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Food and Agriculture
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Продовольственная и
сельскохозяйственная организация
Объединенных Наций

Organización de las
Naciones Unidas para la
Alimentación y la Agricultura

منظمة
الغذية والزراعة
للأمم المتحدة

FINANCE COMMITTEE

Hundred and Eightieth Session

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Report on Investments 2019

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EXECUTIVE SUMMARY

- **Short-term Investments:** This USD 1 539 million portfolio represents mainly unspent Trust Fund balances held pending disbursements on project implementation. Funds are diversified as to type and holdings and are invested with specialized asset managers and in deposits with the BIS. In 2019, given FAO's prudent, low risk investment style and the interest rate environment in the United States, the total return was 2.44 percent, versus the benchmark of 2.20 percent, representing an excess return of 24 basis points.
- **Long-term Investments:** This USD 555 million portfolio represents the accumulated assets set aside over a period of decades to fund the Organization's share of staff-related liabilities, which amounted to USD 1 481.7 million at 31 December 2019. Compared with the USD 1 364.5 million as per year-end 2018 this represents an increase of USD 117 million. The liabilities are comprised of the Staff Compensation Plan, Separation Payment Scheme, After Service Medical Coverage (ASMC) and the Termination of Service Payment Scheme. Invested assets are 50 percent in Equities and 50 percent in Fixed Income securities. In 2019, the long-term portfolio yielded 12.80 percent, while its benchmark return was 14.04 percent, giving an underperformance of 1.24 percent. The Euro lost 2.22 percent of its value versus the USD in 2019, this negatively impacted the return of the Euro portfolio when converted into United States Dollar.
- **Investment Governance:** The strategic asset allocations for Short-term and Long-term investments are designed in close collaboration with the Organization's technical adviser, the World Bank. Asset and Liability (ALM) studies are conducted by specialized firms, reviewed by both the Advisory Committee on Investments (a committee composed of high-level experts from organizations such as the UN Joint Staff Pension Fund (UNJSPF), the Bank for International Settlements (BIS), the Asian Development Bank and Cornell University), and the internal Investment Committee with the final approval of the Director-General.

GUIDANCE SOUGHT FROM THE FINANCE COMMITTEE

- The Finance Committee is invited to take note of this information document.

Draft Advice

- **The Finance Committee took note of the Report on Investments 2019.**

1. This document is submitted to the Finance Committee for information, in accordance with Financial Regulation IX, which provides, in part, as follows: “The Director-General may invest monies not needed for immediate requirements seeking, wherever practicable, the advice of an Advisory Committee on Investments. At least once a year the Director-General shall include in the financial statements submitted to the Finance Committee a statement of the investments currently held.”

2. The Organization manages two general pools of investments: Short-term Investments, which represent mainly unspent Trust Fund balances held pending disbursements on project implementation, but can include amounts of Regular Programme Assessed Contributions received, but not yet spent during the calendar year; and Long-term Investments, which represent the accumulated assets set aside over a period of decades to fund the Organization’s share of staff-related liabilities.

Short-term Investments

3. Short-term investments consist largely of Trust Fund deposits held pending disbursement on project implementation and any cash representing the reserves of Regular Programme and other assets. The investments are managed by asset managers specialized in short-term investments: Wellington Management, the Northern Trust Company, HSBC, the World Bank and Wells Capital Management or invested in deposits with the Bank for International Settlements.

4. The market value (in United States Dollars) of the short-term portfolios at 31 December 2019 was USD 1 539 million versus USD 1 373 million at 31 December 2018.

5. The funds are invested with both external managers and deposits with the Bank for International Settlements using specific, low risk mandates to ensure preservation of capital.

6. Specific details on the mandates include:

a) Northern Trust: the Organization makes use of the Northern Trust Government Select Fund as a “liquidity fund”, investing end of day excess United States Dollars cash balances in a low risk mutual fund. The Government Select Fund consists mainly of securities issued or guaranteed as to principal and interest by the Government of the United States or by its agencies, instrumentalities or sponsored enterprises.

b) Bank for International Settlements: this is a portfolio consisting of a substantial level of staggered deposits. The Bank for International Settlements (BIS) offers the highest level of credit quality due to its structural integration with 50 central banks and monetary authorities.

c) Wellington Management: this mandate has restrictive guidelines allowing investments in only very low risk instruments or instruments fully guaranteed by the Government of the United States such as United States (US) T Bills, US government agencies and US government backed securities. The average duration is three months.

d) World Bank: similarly restrictive guidelines and tight risk limits allowing only investments in government securities, government agencies, other official entities and multilateral organization securities and high ranked bank and other financial institution obligations. The average duration is only slightly longer than Wellington at six months.

e) Wells Capital Management: this portfolio has a slightly longer average duration than Wellington and the World Bank, up to 12 months, while maintaining similarly restrictive guidelines and tight risk limits. Investments are only in government securities, government agencies, other official entities and multilateral organization securities and high ranked bank and other financial institution obligations.

f) HSBC Euro Liquidity Fund: like the Northern Trust Government Select Fund, the HSBC Euro Liquidity fund serves a similar purpose, but for temporary, very short-term excess bank balances in Euro. The Organization has traditionally had limited cash balances in Euro due to delays in the receipt of contributions. Consequently, balances invested in Euro remained proportionally low throughout 2019.

7. The breakdown of invested short-term portfolio assets is as per the below table with a comparison with the previous year.

	At 31 December 2018	At 31 December 2019
NT Government Select Fund	26,718,213.83	49,222,409.00
Bank for International Settlements	595,883,258.78	644,220,862.00
Wellington AM	310,411,629.65	348,120,121.00
World Bank	259,518,212.07	306,104,606.00
Wells Capital Management	155,993,356.38	160,447,777.00
HSBC EUR Liquidity Fund*	24,572,296.91	31,313,781.99
Total	1,373,096,967.62	1,539,429,556.99

*Fund is in EUR. Values are converted at the 31 Dec UN Rate. For 2019, EUR 28 057 148,66 converted at the 31/12/2019 UN Rate

8. The overall return on the Short-term Investment portfolio was 2.44 percent in 2019 versus the benchmark return of 2.20 percent, indicating an excess return of 0.24 percent.

9. Both Absolute and excess return have increased over recent years, thanks to the positive interest rate in the United States. Individual manager returns are broken down by portfolio in the following table.

2019 Short Term Portfolio Return

Actively Managed

Manager	Wells Capital Management	2.96%
<i>Benchmark</i>	<i>ICE Bofa Merrill Lynch U.S. Treasury Notes & Bonds, 0-2 Yr Index</i>	<i>2.90%</i>
Manager	World Bank	2.67%
<i>Benchmark</i>	<i>ICE Bofa Merrill Lynch U.S. Treasury Notes & Bonds, 0-1 Yr Index</i>	<i>2.57%</i>
Manager	Wellington Management	2.46%
<i>Benchmark</i>	<i>ICE Merrill Lynch 3 Month T-Bills</i>	<i>2.28%</i>

Deposits and Liquidity Funds

Manager	Northern Trust Liquidity Fund	2.07%
Institution	BIS	2.21%
<i>Benchmark</i>	<i>1 Month T-Bills</i>	<i>2.20%</i>

TOTAL ST PORTFOLIO

Portfolio Return (weighted average of all short term asset returns)	2.44%
Benchmark Return (1 Month T-Bills)	2.20%
Excess Return (portfolio return over benchmark)	0.24%

Risk Management of the Short-term Portfolio

10. The primary objectives of the Organization's short-term investment policy in order of importance are: security of principal, liquidity, rate of return. The Organization has further defined "low-risk" as the maximum risk allowed where the probability of any negative return over twelve months is statistically negligible. While there are many risk metrics the Organization follows when managing its short-term investments, three key factors used to measure and manage investment risk are; duration, credit risk and diversification.

- a) Duration is a measure of a bond's sensitivity to changes in interest rate. The lower the duration, the lower the sensitivity and thus volatility in returns.
- b) Credit risk is the measure of a bond's likelihood to default on payment. The better the rating, the lower the likelihood of default. Using Standard and Poor's ratings, AAA is the highest

rating possible (and the rate of current United States Government debt), BBB is defined the lowest rating where security can still be considered “investment grade”. D is the lowest rating and stands for default. The average Short-term portfolio rating is AAA/AA

- c) Diversification: within the United States Dollar denominated high quality fixed income, the portfolio is diversified across issuers, duration and credit rating

11. While external managers are allowed some divergence from the parameters that define the authorized credit ratings and duration of securities in their mandates, the Organization’s strategy is to maintain an overall weighted average duration of approximately three months. A diversified portfolio with a limited duration using highly rated instruments allows FAO to maximize income while capping risk at a low and acceptable level. An asset and liability study was conducted in 2018 to confirm the appropriate duration within the new interest rate environment, given FAO's risk tolerance. The Investment Committee has reviewed this and presented its considerations to management. The table below depicts the results of the Organization's risk management strategy, showing the diversification of assets by manager, the weighted average duration of the portfolio as well as the average credit rating of the portfolio at 31 December 2018. Results exclude the HSBC Euro Liquidity Fund.

	Weight in Portfolio	Duration	Weighted Average duration	Average Credit Rating (S&P Scale)
NT Government Select Fund	3.26%	-	0.000	N/A
Bank for International Settlements	42.72%	0.03	0.013	N/A
Wellington AM	23.08%	0.19	0.044	AA/A
World Bank	20.30%	0.51	0.104	AAA/AA
Wells Capital Management	10.64%	0.93	0.099	AAA/AA
Total			0.26	AAA/AA

Long-term Investments

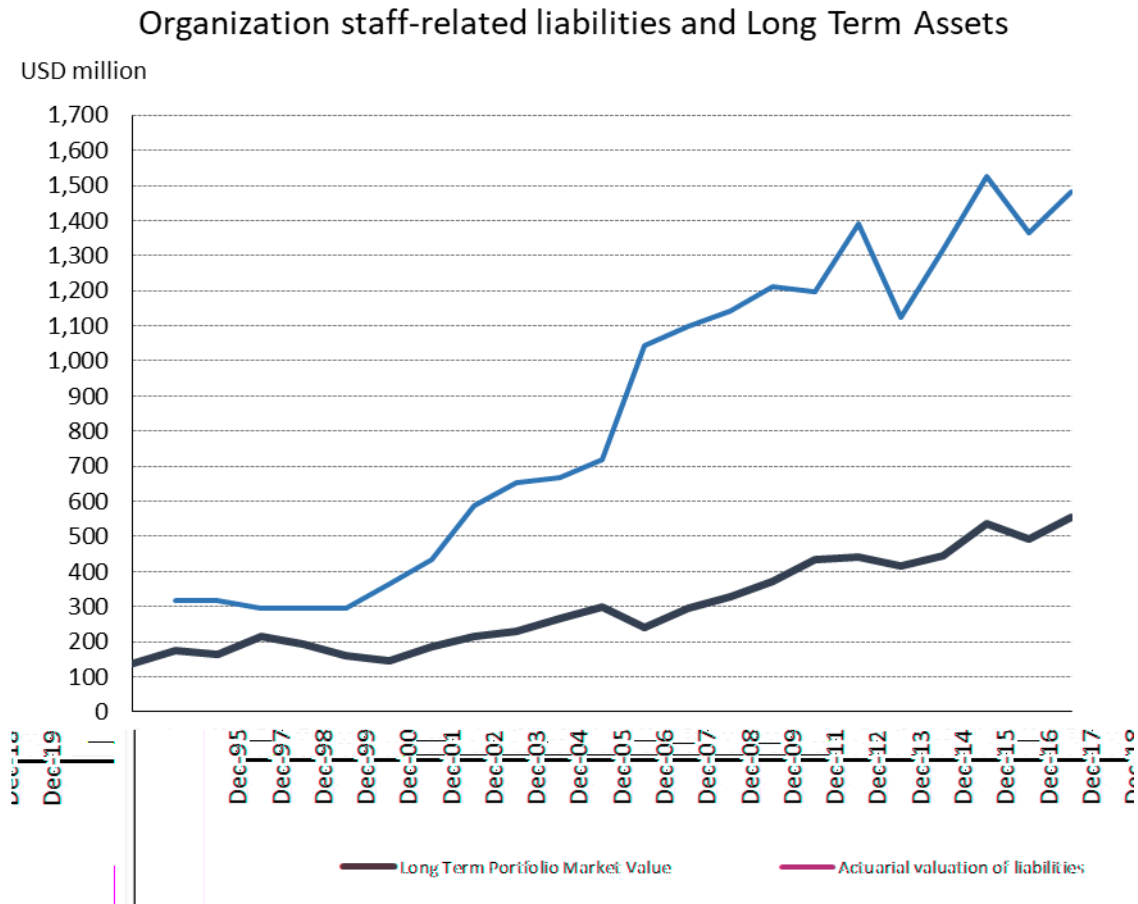
12. The long-term investment portfolio represents an accumulation in the value of securities and re-invested income over more than 30 years.

13. The principal objective of the portfolio is to fund the Organization’s share of staff-related liabilities:

- 1) Staff Compensation Plan – Provides benefits in the event of injury, illnesses or death attributable to the performance of official duties.
- 2) Separation Payment Scheme – In conformity with the Flemming principle adopted in the UN system regarding local employment conditions, this scheme for General Service staff is similar to the separation scheme provided under Italian labour legislation.
- 3) After Service Medical Coverage (ASMC) – A medical insurance plan for eligible retired staff and their families where the cost of insurance is shared between the retiree and the Organization.

4) Termination of Service Payment Scheme – Consists of benefits payable to staff upon separation from service; Repatriation Grant, Repatriation Travel and Removal, Commutation of Accrued Leave, Termination Indemnity.

14. The chart below shows the evolution of the market value of the long-term investment portfolio since 1995 compared with the actuarial valuation of the staff-related liabilities (since 1997).



15. An actuarial valuation of these liabilities has been performed each biennium since 1996-97. The last valuation as of 31 December 2019, carried out by a specialized firm, placed the Organization’s share of total staff-related liabilities at USD 1481.7 million, USD 117 million above the figure for 2018 of USD 1364.5 million. Staff-related liabilities are presented to the Finance Committee in document FC 180/4 2019 Actuarial Valuation of Staff Related Liabilities.

16. Of the total USD 1481.7 million of all staff-related liabilities, USD 1 348.2 million represented the liability of After Service Medical Coverage (ASMC). The Conference authorized biennial funding towards the past-service ASMC liability of USD 14.1 million in 2016-2017. The same amounts were authorized in 2004-2005, 2006-2007, 2008-2009, 2010-2011, 2012-2013, 2014-2015 and 2016-17.

17. No ASMC Funding was included in the biennial budget for 2018-2019.

18. The asset allocation of the portfolio provides for a 50/50 ratio between equities and bonds. In 2018, an asset and liability study was conducted to reconfirm the most appropriate asset allocation given the objectives of the long-term assets and FAO's risk tolerance. The Investment Committee has reviewed the results of this study and has proposed a review of the current asset allocation to the Director-General.

19. The market value of the asset allocation as at 31 December 2019 is shown below:

2019 Long Term Portfolio Asset Allocation

Manager	% Portfolio	Assets USD
Equity		
PanAgora AM	52.19%	289,849,144.00
Fixed Income		
LGT AM	19.08%	105,974,456.00
BNP AM	28.73%	159,582,679.00
TOTAL LT PORTFOLIO		555,406,279.00

values at 31/12/19

20. This portfolio is rebalanced if the weights of the individual equity and fixed income portions deviate more than +/- 5 percent from the established 50 percent thresholds.

21. The measurement of performance is by comparison with the following benchmarks:

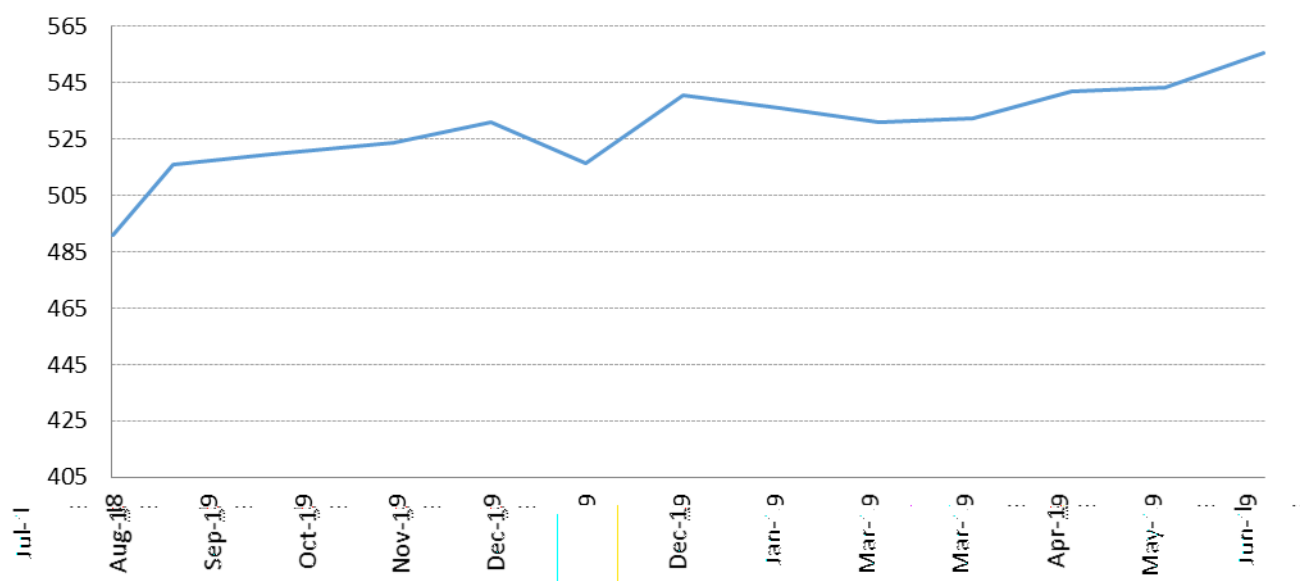
- For the equity portfolio: 80 percent The Morgan Stanley Capital International Inc All Country Index + 20 percent The Morgan Stanley Capital International Inc Emerging Markets Index;
- For the fixed income portfolio:
 - For the mandate awarded to LGT , A blend of 80 percent Barclays World Government Inflation Linked Bonds Index + 20 percent and ICE Merrill Lynch EMU Direct Government AAA Bonds Index;
 - For the mandate awarded to BNP, A blend of 55 percent Barclays World Government Inflation Linked Bonds Index + 15 percent and ICE Merrill Lynch EMU Direct Government AAA Bonds Index + 15 percent Barclays EU Credit Corp + 15 percent Barclays US Credit Corp.

22. These benchmarks fairly represent the geographical and sector allocation of the portfolio and have been reviewed by the Investment Committee and by the Organization's investment technical advisor, the World Bank.

23. During the year the Long-term investments increased from USD 491 million to USD 555 million, the Chart below illustrates the evolution of the long-term investment portfolio in 2019.

2019 - Long Term Portfolio Market Values

USD Millions



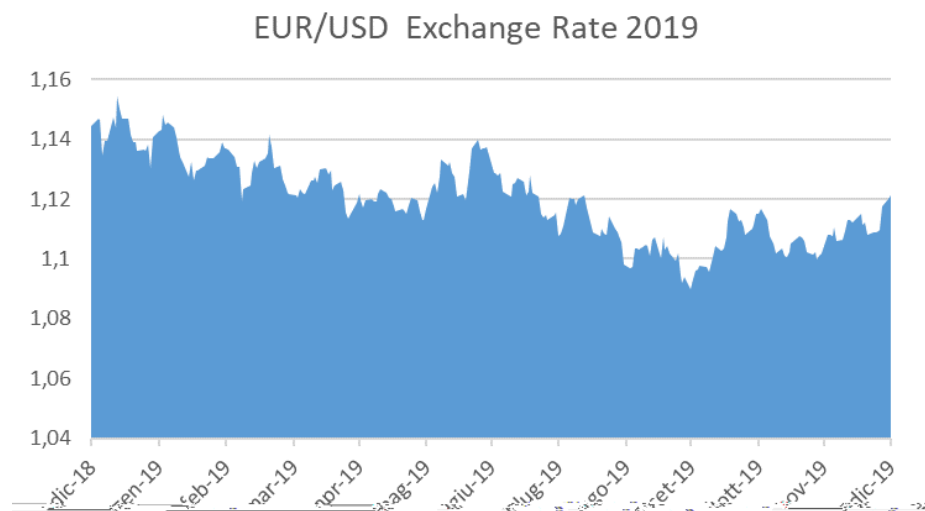
24. The overall performance of the long-term investments for 2019, represented in United States Dollars was 12.80 percent versus the benchmark return of 14.04 percent, representing an underperformance of - 1.24 percent. Detailed performance of each individual portfolio against its appropriate benchmark is shown in the table below.

2019 Long Term Portfolio Return

Equity, USD Denominated		USD RETURNS	EUR RETURNS
Manager	PanAgora AM	22.53%	
<i>Benchmark</i>	<i>80% MSCI World Index + 20% MSCI Emerging Markets Index</i>	25.37%	
Fixed Income, EUR Denominated			
Manager	LGT AM	2.95%	4.84%
<i>Benchmark</i>	<i>80% Barclays World Gov't Inflation Link'd +20% ICE Merrill Lynch EMU Direct Gov't AAA Bond Index, hedged to EUR</i>	3.03%	4.93%
Manager	BNP AM	4.40%	6.32%
<i>Benchmark</i>	<i>55% Barclays World Gov't Inflation Link'd + 15% ICE Merrill Lynch EMU Direct Gov't AAA Bond Index + 15% Barclays EU Credit Corp + 15% Barclays US Credit Corp, hedged to EUR</i>	4.12%	6.04%
TOTAL LT PORTFOLIO USD RETURN		12.80%	
Portfolio Return (weighted average of equity and fixed income portfolios)		12.80%	
Benchmark Return (weighted average of equity and fixed income portfolio benchmarks)		14.04%	
Excess Return (portfolio return over benchmark)		-1.24%	
<i>EUR/USD Annual Performance</i>			-2.22%
Bloomberg closing values at 31/12/19			

25. The fixed income portfolios are denominated, managed and measured in Euro. This is because the underlying ASMC liability has a substantial Euro component and it is important to match, to the extent possible, assets and liabilities in long-term portfolios. The investment returns as measured in Euro are actually better than the United States Dollar converted returns. This is due to the fact that the

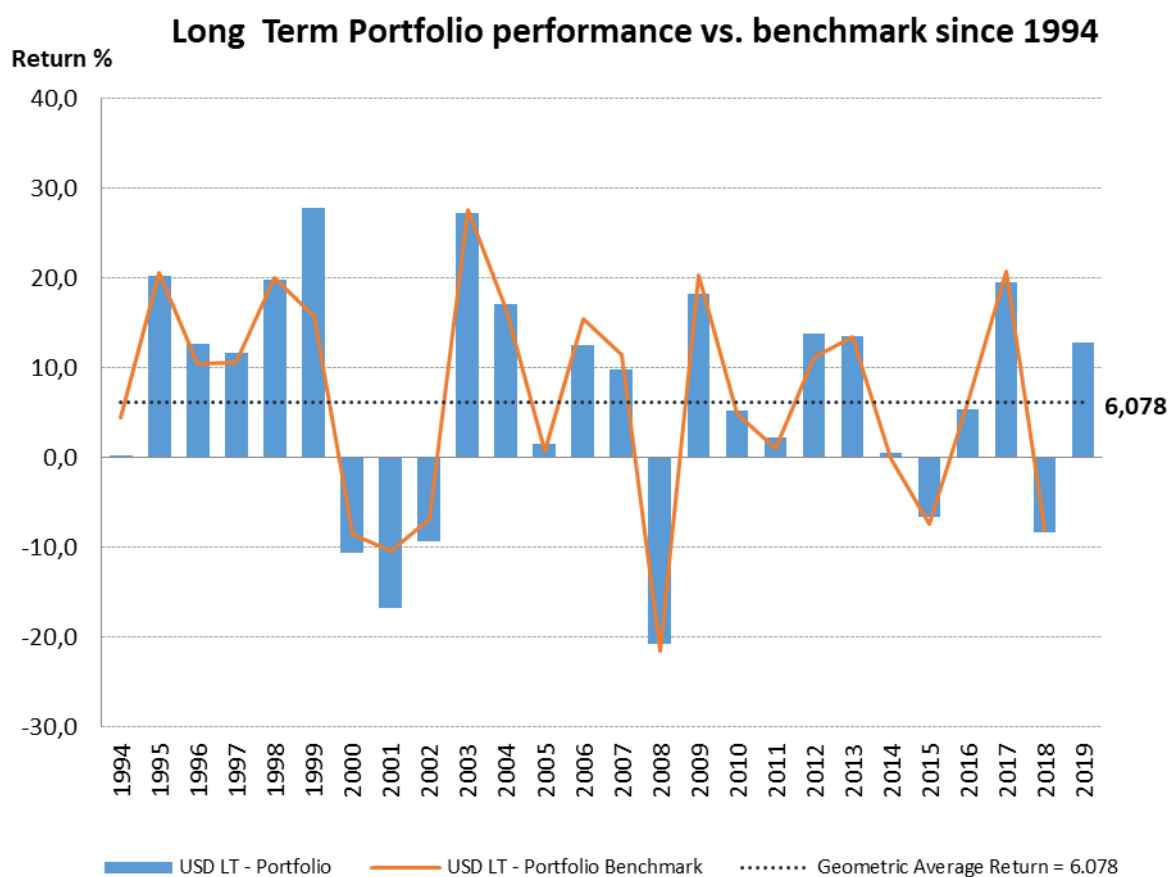
Euro depreciated approximately 2.22 percent over the year. This depressed the value of the Euro investments when measured in United States Dollars. However, it is important to point out that the Euro depreciation would have a similar effect on liabilities, leading to a relative decrease in their value when measured in United States Dollars.



26. While annual performance versus the benchmark is an important measurement, such investments have a much longer time horizon to achieve their objectives. The Organization closely monitors investment performance over several years and several market cycles to filter out the short-term volatility and understand the longer-term trends of the chosen investment styles and objectives. In the market returns, shown below, it will be noted that the current mandates have returned 3.96 percent (based in United States Dollars) since inception.

2019 Long Term Portfolio Return								
		Market Value USD, 000s	Weight in Portfolio	2019 USD RETURNS	2019 EUR RETURNS	3Y USD RETURNS	5Y USD RETURNS	Since Inception RETURNS
Manager	PanAgora AM	289,849.14	52.19%	22.53%		10.49%	7.21%	6.30%
	<i>Benchmark</i>			25.37%		12.31%	8.07%	5.17%
Manager	LGT AM	105,974.46	19.08%	2.95%	4.84%	3.65%	0.16%	0.64%
	<i>Benchmark</i>			3.03%	4.93%	3.45%		
Manager	BNP AM	159,582.68	28.73%	4.40%	6.32%	4.13%	0.91%	1.06%
	<i>Benchmark</i>			4.12%	6.04%	3.92%		
TOTAL LT PORTFOLIO USD RETURN		555,406.28		12.80%		7.33%	4.00%	3.96%
Consolidated LT Benchmark				14.04%		8.13%	4.45%	3.71%

27. The table below shows the annual returns of all long-term invested assets (current and prior mandates) since 1994 compared with their benchmarks. As is evident, returns have closely mirrored their benchmarks during the past twenty-five years. The dotted line represents the geometric mean, or average return over this period.



Risk Management of the Long-term Portfolio

28. Like the short-term investments, the long-term investments have a rigorous risk management structure in place. To complement risk reporting provided by external managers, the Organization recently implemented a risk management service with its custodial bank, Northern Trust that provides independent monthly reporting on the risk factors affecting the portfolio. This detailed report allows CSF to deconstruct the portfolios to measure:

- a) Sources of risk: asset allocation, security selection, over/underweight sectors/regions, duration, currency, etc.
- b) Mitigations of risk: diversification benefits (sector, style, duration structure), correlation, or decorrelation between portfolios.
- c) Scenario testing: the portfolios are stress tested to see how they would react under various real past scenarios to gage the potential Value at Risk (VAR), should similar market shocks happen today.
- d) The Organization will continue to develop its risk management structure to ensure that funds are managed most closely aligned to its liabilities. Monthly reports to the Investment Committee will highlight changes in any risk factors. In addition, the Treasury Unit carries out quarterly calls to investment managers and annual compliance visits.

Investment Expenses

29. The costs associated with management of the short- and long-term investments are detailed below. The most significant fees are those associated with the external management of the portfolios. These fees are calculated based on an agreed percentage of assets under management, changing as the value of the underlying assets change. A renegotiation of fees with one of the short-term portfolio managers resulted in a saving of USD 50 000 over the year.

30. The overall expense ratio for the management and oversight of the investments in 2019 was 0.125 percent, lower than the ratio in 2018 of 0.142 percent. Although expenses were reduced by just over USD 14 000, the ratio improved as asset under management increased by USD 230 million, leading to lower relative costs.

Investment Service Provided	2019 Expenditures in USD
Management, custodial and advisory fees	1,910,786.22
Treasury staffing (three professional posts)	629,128.03
Advisory Committee on Investments Meetings, Investor compliance and Training Costs	40,248.46
Bloomberg Terminals	44,775.00
Total Expenses	2,624,937.71
Total Assets at 31/12/2019	2,094,835,835.99
Total Expense Ratio	0.125%

Investment Governance at FAO

31. A detailed strategic asset allocation review for Long-term investments is conducted by specialized firms within the context of an Asset and Liability study (ALM). Reviews are conducted approximately every five years. This most recent study was conducted at the end of 2018, which confirmed that the Organization's portfolio is very close to the "efficient frontier". The ALM conclusions suggested minor changes in the asset allocation to improve possible performance without increasing risk levels. The ALM results have been reviewed by the Investment Committee and a suggestion for the implementation of a new asset allocation is being considered by Senior Management.

32. Short-term asset allocation strategies are designed in close collaboration with FAO's technical investment adviser, the World Bank. A review carried out by the World Bank in 2018 suggested a lengthening of the overall duration from three months to six months could improve returns at no additional risk. Implementation of this duration extension would require a change in the investment strategy, which is currently under review by Senior Management.

33. As indicated in paragraphs 31 and 32, the results of asset allocation studies are reviewed by FAO's internal Investment Committee. Final recommendations are forwarded to the Director-General for approval. The Investment Committee is made up of the heads of finance, budget, legal, audit, the treasurers of IFAD and WFP and is chaired by the Assistant Director-General of Corporate Services (CS).

34. The Organization also seeks investment advice from the Advisory Committee on Investments in accordance with Financial Regulation 9.1. The ACI is an external committee composed of high-level experts from organizations such as the UNJSPF, Cornell University, BIS and the Asian Development Bank.

35. The management of assets in the equity and fixed-income markets is carried out by specialized external asset managers in accordance with FAO's detailed written guidelines. These managers are chosen through open, international calls for tender with a final selection process carried out with the assistance of the World Bank.

36. Day-to-day control over the external managers, including daily compliance monitoring, is carried out by the Organization's Treasury unit in the Finance Division. The Treasury unit also provides regular reporting to the Director of Finance, internal Investment Committee and Senior Management. On-site compliance visits and quarterly compliance calls to the external asset managers and the securities custodian are carried out by the Treasury Unit.

37. Finally, a detailed report on FAO's investments is provided annually to the Finance Committee. This report is available on the internet website of the Finance Committee.