

Document:	<u>EB 2011/103/R.33/Add.1</u>
Agenda:	<u>12(b)(ii)</u>
Date:	<u>14 September 2011</u>
Distribution:	<u>Public</u>
Original:	<u>English</u>

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Enabling poor rural people
to overcome poverty

IFAD's Investment Policy Statement

Addendum

Executive Board — 103rd Session
Rome, 14-15 September 2011

For: **Information**

IFAD's Investment Policy Statement

Addendum

1. The attention of the Executive Board is drawn to the following addendum to IFAD's Investment Policy Statement (EB 2011/103/R.33).
2. This additional information is provided in response to specific questions raised by the Audit Committee during its review of IFAD's Investment Policy Statement on 8 September 2011.

I. Asset class eligibility: comparison between IFAD and other international financial institutions

3. IFAD's investments are limited to the fixed income asset class. Each type of security within this asset class has a minimum credit rating that is broadly in line with other international financial institutions (IFIs), as shown in table 1 below.

Table 1: Eligible asset classes and minimum credit rating criteria

		IFAD	IBRD	IDA	AsDB	AsDF	AfDB	AfDF
Fixed Income	Government Developed	AA-	AA-	AA-	Member Countries	Member Countries	AA-	AA-
	Government Emerging	BBB- ^a	no rating for local currency	no rating for local currency	Member Countries	Member Countries	less stringent than AA- if local currency ^b	N/A
	Agency	AA-	AA-	AA-	Member Countries	Member Countries	AA-	AA-
	Corporate	A- ^a	AAA	AAA	A-	A-	AA-	N/A
	ABS/MBS	AAA	AAA	AAA	AAA	AAA	AAA	AAA

^a Proposed for emerging markets and corporate bonds.

^b The Finance Committee approves counterparties that are rated below the minimum rating requirements.

IBRD: International Bank for Reconstruction and Development; IDA: International Development Association; AsDB: Asian Development Bank; AsDF: Asian Development Fund; AfDB: African Development Bank; AfDF: African Development Fund
ABS: asset-backed securities; MBS: mortgage-backed securities.

4. While other asset classes such as equity investments or repurchase agreements are largely eligible and actively included within other IFIs' portfolios (as shown in table 2), IFAD's Investment Policy Statement does not allow exposure to these instruments.

Table 2: Other eligible asset classes

		IFAD	IBRD	IDA	AsDB	AsDF	AfDB	AfDF
Other asset classes	Equities	not eligible	eligible ^a	not eligible	not eligible	not eligible	not eligible	not eligible
	Repurchase agreements	not eligible	eligible	eligible	eligible	eligible	eligible	eligible
	Securities lending	discontinued in 2010	eligible	eligible	eligible	eligible	eligible	not eligible

^a Increasing equity exposure under consideration.

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II. Supplementary information on risk monitoring software

5. As stated in section IV, Risk management framework and performance measurement (EB 2011/103/R.33), a risk budgeting framework is proposed as the basis for the revised asset allocation.
6. To implement this framework, IFAD requires an enhanced risk management system that allows for continuous monitoring of risk levels in the investment portfolio, especially on an ex ante basis, in order to intervene when needed to safeguard capital security.
7. IFAD has therefore initiated a bidding process with three leading firms in the industry of risk management software tools to select a software package provider. The bidding will be completed during the first week of October. Full implementation of the risk budgeting framework is foreseen by the end of the first quarter of 2012, in conjunction with several new externally managed mandates which will come into play under the new investment policy.
8. The software will equip IFAD's Treasury Services Division with the ability to perform ex ante (i.e. predictive) risk analyses on the portfolio in order to identify risk factors by, inter alia: holding, industry sector, currency, country and credit rating, and to optimize the portfolio's risk/return profile. Furthermore, the software will allow for stress-testing (simulations) of the risk levels in the investment portfolio under several financial assumptions, including yield curve changes and currency fluctuations.
9. Through this tool, IFAD will be able to identify optimal asset allocations for the eligible asset classes and evaluate the impact of, inter alia, inclusion/exclusion of an asset class, and changes in duration and in credit floor.
10. The tool will thereby not only support potential corrective actions on investments by means of risk reductions, but also support Management's investment decisions on the basis of solid analytics.
11. Other IFIs use similar tools to support risk management decisions and investment strategies, as verified during a recent IFAD mission to IBRD, IDA and the Inter-American Development Bank.