

**SUBJECT: INVESTMENT COMMITTEE CHAIR REPORT**

**Category: For Information**

### **Section A: Introduction**

- This report provides the Board with an overview of the macro economic environment and the activities of the Investment Committee since the Board last met in December 2016. The Investment Committee met in February and May 2017.
- The update includes year-to-date April 2017 performance figures for the long-term portfolio as well as the ultra-low and short duration fixed income strategies overseen by the Investments team. Gavi uses both active and passive investment managers.
- Declining unemployment and higher consumer spending are key signs that the global economy continues to pick up strength in the first half of 2017. The April World Economic Outlook report published by the IMF reported a 3.1% global growth rate in calendar year 2016. Its global growth estimates for 2017 and 2018 are 3.5% and 3.6%, respectively.
- While political challenges are still a factor, the Macron victory in France sealed the outcome of a series of key electoral challenges that could have negatively impacted market momentum and global economic growth. Markets have shifted their focus back to corporate earnings and key economic statistics. The current outlook for economic growth is supportive for global equities and much is debatably priced into current valuations. Equity performance continues to vary by region. For example, in contrast to 2016, European equities this year are outpacing US equities, particularly in USD terms.
- With growing confidence in the US economy, the US Federal Reserve has signalled another near term rate increase, likely at its June meeting. If enacted it would be the third in a 6-month period, and only the fourth rate increase since the 2008 financial crisis. In addition, the Fed may also start to reduce its balance sheet by re-investing only a portion of maturing assets (US Treasury and mortgage-backed securities). The European Central Bank is expected to follow suit but it is unlikely it will take similar action before 2018.
- Another defining feature of 2017 is the weakness of the US Dollar relative to other major currencies. The euro has been particularly strong against the US dollar in 2017.

- We have to recognise that year-to-date market volatility has been low despite a number of geopolitical factors which might normally raise volatility. While Gavi's portfolios are conservatively oriented relative to its institutional peers, the Investment Committee remains mindful of the Board's risk appetite, and the need for the portfolios to support programmatic and administrative outlays when needed.
- The total portfolio reported for this update is US\$ 1.8 billion of which US\$ 1.0 billion is invested in the short-term portfolio and the remaining US\$ 0.8 billion in the long-term portfolio. As a reminder, these figures do not include monies in the UNICEF Procurement Account or any IFFIm assets.
- The short-term portfolio includes donor contributions that will not be spent within the next 6 to 9 months as well as redemption proceeds from the long-term portfolio. It is invested in high quality, liquid strategies such as ultra-low and short duration fixed income. The 2017 year-to-date return of the short-term portfolio is 0.5%.
- The long-term portfolio has 4 major allocations: Fixed income, equity, tactical, and multi-exposure. The portfolio has traditionally had a large allocation to fixed income. However, in Q3 2016 the Committee reviewed and implemented a set of modestly revised target allocations across the long-term portfolio. The principal conclusion was to reduce directional fixed income exposure in recognition that the 30 year bull market in bonds provided little upside from current valuations. The multi-exposure category which provides tactical and managerial flexibility to invest across different asset classes is intended to be the principal beneficiary. The portfolio remains underweight in its target multi-exposure category, and the Investments team continues to conduct due diligence on multi-exposure strategies to present to the Investment Committee, in order to put the long-term portfolio on a course to meet its asset allocation targets.
- In 2017, the Investments team created a policy benchmark that would allow it to measure the actual long-term portfolio against a policy portfolio—a portfolio based on benchmarks weighted at the target allocations. Year-to-date through April month end 2017, the long-term portfolio outperformed the policy benchmark, 4.7% versus 3.7%.
- The Investment Committee's focus is to ensure the portfolios' risk levels are appropriate for Gavi's risk appetite. Before recommending an investment manager, the Investments team conducts due diligence on their firm, their strategies, and staff. If the manager is approved, then a core set of activities ensues: quarterly performance reviews, quarterly compliance questionnaires, a semi-annual Socially Responsible Investment (SRI) review (if relevant), an annual audited financial statements review and an annual internal controls review. The team regularly reports to the Investment Committee on their activities and analysis.
- The Investment Committee charter underwent a review in 2016 as part of broader review associated with the Board and Committee self-evaluation

process. There are additional edits proposed in order to keep it consistent with other Gavi charters. The Investment Committee expects to review the final version at its next meeting in August 2017.

- Key vendors undergo periodic review for their fees and scope of services. In May, Gavi issued a request for proposal for a global custodian, whose primary responsibilities are to provide the official books and records for Gavi's investments, and to assist in investment transactions.
- The Investment Committee's priorities centre on evaluating various threads of risk: market, liquidity, and reputational. Internal Audit conducted their first audit of investment management processes starting in 2015. All issues identified during the audit have been closed. Internal Audit subsequently assigned a low risk rating to investment management processes during their last annual risk assessment exercise
- The Investment Committee also actively participates in reviews of recommended investment managers as part of the transition process for the long-term portfolio. Specifically, investment managers of strategies that have never been used in Gavi's portfolios require particular attention.
- The Investment Committee Chair report is attached in the form of a presentation as Annex A.

### **Annexes**

Annex A: Investment Chair report (PowerPoint)

# INVESTMENT COMMITTEE CHAIR REPORT

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BOARD MEETING

**Stephen Zinser**

14-15 June 2017, Geneva, Switzerland



Reach every child

[www.gavi.org](http://www.gavi.org)

# SUMMARY

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- **Macro Environment and Market Commentary**
- **Portfolio and Performance Review**
- **Key Highlights 1H2017**
- **Key 2H2017 Priorities**

# MARKET SENTIMENT: REMAINS POSITIVE

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**European anti-establishment and populist movements in remission but not to be dismissed:** After a sweeping Macron victory, broader positive market sentiment emerged around European economic conditions.

**Markets factored in US fiscal expansion and structural reforms even though benefits are yet to be observed:** Pro-business sentiment continues to propel US market despite limited implementation.

**US and European central banks reduce their market intervention:** Huge asset purchases supported markets and provided liquidity but those programmes are approaching the wind-down phase.

# MARKET COMMENTARY

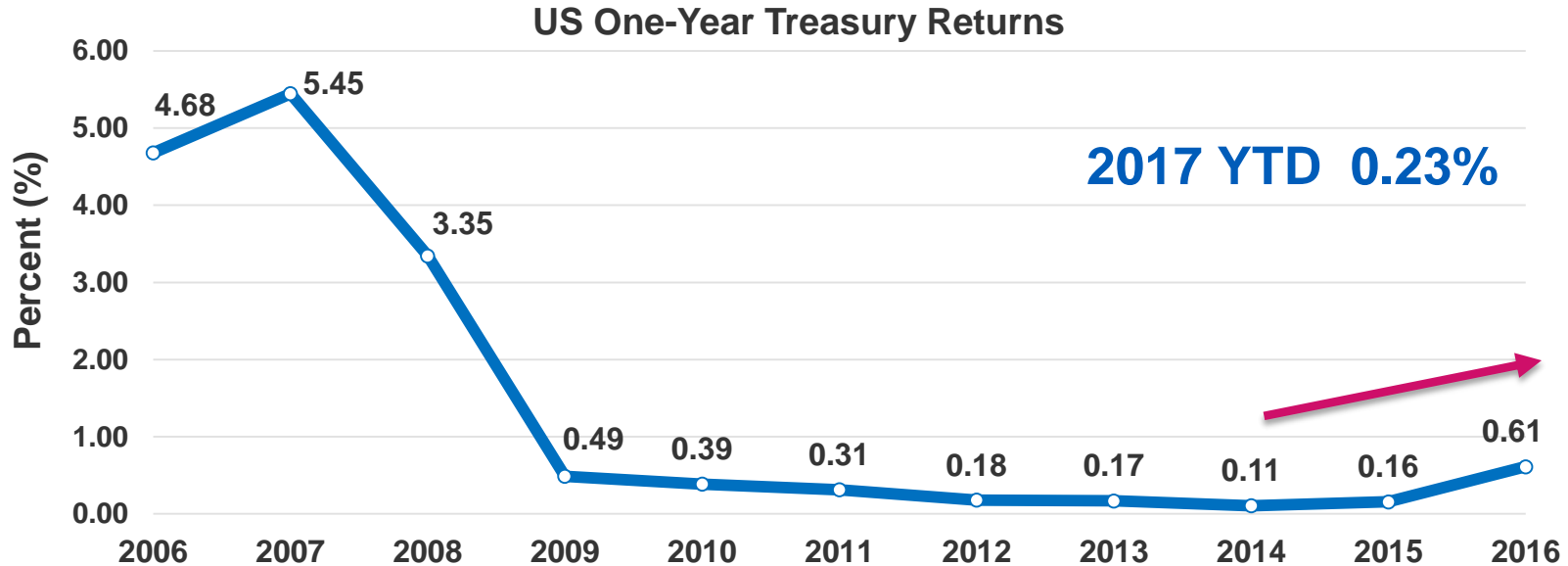
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**Equity markets:** European markets outperformed US markets on a year-to-date basis. Emerging markets, which initially suffered after the US election, enjoyed stellar performance.

**Fixed income:** Markets rewarded higher risk despite full valuations. Emerging markets fixed income enjoyed very strong performance.

**Currencies:** Strong exchange rates often are indicators of economic strength. The US dollar enjoyed dominance in 2014 through 2016 but has waned in 2017. In particular, the euro has gained against the US dollar year-to-date.

# CASH IS NO LONGER TRASH

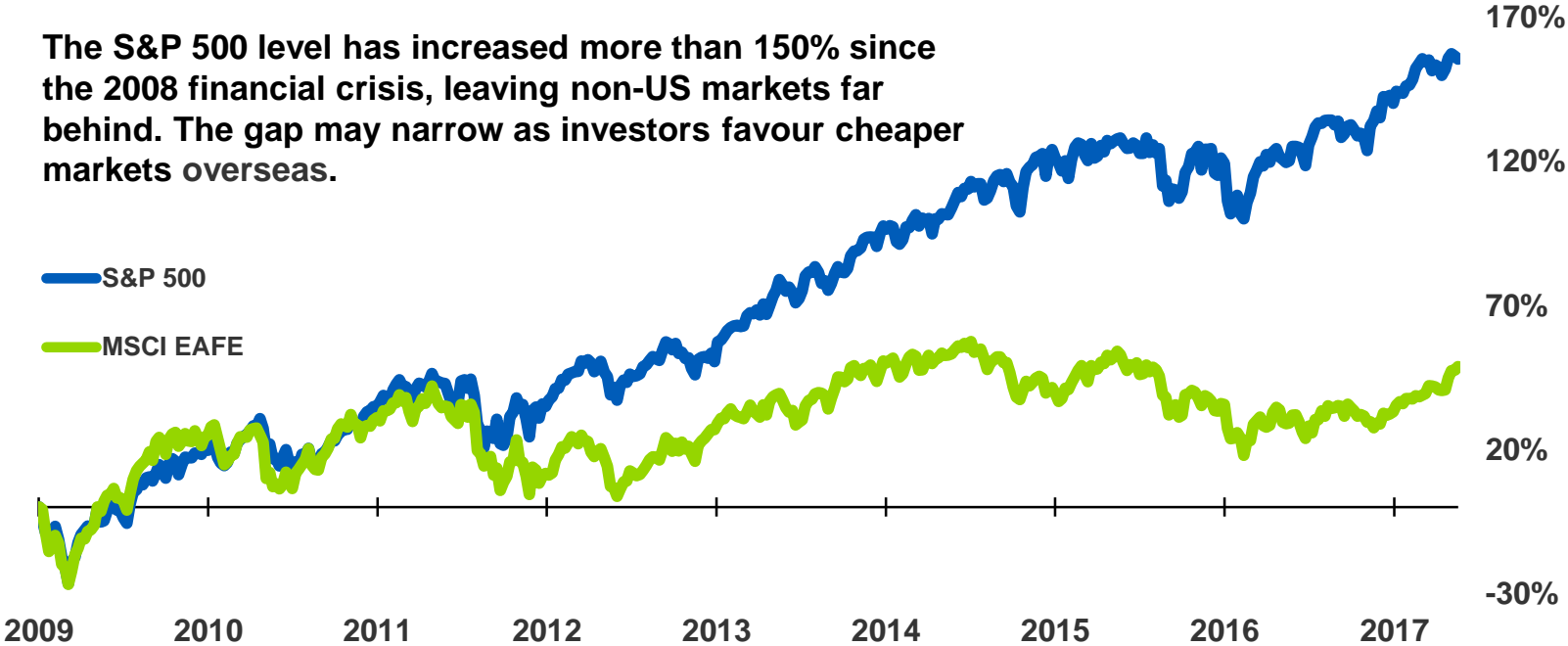


Data as of 31 May 2017  
Source: Bloomberg



# MIND THE GAP

The S&P 500 level has increased more than 150% since the 2008 financial crisis, leaving non-US markets far behind. The gap may narrow as investors favour cheaper markets overseas.



Data as of 22 May 2017  
Source: Bloomberg

# TOP 5 CONSTITUENTS: US VS NON-US

The top five constituents of the S&P 500 are supercharged tech stocks while the EAFE's leaders are conservative, relatively steady stocks.

S&P 500 (US)	Index Weight	MSCI EAFE (Non-US)	Index Weight
Apple	3.93%	Nestle	1.84%
Alphabet	2.72%	Roche Holding	1.40%
Microsoft	2.59%	Novartis	1.29%
Amazon.com	1.83%	HSBC Holdings	1.25%
Facebook	1.72%	Toyota Motor	1.02%

# PORTFOLIO OBJECTIVES

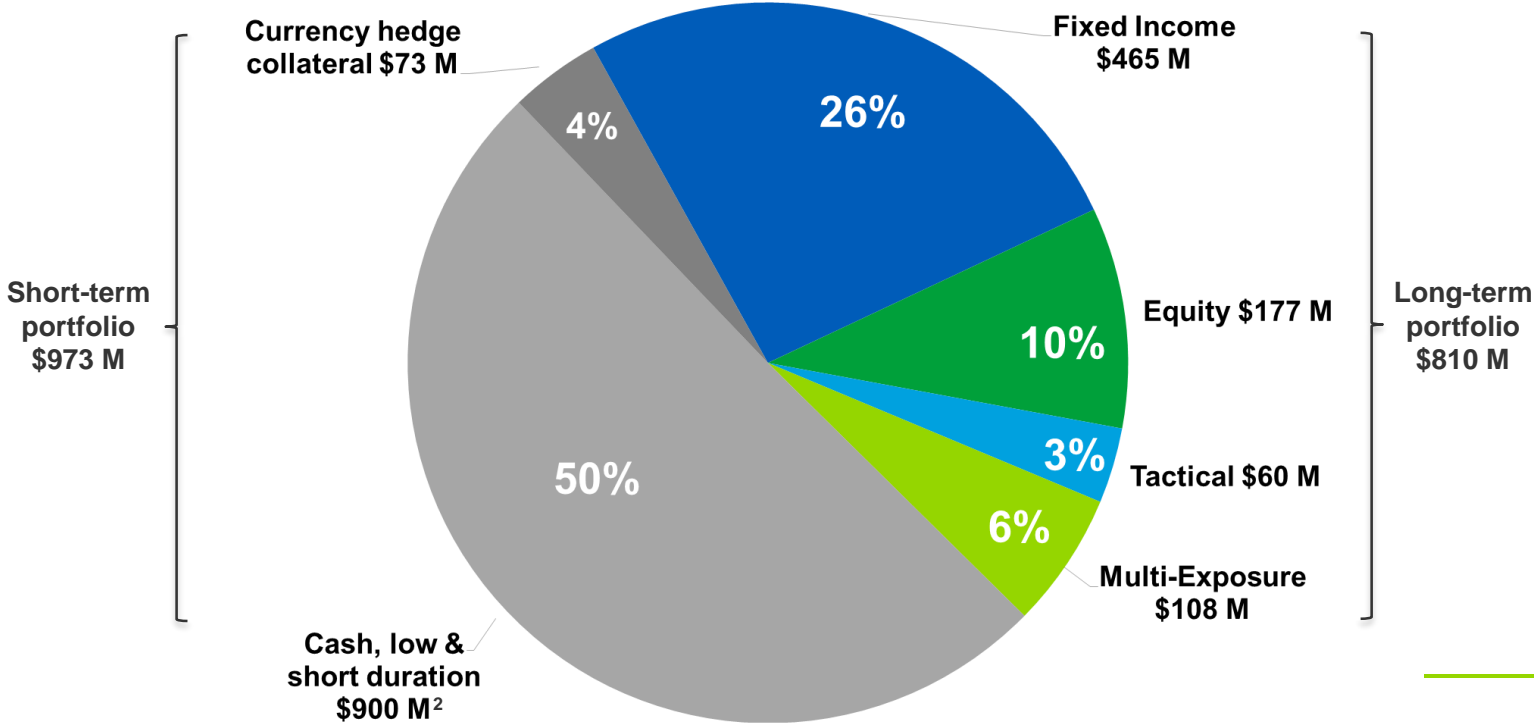
## Short-term

- Maintain **liquidity** to meet anticipated operating requirements.
- Provide for prudent diversification of investments to minimise credit and market risk exposure.
- Generate income.

## Long-term

- Generate a **positive real (after inflation) return**.
- Generate income for current spending.
- Provide a prudent degree of **growth** in assets to support future spending.
- Provide for **prudent diversification** of investments to minimise correlation among investment strategies.
- Maintain liquidity to meet unanticipated operating requirements.
- Maintain overall portfolio volatility within acceptable risk levels.

# GAVI PORTFOLIOS (\$1.8 BILLION<sup>1</sup> )



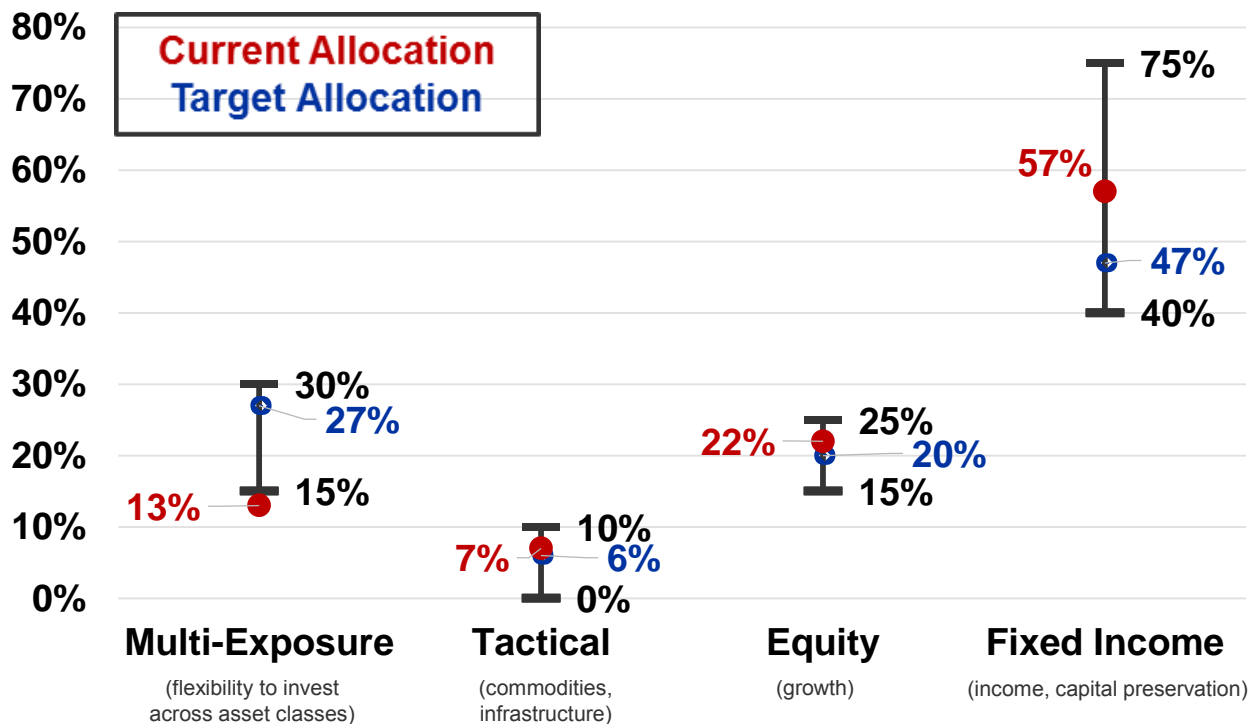
Data as of 30 April 2017

<sup>1</sup> Excludes UNICEF Procurement account of \$446 M and IFFIm assets.

<sup>2</sup> Excludes \$61.5 M in operating cash, and \$9 M in redemption proceeds from Angeles (remaining 10%)

# LONG-TERM PORTFOLIO EXPOSURES: CURRENT ALLOCATION AND RANGES

ANNEX A



Data as of 30 April 2017 (internal estimates)

# PORTFOLIO NET RETURNS

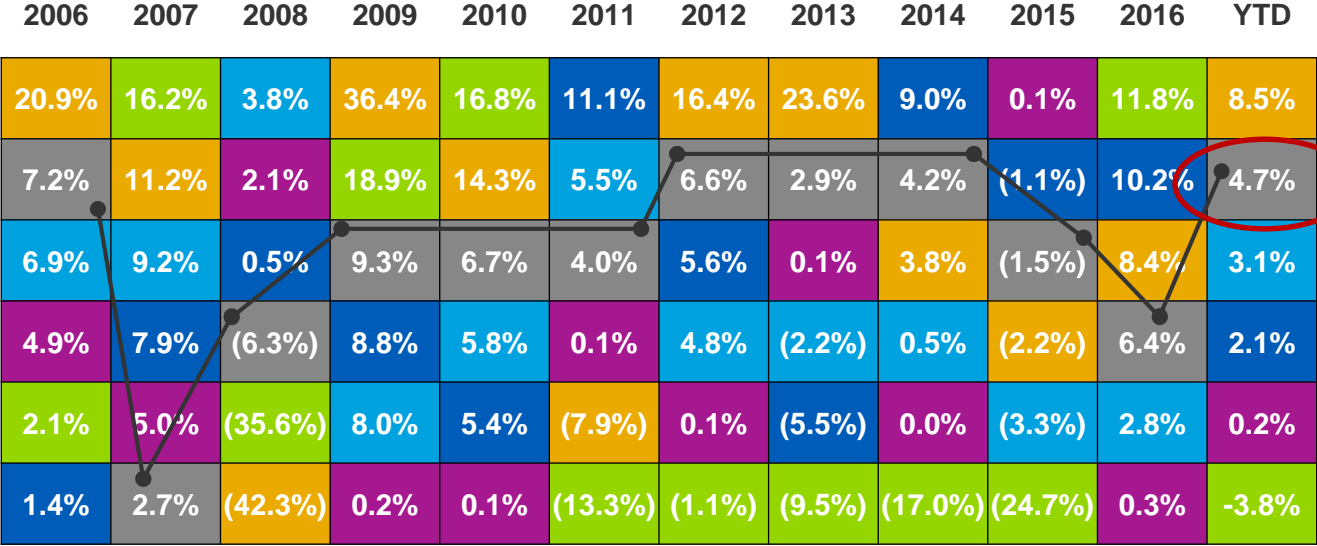
The total portfolio generated estimated year-to-date net investment income of \$41.9 M, and since inception, \$481.0 M.

Portfolio returns	2012	2013	2014	2015	2016	YTD
Long-term portfolio	6.6%	2.9%	4.2%	-1.5%	6.4%	4.7%
Short-term portfolio	0.9%	0.4%	0.2%	0.4%	0.9%	0.5%

Data as of 30 April 2017

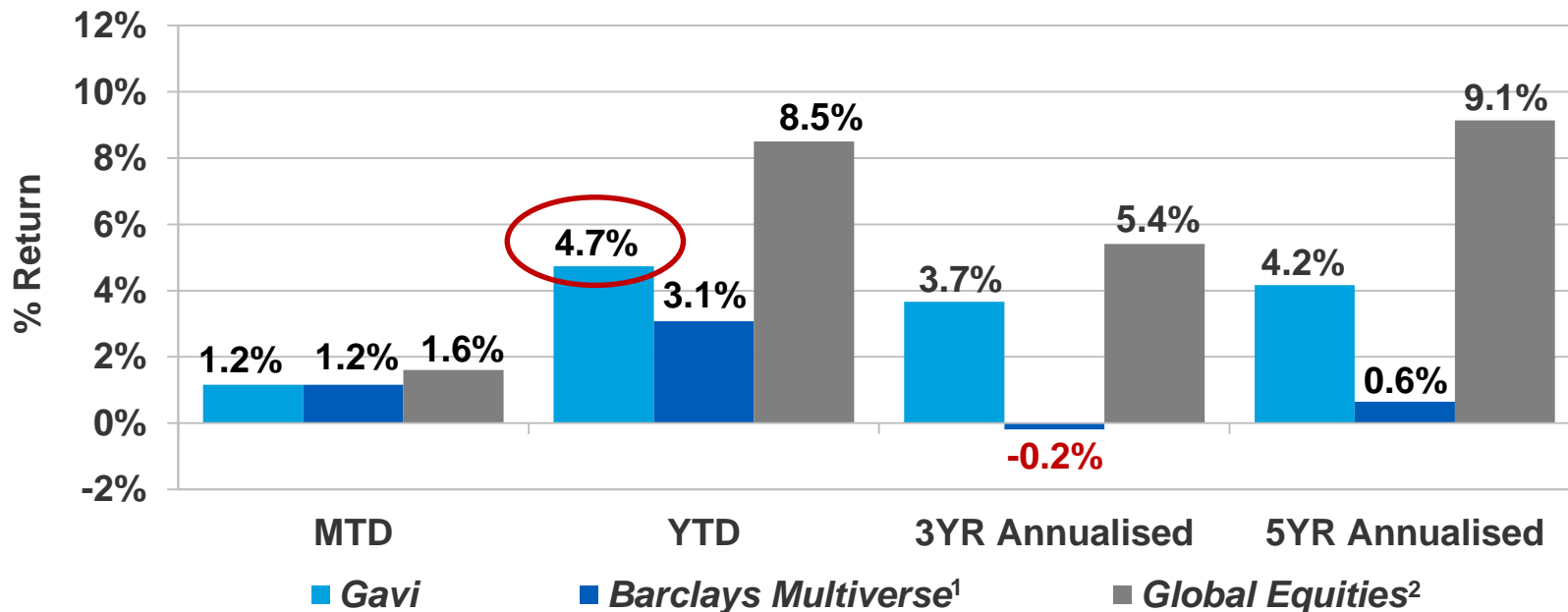
Source: internal estimates, short-term portfolio figures based on strategies managed by the Investments team

# COMPARISON OF RETURNS



Data as of 30 April 2017  
 Source: Bloomberg, internal estimates

# LONG-TERM PORTFOLIO PERFORMANCE



Data as of 30 April 2017

Source: Bloomberg, internal estimates

(1) Barclays Multiverse is a broad, global fixed income index.

(2) MSCI ACWI is a broad, global equity index.



# LONG-TERM PORTFOLIO RETURNS

Exposure vs. Benchmark	2013	2014	2015	2016	YTD
<b>Fixed Income</b>	<b>0.8%</b>	<b>3.4%</b>	<b>1.0%</b>	<b>6.1%</b>	<b>3.0%</b>
<i>Barclays Multiverse<sup>1</sup></i>	<i>(1.0%)</i>	<i>(0.5%)</i>	<i>(3.3%)</i>	<i>2.8%</i>	<i>3.1%</i>
<b>Equity</b>	<b>25.2%</b>	<b>6.4%</b>	<b>(1.5%)</b>	<b>6.4%</b>	<b>8.8%</b>
<i>MSCI ACWI IMI</i>	<i>23.6%</i>	<i>3.8%</i>	<i>(2.2%)</i>	<i>8.4%</i>	<i>8.5%</i>
<b>Tactical</b>	--	<b>5.1%<sup>3</sup></b>	<b>(9.8%)</b>	<b>16.0%</b>	<b>4.9%</b>
<i>BofA Merrill US 1-Year Treasury<sup>2</sup></i>	--	<i>0.1%</i>	<i>0.2%</i>	<i>0.8%</i>	<i>0.2%</i>
<b>Multi-exposure</b>	<b>(0.7%)</b>	<b>4.4%</b>	<b>(4.3%)</b>	<b>4.7%</b>	<b>6.5%</b>
<i>3-Month LIBOR + 5%<sup>4</sup></i>	<i>N/A</i>	<i>N/A</i>	<i>N/A</i>	<i>N/A</i>	<i>2.0%</i>
<b>Long-term portfolio</b>	<b>2.9%</b>	<b>4.2%</b>	<b>(1.5%)</b>	<b>6.4%</b>	<b>4.7%</b>

(1) From 1 March 2014 to present

(2) From 1 October 2014

(3) Inception date 30 May 2014

(4) Multi-Exposure benchmark not implemented until March 2016

# KEY HIGHLIGHTS 1H2017

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## Long-Term Portfolio Allocation

The Committee continues to add less-directional and lowly correlated strategies that should help dampen volatility in portfolio returns, and protect capital in more challenging markets.

**Update: The Committee approved several recommendations for the termination and hiring of managers. Moving the portfolio to the recommended target allocations is a key priority.**

## Risk Monitoring

Completed the following reviews: Two sets of quarterly compliance questionnaires, one semi-annual Socially Responsible Investment screening, and the annual audited financial statement review.

**Update: These reviews provide additional insights into our investment managers.**

# KEY HIGHLIGHTS 1H2017 (CONT)

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## Investment Committee Charter

The Investment Committee joined the first round of committee charter updates that came out of a broader review associated with the Board and Committee self-evaluation process.

**Update: The Investment Committee charter will be edited to ensure consistency across Gavi charters. The final draft will be reviewed in August.**

## Global Custodian RFP

The global custodian provides the official books and records for Gavi's investments. The last RFP was issued in 2008.

**Update: Four candidates, including the current vendor, indicated their intent to participate.**

# KEY 2H2017 PRIORITIES

## Maintain focus on risk

Markets have had a good run. Be prepared for a correction.

## Maintain robust monitoring practices

All issues identified during the 2015-2016 audit have been closed. Internal Audit subsequently assigned a low risk rating.

## Ensure smooth manager transition

The Committee continues to rationalise the number of investment managers as part of the portfolio re-allocation process. The Committee champions negotiating improved fee structures wherever possible.

**THANK YOU**

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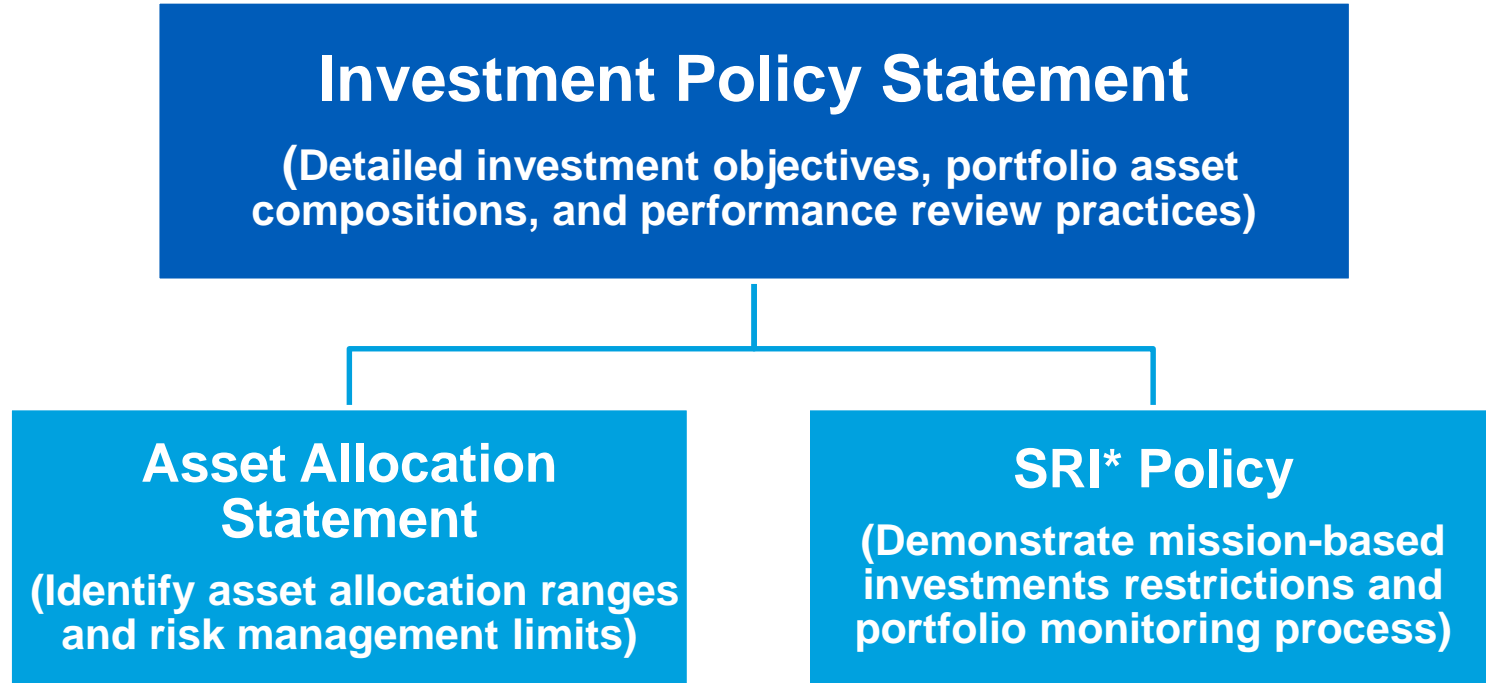


# APPENDIX

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# INVESTMENT POLICIES

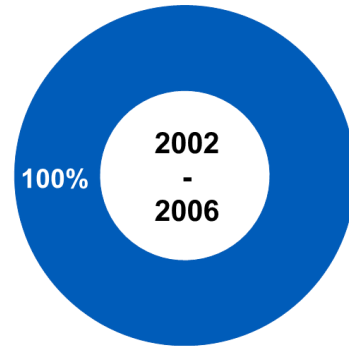
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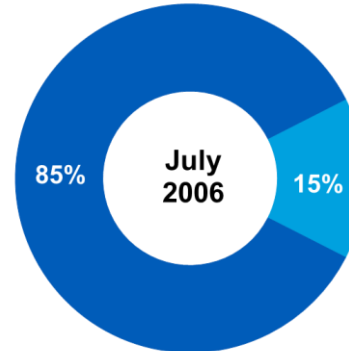
\*Socially Responsible Investment

# LONG-TERM PORTFOLIO EVOLUTION

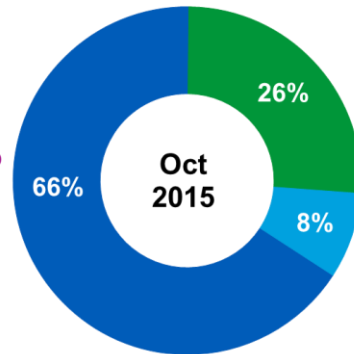
(1) Conservative, US centric, short-term fixed income



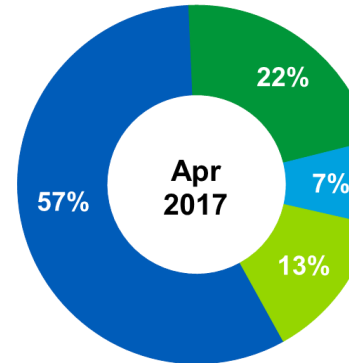
(2) Launch of IFFIm extended investment horizon; added inflation hedge assets



(3) Further diversification into less correlated assets



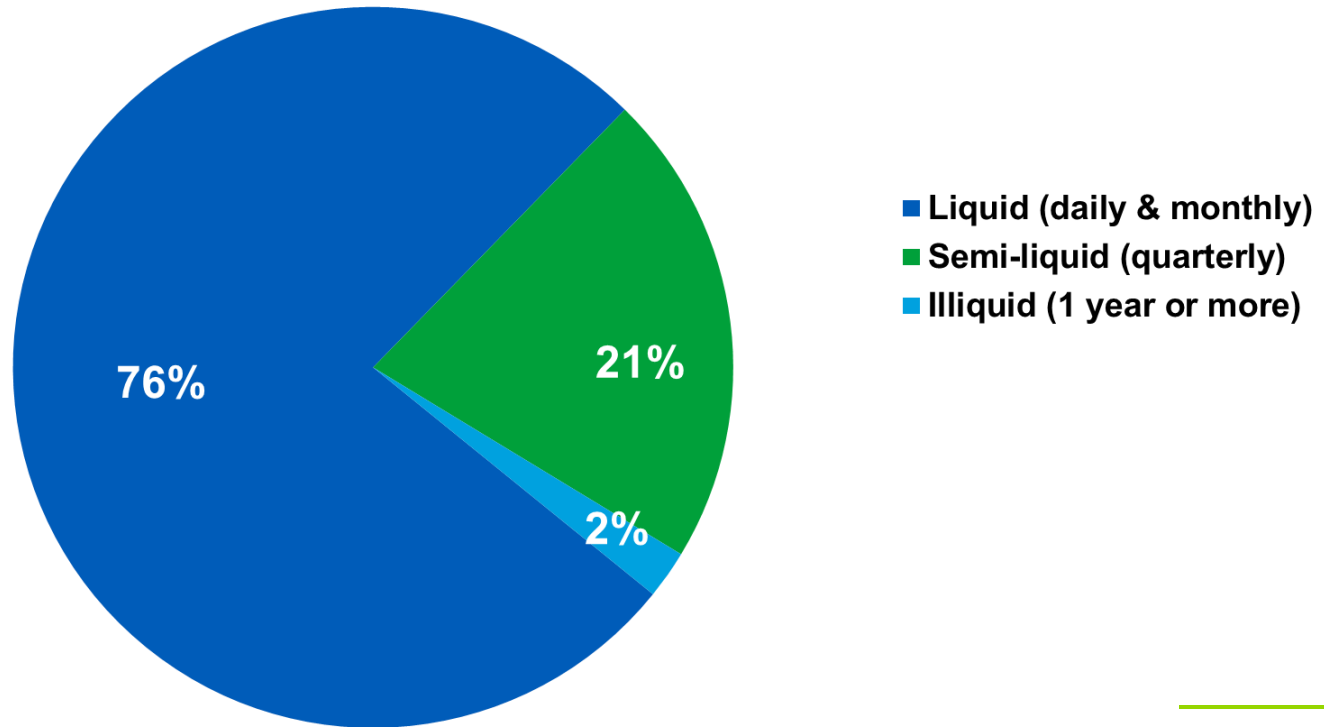
(4) Added multi-exposure in May 2016.





# LONG-TERM PORTFOLIO LIQUIDITY

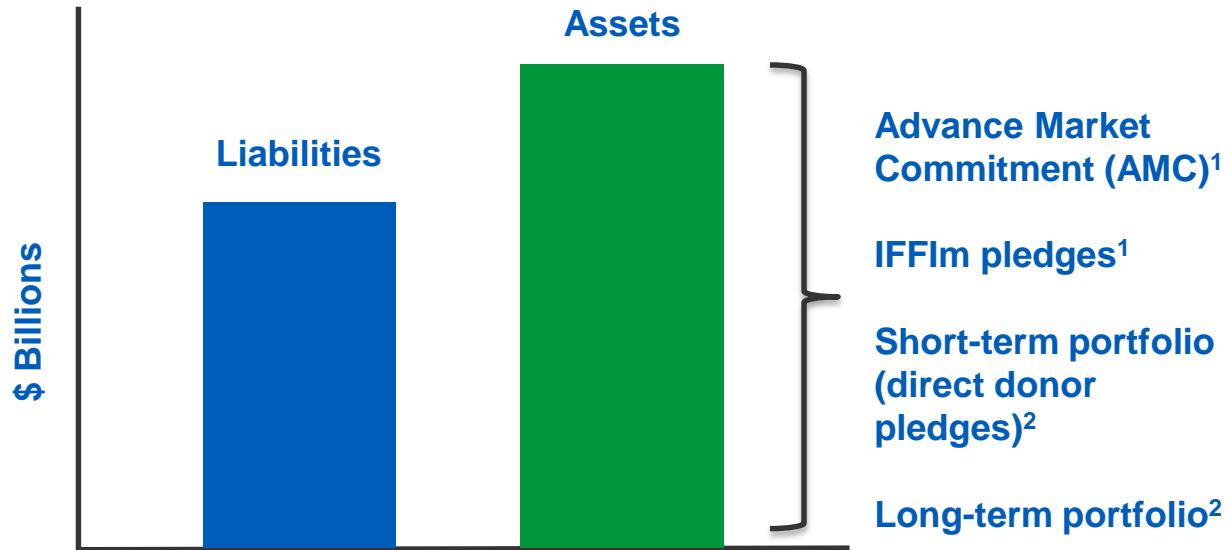
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Data as of 30 April 2017

# STABILITY AND SOLVENCY

## Assets Must Be Greater Than Programme Liabilities



(1) Assets managed by the World Bank Group.

(2) Assets managed by the Investments team with oversight by the Investment Committee

# ASSETS BY TIME HORIZON

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	Short-term	Intermediate	Long-term
Short-term portfolio	X		
Advance Market Commitments		X	
IFFIm Pledges (contractual)			X
Long-term portfolio			X

# EXPOSURE CHARACTERISTICS

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<b>Characteristics</b>	
<b>Fixed Income (40% - 75%)</b>	<b>Capital preservation, income</b>
<b>Equity (15% - 25%)</b>	<b>Growth, inflation hedge (moderate)</b>
<b>Tactical (0% - 10%)</b>	<b>Less correlated assets lacking the typical characteristics of fixed income or equity</b>
<b>Multi-exposure (15%-30%)</b>	<b>Liquid, flexible, and risk diversified strategies</b>

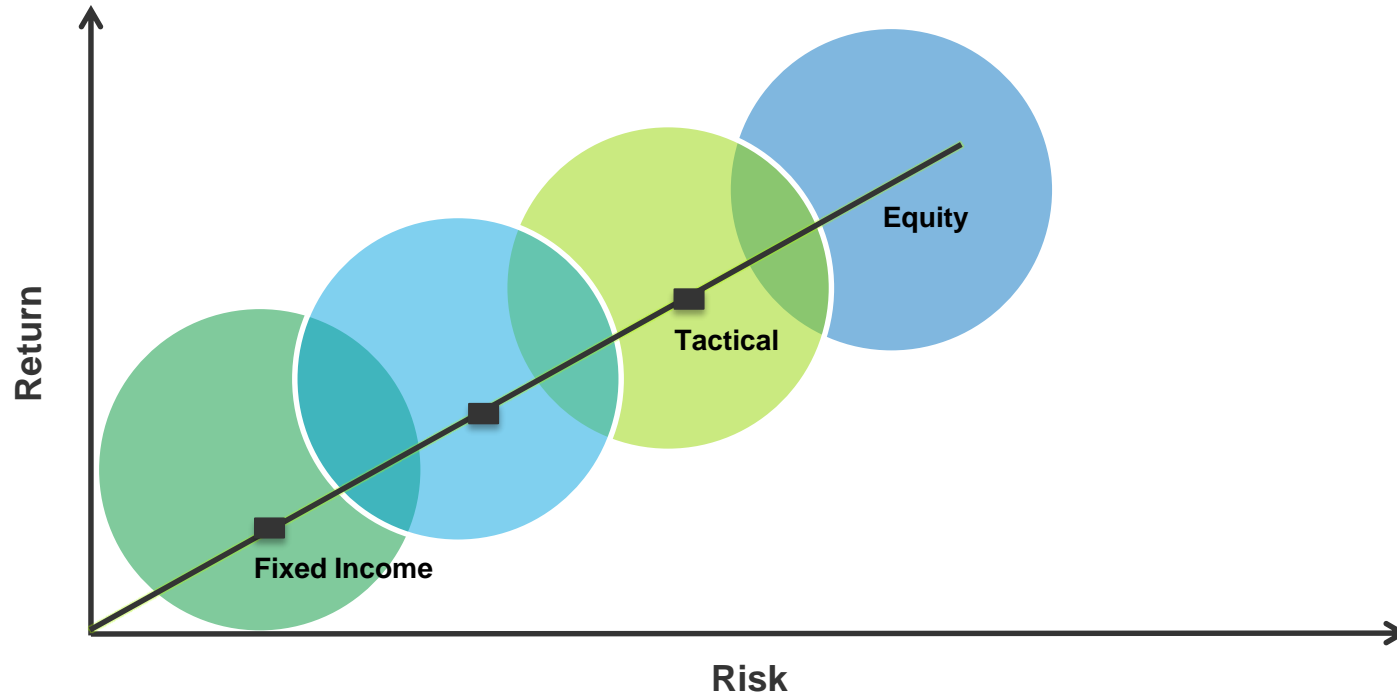
# ASSET ALLOCATION: WHAT TO CONSIDER

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**In assessing an appropriate mix of investments, the Investments team with the guidance of the Investment Committee and a strategic consultant considers the following:**

1. Appetite for volatility/risk
2. Balancing liquidity of investments
3. Frequency and size of drawdowns (to pay liabilities)
4. Diversification (adding investments that will behave differently under various economic scenarios)

# RISK VERSUS RETURN



# FIXED INCOME

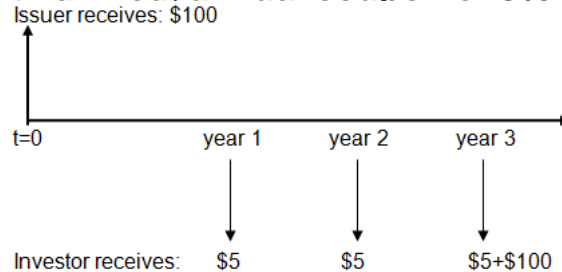
## Definition:

A financial obligation from an issuer (e.g., a government) to the investor which typically includes:

1. Periodic interest (coupon) payments
2. Repayment of principal at maturity

• **Example:**

**\$100, 3-year obligation with a fixed, annual coupon of 5%**



Total return: At the end of 3 years, the investor receives \$15 in coupon payments and his/her principal of \$100

# EQUITY

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## Definition:

A security that provides the investor with an equity or ownership stake in a company. The investor seeks to earn at least one of the following:

1. Dividends (profit distribution)
2. Capital gain (market value at sale – purchase price)

**Stocks are *not* a short-term investment; in general they are appropriate for investors who have a time horizon greater than 5 years.**



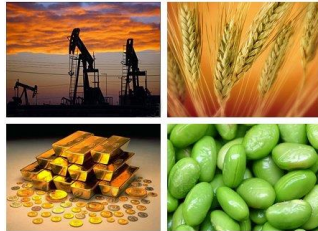
# TACTICAL

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## Definition:

Investments that serve as diversifiers within the GAVI long-term portfolio. They do not share the typical characteristics of fixed income and equity. Examples include:

- Commodities
- Infrastructure
- Real estate investment trusts



# MULTI-EXPOSURE

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## Definition:

Investing in a combination of various asset classes through the use of liquid, flexible strategies. It serves the goal of diversifying risk and mitigating volatility.

These strategies may include common asset classes such as:

- Equity
- Fixed Income
- Currencies
- Commodities

# SOCIALLY RESPONSIBLE INVESTMENT (SRI)

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- Gavi SRI Policy requires **semi-annual negative screening** on investments in companies that produce **tobacco products, weapons, landmines/cluster munitions** and companies that have or are alleged to have **material breaches of human rights and child labour standards**.
- Gavi only screens individual company holdings, e.g., public equities and corporate bonds. Some corporate investments are not screened because the fund holdings are not transparent or in index funds.
- The value of noncompliant companies in each fund cannot exceed **2%**. An internal evaluation will be initiated for a fund if it has breached the 2% limit for two consecutive screenings.

**Thank you**

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