from time to time, is provided to each external investment manager retained to provide investment services to IFAD. Each manager will acknowledge receipt of the document and acceptance of its content in writing as part of the agreement.

E. Responsibilities for monitoring external investment managers, the custodian bank(s) and financial advisers

15. The President will ensure that dedicated organizational units are made responsible for developing and maintaining relationships with external investment managers, custodian banks and financial advisers.

16. These units will ensure that appointed investment managers fulfil their mandates within the contractual obligations outlined in the relevant investment management agreement, including the investment guidelines incorporated into each agreement.

F. Responsibilities for internally managed investments

17. The President will ensure that internal investment portfolios are managed appropriately by the relevant organizational unit in line with this IPS and the specific investment guidelines.

III. Investments, return and risk objectives

A. Overall investment objective

18. Regulation VIII (2) of the Financial Regulations of IFAD forms the basis of IFAD's investment objectives, which for the purpose of this IPS are:

    (i) **Security** - preservation of the value of invested assets;

    (ii) **Liquidity** - resources must be readily available if and as required by operations; and

    (iii) **Return** - the highest possible return within the above conditions in a non-speculative manner.

B. Risk tolerance

19. The level of risk taken should be consistent with the overall investment objective of the Fund. Consequently, IFAD will only accept non-speculative risk in order to achieve its investment objectives. The risk tolerance level for the portfolio is set at a conditional value at risk of 3 per cent.

C. Return on investment requirements

20. The primary objective of IFAD's investments, as stated above, is to maintain the security and liquidity of funds invested. Subject to these two parameters, IFAD seeks to maximize prudently the total return on its investments.

D. Eligible asset classes

21. The following asset classes are eligible within IFAD's asset allocation (see table 1 below for asset class rating floors):

    Money market instruments

    (i) Time deposits, certificates of deposit, commercial paper, treasury bills and money funds

    Fixed-income securities

    (i) Government and government agencies, at national or subnational level

    (ii) Supranationals

    (iii) Asset-backed securities (only agency-issued or guaranteed)

    (iv) Corporates

    (v) Callable bonds

(vi) Covered bonds

Derivatives are allowed only for hedging purposes:[2]

(i) Currency forwards

(ii) Exchange-traded futures and options

(iii) Interest rate swaps

(iv) Cross currency swaps

(v) Credit default swaps

(vi) Asset swaps

22. IFAD can enter into securities-lending agreements as well as repurchase and reverse-repurchase transactions.

23. IFAD does not use any form of leverage and does not use derivatives contracts to leverage positions in the investment portfolio.

E. Environmental, social and governance principles

24. Responsible investing entails, in addition to more traditional factors, the consideration of environmental, social and governance factors in the choice of financial investments.

25. IFAD is a responsible investor. The Fund’s main objective is to invest in securities where the issuer, at a minimum, adheres to fundamental principles of human rights, labour, environment and anti-corruption. Therefore IFAD adheres to the Ten Principles of the United Nations Global Compact (UNGC).[3] Only investments that comply with the UNGC principles are considered by IFAD as eligible for investment.

26. Compliance with UNGC principles is ensured through systematic exclusion by norms-based screening of securities issued by entities:

    (i) involved with unethical products or services, including but not limited to weapons and ammunitions, coal extraction, coal-fired power generation, tobacco, alcohol, and gambling; and

    (ii) included in the United Nations Security Council Consolidated List of sanctioned countries.[4]

27. Subject to availability of market issuance and the risk tolerance levels prescribed in section IV, IFAD endeavours to invest in green bonds and other thematic environmental, social and governance securities, including: supranationals; sovereign and government agency bonds; corporate bonds and asset-backed securities in the impact bond market.

F. Foreign currency management

28. IFAD aims to ensure that its assets are held in the same currency composition as its future commitments.

IV. Risk management of the investment portfolio

29. The President will ensure that risk tolerance levels are constantly monitored and reviewed by the relevant organizational unit. Through the report on IFAD’s investment portfolio, the Executive Board will receive updates on overall portfolio and individual investment portfolio risk levels, and will be informed of any adjustments to be made to align these with agreed risk levels.

[2] This restriction does not apply to call options embedded in fixed income instruments, e.g. callable bonds.
[3] https://www.unglobalcompact.org/what-is-gc/mission/principles.
[4] https://www.un.org/securitycouncil/content/un-sc-consolidated-list.

30. Any risk-mitigating measures taken will be reported to the Executive Board as part of the report on IFAD's investment portfolio.

A. Risk reporting

31. The President will ensure that analyses are performed and reports are prepared on the following financial risks emanating from the investment portfolio by the relevant organizational unit.

Market risk

32. Market risk is monitored for the overall portfolio and for single mandates based on measures provided on a monthly basis by the global custodian or by another external risk management company.

Credit risk

33. Credit risk relating to securities classified as eligible asset classes is managed through the establishment of a minimum rating floor in line with table 1 below and, in line with paragraph 35 below, a specified percentage of investments is allocated to higher-rated companies. The eligibility of individual securities and issuers is determined on the basis of ratings by major credit rating agencies. For investment management purposes, credit analyses by security and by issuer will be performed – for all internally managed investments and, on a selective basis, for externally managed assets, and for commercial and central banks – using financial information systems, credit analysis provider(s) and other sources. All other credit analysis will be performed and reported as an integral part of risk management.

34. The following table shows the rating floor for each eligible asset class. The rating that is compared to the rating floor is the second best rating of three agencies, Standard & Poor's (S&P), Moody's[5] or Fitch. This implies that the issuer, or the security, must be rated by a minimum of two out of the three agencies.

Table 1
Asset class rating floors

	Credit rating floors
Money market instruments	Single A-
Fixed-income securities: both nominal and inflation linked	
• Government and government agencies fixed-income securities at national or subnational level	Single A-
• Supranationals	Single A-
• Asset-backed securities (only agency-issued or guaranteed)	Triple A
• Covered bonds	Single A-
• Corporate bonds	Single A-
• Callable bonds	Single A-
Derivatives: for hedging purposes only	
• Currency forwards	Single A- counterparty rating
• Exchange-traded futures and options	
• Interest rate swaps	
• Cross currency swaps	
• Credit default swaps	
• Asset swaps	
Repurchase and reverse-repurchase transactions	Single A- counterparty rating

35. The share of fixed-income investments in rating category AA- and above should be at least 60 per cent.

Counterparty risk

[5] For Moody's ratings, the equivalent rating scale shall apply.

36. Counterparty risk arising from securities trading is managed through the establishment of a minimum rating for trading counterparties, as set out in paragraph 37 below. Counterparty risk will also be managed by capping exposure to each issuer or bank. Counterparty risk analyses are performed for the purpose of investment management using financial information systems, credit analysis providers and other sources. All other counterparty risk analysis will be performed and reported as an integral part of risk management.

37. Counterparties for trading purposes shall be rated at minimum investment grade by at least one of the following: S&P, Moody's or Fitch, and the Fund's exposure to any such counterparties will be capped on a case-by-case basis at an appropriate limit approved by the President.

38. Counterparties for operational cash and cash management purposes (including payments and short-term investments) may be rated non-investment grade by any of the following: S&P, Moody's or Fitch, provided that the Fund's exposure to any such counterparties is capped on a case-by-case basis at an appropriate limit approved by the President.

Country risk

39. Country risk is a collection of risks associated with investing in a particular country. These risks include political risk and sovereign risk. Country risk is managed for all investments through the establishment of maximum country exposure concentrations within the guidelines of every individual investment portfolio. Country exposures are monitored on a daily basis.

Currency risk

40. IFAD manages the currency risk that results from any mismatch between the currency composition of its assets and the currency composition of its future commitments through an interim cash flow-based approach.

41. The risk is managed by monitoring any mismatches and implementing a realignment strategy if any deviations become significant.

Interest rate risk

42. Interest rate risk is monitored on the overall investment portfolio and on the individual portfolios. Risk measurements include duration, value at risk and conditional value at risk.

Liquidity risk

43. Sufficient liquidity must be readily available to ensure IFAD's ability to meet its disbursement obligations.

Legal risk

44. The President will ensure that any legal risk is assessed by the Office of the General Counsel.

Operational risk

45. Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events. The President will ensure that operational risk is addressed by establishing a clearly defined framework of responsibility and accountability within IFAD's financial structure.

Integrity risk

46. IFAD's Anti-Money Laundering and Countering the Financing of Terrorism Policy seeks to reduce the risk of IFAD conducting business with counterparties that are on a sanctions list adopted by IFAD, or that have been involved in money laundering, financing terrorism or related activities. This risk is monitored to reduce IFAD's exposure to serious reputational damage, financial loss or legal liability.

47. The President will ensure the screening of all potential counterparties and the ongoing monitoring of existing counterparties.

B. Performance reporting

48. The overall portfolio and benchmark performance in local currency terms will be reported semi-annually to the Executive Board. The report will include comparative performance figures for the previous quarters and previous year.

C. Monitoring of compliance

49. The President will ensure that the relevant organizational unit monitors the external and internal investment managers' compliance with IFAD's investment guidelines on a daily basis. Should a compliance breach arise, it will be analysed and any necessary action taken.

V. Asset allocation and tranching of portfolio

50. As the investments are fully committed, management of investments and their risk tolerance need to be linked to, and guided by, IFAD's short-term liquidity needs.

51. The liquidity portfolio is subdivided into tranches. This helps guide the management of investments with respect to IFAD's paramount considerations of security and liquidity.

52. IFAD's liquidity portfolio is therefore split into tranches, as follows:

(i) **Transaction tranche**

Purpose. To facilitate near-term payments for IFAD's operations or administrative expenditures, to guarantee that enough cash and cash equivalents are available to meet immediate payment obligations.

Size. Based on projected funds needed immediately for IFAD's operations or administrative expenditures.

Investments. Cash balances and the most liquid instruments that count as cash equivalents

(ii) **Liquidity tranche**

Purpose. The liquidity tranche will replenish the transaction tranche as and when necessary and receives excess cash from the transaction tranche. It guarantees that enough instruments are available that can easily be translated into cash. Together with the transaction tranche it ensures that expected and unforeseen short-term liquidity requirements are met.

Size. Together with the transaction tranche, the liquidity tranche is targeted to hold, at a minimum, the projected gross outflows for three months and a buffer amount based on an assessment of the risk of unforeseen liquidity requirements. If the combined value of these tranches goes below the prescribed level, a plan will be prepared by the Treasury Services Division on when to transfer funds from the investment tranche in light of liquidity needs while taking into consideration market conditions and liquidation costs.

Investments. A combination of short-term and liquid assets. Foremost consideration will be given to capital preservation and the ability to liquidate in a timely manner.

(iii) **Investment tranche**

Purpose. Funds not needed in the short term and assumed to be disbursed over the medium term. This tranche allows IFAD to optimize prudently the total expected returns on its investments.

Size. The funds that remain in the liquidity portfolio after allocation to the transaction tranche and the liquidity tranche. The size of the investment tranche needs to be assessed as relatively stable to prevent liquidation and allow for an optimal strategic asset allocation.

Investments. All investments as allowed in the IPS.

53. Each tranche is allocated a specific component of the IPS's risk tolerance level and will be measured against respective benchmarks as per the investment portfolio guidelines.