



Report to the GAVI Alliance Board

7-8 July 2011

Subject:	Revision to Cash Investment Policy
Report of:	Barry Greene, MD, Finance and Operations
Authored by:	Jeanne Shen, Senior Director, Investments
Agenda item:	12e
Category:	For Decision
Strategic goal:	Alliance operations

Section A: Overview

1. Purpose of the report

- 1.1 The purpose of this Report is to present a revised Cash and Short-Term Investments Policy ("Policy") to replace the existing Cash Investment Policy approved in June 2009. The proposed Policy expands the investment options and guidelines to include short-term investments for cash pools.

2. Recommendations

- 2.1 The Investment Committee recommends that the GAVI Alliance Board approve the revised Cash and Short-Term Investments Policy and adopt the following resolution:

The GAVI Alliance Board:

Approves the Cash and Short-Term Investments Policy attached as Appendix A to the report on the Revision to the Cash Investment Policy, Doc #12e.

3. Executive summary

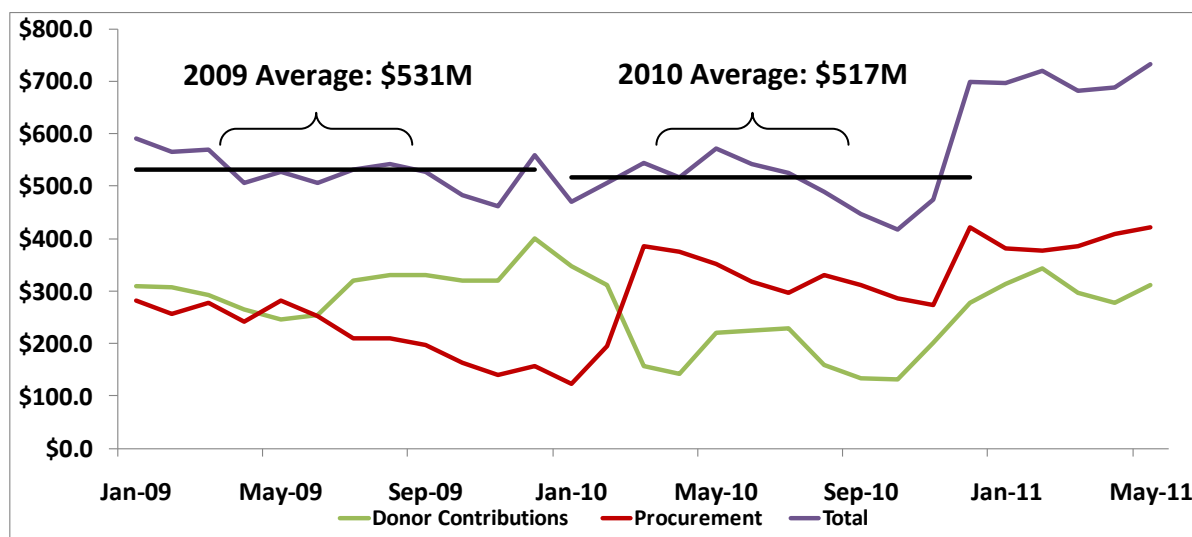
- 3.1 The GAVI Alliance Board approved the current Cash Investment Policy in June 2009. The permitted investments according to that policy include **money market funds** and **bank deposits**.
- 3.2 The GAVI Alliance Secretariat receives donor contributions on an ongoing basis. Most of these funds are subsequently transferred to a vaccine procurement account when UNICEF places orders for GAVI-supported vaccines, and held in that "Procurement Account" until paid to UNICEF when the vaccine payment becomes due some months later. Prior to being

transferred to the Procurement Account, donor contributions are held in GAVI's general cash pool, as are funds that will be disbursed for cash-based support and business plan costs. Thus, there are two cash pools held by the GAVI Alliance:

- (a) Donor contributions pool (\$311 million as of 31 May 2011); and
- (b) Procurement Account (\$422 million as of 31 May 2011).

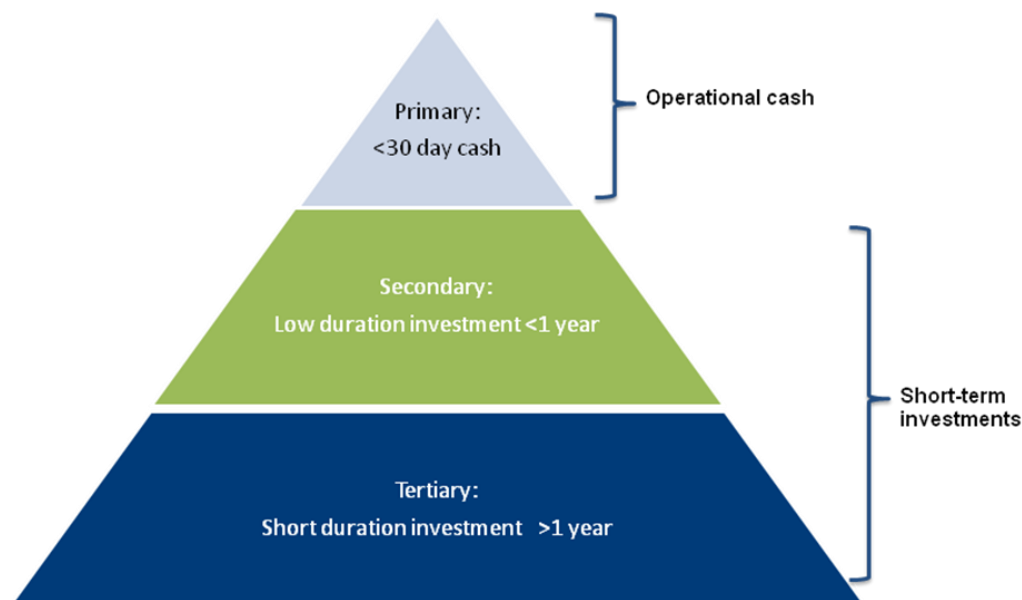
- 3.3 If approved, the proposed Policy will initially be implemented for the donor contributions pool. Depending on the outcome of discussions regarding cash management with UNICEF (Finance and Supply Division), the Policy may in the future be implemented for the Procurement Account.
- 3.4 At the 18 March 2011 Investment Committee meeting, the Secretariat presented the current Cash Investment Policy framework, noting that it supports an underlying need for daily liquidity. However, the historical pattern of spending and the cash forecast indicates that GAVI Alliance does not require daily liquidity. The graph below depicts the monthly cash balances for the two cash pools. While the cash balances clearly move from month-to-month, there is also a significant core amount that is retained.

GAVI Alliance Cash Balances (\$ Millions)



- 3.5 Therefore, GAVI's cash pools may be more effectively managed if the Secretariat had additional high quality, liquid investment options to stratify the cash pools, allowing them to manage to a weighted investment horizon of one year, in order to increase investment returns.
- 3.6 The Investment Committee concurred with the Secretariat's proposal for a stratification of the cash pools into Operational Cash (i.e., 30-day cash

requirements) and Short-Term Investments, whereas the existing Cash Investment Policy does not permit Short-Term Investments.



- 3.7 The amount invested in each component will depend on the rolling 12-month cash forecast. In other words, the proposed Policy does not contemplate a set of static policy targets for each component. If the Secretariat forecasts a month (i.e., 30-day cash requirements) of high expenditures, then the allocation to Operational Cash will be high. Conversely, if the forecasted expenditure for a specific month is low, then the allocation to Operational Cash will be low.
- 3.8 The proposed Policy deepens the investment guidelines and the limits on acceptable securities for Operational Cash from existing levels, particularly with respect to credit, maturity and sector limits of money market funds, the main investment used in this category. For details, please refer to Appendix A, sections 5.4 and 5.5 of the Policy.
- 3.9 As noted in Section 3.6 above, the proposed Policy extends the list of permitted investments to include Short-Term Investments, such that the list of permitted investments would be as follows:

Investment	Category	Management
Deposits	Operational cash	Internal (GAVI staff)
Money Market Fund	Operational cash	External (fund manager)
Low Duration Fixed Income	Short-term investments	External (fund manager)
Short Duration Fixed Income	Short-term investments	External (fund manager)

- 3.10 The 2 main components of Short-Term Investments are low duration fixed income and short duration fixed income. The proposed Policy provides broad investment guidelines and limits on acceptable securities, including credit and sector limits, for Short-Term Investments. These guidelines and limits, as detailed in section 6.4 of the Policy, have been reviewed by the Investment Committee.
- 3.11 Low duration and short duration fixed income are graduated extensions of money market funds; they invest in similar, short-dated securities. Table A on page 7 provides a comparison of security types.

4. Context

- 4.1 By way of comparison, the table below illustrates the net investment performance (i.e., net of fees) of the existing money market fund versus the investment strategies that are currently under consideration. (Deposits are excluded from this comparison as they are used selectively so parallel data is not available.)

	Operational Cash	Short –Term Investments	
	Money Market (a)	Low Duration (b)	Short Duration (c)
2001	4.08%	5.76%	8.06%
2002	1.68%	3.90%	6.19%
2003	1.04%	1.61%	2.30%
2004	1.23%	0.89%	1.21%
2005	3.09%	2.30%	1.99%
2006	4.84%	4.78%	4.57%
2007	5.09%	5.19%	6.33%
2008	2.76%	4.02%	3.88%
2009	0.50%	1.92%	5.20%
2010	0.12%	1.16%	3.29%
YTD 2011(d)	0.07%	0.56%	1.25%

- (a) JPMorgan US Dollar Liquidity
(b) Dimensional One-Year Fixed Income Portfolio
(c) JPMorgan Short Duration Bond Fund
(d) Year-to-date net performance through May 2011

- 4.2 As a result of the severe market dislocation in 2007 and 2008, the US Securities and Exchange Commission (“SEC”) adopted new rules for money market funds in 2010. Examples of the new rules include increasing the credit quality, reducing the maximum weighted average maturity, and imposing minimum levels of daily liquid assets and weekly liquid assets. GAVI had been invested in the highest quality money market funds known as prime money market funds so the new maturity and liquidity rules were the primary changes that affected cash investments.
- 4.3 The implication of the new SEC rules for money markets is that current and future net returns will not be comparable to pre-2010 net returns. The

regulatory limits have led, and will continue to lead to relatively low net investment performance. Accordingly, access to high-quality short-term investments will be necessary in order to enhance investment performance.

5. Conclusions

- 5.1 The proposed Cash and Short-Term Investments Policy will allow GAVI to generate additional investment income with a prudent level of risk. The Investment Committee considered and endorsed the proposed Cash and Short-Term Investments Policy.

Section B: Implications

6. Impact on countries

- 6.1 While there is no direct impact on countries, the Secretariat expects the proposed Policy will provide more net investment income to support programmes than would otherwise be expected under the existing Cash Investment Policy.

7. Impact on the Business Plan / Budget / Programme Financing

- 7.1 There will be additional due diligence requirements consistent with the hiring of new investment managers. However, the GAVI Investments Team has a strong risk management infrastructure in place, and anticipates that the implementation of the proposed Cash and Short-Term Investments Policy can be managed with existing staff levels.

8. Risk implications and mitigations

- 8.1 Like the existing policy, the proposed Cash and Short-Term Investments Policy would maintain capital preservation as a primary objective. The Secretariat believes that GAVI can adhere to a prudently conservative stance by expanding the objectives to the following:
- (a) Preserve the value and safety of the principal involved;
 - (b) Maintain liquidity coordinated with the anticipated cash requirement; and
 - (c) Provide prudent diversification of risk to minimise market and credit exposure.

- 8.2 Operational Cash and Short-Term investments face similar risks. A majority of the risk can be mitigated given the investments strategies are inherently conservative, as summarized in the following table:

Risk	Assessment	Mitigating Factors
Credit	Low	High quality securities
Liquidity	Low	- Diversified pools - Short Maturities
Duration^(a)	Low	- Short Maturities - Exposure to floating rate securities
Income	Medium	Investment income will be subject to changes in yield curve; however, expansion into Short-Term Investments will provide an opportunity to increase investment income.

(a) Duration is the sensitivity of fixed income securities to changes in interest rate levels, or a measure of the volatility of bond prices.

9. Legal implications

- 9.1 The Secretariat expects to utilise investment funds that will have standard documentation so GAVI Alliance Legal team should be able to review the investment management documents. However, the Legal team may opt to use outside counsel for a review.

10. Consultation

- 10.1 The Investment Committee as well as internal constituents within the GAVI Alliance Secretariat were consulted. Several external constituents on the GAVI Alliance Board have also been consulted.

11. Gender equality implications

- 11.1 There are no gender equality implications.

12. Implications for the Secretariat

- 12.1 As noted in Section 6, the Secretariat expects the proposed Cash and Short-Term Investments policy will provide more net investment income to support GAVI programmes.

Table A. Comparison of security types

	Operational Cash	(new) Short-Term Investments	
	Money Market (a)	Low Duration (b)	Short Duration (c)
Deposits	X	X	
US Government Agency	X	X	X
Government	X	X	X
Supranational		X	
Corporate Bonds	X	X	X
Repurchase Agreements	X		
Bank Notes		X	
Asset Backed			X
Mortgage			X
Municipal			X

(a) JPMorgan US Dollar Liquidity

(b) Dimensional One-Year Fixed Income Portfolio

(c) JPMorgan Short Duration Bond Fund

APPENDIX A

DOCUMENT ADMINISTRATION

VERSION NUMBER	APPROVAL PROCESS	DATE
1.0	Reviewed by: GAVI Investment Committee	26 May 2011
	To be approved by: GAVI Alliance Board	08 July 2011
		Effective from: 08 July 2011
		Review: Periodical, at least annually, by the GAVI Alliance Secretariat

GAVI Alliance Cash and Short-Term Investments Policy

1. Introduction and scope

- 1.1 The purpose of this Cash and Short-Term Investments Policy is to assist the Investment Committee (“Committee”), and the Managing Director of Finance & Operations and his/her designates (the “Finance staff”) of the GAVI Alliance, in effectively supervising, monitoring, and managing cash and short-term investment assets under its care.
- 1.2 Cash and Short-Term Investments are differentiated for purposes of this Policy from the GAVI Alliance Investment Portfolio, which is subject to the Investment Policy approved in June 2009.
- 1.3 There are 2 components referenced in this Policy:
 - a) Operational Cash, being cash and cash equivalents held to cater for 30-day operational needs of the Alliance; and
 - b) Short-term investments, which includes low and short duration fixed income mandates.
- 1.4 This Policy does not apply cash and short-term investments managed by the GAVI Campaign or the World Bank. These investments are subject to the investment policies of these entities.
- 1.5 This Policy shall apply to the vaccine procurement accounts opened for the benefit of UNICEF as well as contributions received directly and managed by GAVI Alliance.

2. Cash and Short-Term Investments goal statement

- 2.1 The cash entrusted to the GAVI Alliance originates from sovereign and private donors. For that reason, capital preservation is a primary goal. Interest income will be sought where consistent with the primary investment goal of capital preservation.
- 2.2 The primary objectives of the GAVI Alliance’s cash and short-term investments, in order of priority, shall be to:
 - Preserve the value and safety of the principal involved;
 - Maintain liquidity coordinated with the anticipated cash requirement; and
 - Provide for prudent diversification of investments to minimise credit and market risk exposure.

3. Manager and financial institution requirements

- 3.1 The assets may be invested by qualified internal staff according to the limitations outlined herein or by qualified external specialty investment managers who have demonstrated skill in a particular asset class.

- 3.2 Internal staff shall have the requisite authorization to execute individual investments in cash and cash equivalents from the Managing Director of Finance and Operations in consultation with the senior staff of the Investments and Treasury teams. Execution of investments with approved institutions by authorised staff is subject to a formal review and approval process.
- 3.3 The GAVI Alliance shall retain qualified external investment managers to manage portfolios based on a specific style and methodology, including money markets, low duration fixed income, and short duration fixed income. External managers will be given full discretion to invest the assets of their portfolios subject to staff review and approval of the manager's prospectus, offering memorandum or the investment guidelines incorporated into the investment management agreement executed with the GAVI Alliance.
- 3.4 The GAVI Alliance will use sound banks in the management of cash. Selected banks shall have a minimum credit rating of A+ or A1 as measured by a major credit rating agency. In addition, banks must display a record of stability in retaining assets and clients. Banks retained by GAVI Alliance shall use their best efforts to obtain the most favourable execution with respect to transactions implemented on behalf of GAVI Alliance. If the credit rating from two of these three sources falls below the minimum level, Finance staff will move the Cash to a bank that complies with the minimum required credit rating as soon as reasonably possible.

4. Permitted cash and short-term investments

- 4.1 GAVI Alliance Cash and Short-term Investments placed with financial institutions will be held in the following Permitted Investments:
 - a) Bank Deposits (see Sections 3.4 and 5.4 for limitations)
 - b) Money Market Funds (see Section 5.5 for limitations)
 - c) Low duration fixed income investment
 - d) Short duration fixed income investment
- 4.2 The Permitted Investments (a - d) may be invested in security types described in Attachment 1. See Section 5 for the specific objectives and guidelines.
- 4.3 The vaccine procurement accounts may invest in the Permitted Investments subject to mutual agreement with UNICEF.

5. Operational cash objectives and guidelines

- 5.1 The primary objective of Operational Cash, comprised of cash and cash equivalents, is to provide capital preservation such that GAVI Alliance can meet its 30-day operational cash needs. Daily liquidity shall be maintained to meet the organisation's immediate cash requirements.

5.2 The benchmarks for the cash portfolios may include the following indices:

Seven-Day USD LIBID

Citigroup 3-Month T-Bill

5.3 Cash investment managers, including both internal staff and external managers retained by the GAVI Alliance, will invest with a capital preservation objective and will be evaluated against specific market indices which represent their investment strategy. In addition, investment results may also be compared to a peer group of returns from other managers investing with a similar style.

5.4 **Internally managed operational cash:** The Managing Director of Finance and Operations, in consultation with the senior staff of the Investments and Treasury teams, may authorise certain cash investments to be managed by qualified staff of the GAVI Alliance. General guidelines for such internal cash management include the following:

- a) Deposits shall only be placed directly with banks that have a minimum long-term rating of A+ or A1 as measured by major credit rating agency. The maximum maturity of deposits placed directly with banks shall be 92 days. In addition, the maximum deposit amount placed with a bank shall be 20% of Operational Cash or \$25 million, whichever is higher.
- b) The provisions of the Credit Ratings section of Policies and Procedures documented in the most recent GAVI Alliance Investment Policy (for the long-term investment portfolio) shall apply regarding credit ratings, split rating and downgrades.

5.5 **Externally managed operational cash:** Operational Cash investments may be made through qualified external specialty investment managers of money markets mandates. Any exemption from the general cash guidelines or the manager's separate account guidelines requires prior approval from the GAVI Alliance. General guidelines for external cash managers include the following:

- a) Managers may invest in U.S. dollar-denominated fixed income securities with maturities of less than thirteen months at time of purchase, issued by or guaranteed by the national and local governments, government agencies as well as commercial paper, bankers' acceptances, certificates of deposit, corporate debentures, and money market or mutual funds.
- b) External investments shall have limits on concentration, credit quality, liquidity and maturity that are broadly in line with the requirements of Rule 2a-7 of the Investment Company Act of 1940.
- c) Sector Exposure: Acceptable investments and their limitations are as follows:

Security Type	Maximum Exposure ¹	Maximum Maturity
Obligations of the United States Government, its agencies and instrumentalities, taxable and tax-exempt, and repurchase agreements collateralised by such obligations.	100%	13 months
Obligations of state and local governments, and their agencies and instrumentalities, taxable and tax-exempt.	50%	13 months
Corporate or deposit notes	50%	13 months
Commercial paper	50%	270 days
Banker's acceptances	50%	90 days
Certificates of deposit	65%	31 days
Mutual or money-market funds with investment guidelines similar to the above.	100%	60 days

d) Credit Quality:

- External investments shall have an average credit rating of AA- or Aa3 as measured by a major credit rating agency.
- The provisions of the Credit Ratings section of Policies and Procedures documented in the most recent GAVI Alliance Investment Policy (for the long-term investment portfolio) shall apply regarding credit ratings, split rating and downgrades.

6. Short-Term Investments objectives and guidelines

- 6.1 The primary objective of the Short-Term Investments portfolio is to provide stable investment returns and to generate income while diversifying GAVI Alliance's investment assets. At a minimum, the GAVI Alliance shall maintain monthly liquidity in the portfolios such that assets may be liquidated when the pool of cash and cash equivalents for 30-day Operational Cash must be replenished.

¹ All percentages expressed herein shall be applied as of the time of purchase unless otherwise stated. The limits shall apply to individual securities and the weighted average characteristics of any mutual fund or other commingled vehicle in which The GAVI Alliance may hold a share of beneficial interest.

- 6.2 The benchmarks for the short-term investment portfolios may include the following indices:

B of A Merrill Lynch 6-Month US Treasury Bill Index

B of A Merrill Lynch 1-Year US Treasury Note Index

Barclays 1-3 Year Government / Credit Index

Barclays 1-5 Year Government / Credit Index

Barclays 1-3 Year Aggregate Index

- 6.3 External managers retained by the GAVI Alliance, will invest with a stable investment return and income objective, and will be evaluated against specific market indices which represent their investment strategy. In addition, investment results may also be compared to a peer group of returns from other managers investing with a similar style. Any exemption from these guidelines or the manager's separate account guidelines requires prior approval from the GAVI Alliance.
- 6.4 Short-term investments shall be made through qualified external specialty investment managers of low and short duration fixed income mandates. General guidelines for the managers include the following:
- a) Managers may invest in fixed income obligations issued by or guaranteed by national and local governments, government agencies, supranational organizations, banks and corporations, including mortgage and asset-backed securities, structured credit fund issues, and money market instruments.
 - b) The weighted average duration of any portfolio shall not exceed the applicable benchmark duration by more than 20%.
 - c) Managers may use spot and forward currency contracts and currency futures.
 - d) Derivative strategies and over the counter futures, options and swaps may be utilised if positions are consistent with the manager's overall investment strategy. Exchange traded futures may be utilised without approval prior to implementation. Specifically, derivatives may be used to a) provide a duration exposure at a lower cost than is possible in the cash market, b) manage the overall duration of the short duration portfolio, and c) hedge. No derivative positions can be established to create positions or exposures that are otherwise prohibited by the policy guidelines.
 - e) The manager may not create leverage within the short duration portfolio through actively borrowing funds via reverse repo, a credit facility, or any similar mechanism in order to purchase securities in addition to equity capital.

- f) Managers may not invest in non-publicly offered securities with the exception of securities issued pursuant to SEC Rule 144-A or Regulation S.
- g) Sector Exposures: Acceptable investments and their limitations are as follows:

Security Type	Maximum Exposure ²
Obligations of the United States Government, its agencies and instrumentalities.	100%
Obligations of state and local governments, and their agencies and instrumentalities.	25%
Mortgage-backed and asset-backed securities.	35%
Corporate debt securities issued by U.S. based corporations.	50%
Obligations of international agencies denominated in U.S. dollars.	25%
Regulated futures contracts traded in the U.S. capital markets.	25% of notional principal amount
U.S. Dollar-denominated instruments issued by Non-U.S. issuers.	25%
Non-Dollar securities or currency-related instruments	10%
Single issuer (that is not the US government or its agencies) For all asset-backed and mortgage-backed securities, if backed by a discrete pool of loans, the security will be considered a unique issuer.	5%

h) Credit Quality:

- The minimum credit rating, at time of purchase, of any issue shall be BBB- or Baa3 as measured by a major credit rating agency.
- The minimum average quality rating of the portfolio will be AA- or Aa3 as measured by a major credit rating agency.
- The provisions of the Credit Ratings section of Policies and Procedures documented in the most recent GAVI Alliance Investment Policy (for the long-term investment portfolio) shall apply regarding credit ratings, split rating and downgrades.

² All percentages expressed herein shall be applied as of the time of purchase unless otherwise stated. The limits shall apply to individual securities and the weighted average characteristics of any mutual fund or other commingled vehicle in which The GAVI Alliance may hold a share of beneficial interest.

7. Policies and procedures

- 7.1 The Policies and Procedures documented in the most recent GAVI Alliance Investment Policy (for the long-term investment portfolio) will also apply to all investments addressed herein. These policies and procedures address Custody of Assets, Use of Derivatives, Securities Lending, and Credit Ratings.

8. Monitoring

- 8.1 GAVI Alliance Finance staff shall monitor the monthly performance of internally managed investments and external specialty investment managers to assure that the Alliance's cash investment objectives are being met. Staff shall report to the Board and the Committee at least semi-annually on cash and short-term investment activities and matters of significance.
- 8.2 Confirmations, safekeeping notices and maturity notices shall be kept on file and are subject to GAVI Alliance's document retention policy.
- 8.3 For further details on monitoring, please see the sections *Investment Management Policy* and *Management Review Procedures – Responsible Parties* of the GAVI Alliance Investment Policy Statement.
- 8.4 The guidelines herein shall be reviewed periodically, and at least annually, by the GAVI Alliance to ensure they are aligned with corporate objectives and funding obligations.

Attachment 1 of Appendix A

Permitted categories of Cash and Short-term Investments

The following broad categories of securities shall be authorised:

Security Type
1. US Government securities: this category consists of Treasury obligations and federal agency issues. Treasury bills and notes and other explicitly guaranteed securities carry the full faith and credit of the United States and, as such, represent the lowest risk investments. Federal agencies—such as Fannie Mae, Freddie Mac, Federal Home Loan Bank and Federal Farm Credit Bank—are institutions chartered by the US Government but their debt is not explicitly guaranteed by the US Government. Nonetheless, agency debt is considered very high quality, and therefore represents low risk investments.
2. Bank obligations: this category consists of bankers' acceptances ("BAs"), certificates of deposit ("CDs") and deposit notes. BAs are short-term obligations of the bank, and so represent the credit risk of the bank. CDs are insured by the FDIC in amounts up to \$250,000. Permissible CDs include <i>domestic</i> CDs, <i>Eurodollar</i> CDs (offshore deposits) and <i>Yankee</i> CDs (US deposits in foreign banks). Deposit notes are negotiable bank CDs.
3. Corporate Debt: debt obligations of companies. Permissible investments include <i>money market funds</i> (funds that invest in corporate debt, among other short-term securities), <i>commercial paper</i> (corporate debt issued with a term less than 270 days), and <i>medium-term notes</i> (corporate debt issued with terms from 270 days to ten years).
4. Municipal Debt: debt obligations of municipalities that include general obligation bonds, tax anticipation notes, revenue anticipation notes, and bond anticipation notes.
5. Repurchase Agreements: repurchase agreements involve the acquisition of immediately available funds through the sale of securities with a simultaneous commitment to repurchase the same securities on a date certain within one year at a specified price. Repo transactions have many characteristics of secured lending arrangements in which the underlying securities serve as collateral.
6. Mortgage Backed Securities: debt obligations backed by pools of mortgages issued by Freddie Mac, Ginnie Mae, Fannie Mae and private institutions. Permissible investments include, but are not limited to, collateralised mortgage obligations, mortgage pass-through securities, commercial mortgage-backed securities, stripped mortgage-backed securities.

7. **Asset Backed Securities:** debt obligations backed by loans, leases or accounts receivable originated by finance companies, banks or other providers of credit. Permissible investments include, but are not limited to, securities backed by automobile, credit card and other consumer assets that have short to intermediate-term maturities because they are backed by relatively short-term assets.