

# **MDB Response to the G20 Action Plan for MDB Balance Sheet Optimisation July 2016**

## **Objective**

The G20 approved the MDB Action Plan on Balance Sheet Optimisation at the 2015 November Antalya meeting. This is part of the wider global agenda on resource mobilisation for supporting SDGs and infrastructure in particular. The Action Plan asks the MDBs to work with their respective shareholders to consider a series of measures that could increase lending through balance sheet optimisation; more effective and efficient use of their existing risk bearing capital to maximize the impact of their activities. Balance sheet optimisation takes into account increased risk sharing to enable more effective capital usage or increased amounts of third party, private sector financing or investment. The Action Plan states that the optimisation is to be done without jeopardising the MDBs' AAA credit ratings, nor adversely impacting their ability to lend in cyclical downturns.

## **Background**

The MDBs for purposes of this paper include: the African Development Bank (AfDB), Asian Development Bank (ADB), European Bank for Reconstruction and Development (EBRD), European Investment Bank (EIB), Inter-American Development Bank (IDB), International Bank for Reconstruction and Development (IBRD) and International Finance Corporation (IFC). The MDBs have varying missions, different shareholding structures and different risk characteristics. As a result and by design, the MDBs business models vary considerably: levels of sovereign and private sector lending and investing, product mix (debt and equity), geographic coverage, level of preferential creditor treatment, as well as access to callable capital, concessional windows, grant monies and donor funds. Against this background, the Boards and management of each MDB need to act based on their understanding of their institution's risk bearing capacity, development objectives as well as sound financial and risk management practices.

In the light of the objectives of maintaining the MDBs' AAA credit ratings without adversely impacting their ability to lend in cyclical downturns, MDB Boards need to consider the factors, in addition to leverage, that impact ratings, such as the ability to generate and retain earnings, portfolio concentration and the relatively illiquid nature of development exposures, business model, funding, market access and liquidity, franchise value and market perception, relevance of their operations to clients' changing needs, shareholders' credit ratings and how rating agencies perceive shareholders' support (e.g. willingness and ability to pay in additional capital in a timely manner or looking at net income allocations).

Given the difference in the rating agencies methodologies which continue to evolve, the MDBs' ability to maintain a AAA rating is dynamic. Accordingly, each MDB must have its own internal approach and models to managing its ratings and financial sustainability.

The MDBs continuously work to ensure their financial sustainability and to meet their strategic objectives as set out in their respective Board approved business plans. The ongoing development and refinement of financial and risk management practices and policies (capital adequacy, prudential limits, provisioning and treasury policies, stress testing, etc.) and reporting continues to provide the Boards with better understanding of the MDBs' risk profiles and capacity. Future capacity will be subject to the events arising in the operating sphere of each of the MDBs and can change materially.

The slowdown of growth, actual or perceived vulnerability of financial systems (NPLs and regulatory changes), turmoil in equity, commodity and currency markets, political economy of respective countries of operation and geo-politics creates an environment of considerable uncertainty. This has led to substantial capital outflows from emerging markets, and a slowing or reduction of domestic and foreign direct investment in many regions of the world. For a number of the MDBs this creates a real challenge of identifying eligible private sector "bankable projects". The inflow of central bank money in some regions is feeding high liquidity in the banking systems, which makes MDBs' money more expensive. The exceptionally low interest rates in recent years and recent trends towards negative rates in a number of countries, and downgrading of sovereign and bank ratings have significantly reduced MDBs ability to generate income and grow their capital base. For MDBs with equity portfolios, the sharp decline in equity markets has reduced income and capital.

Regulatory changes pose challenges to the MDBs in many ways. For the MDBs which work with financial institutions as an important part of their private sector business model delivery, capital requirements and regulatory compliance ultimately increase the cost of doing business for the private sector clients. The cost of doing business with MDBs can also increase due to regulatory treatment of MDBs' hedging activities. MDBs' ability to increase investment and mobilise capital through B loan structures, insurance companies or pension funds is directly related to the capital relief or other constraints for third party investors provided under regulation. Under new regulations, the MDB loans, including trade finance, to partner banks are eligible for bail-in, thereby increasing the risk of these loans. All of these have an impact on the cost to the ultimate borrowers or, in the case of sovereign borrowers, are absorbed by the MDBs. Furthermore, MDBs have to take into account these regulatory changes in the context of their risk policies and the way the rating agencies consider such developments as "market practice" for rating purposes.

With respect to net income measures in the Action Plan and while some MDBs have implemented cost saving measures, it is important to note that institutional effectiveness should be considered along with the institutional efficiency. To ensure the effectiveness of operations, it is prudent, to the extent growth of operations is envisaged, to match plans for substantial increases in investing with a more strategic staffing framework and provide commensurate level of budgetary resources to support all aspect of operations and facilities including attracting and retaining staff.



## G20 Action Plan for MDB Balance Sheet Optimisation



In summary the G20 Action Plan includes the following five actions:

1. Engage with shareholders and credit rating agencies with options for increased capital efficiency while maintaining AAA ratings and highest standards of balance sheet quality.
2. Consider fully deploying exposure exchanges as a mechanism to reduce sovereign concentration risk.
3. Develop concrete proposals for financial innovations using their concessional windows within prudential risk management and debt sustainability frameworks.
4. Evaluate full range of instruments that share risk in their non-sovereign operations with private investors to free up risk capital or crowd-in and mobilize additional resources. Risk transfer should also be considered, e.g., through guarantees or concessional finance from donors.
5. Engage shareholders in considering net income measures that could improve their capital position. Examine value-for-money agenda.

The MDBs have been and continue to undertake a number of measures to ensure they continue to meet their mandates. The tables in the annex outline each MDB's response to the five action points, setting out activities already implemented as well as areas for additional future work. Below is a table which summarises these actions:

	Capital Efficiency	Exposure Exchanges	Concessional Windows	NSG Risk Transfer and Mobilization	Net Income Measures
AfDB	↑	✓	→	→	✓
ADB	↑	→	↑	↑	✓
EBRD	✓	≠	≠	→	↑
EIB	✓	→	≠	↑	✓
IDB	✓	✓	↑	→	✓
IBRD	↑	✓	↑	→	→
IFC	✓	≠	≠	✓	↑

 Measures Implemented  
 Measures Under Implementation

 Additional Work Planned  
 Not Applicable

The table above shows that the MDBs are already highly engaged around all five of the G20 Action Plan recommendations.

In summary, the applicable action plans have been implemented as relevant at all of the institutions:

1. **Capital efficiency:** a majority of institutions has revised their capital metrics and implemented policies aimed at more efficient use of capital, while also taking into consideration rating agency perspectives. While refinements in this area will continue, there is limited scope for material changes without also affecting the current rating strength of the institutions.
2. **Exposure exchanges:** five institutions have collaborated in establishing a framework and three have signed agreements consistent with their respective portfolio needs. While there is limited scope for further exchanges for some of the institutions that have already participated, MDBs are nevertheless open to exchanges with other institutions in the future in accordance with the development of their portfolios and risk profiles.
3. **Concessional windows:** these measures are only applicable to a subset of institutions, two of which are close to merging the windows into ordinary capital and one is already actively discussing measures to leverage the concessional window.
4. **NSG risk transfer and mobilization:** all institutions with private sector portfolios are active in this area. The key to implementation is to find the right balance between scarce first-loss capacity and risk-revenue sharing. Co-investment capacity is also in limited supply.
5. **Net income measures:** available actions in this domain have already been deployed or are underway. Some of these measures need to be implemented in ways that do not negatively affect the business profile of the institutions as assessed by rating agencies.

With all the recommendations already implemented or underway, MDBs are successfully implementing efforts to optimise their capital. Further benefits may be gained in those areas where additional future work is being planned, and ongoing development may lead to new action opportunities. As outlined in the attached annexes, in addition to measures already undertaken, a number of the MDBs have also identified such areas for future work. They will work on these additional ideas and develop concrete action steps as these ideas evolve.

After several decades of expansion, the global financial system is undergoing a generalised retrenchment, particularly acute in the case of banks and bond markets. In many markets, the Development Banks and governments are among the principal lenders able to fund development projects. MDBs ability to mobilize investment is a key element to future meeting financing needs. As demonstrated in this note, MDBs are committed to efficiently and effectively utilise existing capital and to continue to develop, in a collaborative manner, new means of leveraging it while also recognizing, as the G20 Action plan paper states, that

these measures are complementary to other efforts to strengthen the capacity of these institutions.

### **Areas Where G20 Engagement Is Needed**

There are a number of areas where MDBs believe G20 engagement can make a real difference in our shared agenda of scaling-up of financing for development.

Maintaining a 'AAA' rating is one of the conditions set-out in the G20 Action Plan. MDBs are a very efficient way to deploy development finance, not only because they combine capital with funds raised on the bond markets, but also because they are able to diversify risk across a larger number of shareholders and projects. The Rating Agencies look to the intentions and support of MDBs shareholders as part of the rating process.

Furthermore, with an increasingly challenging external environment, very low or negative interest rates in developed markets together with the earnings spread between funding and investment rates are taking a toll on some MDBs capacity to generate capital from internal sources. This is a relatively new development which has had a direct consequence in terms of MDBs ability to scale their operations in line with the development financing needs. The reduction of relative capacity is undesirable in a low growth environment where MDBs are asked to step up and increase investment levels.

The MDBs continue to review their operations and efficiencies to improve capital capacity, but to help the MDBs deliver on their mandates while maintaining their "AAA" ratings and crisis lending capacity, and using their financial assistance to catalyse, mobilize and crowd-in both public and private sources of funds for development, the G20 could assist the MDBs by considering the following actions:

1. The G20 to clearly express their support for the key role of MDBs in increasing the level of financing to achieve the SDGs and in mobilizing public and private sector investment. That may help strengthen the rating agency perception of shareholder support.
2. A complementary action to reinforce the support for MDBs' key role is to reconsider the current approach to Net Income Allocation across the MDBs which is not sustainable, particularly as long as the current interest rate environment persists.
3. Increased donor funds provided for non-technical cooperation / ODA countries to expand first loss coverage and other forms of structured investments would further assist the MDBs in mobilising private financing.
4. The G20 to encourage their own export credit agencies (ECAs) to recognize the preferred creditor status granted to MDBs as unique to them and to explore more practical and flexible solutions in inter-creditor arrangements for co-financing with MDBs. This would benefit the economies of emerging markets by bringing more debt capitals from both ECAs and MDBs as well as mobilizing more private sector capital through MDB B loans and ECAs' co-financing products.

5. The MDBs would welcome the G20 pursuing directly through the Financial Stability Board and more broadly through the Basel Committee an agenda that takes under consideration of the unintended consequences of regulation. In particular:
  - a. The capital treatment of the various asset classes that is central to mobilisation of private sector investment, from longer term loans (in particular capital treatment for B loans) to equity (capital treatment for equity funds) and structured finance.
  - b. The capital treatment for investors of their exposures to MDBs in light of the possible Basel Committee revision of sovereign risk treatment, thus ensuring steady demand for MDB bonds and low funding cost needed to execute the MDB mandates.

This support will strengthen the market perception of MDBs which, in turn, will further enable the MDBs to attract, develop and retain globally minded talent, motivated by achieving development goals and able to continue promoting a collaborative agenda.

#### **Annexes: Individual MDB Action Plans**

1. African Development Bank
2. Asian Development Bank
3. European Bank for Reconstruction and Development
4. European Investment Bank
5. Inter-American Development Bank
6. International Bank for Reconstruction and Development (World Bank)
7. International Financial Corporation

## African Development Bank (AfDB)

Action Item	What We Have Done	What More We Could Do	Constraints/Comments
<p><b>1 – Increased Capital Efficiency</b></p>	<p>In 2014, the Bank converted to a full economic capital model for more accurate capital adequacy measurement and setting of risk limits.</p> <p>To fully leverage its new economic capital model, the Bank switched to using default and loss data from the Global Emerging Markets (GEMS) risk database. MDBs established GEMS in 2009 to pool credit risk data</p> <p>The Board of Directors also approved a reduction in the risk capital charges for equity investments from 100% to 85% for unlisted and 75% for listed equity participations.</p>	<p>In 2016, the Bank will review its “risk appetite statement”. This may lead to further efficiency gains for capital charges and higher limits for certain core risks.</p>	<p>Although the AfDB’s internal capital adequacy model is used to inform management decisions, the S&amp;P RAC ratio is given almost equal weight. Therefore to the extent that improving our internal models causes a misalignment with the S&amp;P RAC ratio, there is limited scope for further efficiency gains.</p>
<p><b>2 – Exposure Exchanges</b></p>	<p>In 2015, the Bank executed the first MDB exposure exchange with the IBRD and IDB.</p> <p>In 2014, to enhance portfolio diversification, the Bank modified its credit policy to allow creditworthy low-income countries to have access, within defined limits, to the Bank’s non-concessional sovereign window.</p>	<p>In 2016, the Bank may consider further exposure exchanges with other MDBs, as well as other sovereign risk transfer mechanisms.</p>	<p>The AfDB’s initial exposure exchange approached the 50% minimum retention ratio for most of its major exposures. Therefore the AfDB has limited space for additional exposure exchanges until its loan book grows.</p>
<p><b>3 – Financial innovation using Concessional Windows</b></p>	<p>Beyond the diversification benefits, the amendment of the AfDB’s credit policy has significantly increased the flow of resources to creditworthy low-income countries.</p> <p>In 2015, the African Development Fund (AfDF) established a private sector credit enhancement facility (PSF) to share risk on non-sovereign lending in low-income.</p>	<p>In 2016, the AfDF will consider a limited program for borrowing from donors on concessional terms to augment regular replenishment resources.</p> <p>In 2016, the AfDF will consider borrowing from donors on concessional terms to smooth fluctuations in internally generated resources and thereby increase funding available over the medium-term.</p>	<p>The AfDF was established by international treaty. Therefore there is limited scope for a simple “merger” as has been done by the ADB. As a result, for now the AfDF will approach the issue of leverage from other angles including how to catalyse more private sector financing in low income countries.</p>

	<p>In 2010, the AfDB and AfDF established a partial risk (PRG) and partial credit guarantee (PCG) programs.</p>	<p>In 2016, the AfDF will consider scaling up the private sector credit enhancement facility.</p> <p>In 2016, the AfDF may also consider adding an instrument to subsidize the interest rate for low-income countries borrowing from the Bank's non-concessional window countries.</p>	
<p><b>4 – Greater use of risk sharing instruments</b></p>	<p>Since 2010, the Bank has had a syndication program using A/B loan structure designed to catalyse commercial financing for non-sovereign operations.</p> <p>In 2005, the Bank concluded arrangements with Japan to provide \$1 billion in co-financing and direct resources for private sector development. The facility was replenished with \$2 billion in 2013.</p> <p>In 2014, the Bank concluded an arrangement with Central Bank of China for a \$2 billion co-financing facility managed by the Bank. Other similarly managed co-financing/risk sharing facilities are being developed.</p> <p>The Private Sector Facility (PSF) established by the ADF in 2015 is a concrete example of a risk transfer instrument designed to improve capital efficiency for the Bank and thereby increase lending capacity.</p> <p>In 2015, the Bank established the Africa 50 Infrastructure Fund (A50) with African countries as co-investors. A50 will co-finance commercially viable infrastructure</p>	<p>In 2016, the Bank may consider its first pilot synthetic securitization to transfer credit risk on a reference portfolio of seasoned non-sovereign operations to a commercial investor.</p> <p>In 2016, the Bank may consider its first sell-down of a portfolio of seasoned private equity funds to a commercial investor(s). This would create additional headroom for new equity investments.</p> <p>The Bank will examine other approaches as well to create additional headroom for new non-sovereign lending such as credit insurance.</p>	<p>MDBs enjoy preferred creditor status on non-sovereign lending that protects against currency transfer and convertibility risks. However, MDBs must be careful in extending preferred creditor treatment to third parties to avoid distorting markets and/or eroding preferred creditor treatment.</p>



	<p>projects with the AfDB and will help mobilize private financing.</p>		
<p><b>5 – Net Income Measures</b></p>	<p>Since 2007, the Bank has significantly increased the share of non-sovereign lending. The non-sovereign portfolio, which is priced for risk, has contributed to an increasing share of the Bank’s net income and reserve growth.</p> <p>In 2011, the Bank updated its income allocation policy to clarify the priority for ensuring adequate reserve growth, which is already enshrined in its charter, to support its risk-taking activity.</p> <p>In 2016, the Bank revised upwards its sovereign lending terms. This measure seeks to ensure that sovereign operations fully cover marginal operational costs and concentration risk.</p>	<p>In the future, the Bank may consider instituting a concentration premium for the largest sovereign borrowers.</p>	<p>The AfDB has traditionally made a significant contribution of net income to AfDF replenishments. In the short-term there may be limitations in the AfDB’s ability to scale down such contributions. However, as the AfDF adopts new innovations to enable it to scale up its resources, the AfDB’s income allocations may become less important.</p>
<p><b>Enhanced supervision of financial and risk management practices by shareholders</b></p>	<p>The AfDB has already adopted a full economic capital model for capital adequacy measurement and limit setting. This is fully disclosed to the Board both in terms of policy setting and semi-annual reporting. It is also disclosed to the rating agencies whenever policy changes are contemplated as well as the annual rating review discussions.</p>	<p>The next major improvement in the Bank’s capital adequacy framework is to consider incorporating a more advanced approach to measurement operation risk and the related capital requirements.</p>	
<p><b>Conclusion: Impact on planned business activities</b></p>	<p><b>Action Item 1:</b> Better measurement of risk and an optimized risk-based limit-setting framework has resulted in an overall increase in the Bank’s lending headroom as well as additional headroom for non-sovereign lending in higher risk (low income) countries. More accurate capital requirements for equity resulted in an increase in equity investing headroom.</p> <p><b>Action Item 2:</b> Increased diversification is expected to decrease the Bank’s sovereign concentrations and improve the Bank’s capital adequacy indicators and create up to \$10 billion of additional lending capacity. Expanding the number of eligible borrowers is</p>		

increasing the diversification of new sovereign lending and thus helping to slow the future build-up of sovereign concentration risks.

**Action Item 3:** In 2015, sovereign lending to low-income countries already represented 21% of total non-concessional sovereign lending by the AfDB. Within the first 3 years, the PSF is expected to catalyse an additional \$1 billion of AfDB non-sovereign lending in low-income countries. PRG/PCGs have enabled PPPs to be financed with only indirect sovereign credit support. It is also enabling countries to use currency swaps to manage foreign exchange risks when borrowing on the international capital markets.

**Action Item 4:** The AfDB's syndication program is still in its early stages. In 2016, the AfDB expects to mobilize at least \$1 billion through its A/B loan program. The facilities with Japan and China have enabled the Bank to significantly scale up its financing for the private sector. The PSF is expected to enable the AfDB to do an additional \$1 billion of private sector financing in low-income countries in the next 3 years. The pilot capital management transactions that the AfDB is examining are expected to pave the way for a mainstreamed program that could enable the Bank to recycle its risk capital and expand its private sector operations by up to 50% in the long-term.

**Action Item 5:** The AfDB's medium-term financial projections indicate a return to growth for internally generated reserves. This is expected to help the Bank's capital position.

## Asian Development Bank (ADB)

Action Item	What We Have Done	What More We Could Do	Constraints/Comments
<p><b>1A – Increased Capital Efficiency</b></p>	<p>Engaged shareholders on this topic several times in last few years:</p> <p>In 2012, ADB reviewed its capital adequacy framework leading to an expanded coverage of risks and a lowering of the main planning metric, the minimum ELR, from 26% to 25%.</p> <p>In 2013, ADB presented a paper on Enhancing ADB’s Lending Capacity to the Board which discussed various options (such as a combination of certain Asian Development Fund (ADF) resources with ordinary capital resources (OCR), an effective increase in loan charges and an increase in the guaranteed portfolio) to increase capital efficiency and lending volumes within a given capital envelope.</p> <p>In 2014, The Midterm Review of ADB’s Strategy 2020 identified a number of action items (such as expanding equity headroom, linking allocation of OCR resources to disbursements) to make ADB a more effective development partner.</p> <p>In 2015, the President approved a pilot implementation of the Economic Capital Planning Framework which provides incentives for more efficient use of the capital notionally allocated to non-sovereign operations.</p>	<p>A working paper for the Review of the Capital Adequacy Framework for the combined balance sheet will be submitted to the Board in Q2 2016. A final paper will be submitted to the Board for decision in Q3 2016. The revised framework will protect ADB’s AAA credit rating in light of projected growth in its risk exposures, particularly loan exposures. It will also broaden coverage to reserve capital for currency risk and a counter-cyclical risk buffer.</p>	<p>Working with Board to determine the size of the cushion to be added to required capital. This cushion would be a countercyclical buffer, cover for disaster risk, etc. and reduce the likelihood of a call on callable capital.</p>

Action Item	What We Have Done	What More We Could Do	Constraints/Comments
<b>1B – Engage Rating Agencies to Evaluate Simulations that More Fully Utilise Capital</b>	In 2014, ADB conducted extensive discussions with the 3 major rating agencies and hired one of these agencies for scenario analysis in connection with the decision to combine ADF with OCR.	No short-term need to revalidate present strategy.	ADB’s efforts towards capital efficiency should be based on its own capital adequacy framework. It may be useful for ADB to supplement these efforts by using the rating agency frameworks as a sanity check. This check can be performed without hiring the rating agencies.
<b>2 – Exposure Exchanges</b>	Active participant in inter-MDB working group which developed the concept and finalized technical details. Participated in the ratings evaluation of a proposed transaction.	Closely monitor the diversity of the operations portfolio post the ADF-OCR combination.	Concentration risk in the sovereign operations portfolio is anticipated to be largely mitigated after the ADF-OCR combination. This remains an option for future consideration after the combination of ADF with OCR has been completed and market-tested.
<b>3 – Financial innovation using Concessional Windows</b>	<p>Approval of combination of ADF-OCR in May 2015. This initiative is the most important contributor to balance sheet optimization for ADB since it will almost triple the equity base from about \$18 billion to about \$50 billion. A major benefit of the combination of resources is that ADB will be able to increase assistance to developing member countries (DMCs) by up to 50%.</p> <p>In particular, ADB assistance to lower-income countries—those most in need—will rise by up to 70%. While the combination will become effective in January 2017, ADB has already started to scale up its operations. The increase in resources will also strengthen ADB's response capacity for crisis lending and disaster financing.</p>	<p>Review entire financial and risk management framework to prepare for implementation of the ADF-OCR combination.</p> <p>Increased use of third party and donor funds.</p>	Major policies being reviewed to enable prudent and sustainable expansion of operations include the Capital Adequacy Framework, the Asset and Liability Management Policy, the Investment Strategy and Authority and the Concessional Assistance Policy. Detailed long-term financial scenarios have been developed to support this review.
<b>4 – Greater use of risk sharing instruments</b>	Since 2010, rapid increase in risk transfers to currently about 17% of the non-sovereign portfolio. These risk transfers have increased lending headroom by (i) improving portfolio quality by 1 rating notch, (ii) creating	ADB is exploring risk transfers in the sovereign portfolio.	<p>Low interest in sovereign portfolio due to low pricing.</p> <p>ADB will continue to promote risk transfers in the non-sovereign portfolio to:</p> <ul style="list-style-type: none"> <li>• Catalyse private sector investment to</li> </ul>

Action Item	What We Have Done	What More We Could Do	Constraints/Comments
	<p>new headroom of approximately \$970 million which is 19% of the current portfolio and (iii) diversifying the portfolio, thereby reducing concentration risk.</p> <p>Crowding in of additional resources through investment in the ASEAN Infrastructure Fund and the Credit Guarantee and Investment Facility as well as serving as lender of record for B loans.</p>		<p>DMCs, including via new counterparties such as reinsurance companies;</p> <ul style="list-style-type: none"> <li>• Improve credit quality and diversify the portfolio;</li> <li>• Reduce prudential limit utilization;</li> <li>• Increase overall headroom for lending operations;</li> <li>• Obtain a private sector opinion on ADB’s underwriting practices; and</li> <li>• Assure stakeholders including rating agencies and investors of sound non-sovereign underwriting policies.</li> </ul>
<p><b>5 – Net Income Measures</b></p>	<p>Effective 2012, ADB introduced maturity-based premia as part of sovereign loan pricing. This was followed by an increase in sovereign loan pricing in 2014. Ongoing implementation of the Strategy 2020 Midterm Review Action Plan aimed at implementation of corporate reform measures to improve corporate efficiency and contain budget growth at a sustainable level to support operations.</p> <p>Among the cost containment measures are (i) meeting a large part of the additional staffing requirements through staff redeployment and optimization, and (ii) a number of efficiency and cost-saving measures, ranging from departments and offices reprioritizing and sequencing resource requirements based on priority work programs and activities set for the medium term to identifying resource reallocations, trade-offs and measures to facilitate effective use of available resources.</p>	<p>Annual review of ADB’s sovereign loan pricing.</p> <p>Pending opportunities for degree and pace of automation and constant upgrading and integration of enterprise resource planning software tools, with commensurate reduction in manual data management functions.</p>	<p>Institutional effectiveness should be considered along with institutional efficiency. To ensure the quality and effectiveness of operations, it may therefore be prudent to match plans for substantial increases in lending with a more strategic staffing framework and provide commensurate level of budgetary resources to support all aspects of operations and facilities.</p> <p>As per guidance received from stakeholders, it is expected that the level of net income transfers from OCR to the ADF grant window from 2017 onwards will increase significantly, subject to annual approval by the Board of Governors (i.e., after the combination of ADF assets with OCR).</p>

Action Item	What We Have Done	What More We Could Do	Constraints/Comments
<p><b>Enhanced supervision of financial and risk management practices by shareholders</b></p>	<p>Provide extensive financial and risk information to Board on a quarterly basis including:</p> <ul style="list-style-type: none"> <li>• Financial statements</li> <li>• Capital adequacy metrics</li> <li>• Credit risk exposures</li> <li>• Market risk exposures</li> <li>• Operational risk exposures</li> <li>• Details of loans, liquidity and borrowings</li> <li>• Major cash flows and financial indicators</li> <li>• Break-up of operating income</li> <li>• Balance sheet projection and financial projection for ADB's three year planning period on a semi-annual basis</li> </ul>	<p>Continue working with peer MDBs and G20 representatives to explore most usable, practical and functional reporting format for the benchmarking purposes of the G20.</p>	<p>ADB is currently providing extensive financial and operational information to its Board.</p> <p>Availability of economic capital may be comparable across institutions. However, there is no inter-MDB and shareholder consensus on the definition of economic capital and so such benchmarking is difficult.</p> <p>ADB's financial and risk management policies are approved by the Board.</p>
<p><b>Conclusion: Impact on planned business activities</b></p>	<p><b>Action Item 1A:</b> A prudential increase in leverage will enable the optimization of lending headroom and the more efficient deployment of capital.</p> <p><b>Action Item 1B:</b> ADB's efforts towards capital efficiency should be based on its own capital adequacy framework which may be supplemented by rating agency frameworks.</p> <p><b>Action Item 2:</b> Exposure exchanges would have a marginal impact for the foreseeable future since the ADF-OCR combination diversifies the operations portfolio and relaxes the capital constraint.</p> <p><b>Action Item 3:</b> The ADF-OCR combination is the most important contributor to balance sheet optimization for ADB since it will almost triple the equity base from about \$18 billion to about \$50 billion.</p> <p><b>Action Item 4:</b> Continue expanding risk transfers to promote efficient and effective use of capital, increase the granularity in the loan portfolio, catalyse investments by a new class of private investors into developing Asia and enable improved management of prudential risk limits.</p> <p><b>Action Item 5:</b> Net income measures will lead to greater institutional efficiency.</p>		

## European Bank for Reconstruction and Development (EBRD)

Action Item	What We Have Done	What More We Could Do	Constraints/Comments
<p><b>1A – Increased Capital Efficiency</b></p>	<p>The Bank adjusted its Capital Adequacy Policy to make it more risk sensitive to better measure capital adequacy. At an overall level the Policy parameters are calibrated against rating agency metrics and the Basel capital adequacy framework. The policy is reviewed annually by the Board of Directors.</p> <p>The Provisioning Policy was reviewed in 2015 and adjusted to incorporate EBRD loss experience and a different market data set, leading to a release of €0.3 billion of general provisions. This marginally increased the capital base, but also refined expected loss metrics as part of focus on financial sustainability (see Action Item 5 below).</p> <p>The decision was taken by shareholders in 2015 to remove the redemption feature of the callable capital shares issued in 2010. This had an important effect in ensuring capital headroom under the statutory capital measure, but also in emphasising shareholder support for the organisation.</p> <p>Management has developed a risk appetite statement to frame forward planning and understand future capital challenges on a risk adjusted basis.</p> <p>The current 3 year rolling business plan envisions a 15% growth in Operating Assets by YE2018.</p>	<p>Periodic review of the Bank’s Capital Adequacy and related policies.</p> <p>Continuing to enhance our multi-year stress testing to understand the potential capital impact of stress events.</p> <p>Some marginal additional capital headroom may be quantified through detailed work to better capture and measure the Bank’s risks (e.g. reflecting the impact of risk sharing arrangements from donors).</p>	<p>The Bank’s capital adequacy is calibrated against the rating agency metrics and the Basel capital adequacy framework. These considerations constrain the overall size of EBRD’s balance sheet and the bank’s capital headroom is limited.</p> <p>If shareholder support factors were to diminish either due to rating downgrades of shareholders (especially AAA rated shareholders under S&amp;P methodology) or to qualitative aspects, this would directly affect EBRD’s capital capacity.</p> <p>As MDBs that predominantly or exclusively lend to the private sector are deemed by rating agencies to be less important to shareholders than sovereign lenders, the financial profile (key Capital Adequacy and Liquidity metrics) have to be higher to ensure a triple-A rating.</p>

Action Item	What We Have Done	What More We Could Do	Constraints/Comments
<b>1B – Engage Rating Agencies to Evaluate Simulations that More Fully Utilise Capital</b>	<p>The Bank sought and received a better treatment for the capital utilisation of equity than under the originally proposed methodology (although it is still punitive).</p> <p>The Bank has engaged in discussions on the capital treatment of envisaged risk-sharing propositions.</p>	<p>The Bank will continue its active dialogue with rating agencies to seek greater variance in capital treatment for investment sub-categories such as Trade Finance and Equity Funds, as well as recognition of shareholder support beyond capital increases</p> <p>Continue to work with shareholders to see what can be done to clarify the process and timing of payments under capital calls.</p>	<p>It would not be appropriate for the Rating Agencies to define parameters for stress and capital utilisation, and then consider this in their rating process.</p> <p>Each MDB has a different portfolio and geography as well as shareholder base; therefore no standard set of parameters can be interpreted in a uniform way. We may, however, engage individually with the agencies on specific issues</p>
<b>2 – Exposure Exchanges</b>	<p>N/A</p>	<p>N/A</p>	<p>EBRD does not currently have a significant sovereign concentration penalty from S&amp;P (EBRD’s sovereign portfolio was 20.9% of the total portfolio and 22.1% of operating assets)</p>
<b>3 – Financial innovation using Concessional Windows</b>	<p>N/A</p>	<p>N/A</p>	<p>The EBRD does not have a concessional investment window.</p>
<b>4 – Greater use of risk sharing instruments</b>	<p>B loan syndication is the Bank’s most important product for private sector mobilisation. In 2015, B loan volume at USD 2 billion, for 17 projects, in 10 countries.</p> <p>We have extended our pool of B lenders, making good progress in sourcing non-bank lenders, in particular with investors who lend to SMEs or green projects.</p> <p>Use of insurance companies in unfunded risk participations.</p>	<p>Seek shareholder support to obtain more favourable capital treatment to incentivise banks to lend alongside EBRD under the B loan program, and for longer tenors.</p> <p>Seek shareholders support to encourage Export Credit Agencies (ECAs) to alter their approach to our preferred creditor status (PCS) as we would be able to close more projects with private sector B loans.</p> <p>Explore A:B loan facilities in terms of A:B loan proportions, use of oversubscriptions.</p>	<p>Ability to attract private sector investors if there is preferred capital treatment under Basel rules (less capital required). Changes directed to increase capital requirements will damage the A:B loan instrument, reducing investment</p> <p>ECAs want equal PCS treatment as MDBs but ECAs are not eligible B lenders. This has resulted in ECAs excluding MDBs in several projects, thus reducing the ability of the MDBs to mobilise commercial banks through B loans.</p> <p>Dilution of the A:B ratio could jeopardise credibility of the lender of record structure on which, i.e., PCS rests, and it gives comfort to co-financiers that we have considerable “skin in the game”.</p>



Action Item	What We Have Done	What More We Could Do	Constraints/Comments
	<p>Bringing new equity investors into the region through new equity participation fund.</p> <p>Working to develop a refinancing market for infrastructure/PPP's post completion to bring private sector funds into the financing of infrastructure through both loans and bonds.</p> <p>Use of donor funds in first-loss structures to enable the bank to take more risk in certain markets, particularly in SME financing.</p> <p>Secondary sales of operating assets to manage risk and allow recycling of capital capacity.</p> <p>Insurance used for loss protection on trade finance.</p> <p>PPP structuring technical cooperation fund to assist countries of operations in structuring of PPP's to be more financeable, including by private sector.</p> <p>Participating in issuance of project finance bonds crowding in private sector financing in infrastructure.</p>	<p>Explore opportunities for B loan investment funds as a way to release of capital and involvement of institutional investors.</p> <p>Explore opportunities for further loan and bond portfolio secondary sales, including B loans, as a tool to allow recycling of the Bank's capital.</p> <p>Explore opportunities for B Bonds/Securitised B loans as this could be instrumental in attracting institutional investor capital to EBRD-financed infra deals.</p> <p>Continue to develop risk sharing with insurance companies In connection with project bonds, explore bilateral support facilities for both construction and operation phases of projects to provide embedded credit enhancement.</p>	<p>Initial market testing has shown that the appetite amongst institutions for IFI private sector loans is limited owing to the risk/return ratio as well as the lack of appetite for unrated loans in the markets in which the EBRD is active.</p> <p>There may be costs associated with selling assets.</p> <p>Insurers' appetite for emerging market credit risk is not yet deep. In addition, EBRD needs to ensure that each instrument is as closed to a guarantee as possible, and EBRD would need a counterparty credit risk approval to be put in place for each insurer.</p> <p>The Bank does not guarantee client bond, as they create challenges for our transition mission and sound banking approach; they may be stripped and/or create a two-tier market in the Bank's name, and may conflict with limitations on providing guarantees in EBRD's Charter.</p> <p>Using donor money for non-TC will depend on donors' interest into these products.</p> <p>Due to the cuts in aid budgets and other competing needs such as responding to the Syrian refugee crisis, and refocusing aid to the poorest countries, a number of traditional donors have reduced their support from the EBRD.</p>
	<p>The Bank raises an average of €340m per year from donors. The target in the Strategy Implementation Plan 2016-2018 is to increase to €400m this year rising to €500m by end 2018.</p>	<p>Donors predominantly support technical cooperation (TC) but there is a growing interest from some donors to provide funds for non-TC including investment grants, guarantees, concessional financing and first loss risk sharing to enable the Bank to take more risk.</p> <p>The Shareholder Special Fund is</p>	

Action Item	What We Have Done	What More We Could Do	Constraints/Comments
	<p>EBRD working together with other MDBs to improve PPP preparation to ensure sound base for execution and confidence with investors of viable projects.</p>	<p>predominantly a tool for TC. Explore possibility of using some allocation for risk sharing.</p> <p>Incorporate new MDBs (AIIB and NDB) into the fold, increase multipartite cooperation, pursue new innovative approaches to collaboration, including initiatives such as the Sustainable Development Investment Partnership (SDIP).</p> <p>Achieve higher levels of leveraging in private sector investment.</p> <p>Continue efforts to support local institutional support for investment as per the work with the G20's new Global Infrastructure Hub (GIH).</p>	<p>The focus of the actions proposed go beyond a mere net increase in financing from the IFIs directly; rather, the set of tools should seek to have the MDBs act as catalysts for greater overall investment in the sector.</p>
<p><b>5 – Net Income Measures</b></p>	<p>An enhanced focus on the financial sustainability of the Bank in the context of planning and ongoing operations. Using a strategic portfolio management approach, the Bank aims to balance the relative transition impact and RAROC of components of the portfolio (such as region) to ensure that the Bank's strategic objectives are pursued whilst achieving a return on risk to build the Bank's capital base to support operations and provide a buffer against stress events.</p> <p>Effective cost control: the Bank has exercised rigorous budget discipline and active reallocation and prioritization of resources.</p> <p>A new policy has been approved by the Board of Directors to increase fees on donor funds, reflecting the associated administrative costs and to bring the Bank's donor fee levels</p>	<p>Tools are being developed to increase transparency on financial sustainability (RAROC metrics) for new projects approved and for actual returns on projects in the portfolio.</p> <p>The Bank has initiated an Operational Effectiveness and Efficiency Programme to deliver strategic approach to realising efficiency in the three year period to 2018.</p> <p>Net income allocation: Stronger focus on mobilising external donor funds and enhancing their planned use; careful consideration of how rating agencies perceived income allocation decisions.</p>	<p>EBRD faces a higher risk environment, including uncertainty in equity markets and an expansion to regions, where risk-return dynamics are less favourable.</p> <p>The Operational Effectiveness and Efficiency Programme focuses on 'doing more with less' to support increased activities and reallocation of resources, rather than reducing overall costs.</p> <p>Ultimately the allocation of net income is a decision for the Bank's shareholders with such decisions being made annually by the Bank's Board of Governors.</p> <p>Net income allocation decisions may be negatively viewed by rating agencies if they are significant and not linked to the mandate of the Bank (when they are regarded as quasi dividends) and/or where they do not reflect the Bank's current financial performance or risk profile at the time.</p>

Action Item	What We Have Done	What More We Could Do	Constraints/Comments
	<p>closer to those of other MDBs.</p> <p>The Bank regularly allocates net income to the EBRD Shareholder Special Fund through which technical assistance and grant financing is provided in support of the Bank’s transition objectives. However, there are also other demands on the Bank’s net income. The Board of Directors have approved a framework to guide Management in developing net income proposals that focus on the Bank’s financial sustainability and the prioritisation of demands.</p>		
<p><b>Enhanced supervision of financial and risk management practices by shareholders</b></p>	<p>Financial, risk and capital information is provided to the Board in quarterly reporting.</p> <p>There was a significant review and updating of the Bank’s financial policies during 2015 with the Board.</p> <p>Upgrading of stress testing and related discussions with the Board.</p> <p>Introduction of financial sustainability issues in the Strategy and Implementation Plan (3-year plan).</p>		<p>Finding meaningful benchmarking across MDBs is going to be challenging, given the differences in their business models, geographies and risk profiles.</p> <p>Rating agencies methodologies’ go beyond financial metrics, so common financial metrics are not comparable with respect to additional investment capacity.</p> <p>‘Supervision’ by and reporting lines directly to capitals would be a radical departure from the long established role of the Board of Directors in such issues. The benefits and modality of such an additional process are unclear.</p>
<p><b>Conclusion: Impact on planned business activities</b></p>	<ul style="list-style-type: none"> <li>• Ability to accumulate capital through net income is challenging given weak equity markets, volatility of currencies (valuation of equities and hedges) and lower earnings on Treasury liquidity portfolio given low (and even negative) interest rates).</li> <li>• Capital capacity under recently reviewed metrics (benchmarked against rating agency and Basel metrics) is relatively limited and is focused on supporting the Bank’s three year rolling business plan.</li> <li>• Any material increase in sovereign exposure at the current a fixed margin would result in lower cost coverage and relatively less capital accumulation.</li> <li>• All efforts generate increased investment by private sector (crowding-in) which, in turn, either allow for more funding for (or risk in) projects or for reducing EBRD exposure allowing capital to be recycled.</li> <li>• Current rolling 3 year plan shows capacity to grow operating assets by 15% by YE2018, given projected growth in capital.</li> </ul>		

## European Investment Bank (EIB)

Action Item	What We Have Done	What More We Could Do	Constraints/Comments
<p><b>1 – Increased Capital Efficiency</b></p>	<p>The Bank is in continuous dialogue with its shareholders with respect to capital.</p> <p>Over the last years the EIB has developed a sophisticated risk management framework aligned with best banking practices and following advanced methods.</p> <p>As part of this risk management framework, the EIB has developed a risk appetite framework where EIB’s risk capacity is the maximum amount of risk which the EIB is able to assume before breaching <i>one</i> or <i>more</i> of the internally-defined constraints in relation to its capital base, liquidity, funding capacity and reputation. EIB’s risk capacity serves as an ultimate constraint for its risk appetite. In turn, EIB’s business objectives should be aligned with its risk appetite.</p> <p>The current 2016-2018 Corporate Operational Plan envisions a considerable increase in the volume of High risk operations covered by a first loss piece guarantee provided by the European Commission.</p>	<p>Develop knowledge-sharing initiatives among MDBs, enabling the extrapolation, where possible, of past successful initiatives among MDBs.</p> <p>Enhancing the Stress Testing Framework, developing the necessary tools, aligned with best banking practice, to properly measure the capital impact that different scenarios could have on the Bank.</p> <p>Continue the performance of Capital Optimization exercises, actively allocating resources in the most optimal way.</p>	<p>The EIB has limited additional risk-bearing capacity, not least given its highly leveraged balance sheet, to increase lending without compromising its AAA rating. Balance sheet strength and the AAA rating are of crucial importance to the EIB.</p> <p>The EIB is continuously monitoring its capital situation in the context of the risk appetite framework approved by its Board.</p> <p>Back in 2011, the Bank had been placed on negative watch by several ratings agencies, demonstrating its use of capital had tested its limits. In 2012, it increased its fully paid-in capital by EUR 10bn to support an increase in lending to projects that support jobs and growth particularly in the European Union.</p> <p>Like other MDBs, EIB capital capacity depends on shareholders support factors, outside EIB control (e.g. S&amp;P rating downgrades of AAA shareholders).</p>
<p><b>2 – Exposure Exchanges</b></p>	<p>The EIB has contributed to the development of the MDB sovereign exposures exchange agreements.</p>	<p>Participate in a non- EU sovereign exposure exchange, thus collectively optimizing MDBs’ balance sheets.</p> <p>Examine the possibility of using CDS.</p>	<p>The EIB is willing to make further use of exposure swaps with MDBs to manage concentration and large exposure risk. The constraint for the EIB is the eligibility of the EEA instrument as an effective credit risk transfer technique from a regulatory perspective.</p>

Action Item	What We Have Done	What More We Could Do	Constraints/Comments
<b>3 – Financial innovation using Concessional Windows</b>	N/A	N/A	
<b>4 – Greater use of risk sharing instruments</b>	<p>The EIB is already using a comprehensive range of instruments to share risks with private investors and public institutions, including syndications, structured finance and guarantees. In order to mitigate its balance sheet risks, the EIB has developed innovative instruments, which use European Commission or Member States’ grant funds to cover losses arising from investments financed by the EIB Group. This mechanism allows the EIB Group to leverage third party funds for the benefit of real economy. Recent examples of such innovation include the Investment Plan for Europe (‘EFSI’ or ‘Juncker Plan’), Innovfin or the SME initiative.</p>	<p>Explore opportunities for expanding the current Investment Plan for Europe to countries outside Europe.</p> <p>Develop new risk-sharing initiatives to respond to the global crises (i.e. Refugees).</p>	<p>The EIB is open to looking at how other MDBs use risk-sharing instruments.</p> <p>Innovative instruments developed by the EIB could serve as models for other MDBs.</p>
<b>5 – Net Income Measures</b>	<p>The EIB has already developed a pricing model based on capital consumption. This enables the Bank to compensate for capital consumed by its operations and to accumulate the funds necessary to ensure an appropriate growth in the EIB capital base.</p>	<p>Continuous calibration / development of the model to accurately reflect the underlying risks.</p>	<p>The capital growth due to the accumulation of pricing revenues obviously takes time and is limited by market constraints and the necessity to transfer a financial advantage to its clients.</p>
<b>Enhanced supervision of financial and risk management practices by shareholders</b>	<p>The EIB has recently revised its Risk Appetite Framework, which is aligned with its Operational Plan, ICAAP, capital planning, capital allocation and stress testing processes.</p> <p>In addition, the EIB aims to apply ‘Best Banking Practice’, i.e. the EIB adheres to financial regulations which</p>	<p>Best Banking Practice is an on-going project that the EIB revises on a regular basis.</p> <p>G20 should nevertheless be attentive to the regulatory developments and their possible incompatibility with the public mission of the MDBs. The unique policy driven objective of the MDBs would</p>	

Action Item	What We Have Done	What More We Could Do	Constraints/Comments
	apply to EU banks.	indeed require preserving specific treatments in relation to the Preferred Creditors Status (PCS), the 0 risk weight of MDBs bonds and sovereign exposures or the inherent high concentration risk.	
<b>Conclusion: Impact on planned business activities</b>	<p><b>Action Item 1:</b> EIB is highly leveraged and has limited additional capacity to increase lending without compromising its AAA rating.</p> <p><b>Action Item 2:</b> The EIB is willing to make further use of exposure swaps with MDBs to manage concentration and large exposure risk in non EU countries.</p> <p><b>Action Item 3:</b> N/A</p> <p><b>Action Item 4:</b> EIB is willing to share expertise in innovative financial instruments and risk sharing techniques developed by the EIB Group with other MDBs.</p> <p><b>Action Item 5:</b> EIB is using sophisticated pricing models calibrated to ensure an appropriate growth in the EIB capital base.</p>		

## **Inter-American Development Bank (IDB)**

<b>Action Item</b>	<b>What We Have Done</b>	<b>What More We Could Do</b>	<b>Constraints/Comments</b>
<b>1 – Increased Capital Efficiency</b>	<p>Already in 2014, the IDB Governors approved a Capital Adequacy Mandate, aimed at maintaining the IDB’s AAA rating with all major agencies, while deploying capital in the most efficient manner.</p> <p>In 2015, the Governors approved further Capital Regulations which take account of the need to maintain operational capacity even in times of stress; this includes building buffers to enable counter-cyclical lending during an economic downturn and establishing clear rules for capital accumulation.</p>	<p>The Board of Directors reviews the Capital Regulations on an annual basis to ensure relevance and ongoing efficiency in capital utilization.</p>	<p>Replicated S&amp;P RAC Methodology to establish analytical basis for challenging results. This resulted in S&amp;P making some adjustments in their methodology.</p> <p>Submitted technical note to S&amp;P for consideration by their Credit Committee proposing various enhancements in the context of their tri-annual review of methodology.</p> <p>Assembled group of international experts and academics to evaluate S&amp;P’s methodology and propose changes.</p>
<b>2 – Exposure Exchanges</b>	<p>In December 2015 IDB signed a framework for Exposure Exchange Agreements (EEA) and executed two transactions, respectively for \$2bn with the IBRD and \$2.9bn with the AfDB.</p> <p>These transactions contributed to a significant reduction of concentration with the top-five borrowers. The related improvement in IDB capital ratios is estimated in the order of two percentage points.</p> <p>Under the EEA documentation, preferred creditor status is fully retained, as the originating MDB maintains its key relationship with the borrowing shareholder.</p>	<p>Expand current EEA framework for participation of other AAA MDBs.</p> <p>Develop additional frameworks to enable participation of non-AAA MDBs and Export Credit Agencies.</p> <p>Explore other sovereign risk transfer mechanisms including private sector.</p>	<p>Gains from EEA diminish with each exchange as concentration also decreases, so the scale for deploying the instrument is limited.</p> <p>Developing exchanges with additional institutions is likely to take significant time and effort, due to differences in statutory frameworks and objectives.</p>

Action Item	What We Have Done	What More We Could Do	Constraints/Comments
<b>3 – Financial innovation using Concessional Windows</b>	<p>IDB Governors have agreed in principle to merging the Fund for Special Operations (FSO) with ordinary capital (ORC) at the IDB annual meetings.</p> <p>This initiative strengthens the provision of concessional finance to low-income countries, while also enabling leverage of concessional resources for balance sheet optimization.</p>	<p>Governors have requested a formal proposal to be approved in the third quarter for implementation on January 1st, 2017.</p>	<p>While enhancing ORC capital adequacy, the merger will also reduce the profitability due to the lower interest rates charged on concessional lending.</p>
<b>4 – Greater use of risk sharing instruments</b>	<p>IDB merged-out its private sector operations into the Inter-American Investment Corporation (IIC) on January 1st, 2016, at the same time strengthening both the capital and lending capacity of the IIC.</p>	<p>The IIC business plan envisages expanding the availability of instruments for operations with private sector investors, with the objective of mobilizing private sector resources for development.</p>	<p>Limited access to concessional resources for blending purposes may be a constraint on mobilization of co-financiers.</p>
<b>5 – Net Income Measures</b>	<p>The Governors of the IDB approved a new Income Management Model in 2015, tying the capital regulations to specific actions on the income side. This new model has already led in 2015 to income measures enacted on both the revenue and the cost side of the Bank.</p> <p>At their annual meetings in April 2016, the Governors approved an enhanced procedure for transfers under the IDB Grant Facility, which fully preserves the net benefit to the receiving country while also optimizing the impact on the balance sheet. The procedure was already applied to 2015 transfers.</p>	<p>Limited room for additional measures, as IDB costs are determined within a Results Based Budget framework and income is constrained by the low interest rate environment.</p>	<p>Increases in sovereign loan charges are limited by competitiveness of lending products and governance issues.</p> <p>Very significant expenditure measures have been applied over the past few years, to finance new initiatives from savings out of existing budget.</p>



Action Item	What We Have Done	What More We Could Do	Constraints/Comments
<p><b>Enhanced supervision of financial and risk management practices by shareholders</b></p>	<p>Comprehensive quarterly Financial Risk Report for Board.</p> <p>Defined risk appetite at Governors level: overall and for specific risk types.</p> <p>Informal exchange of policy approaches within MDB fora.</p>	<p>Implement a more formal exchange and alignment of policies, e.g., by expanding the existing information exchange at GEMs or in the EEA working group.</p>	<p>Individual mandates, shareholder composition and institutional nature of MDBs make comparisons challenging and call for individualized approaches, subject to each MDB governance.</p>
<p><b>Conclusion: Impact on planned business activities</b></p>	<p><b>Action item 1:</b> Capital adequacy framework has been reviewed recently and is subject to annual revisions. Limited scope to further enhance capacity within the framework.</p> <p><b>Action item 2:</b> Two EEAs have been executed and there is still some room for additional EEAs and other types of risk transfers (SG and NSG). These efforts are however unlikely to materialize in the short term.</p> <p><b>Action item 3:</b> The ORC/FSO merger will provide both windows with more capacity in the short and medium-term but will need to be supplemented with other measures (including capital increase) in the long-term due to the expected lower equity generation from subsidizing concessional lending out of ORC resources.</p> <p><b>Action item 4:</b> The private sector mandate is now managed within a dedicated institution, the Inter-American Investment Corporation (IIC). IDB and IIC are jointly looking at opportunities for greater use of risk sharing instruments.</p> <p><b>Action item 5:</b> Ability to accumulate capital through net income is already at relatively high and stable level due to SG loan charges and effective ALM policies. Further improvements are dependent on a general normalization of interest rate levels in the economy.</p>		

## International Bank for Reconstruction and Development (IBRD/World Bank)

Action Item	What We Have Done	What More We Could Do	Constraints/Comments
<p><b>1 – Increased Capital Efficiency</b></p>	<p>In 2014, put in place measures to grow revenues, control costs and leverage more (“Margins for Manoeuvre”).</p> <p>Increasing IBRD’s Single Borrower Limit (SBL) by \$2.5 billion, with a 50 basis point (bp) surcharge on the incremental amount.</p> <p>Revising IBRD’s minimum equity-to-loan ratio from 23 percent to 20 percent, reflecting improvements in portfolio credit risk, enabling more efficient utilization of shareholder capital while remaining financially prudent.</p> <p>Changing IBRD’s loan terms, restoring the 25bp commitment fee, charged on undisbursed balances, and offering longer maturities with increased maturity differentiation.</p> <p>Initiated Expenditure Reduction to reduce WBG annual cost base by \$400 million.</p> <p>Adopted budget anchor that would cap administrative expenses to loan spread income.</p>	<p>Implementation of Expenditure Reduction underway.</p> <p>Continued engagement with rating agencies.</p>	<p>Limited room on IBRD to increase leverage given worsening external risks and global headwinds.</p> <p>Seeking to raise revenues via further price increases would be challenging given recent measures as part of Margins for Manoeuvre, but could be considered as part of a larger package with shareholders. Further cost reduction would be challenging given growing demands especially in more difficult environments.</p>
	<p>Ratings and capital adequacy implications of MDB EEA were assessed in FY16 using rating agency Ratings Evaluation Service.</p> <p>In FY16, the World Bank conducted extensive discussions with the major rating agencies and hired two</p>		<p>Continued strong replenishments critical for IDA leveraging as a strongly rated issuer.</p>

Action Item	What We Have Done	What More We Could Do	Constraints/Comments
	<p>agencies for scenario analysis in connection with the IDA leveraging proposal. The proposal is now being developed further.</p>		
<p><b>2 – Exposure Exchanges</b></p>	<p>In FY14, IBRD entered into an innovative exposure exchange agreement with the Multilateral Investment Guarantee Agency (MIGA). The first exchange was of an IBRD exposure to Brazil for a MIGA exposure to Panama.</p> <p>In FY16, IBRD, the African Development Bank (AfDB) and the Inter-American Development Bank (IDB) have approved an innovative framework agreement for an exchange of sovereign exposures that will collectively optimize their balance sheets for greater development effectiveness. The first three bilateral exposure exchange agreements within this new framework is for a total of about US\$6.5 billion.</p>	<p>Additional exposure exchange agreements over the medium term with other MDBs subject to their interest.</p>	<p>This remains an option for future consideration. Constraints are: (i) finding matching exposures; (ii) diminishing returns for the IBRD; (iii) regulatory or other constraints of potential partner institutions.</p>
<p><b>3 – Financial innovation using Concessional Windows</b></p>	<p>IDA 17 replenishment resulted in a record replenishment size of \$52.1 billion to finance projects over FY15-FY17 due to the following innovations:</p> <ul style="list-style-type: none"> <li>• IDA Loan participations</li> <li>• IDA Guarantees</li> <li>• Use of Concessional Partner Loans in IDA17</li> </ul> <p>IDA is currently exploring options for further expanding IDA’s range of products to include financing mobilized by leveraging IDA’s equity (IDA+).</p>	<p>Leverage IDA’s equity.</p>	<p>Shareholder consultations on leveraging mechanisms underway.</p>

Action Item	What We Have Done	What More We Could Do	Constraints/Comments
	<p>A scale-up facility will be implemented in FY17 to meet the additional demand from all countries with appropriate debt sustainability and absorptive capacity.</p>		
<p><b>4 – Greater use of risk sharing instruments</b></p>	<p>IBRD updated its operational policies to facilitate the use of its guarantee products and with a view of increasing leverage of guaranteed operations. The number and volume of guaranteed operations has increased over the past few years.</p> <p>A particular mechanism to incentivize their use is a capital set aside for part of the exposure associated with the guarantees.</p> <p>Additionally, as part of updating IBRD’s capital charge methodology, IBRD can assess whether a particular guarantee has a lower risk than an equivalent loan to the sovereign and thus merit a lower capital charge.</p>	<p>Increase marketing of IBRD guarantee products to private market participants.</p>	<p>Limitations to using the set aside of capital as aggregate capital constraints become more binding. Other “risk transfer” and mobilization are less applicable due to sovereign exposures and cooperative pricing.</p>
<p><b>5 – Net Income Measures</b></p>	<p>In FY14, IBRD’s loans terms were revised, including restoring the 25 basis point commitment fee charged on undisbursed balances, and offering longer maturities with increased maturity differentiation accompanied by a maturity premium.</p> <p>At the same time, IBRD’s Single Borrower Limit was increased by \$2.5 billion for Brazil, China, Indonesia, India, and Mexico, with a 50 basis point surcharge on the incremental amount.</p> <p>In addition to the above, other Margins for Manoeuvre measures set to expand IBRD’s margins:</p>	<p>Annual review of IBRD’s sovereign loan pricing. Examine implementation of special development policy loan pricing for countries in crisis or other forms of differentiated pricing. Consider modifications to net income transfers.</p> <p>Consider a rules-based approach for net income allocation.</p>	<p>Budget planning would need to reflect substantial increase in lending operations and need to ensure the quality and effectiveness of operations, especially in more challenging environments.</p>

Action Item	What We Have Done	What More We Could Do	Constraints/Comments
	<ul style="list-style-type: none"> <li>• Increased lending enabled by lowering of minimum E/L ratio from 23% to 20%;</li> <li>• Expenditure reduction;</li> <li>• Greater Trust Funds cost recovery.</li> </ul>		
<p><b>Enhanced supervision of financial and risk management practices by shareholders</b></p>	<p>Provide extensive financial and risk information to Board on, at least, a quarterly basis including:</p> <ul style="list-style-type: none"> <li>• Financial statements</li> <li>• Capital adequacy metrics</li> <li>• Credit risk exposures</li> <li>• Market risk exposures</li> <li>• Operational risk exposures</li> </ul> <p>Annual engagement with Board on Medium Term Financial Outlook for income and capital adequacy.</p>		
<p><b>Conclusion: Impact on planned business activities</b></p>	<p><b>Action Item 1:</b> IBRD increased its capacity substantially from its level of just \$15 billion prior to these actions.</p> <p><b>Action Item 2:</b> Each exposure exchange agreements will improve the diversification of each organization’s portfolios, thereby freeing up capacity to support additional business. Limited benefit for IBRD due to constraints mentioned in table.</p> <p><b>Action Item 3:</b> Potential for additional financing to IDA countries. World Bank will be able to provide sustainable additional financial capacity to help low-income countries. Subject to continued strong replenishments, the IDA+ proposal has the capacity to channel scarce concessionality to where it is most needed.</p> <p><b>Action Item 4:</b> Increased ability to leverage private sector financing to member countries, by having IBRD managing sovereign risks which private sector participants are reluctant to bear.</p> <p><b>Action Item 5:</b> IBRD will improve its financial sustainability.</p>		

## International Finance Corporation (IFC)

Action Item	What We Have Done	What More We Could Do	Constraints/Comments
<p><b>1 – Increased Capital Efficiency</b></p>	<p>IFC has had an economic capital framework in place since 2007. IFC continuously reviews and updates this EC framework and updates shareholders on changes.</p> <p>IFC’s capital framework is aligned with industry best practices and international regulatory (“Basel”) frameworks. IFC’s capital models have been reviewed twice by external specialists in the last 6 years, to make sure they are aligned with best practice.</p> <p>IFC engaged with its Board in 2010 on the establishment of a capital buffer, and in 2012 on the setting of a risk tolerance range for capital adequacy.</p> <p>IFC has a ‘very strong’ business profile rating from S&amp;P and no callable capital, so we have to manage to a higher Risk Adjusted Capital (RAC) ratio than most other MDBs in order to preserve our AAA rating.</p> <p>IFC regularly engages with the rating agencies on their methodologies and their application to IFC.</p>	<p>IFC is currently undertaking a significant enhancement of its risk and portfolio management systems, which includes the implementation of a new risk rating system and economic capital engine. This will add further granularity and accuracy in calculating and allocating capital.</p> <p>IFC will continue to review and update its risk management framework on an ongoing basis.</p> <p>IFC will continue to engage with the rating agencies on their methodologies and application to IFC.</p>	<p>Unlike public sector MDBs, IFC’s portfolio of EM debt and equities is much riskier than for public sector MDB investments and requires significantly more capital backing.</p> <p>All of IFC’s assets are backed with risk-based capital, including off-balance sheet commitments and the Treasury portfolio. IFC also holds capital for operational risk.</p> <p>IFC manages its capital adequacy according to our internal capital frameworks. IFC does not manage according to rating agency methodologies, given the differences between the agencies and the changing nature of the methodologies themselves. We do, however, keep track of our capital and liquidity position under the rating agency methodologies and use these for comparative purposes and for stress testing.</p>
<p><b>2 – Exposure Exchanges</b></p>	<p>Concentration impacts on the S&amp;P RAC ratio or the Moody’s methodology are not an issue for IFC’s globally-diversified portfolio.</p> <p>IFC uses market solutions where necessary to reduce exposures to manage our exposures according to our limits framework, e.g. via synthetic hedges or asset sales.</p>		<p>IFC has a highly diversified portfolio, geographically and by sector. IFC’s equity portfolio is the most diverse of any private equity firm in emerging markets.</p>

Action Item	What We Have Done	What More We Could Do	Constraints/Comments
<b>3 – Financial innovation using Concessional Windows</b>	IFC does not have a concessional window but leverages blended finance (including selectively from IDA) when appropriate (e.g. public goods) to enable investments that cannot be financed on a solely commercial basis – these blended investments currently represent an extremely small portion of IFC’s portfolio.	IFC is actively participating in the ongoing discussions around the IDA 18 replenishment, regarding leveraging IDA equity for the possible establishment of an IDA private sector window.	Subject to IDA deputies decision, this window would be instrumental in expanding investment in fragile and conflict affected states (FCS) and low income IDA countries.
<b>4 – Greater use of risk sharing instruments</b>	<p>IFC already has a full range of risk sharing instruments in place to mobilize outside investment (over \$56 billion since inception), such as:</p> <ul style="list-style-type: none"> <li>• Syndications - via B loans and programmatically via the Managed Co-lending Portfolio Program (MCP), which allows categories of investors to invest in a portion of IFC’s overall portfolio;</li> <li>• Parallel loans including from MDBs;</li> <li>• Asset Management Company (AMC), which has raised over \$6.7 billion in private equity to be invested alongside IFC;</li> <li>• Structured finance investments; risk-sharing facilities;</li> <li>• A loan participations (ALPS) and unfunded risk participations (URPS), whereby IFC has sold or synthetically transferred the risk of existing loans to outside investors.</li> </ul> <p>IFC core mobilization was \$7.1 billion in FY15 - approximately 70 percent of IFC’s own-account volume.</p>	IFC actively works to expand its ability to bring in additional private sector financing, in particular via the establishment of programs to mobilize at a portfolio level, and by building partnerships with new categories of outside investors (e.g. insurance companies, sovereign wealth funds, government agencies, private equity funds, banks) and creating new asset classes.	IFC’s ability to expand its mobilization activities depends on the external climate for investments as well as the appetite of investors for particular products, geographies and sectors. There is less appetite for mobilization in frontier markets.
<b>5 – Net Income Measures</b>	IFC’s investments are on a market basis; part of our mandate is that we do not provide subsidized financing. Our pricing for all of our products is market-based and generating a sufficient risk-adjusted return		IFC designations to IDA follow a sliding-scale formula. Discussion are underway with shareholders to determine the best way for IFC to support private sector investment in IDA countries as part of the ongoing IDA 18

Action Item	What We Have Done	What More We Could Do	Constraints/Comments
	<p>on capital to cover all costs and generate a profit.</p> <p>IFC has already taken a thorough review to manage expenditures to ensure they are being used in the most efficient way possible, in accordance with the WBG expenditure review. Gross savings from the expenditure review are expected to reach \$50 million by June 30, 2016.</p> <p>IFC designations to IDA are governed by a sliding-scale formula, based on the level of allocable income generated by IFC during the fiscal year.</p> <p>IFC has already contributed \$3.5 billion from retained earnings to the IDA public sector window. With leverage, mobilization and co-financing, IFC could have supported \$70 billion more in private sector investments if we had kept this capital. This would be leveraged even more over time by IFC's ability to generate a profitable return on its capital.</p>		<p>Replenishment and private sector window.</p>
<p><b>Enhanced supervision of financial and risk management practices by shareholders</b></p>	<p>IFC provides extensive financial, risk and portfolio information to the Board, including:</p> <ul style="list-style-type: none"> <li>• Financial statements</li> <li>• Quarterly risk and portfolio reports, covering key risk indicators, capital adequacy, portfolio composition and performance for the debt equity and treasury portfolios, environmental and social, distressed assets and reputation/integrity risk (KYC).</li> <li>• Financial Risk Management and Capital Adequacy paper (annual)</li> <li>• Annual Portfolio Review paper</li> <li>• periodic technical briefings of various aspects of risk management</li> </ul>		<p>IFC is currently providing extensive financial and operational information to its Board; we have had a long and deep engagement with the Board on risk and capital issues.</p> <p>IFC's profile is very different from most MDBs and therefore any attempts to develop common benchmarks would have very limited applicability to IFC.</p> <p>IFC's experience with the rating agency methodologies is a clear example of the challenges in developing a common benchmark for MDBs. In many ways, IFC is an outlier in the application of the methodologies and we have spent years engaging with the rating agencies to</p>



Action Item	What We Have Done	What More We Could Do	Constraints/Comments
	<ul style="list-style-type: none"> <li>Strategy and Business Outlook paper, which features management assessment of risks.</li> </ul>		try to clarify and modify the application of these frameworks to better fit IFC's activities and portfolio.
<p><b>Conclusion: Impact on planned business activities</b></p>	<p><b>Action item 1:</b> IFC's capital position is more constrained than its leverage position; IFC's capital adequacy is approaching the board-approved minimum tolerance threshold. IFC's future growth will depend on its ability to generate and retain profits, which is challenging in the current economic and financial climate.</p> <p><b>Action item 2:</b> IFC benefits from an extremely well-diversified portfolio, supported by an exposure limits framework and market-based solutions to manage concentration risk. No additional action needed.</p> <p><b>Action item 3:</b> Even though IFC does not currently have access to a concessional finance window, IFC is already doing a significant amount of investments in IDA and FCS countries. IFC is participating in the ongoing IDA rethink regarding the possible establishment of a private sector IDA window.</p> <p><b>Action item 4:</b> IFC already has a full range of risk sharing instruments in place to bring in significant amounts of private sector capital, including sponsor capital, such as: syndicated loans, AMC, Managed Co-lender Participation Program, A loan participations, unfunded risk participations and structured products which contribute to mobilizing substantial investor financing for projects in emerging markets.</p> <p><b>Action item 5:</b> IFC as a lender and investor in private companies is very market-oriented. IFC uses risk-adjusted pricing and profitability measures in investment decisions. The measures taken as part of the WBG expenditure review will enhance IFC's profitability going forward. IFC designations to IDA are governed by a sliding-scale formula. IFC has given \$3.5 billion to IDA, which is more than our paid-in capital of \$2.6 billion. IFC shareholders are discussing the best way going forward for IFC to support private sector development in IDA countries as part of the IDA 18 Replenishment discussions.</p>		