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| Distribution: | Restricted | **EB 2000/69/R.3** | 19 April 2000 |
| Original: | English | **Agenda Item 3(b)(i)** | English |

**IFAD**

**INTERNATIONAL FUND FOR AGRICULTURAL DEVELOPMENT**

**Executive Board – Sixty-Ninth Session**

Rome, 3-4 May 2000

# REPORT ON IFAD'S INVESTMENT PORTFOLIO FOR 1999

## I. INTRODUCTION

1. The following report on IFAD's investment portfolio covers the year ending 31 December 1999 and includes comparative figures for the year ending 31 December 1998. In addition, Annex XXIII includes a report on the performance of the investment portfolio during the fourth quarter of 1999.

## II. HIGHLIGHTS

2. Investments in 1999 were influenced not only by strong economic growth in the United States and Europe and the beginning of a recovery in Japan, but also by fears of interest rate increases to curb inflation.

3. Economic conditions favoured equities investments. IFAD's equities portfolio achieved a rate of return of 49.71% in 1999, outperforming the benchmark by some 564 basis points.

4. Fixed-income investments, on the other hand, were affected by increases in interest rates and performed poorly. The rate of return for IFAD's fixed-income portfolio was –1.85%, reflecting an underperformance relative to the benchmark of 104 basis points.

5. In aggregate, net investment income amounted to USD 194 469 000 (excluding special items amounting to USD 2 044 000 described in paragraph 39), representing an average rate of return of 8.78% and an average outperformance over the benchmark of 64 basis points. This represents an increase in investment income and in the rate return of the portfolio over both 1997 and 1998 of 7.54% and 8.50%, respectively. It also means that, for the fourth year in succession since 1996, IFAD has exceeded its target of achieving an average real rate of return of 5% over three-year rolling periods.

6. The amount of the investment portfolio increased from USD 2 268 295 000 at the end of 1998 to USD 2 331 030 000 equivalent at the end of 1999, despite negative exchange movements of USD 53 924 000 that were mainly attributable to the strengthening of the United States Dollar against the Euro.

7. The diversification programme proceeded with the funding of mandates in the amount of USD 200 million and in the appointment of four external investment managers for global equities involving mandates amounting to USD 360 million, which will be funded in 2000.

## III. INVESTMENT CONDITIONS AND STRATEGY

8. This section reviews the economic and investment environment prevailing in 1999.

### A. Economic Background

#### Gross Domestic Product

9. Annex I shows percentage change in real gross domestic product (GDP) for the countries whose currencies are included in the Special Drawing Rights (SDR) valuation basket, namely, the Euro zone countries, Japan, the United Kingdom and the United States.

10. In 1998, the United States economy grew by 4.30% and growth remained strong in 1999 at an estimated rate of 4.0%, with strong consumer demand leading the way. There is as yet very limited evidence of a slowdown in the United States economy (forecast for 2000, 4%). Despite the interest rate increases in 1999, consumer confidence remains at historically very high levels, supported by strong labour markets and significant stock market gains.

11. In Japan, the economy contracted by 2.9% in 1998, but grew by an estimated 0.8% in 1999. Consumer and business confidence has rebounded to some extent, supported by the many government initiatives. The recovery is expected to continue in 2000 (forecast for 2000, 1.0%) despite weaker than expected data for the end of 1999. In order to ensure that economic improvement continues in 2000, the Government has announced another extensive fiscal programme.

12. In the Euro zone, the economy grew by 2.5% in 1998, but the economy slowed down to an estimated growth of 2.1% in 1999. Signs of an economic recovery in Europe grew during the second half of 1999 and are now increasingly recognized (growth forecast for 2000, 2.9%). The low real interest rates and the still weak currency should continue to support the broadening recovery. Business confidence has improved and rising employment should support growth in consumer spending.

13. In the United Kingdom, the economy grew by 2.2% in 1998 and by 2.9% in 1999 (forecast for 2000, 3.0%). Further acceleration in growth may be held back by the Bank of England’s recent series of interest rate increases to combat inflation risk, and by the strength of the Pound Sterling against the Euro. The United Kingdom does most of its trade with the 11 countries that have the Euro as their common currency.

14. In 1998, the global economy grew by 1.7% and the estimated growth rate for 1999 is around 2.6%. In Latin America, the economy grew by 2.1% in 1998 but fell to an estimated 0.1% in 1999. Asia’s emerging markets grew by 0.2% in 1998 and growth accelerated to an estimated 5.8% in 1999.

15. In 2000, regional contributions to global growth are expected to become more evenly balanced, with forecasts of stronger growth in Europe and the emerging markets. The global growth rate is expected to accelerate further (forecast for 2000, 3.3%), with Latin America’s economic growth expected to accelerate to 3.9% and Asia’s emerging economies forecast to accelerate to 6.3%.

## Inflation

16. Annex II shows the inflation figures for the countries whose currencies are included in the SDR valuation basket.

17. In 1999, the impact of rising oil prices was significant but core inflation rates, i.e. consumer prices apart from energy and food prices, generally remained subdued. In the United States, core inflation increased at its slowest rate in 34 years, despite the strong economic expansion and the very tight labour markets which continued to worry the Federal Reserve Bank. The inflation rate was helped by the increase in net imports and by import prices that were restrained due to weak demand outside the United States, caused by the slowdown in Asia and other developing markets. With demand now picking up, commodity prices are rising.

18. In Japan, there are as yet no clear inflationary concerns, due to downward price pressures from the large output gap and cheaper import prices because of the strongly strengthening Yen in 1999.

19. In the Euro zone, the inflation rate showed signs of accelerating owing to faster economic growth and raising import costs due to the Euro's decline and rising oil prices.

20. In the United Kingdom, low unemployment, rising wages and soaring house prices are driving consumer demand and may threaten to boost the inflation rate. The Pound Sterling's strengthening against the Euro has been holding inflation back.

21. After the downward trend in inflation rates in 1999 for Latin America and for Asia's emerging markets, inflation rates are expected to remain relatively stable in 2000.

## Labour-Market Development

22. Annex III shows unemployment rates as a percentage of the labour force for countries whose currencies are included in the SDR valuation basket.

23. In the United States, unemployment is almost at a 30-year low, while Japan's figures are at their highest level for the past 50 years. Unemployment has been gradually falling in the Euro area and in the United Kingdom, which is now registering its lowest unemployment levels in 20 years. In 2000, the unemployment situation is expected to remain relatively stable in the four regions.

## Monetary Policies

24. Annex IV shows the evolution of central bank and government-controlled interest rates for countries whose currencies are included in the SDR valuation basket.

25. The United States Federal Reserve Bank kept the overnight rate stable until June 1999, when it was raised by 25 basis points to 5% per annum to combat the risk of inflation. The interest rates were raised again in August and November by 25 basis points each time, bringing the interest rate to 5.5%. The risk of inflation continued to be affected by the very tight labour markets.

26. In Japan, the official discount rate remained unchanged at 0.5% per annum.

27. In the Euro zone, the official Euro overnight rate was cut in April from 3% per annum to 2.5% per annum. The rate was increased again in November to 3%.

28. The Bank of England cut interest rates in a series of cuts in the first half of the year, bringing the bank rate down from 6.25% to 5% in June. In September, the interest rate was unexpectedly raised by 25 basis points in order to ease the threat that surging house prices and the lowest unemployment level in two decades would boost inflation. The rate was further increased by 25 basis points to 5.5% in November.

### Exchange Rates

29. Annex V illustrates the end-of-the-month exchange rates for the United States Dollar against the four currencies in the SDR valuation basket.

30. A surprise in 1999 was the strength of the Japanese Yen and the weakness of the Euro. The Yen appreciated by 11% against the United States Dollar while the Euro depreciated by 15%. Capital inflows acted as a major support for the Yen. The rise in the stock market was largely supported by foreign buying.

31. The Euro's weakness arose from the negative impact of short-term interest differentials and the weaker economy relative to the United States. The Euro also suffered from capital outflows, which more than offset the current account surplus. The Pound Sterling depreciated by 3% against the United States Dollar during the year, but appreciated significantly against the Euro.

### Fiscal Policy

32. Annex VI shows budget deficits as a percentage of GDP for countries whose currencies are included in the SDR valuation basket.

33. In the United States, the budget surplus increased in 1999 and is estimated to remain around the same level in 2000. The Euro zone improved, showing a smaller deficit in 1999, which is expected to decrease further in 2000. In the United Kingdom, the balanced budget is forecast to continue. In Japan, however, the deficit increased significantly in 1999 and is forecast to remain at the same level in 2000.

## B. Financial Markets

34. Annex VII shows the evolution of short and long-term interest rates for the countries whose currencies are included in the SDR valuation basket. In the United States, the Euro zone and the United Kingdom, interest rates increased sharply in response to better-than-expected global growth and higher oil prices. In the United States the ten-year bond interest rate increased by more than 170 basis points; in the Euro zone, it increased by more than 140 basis points and in the United Kingdom by 110 basis points. Japan was the only major market with falling interest rates. The Japanese ten-year interest rate ended the year almost 50 basis points lower as credit quality fears of late-1998 were unwound, as the Bank of Japan maintained its low interest rate policy and as the Japanese Trust Fund Bureau continued to buy bonds.

35. Short-term interest rates generally fell during the first half year, but except for Japan they rose in the second half due to monetary tightenings and fears of future tightenings.

36. Annex VIII shows bond market returns for countries included in the J.P. Morgan Global Government Bond Traded Index. The benchmark index included both coupon and capital gains and losses, in line with market practice. The Japanese bond market was the only positively performing market; all other countries registered negative returns, as indicated by the development of bond yields.

37. Annex IX shows the performance of the J.P. Morgan Global Government Bond Traded Index (reweighted for currency matching purposes) in local currency terms compared with the Salomon Brothers Broad Investment Grade (BIG) Index. The latter includes United States Treasury bonds as well as mortgage, corporate and emerging market bonds denominated in United States Dollars, and is used as the benchmark for IFAD's diversified fixed-interest portfolio. The chart indicates that the Dollar-based diversified fixed-interest market outperformed the government bond index during the last months of 1999 due to significantly narrowing spreads of corporate bonds.

38. Annex X shows the development of the five equity markets in which IFAD has invested: Japan, Asia and Australasia (excluding Japan), emerging markets, North America and Europe. All markets performed very positively during the year and in particular during the fourth quarter. The performance in emerging markets and Japan, followed by Asia and Australasia, was particularly strong. The performance was in response to strong economic growth, despite some month-on-month negative returns during the year due to fears of monetary tightenings. In many markets, and particularly in the United States, the performance of growth-oriented and technology equities was very strong.

## IV. RATE OF RETURN AND INVESTMENT STRATEGY

### Overall Portfolio

39. According to IFAD's financial statements for 1999, investment income amounted to USD 196 513 000 equivalent. This amount includes income from Supplementary Funds relating to prior years amounting to USD 1 726 000 and net investment income of USD 318 000 from the Highly-Indebted Poor Countries Debt Initiative (HIPC-DI), which derives from investments in time deposits that are managed internally.

40. Excluding the special items amounting to USD 2 044 000 (1998 – NIL), net investment income in 1999 amounted to USD 194 469 000 equivalent (1998 – USD 187 899 000 equivalent). In line with market practice, capital gains and losses include both realized and unrealized gains and losses. All amounts are included on an accrual basis. Table 1 summarizes net investment income earned during the period under review, while further details of income are provided in Tables 5 and 9 for fixed-interest and equities investments, respectively.

**Table 1: Investment Income**
(USD '000 equivalent)

| | **1999 Fixed-Interest Portfolio** | **1999 Equity Portfolio** | **1999 Overall Portfolio** | **1998 Overall Portfolio** |
|---|---|---|---|---|
| Interest from fixed-interest investments and bank accounts | 89 333 | 920 | 90 253 | 112 668 |
| Dividend income from equities | 114 | 8 570 | 8 684 | 5 654 |
| Realized capital gains | (30 200) | 34 061 | 3 861 | 40 846 |
| Unrealized capital gains | (91 437) | 192 709 | 101 272 | 36 111 |
| **Subtotal: Gross investment income** | **(32 190)** | **236 260** | **204 070** | **195 279** |
| Securities lending income | 424 | 115 | 539 | 905 |
| Investment manager fees | (3 477) | (3 715) | (7 192) | (5 660) |
| Custody fees | (1 144) | (726) | (1 870) | (1 469) |
| Financial advisory and other investment management fees | (374) | (134) | (508) | (610) |
| Taxes | (5) | (281) | (286) | (129) |
| Other investment expenses | (265) | (19) | (284) | (417) |
| **Net investment income** | **(37 031)** | **231 500** | **194 469** | **187 899** |

41. Movements affecting the overall portfolio during 1999 are shown in Table 2. During the year, USD 214 540 000 equivalent was transferred in tranches from the fixed-interest portfolio to the equities portfolio. Further details of movements in cash and investments are provided in Tables 6 and 10 for fixed-interest and equity investments, respectively.

42. Annex XI includes a comparison of gross income for the major portions of the portfolio since the start of the diversification process in 1997, providing an analysis of realized and unrealized capital gains and losses. This indicates that, over a three-year period, capital gains for the fixed-interest portfolio have amounted to USD 32 907 000 while capital gains for the equities portfolio have amounted to USD 190 375 000, representing in aggregate some 39.2% of overall gross investment income for the period.

**Table 2: Movements in Cash and Investments – Year 1999**
(USD '000 equivalent)

| | Fixed-Interest Portfolio | Equities Portfolio | Overall Portfolio |
|---|---|---|---|
| Opening balance (31 December 1998) | 1 927 719 | 340 576 | 2 268 295 |
| Transfers between portfolios | (214 540) | 214 540 | - |
| Other net flows | (77 810) | - | (77 810) |
| Gross investment income | (32 190) | 236 260 | 204 070 |
| Securities lending income | 424 | 115 | 539 |
| Fees, charges and taxes | (5 265) | (4 875) | (10 140) |
| Movements on exchange | (62 434) | 8 510 | (53 924) |
| Closing balance (31 December 1999) | 1 535 904 | 795 126 | 2 331 030 |

43. After taking investment expenses into account, including fees for custody and investment management, the overall rate of return of the portfolio in 1999 was 8.78% (1998 – 8.50%), net of movements on exchange. Returns in 1999 were affected by weak performance in fixed-interest markets during the first three quarters of the year, but these were followed by positive performance in the fourth quarter. Equity markets contributed very positively during the year, except for a correction in the third quarter. Equity markets in general rallied in the fourth quarter.

44. The performance of the various mandates of the investment portfolio is measured against pre-assigned independent benchmarks indicating the return that may be expected through passive management of defined sectors of the market. Table 3 compares the return of each major section of the portfolio with the appropriate benchmark rate of return. Table 3 shows an overall outperformance of 66 basis points in 1999 (1998 – outperformance 153 basis points). This information is presented graphically in Annex XII, Chart 1.

**Table 3: Overall Performance Compared with Benchmarks –1999**

| | Rate of Return % | | Out/(Under) Performance |
|---|---|---|---|
| **Portfolio** | **Portfolio** | **Benchmark** | |
| Total fixed-interest | (1.85) | (0.81) | (1.04) |
| Total equities | 49.71 | 44.07 | 5.64 |
| Overall portfolio gross rate of return | 9.22 | 8.56 | 0.66 |
| Less expenses | (0.44) | (0.44) | 0.00 |
| Overall portfolio net rate of return | 8.78 | 8.12 | 0.66 |
| C.f. 1998 net rate of return | 8.50 | 6.97 | 1.53 |

45. The overall performance of the portfolio is also compared with IFAD's target of achieving an average real rate of return of five percent or more over three-year rolling periods. Table 4 shows the real rate of return of the portfolio from 1994 onwards, and indicates that the target has been met and exceeded in each of the last three-year rolling periods.

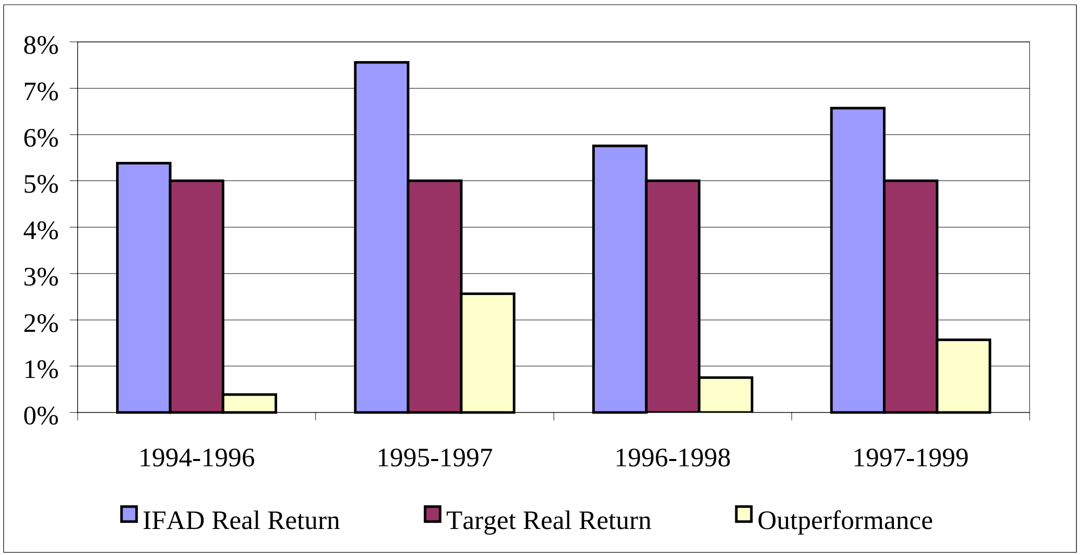
**Table 4: Real Returns on IFAD's Overall Portfolio**

| | IFAD Nominal Rate of Return | SDR Inflation Rate | IFAD Real Rate of Return | Average Three-Year Real Rate of Return |
|---|---|---|---|---|
| **1999** | 8.7% | 1.8% | 6.9% | 6.5% |
| **1998*** | 8.5% | 1.4% | 7.1% | 5.8% |
| **1997** | 7.5% | 2.0% | 5.5% | 7.6% |
| **1996** | 6.7% | 2.0% | 4.7% | 5.4% |
| **1995** | 14.6% | 1.9% | 12.7% | Na |
| **1994** | 1.3% | 2.1% | -0.8% | Na |

* 1998 inflation rates adjusted to final values. The average three-year real rate of return for 1998 remained at 5.8%.

46. A comparison between actual performance and the target is shown graphically in Figure 1.

**Figure 1: Average Three-Year Real Returns Compared to Target Returns**




**Fixed-Interest Portfolio**

47. The fixed-interest portfolio consists of three sub-portfolios: the internally-managed portfolio, the externally-managed global fixed-interest portfolio and the diversified fixed-interest portfolio.

48. In aggregate, the loss from fixed-interest investments in 1999 amounted to USD 37 031 000 equivalent, as shown in Table 5. The loss is attributable to the global fixed-interest portfolio as the internally-managed and the diversified fixed-interest portfolios performed positively.

**Table 5: Investment Income on Fixed-Interest Portfolio – Year 1999**
(USD '000 equivalent)

| | Internally-Managed Portfolio | Global Fixed-Interest Portfolio | Diversified Fixed-Interest Portfolio | Total Fixed-Interest Portfolio |
|---|---|---|---|---|
| Interest from fixed-interest investments and bank accounts | 3 354 | 73 830 | 12 149 | 89 333 |
| Dividend income from equities | - | - | 114 | 114 |
| Realized capital gains | - | (25 307) | (4 893) | (30 200) |
| Unrealized capital gains | - | (88 844) | (2 593) | (91 437) |
| **Subtotal: Gross investment income** | **3 354** | **(40 321)** | **4 777** | **(32 190)** |
| Securities lending income | 10 | 364 | 50 | 424 |
| Investment manager fees | - | (2 661) | (816) | (3 477) |
| Custody fees | (51) | (986) | (107) | (1 144) |
| Financial advisory and other investment management fees | (9) | (318) | (47) | (374) |
| Taxes | - | - | (5) | (5) |
| Other investment expenses | (190) | (55) | (20) | (265) |
| **Net investment income** | **3 114** | **(43 977)** | **3 832** | **(37 031)** |

49. Movements affecting the total fixed-interest portfolio in 1999 are shown in Table 6. A total of USD 226 340 000 was transferred in tranches from the global fixed-interest portfolio. Of that, USD 200 million was transferred to the equities portfolio to fund new mandates and USD 10 million to fund the currency overlay mandate as part of the diversification process. The balance of USD 16 340 000 was used to cover administrative expenses, loans and grant disbursements and the payment of investment management fees and other charges.

**Table 6: Movements in the Fixed-Interest Portfolio – Year 1999**
(USD '000 equivalent)

| | Internally Managed Portfolio | Global Fixed-Interest Portfolio | Diversified Fixed-Interest Portfolio | Total Fixed-Interest Portfolio |
|---|---|---|---|---|
| Opening balance (31 December 1998) | 135 126 | 1 585 752 | 206 841 | 1 927 719 |
| Transfers between portfolios | 10 879 | (226 340) | 921 | (214 540) |
| Other net flows | (77 810) | - | - | (77 810) |
| Gross investment income | 3 354 | (40 321) | 4 777 | (32 190) |
| Securities lending income | 10 | 364 | 50 | 424 |
| Fees, charges and taxes | (250) | (4 020) | (995) | (5 265) |
| Movements on exchange | (1 030) | (61 169) | (235) | (62 434) |
| Closing balance ( 31 December 1999) | 70 279 | 1 254 266 | 211 359 | 1 535 904 |

50. The performance of the fixed-interest portfolio by type of mandate is presented in Table 7. This information is presented graphically in Annex XIII, Chart 1.

**Table 7: Fixed-Interest Performance Compared With Benchmarks – Year 1999**

| | Rate of Return % | | Out/(Under) Performance |
|---|---|---|---|
| **Portfolio** | **Portfolio** | **Benchmark** | |
| Internally-managed portfolio | 4.21 | 3.67 | 0.54 |
| Global fixed-interest | (2.83) | (1.07) | (1.76) |
| Diversified fixed-interest | 2.30 | (0.90) | 3.20 |
| Total fixed-interest | (1.85) | (0.81) | (1.04) |
| Year 1998 total fixed-interest | 11.52 | 10.23 | 1.29 |

51. As indicated in Table 7, the overall return for the fixed-interest portfolio was -1.85%. This is compared to the aggregate benchmark return of -0.81%, resulting in an underperformance of 104 basis points for the total fixed-interest portfolio.

52. The global fixed-interest portfolio's underperformance of 176 basis points and the mandate's relative size caused the underperformance of the total fixed-interest portfolio. A performance attribution analysis for the global fixed-interest portfolio is shown in Annex XIV for the total year and by quarter. In summary:

- Some 80 basis points of underperformance were due to the managers' country allocation. The most significant impact arose from underweighting the Japanese bond market, which was by far the best performing market in 1999. This was due to capital inflows, especially from domestic investors.

- Another 80 basis points of underperformance was mainly due to bond selection and duration. On average the overall portfolio duration was slightly short compared to benchmark, as also indicated in Table 8. However, and especially at the beginning of the year, several managers maintained a long duration for United States Dollar bonds when yields were rising, which contributed negatively to performance. In the third quarter, despite further decreased overall duration, managers generally suffered from having a long duration in Euro denominated bonds, when bond yields were rising significantly due to signs of economic recovery and monetary tightening.

53. The diversified fixed-interest portfolio outperformed its benchmark by 320 basis points in 1999. A performance attribution analysis for the diversified fixed-interest portfolio is shown in Annex XV for the total year and by quarter. In summary:

- Some 50 basis points of the outperformance was due to the managers' sector allocation. The most significant impact arose from underweighting United States Treasury bonds against other sectors such as corporate and emerging market debt.

- Some 60 basis points of the outperformance came from bond selection, including impact from duration and credit quality. In the fourth quarter in particular, the managers benefited from significantly narrowing spreads on corporate and emerging market debt. Selection of mortgage-backed securities had a negative impact, especially towards the beginning of the year. On average, the portfolio's duration was slightly long, as indicated in Table 8.

- Some 160 basis points of the outperformance was due to cash holdings in periods of negative returns.

**Table 8: Duration of the Global Fixed-Interest and the Diversified Fixed-Interest Portfolio**

| | 31 December 1999 | 31 December 1998 |
|---|---|---|
| Global fixed-interest portfolio | 5.30 | 6.01 |
| Global fixed-interest benchmark | 5.84 | 5.89 |
| Diversified fixed-interest portfolio | 5.21 | 5.06 |
| Diversified fixed-interest benchmark | 5.09 | 4.56 |

## Equities Portfolio

54. The equities portfolio comprised six externally-managed sub-portfolios by the end of 1999. These were Japanese equities, Asian and Australasian equities, emerging markets equities, North American equities, European equities and a currency overlay mandate.

55. The aggregate net income attributable to the equities portfolio in 1999 amounted to a gain of USD 231 500 000 equivalent. The income by sub-portfolio is shown in Table 9.

**Table 9: Investment Income on Equities – Year 1999**
(USD '000 equivalent)

| | Japanese Equities | Asian and Australasian Equities | Emerging Markets Equities | Currency Overlay | North American Equities | European Equities | Total Equities |
|---|---|---|---|---|---|---|---|
| Interest from fixed-interest investments and bank accounts | - | 98 | 157 | 364 | 44 | 257 | 920 |
| Dividend income from equities | 824 | 2 080 | 2 600 | - | 1 891 | 1 175 | 8 570 |
| Realized capital gains | 7 058 | 13 591 | (4 218) | - | 19 201 | (1 571) | 34 061 |
| Unrealized capital gains | 63 192 | 26 209 | 44 053 | - | 28 229 | 31 026 | 192 709 |
| **Subtotal: Gross investment income** | **71 074** | **41 978** | **42 592** | **364** | **49 365** | **30 887** | **236 260** |
| Securities lending income | 26 | 21 | 22 | 1 | 31 | 14 | 115 |
| Investment manager fees | (626) | (595) | (1 250) | (25) | (911) | (308) | (3 715) |
| Custody fees | (79) | (121) | (379) | (4) | (95) | (48) | (726) |
| Financial advisory and other investment management fees | (29) | (23) | (24) | (3) | (36) | (19) | (134) |
| Taxes | - | (54) | (114) | - | (30) | (83) | (281) |
| Other investment expenses | (10) | (5) | 24 | (1) | (10) | (17) | (19) |
| **Net investment income** | **70 356** | **41 201** | **40 871** | **332** | **48 314** | **30 426** | **231 500** |

56. Movements affecting the equities portfolio in 1999 are shown in Table 10. During the year, a total amount of USD 210 million was transferred from the fixed-interest portfolio to fund North American equities mandates, Pan-European equities mandates and the currency overlay mandate.

**Table 10: Movements in the Equities Portfolio – Year 1999**
(USD '000 equivalent)

| | Japanese Equities | Asian and Australasian Equities | Emerging Markets Equities | Currency Overlay | North American Equities | European Equities | Total Equities |
|---|---|---|---|---|---|---|---|
| Opening balance(31 December 1998) | 95 156 | 76 541 | 77 844 | - | 91 035 | - | 340 576 |
| Transfers between portfolios | 718 | 727 | 1 639 | 10 032 | 81 025 | 120 399 | 214 540 |
| Gross investment income | 71 074 | 41 978 | 42 592 | 364 | 49 365 | 30 887 | 236 260 |
| Securities lending income | 26 | 21 | 22 | 1 | 31 | 14 | 115 |
| Fees, charges and taxes | (744) | (798) | (1 743) | (33) | (1 082) | (475) | (4 875) |
| Movements on exchange | 11 376 | 2 163 | 1 761 | (498) | - | (6 292) | 8 510 |
| Closing balance(31 December 1999) | 177 606 | 120 632 | 122 115 | 9 866 | 220 374 | 144 533 | 795 126 |

57. The performance of the equities portfolio by type of mandate is shown in Table 11. This information is presented graphically in Annex XVI, Chart 1.

**Table 11: Equities Performance Compared with Benchmarks – Year 1999**

| | Rate of Return % | | Out/(Under) Performance |
|---|---|---|---|
| **Portfolio** | **Portfolio** | **Benchmark** | |
| Equities Japan | 74.74 | 59.82 | 14.92 |
| Equities Asia and Australasia (excluding Japan) | 54.65 | 45.26 | 9.39 |
| Equities emerging markets | 55.41 | 68.50 | (13.09) |
| Equities North America (funded 1998-1999) | 34.51 | 21.43 | 13.08 |
| Equities Europe (funded Feb-Oct '99) | 24.22 | 27.19 | (2.97) |
| Total Equities | 49.71 | 44.07 | 5.64 |
| Year 1998 total equities | (7.05) | (10.03) | 2.98 |

58. As indicated in Table 11, at 49.71%, the overall return for the equity portfolio was very strong. This is compared to the aggregate benchmark return of 44.07%, resulting in an outperformance of 564 basis points for the total equities portfolio. The Japanese, Asian, Australasian and North American mandates outperformed their benchmarks significantly. The European equities and the emerging market portfolios underperformed. A performance attribution analysis for the different equity mandates is shown in Annex XVII by quarter. In summary:

- The Japanese equities mandate showed an outperformance in all quarters and benefited mainly from sector weighting. This was particularly clear in the fourth quarter, when the mandate benefited from its low exposure to the banking sector and successfully compensated its underweight position in software with an overweight position in electronic hardware.

- The Asian and Australasian mandate benefited clearly from stock selection in several countries, although the third quarter's exposure and selection in India was especially beneficial.

- The emerging markets mandate suffered from its country allocation, although this was partly offset by strong stock selection in several markets.

- The North American mandate benefited in particular from overweighting strongly performing technology sectors and from very strong stock selection within these sectors. During the year, the growth-oriented style clearly outperformed the value-oriented style. The growth-oriented style had a bigger percentage weight within the North American mandate.

- The European equities mandate underperformed despite strong performance in the fourth quarter, when the mandate benefited especially from exposure to the strongly outperforming Nordic countries and the telecommunications sector.

## Portfolio Performance Compared with Universe

59. Table 12 shows a comparison of the 1999 performance of IFAD's externally-managed mandates against a universe of investment managers provided by IFAD's financial advisors. The comparison uses returns in United States Dollars and includes an element of exchange gain and loss rather than local currency returns which are used elsewhere in this report. The comparison is also of an indicative nature, since all portfolios have their own specific investment guidelines, which do not match precisely the guidelines used by IFAD. As indicated in Table 12, two mandates of IFAD's investment portfolio showed a strong outperformance against both the universe as well as their own

benchmarks - the North American and Japanese equities mandates. Two mandates showed an underperformance against both the universe and their own benchmarks - the global fixed-interest portfolio and the emerging market equities.

**Table 12: Portfolio Performance Compared with Manager Universe for Year 1999**

| Type of Mandate | No. of Managers in Universe | Rate of Return % in USD terms[1] | | | | |
|---|---|---|---|---|---|---|
| | | Median Universe Performance | IFAD Investment Portfolio | IFAD Benchmark | IFAD Out/(Under) Performance against Universe | IFAD Out/(Under) Performance against Benchmark |
| Global fixed-interest | 70 | (4.66) | (6.57) | (4.54) | (1.91) | (2.03) |
| Diversified fixed-interest | 44 | 4.25 | 2.15 | (0.90) | (2.10) | 3.05 |
| Equities Japan | 26 | 74.61 | 86.65 | 76.08 | 12.04 | 10.57 |
| Equities Asia and Australasia (excluding Japan) | 20 | 74.57 | 57.61 | 49.67 | (16.96) | 7.94 |
| Equities emerging markets | 70 | 69.58 | 56.87 | 59.01 | (12.71) | (2.14) |
| Equities North America[2] | 800 | 19.81 | 34.51 | 21.43 | 14.70 | 13.08 |
| Equities Europe[3] | 35 | 22.72 | 22.55 | 19.66 | (0.17) | 2.89 |
| Aggregate[4] | 1066 | 10.18 | 9.17 | 8.33 | (1.01) | 0.84 |

1 The differences in returns for IFAD's investment portfolio and its benchmarks in this table and other tables in the report are due to movements on exchange rates.

2 IFAD's North American equities mandate was initially funded in 1998. Further tranches were funded in the second and third quarters of 1999.

3 IFAD's European equities mandate was initially funded in February 1999. Further tranches were funded in the third and fourth quarters of 1999.

4 Includes the internally-managed portfolio.

## V. COMPOSITION OF THE PORTFOLIO

### General

60. As of 31 December 1999, the Fund's investment portfolio amounted to USD 2 331 030 000 equivalent (31 December 1998 – USD 2 268 295 000 equivalent), excluding amounts subject to restriction provided by donors for participation in specific IFAD projects and activities. In 1999, prior to taking account of movements in exchange rates, the amount of the portfolio increased by USD 116 659 000 equivalent (1998 – USD 49 124 000 equivalent). An analysis of cash flows is given in Annex XVIII and summarized in Table 13.

**Table 13: Analysis of Cash Flows in the Overall Portfolio**
(USD '000 equivalent)

| | 12 Months to 31 December 1999 | 12 Months to 31 December 1998 |
|---|---|---|
| Opening balance 1 January | 2 268 295 | 2 150 730 |
| Net investment income | 194 469 | 187 899 |
| Other inflows | 278 064 | 245 638 |
| Outflows | (355 874) | (384 413) |
| Increase, prior to exchange movements | 116 659 | 49 124 |
| Exchange movements | (53 924) | 68 441 |
| Closing balance 31 December | 2 331 030 | 2 268 295 |

## Composition of the Portfolio by Instrument

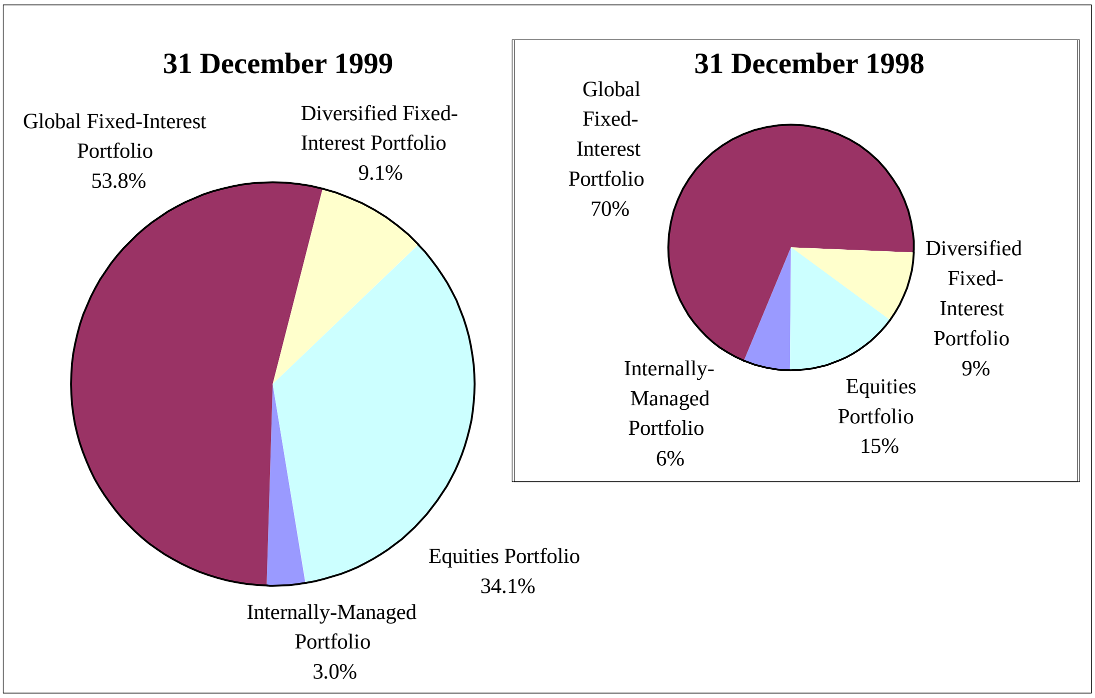
61. IFAD's portfolio is divided into fixed-interest and equities portfolios. Table 14 provides an analysis of the instruments found in each of the main sections of the investment portfolio, while a more detailed analysis of the fixed-interest portfolio is found in Annex XIX.

**Table 14: Analysis of the Portfolio by Type of Mandate and by Instrument at 31 December 1999**
(USD '000 equivalent)

| Instruments | Total Fixed-Interest Portfolio 31.12.1999 | Total Equities Portfolio 31.12.1999 | Overall Portfolio 31.12.1999 | Overall Portfolio 31.12.1998 |
|---|---|---|---|---|
| Cash | 67 849 | 4 040 | 71 889 | 60 848 |
| Time deposits | 153 278 | 18 590 | 171 868 | 201 442 |
| Treasury bills | - | - | - | 173 |
| Global government bonds | 1 171 821 | - | 1 171 821 | 1 545 332 |
| Emerging market bonds | 35 182 | - | 35 182 | 13 603 |
| Mortgage-backed securities | 60 760 | - | 60 760 | 90 440 |
| Asset-backed securities | 2 999 | - | 2 999 | 1 965 |
| Corporate bonds | 69 983 | 58 | 70 041 | 52 698 |
| Equities | - | 770 369 | 770 369 | 324 500 |
| Futures | 48 | - | 48 | 422 |
| Options | (30) | - | (30) | - |
| Open trades | (54 328) | 1 490 | (52 838) | (64 082) |
| Accrued interest income | 27 435 | 2 | 27 437 | 33 593 |
| Dividends receivable | - | 577 | 577 | 407 |
| Non-convertible currencies | 907 | - | 907 | 6 954 |
| **Total** | **1 535 904** | **795 126** | **2 331 030** | **2 268 295** |
| **Percentage** | **65.9%** | **34.1%** | **100.0%** | **100.0%** |

62. An analysis of the portfolio by type of mandate is found in Figure 2. The major change during the course of the year has been the increase in the equities portfolio from 15% of the overall portfolio as at 31 December 1998 to 34.1% at 31 December 1999. This increase has been due partly to transfers from the global fixed-interest portfolio as part of the diversification exercise, and partly to the high level of investment income earned on equities in 1999.

**Figure 2: Analysis of the Portfolio by Type of Mandate**




## Composition of the Portfolio by Currency

63. The majority of IFAD's commitments are expressed in SDRs. Consequently, IFAD's overall assets are maintained in such a way as to ensure that, to the extent possible, commitments for undisbursed loans and grants denominated in SDRs are matched by assets denominated in the currencies and in the ratios of the SDR valuation basket. Similarly, the general reserve and commitments for grants denominated in United States Dollar are matched by assets denominated in the same currency.

64. Every five years, the Executive Board of the International Monetary Fund (IMF) reviews the SDR valuation basket in order to determine which currencies should be part of the basket and which percentage weight should apply to each currency at the date of the reweighting of the basket.

65. The last such review was in September 1995 and weights were determined for each of the five component currencies which were applied to the reweighting of the valuation basket on 1 January 1996. The units of each currency which constitute the basket for the five-year period 1 January 1996-31 December 2000 were determined on the basis of the agreed weights and market exchange rates as at 31 December 1995.

66. With its introduction on 1 January 1999, the Euro has been included in the valuation basket as the currency of both France and Germany. The new units applicable, together with their weights as at 1 January 1999 and 31 December 1999, are shown in Table 15.

### Table 15: Units and Weights Applicable to the SDR Valuation Basket

| | 1 January 1999 | | 31 December 1999 | |
|---|---|---|---|---|
| **Currency** | **Units** | **Percentage Weight** | **Units** | **Percentage Weight** |
| USD | 0.5821 | 41.5 | 0.5821 | 42.4 |
| EUR | 0.3519 | 29.3 | 0.3519 | 25.8 |
| JPY | 27.200 | 16.8 | 27.200 | 19.4 |
| GBP | 0.105 | 12.4 | 0.105 | 12.4 |
| | | **100.0** | | **100.0** |

67. During the course of 2000, IMF will discuss the various options for the future of the valuation basket, which include the possibility of a tri-polar SDR comprising the Euro, the Japanese Yen and the United States Dollar, or a larger basket of currencies.

68. As at 31 December 1999, assets in the form of cash, investments, promissory notes and amounts receivable from contributors under the Fourth Replenishment amounted to USD 2 821 336 000 equivalent (31 December 1998 – USD 2 889 006 000 equivalent). An analysis showing the cash and investments, promissory notes and amounts receivable from contributors in currency terms may be found in Annex XX.

69. Holdings of assets denominated in currencies not included in the SDR valuation basket amounted to USD 449 154 000 at 31 December 1999 (1998 – USD 373 392 000). These are allocated to currency groups, as indicated in Table 16.

### Table 16: Allocation of Assets to Currency Groups
(USD '000 equivalent)

| Currency Group | Currencies Included in SDR Basket | Currencies Subject to Overlay Arrangements | European Currencies Not Included in the SDR Valuation Basket | Other Currencies Not Included in the SDR Valuation Basket | Non-Convertible Currencies | Total Currencies Per Group |
|---|---|---|---|---|---|---|
| USD | 971 793 | 121 674 | - | 157 837 | 2 535 | 1 253 839 |
| EUR | 591 878 | - | 167 108 | - | - | 758 986 |
| JPY | 473 716 | - | - | - | - | 473 716 |
| GBP | 334 795 | - | - | - | - | 334 795 |
| | 2 372 182 | 121 674 | 167 108 | 157 837 | 2 535 | 2 821 336 |

70. The alignment of the assets by currency group against the SDR valuation basket at 31 December 1999 is shown in Table 17. The balance of the General Reserve at 31 December 1999 and commitment for grants denominated in United States Dollars at 31 December 1999 amounted to USD 95 000 000 and USD 60 551 000, respectively.

**Table 17: Alignment of Assets Per Currency Group with the Currency Composition of the SDR Valuation Basket at 31 December 1999**
(USD '000 equivalent)

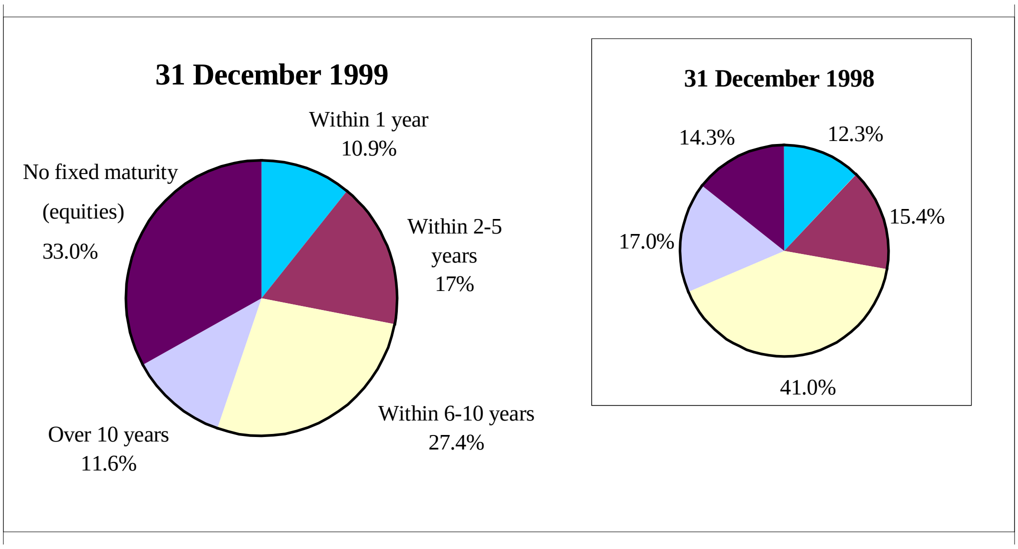
| Currency Group | Amount per Currency Group | Less: Commitments Denominated in USD | Net Assets per Currency Group | Net Assets % | Compare SDR Weights % |
|---|---|---|---|---|---|
| USD | 1 253 839 | (155 551) | 1 098 288 | 41.2 | 42.4 |
| EUR | 758 986 | - | 758 986 | 28.5 | 25.8 |
| JPY | 473 716 | - | 473 716 | 17.8 | 19.4 |
| GBP | 334 775 | - | 334 795 | 12.5 | 12.4 |
| | 2 821 336 | (155 551) | 2 665 785 | 100.0 | 100.0 |

71. As at 31 December 1999, there were shortfalls in currency group holdings of United States Dollars and Japanese Yen, and currency group excess holdings of Euros and Pounds Sterling. The shortfall in holdings of Japanese Yen reflects the aggregate, unhedged, underweight position for bonds denominated in Japanese Yen held in the global government bonds portfolio.

## Maturity of Investments

72. Annex XXI provides details of the composition of the portfolio by maturity as of 31 December 1999, while Figure 3 shows the maturity of the portfolio graphically.

**Figure 3: Maturity Structure of the Investment Portfolio**



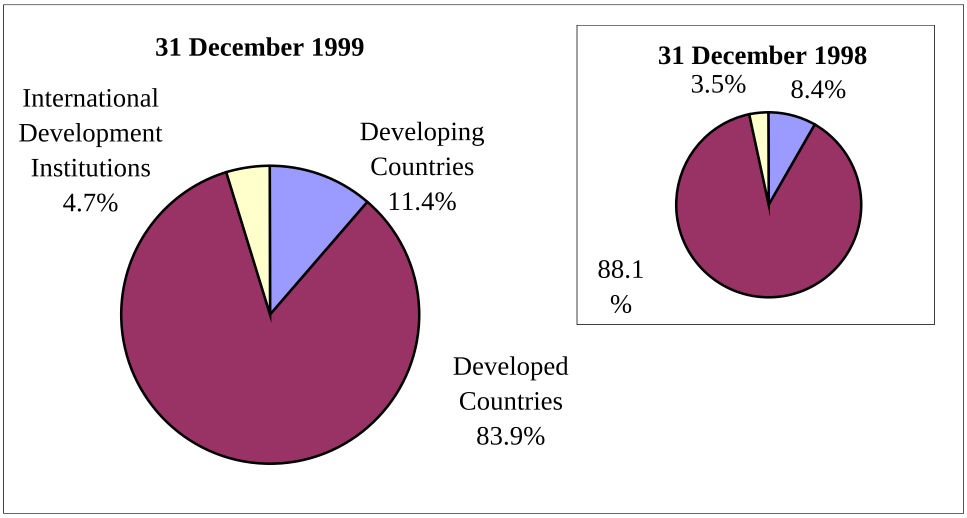

73. The average life to maturity at 31 December 1999 was nine years (31 December 1998 – eight years and three months).

## Diversification by Country

74. It is IFAD's practice to diversify its investments with respect to countries. IFAD invests in suitable instruments issued by eligible institutions in both developed and developing Member States, and in obligations issued by eligible development-related intergovernmental institutions. Annex XXII provides details by type of instrument and by region in the case of developing countries, while Figure 4 shows the overall diversification by Member States graphically. The percentage of

investments in developing countries and international development institutions at 31 December 1999 shows an increase compared to the previous year, due largely to capital gains resulting from investments in emerging markets bonds and equities markets.

**Figure 4: Diversification by Country**




## VI. DIVERSIFICATION OF THE PORTFOLIO

75. The diversification programme involves a gradual shift in the composition of IFAD’s investment portfolio from such fixed-interest investments as global government bonds and time deposits into a wider range of fixed income assets such as corporate bonds and mortgage-backed securities, and into equities.

76. The programme was commenced in 1997, with the target of moving some USD 200 million into diversified fixed-income mandates and some USD 1000 million into equities mandates. By the beginning of 1999, the external investment managers for the diversified fixed-income mandates had been identified and appointed, and the mandates had been fully funded. With regard to equities mandates, by the same time, external investment managers had been appointed for mandates amounting to USD 580 million, of which some USD 360 million had been funded.

77. During the course of 1999, a further USD 200 million was transferred from the global government bond portfolio to equities mandates, of which USD 80 million was for North American equities mandates and USD 120 million for Pan-European equities mandates.

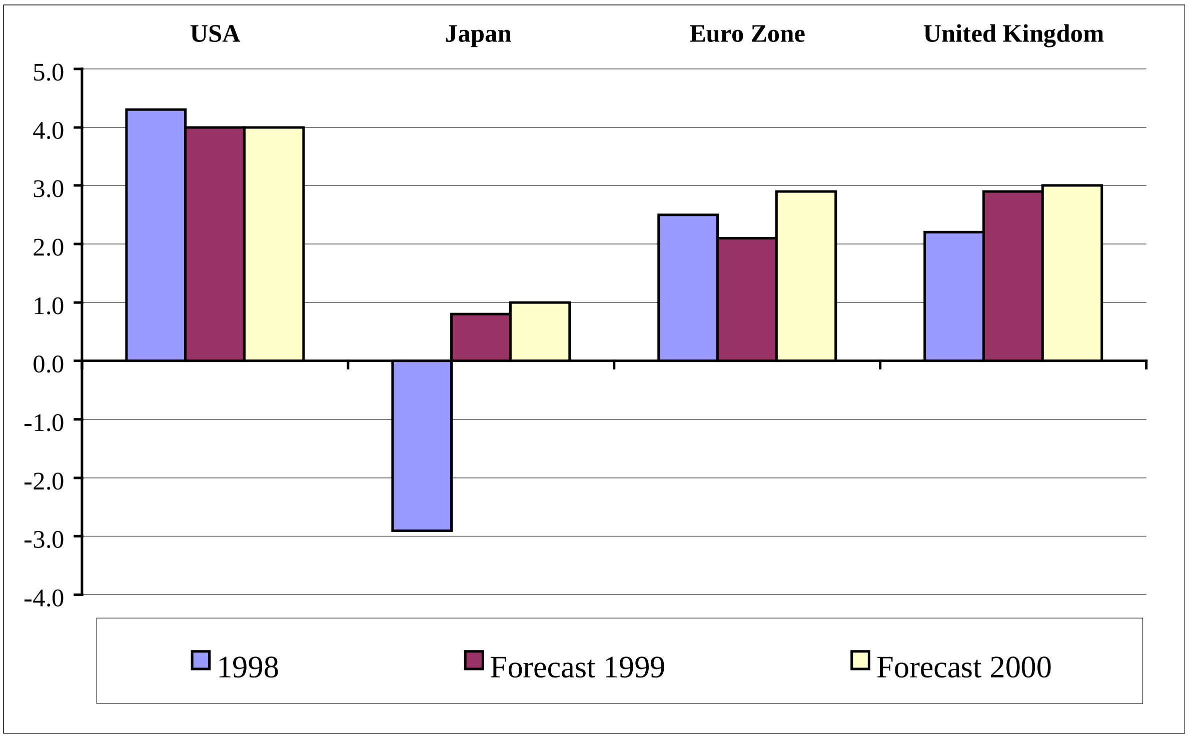
78. The selection process for external investment managers for the global equities mandates was completed in July 1999. Four managers were selected to manage an aggregate amount of USD 360 million.

79. Thus, of the amount of USD 1 000 million originally allocated for investments in the equities markets, by the end of 1999, external investment managers had been appointed for mandates amounting to USD 940 million, of which some USD 560 million had been funded, leaving a balance of USD 380 million to be funded in 2000.

80. In addition, a currency overlay mandate was funded in April 1999 to cover IFAD’s exposure to currencies resulting from the equities mandate for Asia and Australasia (excluding Japan) and for the emerging markets equities mandate.

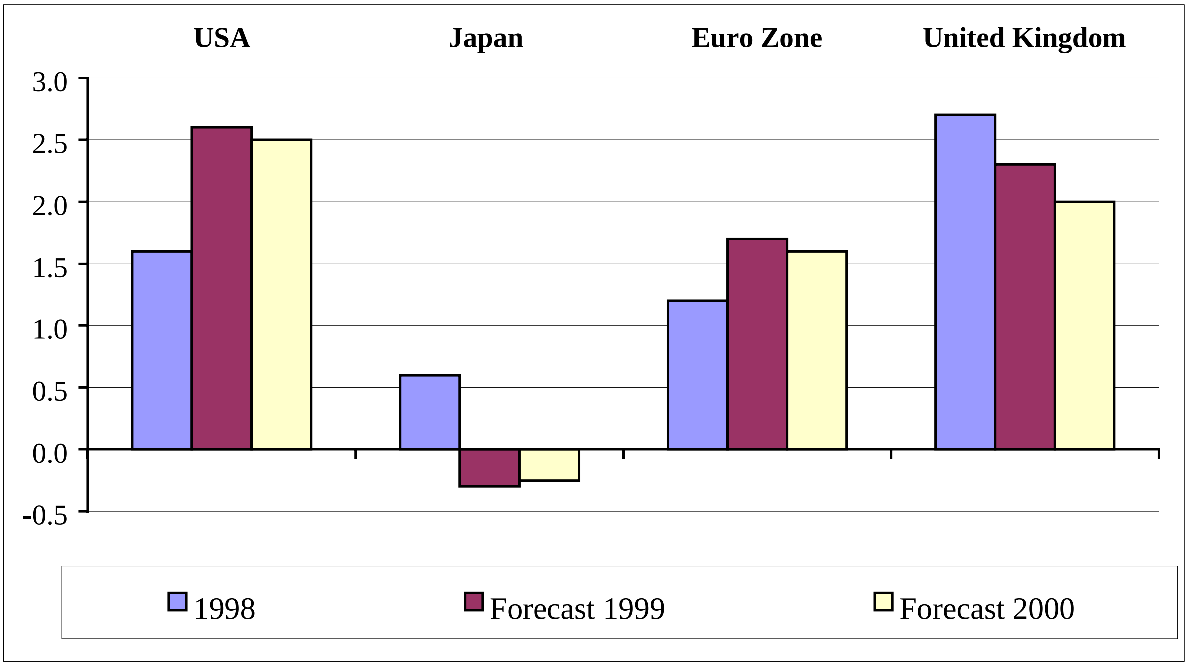
81. Work also started in 1999 on identifying an external investment manager for a Pan-European small and medium capitalization equities mandate amounting to USD 60 million. It is expected that the manager will be appointed and funded during the course of 2000.

## Annual Percentage Change in Real GDP



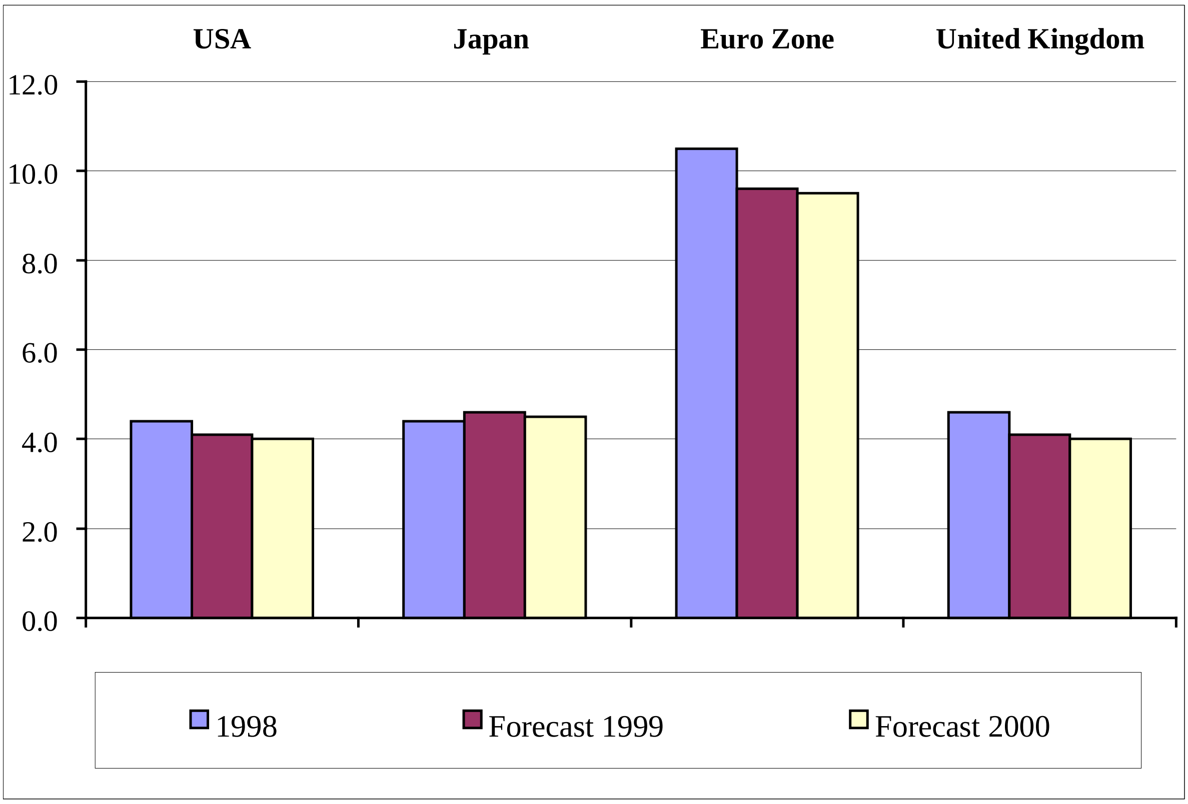

Source: Bloomberg, JP Morgan

**Consumer Price Index – Annualized Rates**




Source: Bloomberg, JP Morgan

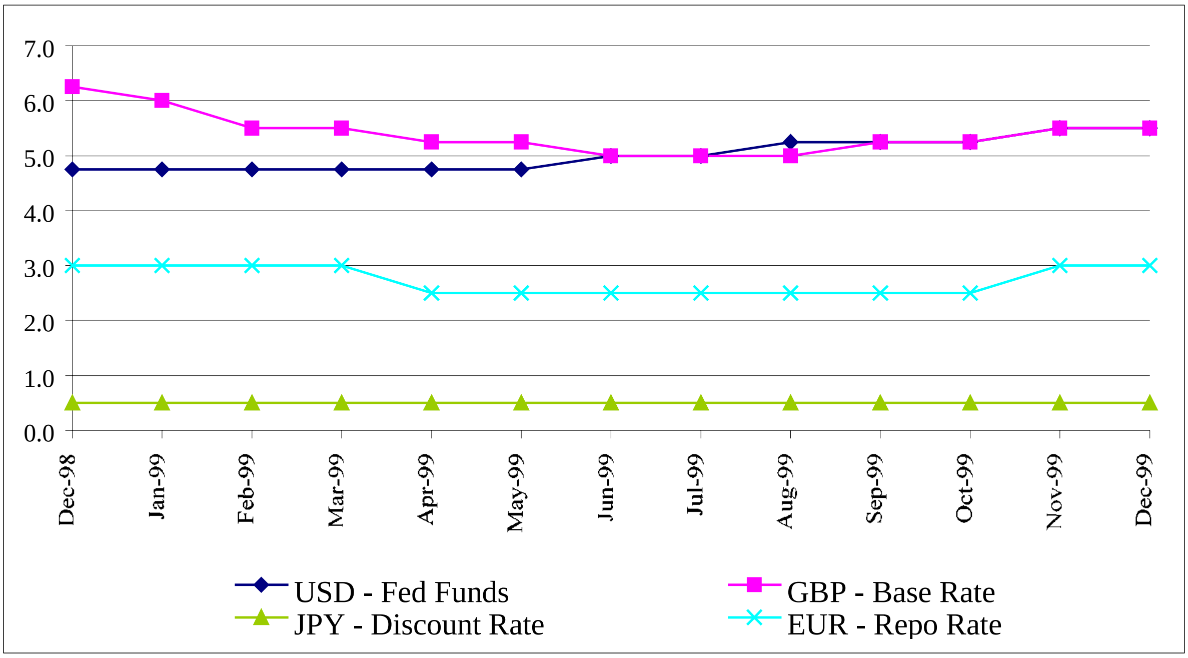
## Unemployment Rate – Percentage of Labour Force




Source: Bloomberg, JP Morgan

## Central Bank and Government-Controlled Interest Rates

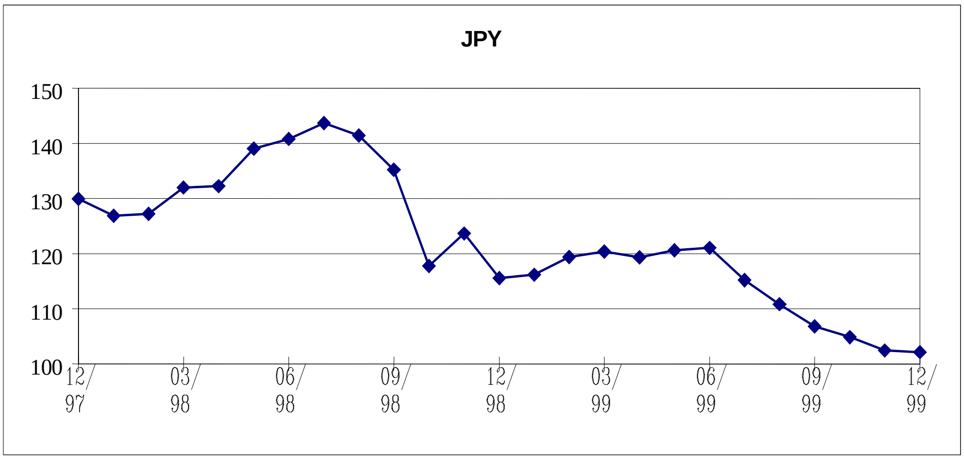
### USD - JPY - GBP - EURO

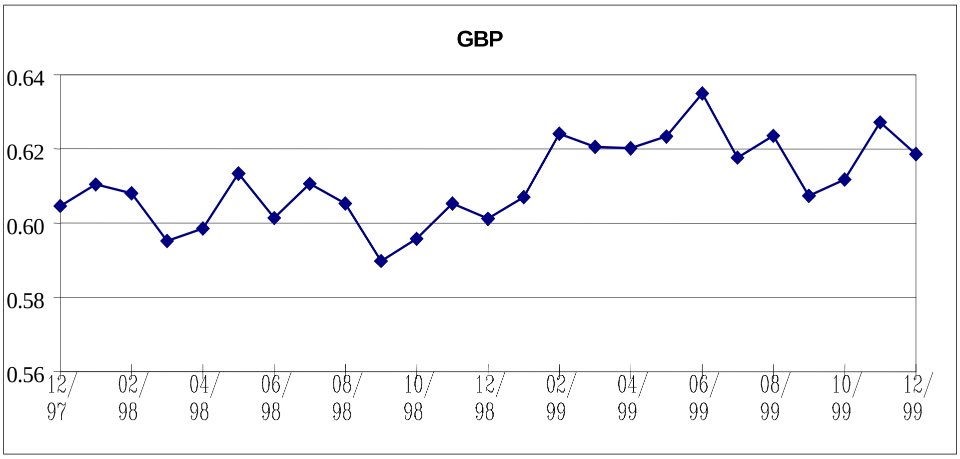


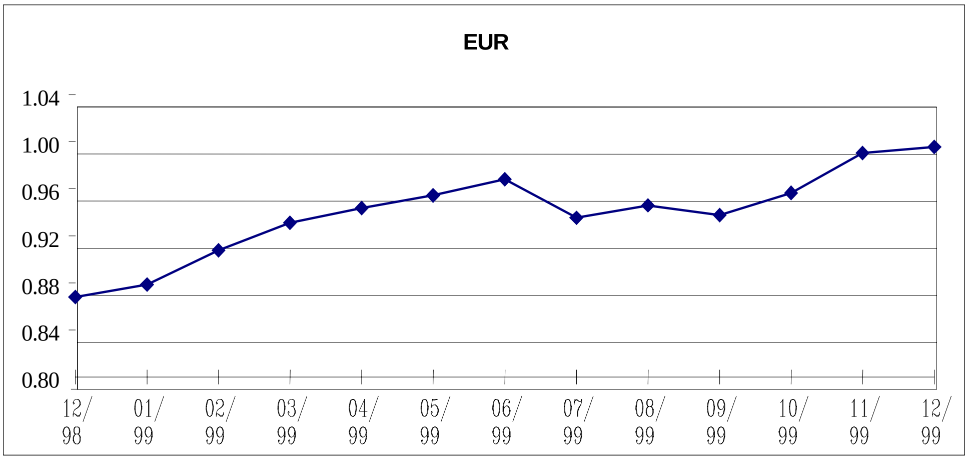

Source: Bloomberg

ANNEX V

## Value of the United States Dollar at IMF Month-End Exchange Rates

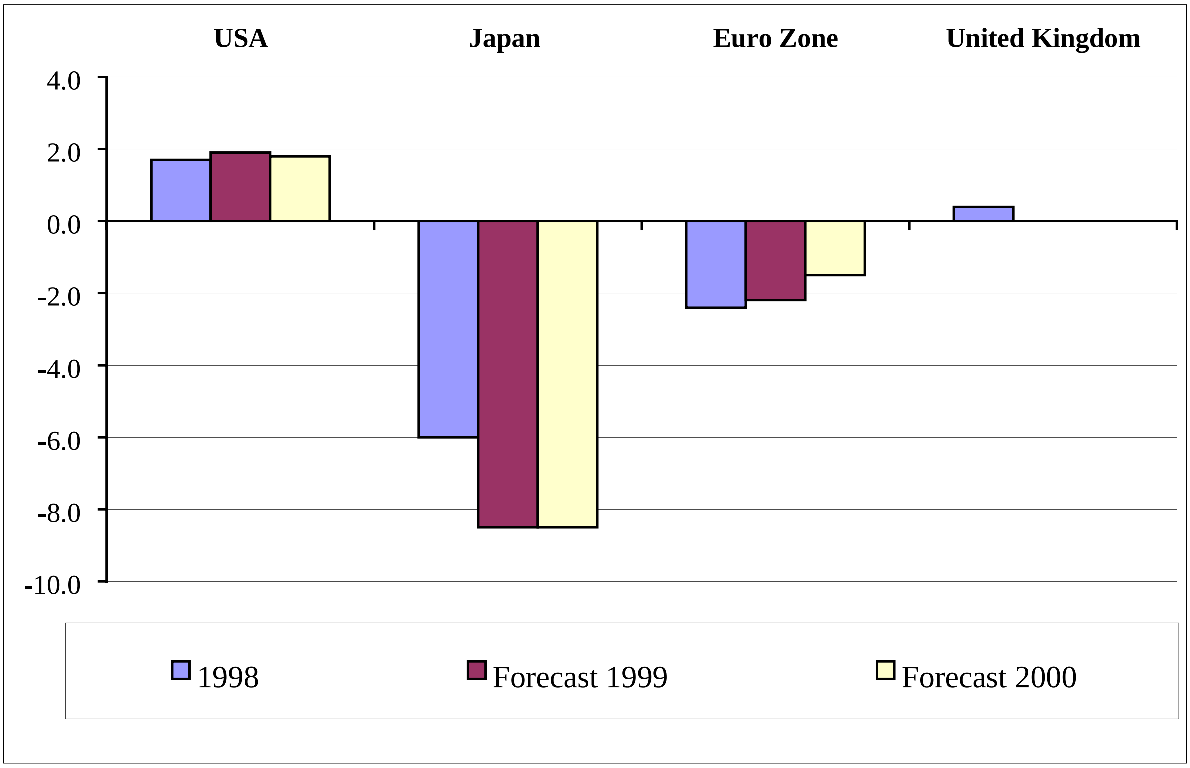



Source: IMF

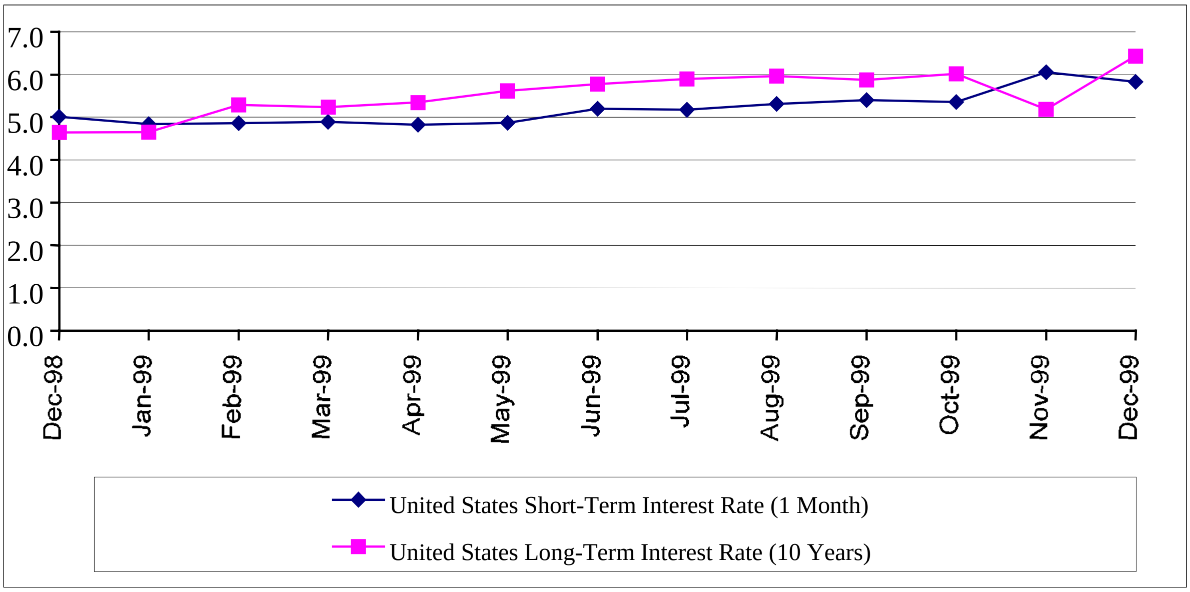
## Budget Deficits – Percentages of GDP



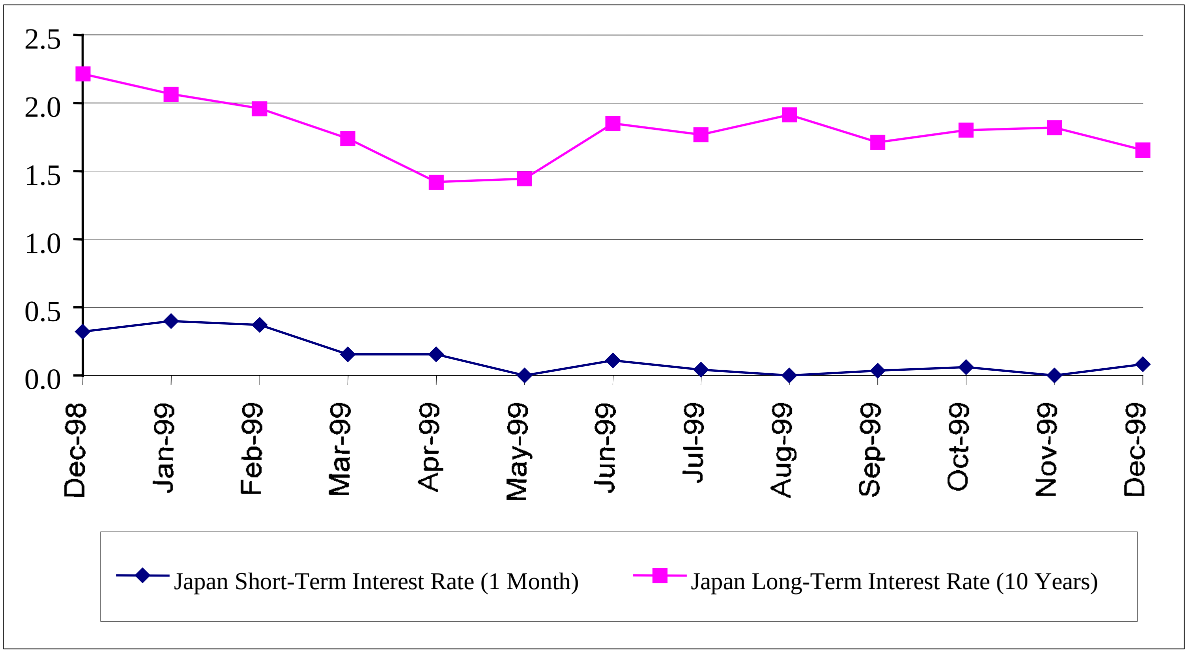

Source: Bloomberg, JP Morgan

## Short and Long-Term Interest Rates

**United States**



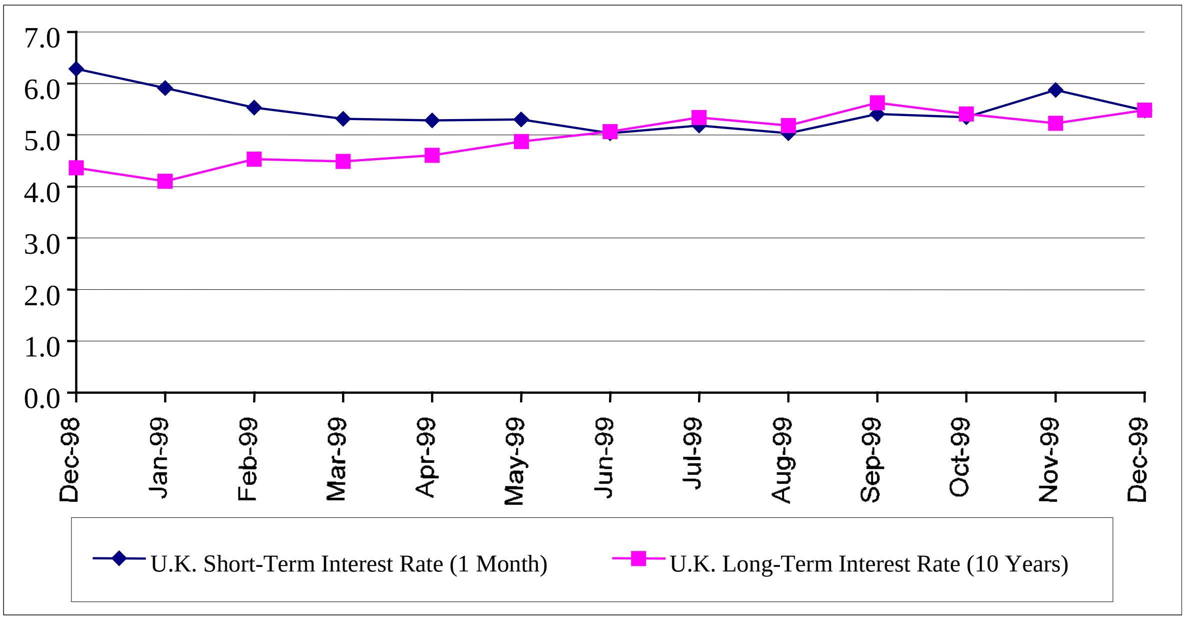

**Japan**



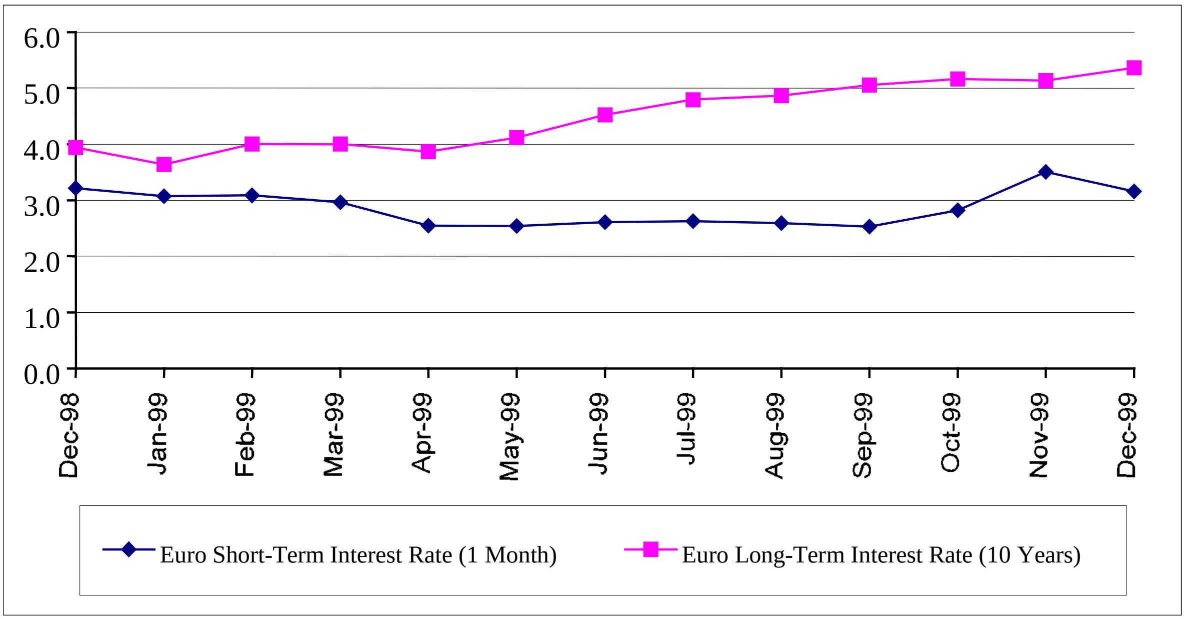

Source: Bloomberg

## Short and Long-Term Interest Rates

### United Kingdom




### Euro Zone




Source: Bloomberg

ANNEX VIII

## Government Bond Returns per Country Included in the J.P. Morgan Government Bond Traded Index

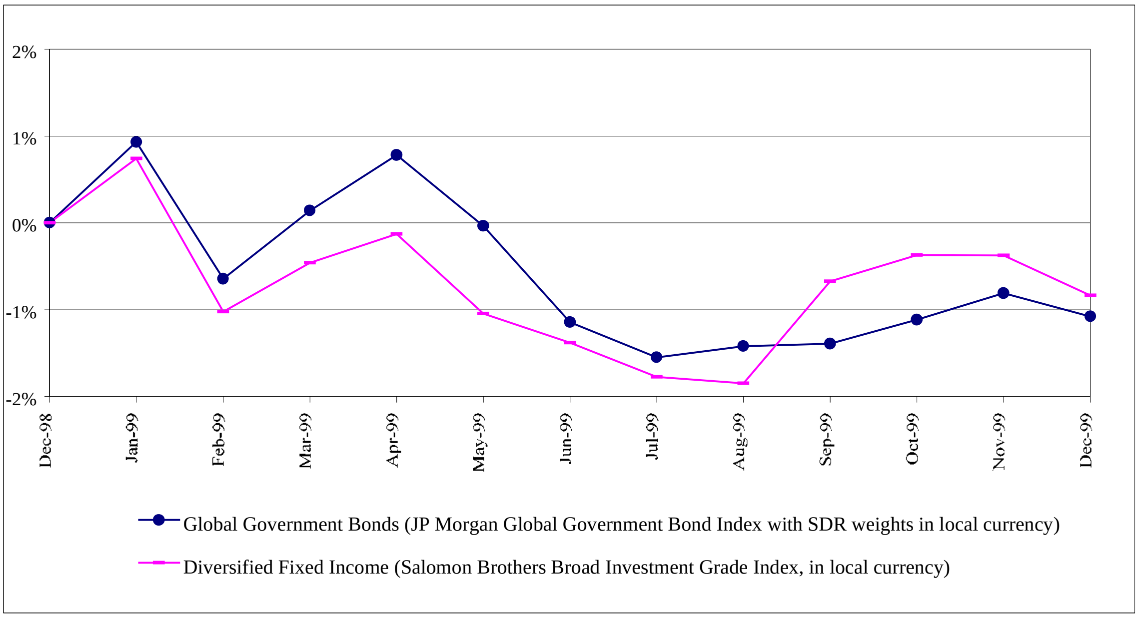
(Percentage in Local Currency Terms)

| Country | 1st quarter 1999 | 2nd quarter 1999 | 3rd quarter 1999 | 4th quarter 1999 | 1999 | 1998 |
|---|---|---|---|---|---|---|
| Australia | -0.48 | -1.89 | 1.49 | -1.55 | -2.45 | 10.29 |
| Belgium | 0.67 | -1.53 | -1.61 | -0.03 | -2.51 | 11.99 |
| Canada | 0.47 | -0.89 | 0.07 | -1.09 | -1.44 | 9.58 |
| Denmark | 1.51 | -1.25 | -1.58 | 0.64 | -0.71 | 10.86 |
| Euro zone | 0.55 | -1.52 | -1.48 | -0.15 | -2.58 | NA |
| France | 0.41 | -1.68 | -1.51 | -0.23 | -2.98 | 12.58 |
| Germany | 0.66 | -1.34 | -1.27 | -0.22 | -2.17 | 11.40 |
| Italy | 0.43 | -1.60 | -1.44 | -0.16 | -2.75 | 12.71 |
| Japan | 3.43 | -0.82 | 1.98 | 0.38 | 5.01 | 0.55 |
| Netherlands | 0.65 | -1.53 | -1.62 | -0.09 | -2.58 | 11.79 |
| Spain | 0.29 | -1.48 | -1.63 | -0.06 | -2.87 | 12.61 |
| Sweden | 1.02 | -2.86 | -2.17 | 1.37 | -2.68 | 14.13 |
| United Kingdom | -0.20 | -1.74 | -1.72 | 2.39 | -1.33 | 19.79 |
| United States | -1.78 | -1.00 | 0.66 | -0.77 | -2.88 | 10.25 |
| **GLOBAL** | **0.20** | **-1.25** | **-0.10** | **-0.05** | **-1.20** | **10.06** |

Source: JP Morgan

## Fixed-Income Market Development in 1999

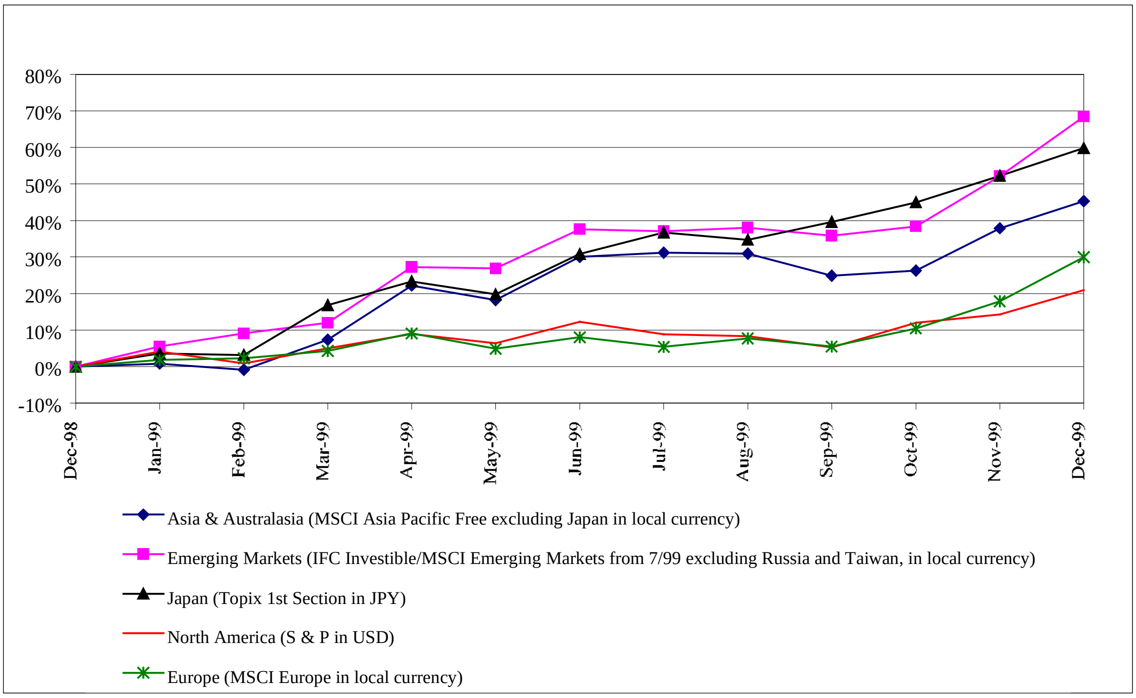
(Monthly data)




Source: State Street Analytics

## Equity Market Development in 1999

(Monthly data)




Source: State Street Analytics

# Gross Income 1997-1999

## OVERALL PORTFOLIO

| | 1999 | 1998 | 1997 | Total 3 Years |
|---|---|---|---|---|
| Realized capital gains/losses | 3 861 | 40 846 | 21 535 | 122 010 |
| Unrealized capital gains/losses | 101 272 | 36 111 | 19 657 | 101 272 |
| Total capital gains | 105 133 | 76 957 | 41 192 | 223 282 |
| Interest income | 90 253 | 112 668 | 128 779 | 331 700 |
| Dividends | 8 684 | 5 654 | 94 | 14 432 |
| **Total Gross Income** | **204 070** | **195 279** | **170 065** | **569 414** |

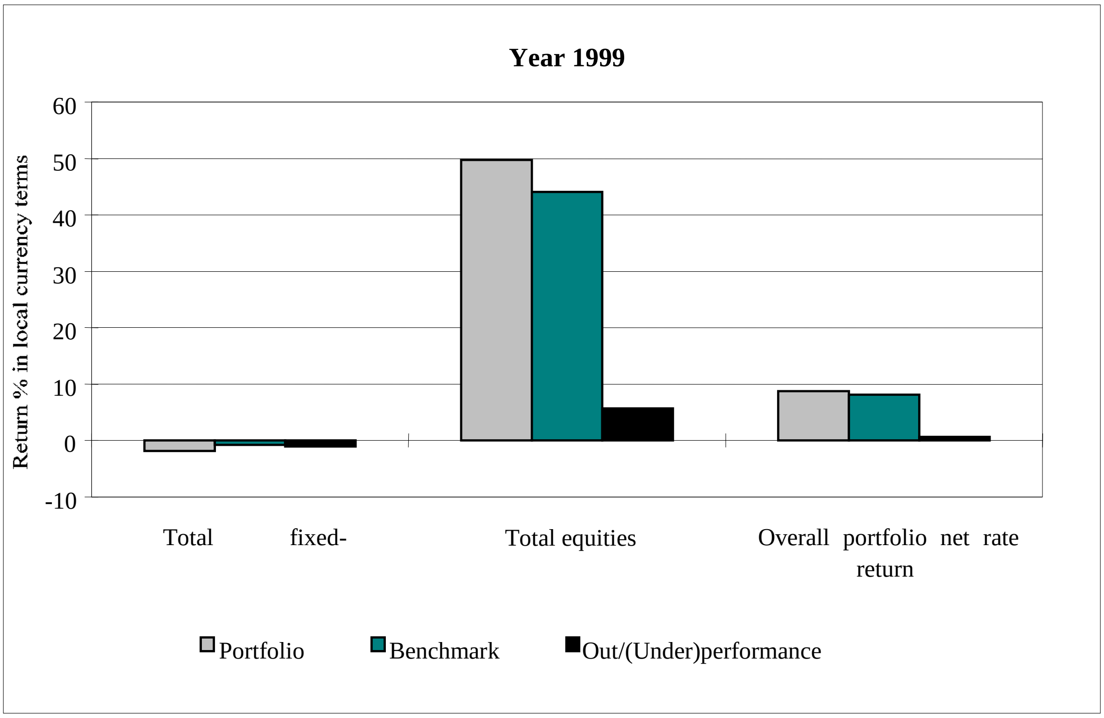
## FIXED-INTEREST PORTFOLIO

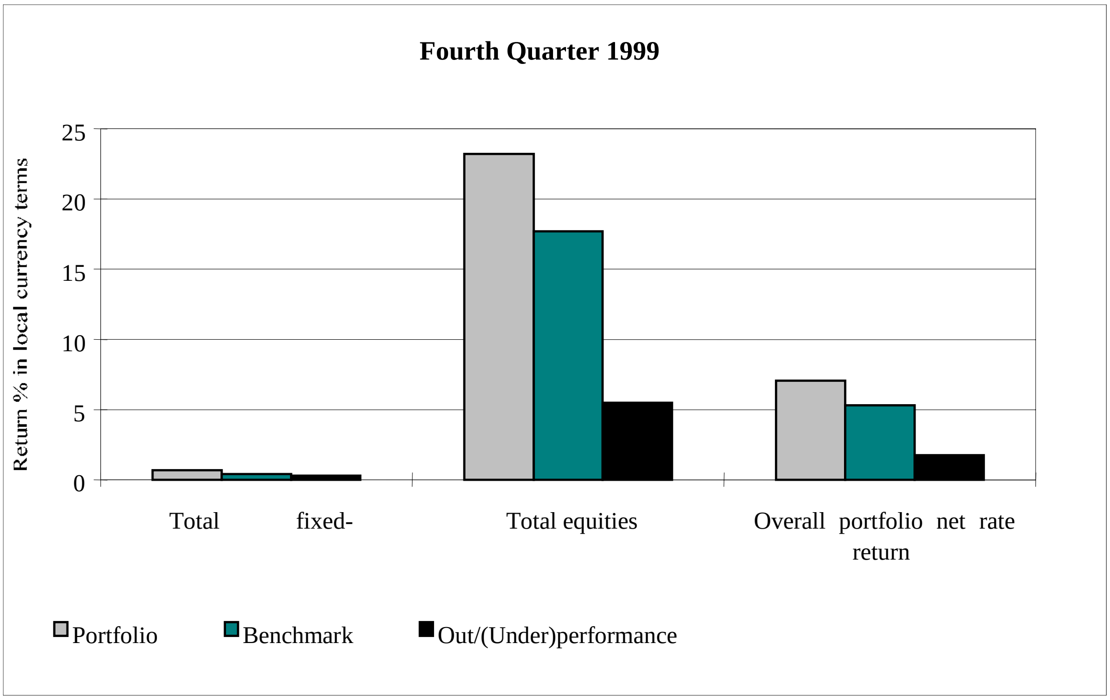
| | 1999 | 1998 | 1997 | Total 3 Years |
|---|---|---|---|---|
| Realized capital gains/losses | (30 200) | 55 708 | 21 493 | 124 344 |
| Unrealized capital gains/losses | (91 437) | 48 521 | 28 822 | (91 437) |
| Total capital gains | (121 637) | 104 229 | 50 315 | 32 907 |
| Interest income | 89 333 | 108 773 | 128 779 | 326 885 |
| Dividends | 114 | - | - | 114 |
| **Total Gross Income** | **(32 190)** | **213 002** | **179 094** | **359 906** |

## EQUITIES PORTFOLIO

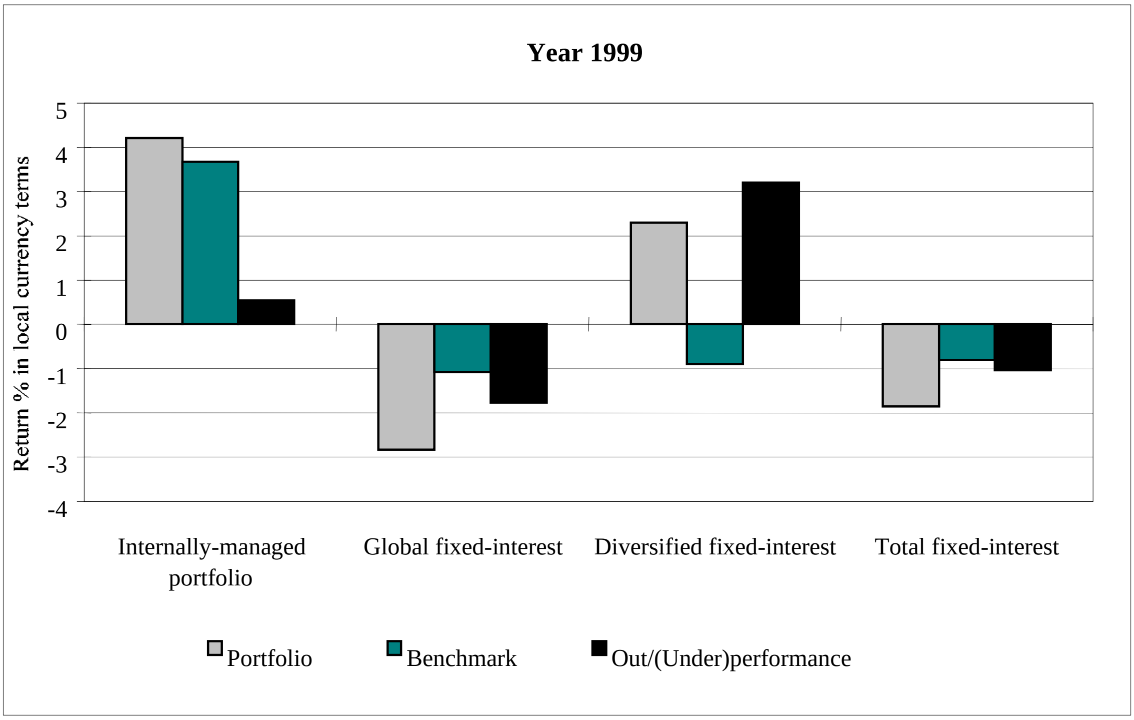
| | 1999 | 1998 | 1997 | Total 3 Years |
|---|---|---|---|---|
| Realized capital gains/losses | 34 061 | (14 862) | 42 | (2 334) |
| Unrealized capital gains/losses | 192 709 | (12 410) | (9 165) | 192 709 |
| Total capital gains | 226 770 | (27 272) | (9 123) | 190 375 |
| Interest income | 920 | 3 895 | 0 | 4 815 |
| Dividends | 8 570 | 5 654 | 94 | 14 318 |
| **Total Gross Income** | **236 260** | **(17 723)** | **(9 029)** | **209 508** |

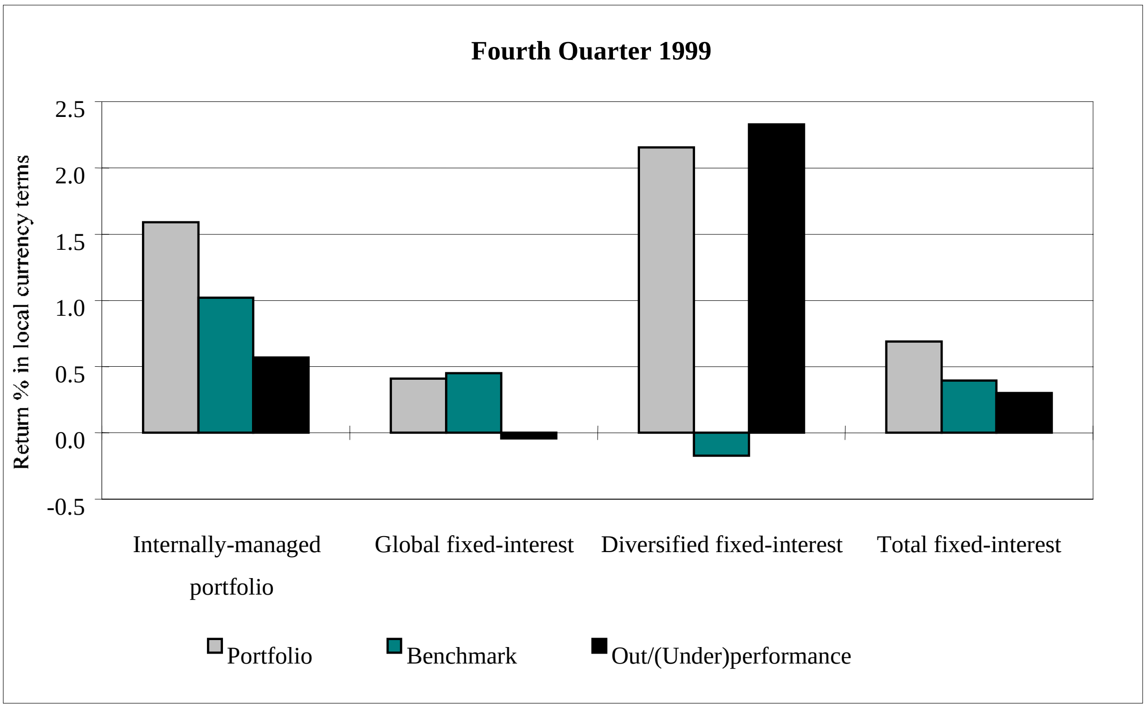
## Performance – Overall Portfolio



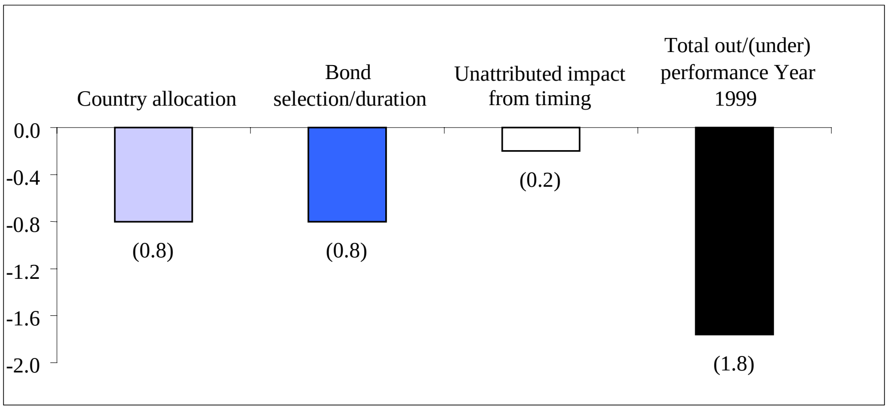
# Performance – Fixed-Interest Portfolio



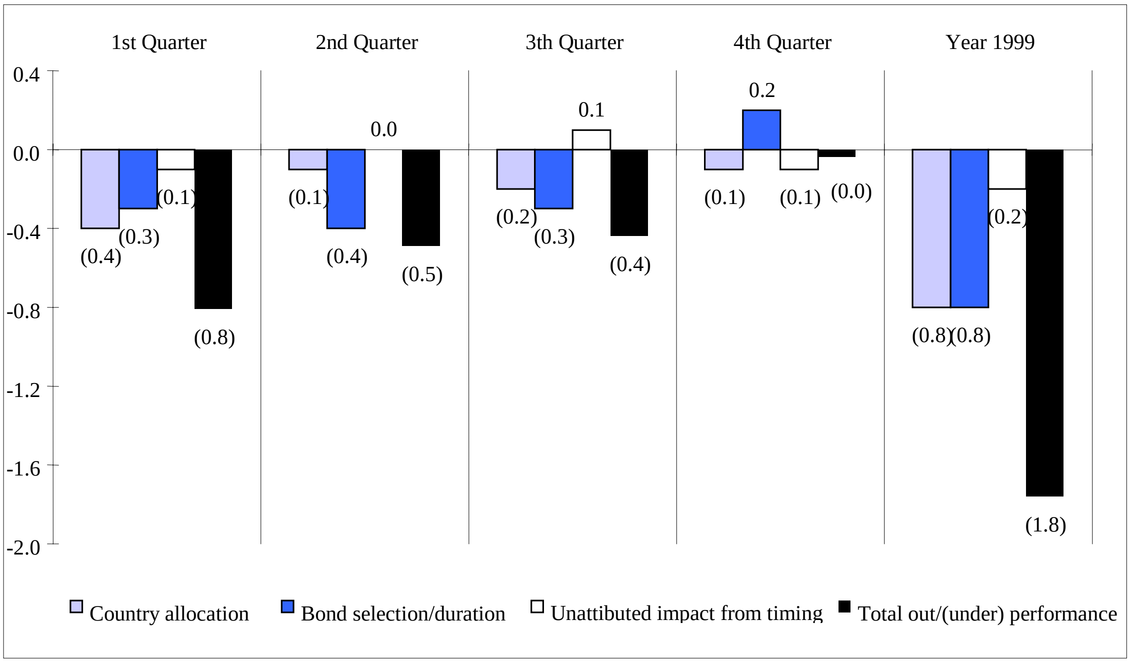



# Performance Attribution for the Global Fixed-Interest Portfolio

**Year 1999**

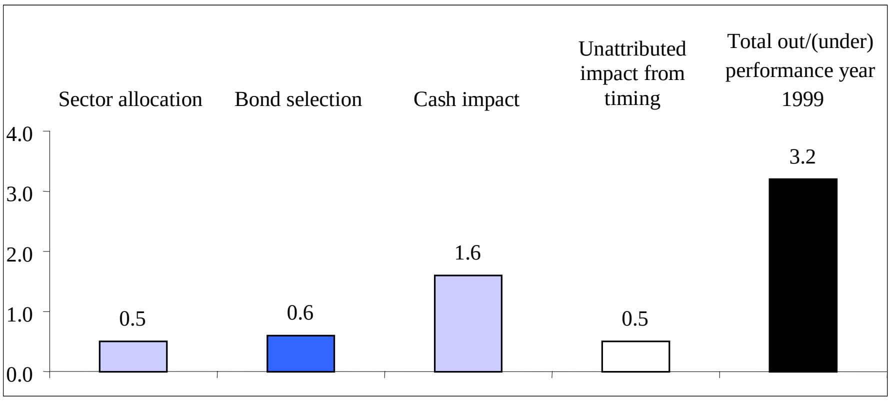



**Year 1999 - Quarterly Analysis**

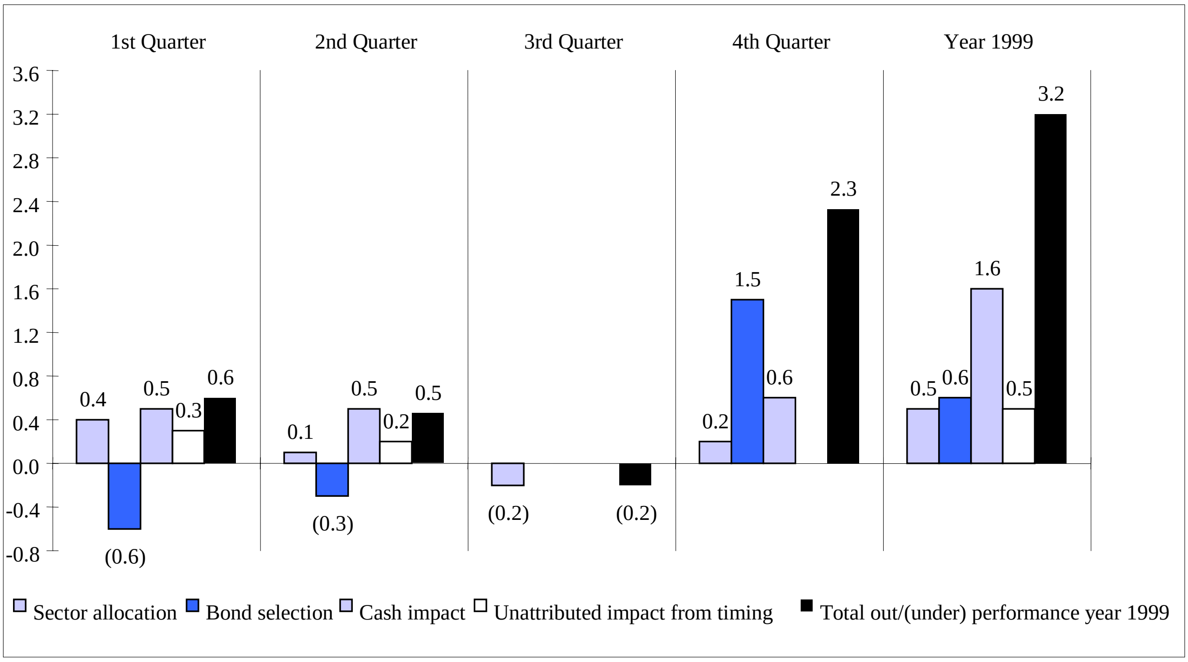


# Performance Attribution for the Diversified Fixed-Interest Portfolio

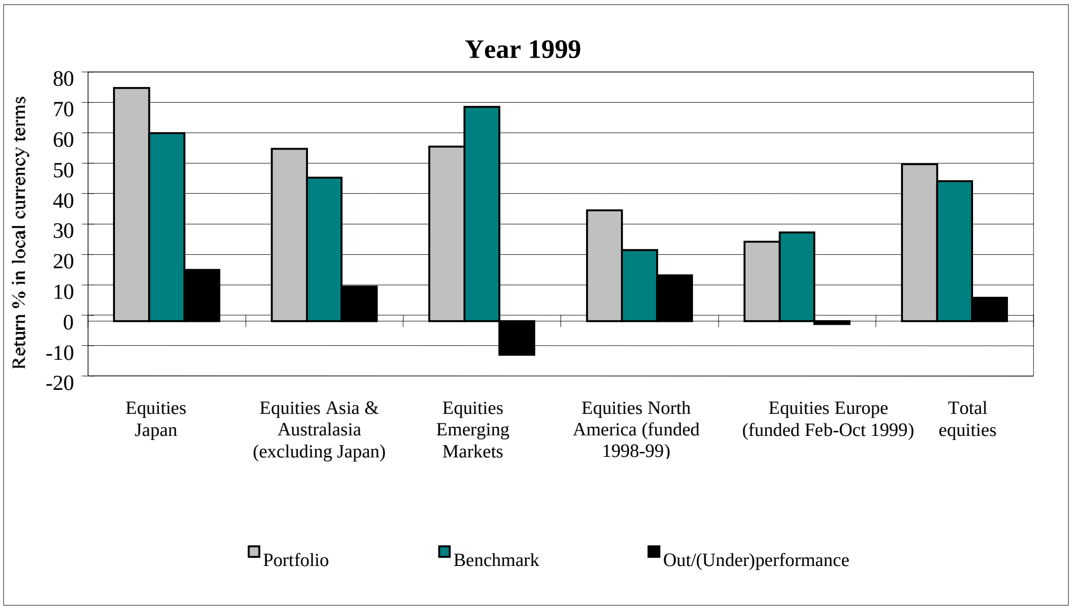
## Year 1999

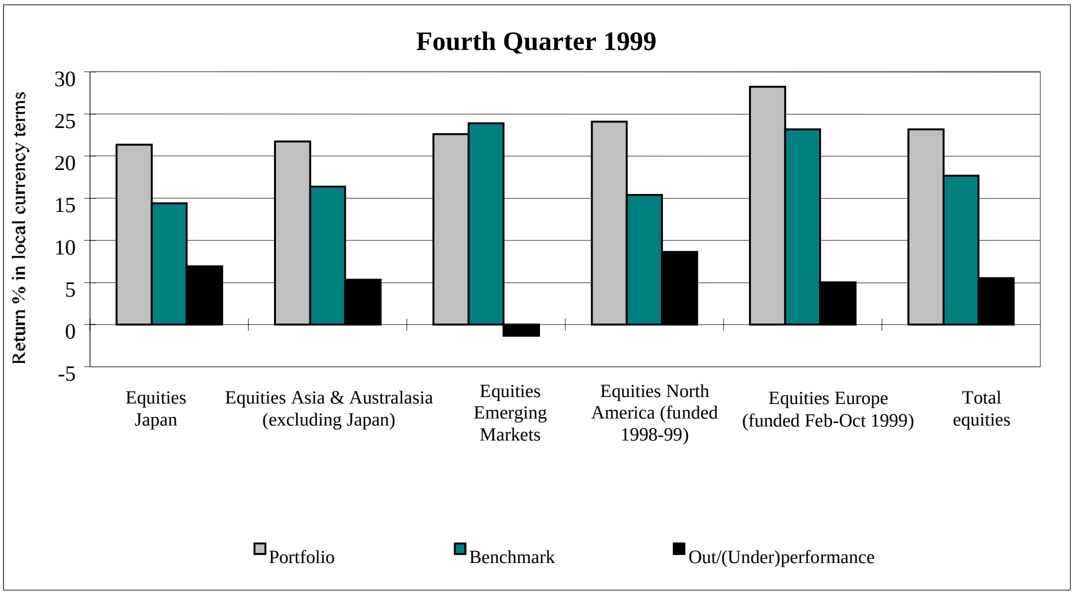



## Year 1999 - Quarterly Analysis



# Performance – Equities Portfolio

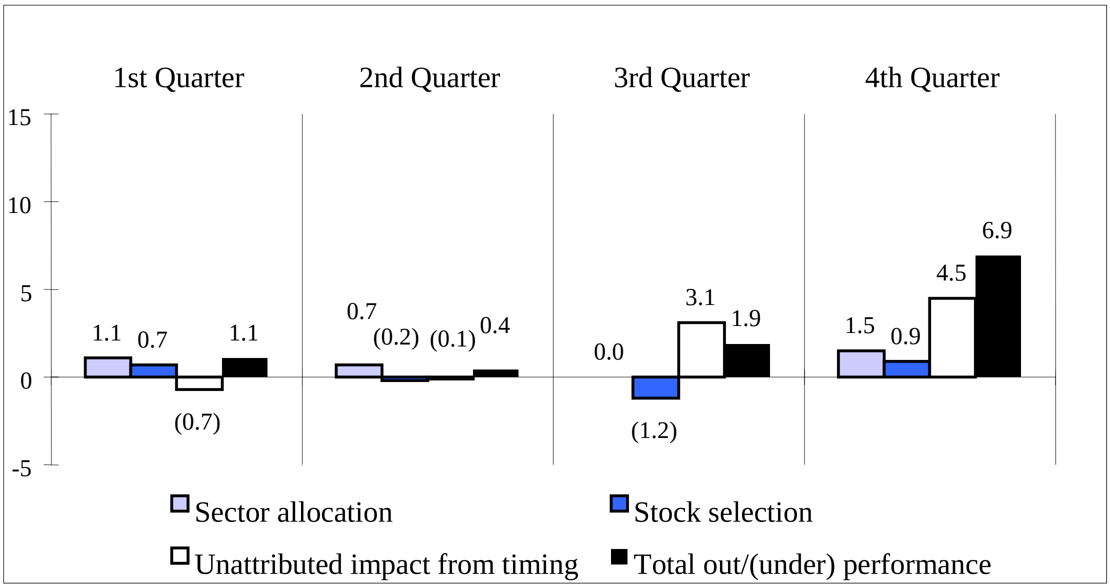


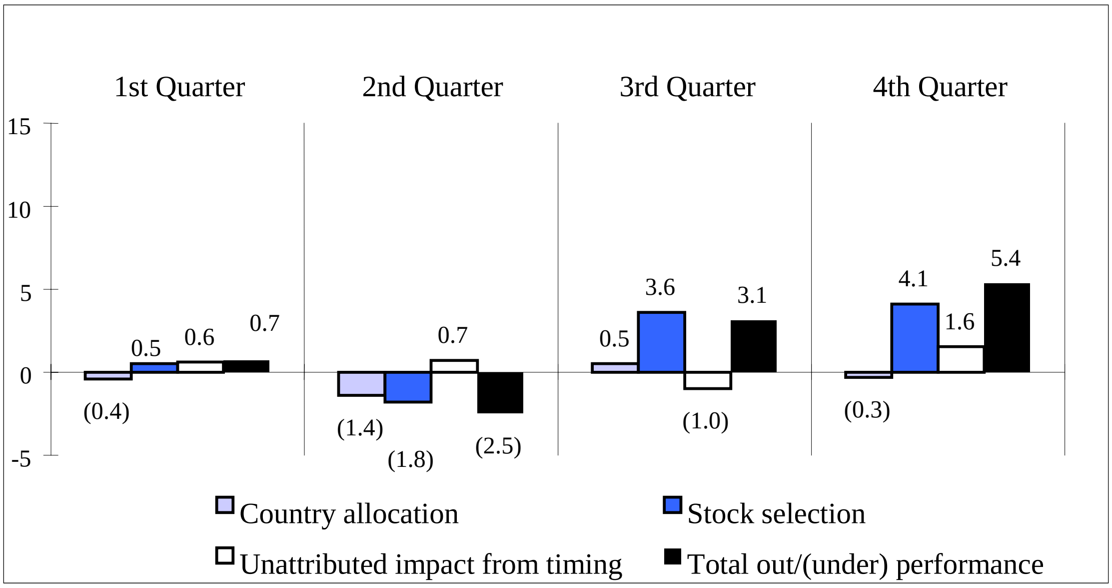
## Performance Attribution for the Equities Portfolio

Quarterly data. Analysis over a longer period would be less exact in the cases of high portfolio turnover combined with significant changes in market prices.

**Japanese Equities**



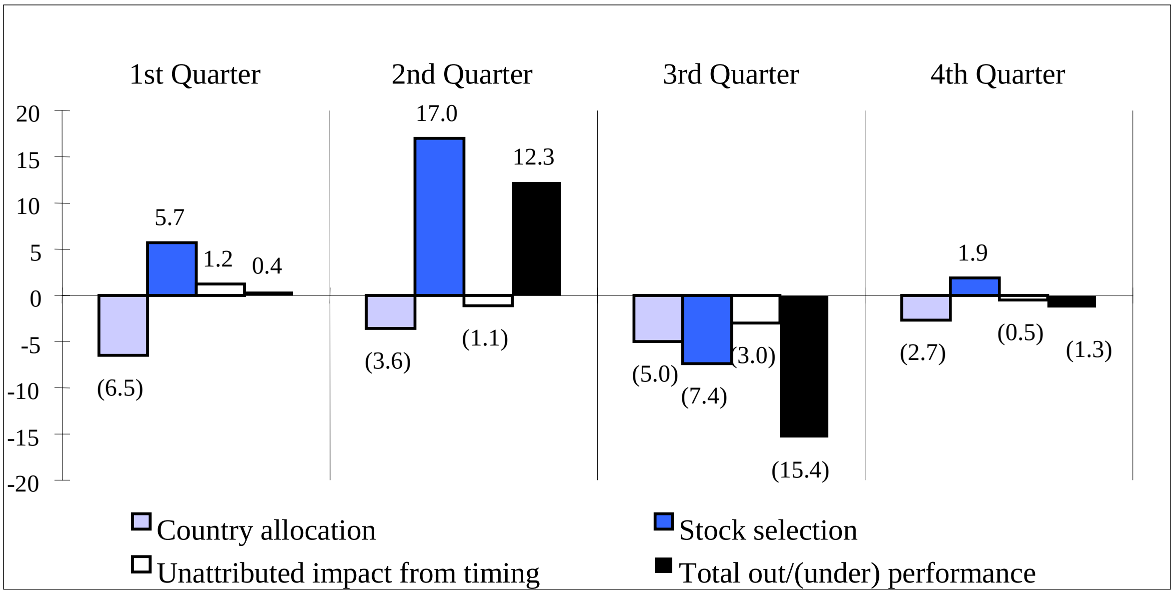

**Asian and Australasian Equities**



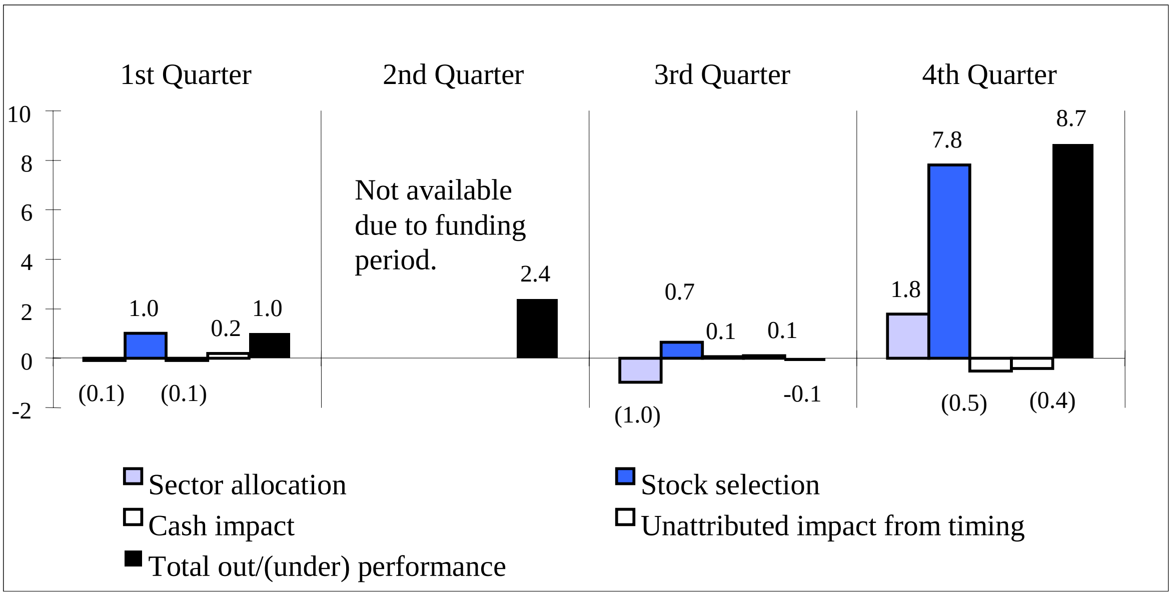
## Performance Attribution for the Equities Portfolio

Quarterly data. Analysis over a longer period would be less exact in the cases of high portfolio turnover combined with significant changes in market prices.

**Emerging Markets Equities**




**North American Equities**




**European Equities**

An aggregated analysis is not available due to the many tranches of funding during the year.

## Analysis of Cash Flows

(USD ‘000 equivalent)

| | 1999 | 1998 |
|---|---|---|
| Balance at 1 January | 2 268 295 | 2 150 730 |
| Investment income | 194 469 | 187 899 |
| Other inflows: | | |
| Loan income received | 44 197 | 41 898 |
| Loan principal repayments | 133 219 | 123 358 |
| Encashment of promissory notes | 78 636 | 75 701 |
| Contributions received in cash | 22 012 | 4 681 |
| Total inflows | 278 064 | 245 638 |
| Outflows: | | |
| Loan disbursements | (283 995) | (298 948) |
| Grant disbursements | (30 100) | (25 212) |
| Payment of administrative expenses | (48 213) | (52 994) |
| Miscellaneous | 6 434 | (7 259) |
| Total outflows | (355 874) | (384 413) |
| Effects of movements in exchange rates | (53 924) | 68 441 |
| Balance at 31 December | 2 331 030 | 2 268 295 |

## Analysis of the Fixed-Interest Portfolio by Type of Mandate and by Instrument at 31 December 1999

(USD ’000 equivalent)

| Instruments | Internally Managed Portfolio | Global Fixed-Interest Portfolio | Diversified Fixed-Interest Portfolio | Total Fixed-Interest Portfolio 31.12.1999 |
|---|---|---|---|---|
| Cash | 32 101 | 19 519 | 16 229 | 67 849 |
| Time deposits | 37 034 | 72 104 | 44 140 | 153 278 |
| Treasury bills | - | - | - | - |
| Global government bonds | - | 1 144 508 | 27 313 | 1 171 821 |
| Emerging market bonds | - | - | 35 182 | 35 182 |
| Mortgage-backed securities | - | - | 60 760 | 60 760 |
| Asset-backed securities | - | - | 2 999 | 2 999 |
| Corporate bonds | - | - | 69 983 | 69 983 |
| Equities | - | - | - | - |
| Futures | - | - | 48 | 48 |
| Options | - | - | (30) | (30) |
| Open trades | (25) | (6 327) | (47 976) | (54 328) |
| Accrued interest income | 262 | 24 462 | 2 711 | 27 435 |
| Dividends receivable | - | - | - | - |
| Non-convertible currencies | 907 | - | - | 907 |
| Total | 70 279 | 1 254 266 | 211 359 | 1 535 904 |
| Percentage | 3.0% | 53.8% | 9.1% | 65.9% |

# Currency Composition of the Investment Portfolio, Holdings of Promissory Notes and Amounts Receivable from Contributors at 31 December 1999

| Currency | Cash and Investments | Promissory* Notes | Amounts Receivable | Total |
|---|---|---|---|---|
| USD | 823 890 | 113 190 | 34 713 | 971 793 |
| EUR | 461 239 | 102 982 | 27 657 | 591 878 |
| JPY | 406 337 | 53 238 | 14 141 | 473 716 |
| GBP | 302 605 | 32 190 | - | 334 795 |
| **Sub-Total** | **1 994 071** | **301 600** | **76 511** | **2 372 182** |
| ARS | 1 925 | - | - | 1 925 |
| AUD | 42 204 | 6 770 | - | 48 974 |
| BRL | 29 | - | - | 29 |
| CAD | 42 567 | 20 400 | 6 302 | 69 269 |
| CHF | 14 548 | 10 514 | - | 25 062 |
| CNY | 110 | - | - | 110 |
| DKK | 40 388 | 25 596 | - | 65 984 |
| EEK | - | - | - | 0 |
| EGP | 834 | - | - | 834 |
| GRD | 2 034 | - | - | 2 034 |
| HKD | 37 874 | - | - | 37 874 |
| HUF | 3 541 | - | - | 3 541 |
| IDR | 10 792 | - | - | 10 792 |
| ILS | 511 | - | - | 511 |
| KRW | 25 034 | - | - | 25 034 |
| MXN | 13 654 | - | - | 13 654 |
| MYR | 302 | - | - | 302 |
| NOK | - | 14 704 | - | 14 704 |
| NZD | 1 328 | 392 | - | 1 720 |
| PHP | 5 154 | - | - | 5 154 |
| PKR | 170 | - | - | 170 |
| SEK | 33 435 | 25 889 | - | 59 324 |
| SGD | 22 796 | - | - | 22 796 |
| SKK | 64 | - | - | 64 |
| THB | 12 640 | - | - | 12 640 |
| TRL | 5 917 | - | - | 5 917 |
| ZAR | 18 201 | - | - | 18 201 |
| **Subtotal** | **336 052** | **104 265** | **6 302** | **446 619** |
| **Total Convertible Currencies** | **2 330 123** | **405 865** | **82 813** | **2 818 801** |
| Non-Convertible Currencies | 907 | 1 628 | - | 2 535 |
| **Total** | **2 331 030** | **407 493** | **82 813** | **2 821 336** |

*Excludes promissory notes deposited for complementary contributions.

## Composition of the Portfolio by Maturity of Investments

(USD ’000 equivalent)

| Period | 31 December 1999 | | 31 December 1998 | |
|---|---|---|---|---|
| | **Amount** | **%** | **Amount** | **%** |
| Within 1 year | 253 573 | 10.9 | 277 886 | 12.3 |
| Within 2-5 years | 398 425 | 17.1 | 349 606 | 15.4 |
| Within 6-10 years | 637 726 | 27.4 | 930 691 | 41.0 |
| Over 10 years | 270 937 | 11.6 | 385 612 | 17.0 |
| No fixed maturity (equities) | 770 369 | 33.0 | 324 500 | 14.3 |
| | 2 331 030 | 100.0 | 2 268 295 | 100.0 |

# Diversification of the Investment Portfolio by Member Countries

## 31 December 1999

| | Cash | Time-Deposits | Fixed-Income Securities | Equities | Other Assets | Total | % |
|---|---|---|---|---|---|---|---|
| Latin America and Caribbean | - | - | 27 446 | 41 130 | - | 68 576 | 2.9 |
| Emerging Europe | 2 | - | 5 055 | 9 522 | - | 14 579 | 0.6 |
| North Africa, Near East | - | 30 907 | 889 | 2 235 | - | 34 031 | 1.5 |
| Sub-Saharan Africa | 4 | - | - | 15 795 | - | 15 799 | 0.7 |
| East and South Asia | 641 | - | 1 792 | 130 285 | - | 132 718 | 5.7 |
| Subtotal Developing Countries | 647 | 30 907 | 35 182 | 198 967 | - | 265 703 | 11.4 |
| Developed Countries | 71 242 | 141 868 | 1 195 557 | 571 402 | (24 806) | 1 955 263 | 83.9 |
| International Development Institutions | - | - | 110 064 | - | - | 110 064 | 4.7 |
| Total | 71 889 | 172 775 | 1 340 803 | 770 369 | (24 806) | 2 331 030 | 100.0 |

## 31 December 1998

| | Cash | Time-Deposits | Fixed-Income Securities | Equities | Other Assets | Total | % |
|---|---|---|---|---|---|---|---|
| Developing Countries | 745 | 56 392 | 16 860 | 116 289 | 347 | 190 633 | 8.4 |
| Developed Countries | 60 771 | 145 542 | 1 609 156 | 214 006 | (30 249) | 1 999 226 | 88.1 |
| International Development Institutions | - | - | 78 195 | - | 241 | 78 436 | 3.5 |
| Total | 61 516 | 201 934 | 1 704 211 | 330 295 | (29 661) | 2 268 295 | 100.0 |

# Rate of Return and Investment Strategy for the Fourth Quarter 1999

## Overall Portfolio

1. Investment income for the fourth quarter of 1999 amounted to USD 158 913 000 equivalent which, added to income for the first nine months of USD 35 556 000 equivalent, amounted to USD 194 469 000 equivalent for the whole year of 1999. In line with market practice, capital gains and losses include both realized and unrealized gains and losses. All amounts are included on an accrual basis. Table 1 summarizes net investment income earned during the period under review, while further details of income are provided in Tables 4 and 7 for fixed-interest and equities investments, respectively.

**Table 1: Investment Income**
(USD '000 equivalent)

| | 4th Quarter 1999 Fixed-Interest Portfolio | 4th Quarter 1999 Equity Portfolio | 4th Quarter 1999 Overall Portfolio | 3rd Quarter 1999 | 2nd Quarter 1999 | 1st Quarter 1999 | 1999 | 1998 |
|---|---|---|---|---|---|---|---|---|
| Interest from fixed-interest investments and bank accounts | 21 760 | 203 | 21 963 | 22 706 | 22 422 | 23 162 | 90 253 | 112 668 |
| Dividend income from equities | - | 2 215 | 2 215 | 2 053 | 2 417 | 1 999 | 8 684 | 5 654 |
| Realized capital gains | (15 319) | 14 257 | (1 062) | (5 472) | (385) | 10 780 | 3 861 | 40 846 |
| Unrealized capital gains | 4 592 | 133 804 | 138 396 | (52 984) | 24 332 | (8 472) | 101 272 | 36 111 |
| **Subtotal: Gross investment income** | **11 033** | **150 479** | **161 512** | **(33 697)** | **48 786** | **27 469** | **204 070** | **195 279** |
| Securities lending income | 55 | 21 | 76 | 160 | 166 | 137 | 539 | 905 |
| Investment manager fees | (829) | (1 230) | (2 059) | (1 863) | (1 697) | (1 573) | (7 192) | (5 660) |
| Custody fees | (140) | (54) | (194) | (689) | (656) | (331) | (1 870) | (1 469) |
| Financial advisory and other investment management fees | (155) | (70) | (225) | (136) | (147) | - | (508) | (610) |
| Taxes | - | (46) | (46) | (25) | (215) | - | (286) | (129) |
| Other investment expenses | (109) | (42) | (151) | (81) | (52) | - | (284) | (417) |
| **Net investment income** | **9 855** | **149 058** | **158 913** | **(36 331)** | **46 185** | **25 702** | **194 469** | **187 899** |

2. Movements affecting the overall portfolio during the fourth quarter are shown in Table 2.

**Table 2: Movements in Overall Portfolio – Fourth Quarter 1999**
(USD '000 equivalent)

| | Fixed-Interest Portfolio | Equities Portfolio | Overall Portfolio |
|---|---|---|---|
| Opening balance (30 September 1999) | 1 596 012 | 622 393 | 2 218 405 |
| Transfers between portfolios | (21 413) | 21 413 | - |
| Other net flows | (25 499) | - | (25 499) |
| Gross investment income | 11 033 | 150 479 | 161 512 |
| Securities lending income | 55 | 21 | 76 |
| Fees, charges and taxes | (1 233) | (1 442) | (2 675) |
| Movements on exchange | (23 051) | 2 262 | (20 789) |
| Closing balance ( 31 December 1999) | 1 535 904 | 795 126 | 2 331 030 |

3. The overall rate of return on the portfolio, net of management and custodian fees, for the fourth quarter of 1999 was 7.07%. Taking account of the rate of return of 1.57% for the first nine months of 1999, this results in a return for the whole year of 1999 of 8.78% compared with 8.5% in 1998. Returns in the fourth quarter were affected by good performance in the fixed-interest sector and a strong rally in the equity markets.

4. The performance of the various sectors of the investment portfolio is measured against preassigned independent benchmarks indicating the return that may be expected through passive management of a defined sector of the market. Table 3 compares the return of each major section of the portfolio with the appropriate benchmark rate of return, and shows an overall outperformance of 177 basis points for the fourth quarter of 1999 compared with an overall underperformance of 109 basis points in the first nine months of 1999. This results in an overall outperformance of 66 basis points for the whole of 1999 (1998 - overall outperformance of 153 basis points). This information is presented graphically in Annex XII.

**Table 3: Overall Performance Compared with Benchmarks – Fourth Quarter 1999**

| | Rate of Return% | | Out/(Under) Performance |
|---|---|---|---|
| **Portfolio** | **Portfolio** | **Benchmark** | |
| Total fixed-interest | 0.69 | 0.39 | 0.30 |
| Total equities | 23.20 | 17.70 | 5.50 |
| Overall portfolio gross rate of return | 7.19 | 5.42 | 1.77 |
| Less expenses | (0.12) | (0.12) | 0.00 |
| Overall portfolio net rate of return | 7.07 | 5.30 | 1.77 |
| Year 1999 overall portfolio net rate of return | 8.78 | 8.12 | 0.66 |
| Year 1998 overall portfolio net rate of return | 8.50 | 6.97 | 1.53 |

5. The fixed-interest portfolio consists of the internally-managed, global fixed-interest and diversified fixed-interest portfolios. In aggregate, the gain for the fourth quarter of 1999 amounted to USD 9 855 000, as shown in Table 4.

**Table 4: Investment Income on Fixed-Interest Portfolio – Fourth Quarter 1999**
(USD ‘000 equivalent)

| | Internally Managed Portfolio | Global-Fixed Interest Portfolio | Diversified Fixed-Interest Portfolio | Total-Fixed Interest Portfolio |
|---|---|---|---|---|
| Interest from fixed-interest investments and bank accounts | 1 062 | 17 452 | 3 246 | 21 760 |
| Dividend income from equities | - | - | - | - |
| Realized capital gains | - | (14 988) | (331) | (15 319) |
| Unrealized capital gains | - | 3 034 | 1 558 | 4 592 |
| **Subtotal: Gross investment income** | **1 062** | **5 498** | **4 473** | **11 033** |
| Securities lending income | - | 48 | 7 | 55 |
| Investment manager fees | - | (621) | (208) | (829) |
| Custody fees | (6) | (116) | (18) | (140) |
| Financial advisory and other investment management fees | - | (134) | (21) | (155) |
| Taxes | - | - | - | - |
| Other investment expenses | (5) | (90) | (14) | (109) |
| **Net investment income** | **1 051** | **4 585** | **4 219** | **9 855** |

6. Movements affecting the fixed-interest portfolio during the fourth quarter of 1999 are shown in Table 5. A total of USD 49 118 000 was transferred from the global fixed-interest portfolio. In October USD 20 million was transferred to the European equities portfolio and the balance of

USD 29 118 000 was used to cover loan and grant disbursements, administrative expenses and the payment of investment manager fees and other charges.

**Table 5: Movements in Fixed-Interest Portfolio – Fourth Quarter 1999**
(USD '000 equivalent)

| | Internally Managed Portfolio | Global Fixed-Interest Portfolio | Diversified Fixed-Interest Portfolio | Total Fixed-Interest Portfolio |
|---|---|---|---|---|
| Opening balance (30 September 1999) | 67 543 | 1 321 564 | 206 905 | 1 596 012 |
| Transfers between portfolios | 27 464 | (49 118) | 241 | (21 413) |
| Other net flows | (25 499) | - | - | (25 499) |
| Gross investment income | 1 062 | 5 498 | 4 473 | 11 033 |
| Securities lending income | 0 | 48 | 7 | 55 |
| Fees, charges and taxes | (11) | (961) | (261) | (1 233) |
| Movements on exchange | (280) | (22 765) | (6) | (23 051) |
| Closing balance ( 31 December 1999) | 70 279 | 1 254 266 | 211 359 | 535 904 |

7. The performance of the fixed-interest portfolio by type of mandate is presented in Table 6. This information is presented graphically in Annex XIII.

**Table 6: Fixed-Interest Performance Compared with Benchmarks – Fourth Quarter 1999**

| | Rate of Return % | | Out/(Under) Performance |
|---|---|---|---|
| **Portfolio** | **Portfolio** | **Benchmark** | |
| Internally-managed portfolio | 1.59 | 1.02 | 0.57 |
| Global fixed-interest | 0.41 | 0.45 | (0.04) |
| Diversified fixed-interest | 2.16 | (0.17) | 2.33 |
| Total fixed-interest | 0.69 | 0.39 | 0.30 |
| Year 1999 total fixed-interest | (1.85) | (0.81) | (1.04) |
| Year 1998 rate of return total fixed-interest | 11.52 | 10.23 | 1.29 |

8. The global fixed-interest sub-portfolio performed positively with 0.41%, which was broadly in line with the benchmark. Keeping a short or neutral duration compared to the benchmark generally supported the global-fixed interest managers.

9. The diversified fixed-interest portfolio was the best performing fixed-interest sub-portfolio with a return of 2.16%, representing an outperformance of 233 basis points against the benchmark. The managers profited from significantly narrowing spreads, especially in corporate and emerging market bonds where spreads narrowed significantly from historically wide levels.

**Equities Portfolio**

10. In aggregate, the gain attributable to the equities portfolio for the fourth quarter of 1999 amounted to USD 149 058 000, as illustrated in Table 7.

### Table 7: Investment Income on Equities Portfolio – Fourth Quarter 1999
(USD '000 equivalent)

| | Japanese Equities | Asian and Australasian Equities | Emerging Markets Equities | Currency Overlay | North American Equities | European Equities | Total Equities Portfolio |
|---|---|---|---|---|---|---|---|
| Interest from fixed-interest investments and bank accounts | - | 17 | 30 | 126 | 1 | 29 | 203 |
| Dividend income from equities | 35 | 619 | 901 | - | 524 | 136 | 2 215 |
| Realized capital gains | 3 777 | 4 672 | (569) | - | 7 269 | (892) | 14 257 |
| Unrealized capital gains | 26 958 | 15 964 | 21 983 | - | 34 985 | 33 914 | 133 804 |
| **Subtotal: Gross investment income** | **30 770** | **21 272** | **22 345** | **126** | **42 779** | **33 187** | **150 479** |
| Securities lending income | 5 | 3 | 3 | - | 6 | 4 | 21 |
| Investment manager fees | (194) | (171) | (350) | - | (379) | (136) | (1 230) |
| Custody fees | (12) | (9) | (9) | (1) | (15) | (8) | (54) |
| Financial advisory and other investment management fees | (15) | (11) | (11) | (2) | (20) | (11) | (70) |
| Taxes | - | (16) | 6 | - | (5) | (31) | (46) |
| Other investment expenses | (10) | (7) | (7) | (1) | (10) | (7) | (42) |
| **Net investment income** | **30 544** | **21 061** | **21 977** | **122** | **42 356** | **32 998** | **149 058** |

11. Movements affecting the equities portfolio during the fourth quarter of 1999 are shown in Table 8. In October 1999, an amount of USD 20 million was transferred to the European equities portfolio from the global fixed-interest portfolio.

### Table 8: Movements in the Equities Portfolio – Fourth Quarter 1999
(USD '000 equivalent)

| | Japanese Equities | Asian and Australasian Equities | Emerging Markets Equities | Currency Overlay | North American Equities | European Equities | Total Equities Portfolio |
|---|---|---|---|---|---|---|---|
| Opening balance (30 September 1999) | 142 015 | 97 794 | 98 485 | 9 749 | 177 596 | 96 754 | 622 393 |
| Transfers between portfolios | 226 | 197 | 375 | 4 | 422 | 20 189 | 21 413 |
| Gross investment income | 30 770 | 21 272 | 22 345 | 126 | 42 779 | 33 187 | 150 479 |
| Securities lending income | 5 | 3 | 3 | - | 6 | 4 | 21 |
| Fees, charges and taxes | (231) | (214) | (371) | (4) | (429) | (193) | (1 442) |
| Movements on exchange | 4 821 | 1 580 | 1 278 | (9) | - | (5 408) | 2 262 |
| Closing balance ( 31 December 1999) | 177 606 | 120 632 | 122 115 | 9 866 | 220 374 | 144 533 | 795 126 |

12. The performance of the equities portfolio by type of mandate is presented in Table 9. This information is presented graphically in Annex XVI, chart 2.

**Table 9: Equities Performance Compared with Benchmarks – Fourth Quarter 1999**

| | Rate of Return % | | Out/(Under) Performance |
|---|---|---|---|
| **Portfolio** | **Portfolio** | **Benchmark** | |
| Equities Japan | 21.36 | 14.43 | 6.93 |
| Equities Asia and Australasia (excluding Japan) | 21.73 | 16.38 | 5.35 |
| Equities emerging markets | 22.62 | 23.92 | (1.30) |
| Equities North America (funded 1998-99) | 24.09 | 15.43 | 8.66 |
| Equities Europe (funded 2-10/1999) | 28.23 | 23.19 | 5.04 |
| Total equities | 23.20 | 17.70 | 5.50 |
| Year 1999 total equities | 49.71 | 44.07 | 5.64 |
| Year 1998 rate of return total equities | (7.05) | (10.03) | 2.98 |

13. The overall equities portfolio performed exceptionally strongly by returning 23.20% and outperforming 5.50% against the aggregate benchmark. All sections of the equity portfolio showed strong returns. Managers added value through weighting of countries and sectors as well as stock selection, although impact from stock selection dominated.

14. The outperforming North American equities portfolio generally benefited from overweighting strongly performing technology sectors and from very strong stock selection within these sectors. Growth stocks continued to outperform value stocks, and therefore managers with a growth-oriented style outperformed those with a value-oriented style.

15. Only the emerging markets portfolio showed an underperformance against the benchmark. The underperformance was mainly due to negative stock selection in Brazil, The Philippines and Singapore, although the portfolio benefited from weighting and selection in several other markets.

# ISO Currency Abbreviations

| CURRENCY CODE | CURRENCY NAME |
|---|---|
| USD | UNITED STATES DOLLAR |
| EUR | EURO |
| JPY | JAPANESE YEN |
| GBP | POUND STERLING |
| ARS | ARGENTINE PESO |
| AUD | AUSTRALIAN DOLLAR |
| BRL | BRAZILIAN REAL |
| CAD | CANADIAN DOLLAR |
| CHF | SWISS FRANC |
| CNY | CHINESE YUAN |
| DKK | DANISH KRONE |
| EGP | EGYPTIAN POUND |
| GRD | GREEK DRACHMA |
| HKD | HONG KONG DOLLAR |
| HUF | HUNGARIAN FORINT |
| IDR | INDONESIAN RUPIAH |
| ILS | ISRAELI SHEKEL |
| KRW | SOUTH KOREAN WON |
| MXN | MEXICAN PESO |
| MYR | MALAYSIAN RIGGIT |
| NOK | NORWEGIAN KRONE |
| NZD | NEW ZEALAND DOLLAR |
| PHP | PHILIPPINE PESO |
| PKR | PAKISTAN RUPEE |
| SEK | SWEDISH KRONA |
| SGD | SINGAPORE DOLLAR |
| SKK | SLOVAK KORUNA |
| THB | THAILAND BAHT |
| TRL | TURKISH LIRA |
| ZAR | SOUTH AFRICAN RAND |

## Duration

1. Duration is the weighted average term-to-maturity of a security's cash flow.

2. Duration is commonly used by investors to estimate the change in value of a single security or of a whole portfolio relative to a change in bond yields. The greater the duration of a bond, the greater its price volatility.

## Forward Contracts

3. A currency forward contract is an agreement for the future delivery of an amount of currency at a specified price at a designated time. Unlike futures contracts, which are traded in organized changes, a forward is traded by direct contact between buyer and seller.

## Futures Contracts

4. A futures contract is an agreement to buy or sell a specific amount of a bond or currency at a specific price at a designated time. Such contracts are traded in organized exchanges for standard lots.

## Options

5. An option is a contract in which the seller of the option grants the buyer the right to purchase at a specified price and at a specified time. The seller grants this right to the buyer in exchange for a certain sum of money called the premium.

6. A call option gives the buyer the right to buy a specific amount of a bond stock or currency at a specified price. A put option gives the buyer the right to sell a specific amount of a bond stock or currency at a specified price. The buyer of an option has the right but not the obligation to exercise the option.

7. IFAD's investment guidelines only permit the use of exchange-traded options. Tailor-made or over-the-counter options may not be used.

## Hedge

8. A hedge is the use of techniques and/or financial instruments to manage or reduce foreign exchange or market risk. Forward exchange contracts are normally used to limit exposure to foreign exchange risk. Losses incurred on forward exchange contracts offset higher levels of interest income earned through investing in markets other than that of the base currency, and are referred to as "hedging costs".

9. Futures and options contracts are normally used to manage market risk.