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Enabling the rural poor  
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## **Report on IFAD's investment portfolio for the second quarter of 2007**

Executive Board – Ninety-first Session  
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For: **Information**

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### **Munehiko Joya**

Treasurer

telephone: +39 06 5459 2251

e-mail: [m.joya@ifad.org](mailto:m.joya@ifad.org)

Queries regarding the dispatch of documentation for this session should be addressed to:

### **Deirdre McGrenra**

Governing Bodies Officer

telephone: +39 06 5459 2374

e-mail: [d.mcgrenra@ifad.org](mailto:d.mcgrenra@ifad.org)

# Report on IFAD's investment portfolio for the second quarter of 2007

## I. Introduction

1. This report on IFAD's investment portfolio presents final data on the second quarter of 2007. It consists of four sections: asset allocation; investment income; rate of return and performance comparison; and liquidity level in IFAD's investment portfolio. Additional information on the period's currency composition and risk measurement will become available after dispatch of this document and will be therefore included as an annex to the report on the third quarter of 2007. The present report contains an annex that provides figures for the entire first quarter of 2007.

## II. Asset allocation

2. Table 1 shows the movements affecting the investment portfolio's major asset classes during the second quarter of 2007 and compares the portfolio's asset allocation with the investment policy allocation.
3. During the period, there was a net outflow of US\$10,254,000 equivalent from the operational cash portfolio, representing disbursements for loans, grants and administrative expenses net of cash receipts and encashment of Member States' contributions.
4. Tactical short-term investments in the amount of US\$25,000,000 equivalent matured during the period. Part of the proceeds were transferred to the operational cash portfolio to cover disbursement needs, and the balance was reinvested in the held-to-maturity portfolio.
5. Changes in the portfolio's allocation ratios also reflected positive net investment income of US\$11,833,000 equivalent.
6. The net movements on foreign exchange totalled US\$3,487,000 equivalent. The United States dollar depreciated against the euro and the British pound sterling, thereby increasing the value of the portfolios including those currencies. The United States dollar appreciated against the Japanese yen, reducing the value of the inflation-indexed bonds portfolio, which is mainly hedged back to the yen.

Table 1

### Movements in cash and investments by portfolio – second quarter 2007

(Thousands of United States dollars equivalent)

	<i>Operational cash<sup>a</sup></i>	<i>Tactical short-term investments<sup>b</sup></i>	<i>Held-to-maturity</i>	<i>Government bonds</i>	<i>Diversified fixed-interest</i>	<i>Inflation-indexed bonds</i>	<i>Total</i>
Opening balance (31 March 2007)	108 108	443 328	405 837	969 798	101 702	338 978	2 367 751
Net investment income/(loss)	1 270	5 673	3 949	1 561	(654)	34	11 833
Transfers due to allocation	18 061	(25 000)	6 939	-	-	-	-
Transfers due to expenses	(646)	42	(10)	382	59	173	-
Net disbursements	(10 254)	-	-	-	-	-	(10 254)
Movements on exchange	806	617	2 785	9 152	(2)	(9 871)	3 487
Closing balance (30 June 2007)	117 345	424 660	419 500	980 893	101 105	329 314	2 372 817
Actual asset allocation	4.9%	17.9%	17.7%	41.3%	4.3%	13.9%	100.0%
Investment policy asset allocation	5.5%	-	-	49.0%	25.5%	20.0%	100.0%
Difference in asset allocation	(0.6%)	17.9%	17.7%	(7.7%)	(21.2%)	(6.1%)	-

<sup>a</sup> Cash and time deposits held with banks, readily available for disbursing loans, grants and administrative expenses.

<sup>b</sup> Short-term instruments (time deposits and commercial papers) maturing by July 2007.

### III. Investment income

7. Fixed-income products were impacted negatively during the period due to the continued tightening policy tone among all major central banks. Additionally, the performance of inflation-indexed bonds was further undermined by the upward growth trend worldwide.
8. Table 2 provides details on net investment income for the second quarter of 2007 by portfolio. Overall net investment income during the period amounted to US\$11,833,000 equivalent, contributing to a year-to-date income of US\$35,971,000 equivalent.

Table 2  
**Net investment income by portfolio – second quarter 2007**  
 (Thousands of United States dollars equivalent)

	<i>Operational cash</i>	<i>Tactical short-term investments</i>	<i>Held-to-maturity</i>	<i>Government bonds</i>	<i>Diversified fixed-interest</i>	<i>Inflation-indexed bonds</i>	<i>Total second quarter</i>	<i>Year-to-date 2007</i>
Interest from fixed-interest investments and bank accounts	1 290	2 332	4 174	10 530	1 314	3 882	23 522	44 982
Realized capital gains/(losses)	2	-	-	(4 355)	(632)	20	(4 965)	(9 021)
Unrealized capital gains/(losses)	2	3 383	-	(4 232)	(1 277)	(3 695)	(5 819)	(5 020)
Amortization/accretion <sup>a</sup>	-	-	(235)	-	-	-	(235)	6 486
Income from securities lending	-	-	56	129	13	43	241	373
<b>Subtotal: gross investment income/(loss)</b>	<b>1 294</b>	<b>5 715</b>	<b>3 995</b>	<b>2 072</b>	<b>(582)</b>	<b>250</b>	<b>12 744</b>	<b>37 800</b>
Investment manager fees	-	-	-	(399)	(56)	(172)	(627)	(1 269)
Custody fees/bank charges	(24)	(3)	(8)	(22)	(7)	(14)	(78)	(150)
Financial advisory and other investment management fees	-	(39)	(38)	(90)	(9)	(30)	(206)	(413)
Tax recoverables	-	-	-	-	-	-	-	3
<b>Net investment income/(loss)</b>	<b>1 270</b>	<b>5 673</b>	<b>3 949</b>	<b>1 561</b>	<b>(654)</b>	<b>34</b>	<b>11 833</b>	<b>35 971</b>

<sup>a</sup> A period's amortization amount represents a portion of the difference between the purchase price and the final redemption value of the held-to-maturity investments in accordance with International Financial Reporting Standards.

### IV. Rate of return and performance comparison

9. Performance is measured against pre-assigned independent benchmarks indicating the return that would be expected through passive management of defined sectors of the market. The indexes used are the J.P. Morgan customized global government bonds index for government bonds, the Lehman Brothers United States aggregate index for diversified fixed-interest bonds and the Barclay customized inflation-linked index for inflation-indexed bonds.
10. Table 3 compares the actual net return on the overall portfolio to the benchmark return. The portfolio returned 0.51 per cent during the second quarter of 2007, net of investment expenses and excluding the impact of foreign exchange movements. This represented an outperformance of 0.06 basis points against the aggregate benchmark. On a year-to-date basis the portfolio returned 1.55 percent, outperforming the benchmark by 0.07 basis points.

Table 3

**IFAD investment portfolio performance compared with benchmarks – second quarter and year-to-date 2007**

(Percentage in local currency terms)

Portfolio	Second quarter 2007 <sup>a</sup>			Year-to-date 2007		
	Rate of return		Out/(Under) performance	Rate of return		Out/(Under) performance
	Portfolio	Benchmark		Portfolio	Benchmark	
<b>Overall gross rate of return<sup>a</sup></b>	<b>0.55</b>	<b>0.49</b>	<b>0.06</b>	<b>1.62</b>	<b>1.55</b>	<b>0.07</b>
Less expenses	(0.04)	(0.04)	-	(0.07)	(0.07)	-
<b>Overall net rate of return<sup>a</sup></b>	<b>0.51</b>	<b>0.45</b>	<b>0.06</b>	<b>1.55</b>	<b>1.48</b>	<b>0.07</b>

<sup>a</sup> The overall benchmark was based on actual portfolio weights at the end of each month during the period.

**V. Liquidity level in IFAD's investment portfolio**

11. IFAD's Liquidity Policy, approved by the Executive Board in December 2006, states that IFAD's liquidity ("highly liquid assets")<sup>1</sup> should remain above the level of US\$437 million for the Seventh Replenishment period.
12. Highly liquid assets in IFAD's investment portfolio as at 30 June 2007 amounted to US\$1,523,000,000 equivalent, which comfortably clears the minimum liquidity requirement (table 4). Part of this liquidity is of a temporary nature, as approximately US\$400,000,000 equivalent tactical short-term portfolio will be maturing by July 2007 and will be reinvested more strategically under the investment policy. Thus the overall liquidity level will decrease to approximately US\$1,000,000,000 equivalent.

Table 4

**Liquidity level in IFAD's investment portfolio – as at 30 June 2007**

(Millions of United States dollars equivalent)

	Actuals	Percentage
<b>(a) Highly liquid assets</b>	<b>1 523</b>	<b>64</b>
Short-term instruments	542	23
Government securities	981	41
<b>(b) Fairly liquid assets</b>	<b>430</b>	<b>18</b>
Non-government securities	430	18
<b>(c) Partially liquid assets</b>	<b>420</b>	<b>18</b>
Held-to-maturity	420	18
<b>Total portfolio</b>	<b>2 373</b>	<b>100</b>

<sup>1</sup> Defined as being convertible to cash quickly without significant loss of value.

# Report on IFAD'S investment portfolio for the first quarter of 2007

## I. Introduction

1. This report on IFAD's investment portfolio presents final data on the first quarter of 2007. It consists of six sections: asset allocation; investment income; rate of return and performance comparison; liquidity level in IFAD's investment portfolio; composition of the investment portfolio by currency; and risk measurement.

## II. Asset allocation

2. Table 1 shows the movements affecting the investment portfolio's major asset classes during the first quarter of 2007 and compares the portfolio's asset allocation with the investment policy allocation.
3. During the period, there was a net outflow of US\$21,896,000 equivalent from the internally managed operational cash portfolio, representing disbursements for loans, grants and administrative expenses net of cash receipts and encashment of Member States' contributions.
4. Tactical short-term investments in the amount of US\$25,000,000 equivalent matured during the quarter and proceeds were transferred to the operational cash portfolio to cover disbursement needs.
5. In March 2007, held-to-maturity securities in the amount of US\$10,000,000 equivalent face value reached maturity. The redeemed amount, in addition to US\$3,066,000 equivalent representing coupon payments, was not reinvested, but transferred to the operational cash portfolio to cover disbursement needs.
6. Changes in the portfolio's allocation ratios also reflected positive net investment income of US\$24,138,000 equivalent and positive movements on foreign exchange of US\$6,907,000 equivalent as the United States dollar depreciated against major currencies.

Table 1

### Movements in cash and investments by portfolio – first quarter 2007

(Thousands of United States dollars equivalent)

	<i>Operational cash<sup>a</sup></i>	<i>Tactical short-term investments<sup>b</sup></i>	<i>Held-to-maturity</i>	<i>Government bonds</i>	<i>Diversified fixed-interest</i>	<i>Inflation-indexed bonds</i>	<i>Total</i>
Opening balance (31 December 2006)	89 574	462 351	413 501	956 055	100 540	336 581	2 358 602
Net investment income	1 016	5 909	3 821	8 533	1 271	3 588	24 138
Transfers due to allocation	39 970	(25 261)	(13 066)	-	(174)	(1 469)	-
Transfers due to expenses	(769)	46	27	428	69	199	-
Net disbursements	(21 896)	-	-	-	-	-	(21 896)
Movements on exchange	213	283	1 554	4 782	(4)	79	6 907
Closing balance (31 March 2007)	108 108	443 328	405 837	969 798	101 702	338 978	2 367 751
Actual asset allocation	4.6%	18.7%	17.1%	41.0%	4.3%	14.3%	100.0%
Investment policy asset allocation	5.5%	-	-	49.0%	25.5%	20.0%	100.0%
Difference in asset allocation	(0.9%)	18.7%	17.1%	(8.0%)	(21.2%)	(5.7%)	-

<sup>a</sup> Cash and time deposits held with banks, readily available for disbursing loans, grants and administrative expenses.

<sup>b</sup> Short-term instruments (time deposits and commercial papers) maturing by July 2007.

### III. Investment income

7. Government bond markets performed well during the period as signs of slower economic growth in the United States and higher default rates in the sub-prime mortgage sector led to flight to quality. Inflation-indexed bonds continued to benefit from inflationary concern during the quarter. Corporate bonds performed well with favourable results on investment, production and retail surveys. In the currency market, the United States dollar continued to depreciate against the euro (-1.16 per cent), the British pound sterling (-0.45 per cent) and the Japanese yen (-1.04 per cent).
8. Table 2 provides details on net investment income for the first quarter of 2007 by portfolio. Overall net investment income during the period amounted to US\$24,138,000 equivalent, to which all portfolios contributed positively.

Table 2  
**Net investment income by portfolio – first quarter 2007**

(Thousands of United States dollars equivalent)

	<i>Operational cash</i>	<i>Tactical short-term investments</i>	<i>Held-to-maturity</i>	<i>Government bonds</i>	<i>Diversified fixed-interest</i>	<i>Inflation-indexed bonds</i>	<i>Total</i>
Interest from fixed-interest investments and bank accounts	807	2 673	4 138	9 924	1 213	2 705	21 460
Realized capital gains/(losses)	200	3 282	-	(3 920)	(116)	(220)	(774)
Unrealized capital gains/(losses)	26	-	-	2 957	243	1 302	4 528
Amortization/accretion <sup>a</sup>	-	-	(290)	-	-	-	(290)
Income from securities lending	-	-	19	91	2	20	132
<b>Subtotal: gross investment income/(loss)</b>	<b>1 033</b>	<b>5 955</b>	<b>3 867</b>	<b>9 052</b>	<b>1 342</b>	<b>3 807</b>	<b>25 056</b>
Investment manager fees	-	-	-	(409)	(56)	(177)	(642)
Custody fees/bank charges	(20)	(6)	(8)	(22)	(5)	(11)	(72)
Financial advisory and other investment management fees	-	(40)	(38)	(88)	(10)	(31)	(207)
Tax recoverables	3	-	-	-	-	-	3
<b>Net investment income</b>	<b>1 016</b>	<b>5 909</b>	<b>3 821</b>	<b>8 533</b>	<b>1 271</b>	<b>3 588</b>	<b>24 138</b>

<sup>a</sup> A period's amortization amount represents a portion of the difference between the purchase price and the final redemption value of the held-to-maturity investments in accordance with International Financial Reporting Standards.

### IV. Rate of return and performance comparison

9. Performance is measured against pre-assigned independent benchmarks indicating the return that would be expected through passive management of defined sectors of the market. The indexes used are the J.P. Morgan customized global government bonds index for government bonds, the Lehman Brothers United States aggregate index for diversified fixed-interest bonds and the Barclay customized inflation-linked index for inflation-indexed bonds.
10. Table 3 compares the actual net return on the overall portfolio to the overall benchmark return. The portfolio returned 1.04 per cent during the first quarter of 2007, net of investment expenses and excluding the impact of foreign exchange movements. This represented an out-performance of 0.01 basis points against the aggregate benchmark. This was a positive performance against the negative return (0.04 per cent) in the same period of 2006.

Table 3

**IFAD investment portfolio performance compared with benchmarks – first quarter 2007**  
(Percentage in local currency terms)

Portfolio	First quarter 2007		
	Rate of return		Out/(Under) performance
	Portfolio	Benchmark	
<b>Overall gross rate of return<sup>a</sup></b>	<b>1.07</b>	<b>1.06</b>	<b>0.01</b>
Less expenses	(0.03)	(0.03)	-
<b>Overall net rate of return<sup>a</sup></b>	<b>1.04</b>	<b>1.03</b>	<b>0.01</b>

<sup>a</sup> The overall benchmark was based on actual portfolio weights at the end of each month during the period.

**V. Liquidity level in IFAD's investment portfolio**

11. IFAD's Liquidity Policy, approved by the Executive Board in December 2006, states that IFAD's liquidity ("highly liquid assets") should remain above the level of US\$ 437 million for the Seventh Replenishment period.
12. Highly liquid assets in IFAD's investment portfolio as at 31 March 2007 amounted to US\$1,521,000,000 equivalent, which comfortably clears the minimum liquidity requirement (table 4). Part of this liquidity is of temporary nature, as approximately US\$400,000,000 equivalent tactical short-term portfolio will be maturing by July 2007 and will be reinvested more strategically. Thus the overall liquidity level will decrease to approximately US\$1,000,000,000 equivalent.

Table 4

**Liquidity level in IFAD's investment portfolio – as at 31 March 2007**

(Millions of United States dollars equivalent)

	Actuals	Percentage
<b>(a) Highly liquid assets</b>	<b>1 521</b>	<b>64</b>
Short-term instruments	551	23
Government securities	970	41
<b>(b) Fairly liquid assets</b>	<b>441</b>	<b>19</b>
Non-government securities	441	19
<b>(c) Partially liquid assets</b>	<b>406</b>	<b>17</b>
Held-to-maturity	406	17
<b>Total portfolio</b>	<b>2 368</b>	<b>100</b>

**VI. Composition of the investment portfolio by currency**

13. The majority of IFAD's commitments are expressed in special drawing rights (SDRs). Consequently, the Fund's overall assets are maintained so 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 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.
14. The Executive Board of the International Monetary Fund reviews the SDR valuation basket every five years to determine which currencies should be part of the basket and what their percentage weight should be at the date of reweighting of the basket.



15. The new units for each of the four currencies composing the SDR valuation basket were determined on 30 December 2005 in such a way that the value of the SDR was precisely US\$1.42927, in terms of both the old units and the new units, which became effective on 1 January 2006. The applicable units, together with their weights as at 1 January 2006 and 31 March 2007, are shown in table 5.

Table 5  
Units and weights applicable to the SDR valuation basket

Currency	1 January 2006		31 March 2007	
	Units	Percentage weight	Units	Percentage weight
US dollar	0.6320	43.7	0.6320	41.9
Euro	0.4100	34.3	0.4100	36.1
Yen	18.4000	10.9	18.4000	10.3
Pound sterling	0.0903	11.1	0.0903	11.7
<b>Total</b>		<b>100.0</b>		<b>100.0</b>

16. At 31 March 2007, assets in the form of cash, investments, promissory notes and contributions receivable from Member States under the Fourth, Fifth, Sixth and Seventh Replenishments, net of provisions, amounted to US\$2,919,153,000 equivalent, as summarized in table 6 (compared with US\$2,865,429,000 equivalent as at 31 December 2006).

Table 6  
Currency composition of assets in the form of cash, investments and other receivables as at 31 March 2007

(Thousands of United States dollars equivalent)

Currency	Cash and investments <sup>a</sup>	Promissory notes <sup>a</sup>	Contributions receivable from Member States	Total
US dollar group <sup>b</sup>	1 136 377	94 988	145 413	1 376 778
Euro group <sup>c</sup>	709 441	141 564	85 522	936 527
Yen	266 118	23 137	15 396	304 651
Pound sterling	255 099	-	46 098	301 197
<b>Total</b>	<b>2 367 035</b>	<b>259 689</b>	<b>292 429</b>	<b>2 919 153</b>

<sup>a</sup> Includes only assets in freely convertible currencies. Excluded assets in non-convertible currencies amounted to US\$716,000 equivalent for cash and investments and US\$1,399,000 equivalent for promissory notes.

<sup>b</sup> Includes assets in Australian, Canadian and New Zealand dollars (AUD, CAD and NZD).

<sup>c</sup> Includes assets in Swiss francs (CHF), Swedish kronor (SEK) and Danish and Norwegian kroner (DKK and NOK).

17. The alignment of assets by currency group against the SDR valuation basket as at 31 March 2007 is shown in table 7. The balance of the commitments denominated in United States dollars at 31 March 2007 amounted to US\$184,549,000 equivalent, composed of the General Reserve (US\$95,000,000) and commitments for grants denominated in United States dollars (US\$89,549,000).

Table 7

**Alignment of assets per currency group with SDR valuation composition – as at 31 March 2007**  
(Thousands of United States dollars equivalent)

Currency	Asset amount	Less: commitments denominated in US dollars	Net asset amount	Net asset amount (Percentage)	SDR weights (Percentage)	Difference (Percentage)
US dollar group <sup>a</sup>	1 376 778	(184 549)	1 192 229	43.7	41.9	1.8
Euro group <sup>b</sup>	936 527	-	936 527	34.2	36.1	(1.9)
Yen	304 651	-	304 651	11.1	10.3	0.8
Pound sterling	301 197	-	301 197	11.0	11.7	(0.7)
<b>Total</b>	<b>2 919 153</b>	<b>(184 549)</b>	<b>2 734 604</b>	<b>100.0</b>	<b>100.0</b>	<b>-</b>

<sup>a</sup> Includes assets in AUD, CAD and NZD.

<sup>b</sup> Includes assets in CHF, SEK, DKK and NOK.

18. As at 31 March 2007, there was an excess allocation in United States dollar currency group holdings (+1.8 per cent) and Japanese yen (+0.8 per cent), which was offset by a shortfall in the Euro currency group (-1.9 per cent) and British pounds sterling (-0.7 per cent).

## VII. Risk measurement

19. With the exception of operational cash, tactical short-term and held-to-maturity investments, investment portfolio performance is subject to market movements. Historically, different asset classes have shown different levels of volatility, often referred to as "risk". Volatility is measured in terms of standard deviation of returns from their mean. At 31 March 2007, the standard deviation of IFAD's investment portfolio was 0.9 per cent, compared with 1.6 per cent for the investment policy.
20. Value-at-risk (VaR) is the measure of risk that IFAD uses to estimate the maximum amount that the portfolio could lose in value over a three-month time horizon, with a 95-per-cent confidence level. Table 8 shows the VaR of IFAD's investment portfolio and policy as at 31 March 2007 and for previous periods.

Table 8

**Value-at-risk (VaR)**

(Forecast horizon of three-months, confidence level of 95 per cent)

Date	Investment portfolio		Investment policy	
	VaR (Percentage)	Amount (Thousands of US dollars)	VaR (Percentage)	Amount (Thousands of US dollars)
31 March 2007	0.7	16 600	1.3	30 800
31 December 2006	0.8	18 000	1.4	32 300
30 September 2006	0.8	19 100	1.4	33 400
30 June 2006	1.1	26 500	1.5	36 200
31 March 2006	1.4	33 200	1.5	35 600
31 December 2005	1.2	28 200	1.4	32 900

21. At 31 March 2007, the investment portfolio's VaR was 0.7 per cent, slightly lower than at the previous quarter's end, and well below the investment policy VaR of 1.3 per cent. The investment policy VaR reflects the policy allocation (table 1).

