



**IFAD**  
**INTERNATIONAL FUND FOR AGRICULTURAL DEVELOPMENT**  
**Executive Board – Seventy-Fourth Session**

Rome, 5-6 December 2001

**REPORT ON IFAD'S INVESTMENT PORTFOLIO FOR THE  
THIRD QUARTER OF 2001**

**I. INTRODUCTION**

1. The following report on IFAD's investment portfolio covers the three-month period ending 30 September 2001 and includes comparative figures for the year to date and earlier years.
2. The report comprises sections on asset allocation, investment income, performance, currency composition and risk measurement.

**II. ASSET ALLOCATION**

3. Table 1 compares the actual allocation of the investment portfolio's four major asset classes to their policy allocation. In the third quarter of 2001 there was a transfer of USD 14 165 000 equivalent from the equities portfolio to the internally-managed portfolio, due to the liquidation in August 2001 of the North American Micro Cap equities mandate. The liquidation of the mandate helped reduce overall portfolio volatility and gains of USD 4 165 000 equivalent were realized. At 30 September 2001, the portfolio's equity allocation showed a 7% underweight compared to policy allocation. The underweight was largely due to the fall in equity prices during the third quarter coupled with the impact of the liquidation.
4. Following the Seventy-Second Session of the Executive Board in April 2001, it was agreed that a review of IFAD's investment policy would be entrusted to three highly-qualified experts selected from the three Lists of Member States. The expert group began its review in June 2001 and presented a report to the President of IFAD on 6 July 2001.
5. The report was submitted to the Seventy-Third Session of the Board as part of document EB 2001/73/R.6 "Report of the President on IFAD's Investment Policy". The latter document also contained Management's comments on the major observations contained in the expert group's report.

6. The report and Management's comments thereon were discussed at a seminar held at the time of the Seventy-Third Session of the Board. The President undertook to formulate a new investment policy in the light of discussions at the seminar and to consult with the List Convenors prior to the Seventy-Fourth Session of the Board.

7. Pending a decision on a new investment policy and asset allocation, therefore, the investment portfolio has not been rebalanced in line with the current policy allocation.

**Table 1: Summary of Movements in Cash and Investments – Third Quarter 2001**  
(USD '000 equivalent)

	Internally-Managed Portfolio	Global Government Bonds	Diversified Fixed-Interest	Equities	Overall Portfolio
<b>Opening balance (30 June 2001)</b>	<b>65 462</b>	<b>793 299</b>	<b>212 204</b>	<b>856 871</b>	<b>1 927 836</b>
Gross investment income (loss)	611	29 901	3 645	(156 763)	(122 606)
Securities lending income	-	15	-	101	116
Fees, charges and taxes	20	(514)	(138)	(1 674)	(2 306)
<b>Net investment income (loss)</b>	<b>631</b>	<b>29 402</b>	<b>3 507</b>	<b>(158 336)</b>	<b>(124 796)</b>
Transfers due to allocation	14 165	-	-	(14 165)	-
Transfers due to expenses	(2 134)	493	138	1 503	-
<b>Transfers between portfolios</b>	<b>12 031</b>	<b>493</b>	<b>138</b>	<b>(12 662)</b>	<b>-</b>
Other net flows	2 744	-	-	-	2 744
Movements on exchange	1 345	33 248	(28)	20 346	54 911
<b>Closing balance (30 September 2001)</b>	<b>82 213</b>	<b>856 442</b>	<b>215 821</b>	<b>706 219</b>	<b>1 860 695</b>
Actual allocation (%)	4.4	46.0	11.6	38.0	100.0
Policy allocation (%)	5.0	40.0	10.0	45.0	100.0
<b>Difference in allocation (%)</b>	<b>(0.6)</b>	<b>6.0</b>	<b>1.6</b>	<b>(7.0)</b>	<b>-</b>

### III. INVESTMENT INCOME

8. Table 2 shows investment income for the four major asset classes. Aggregate net investment income in the third quarter of 2001 amounted to a loss of USD 124 796 000 equivalent, which, added to the loss of USD 21 833 000 equivalent in the first six months of 2001, amounts to a loss of USD 146 629 000 equivalent for the first nine months of 2001 (2000 – a loss of USD 47 850 000 equivalent).

9. In the third quarter of 2001, global equity markets came under pressure from increasing signs of global economic weakness. Stocks tumbled further in September 2001 in the wake of terrorist attacks in the United States. On the other hand, government bond markets rallied following interest rate cuts coordinated by a number of central banks.

**Table 2: Net Investment Income**  
(USD '000 equivalent)

Portfolio	3 <sup>rd</sup> Quarter 2001	2 <sup>nd</sup> Quarter 2001	1 <sup>st</sup> Quarter 2001	Year to Date 2001	2000	1999	1998	1997
Internally-managed port.	631	578	413	1 622	3 654	3 114	4 834	18 633
Global government bonds	29 402	(6 982)	18 027	40 447	74 625	(43 977)	195 506	154 228
Diversified fixed-interest	3 507	52	6 130	9 689	17 615	3 832	6 130	-
Total equities	(158 336)	44 573	(84 624)	(198 387)	(143 744)	231 500	(18 571)	(8 921)
<b>Overall portfolio</b>	<b>(124 796)</b>	<b>38 221</b>	<b>(60 054)</b>	<b>(146 629)</b>	<b>(47 850)</b>	<b>194 469</b>	<b>187 899</b>	<b>163 940</b>

10. Table 3 shows net income for the various sectors of the fixed-interest portfolio for the third quarter of 2001. The government bonds portfolio performed strongly, slightly outperforming its benchmark, mainly due to overweighting United States bond markets against Japanese bonds. The diversified fixed-interest portfolio performed positively, but recorded an underperformance largely due to being overweighted in corporate bonds while underweighting the rallying United States Treasury bonds, which benefited from a flight to quality in September.

**Table 3: Investment Income on the Fixed-Interest Portfolio – Third Quarter 2001**  
(USD '000 equivalent)

	Internally- Managed Portfolio	Global Government Bonds	Diversified Fixed-Interest Portfolio	Total Fixed- Interest Portfolio
Interest from fixed-interest investments and bank accounts	611	11 186	3 516	15 313
Dividend income from equities	-	-	-	-
Realized capital gains (losses)	-	943	(815)	128
Unrealized capital gains	-	17 772	944	18 716
<b>Subtotal: Gross investment income</b>	<b>611</b>	<b>29 901</b>	<b>3 645</b>	<b>34 157</b>
Securities lending income	-	15	-	15
Investment manager fees	-	(373)	(77)	(450)
Custody fees	(25)	(91)	(49)	(165)
Financial advisory and other investment management fees	-	(44)	(12)	(56)
Taxes	-	1	(1)	-
Other investment income/(expenses)	45	(7)	1	39
<b>Net investment income</b>	<b>631</b>	<b>29 402</b>	<b>3 507</b>	<b>33 540</b>
<b>Gross rate of return (3rd quarter) (%)</b>	<b>0.83</b>	<b>3.77</b>	<b>1.72</b>	<b>3.22</b>
<b>Benchmark rate of return (3rd quarter) (%)</b>	<b>0.43</b>	<b>3.51</b>	<b>4.72</b>	<b>3.59</b>
<b>Out/(under) performance (3rd quarter)</b>	<b>0.40</b>	<b>0.26</b>	<b>(3.00)</b>	<b>(0.37)</b>

11. Table 4 shows the net income for the various mandates of the equities portfolio for the third quarter of 2001. All equity mandates showed negative returns due to prevailing investment conditions. Globally, on an industry-sector basis, most sectors were affected negatively although the most defensive sectors, such as consumer staples and health care, gained slightly. Three of the portfolio's equity mandates outperformed their benchmarks. In the case of the emerging markets equities mandate and the Asian and Australasian equities mandate, this was largely due to low exposure to the quarter's main underperforming markets, such as China and Argentina, while holding relatively high amounts of cash and time deposits. The underperformance of the North American equities mandate was the main contributing factor to the overall equity portfolio's underperformance. The mandate's underperformance was largely due to negative stock selection in several sectors, while the mandate's relatively neutral sector weighting had only a minor negative impact.

**Table 4: Investment Income on the Equities Portfolio – Third Quarter 2001**  
(USD '000 equivalent)

	Japanese Equities	Asian and Australasian Equities	Emerging Markets Equities	Currency Overlay	North American Equities	European Equities	Global Equities	Total Equities Portfolio
Interest from fixed-interest investments and bank accounts	-	35	39	83	3	6	4	170
Dividend income from equities	327	981	108	-	577	539	629	3 161
Realized capital losses	(2 104)	(1 353)	(3 627)	-	(6 662)	(7 129)	(8 109)	(28 984)
Unrealized capital losses	(20 642)	(13 928)	(9 594)	-	(33 846)	(25 552)	(27 548)	(131 110)
<b>Subtotal: Gross investment income (loss)</b>	<b>(22 419)</b>	<b>(14 265)</b>	<b>(13 074)</b>	<b>83</b>	<b>(39 928)</b>	<b>(32 136)</b>	<b>(35 024)</b>	<b>(156 763)</b>
Securities lending income	8	17	3	-	32	32	9	101
Investment manager fees	(125)	(132)	(227)	-	(268)	(170)	(223)	(1 145)
Custody fees	(12)	(38)	(94)	(7)	(75)	(48)	(90)	(364)
Financial advisory and other investment management fees	(7)	(5)	(4)	(1)	(12)	(8)	(11)	(48)
Taxes	-	(32)	(10)	-	22	(62)	(37)	(119)
Other investment expenses	-	-	(1)	-	-	3	-	2
<b>Net investment income (loss)</b>	<b>(22 555)</b>	<b>(14 455)</b>	<b>(13 407)</b>	<b>75</b>	<b>(40 229)</b>	<b>(32 389)</b>	<b>(35 376)</b>	<b>(158 336)</b>
<b>Gross rate of return (3rd quarter) (%)</b>	<b>(19.22)</b>	<b>(15.44)</b>	<b>(16.47)</b>	<b>NA</b>	<b>(19.68)</b>	<b>(21.24)</b>	<b>(17.86)</b>	<b>(18.46)</b>
<b>Benchmark rate of return (3rd quarter) (%)</b>	<b>(21.04)</b>	<b>(17.43)</b>	<b>(17.12)</b>	<b>NA</b>	<b>(15.64)</b>	<b>(18.90)</b>	<b>(16.35)</b>	<b>(17.27)</b>
<b>Out/(under) performance (3rd quarter)</b>	<b>1.82</b>	<b>1.99</b>	<b>0.65</b>	<b>NA</b>	<b>(4.04)</b>	<b>(2.34)</b>	<b>(1.51)</b>	<b>(1.19)</b>

Note: NA = not applicable

#### IV. PERFORMANCE

12. The performance of the various mandates of the investment portfolio is measured against preassigned independent benchmarks, indicating the return that would be expected through passive management of defined sectors of the market. The principal indexes used are the JP Morgan Global Government Bonds Index and the Morgan Stanley Capitalization Index for global equities.

13. As shown in Table 5, there was an overall negative return of 6.53% in the third quarter of 2001, reflecting an underperformance of 78 basis points against the benchmark. The quarter's overall underperformance was due to the underperformance in diversified fixed-interest and equities.

**Table 5: Overall Performance Compared with Benchmarks – Third Quarter 2001**

Portfolio	Third Quarter 2001			Year to Date 2001		
	Rate of Return (%)		Out/(Under) Performance	Rate of Return %		Out/(Under) Performance
	Portfolio	Benchmark		Portfolio	Benchmark	
Internally-managed portfolio	0.83	0.43	0.40	3.24	2.03	1.21
Global government bonds	3.77	3.51	0.26	5.09	5.00	0.09
Diversified fixed-interest	1.72	4.72	(3.00)	5.06	8.50	(3.44)
Total equities	(18.46)	(17.27)	(1.19)	(21.42)	(20.44)	(0.98)
Overall portfolio gross rate of return	(6.41)	(5.63)	(0.78)	(7.07)	(6.31)	(0.76)
Less expenses	(0.12)	(0.12)	0.00	(0.38)	(0.38)	0.00
<b>Overall portfolio net rate of return</b>	<b>(6.53)</b>	<b>(5.75)</b>	<b>(0.78)</b>	<b>(7.45)</b>	<b>(6.69)</b>	<b>(0.76)</b>

14. Details of the performance in the nine-month period ending 30 September 2001 are presented in the form of a graph in the annex to this report.

## V. CURRENCY COMPOSITION

15. The majority of IFAD's commitments are expressed in Special Drawing Rights (SDRs). Consequently, the Fund's overall assets are maintained in such a way as to ensure that commitments for undisbursed loans and grants denominated in SDRs are matched, to the extent possible, 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 Dollars are matched by assets denominated in the same currency.

16. The Executive Board of the International Monetary Fund (IMF) reviews the SDR valuation basket every five years 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.

17. New units for each of the four currencies comprising the valuation basket were determined on 29 December 2000 in such a way that the value of the SDR was precisely USD 1.30291 in terms of both the old and the new units, which became effective on 1 January 2001. The units applicable, together with their weights as of 1 January and 30 September 2001, are shown in Table 6.

**Table 6: Units and Weights Applicable to the SDR Valuation Basket**

Currency	1 January 2001		30 September 2001	
	Units	Percentage Weight	Units	Percentage Weight
USD	0.577	44.3	0.577	44.9
EUR	0.426	30.4	0.426	30.2
JPY	21.000	14.0	21.000	13.7
GBP	0.0984	11.3	0.0984	11.2
<b>Total</b>		<b>100.0</b>		<b>100.0</b>

18. As of 30 September 2001, assets in the form of cash, investments, promissory notes and amounts receivable from contributors under the Fourth and Fifth Replenishments amounted to USD 2 311 142 000 equivalent (31 December 2000 – USD 2 442 485 000 equivalent), as indicated in Table 7 below.

**Table 7: Currency Composition of Assets at 30 September 2001**  
(USD '000 equivalent)

	Cash and Investments	Promissory Notes	Amounts Receivable from Contributors	Total
USD	719 342	42 090	59 050	820 482
EUR	456 328	66 983	74 577	597 888
JPY	214 156	15 403	-	229 559
GBP	212 244	23 443	-	235 687
Other	258 625	123 936	44 965	427 526
<b>Total</b>	<b>1 860 695</b>	<b>271 855</b>	<b>178 592</b>	<b>2 311 142</b>

19. Holdings of assets denominated in currencies not included in the SDR valuation basket amounted to USD 427 526 000 equivalent at 30 September 2001 (31 December 2000 – USD 388 305 000 equivalent). These are allocated to currency groups, as indicated in Table 8.

**Table 8: Allocation of Assets to Currency Groups at 30 September 2001**  
(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	820 482	152 681	-	93 961	2 106	1 069 230
EUR	597 888	-	178 778	-	-	776 666
JPY	229 559	-	-	-	-	229 559
GBP	235 687	-	-	-	-	235 687
<b>Total</b>	<b>1 883 616</b>	<b>152 681</b>	<b>178 778</b>	<b>93 961</b>	<b>2 106</b>	<b>2 311 142</b>

20. The alignment of assets by currency group against the SDR valuation basket at 30 September 2001 is shown in Table 9. The balance of the General Reserve at 30 September 2001 and the commitment for grants denominated in United States dollars on the same date amounted to USD 95 000 000 and USD 65 092 000, respectively.

**Table 9: Alignment of Assets per Currency Group with the Currency Composition of the SDR Valuation Basket at 30 September 2001**  
(USD '000 equivalent)

Currency Group	Amount per Currency Group	Less: Commitment Denominated in USD	Net Assets per Currency Group	Net Assets %	Compare SDR Weights % 30.09.2001
USD	1 069 230	(160 092)	909 138	42.3	44.9
EUR	776 666	-	776 666	36.1	30.2
JPY	229 559	-	229 559	10.7	13.7
GBP	235 687	-	235 687	10.9	11.2
<b>Total</b>	<b>2 311 142</b>	<b>(160 092)</b>	<b>2 151 050</b>	<b>100.0</b>	<b>100.0</b>

21. As of 30 September 2001, there were substantial excess euro currency group holdings and shortfalls in holdings of Japanese yen and pounds sterling and of United States dollar currency group holdings. The excess in euro currency group holdings is due partly to the receipt during the third quarter of 2001 of instruments of contribution and promissory notes relating to the Fifth Replenishment from a large number of European Member States, and partly to an overweight currency position in euro in the global government bonds portfolio. The underweight position in Japanese yen is also partly due to an underweight position in government bonds denominated in Japanese yen. The situation is expected to rectify itself to a large extent with the receipt of contributions to the Fifth Replenishment denominated in Japanese yen, pounds sterling and United States dollars.

## VI. RISK MEASUREMENT

22. The investment portfolio is subject to fluctuations in returns due to economic and market conditions. Historically, different asset classes have shown different levels of volatility, often referred to as 'risk'. Volatility is measured in terms of standard deviations of portfolio returns from their mean.

23. As of 30 September 2001, the standard deviation of IFAD's current overall policy allocation was 7.6 %, based on five years of historical monthly data. This means that, with a 67% probability, the annual return will fall within the range of +/- 7.6 % of the target rate of return.



24. Value-at-risk (VaR) is the measure of risk that IFAD uses to estimate the maximum amount the portfolio could lose over a three-month time horizon, with a 95% confidence level. Table 10 shows the VaR of IFAD's actual portfolio and current policy allocation, based on five years of historical monthly data. At 30 September 2001, the actual portfolio's VaR was notably lower than at previous quarter ends, reflecting the portfolio's currently lower equity allocation. The table also indicates that the risk associated with the actual portfolio has been consistently lower than the policy allocation.

**Table 10: Value-at-Risk (VaR)**

(Forecast horizon: three months; confidence level: 95 %)

Date	Portfolio		Policy	
	VaR %	Amount USD '000	VaR %	Amount USD '000
30 September 2001	4.9	90 800	6.3	116 300
30 June 2001	5.6	109 000	6.1	117 700
31 March 2001	5.3	100 700	6.0	114 200
31 December 2000	5.3	108 700	5.9	121 200

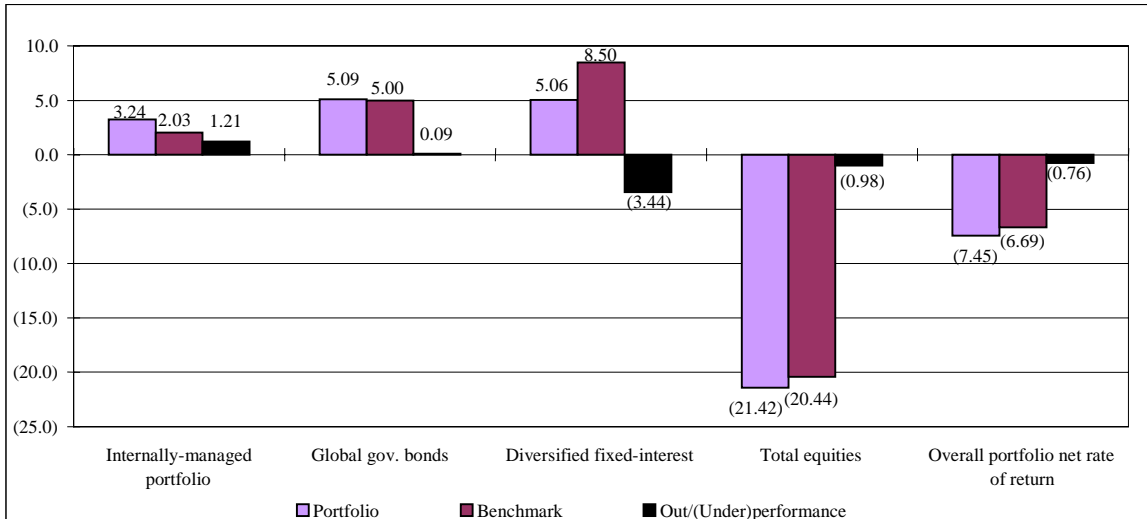






PERFORMANCE YEAR TO DATE

OVERALL PORTFOLIO



EQUITIES PORTFOLIO

