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Enabling poor rural people
to overcome poverty

Report on IFAD's investment portfolio for the third quarter of 2008

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For: **Information**

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Report on IFAD's investment portfolio for the third quarter of 2008

I. Executive summary

1. IFAD's investment portfolio performed positively during the first three quarters of 2008, with a net investment rate of return for the nine-month period of 3.18 per cent. After the slowdown in performance in the second quarter, the third quarter performed strongly despite market conditions. The year-to-date net investment income for the period amounts to US\$77,896,000 equivalent. At the end of September 2008, IFAD's investment portfolio was valued at US\$2,467,436,000 equivalent.

II. Introduction

2. This report on IFAD's investment portfolio presents final data on the third quarter of 2008. It consists of six sections covering asset allocation; investment income; rate of return and performance comparison; liquidity level; currency composition; and risk measurement in IFAD's investment portfolio. An annex to the report provides additional information pertaining to the currency composition for the second quarter of 2008.

III. Asset allocation

3. Table 1 shows the movements affecting the investment portfolio's major asset classes during the third quarter of 2008 and compares the portfolio's asset allocation with the investment policy allocation.
4. During the period, there was a net outflow of US\$36,938,000 equivalent from the operational cash portfolio, representing disbursements for loans, grants and administrative expenses net of cash receipts and encashment of Member States' contributions.
5. During the third quarter, US\$22,108,000 equivalent was transferred from the short-term tactical instruments portfolio to the operational cash portfolio. In addition, US\$8,035,000 equivalent from the held-to-maturity portfolio and US\$4,613,000 equivalent from the inflation-indexed bonds portfolio, both representing coupon payments, were transferred to the operational cash portfolio.
6. The net movements on foreign exchange totalled negative US\$124,003,000 equivalent for the third quarter of 2008, translating to a year-to-date foreign exchange impact of negative US\$48,300,000 equivalent. The third quarter movement was a result of a strong United States dollar appreciating against the euro and the British pound sterling, while remaining stable against the Japanese yen.
7. The investment portfolio value decreased from US\$2,589,991,000 equivalent as at 1 July 2008 to US\$2,467,436,000 equivalent as at 30 September 2008 in United States dollar terms. This was due to the positive investment income of US\$38,386,000 equivalent being offset by negative foreign exchange movements of US\$124,003,000 and net outflows of US\$36,938,000 equivalent.

Table 1

Movements in cash and investments by portfolio, third quarter 2008

(Thousands of United States dollars equivalent)

	<i>Operational cash^a</i>	<i>Short-term tactical instruments^b</i>	<i>Held-to-maturity</i>	<i>Global government bonds</i>	<i>Diversified fixed-interest bonds</i>	<i>Inflation-indexed bonds</i>	<i>Total</i>
Opening balance (1 July 2008)	184 758	21 979	441 272	1 117 726	427 529	396 727	2 589 991
Net investment income	1 306	128	4 080	30 185	519	2 168	38 386
Transfers due to allocation	34 756	(22 108)	(8 035)	-	-	(4 613)	-
Transfers due to expenses/income	(41)	2	(155)	54	57	83	-
Net disbursements	(36 938)	-	-	-	-	-	(36 938)
Movements on exchange	(8 206)	-	(24 818)	(74 921)	(62)	(15 996)	(124 003)
Closing balance (30 September 2008)	175 635	1 412 344	1 073 044	428 043	378 369	2 467 436	
Actual asset allocation	7.1%	-	16.7%	43.5%	17.4%	15.3%	100.0%
Investment policy asset allocation	5.5%	-	16.7%	43.2%	14.6%	20.0%	100.0%
Difference in asset allocation	1.6%	-	-	0.3%	2.8%	(4.7)%	-

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

^b Funds from the short-term tactical instruments matured during the latter part of the third quarter and were transferred to operational cash.

IV. Investment income

8. After the slowdown in the second quarter, the fixed-income markets rallied to perform positively in the third quarter of 2008. Despite the turmoil in the financial markets, IFAD's very conservative and high-quality investment portfolio benefited from investors' flight to quality, in particular the global government bonds portfolio. During the third quarter of 2008, the central banks of Japan, the United Kingdom and the United States maintained interest rates unchanged, while the European Central Bank increased its interest rate from 4.00 per cent to 4.25 per cent as inflation remained its primary concern. In the currency market, the United States dollar strongly appreciated against the euro (+12.17 per cent) and the British pound sterling (+11.65 per cent), while remaining flat against the Japanese yen (+0.15 per cent).
9. Table 2 provides details on net investment income for the third quarter of 2008 by portfolio. Overall year-to-date net investment income amounted to US\$77,896,000 equivalent, with a positive third quarter result of US\$38,386,000 equivalent.

Table 2
Net investment income by portfolio, third quarter 2008^a
 (Thousands of United States dollars equivalent)

	<i>Operational cash</i>	<i>Short-term tactical instruments</i>	<i>Held-to-maturity</i>	<i>Global government bonds</i>	<i>Diversified fixed-interest bonds</i>	<i>Inflation-indexed bonds</i>	<i>Total third quarter</i>	<i>Year-to-date 2008</i>
Interest from fixed-interest investments and bank accounts	1 331	1	4 047	10 374	4 734	5 162	25 649	77 451
Realized capital gains	6	196	-	57	3 657	4 203	8 119	23 645
Unrealized capital gains/(losses)	-	(68)	-	19 808	(7 815)	(7 114)	4 811	(22 695)
Amortization/accretion	-	-	(121)	-	-	-	(121)	(408)
Income from securities lending	-	-	193	503	201	178	1 075	3 444
Subtotal: gross investment income	1 337	129	4 119	30 742	777	2 429	39 533	81 437
Investment manager fees	-	-	-	(453)	(202)	(212)	(867)	(2 616)
Custody fees/bank charges	(33)	(1)	(9)	(25)	(24)	(21)	(113)	(328)
Financial advisory and other investment management fees	-	-	(30)	(79)	(32)	(28)	(169)	(602)
Taxes recoverable	2	-	-	-	-	-	2	5
Net investment income	1 306	128	4 080	30 185	519	2 168	38 386	77 896

^a A period's amortization/accretion 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. Towards the end of the third quarter of 2008, the Fund was advised by its custodian bank of a possible deficiency in the investments funded by the security lending collateral and managed by the custodian bank. This matter is currently under review and will be reported based on further analysis.

V. Rate of return and performance comparison

- 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 Barclays customized inflation-linked index for inflation-indexed bonds.
- Table 3 compares the actual net return on the overall portfolio to the benchmark return. On a year-to-date basis, the portfolio returned 3.18 per cent, underperforming the benchmark by 17 basis points. The portfolio returned 1.61 per cent during the third quarter of 2008, net of investment expenses and excluding the impact of foreign exchange movements. This represented an underperformance of one basis point against the aggregate benchmark.

Table 3

IFAD investment portfolio performance compared with benchmarks, third quarter and year-to-date 2008

(Percentage in local currency terms)

Portfolio	Third quarter 2008 ^a			Year-to-date 2008		
	Rate of return		Out/(Under) performance	Rate of return		Out/(Under) performance
	Portfolio	Benchmark		Portfolio	Benchmark	
Overall gross rate of return^a	1.65	1.66	(0.01)	3.33	3.50	(0.17)
Less expenses	(0.04)	(0.04)	-	(0.15)	(0.15)	-
Overall net rate of return^a	1.61	1.62	(0.01)	3.18	3.35	(0.17)

^a The overall benchmark was based on actual portfolio weights at the end of each month during the period.**VI. Liquidity level in IFAD's investment portfolio**

- IFAD's Liquidity Policy, approved by the Executive Board in December 2006, states that IFAD's liquidity ("highly liquid assets")¹ should remain above the level of US\$437 million over the Seventh Replenishment period.
- Highly liquid assets in IFAD's investment portfolio as at 30 September 2008 amounted to US\$1,248,700,000 equivalent, which comfortably clears the minimum liquidity requirement (table 4).

Table 4

Liquidity level in IFAD's investment portfolio, as at 30 September 2008
(Millions of United States dollars equivalent)

	Actuals	Percentage
Highly liquid assets	1 248.7	50.6
Short-term instruments	175.6	7.1
Government securities	1 073.1	43.5
Fairly liquid assets	806.4	32.7
Non-government securities	806.4	32.7
Partially liquid assets	412.3	16.7
Held-to-maturity	412.3	16.7
Total portfolio	2 467.4	100.0

VII. Composition of the investment portfolio by currency

- 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.
- 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 the basket is reweighted.

¹ Defined as being convertible to cash quickly and without significant loss of value.

16. 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. They became effective on 1 January 2006. The applicable units, together with their weights as at 1 January 2006 and 30 September 2008, are shown in table 5.

Table 5
Units and weights applicable to the SDR valuation basket

Currency	1 January 2006		30 September 2008	
	Units	Percentage weight	Units	Percentage weight
United States dollar	0.6320	43.7	0.6320	41.0
Euro	0.4100	34.3	0.4100	37.4
Yen	18.4000	10.9	18.4000	11.2
Pound sterling	0.0903	11.1	0.0903	10.4
Total		100.0		100.0

17. At 30 September 2008, assets in the form of cash, investments, promissory notes and contributions receivable from Member States, net of provisions, amounted to US\$2,813,156,000 equivalent, as summarized in table 6 (compared with US\$3,062,214,000 equivalent as at 31 December 2007).

Table 6
Currency composition of assets in the form of cash, investments and other receivables, as at 30 September 2008
(Thousands of United States dollars equivalent)

Currency	Cash and investments ^a	Promissory notes ^a	Contributions receivable from Member States	Total
United States dollar group ^b	1 062 335	85 822	64 121	1 212 278
Euro group ^c	838 323	67 320	55 342	960 985
Yen	309 612	17 123	-	326 735
Pound sterling	256 610	-	56 548	313 158
Total	2 466 880	170 265	176 011	2 813 156

^a Includes only assets in freely convertible currencies. Excluded assets in non-convertible currencies amounted to US\$555,000 equivalent for cash and investments, and US\$1,399,000 equivalent for promissory notes.

^b Includes assets in Australian, Canadian and New Zealand dollars.

^c Includes assets in Swiss francs, Swedish kronor, and Danish and Norwegian kroner.

18. The alignment of assets by currency group against the SDR valuation basket as at 30 September 2008 is shown in table 7. The balance of the commitments denominated in United States dollars at 30 September 2008 amounted to US\$169,945,000 equivalent, composed of the general reserve totalling US\$95,000,000 equivalent and commitments for grants denominated in United States dollars totalling US\$74,945,000 equivalent.

Table 7

Alignment of assets per currency group with SDR valuation composition, as at 30 September 2008

(Thousands of United States dollars equivalent)

<i>Currency</i>	<i>Asset amount</i>	<i>Less: commitments denominated in United States dollars</i>	<i>Net asset amount</i>	<i>Net asset amount (percentage)</i>	<i>SDR weights (percentage)</i>	<i>Difference (percentage)</i>
United States dollar group ^a	1 212 278	(169 945)	1 042 333	39.4	41.0	(1.6)
Euro group ^b	960 985	-	960 985	36.4	37.4	(1.0)
Yen	326 735	-	326 735	12.4	11.2	1.2
Pound sterling	313 158	-	313 158	11.8	10.4	1.4
Total	2 813 156	(169 945)	2 643 211	100.0	100.0	-

^a Includes assets in Australian, Canadian and New Zealand dollars.^b Includes assets in Swiss francs, Swedish kronor, and Danish and Norwegian kroner.

19. As at 30 September 2008, there was an excess allocation in British pounds sterling (+1.4 per cent) and Japanese yen (+1.2 per cent), which was offset by a shortfall in the United States dollar currency group (-1.6 per cent) and the euro currency group (1.0 per cent).
20. IFAD's Treasury Division takes active measures to bring the currency allocation more in line with the SDR basket. Despite foreign exchange conversions throughout the third quarter, the volatility in the foreign exchange market has impaired any proactive corrections.

VIII. Risk measurement

21. With the exception of operational cash 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 30 September 2008, the standard deviation of IFAD's investment portfolio was 1.7 per cent, compared with 1.8 per cent for the investment policy.
22. 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 confidence level of 95 per cent. Table 8 shows the VaR of IFAD's investment portfolio and policy as at 30 September 2008 and for previous periods.

Table 8
Value-at-risk (VaR)
 (Forecast horizon of three months, confidence level of 95 per cent)

<i>Date</i>	<i>Investment portfolio</i>		<i>Investment policy</i>	
	<i>VaR (percentage)^a</i>	<i>Amount (thousands of United States dollars)</i>	<i>VaR (percentage)^a</i>	<i>Amount (thousands of United States dollars)</i>
30 September 2008	1.4	34 544	1.5	37 012
30 June 2008	1.4	36 300	1.6	41 400
31 March 2008	1.3	35 300	1.5	39 400
31 December 2007	1.3	32 500	1.4	35 000
30 September 2007	1.4	33 900	1.4	33 900
30 June 2007	0.9	21 400	1.4	33 200
31 March 2007	0.7	16 600	1.3	30 800

^aBased on rounded figures.

23. At 30 September 2008, the investment portfolio's VaR was 1.4 per cent, lower than the investment policy's VaR of 1.5 per cent.

Report on IFAD's investment portfolio for the second quarter of 2008

I. Introduction

1. This report on IFAD's investment portfolio presents additional information on the second quarter of 2008, specifically the currency composition of the investment portfolio.

II. Composition of the investment portfolio by currency

2. 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.
3. 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 the basket is reweighted.
4. 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 30 June 2008, are shown in table 1.

Table 1
Units and weights applicable to the SDR valuation basket

Currency	1 January 2006		30 June 2008	
	Units	Percentage weight	Units	Percentage weight
United States dollar	0.6320	43.7	0.6320	38.8
Euro	0.4100	34.3	0.4100	39.6
Yen	18.4000	10.9	18.4000	10.6
Pound sterling	0.0903	11.1	0.0903	11.0
Total		100.0		100.0

5. As at 30 June 2008, assets in the form of cash, investments, promissory notes and contributions receivable from Member States, net of provisions, amounted to US\$3,022,034,000 equivalent, as summarized in table 2 (compared with US\$3,062,214,000 equivalent as at 31 December 2007).

Table 2
**Currency composition of assets in the form of cash, investments and other receivables,
as at 30 June 2008**
(Thousands of United States dollars equivalent)

<i>Currency</i>	<i>Cash and investments^a</i>	<i>Promissory notes^a</i>	<i>Contributions receivable from Member States</i>	<i>Total</i>
United States dollar group ^b	1 084 400	96 935	67 320	1 248 655
Euro group ^c	913 913	101 050	67 559	1 082 522
Yen	316 014	25 723	-	341 737
Pound sterling	275 030	-	74 090	349 120
Total	2 589 357	223 708	208 969	3 022 034

^a Includes only assets in freely convertible currencies. Excluded assets in non-convertible currencies amounted to US\$635,000 equivalent for cash and investments and US\$1,399,000 equivalent for promissory notes.

^b Includes assets in Australian, Canadian and New Zealand dollars.

^c Includes assets in Swiss francs, Swedish kronor, and Danish and Norwegian kroner.

6. The alignment of assets by currency group against the SDR valuation basket as at 30 June 2008 is shown in table 3. The balance of the commitments denominated in United States dollars at 30 June 2008 amounted to US\$172,714,000 equivalent, composed of the general reserve US\$95,000,000 equivalent and commitments for grants denominated in United States dollars US\$77,714,000 equivalent.

Table 3
**Alignment of assets per currency group with SDR valuation composition,
as at 30 June 2008**
(Thousands of United States dollars equivalent)

<i>Currency</i>	<i>Asset amount</i>	<i>Less: commitments denominated in United States dollars</i>	<i>Net asset amount</i>	<i>Net asset amount (percentage)</i>	<i>SDR weights (percentage)</i>	<i>Difference (percentage)</i>
United States dollar group ^a	1 248 655	(172 714)	1 075 941	37.8	38.8	(1.0)
Euro group ^b	1 082 522	-	1 082 522	38.0	39.6	(1.6)
Yen	341 737	-	341 737	12.0	10.6	1.4
Pound sterling	349 120	-	349 120	12.2	11.0	1.2
Total	3 022 034	(172 714)	2 849 320	100.0	100.0	-

^a Includes assets in Australian, Canadian and New Zealand dollars.

^b Includes assets in Swiss francs, Swedish kronor, and Danish and Norwegian kroner.

7. As at 30 June 2008, there was an excess allocation in British pounds sterling (+1.2 per cent) and Japanese yen (+1.4 per cent), which was offset by a shortfall in the United States dollar currency group (-1.0 per cent) and the euro currency group (-1.6 per cent).