

SUBJECT: INVESTMENT COMMITTEE CHAIR REPORT

Category: For Information

Section A: Introduction

- This report provides the Board with an overview of the macroeconomic environment, portfolio performance, and the activities of the Investment Committee since the Board last met in June 2017.
- In calendar year 2017, the Committee met 4 times (February, May, August and November). As mentioned in the June report, the Investment Committee charter underwent a review in 2016 as part of a broader review associated with the Board and Committee self-evaluation process. The Investment Committee charter required additional edits in order to keep it consistent with other Gavi charters. The Investment Committee approved the editorial changes in August.
- The global economy sustained its growth trajectory into the second half of 2017 on the back of solid corporate earnings, low unemployment and improving consumer confidence levels. The IMF's October 2017 World Economic Outlook publication lifted both its 2017 and 2018 forecasts of global economic growth by 0.1% to 3.6% and 3.7% respectively, well ahead of 3.2% achieved in 2016.
- After the 2008 financial crisis, major central banks pursued exceptionally loose monetary policy to encourage borrowing, increase risk appetite and raise asset prices. In addition, they purchased bonds to flood their economies with liquidity, which resulted in massive increases in their balance sheets. With economic recovery firmly in place, the major central banks have begun to increase rates and/or reduce monetary stimulus programmes. Since the last Gavi Alliance Board meeting in June, major central banks have announced the following:
 - The US Federal Reserve began to reduce its US\$ 4.5 trillion balance sheet;
 - The European Central Bank will reduce the amount of its monthly bond purchases but also extend the duration of this QE programme;
 - The Bank of England increased interest rates by 0.25%, the first rise in a decade.
- The change in leadership of the US Federal Reserve in February 2018 is another development being closely watched by investors. The outgoing Federal Reserve chairwoman Janet Yellen and the incoming Federal

Reserve chairman Jerome Powell appear to have similar policymaking priorities, and markets have remained unperturbed. However, it will be the actual decisions and announcements coming out of the Fed when Mr Powell assumes his new role that will matter.

- The Investment Committee remains cautious on current market volatility levels that are near record lows and asset prices that are near historic highs. Investors who think the markets' strength is primarily a reflection of the solid global economy see little to fear. However it is likely that "normal" market functioning is being suppressed by central bank flows which are now reducing. Thus far in 2017, financial markets have been immune to geopolitical or other normally market moving events. This indifference is not sustainable in the long term, particularly as positions have grown increasingly crowded as the rally has progressed. Investors such as Gavi should not become accustomed to such low volatility levels or indeed the extent and consistency of the returns which have been generated in the Long Term Portfolio this year.
- At the Investment Committee's November meeting, the consultant NEPC presented an independent risk assessment of Gavi's long-term investment portfolio. This has now become a valuable annual review. NEPC uses 3 methodologies (asset allocation-based, sensitivity-based, and portfolio-based) to evaluate overall portfolio risk. The conclusion was that current target allocations were still appropriate and NEPC made no structural recommendations. NEPC also performed a Value-at-Risk (VAR) analysis on the portfolio. VAR is a probability-based measure of potential loss. This showed a potential loss scenario of 8% in a one standard deviation event, which is meaningfully lower than that of a traditional 60% equity/40% fixed income institutional portfolio (13.3% loss). Furthermore, NEPC noted aspects of portfolio implementation cannot be fully configured into Value-at-Risk, so Gavi's inclusion of investment managers that focus on downside risk should also help to buffer portfolio volatility. This was indeed the case in January 2016 when portfolio marked-to-market losses were well below what the models predicted.
- The Investments team conducts an annual risk rating of individual managers it oversees, and the outcomes determine due diligence priorities for the following calendar year. While the ability of a manager to deliver solid performance is a positive consideration, the team takes a comprehensive approach to evaluating managers across a dozen risk factors in order to assign an overall risk rating. Example of such factors include the complexity of the investment, senior management stability, internal controls assessment and quality of service. At the November 2017 meeting, the Investment Committee reviewed the risk rating analyses and endorsed the team's findings.
- The Chair update includes year-to-date September 2017 performance figures for the long-term and short-term portfolios overseen by the Investments team. As a reminder, Gavi uses both active and passive investment strategies.

- The total portfolio reported for this update is US\$ 2.1 billion, of which US\$ 1.1 billion is invested in the short-term portfolio, and the remaining US\$ 1.0 billion in the long-term portfolio. As a reminder, these figures do not include the UNICEF Procurement Account or 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 (pending reinvestment) from the long-term portfolio. The short term portfolio 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 1.0%.
- The long-term portfolio has four major allocations: Fixed income, equity, tactical, and multi-exposure. The major theme of the last two annual asset allocation and risk reviews remain consistent: Reduce directional exposures given high current valuations in favour of the absolute return oriented multi-exposure category which provide tactical and managerial flexibility to invest across different asset classes. The portfolio remains modestly underweight relative to its target multi-exposure category, and the Investments team continues to make progress in closing the gap.
- Year-to-date through September 2017, the long-term portfolio outperformed its policy benchmark, 9.3% versus 7.7%. Preliminary results for October show a further gain of 0.7%. October year-to-date investment income generated for GAVI amounts to approximately US\$ 94.6 million.
- The long-term portfolio has more than half of its allocation to fixed income given Gavi's conservative risk profile. On a composite basis, the fixed income allocation delivered 5.7% despite the low interest rate environment. The strongest performing allocation was equities, which delivered a composite performance of 17.9%. The Tactical and Multi-exposure categories have also performed solidly this year and have delivered 10.3% and 11.9% respectively.
- The Investment Committee Chair report is attached in the form of a presentation as Annex A.

Annexes

Annex A: Investment Committee Chair report

INVESTMENT COMMITTEE CHAIR REPORT

BOARD MEETING

Stephen Zinser

29-30 November 2017, Vientiane, Lao PDR



Summary

- **Macro Environment and Market Commentary**
- **Portfolio and Performance Review**
- **Key Highlights of 2H2017**
- **Key 2018 Priorities**

Market Sentiment: Mixed

A broad run-up in asset valuations has left little low hanging fruit: Signs of moderating risk appetite have emerged.

Economic growth remains solid in the US, Europe (ex-UK), China and Japan. Major central banks have begun to pare back monetary stimulus and/or raise interest rates: The change in leadership of the US Federal Reserve will be under close scrutiny.

Geopolitical risk continues to be a factor: Market enthusiasm swept aside political risk this year but markets are beginning to reassess implications.

Market Commentary

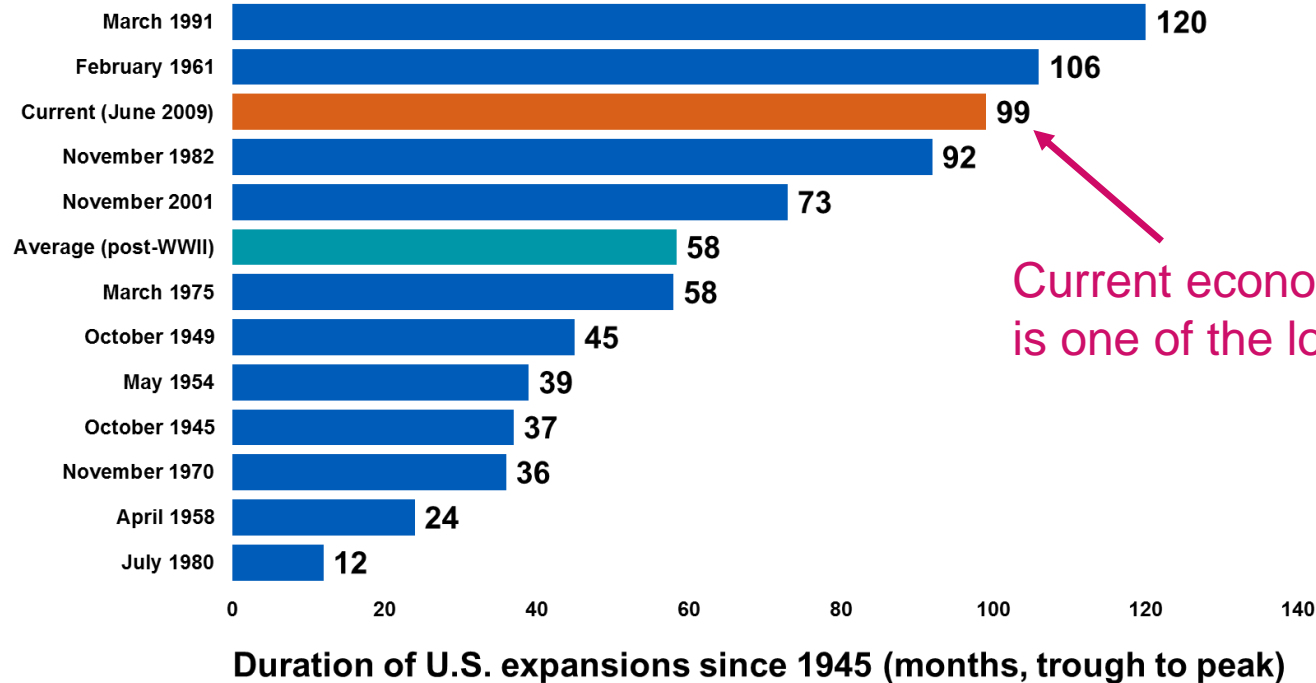
Equity markets: European and US markets have performed well this year. Emerging markets, however, was the biggest contributor to the global equity rally.

Fixed income: Emerging markets and high yield fixed income have enjoyed solid performance. Moderating risk appetite and tight spreads will cap further gains.

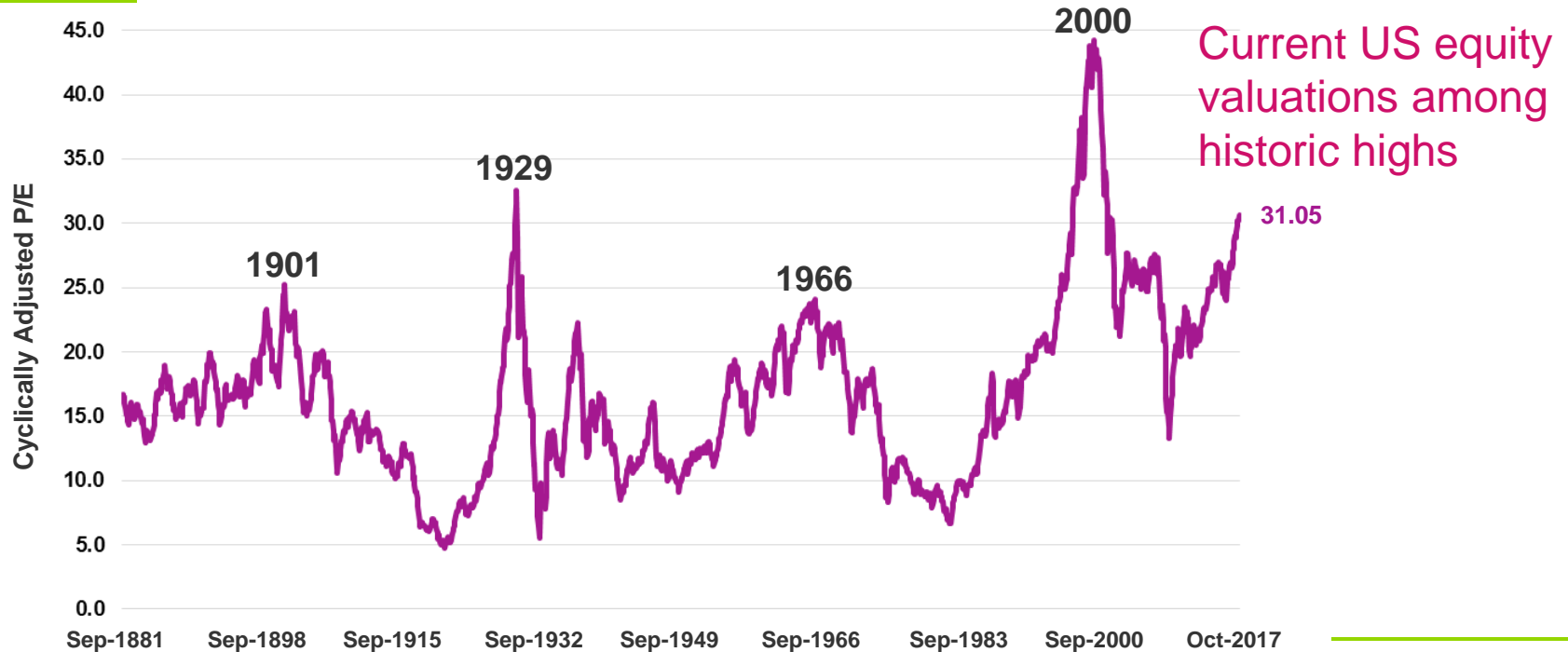
Currencies: US dollar weakness has been the big surprise this year, losing 10.7% against the euro

Commodities: Higher demand due to stronger global economic growth and compliance with OPEC's supply cuts have produced tighter oil supplies and higher prices.

US Economic Expansions

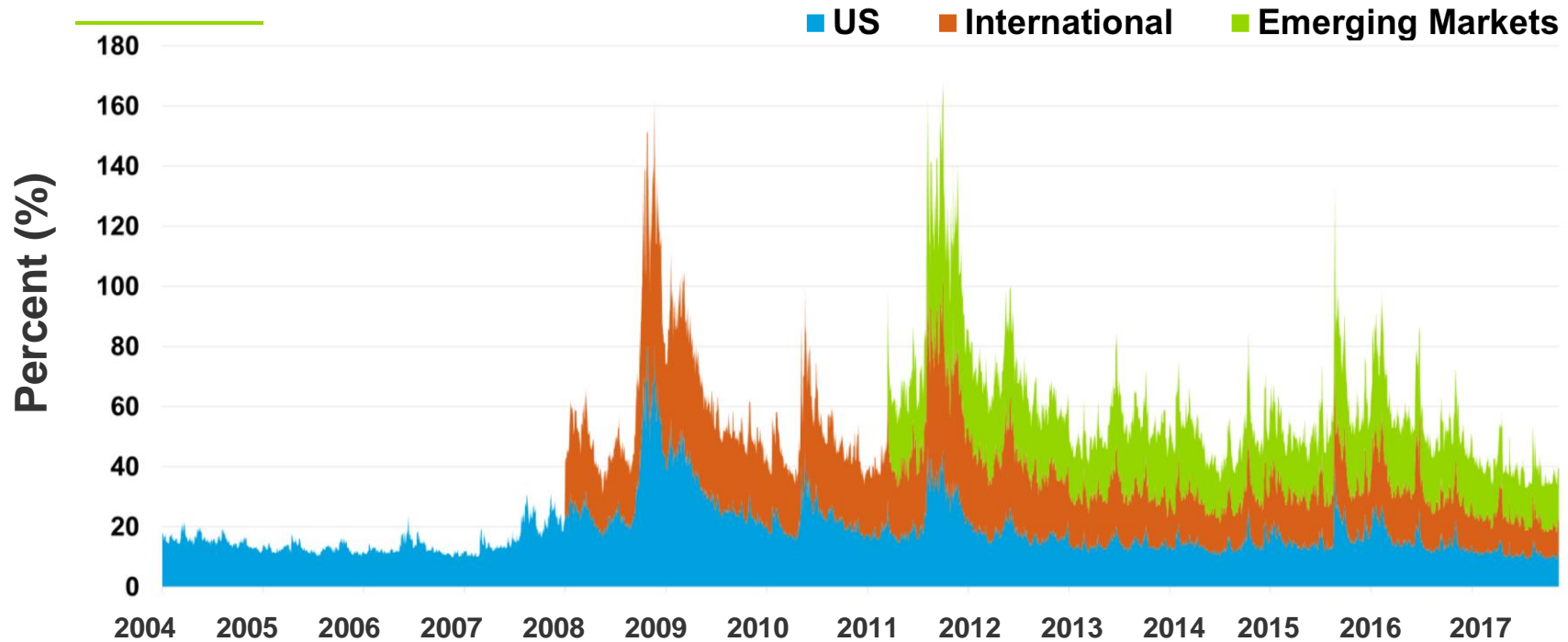


Shiller's Price Earning Ratio



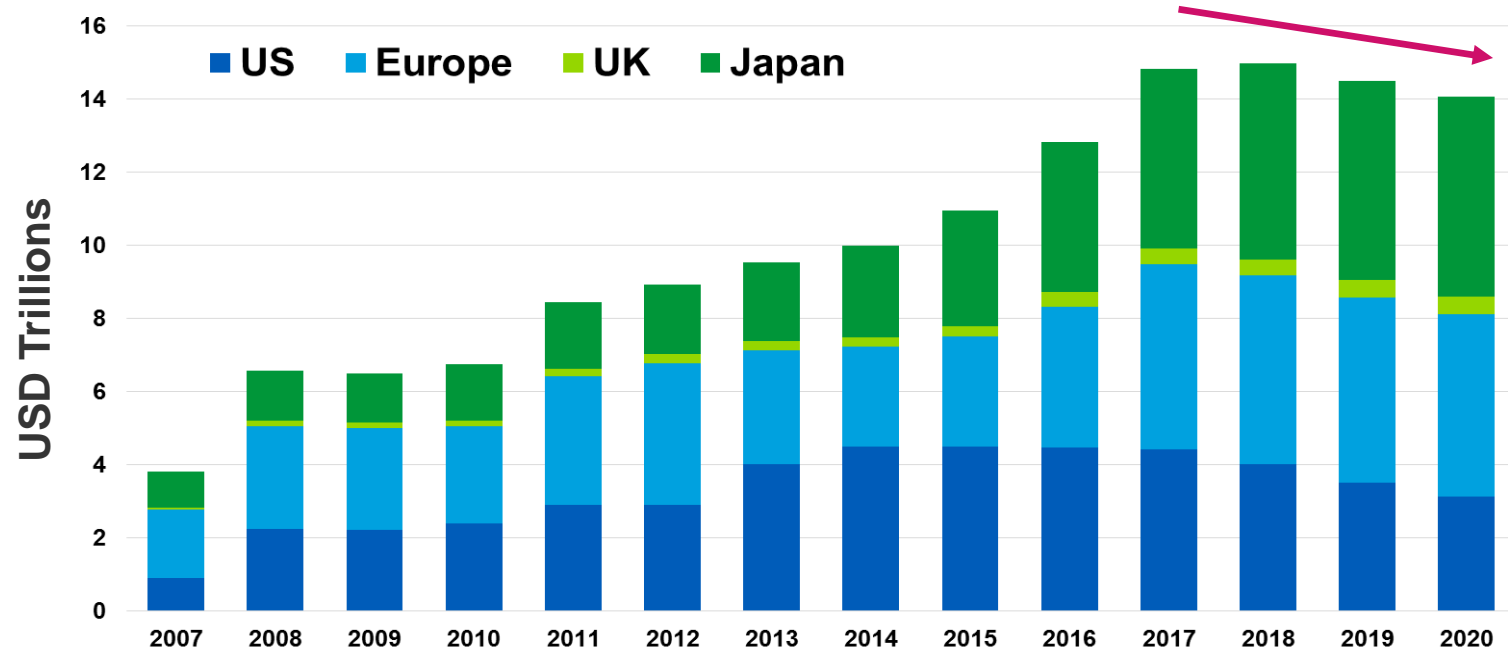
Source: Shiller US Stock Markets 1871-Present and CAPE Ratio produced by Yale School of Management, Data as of October 2017

Low Equity Volatility - Globally



Data as of 13 November 2017
Source: Chicago Board of Exchange

Central Bank Balance Sheets

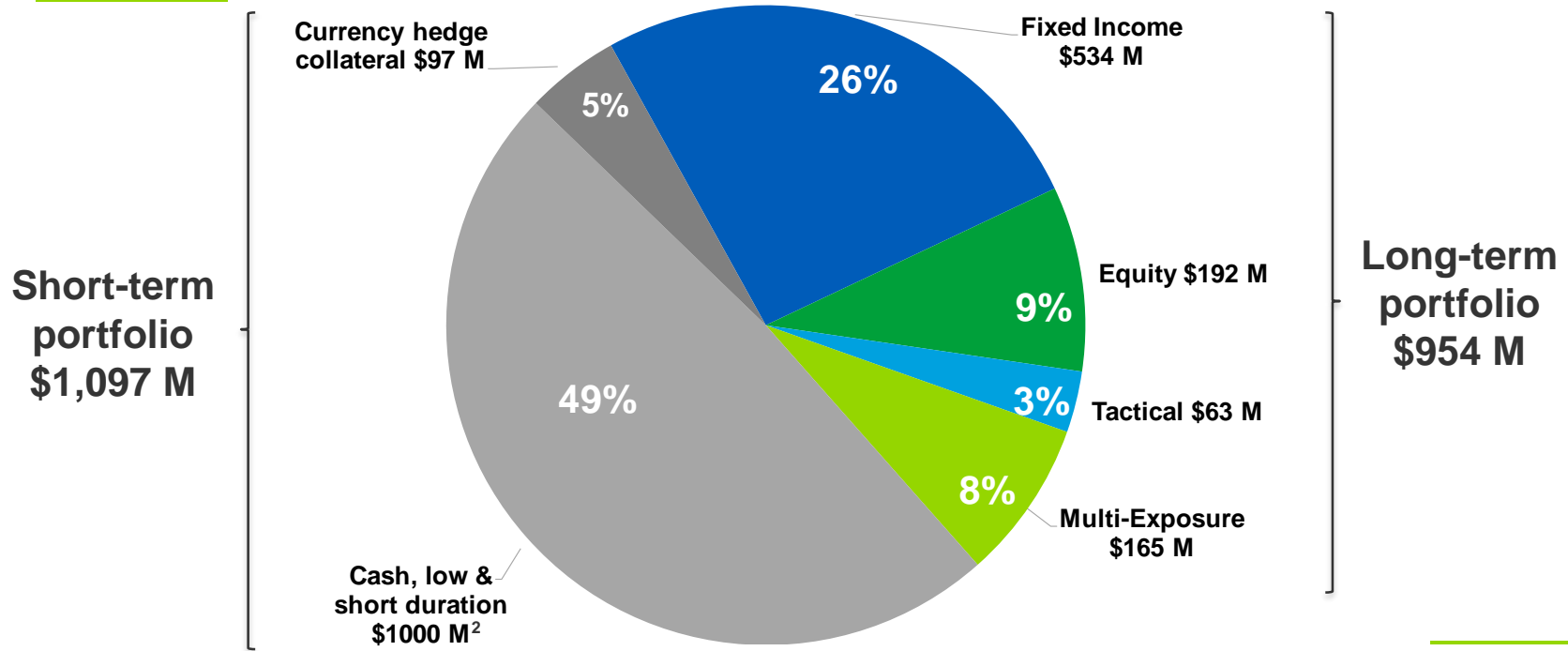


Data as of 30 September 2017
Source: Reams Asset Management, JPMorgan

Portfolio Objectives

Short-term	Long-term
<ul style="list-style-type: none">• Maintain liquidity to meet anticipated operating requirements.• Provide for prudent diversification of investments to minimize credit and market risk exposure.• Generate income.	<ul style="list-style-type: none">• 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 Portfolio Allocation (US\$ 2.1 B)¹

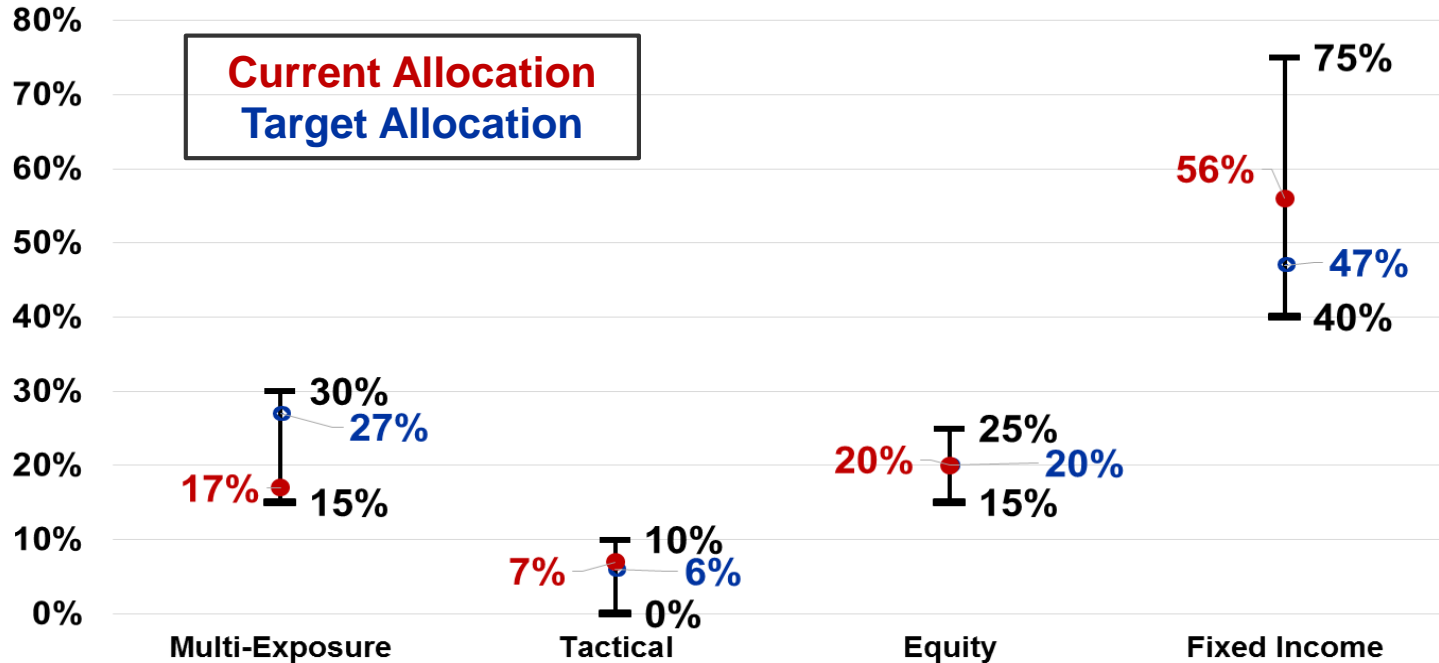


Data as of 30 September 2017

¹ Excludes UNICEF Procurement account of \$383 M and IFFIm assets.

² Excludes \$42.2 M in operating cash.

Long-Term Portfolio: Asset Allocation Ranges



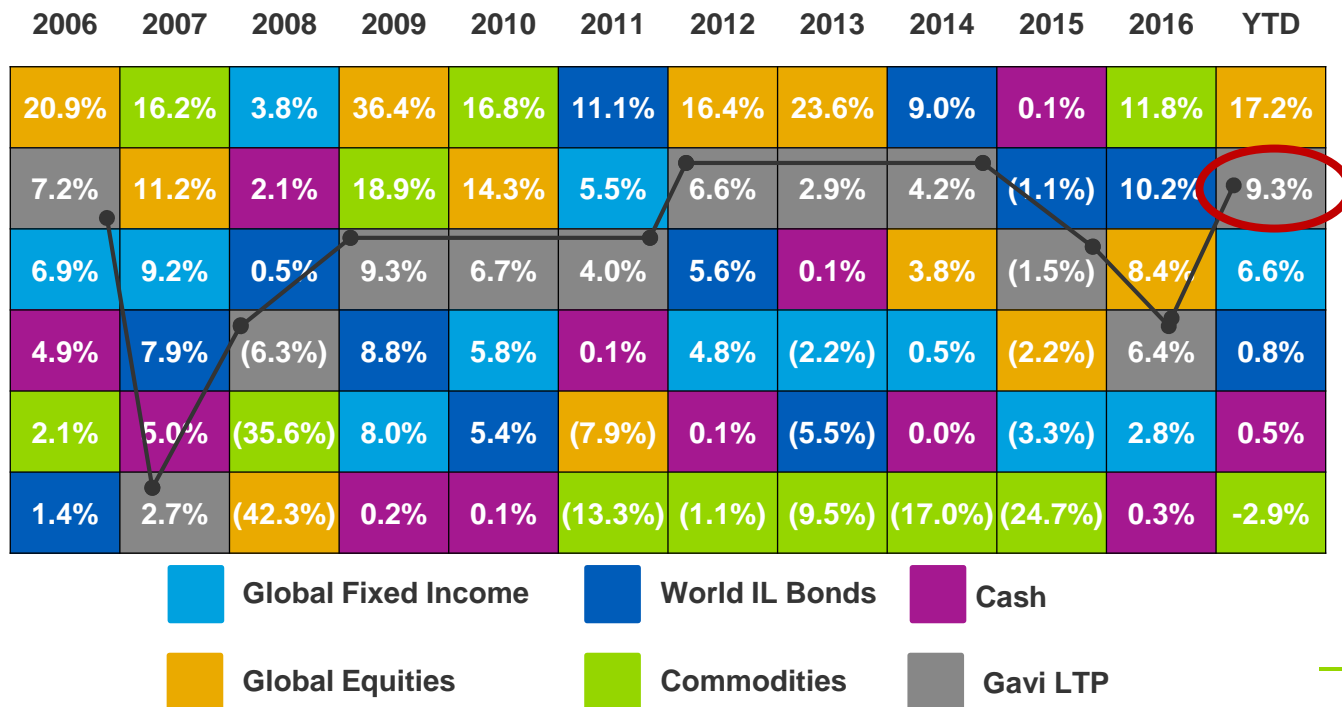
Portfolio Net Returns

Through September 2017, the total portfolio generated net investment income of US\$ 87.9 M, and since inception, US\$ 527 M.

Portfolio returns	2012	2013	2014	2015	2016	YTD
Long-term portfolio	6.6%	2.9%	4.2%	-1.5%	6.4%	9.3%
Short-term portfolio	0.9%	0.4%	0.2%	0.4%	0.9%	1.0%

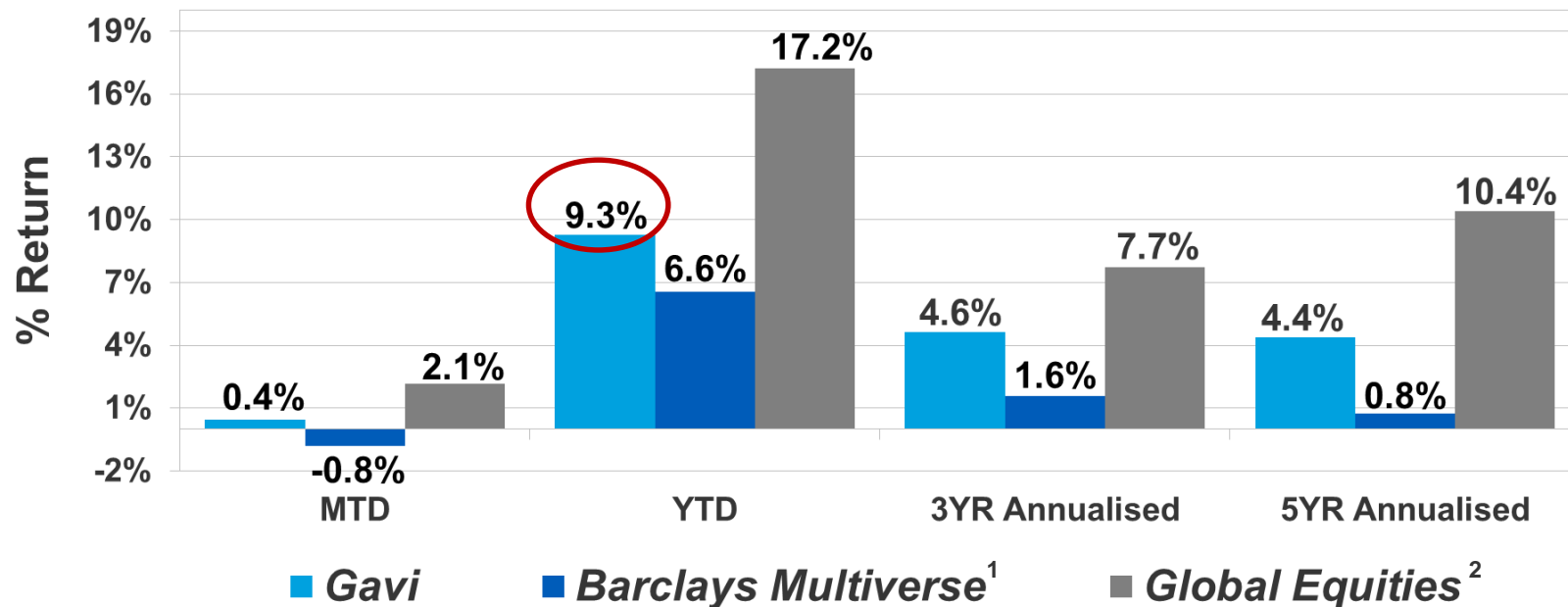
The preliminary October performance estimate for the long-term portfolio is +0.7% which brings YTD investment income to US\$ 94.6 M.

Comparison of Indices Returns



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

Long-Term Portfolio Performance



Data as of 30 September 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
Fixed Income	0.8%	3.4%	0.9%	6.0%	5.7%
<i>Barclays Multiverse¹</i>	<i>(1.0%)</i>	<i>(0.5%)</i>	<i>(3.3%)</i>	<i>2.8%</i>	<i>6.6%</i>
Equity	25.2%	6.4%	(1.6%)	6.4%	17.9%
<i>MSCI ACWI IMI</i>	<i>23.6%</i>	<i>3.8%</i>	<i>(2.2%)</i>	<i>8.4%</i>	<i>17.2%</i>
Tactical	--	5.1%³	(10.3%)	16.0%	10.3%
<i>BofA Merrill US 1-Year Treasury²</i>	<i>--</i>	<i>0.1%</i>	<i>0.2%</i>	<i>0.8%</i>	<i>0.6%</i>
Multi-exposure	(0.7%)	4.4%	(4.3%)	4.7%	11.9%
<i>3-Month LIBOR + 5%⁴</i>	<i>N/A</i>	<i>N/A</i>	<i>N/A</i>	<i>N/A</i>	<i>4.7%</i>
Long-term portfolio	2.9%	4.2%	(1.6%)	6.4%	9.3%

(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 of 2H2017

Long-Term Portfolio Allocation

The Committee approved recommendations to reduce US equity exposure in favour of non US exposure, lower the fixed income credit allocation, and continue to add less correlated strategies that dampen volatility and directionality in the portfolio.

Update: The Committee approved activity throughout 2017 and into 1Q 2018.

Annual NEPC Risk Review

In November 2017, the Committee reviewed portfolio exposures using Value-at-Risk (probability-based measure of potential loss) and investment manager correlations.

Update: Risks reviewed are acceptable in light of Gavi's objectives.

Risk Monitoring

Completed the following reviews: Two sets of quarterly compliance questionnaires, one semi-annual Socially Responsible Investment screening, and the annual risk ratings.

Update: These reviews provide additional insights into our investment managers beyond performance, and help to set priorities for 2018 due diligence activities .

Key 2018 Priorities

Maintain focus on risk

Be prepared for higher levels of volatility. Finalise allocations into less directional strategies.

Maintain robust monitoring practices

Gavi retains a limited number of investment managers in order to conduct in-depth due diligence throughout the life of the relationship.

SRI Policy

The Committee will continue to update and fine tune the policy given the changing landscape and preferences in responsible investing.

THANK YOU

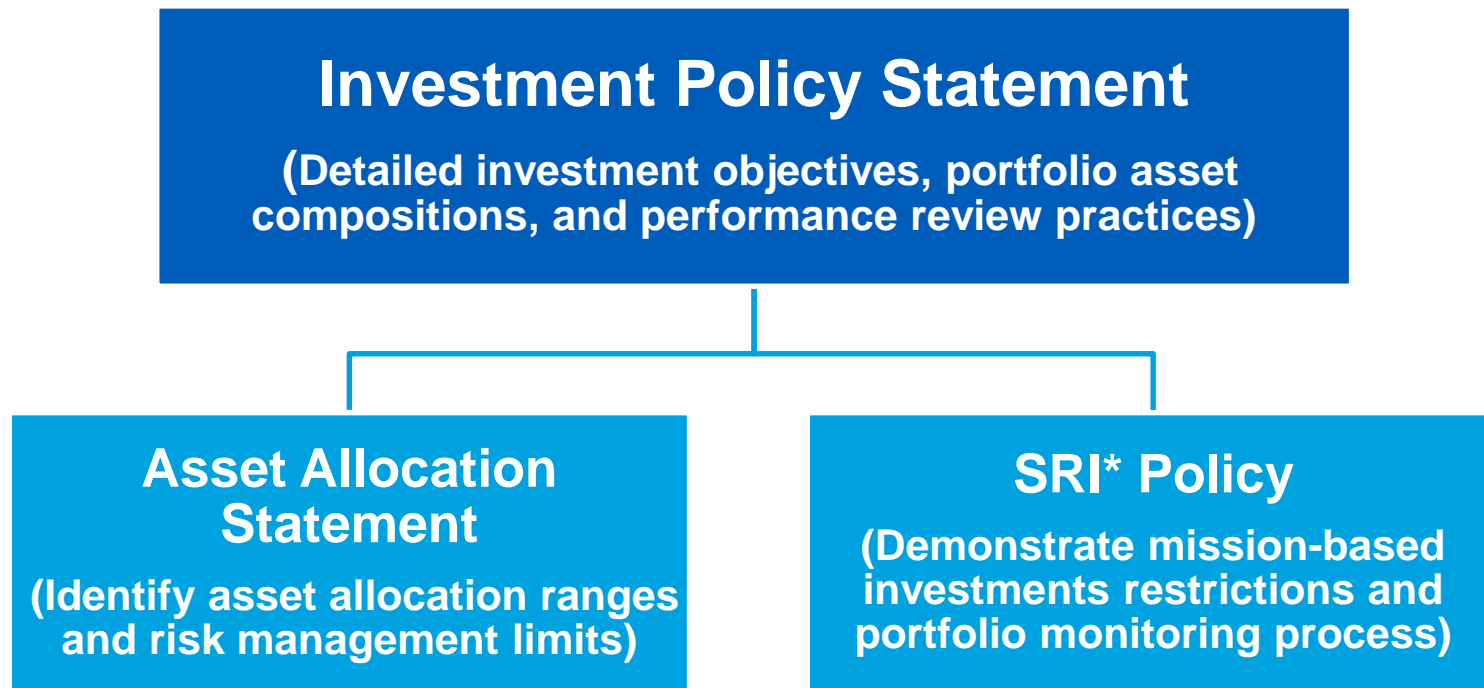


Reach every child

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APPENDIX

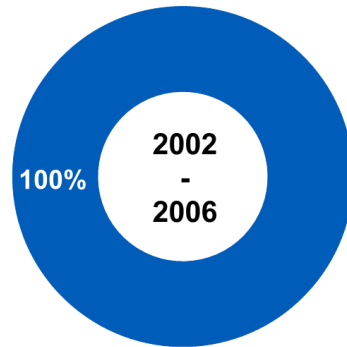
Investment Policies



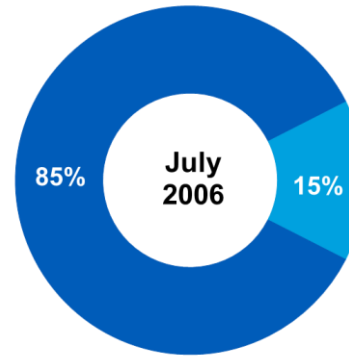
*Socially Responsible Investment

Long-Term Portfolio Evolution

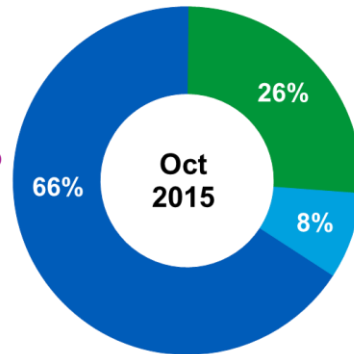
(1) Conservative, US centric, short-term fixed income



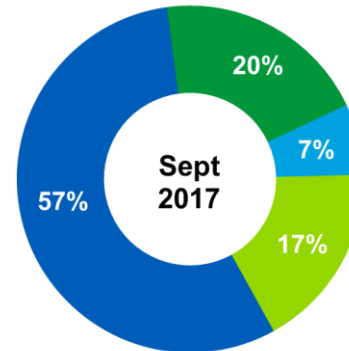
(2) Launch of IFFIm extended investment horizon; added inflation hedge assets



(3) Further diversification into less correlated assets

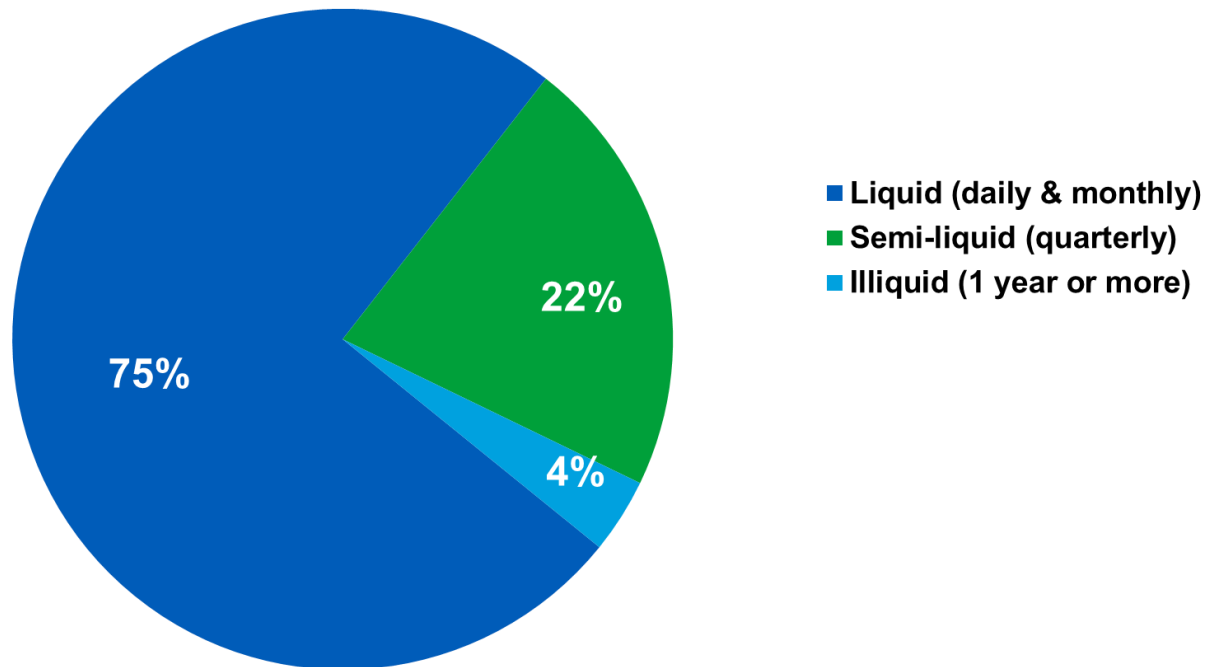


(4) Added multi-exposure in May 2016.



Board meeting
29-30 November 2017

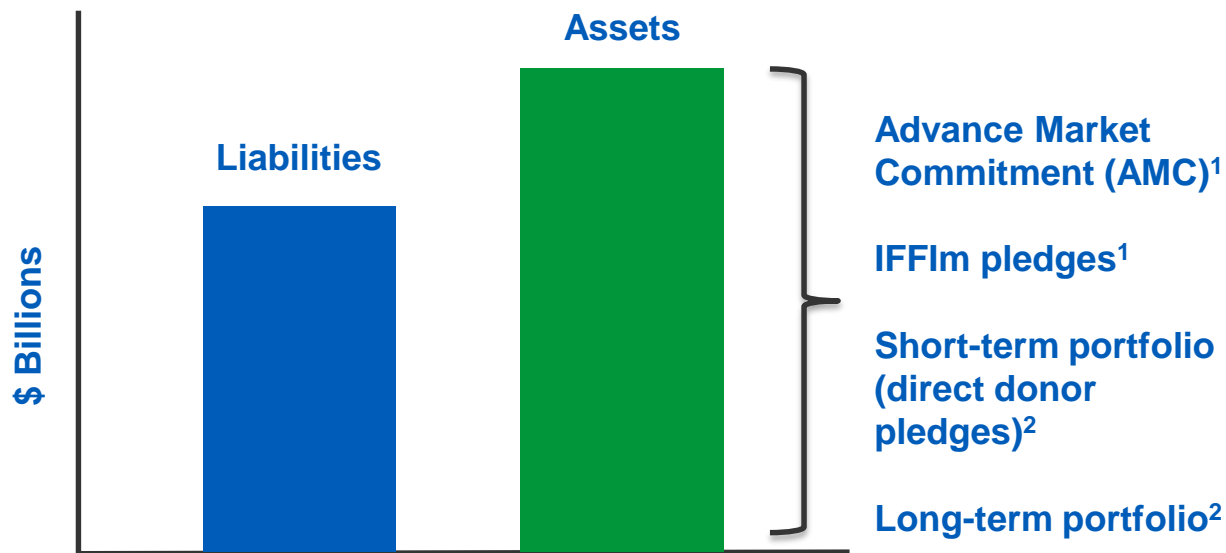
Long-Term Portfolio Liquidity



Data as of 30 September 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

Exposure Characteristics

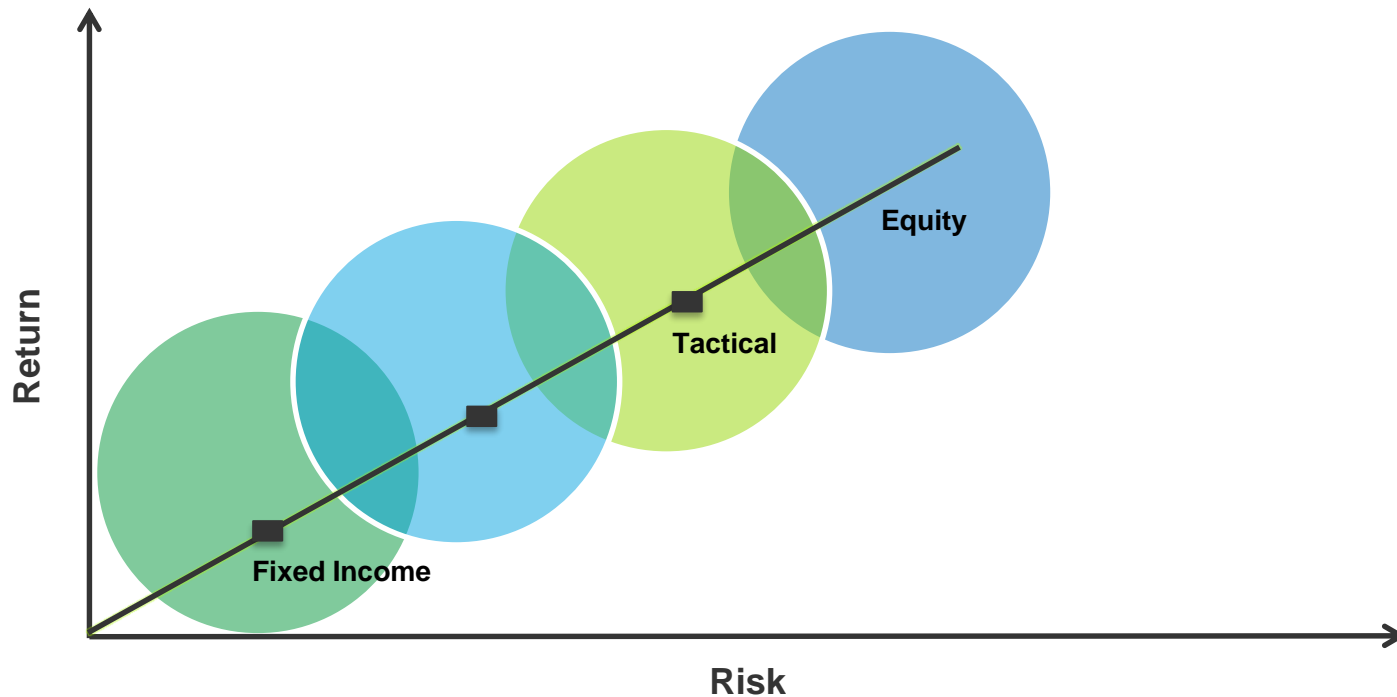
Characteristics	
Fixed Income (40% - 75%)	Capital preservation, income
Equity (15% - 25%)	Growth, inflation hedge (moderate)
Tactical (0% - 10%)	Less correlated assets lacking the typical characteristics of fixed income or equity
Multi-exposure (15%-30%)	Liquid, flexible, and risk diversified strategies

Asset Allocation: What to Consider

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

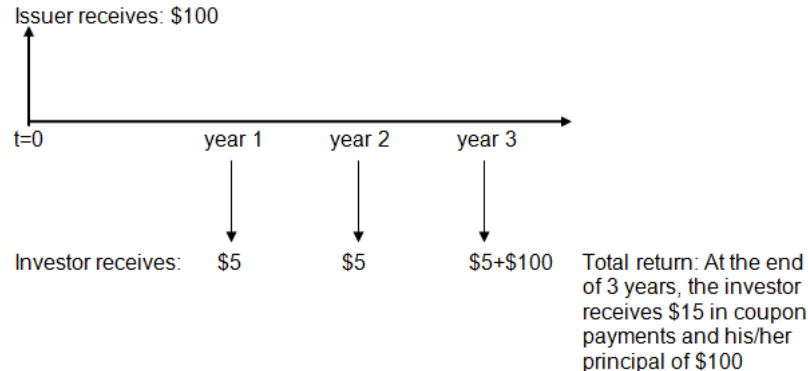
Definition:

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%



Equity

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)

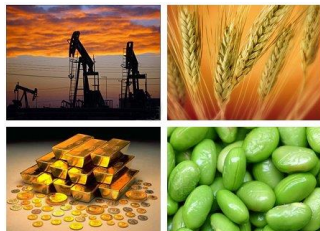
Stocks are *not* a short-term investment; in general they are appropriate for investors who have a time horizon greater than 5 years.

Tactical

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

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)

- 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

