

# **Enabling Sustainable Growth: IFC's FY16 Budget**

**Approved by IFC's Board of Directors on June 25, 2015**

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# Table of Contents

<b>EXECUTIVE SUMMARY .....</b>	<b>1</b>
<b>I. IFC BUSINESS MODEL &amp; FINANCIAL SUSTAINABILITY OVERVIEW .....</b>	<b>2</b>
A. IFC'S STRATEGIC DIRECTION .....	2
B. THE MEANING OF FINANCIAL SUSTAINABILITY AT IFC .....	6
C. IFC'S FINANCIAL VALUE CHAIN .....	7
D. THE INTERFACE OF FINANCIAL SUSTAINABILITY WITH DEVELOPMENT IMPACT .....	9
E. MAKING TRADE-OFFS .....	10
<b>II. BUDGET PRINCIPLES &amp; PROCESS .....</b>	<b>14</b>
A. BUDGET PROCESS .....	14
B. BUDGET AS FULL PROFIT & LOSS .....	14
C. EVOLUTION FROM DEPARTMENT TO DEPLOYMENT AND DELIVERY .....	15
<b>III. PROFITABILITY OVERALL: PORTFOLIO AND PROFITABILITY .....</b>	<b>16</b>
A. PORTFOLIO .....	16
B. CONTROLLABLE INCOME OVERVIEW .....	18
C. PROFITABILITY OF STRATEGIC PRIORITIES .....	19
<b>IV. PROFITABILITY DRIVERS: REVENUE .....</b>	<b>21</b>
A. INVESTMENT OPERATIONS .....	21
<b>INVESTMENTS: EQUITY .....</b>	<b>21</b>
<b>INVESTMENTS: LOANS .....</b>	<b>22</b>
<b>INVESTMENTS: TRADE &amp; COMMODITY FINANCE .....</b>	<b>23</b>
<b>INVESTMENTS: GLOBAL PORTFOLIO APPROACH AND DIVERSIFICATION BENEFITS .....</b>	<b>24</b>
B. ADVISORY SERVICES .....	26
C. TREASURY & SYNDICATED LOANS .....	26
D. ASSET MANAGEMENT COMPANY .....	27
<b>V. PROFITABILITY DRIVERS: EXPENSES .....</b>	<b>29</b>
A. MAJOR EXPENSE DRIVERS .....	29
B. RESOURCE USAGE BY SELECTED STRATEGIC PRIORITIES .....	30
C. UPDATE ON EXPENDITURE REVIEW .....	32
IFC IS COMMITTED TO DELIVER 18% OF TOTAL WBG SAVINGS IN LINE WITH THE INITIAL ESTIMATES. THIS CORRESPONDS TO APPROXIMATELY \$71.3 MILLION IN GROSS SAVINGS OVER FY15-18. THE EXPENDITURE REVIEW DESIGN STAGE IS COMPLETE, AND IFC IS ALREADY MAKING PROGRESS AGAINST ALL MEASURES CURRENTLY IN IMPLEMENTATION. IFC IS MEASURING RESULTS BASED ON WHETHER IFC HAS DIRECT ACCOUNTABILITY OR IFC HAS INPUT INTO WBG DECISION-MAKING BUT WHERE IFC'S GROSS SAVINGS WILL DEPEND ON POLICY APPROVAL AND IMPLEMENTATION ACTIONS AT THE WBG LEVEL. D. UPDATE ON AREAS FOR POTENTIALLY INCREASED RESOURCE INTENSITY IN FY15 BUDGET PAPER .....	32
E. AREAS FOR INCREASED RESOURCE INTENSITY IN FY16 .....	35
<b>VI. IFC'S TOTAL RESOURCES .....</b>	<b>38</b>

A.	TOTAL RESOURCES .....	38
B.	TOTAL ADMINISTRATIVE BUDGET .....	42
C.	ADVISORY SERVICES .....	45
D.	OTHER SOURCES OF FUNDS .....	45
E.	CAPITAL BUDGET .....	47
<b>VII.</b>	<b>RECOMMENDATIONS .....</b>	<b>50</b>
A.	ADMINISTRATIVE BUDGET AUTHORITY .....	50
B.	CAPITAL BUDGET AUTHORITY .....	50
C.	SPECIAL INITIATIVES .....	50
<b>Chart 1.</b>	<b>Ex-Post Correlation of IFC Return on Capital with Client Development Results .....</b>	<b>11</b>
<b>Chart 2.</b>	<b>Committed Portfolio Composition, FCS/IDA/Total IFC, Average FY12-14 .....</b>	<b>11</b>
<b>Chart 3.</b>	<b>Portfolio Risk Measures, FCS/IDA/Total IFC, Average FY12-FY14 .....</b>	<b>12</b>
<b>Chart 4.</b>	<b>Cash Income Return on Average Capital, FCS/IDA/Total IFC, Average FY12-14 .....</b>	<b>12</b>
<b>Chart 5.</b>	<b>Net Loan &amp; Fee Rev Coverage of Total Expenditure, FCS/IDA/IFC Total, Average FY12-14 .....</b>	<b>13</b>
<b>Chart 6.</b>	<b>Committed Portfolio Evolution within FY15 .....</b>	<b>17</b>
<b>Chart 7.</b>	<b>Program and Portfolio Outlook, FY13-18P (\$, billions) .....</b>	<b>17</b>
<b>Chart 8.</b>	<b>Historical Trends in IFC's Revenue and Income Performance, FY06-FY15Q3 (\$, millions) .....</b>	<b>18</b>
<b>Chart 9.</b>	<b>Cash Income Return on Average Capital by Strategic Focus Area .....</b>	<b>20</b>
<b>Chart 10.</b>	<b>Net Loan &amp; Fee Rev Coverage of Total Expenditure by Strategic Focus Area .....</b>	<b>20</b>
<b>Chart 11.</b>	<b>Quarterly Trends in Equity Write-downs (\$, millions) .....</b>	<b>21</b>
<b>Chart 12.</b>	<b>Trends in Non-Performing Loans, FY08Q4-FY15Q3 (\$, millions) .....</b>	<b>22</b>
<b>Chart 13.</b>	<b>IFC Portfolio by Region, FY15 Q3-end (Total = \$48.5 billion) .....</b>	<b>24</b>
<b>Chart 14.</b>	<b>IFC Portfolio by Sector, FY15 Q3-end (Total = \$48.5 billion) .....</b>	<b>24</b>
<b>Chart 15.</b>	<b>Cash Income by Region, FY15 Q3-end .....</b>	<b>25</b>
<b>Chart 16.</b>	<b>Cash Income Return on Average Capital, by Region .....</b>	<b>25</b>
<b>Chart 17.</b>	<b>Net Loan &amp; Fee Revenue Coverage of Total Expenditure, by Region .....</b>	<b>26</b>
<b>Chart 18.</b>	<b>Nominal Increases to IFC's Total Resources &amp; Administrative Budget, FY11 Budget to FY18 Indicative .....</b>	<b>39</b>
<b>Chart 19.</b>	<b>Total Resources as a Percentage of IFC Assets under Management, FY05-18E .....</b>	<b>41</b>
<b>Figure 1.</b>	<b>Regional Strategy Overviews .....</b>	<b>2</b>
<b>Figure 2.</b>	<b>Investment Services Provide the Largest Contribution to Funding IFC's Work .....</b>	<b>7</b>
<b>Figure 3.</b>	<b>IFC's Advisory Services Delivery Model Leverages External Funding and IFC's Own Resources .....</b>	<b>8</b>
<b>Figure 4.</b>	<b>Liquid Asset Management Revenue (and Expense) is Also Critical to IFC's Financial Flows .....</b>	<b>9</b>
<b>Figure 5.</b>	<b>IFC Budget Formulation Process .....</b>	<b>14</b>
<b>Figure 6.</b>	<b>IFC's FY16 Sources of Funds (\$, millions) .....</b>	<b>38</b>

<b>Table 1. Emerging and Growth Opportunities: Program &amp; Approach by Region and Sector/Theme.....</b>	<b>5</b>
<b>Table 2. IFC Total Commitment Volume, Historic and Projected (\$, billions).....</b>	<b>16</b>
<b>Table 3. Controllable Income (\$, millions).....</b>	<b>19</b>
<b>Table 4. Profitability and Productivity Metrics Monitored for Investment Operations.....</b>	<b>19</b>
<b>Table 5. Short-Term Finance Projections, FY12-18P (\$, billions) .....</b>	<b>23</b>
<b>Table 6. IFC-IBRD Shared Service Agreements (\$, millions, nominal terms).....</b>	<b>30</b>
<b>Table 7. Total Investment Operations Administrative Expenses + Core Fees, by Region, IDA &amp; FCS.....</b>	<b>31</b>
<b>Table 8. Total Committed Portfolio, by Region, IDA &amp; FCS .....</b>	<b>31</b>
<b>Table 9. Advisory Services, Strategic Emphasis Areas, FY12-15 Q3-end (\$, millions and %).....</b>	<b>32</b>
<b>Table 10. Advisory Services, Program Spend by Region, FY12-FY15 Q3-end (\$, millions and %).....</b>	<b>32</b>
<b>Table 11. IFC Total Resources, FY14 Actual to FY16 Budget (\$, millions, nominal) .....</b>	<b>39</b>
<b>Table 12. FY16 Increase in Total Resources (\$, millions) .....</b>	<b>40</b>
<b>Table 13. FY16 Funding Envelopes (% of All Units Funding) .....</b>	<b>41</b>
<b>Table 14. Total Resources by Cost Category, FY14 Actual to FY16 Budget (\$, millions) .....</b>	<b>42</b>
<b>Table 15. Total Administrative Budget, FY16 vs. FY15 (\$, millions) .....</b>	<b>43</b>
<b>Table 16. Total Administrative Budget by Cost Category (\$, millions) .....</b>	<b>44</b>
<b>Table 17. Advisory Services by Funding Source, FY13-18E .....</b>	<b>45</b>
<b>Table 18. FMTAAS Designations vs. Annual Spending Authority, FY05-18E (\$, millions).....</b>	<b>45</b>
<b>Table 19. Capital Budget, FY14-16 (\$, millions).....</b>	<b>47</b>

## Glossary

AS	-	Advisory Services
AMC	-	Asset Management Company
CAGR	-	Compound Annual Growth Rate
CAO	-	Compliance Advisor Ombudsman
EAP	-	East Asia & the Pacific
ECA	-	Eastern Europe & Central Asia
ESG	-	Environment, Social and Governance
FCS	-	Fragile and Conflict Situations
FMTAAS	-	Funding Mechanism for Technical Assistance and Advisory Services
FY	-	Fiscal Year
GAM	-	Global Administrative Manager
GSD	-	General Services Department
HQ	-	Headquarters
HR	-	Human Resources
IBRD	-	International Bank for Reconstruction and Development
ICT	-	Information & Communication Technology
IDA	-	International Development Association
IEG	-	Independent Evaluation Group
IFC	-	International Finance Corporation
IS	-	Investment Services
IT	-	Information Technology
LAC	-	Latin America & the Caribbean
LAM	-	Liquid Asset Management
LTF	-	Long-Term Finance
MENA	-	Middle East & North Africa
NPL	-	Non-Performing Loan
P&L	-	Profit & Loss Statement
RAROC	-	Risk Adjusted Return on Capital
SME	-	Small and Medium Enterprise
SA	-	South Asia
SSA	-	Shared Services Agreement
SSA	-	Sub-Saharan Africa
STF	-	Short-Term Finance
WBG	-	World Bank Group

## Executive Summary

- i) The International Finance Corporation's Fiscal Year 2016 Budget paper presents its operational delivery framework to meet private sector Client demand and best position our human resource and financial capital toward achieving the WBG twin goals. The paper seeks Board authorization for the budget required to not only ensure IFC's existing financial assets are safeguarded, but also increase our presence and impact in an ever-changing economic landscape.
- ii) **Section I** of the report provides context as to how IFC plans to achieve its strategic goals within a strong financial sustainability framework. IFC approaches implementation of its strategy with an in-depth understanding of its financial realities on the ground. The diversification of its balance sheet across financial instruments, geographies and sectors provides the ability to take on risks and balance fiscal returns with development impact. This is all done in concert with assessment of capital adequacy implications and managed as a dynamic, mainstreamed business activity.
- iii) The principles underpinning IFC's budgetary resource dispersion and deployment are further explained in **Section II**. IFC views budget through the lens of its entire profit & loss statement; expenses are one key driver of IFC's financial sustainability and are managed as such. Under the Refocused IFC delivery model and with the goal to deploy resources in the most effective and efficient manner, where and how resources are deployed are equally if not more relevant than where the resources reside. IFC's business model is unique, and our resource flexibility affords us the real-time responsiveness that private sector Clients need. Given its integrated delivery model, not all trade-offs equal elimination of efforts; rather, IFC has been able to transform its tactics through a convergence of skills so that it serves with an all-encompassing approach.
- iv) The overall market environment has and will continue to significantly influence IFC's financial performance as evidenced by its FY15 year-to-date results. In particular, select geo-political situations, declining oil prices, and the strengthening of the U.S. dollar versus a number of emerging markets currencies have meaningfully affected IFC's equity and debt instrument performance. **Section III** of the paper discusses these impacts further. **Section IV** discusses revenue across products as well as business lines in more detail.
- v) **Section V** elaborates on expenses, including optimizing resources to support a sustainable growth trajectory. Finally, **Section VI** presents IFC's Total Resources, including Management's proposal for an FY16 total administrative budget of \$976 million, an increase of 2.5% in nominal terms. Since a significant component of this increase will be consumed by inflation adjustments, Management has sought further savings and efficiencies from the expenditure review, shared services and other sources that could be released for redeployment. The redeployment effort, in combination with the non-inflation share of budget increase, will provide additional funding for IFC's variable pay program, strategic staffing plans, and other strategic programs geared to supporting staff in furtherance of the World Bank Group's twin goals. A three year budget outlook will complement the expense projections within IFC's income statement, further demonstrating IFC's continued fiscal prudence in support of a strategic growth program and thoughtfully managed portfolio.

# I. IFC BUSINESS MODEL & FINANCIAL SUSTAINABILITY OVERVIEW

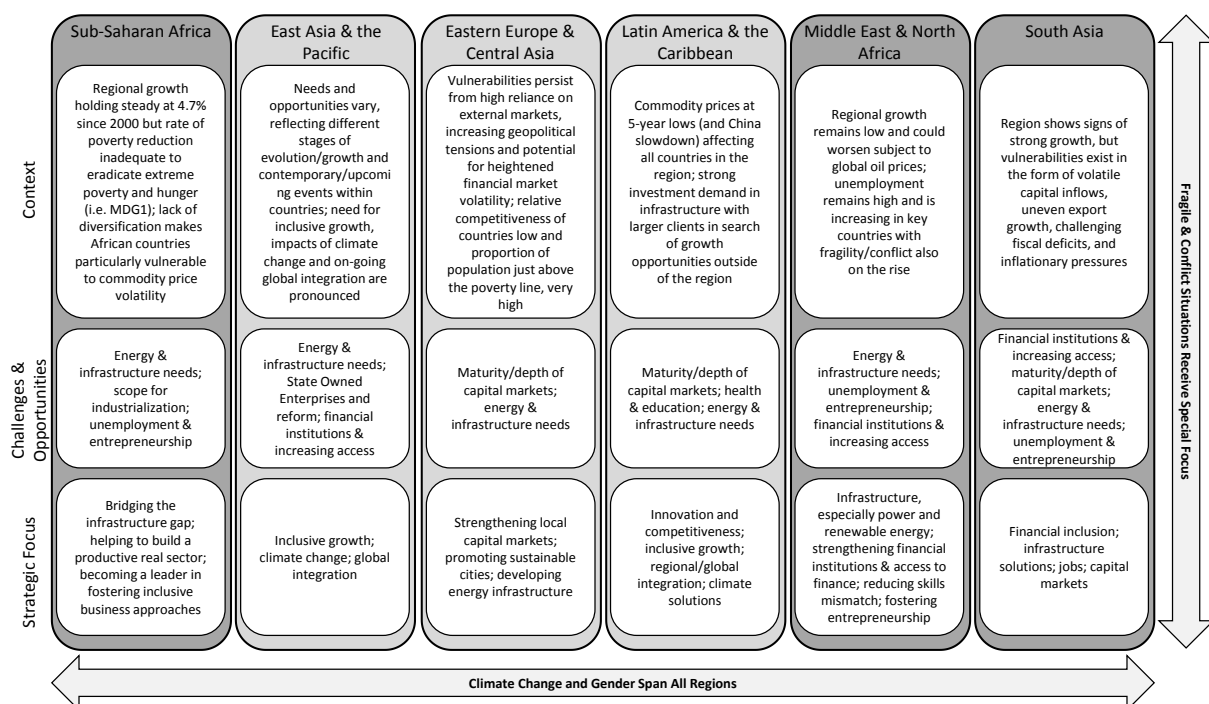
## A. IFC'S STRATEGIC DIRECTION

1.1 **Global context.** IFC is operating in a challenging macro environment of slowing global growth, rising inequality, and a changing financial landscape. Compounding this picture, many developing countries continue to face significant development challenges, in particular:

- i) Access to infrastructure, with over 80% of the world's population in emerging economies and developing countries still struggling with poor infrastructure and uneven service levels;
- ii) Access to finance, with more than 1 billion unbanked;
- iii) Agribusiness and food supply chains, with many of the world's poor depending on agriculture for livelihoods;
- iv) Climate change, which is one of the most significant challenges to development;
- v) Lack of jobs, which offer the surest pathway out of poverty;
- vi) Lack of supportive investment climates for business, which are critical to attract private capital flows and enable productive investment by firms; and,
- vii) Challenges of Fragile and Conflict Situations, which will be home to the majority of the world's poor by 2030.

1.2 While these development challenges are global, each geographic region faces particular constraints and opportunities.

**Figure 1. Regional Strategy Overviews**





1.3 **Program Approach.** In selecting areas of focus and interventions over FY16-18, IFC will be aiming to help address many of these challenges, growing in order to deliver greater impact while also maintaining a strong financial position. Management will make calibrated adjustments based on prevailing opportunities and challenges, in line with IFC's dynamic private sector-oriented business model.

1.4 Consistent with its established focus areas, IFC's main geographic priority remains FCS, where IFC's role is to remove major constraints to business growth, including through mechanisms that enable higher-risk activities, and to reduce the perception of geopolitical risk. IFC expects its FCS engagement to grow at a faster rate, over time, where they are able to be further enhanced with additional risk capital. Sub-Saharan Africa, Middle East & North Africa, and South Asia remain regional priorities as well. IFC is implementing new initiatives to unlock additional investment opportunities. These include: i) significant enhancements of the FCS Risk Envelope to broaden the type of deals eligible; ii) mobilization of new pools of risk capital and blended finance instruments to fill key gaps and encourage developers to bring high-impact projects to market; and iii) increased upstream work to help expand deal flow and build client capacity. IFC is also revising its incentives framework, including increased awards for staff contributions to FCS operations and portfolio support.

1.5 The approaches to addressing individual fragile and conflict situations will differ as flexibility is required to manage differentiated contexts, security risks, and varying levels and types of opportunities. In addition to closely coordinating as one WBG on complex projects requiring upstream support from the Bank, IFC will leverage many other programs, including but not limited to the Conflict Affected States in Africa Initiative and increased engagements via Cross-Cutting Solutions Areas. Management will also endeavor to increase operational team focus in these areas through boosted incentives for such important efforts.

1.6 From a sector perspective, IFC intends to increase the pace of its infrastructure (particularly power and clean energy) investments faster than in other industries. It will also employ new approaches to address certain aspects of the core program (e.g., in health and education), where there is much greater potential for innovation and Public Private Partnership solutions.

1.7 Thematically, IFC will focus on areas with potential for significant development impact, as identified through its planning process. These include addressing:

- i) The role of technology across the range of IFC's interventions, in particular for financial services;
- ii) The speedier provision of basic infrastructure, in particular power and clean energy
- iii) The role of capital markets in plugging the financing and viability gap across core sectors;
- iv) The adoption of a more systematic approach to identifying value chains and playing a catalytic role in enabling the development of platforms (e.g., in housing and power generation); and,
- v) The empowerment of local entrepreneurs with global know-how and the financial strength to deliver platform solutions in local markets for sustainable, long term development.

1.8 Climate and gender continue to be important cross-cutting strategic themes across IFC's entire business, sectorally and geographically.

1.9 **Climate change.** IFC is focusing on four strategic areas of climate business: clean energy; sustainable cities; climate-smart agribusiness and food security; and industrial efficiency. IFC is providing investment and advisory services along the clean energy value chain, from regulatory reform and equipment manufacturing to capacity installation. IFC has steadily invested in manufacturing of renewable energy components and also sees opportunity in battery storage and power distribution efficiency. In line

with the World Bank Group strategy on low carbon, livable cities, IFC is exploring business opportunities in water and energy efficient buildings, and providing private sector solutions for transport and waste management. For example, in efficient lighting, IFC and World Bank staff are working together to approach city clients and help them investigate public or private financing for efficient street lighting. The team is already working in several countries in LAC and in India. To reduce food waste and improve efficiency in the agribusiness value chain, IFC is exploring opportunities in efficient irrigation systems, refrigeration, and other technology, and in captive generation of renewable energy for agribusiness clients. In industrial efficiency, IFC has a strong track record in sector studies and firm audits for efficiency opportunities and has a streamlined lending facility for efficiency improvements. Building on this expertise, IFC is investigating new financial solutions, including vendor finance, to scale up energy efficiency. To further increase market penetration of existing technologies, IFC is also exploring new financial products, with an initial focus on LED lighting and HVAC equipment. Finally, climate resilience and adaptation is a growing area of IFC attention, with climate risk tools under development. IFC research has focused on climate adaptation needs specific to financial institutions, hydropower, manufacturing, agribusiness, and ports. IFC has also invested in several adaptation projects

**1.10 Gender.** The IFC Gender Secretariat collaborates with clients, partners and colleagues to offer services that promote gender-inclusive growth, such as including men and women in supply chains and in company-community relationships; enabling women-owned businesses to access financial services, coaching and markets; promoting access to qualified women candidates for board and executive leadership positions; and, advancing equal employment and promotion opportunities for men and women. IFC gender-focused investments span all sectors but are most highly concentrated in financial inclusion and agribusiness. Employment is also an area of particular focus for gender. The Secretariat leads SheWorks, a WBG partnership to enhance women's employment in the private sector. SheWorks brings together leading companies representing a variety of regions and sectors to regularly share knowledge and best practices in women's employment. IFC coordinates closely with its WBG counterparts in both the Climate Change and Gender Cross-Cutting Solution Areas to develop focused, complementary approaches to these broad challenges. IFC's commitment to the One WBG approach is similarly seen in evolving joint Global Practices, which facilitate IFC's work in financial inclusion and investment climate, for example.

**1.11** Table 1 illustrates the regional view of several key emerging and growth opportunities for particular sectors and themes.

**Table 1. Emerging and Growth Opportunities: Program & Approach by Region and Sector/Theme**

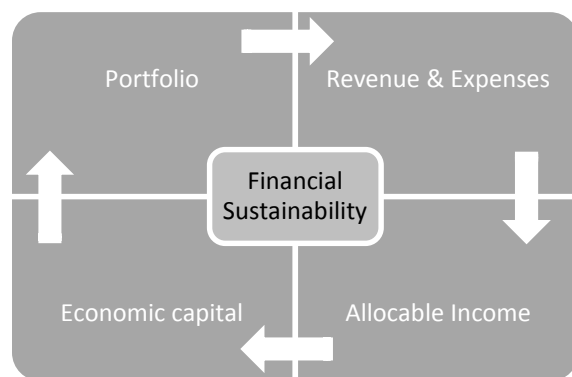
Thematic component ↑ Increased thematic component	Sub-Saharan Africa	East Asia	Eastern Europe & Central Asia	Latin America & the Caribbean	Middle East & North Africa	South Asia	Details
Access to Finance	↑	↑				↑	Access to Finance is front and center in IFC's development agenda across all regions. Improving access to finance is critical to job creation and financial inclusion. This will be accomplished by strengthening existing financial institutions, modernizing payment systems, reforming State-Owned Enterprise banking, deepening local capital markets and developing the insurance subsector where needed. Further promotion of regional integration and competitiveness is important, along with the establishment of crisis response mechanisms. Access to finance is a foundation that underlies all of IFC's efforts to further develop the private sector in emerging markets.
Agribusiness	↑		↑	↑			IFC agribusiness efforts in Africa will focus on building a productive real sector, including by scaling up agribusiness value chain investments. In EAP, the program will scale up manufacturing and agribusiness investments in Indonesia; health, education and animal protein investments in China; and affordable housing (green buildings) across the region. IFC will invest along agribusiness value chains focused on MSMEs in LAC.
Capital Markets Development		↑	↑	↑		↑	IFC will catalyze private equity in SSA to meet increased regional demand for growth capital. In ECA, it will help countries develop capital markets, diversify their financing and mobilize domestic resources for investment. IFC will participate in initiatives that deepen capital markets. Capital markets development in LAC will be two-fold: engaging with Debt and Asset Recovery Program platforms and mobilizing institutional investors through structured products; supporting second tier financial institutions to tap local currency bond markets and on-lend to developers in health and education platforms.
Cities			↑	↑		↑	IFC will help finance sustainable cities in all regions with particular emphasis in LAC, EAP, and SSA. The challenges of continued urbanization can be addressed through investment in affordable housing and by fostering collaboration in social services, education, infrastructure and waste management. Similarly, IFC's promotion of green buildings supports sustainable urban environments.
Cross Border Investments	↑	↑			↑		IFC will play its catalytic role by connecting firms from China, Japan, Korea, Singapore, and Malaysia with viable partners in Frontier Markets. In particular, IFC seeks to co-invest with platform companies while partnering with domestic and international players who can target large assets.
Information and Communic. Technology / FinTech	↑	↑				↑	Across the globe, IFC is identifying new opportunities for rapid development that arise from constant innovation in the ICT sector. The greatest impact can be made by increasing access to broadband and mobile telephony in countries with substandard services. Where access is not a primary limitation, IFC can build upon and improve existing infrastructures and expand services into areas such as mobile banking. Further development of ICT will be catalyzed by creation of Climate or Growth Funds where feasible.
Power and Clean Energy	↑	↑	↑	↑		↑	Power is a critical sector for development in all regions. IFC can help tackle the energy gap by focusing on renewables and delivering infrastructure solutions that promote clean energy. IFC will maximize its impact by focusing on power generation in Fragile and Conflict Situations and helping to turn around lagging State Owned Enterprises. Promoting regional connectivity and ensuring collaboration with regional and international partners will be critical to successfully closing the energy gap
Small and Medium Enterprises, and Promoting Local Entrepreneurship	↑		↑		↑		IFC's objective is to maximize its impact on job creation by supporting SMEs, which are generally second tier companies. IFC seeks to better balance its Client base beyond large tier one companies, especially in Manufacturing, Agribusiness and Services. In MENA, a focus on manufacturing, tourism, retail, and telecom will help address systemic unemployment. This includes reducing skills mismatch to align with private sector needs. In South Asia, IFC investments and assistance to financially distressed companies will support job creation in the garment industry and tourism. Efforts in SSA support diversification and industrialization with particular focus on construction, agri-supply chains and access to energy.

1.12 IFC Management’s desire to integrate delivery capacity for better client service, development impact, and operational efficiency in service of this strategy is evident in recent organizational structure changes. This includes the further incorporation of key units previously residing within Global Partnerships into Global Client services, which should facilitate improved linkage of economic analyses and geographic diagnostics with operational execution. In particular, the Systematic Country Diagnostics/Country Partnership Framework process will become more efficient as strategic capacity, industry/sector specialization and geographic reach are more explicitly linked. In addition, IFC’s Finance Business Partnership function overseeing all resource matters has converged with the strategic Stakeholder Engagement unit. This will facilitate a more seamless view of strategy and resources throughout the planning cycle as well as provide even more harmonized and reporting to and engagements with the Board.

1.13 IFC will monitor progress on all of these priorities and report back to the Board in next year’s Strategy & Business Outlook.

## B. THE MEANING OF FINANCIAL SUSTAINABILITY AT IFC

1.14 Financial sustainability – the counterpart to development impact – is the organization’s ongoing ability to accomplish its mission by generating and maintaining sufficient financial resources through business activities and resulting profitability. In the absence of callable capital, IFC’s financial structure requires internal generation of available resources through income earnings.



1.15 In any given year, IFC’s portfolio evolves as a result of new business generation and performance of the existing portfolio. Operational opportunities and outcomes are driven by economic and market performance; this performance serves as a catalyst for new and transformational Client prospects and delivers financial remuneration through IFC’s income statement. IFC’s capital position provides a dynamic framework for these developments and evolves based on business line, geographic, industry, and financial diversification.

1.16 To ensure IFC’s financial sustainability while maximizing its development impact, it is imperative to correctly understand, measure and manage the risks that IFC takes. As a development institution focused exclusively on the private sector, IFC has access to unique opportunities, but it also faces unique challenges that set it apart from other Multilateral Lending Institutions. These challenges require on-going vigilance to ensure that IFC has the financial resources required to implement its program while maintaining its triple-A rating. This requires expert staff to closely monitor that capital is appropriately allocated across regions, sectors and strategic priorities, and that investments earn a rate of return that is commensurate with the risks taken.

1.17 Prudent risk management and effective use of financial resources are the twin pillars of IFC’s Financial Risk Management framework, helping ensure that IFC maximizes its development impact while

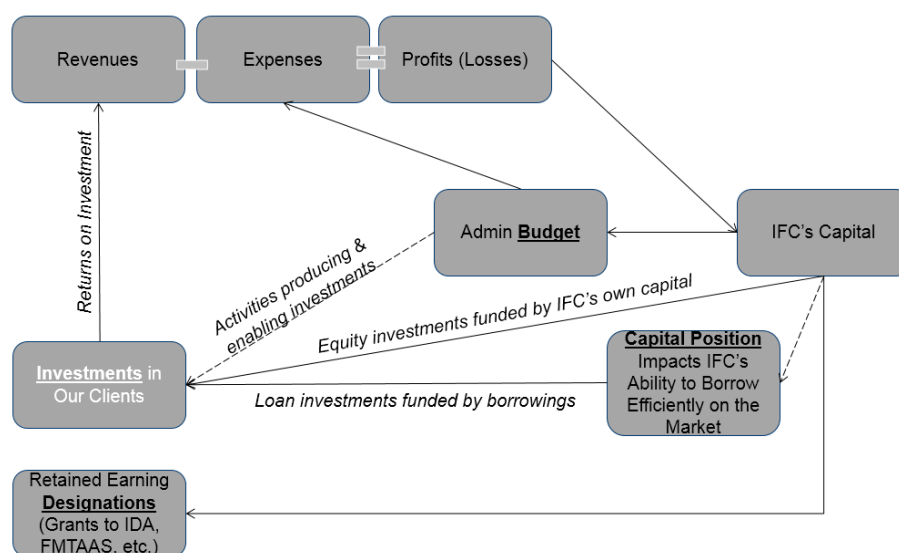
remaining financially sustainable. Economic capital is the foundation of financial risk management at IFC. It is used to gauge the relative riskiness of different products and markets, to estimate their contribution to the overall risk of the portfolio, to measure the total amount of capital that IFC needs to hold to operate, and to measure financial return on investments relative to the risk taken. A more detailed discussion on IFC's financial risk management framework and economic capital is to be found in the upcoming FY15 report on Financial Risk Management.

## C. IFC'S FINANCIAL VALUE CHAIN

**1.18 Investment Services (including AMC).** IFC's profits directly or indirectly fund most of its activities; return on investments in Client companies is the largest contributor. In particular, equity investments enhance financial sustainability as they are one of the main sources of revenue for IFC (dividends, realized capital gains), which support growth in IFC's economic capital. Through these investments, IFC supports Client companies to take on risks, launch innovative ventures and grow their companies, and improve their corporate governance and risk management. IFC leverages more funding from other investors through its equity investments than through its loan investments.

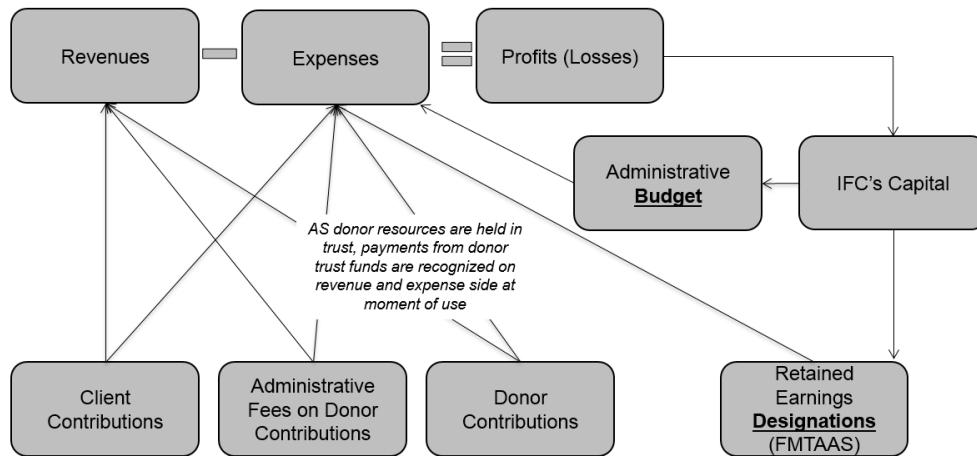
**1.19** Income from IFC's operations flows to its capital base, which in turn is used to: (i) fund its equity investments; (ii) provide the capital buffer necessary to maintain its triple-A rating and borrow effectively in the capital markets, which is used to fund its loan investments; and (iii) fund the administrative budget, which supports and enables IFC's business operations.

**Figure 2. Investment Services Provide the Largest Contribution to Funding IFC's Work**



**1.20 Advisory Services.** The AS funding model draws on IFC, donor and client sources. Each source has its strengths and weaknesses, but in combination they can create a robust and diversified funding model. A key part of recent reforms has been to further strengthen the financial sustainability of AS.

**Figure 3. IFC's Advisory Services Delivery Model Leverages External Funding and IFC's Own Resources**



**1.21 AS Trends and FY15 Highlights.** IFC's Advisory Services enable IFC's reach by strengthening Client capacity, assisting governments in design and implementation of Public Private Partnership transactions, and helping governments and non-government institutions improve the enabling environment for private investment. A key part of recent reforms has been to further strengthen the financial sustainability of AS:

- i) Leverage partially mainstreamed IFC contributions. IFC's contribution to AS can be used to fund benefits beyond those paid for by clients and to seed activity in areas before donor interest has materialized. As approved in IFC's FY12 Business Plan & Budget,<sup>1</sup> IFC Management has partially mainstreamed IFC's contribution to AS from IFC net income (via FMTAAS) to IFC's administrative budget. Phase two of this process was rolled out in FY14.
- ii) Donor Contributions. Ongoing efforts focus on enhancing the strategic management of key donor relationships and on strengthening a WBG-wide approach to donor relationship management while actively developing new partnerships with corporate, philanthropic, and other non-traditional partners. Donor support to Advisory remains robust.
- iii) Client Contributions. IFC's AS pricing policy uses client contributions first and foremost as a tool to strengthen client ownership and commitment to implementation as well as to ensure that any subsidy embedded in AS pricing is justified by the public benefit involved. This approach has the additional benefit of further diversifying and strengthening the AS funding model. The pricing policy for advice to governments on enabling environment work takes into account the income level of the recipient government, and it recognizes in-kind and other contributions.

**1.22** Under the Refocused IFC organizational changes to better serve IFC's clients and strengthen its impact, AS is more closely aligned with investment services, other IFC departments, and relevant joint Global Practices. Accordingly, IS, AS and support teams are working to refine reporting, including that related to portfolio and profitability, to incorporate these changes.

**1.23 Liquid Asset Management.** The objective of Liquid Asset Management in IFC's treasury operations is to achieve reasonable returns while maintaining IFC's risks within acceptable levels all the while ensuring that funding for IFC investments is available as needed. The primary funding source for liquid

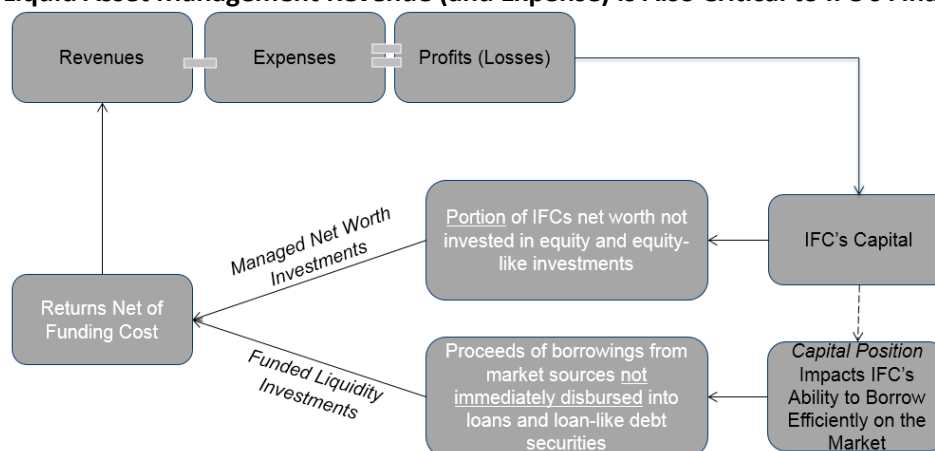
<sup>1</sup> IFC FY12 Business Plan & Budget (SECPO/IFC/R2011-0167), paragraphs 4.83-4.91.

assets for IFC is borrowings from market sources. Proceeds of borrowings from market sources not immediately disbursed into loans and loan-like debt securities (Funded Liquidity) are managed internally against money market benchmarks. The second funding source of liquid assets is that portion of IFC's net worth not invested in equity and equity-like investments (Managed Net Worth), which is managed against a U.S. Treasury benchmark.

1.24 IFC's assets are invested in a full range of highly rated financial instruments such as asset-backed securities, U.S. and other government or agency bonds, repurchase agreements, deposits assets, and mortgage backed securities and derivatives. Liquid Asset Management revenue is dependent on market trends and is therefore relatively volatile.

1.25 IFC and IBRD both benefit from very low funding costs. For most financial institutions, assets held in liquidity are decremental to capital. For IFC and other International Financial Institutions, assets held in liquidity are likely to be accretive to capital (so called "positive carry"). That is, due to low funding cost, IFC expects to earn a return on capital from its liquid assets investments that exceeds its cost of capital.

**Figure 4. Liquid Asset Management Revenue (and Expense) is Also Critical to IFC's Financial Flows**



## D. THE INTERFACE OF FINANCIAL SUSTAINABILITY WITH DEVELOPMENT IMPACT

1.26 Financial sustainability and development impact are inextricably linked and equally important. Both allow IFC to have the resources needed to fulfill its mission. Moreover, if IFC investments have good development results and are financially sustainable, they are more likely to demonstrate to other players in their markets that there is a business case for such investments. The expectation is that other private sector investors will follow and enter these new markets or expand their operations.

1.27 IFC has found that financial performance of Client companies tends to be closely correlated with strong development results.<sup>2</sup> IFC experience and Development Outcome Tracking System data have shown that better environmental and social performance is also associated with better financial performance (companies with financial problems tend to apply inadequate resources and attention to environmental and social matters). In order to understand in greater depth the effects of investments on jobs (indirect, induced and second order) and economic growth, IFC is now more systematically allocating resources to evaluation in strategic sectors.

## **E. MAKING TRADE-OFFS**

1.28 IFC has been moving toward a more explicit focus on profitability and optimization of its return on capital. While profitability is critical to sustain IFC's service to Clients in the long run, IFC's developmental impact mandate sometimes creates a trade-off between optimizing its own returns and investing in countries with more challenging business environments. It is always important for IFC's Clients to achieve financial sustainability so that they can create and maintain developmental impact for their own ultimate Clients and communities.

1.29 Given the nature of its business, IFC continues to take risks and invest in markets where conditions are difficult in order to accomplish its developmental mandate. Such markets include FCS and IDA countries that have urgent development needs. IFC's efforts to allocate resources in the most effective way consider where trade-offs will have to be made in order to take smart risks balanced with solid financial outcomes. In strategic priority areas such as FCS and IDA where risks and costs are higher, IFC pays close attention to the impact of these investments within its total portfolio to determine the volume and composition of IFC's overall new business and portfolio at any given time.

1.30 There is a strong correlation between (1) IFC return on economic capital and (2) client development results (investment development outcome success includes the underlying project's own financial performance as well as wider economic performance, environmental & social performance, and private sector development). These two dimensions of IFC's work are fundamentally linked (i.e., a financially unsustainable project is unlikely to create lasting development impact). IFC would not engage in a profitable enterprise without the potential for significant development impact, but it would also be unlikely to find a highly developmental project without some element of financial sustainability, even if only marginally potentially profitable for IFC.

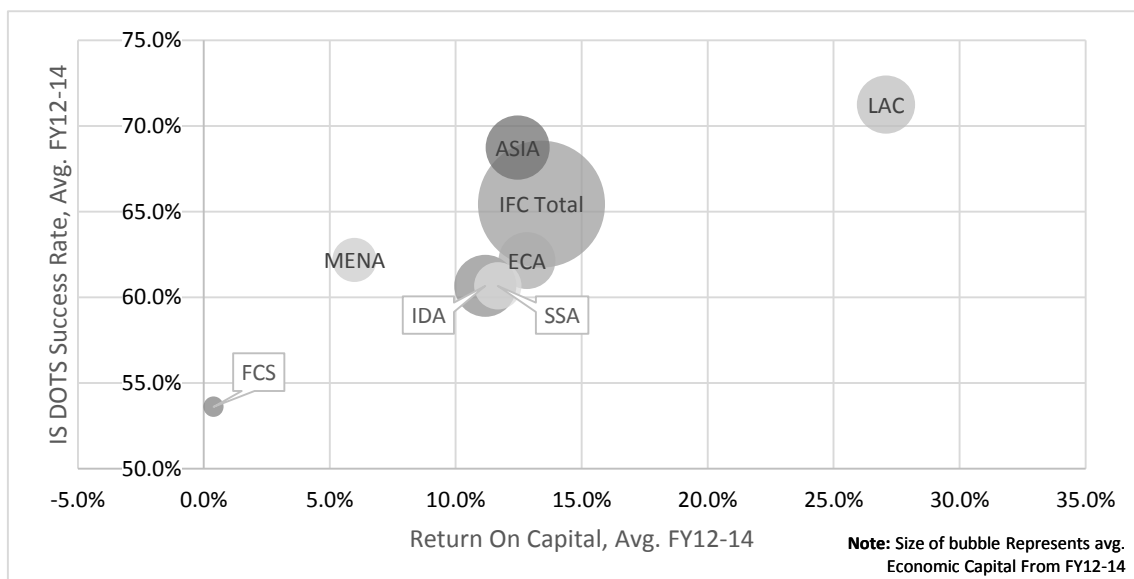
1.31 The chart below also shows that geographic profiles vary significantly, underscoring the need for diversification and customization.

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<sup>2</sup> From analysis shown in APR FY06 to FY13. The main reasons why financial performance may differ from development results are externalities or market distortions; IFC addresses market distortions and externalities in its screening and monitoring.

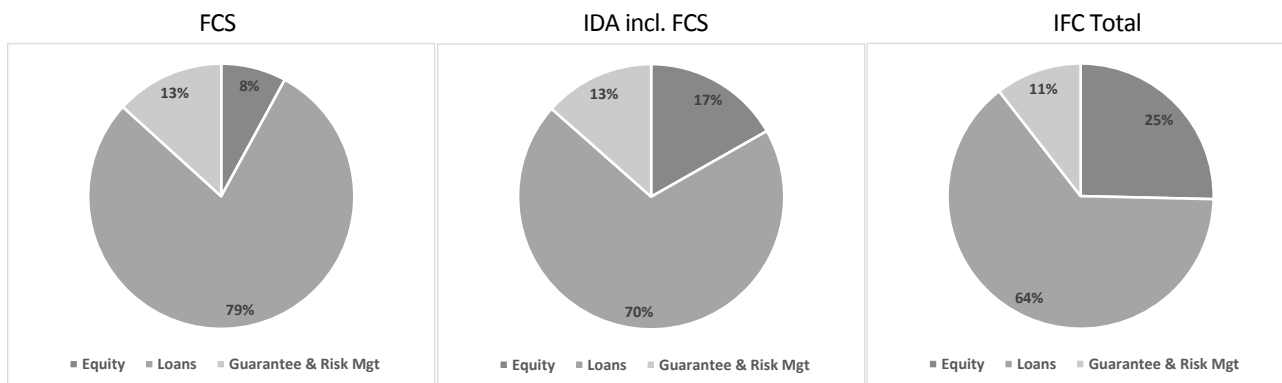


**Chart 1. Ex-Post Correlation of IFC Return on Capital with Client Development Results**



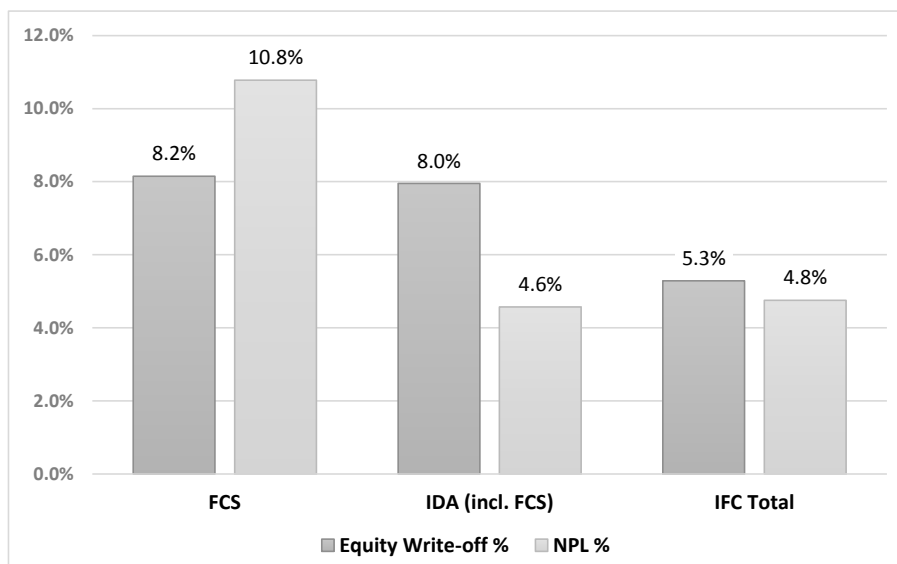
1.32 Since investment risk is higher in FCS and IDA countries, the committed portfolio concentrated in these areas is more heavily weighted in loan products and thus has a smaller proportion of equity compared to the IFC total portfolio. Loan products accounted for 79% and 70% in the FCS and IDA respective portfolios on average from FY12-14, compared to 64% for the total IFC portfolio.

**Chart 2. Committed Portfolio Composition, FCS/IDA/Total IFC, Average FY12-14**



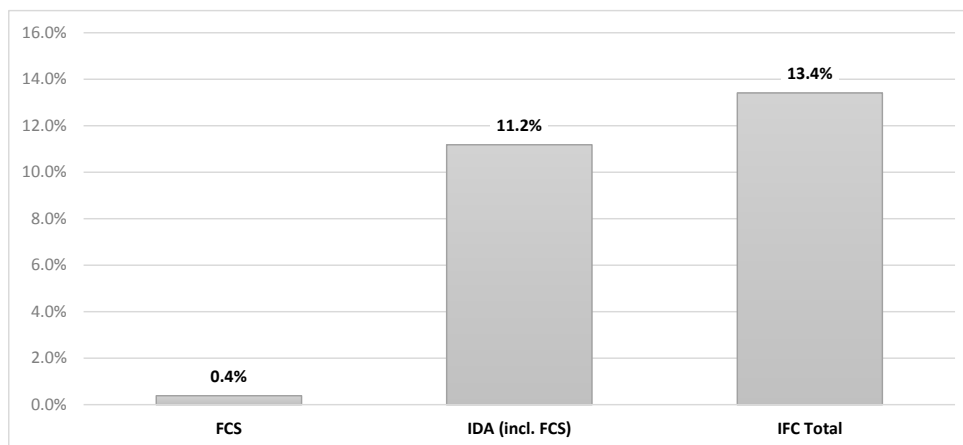
1.33 Loans comprise the majority of FCS committed portfolio. Non-performing loans as a percentage of average outstanding loans in FCS was 10.8% from FY12-14, more than double the total IFC rate of 4.8% during that time. This means that the non-performing principal in FCS countries represented 8.3% of total IFC NPL principal, while accounting for only 3.7% of the total loans outstanding. The NPL percentage for the IDA portfolio during the period was 4.6%, slightly lower than the total IFC average, which was partially driven higher by the subset of FCS delinquent loans. Equity risk is also higher in FCS and IDA countries, as demonstrated by higher write-downs as a percentage of outstanding exposure.

**Chart 3. Portfolio Risk Measures, FCS/IDA/Total IFC, Average FY12-FY14**



1.34 FCS and IDA countries also yield a lower return on average invested capital based on cash income.<sup>3</sup> This metric measures how profitable projects and portfolios are relative to average capital required to support these investments. The FCS returns are exceptionally low driven by the higher cost of doing business in these areas and low equity revenues; equity accounts for only 12% of total revenues in FCS vs. 47% for IDA and 53% for all of IFC. Equity products have higher expected returns because of the higher risk characteristics of the investment.

**Chart 4. Cash Income Return on Average Capital, FCS/IDA/Total IFC, Average FY12-14**

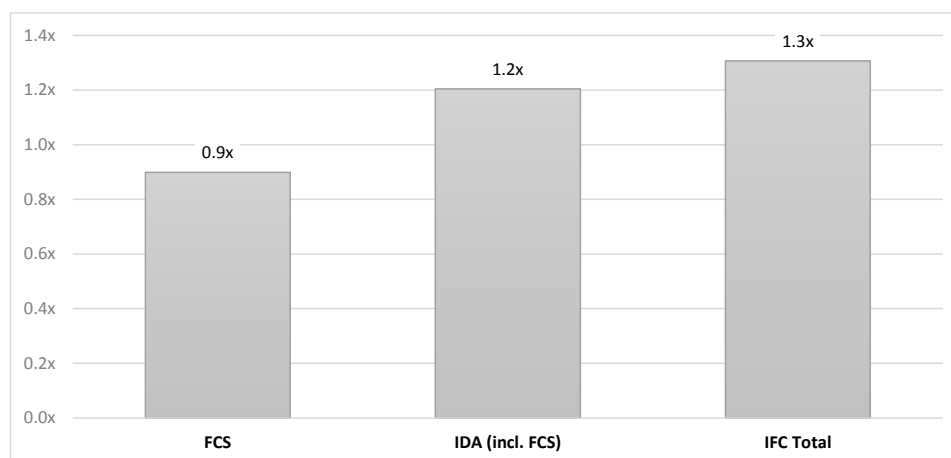


1.35 Another profitability metric under continual usage is the Net Loan & Fee Revenue Coverage of Expenses ratio, which measures a portfolio's ability to cover expenses with stable revenue sources that are less impacted by market volatility. The IFC has a ratio of 1.31x on average from FY12-14, showing

<sup>3</sup> Cash Income is a profitability measure for Investment Operations incorporating all realized revenue and expense drivers.

Investment Operations' ability to cover its costs through its more stable revenue drivers with a healthy 31% buffer. The FCS coverage ratio of 0.90x is below the breakeven ratio of 1.00, implying that the FCS would not be able to cover its expenses with stable revenue sources, even though the majority of its portfolio are loans.

**Chart 5. Net Loan & Fee Rev Coverage of Total Expenditure, FCS/IDA/IFC Total, Average FY12-14**



1.36 IFC maintains its determination to invest in FCS when financial sustainability is achievable; when this entails lesser returns on average, IFC will seek to more explicitly balance compensation elsewhere.

1.37 IFC Management looks forward to a series of informal engagements with the Board in late-FY15 and throughout FY16 on a range of strategic topics that have been identified as meriting further discussion. These will include how IFC has adapted its organizational structure to meet business needs and what early results are emerging.

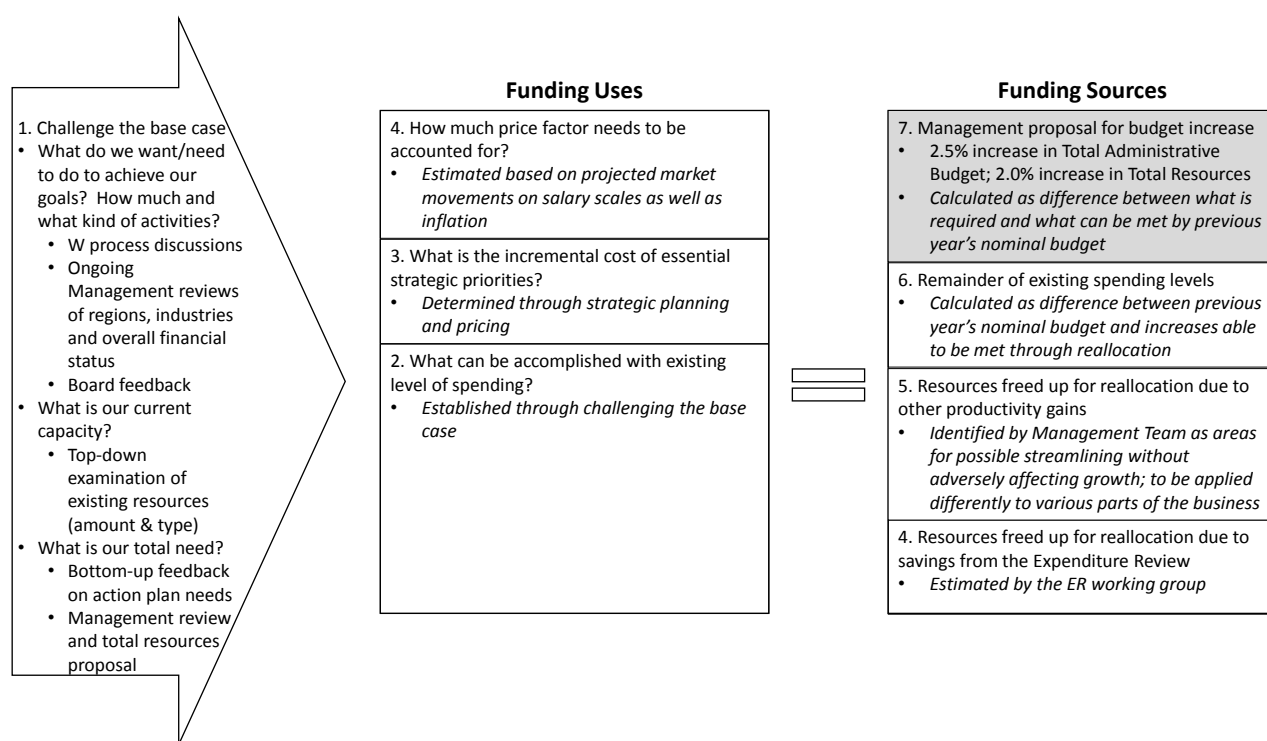
1.38 The evolving intersection of strategic focus, client demand, and opportunity for both development impact and financial sustainability (which are strongly linked), will continue to drive IFC's operational choices and the resource usage that supports them. Please see Section II for more information on budget principles and process.

## II. BUDGET PRINCIPLES & PROCESS

### A. BUDGET PROCESS

2.1 IFC's budgetary framework provides for provisioning of funding for expenses, which follow accrual accounting principles. As part of the budget process, Management analyzes where and how resources are used, considers the deployment and utilization of resources within IFC's profit and loss statement, and deploys resources regardless of whose budget funded them in order to effectively use resources to meet IFC's strategic goals. Figure 5 depicts the process through which IFC developed the FY16 budget recommendations for Board approval.

Figure 5. IFC Budget Formulation Process



### B. BUDGET AS FULL PROFIT & LOSS

2.2 Traditionally, budgeting within the World Bank Group has been focused on expenses. However, as part of the increased emphasis on financial sustainability, IFC has been shifting its budget paper narratives and figures to the entire profit and loss statement over the last few years. This puts resource usage in the context of overall delivery. Accordingly, the FY16 Budget Paper's structure reflects this crucial need for holistic review of both revenues and expenses when determining future spending authority. The corporate P&L view also echoes IFC's extensive cross-department business model.

**2.3 Expenses in P&L.** Diving deeper in to the P&L, Management considers both the deployment and utilization of resources. Corporate level expenses are disaggregated further to understand consumption by function. For operations, this allows a better view of the true cost of doing business and further presents how resources are deployed regardless of whose budget funds them. IFC staff records time against the investment project worked on, which is further reflected in the operational department P&L. "Cross-support" is thereby captured in management accounting (P&L), preventing the need for time-consuming resource transfers. The ability to analyze where and how the resources are used is enabled through management information systems that provide information down to the Client level.

**2.4 Budget.** Flowing from Management evaluation of integrated resource needs across IFC, in any given fiscal year, indicative budgets are allocated to units as a starting point to address where resources reside based on the organizational structure. Indicative budget envelopes themselves are developed both from a corporate, "top-down" perspective, as well as "bottom-up"; the latter is led by IFC's budget and finance network who are globally dispersed across regions and industries and who serve as their respective Controllers. These staff are also responsible for ensuring governance of the budgets, including reporting and strategic guidance on their usage. In-built flexibility provides dynamic opportunities for both informal sharing of resources for combined efforts (more frequent) and formal transfer of budget (less frequent).

**2.5** The guiding principles underlying how budgets are aligned with the organization begin with its largest driver, the staff. The costs of operating a decentralized ecology via regional offices are kept in regional departments. Those expense drivers that are controllable and therefore more flexible (i.e. travel, contractual services etc.) allow not only for strategic shifts and flexibility to balance increased resource intensity in one area by reducing another, but also assist IFC in managing its expenditure review targets where it has direct control and accountability.

## **C. EVOLUTION FROM DEPARTMENT TO DEPLOYMENT AND DELIVERY**

**2.6** While budget envelopes serve as a key component of strategic planning, IFC is not bound by work program agreements, which create more prescriptive utilization principles for the resources themselves. Through the Refocused structure, IFC has an effective delivery framework that allows for the identification of budget needs through central and operationally dedicated staff, with further ability to allocate and reallocate given the expense outcomes to-date; these are in turn assessed against additional Client and subsequent resource needs.

**2.7** Accordingly, IFC Management is committed to further reducing any structural impediments to resource flexibility in the service of Clients. As an example, by recently introducing the Global Administrative Manager function to IFC's three largest industry groups, Management has brought together many support functions, such as budget & finance, knowledge management, and linkages with WBG HR, IT, training. It has also integrated Advisory Services in each industry to increase efficiency within the departments. This both encourages better efficiencies across functions and enables much better cross-departmental coordination as the new WBG and IFC organizational structures and integrated processes are implemented. The GAM is expected to work directly with Regional Industry Heads and Sector Heads to negotiate optimal staffing deployment to ensure that IFC's most skilled resources are deployed to its Clients. The goal is to map the most capable knowledge and specialization to leverage Client capabilities to the fullest. Deployment of more junior staff as well as support resources will continue to be managed largely on a regional basis by the Regional Industry Heads through talent tools such as the staff marketplace to help gain additional efficiencies while framing career development.

### III. PROFITABILITY OVERALL: PORTFOLIO AND PROFITABILITY

3.1 IFC's investment portfolio continually evolves as a result of Client demand, and this portfolio is the main driver of IFC's financial results as well as its economic capital. IFC's income is affected by a number of factors that contribute to its volatile performance. Focus on controllable income allows for drivers less bound by market movements to be separated in order to provide a better ex-ante view of IFC's income.

#### A. PORTFOLIO

3.2 **Portfolio Trends.** IFC's committed investment portfolio stood at \$48.5 billion as of FY15 Quarter 3-end, of which 63% was in loans, 28% in equity, and 9% in guarantees and risk management products, corresponding to \$15.3 billion in total economic capital.

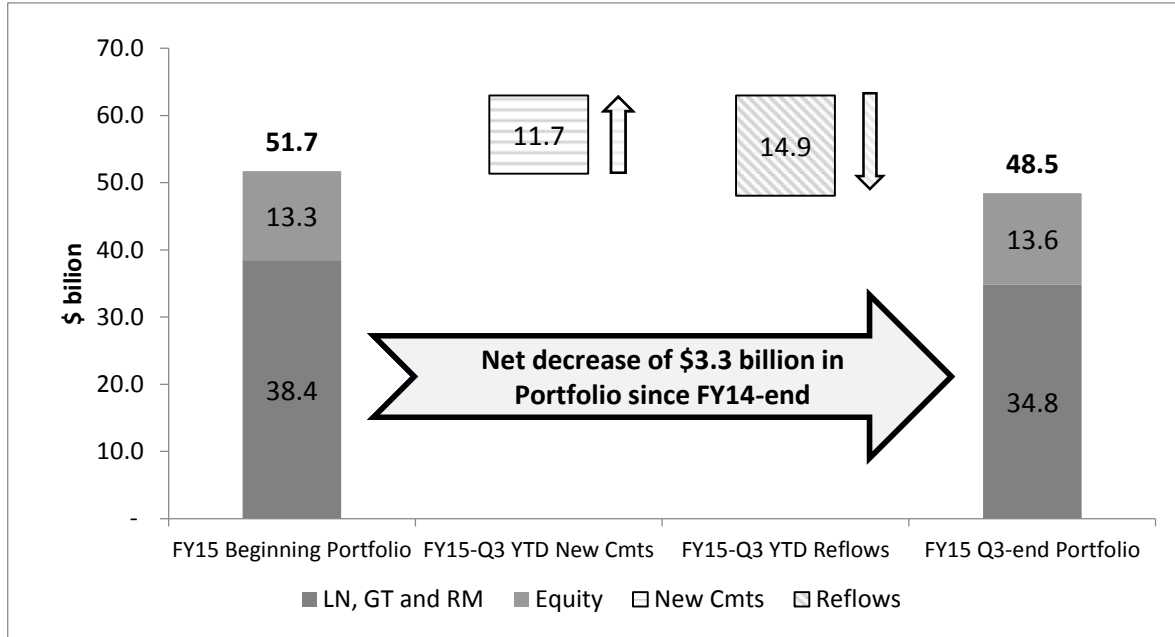
3.3 Increased growth seen through own account commitments has historically been the largest driver of IFC's portfolio. As presented in its FY16-18 Strategy & Business Outlook paper, IFC aims for a potential Long-Term Finance investment volume growth trajectory of 8-10% per year during FY15-18. Mobilization allows IFC to leverage its own capital even further through the inclusion of outside investors and is also expected to grow at the same levels.

**Table 2. IFC Total Commitment Volume, Historic and Projected (\$, billions)**

	FY12A	FY13A	FY14A	FY15E	FY16P	FY17P	FY18P	CAGR FY15E-18P
Long-Term Finance	9.2	11	10	10.3 - 11.3	11.4 - 13.1	12.3 - 14.3	13.0 - 15.1	8 - 10%
Mobilization	4.9	6.5	5.1	5.6 - 6.6	5.7 - 6.6	6.3 - 7.3	7.0 - 8.7	8 - 10%
<b>Total (LTF + Mobilization)</b>	<b>14.1</b>	<b>17.5</b>	<b>15.1</b>	<b>15.9 - 17.9</b>	<b>17.2 - 19.7</b>	<b>18.5 - 21.7</b>	<b>20.0 - 23.8</b>	<b>8 - 10%</b>

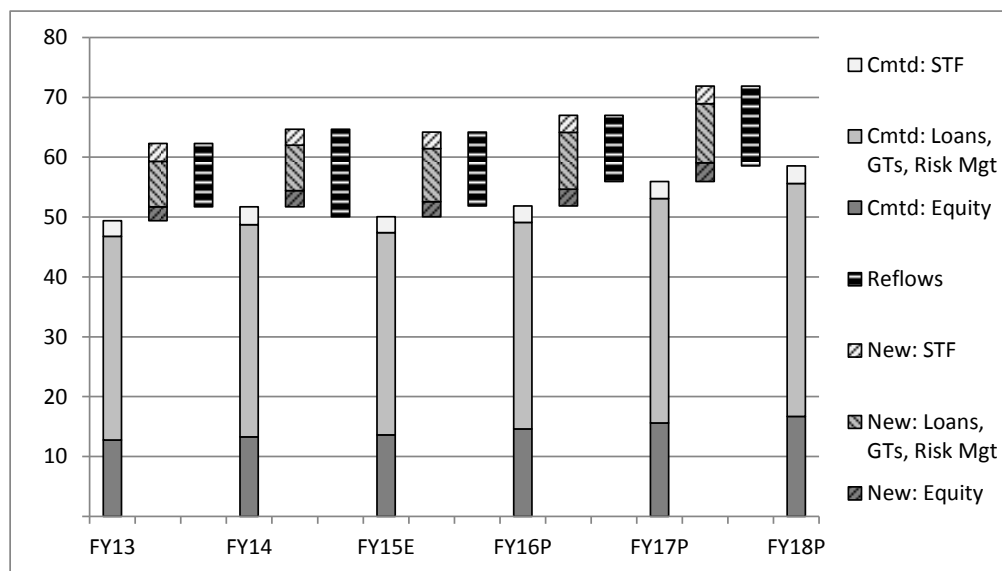
3.4 Growth rates of the committed portfolio are generally more stable year-on-year given the acquired stock of several years' worth of long-term investments coupled with the offsetting of reflows (e.g., repayments, prepayments, cancellations, sales, etc.). In FY15, however, there have been an exceptional volume of reflow activities, as the total reflows through three quarters in FY15 are already exceeding total reflows for all of FY14. These reflows include higher prepayments and cancellations, large portfolio equity sales marked by IFC exiting existing investments, as well as the impact of currency fluctuations on investment valuations, have resulted in a decline from the FY14-end portfolio, making the outlook challenging. This also underscores why IFC takes a portfolio based approach to its growth and carefully considers expectations for future reflows which will further shape the risk profile and composition of underlying investments. Changes in IFC's portfolio are equally if not more crucial to understand than changes to new commitments, given the fact that portfolio is the main driver of financial results as well as IFC's economic capital. A more detailed outlook of the three-year portfolio as well as its impact on IFC's economic capital will be presented and discussed in more detail within the FY15 Financial Risk Management paper.

**Chart 6. Committed Portfolio Evolution within FY15**



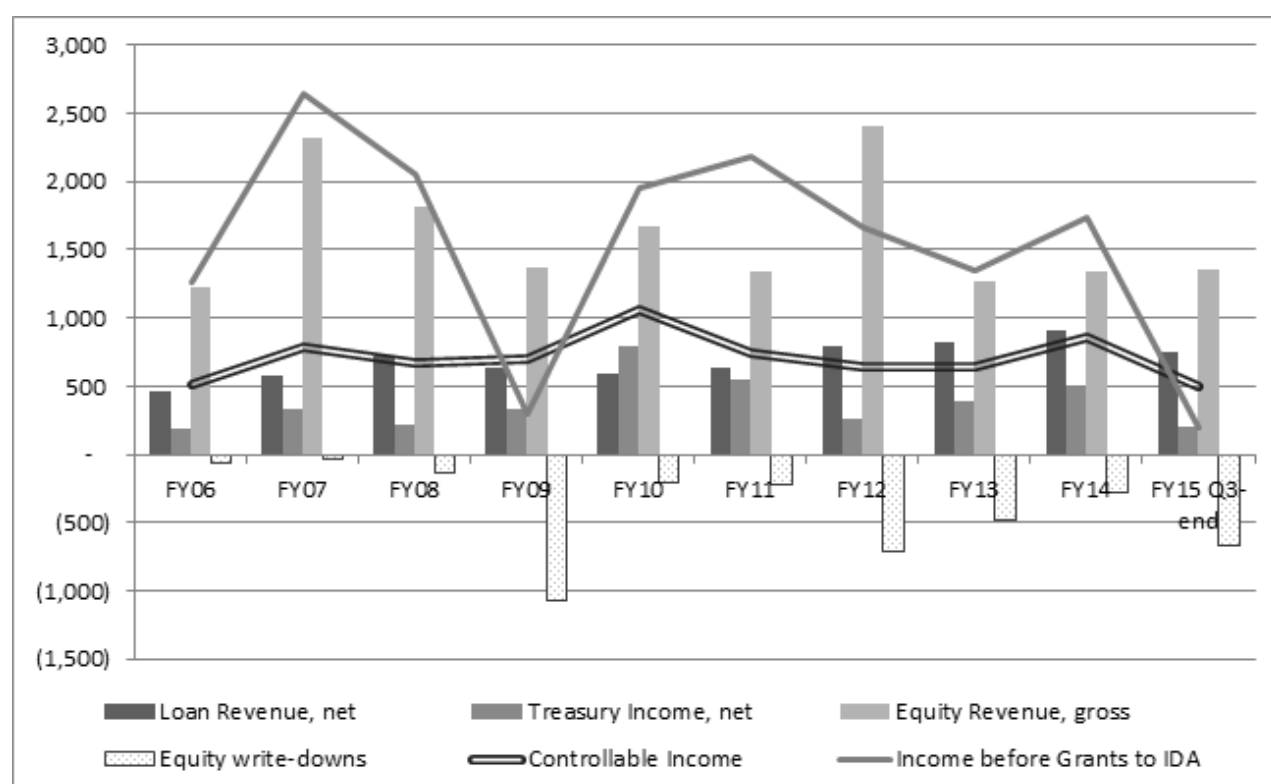
3.5 Despite the decrease in portfolio size in FY15, IFC's committed investment portfolio has been growing at an average rate of about 12% per annum over the last 10 years, reaching \$51.7 billion at the end of FY14. Based on most recent estimates under a base case scenario, IFC's committed portfolio is expected to grow at a compounded annual growth rate of 3% between FY14 and FY18. The projected decrease in portfolio growth compared to historical rates is in part attributable to the need to manage growth of the own account portfolio with limited capital availability, changes to portfolio reflows such as those experienced in FY15 year-to-date, as well as the emphasis on mobilizing third party capital.

**Chart 7. Program and Portfolio Outlook, FY13-18P (\$, billions)**



3.6 **Profitability trends.** IFC's income is affected by a number of factors that contribute to its volatile performance. Historically this has resulted in both favorable as well as adverse results seen through its Income before Grants to IDA. In FY15, global equity markets in emerging economies have generally declined systematically. Taken together with economic downturns in certain geographies, the depreciation of most of IFC's investment currencies against the US Dollar (IFC's reporting currency) and the downward trend in oil prices, these factors have negatively impacted IFC's equity investment portfolio in particular. Despite high capital gains realized early in the fiscal year, IFC has recorded significant equity write-downs. The low equity revenue, net of write-downs, was somewhat offset by solid loan revenue and good revenue from liquid assets.

**Chart 8. Historical Trends in IFC's Revenue and Income Performance, FY06-FY15Q3 (\$, millions)**



## B. CONTROLLABLE INCOME OVERVIEW

3.7 In its FY15 Budget paper IFC introduced the concept of "Controllable Income", which allows for drivers less bound by market movements to be separated in order to provide a better ex-ante view of IFC's income. The first three quarters of FY15 demonstrated the impact of external occurrences on IFC's income statement in the form of equity write-downs and changes to unrealized gains and losses through valuation. Such results only reaffirm the unstable patterns which can be seen in any given quarter. Within a controllable income frame, Management can make a closer determination as to FY-end results.



**Table 3. Controllable Income (\$, millions)**

	FY09 (A)	FY10 (A)	FY11 (A)	FY12 (A)	FY13 (A)	FY14 (A)	FY15 Q3-end
Loan & fee revenue (net)	694	677	719	883	954	1,027	836
Treasury revenue (net)	331	796	542	267	389	494	206
Dividends	318	292	289	288	262	285	172
Advisory Services gross-up	0	0	0	269	239	254	172
Other revenue*	120	142	177	143	194	221	185
Controllable revenue	1,463	1,907	1,727	1,850	2,038	2,281	1,571
Total expenses (incl. AS)	(764)	(853)	(981)	(1,207)	(1,401)	(1,418)	(1,076)
<b>Controllable income</b>	<b>699</b>	<b>1,054</b>	<b>746</b>	<b>643</b>	<b>637</b>	<b>863</b>	<b>495</b>

\*includes Custody fees, Service Fees and other revenues

## C. PROFITABILITY OF STRATEGIC PRIORITIES

3.8 **Metrics.** IFC has been developing metrics which would allow monitoring of performance and measurement of success in the most effective way. The Corporate and Department Scorecards are now streamlined and aligned with the World Bank Group Scorecard. They have also evolved to balance development impact, financial sustainability, and quality of delivery for clients, while at the same time continuing IFC's focus on areas of climate change, FCS and IDA. IFC Management has continued its shift from counting transactions and commitment volume and more toward financial sustainability and impact. There is also a shift toward giving greater weight in determining rewards to corporate performance relative to department results, to promote cross-departmental collaboration.

**Table 4. Profitability and Productivity Metrics Monitored for Investment Operations**

<b>Dimension</b>	<b>Quantitative Measures</b>
Financial Sustainability	Controllable Cash income <sup>4</sup>
	Cash Income <sup>5</sup>
	Net Loan & Fee Revenue Coverage of Total Expenditure
	Equity Internal Rate of Return (IRR)
	Loan Risk Adjusted Return on Capital (RAROC)
	Total Costs over Assets Under Management
Delivery for Clients	Total LTF Commitment Volume
	STF Outstanding Portfolio
	Increase in % of LTF Deals where Mandate to Disbursement time < 250 Days

3.9 In addition to the quantitative measures shown above, greater consideration will be given to qualitative factors such as approach and progress in enhancing overall impact, progress on WBG cooperation and progress in implementing the client coverage model, as validated by internal Business and Client Reviews. In monitoring these metrics, IFC also is spearheading a cultural change in the way

<sup>4</sup> Controllable Cash Income is a profitability measure for Investment Operations incorporating stable and predictable revenue and expense drivers. It excludes realized capital gains and corporate overhead.

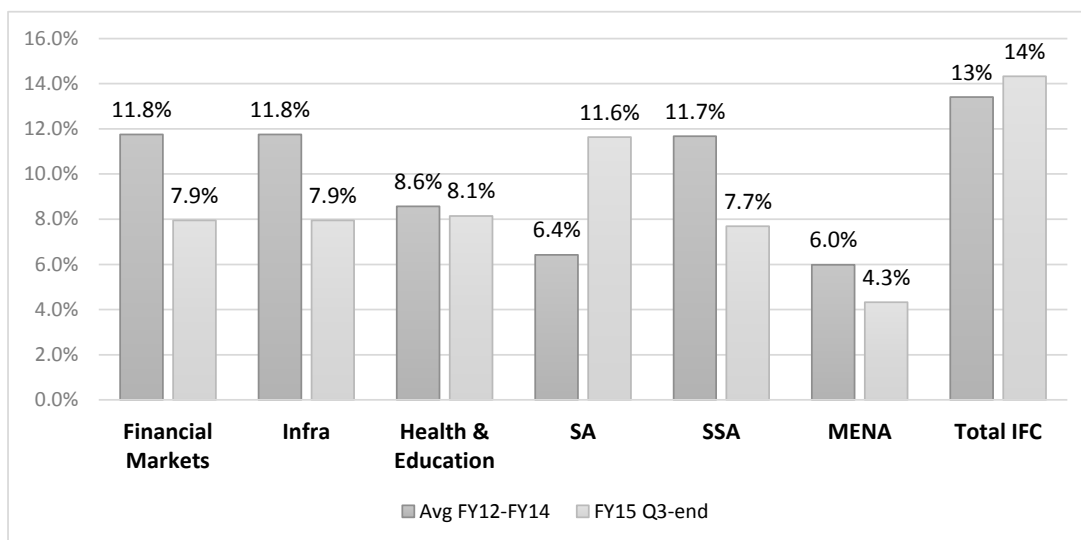
<sup>5</sup> Cash Income is a profitability measure for Investment Operations incorporating all realized revenue and expense drivers. It equals Controllable Cash Income plus realized capital gains and less corporate overhead.

operations are assessed for impact as well as incentivizing staff toward achievement of financial sustainability and productivity goals.

### Select Metrics for Operations and their results across Strategic Areas

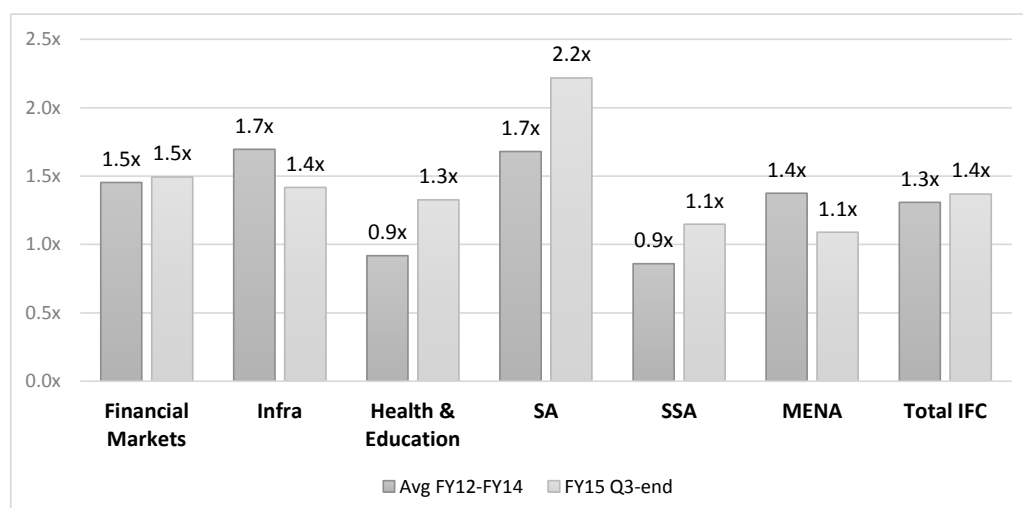
3.10 The returns on average capital for strategic focus areas have historically been lower than the total IFC average. The drivers of lower returns vary by focus area, however these individual focus area portfolios are not as diversified as the total IFC portfolio, thus do not capture the same degree of benefit from the IFC global portfolio approach, as highlighted in para 4.10.

**Chart 9. Cash Income Return on Average Capital by Strategic Focus Area**



3.11 IFC's strategic focus areas have for the most part been able to cover their expenses with revenues generated from stable revenues. South Asia and Infrastructure in particular have delivered strong loan and fee revenues that outperform the IFC average.

**Chart 10. Net Loan & Fee Rev Coverage of Total Expenditure by Strategic Focus Area**



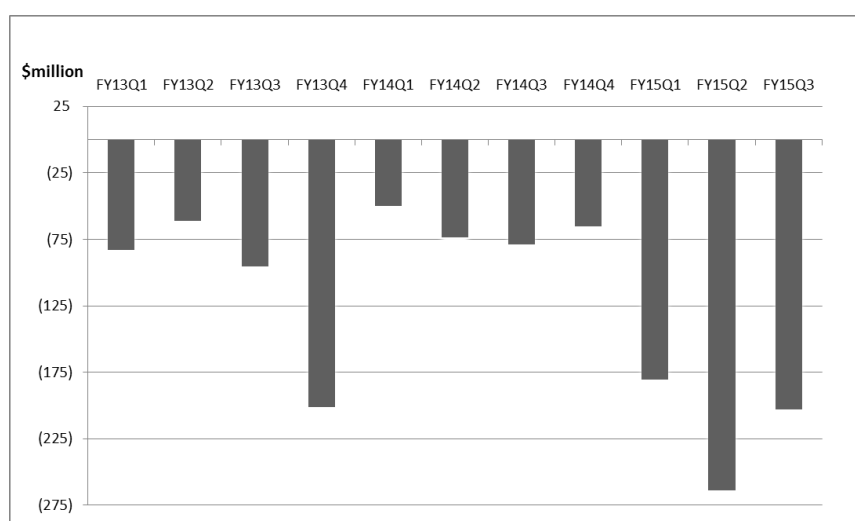
## IV. PROFITABILITY DRIVERS: REVENUE

### A. INVESTMENT OPERATIONS

#### INVESTMENTS: EQUITY

4.1 Revenue from equity investment portfolio is impacted by global climate for emerging market equities, fluctuations in currency and commodity markets and company-specific performance for equity investments. Such impacts resulting in valuation of equities below cost are immediately captured in the form of equity write-downs, which are deducted from the portfolio until such time when the equity is sold. Chart 11 indicates how volatile the performance of equity write-downs can be within any given fiscal year.

**Chart 11. Quarterly Trends in Equity Write-downs (\$, millions)**



4.2 In the current environment in Emerging Markets, the prevailing headwinds in conjunction with the uncertainty around the expected timing of potential interest rate increases in developed markets make it extremely challenging to accurately forecast IFC's expected bottom line income from equity on an accounting basis. Nevertheless, despite the increasing volatility, IFC's portfolio is holding up well and continues to maintain substantial levels of unrealized accounting capital gains which are expected to help the corporation maintain a healthy level of cash income from equity sales.

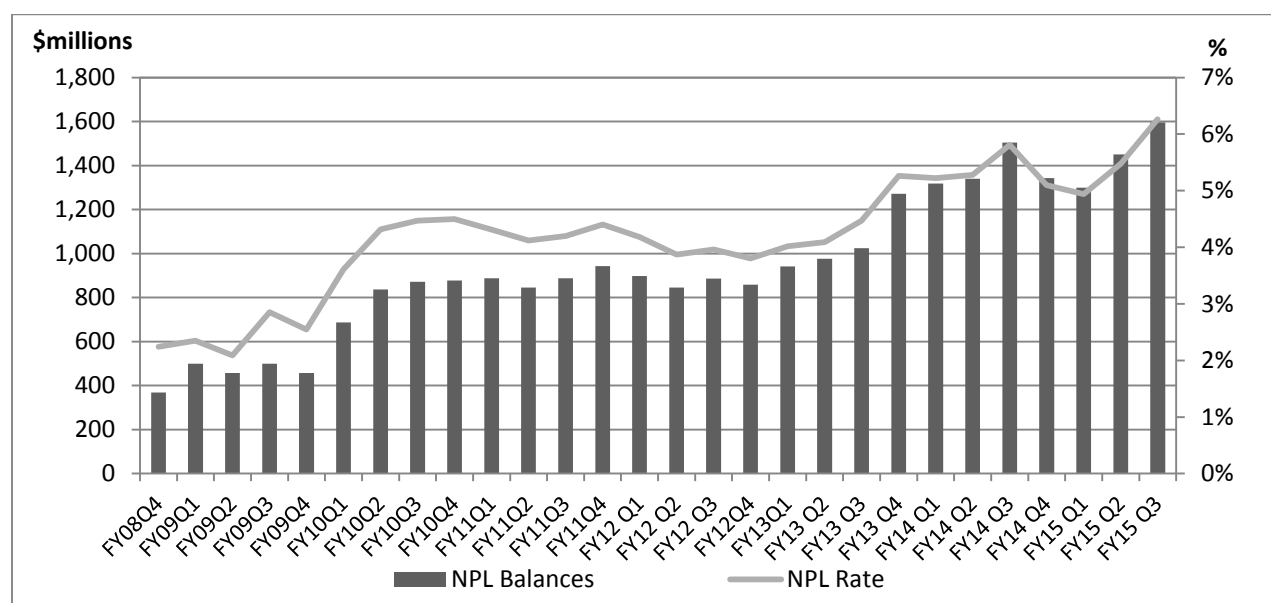
4.3 The timing and amount of realized capital gains are extremely difficult to predict with accuracy, particularly as the time horizon lengthens. IFC has a disciplined bottom-up equity sales process, overseen by Senior Management. The ultimate objective is to maximize value, subject to completion of IFC's development role. For each company in the portfolio, sales decisions are based on an analysis of development role, performance of the company, market environment, and future expected prospects. This rigorous holistic portfolio review allows IFC to detect vulnerabilities that may trigger action (i.e., either sale or restructuring) thereby limiting its downside and/or adding value.

## INVESTMENTS: LOANS

4.4 IFC's loan revenue has been stable over the past few years. The average annual realized income from loans (including trade & commodity finance) from FY12 to FY14 has been \$955 million, and the revenue from loans for the first 3 quarters of FY15 has been \$836 million, up about 9% year-on-year (but with a higher amount of provisions).

4.5 The main drivers for loan revenue are growth of the committed portfolio, the rate of disbursement, and the pricing of our loans. Other factors that can influence loan revenue include the level of cancellations and prepayments, and the amount of non-performing loans and provisions. In FY15, committed exposure has dropped, but the rate of disbursement has increased a little, leaving IFC's outstanding loan portfolio nearly unchanged. Pricing has also been relatively stable, with the spread on senior US\$-denominated loans slowly climbing higher throughout the year. Both cancellations and prepayments have increased in FY15, driven mainly by a handful of large loans that have been cancelled or prepaid. Reasons for the cancellation/prepayment are largely project-specific, but in several cases, the appreciation of the US\$ (making the loans more expensive in local currency terms) seems to have played a role. NPLs have steadily increased in FY15, and, although to-date this has been driven by a few large loans going into NPL status without a clear regional or sectoral trend, Management is in frequent discussions to understand further impact on the remainder of its portfolio.

**Chart 12. Trends in Non-Performing Loans, FY08Q4-FY15Q3 (\$, millions)**



4.6 Going forward, while some factors may fluctuate, IFC is carefully monitoring its loan portfolio and expects the overall loan revenue to continue to grow steadily and more than cover administrative expenses.

4.7 IFC's Special Operations unit is solely dedicated to working with operational teams and Clients to resolve issues within IFC's portfolio. In light of results to-date, this unit will continue to step up its

resolutions and cash recoveries by, among other initiatives: (i) monitoring projects at risk so that it is involved at an earlier stage and add maximum value; (ii) streamline the approval process for restructurings to increase efficiencies and the speed of decision making; (iii) develop a more systematic approach to distressed loan sales as a resolution mechanism; and, (iv) disseminate lessons learnt widely to ensure effective dissemination of feedback into the new business process.

## INVESTMENTS: TRADE & COMMODITY FINANCE

4.8 **Trade and Commodity Finance.** Through its suite of Trade and Commodity Finance (TCF) products, including portfolio risk-sharing, working capital loans, and trade guarantees, among others, IFC complements its classic long-term projects with short-term investments while effectively delivering return on capital. In FY15, measurement of short-term finance, which represents two-thirds of IFC's TCF exposure, shifted from accumulative commitments to average outstanding portfolio to more accurately reflect both its contribution to IFC's annual program and how these business lines are overseen. Both the Global Trade Finance Program (GTFP) and other TCF products are managed with significant consideration of resulting return on risk-adjusted capital. Financial results show that the portfolio for each business line has exceeded its fully loaded break-even size. With the operational foundation in place, these products provide stable, recurring revenue through lower-risk, shorter-tenor exposures, providing a counterbalance to the portfolio of IFC's classic longer-tenor investments.

4.9 Revenue from GTFP comes almost exclusively in the form of fee income, while other TCF products generate significant income from interest as well as fees. (For example, about \$8 million of TCF revenue attributable to FIG in FY15 is broken out as TCF interest income; the remaining \$7 million in fee income is consolidated into FIG.) Yields on TCF facilities are generally in line with what is available in local markets, given the fact that most trade finance is demand-driven and IFC is a price-taker. Along with prices, other factors that affect the portfolio size (e.g., number of instruments issued, instrument tenor, replenishment rates, etc.) drive program profitability. TCF facilities currently represent \$4.2 billion, or 11 percent of total IFC portfolio, while using 3 percent of its economic capital, demonstrating a resource efficient and scalable business that can quickly and effectively channel resources to respond to crises and market gaps (global financial crisis, Ebola outbreak, etc.) and extend IFC's reach in challenging markets. Overall, the TCF portfolio is expected to continue to increase at a CAGR of 3-4 percent over the next three years. As the portfolio grows, revenue is expected to increase in kind, given current market assumptions.

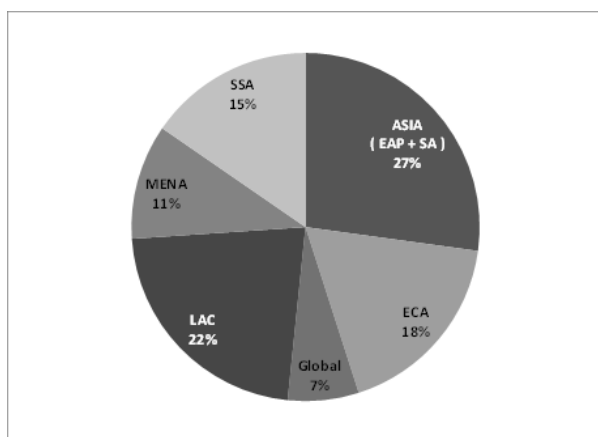
**Table 5. Short-Term Finance Projections, FY12-18P (\$, billions)**

	FY12A	FY13A	FY14A	FY15P	FY16P	FY17P	FY18P	CAGR FY15P- 18P
<b>Average Outstanding</b>	2.5	2.7	3.0	2.6-2.8	2.7-2.9	2.8-3.0	2.9-3.1	3 - 4%

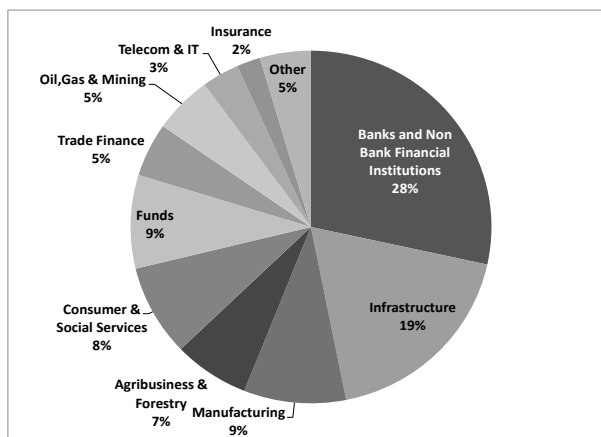
## INVESTMENTS: GLOBAL PORTFOLIO APPROACH AND DIVERSIFICATION BENEFITS

4.10 One key advantage IFC has is its global portfolio approach, which has allowed IFC to generate sustainable income overtime. IFC's diverse investment portfolio is composed of multiple investment instruments that are concentrated in various geographic regions and industry sectors. Additionally, IFC employs prudent portfolio management and capital limits on countries and clients. This multi-faceted approach reduces unsystematic market risks that would arise from over-concentration and dependencies on individual investments.

**Chart 13. IFC Portfolio by Region, FY15 Q3-end (Total = \$48.5 billion)**

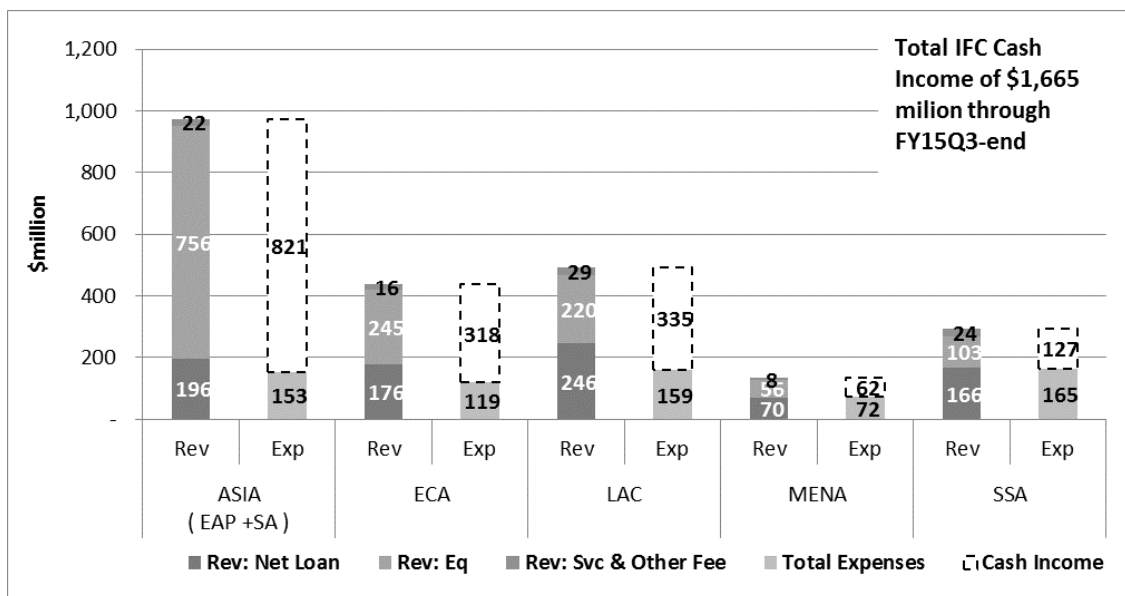


**Chart 14. IFC Portfolio by Sector, FY15 Q3-end (Total = \$48.5 billion)**



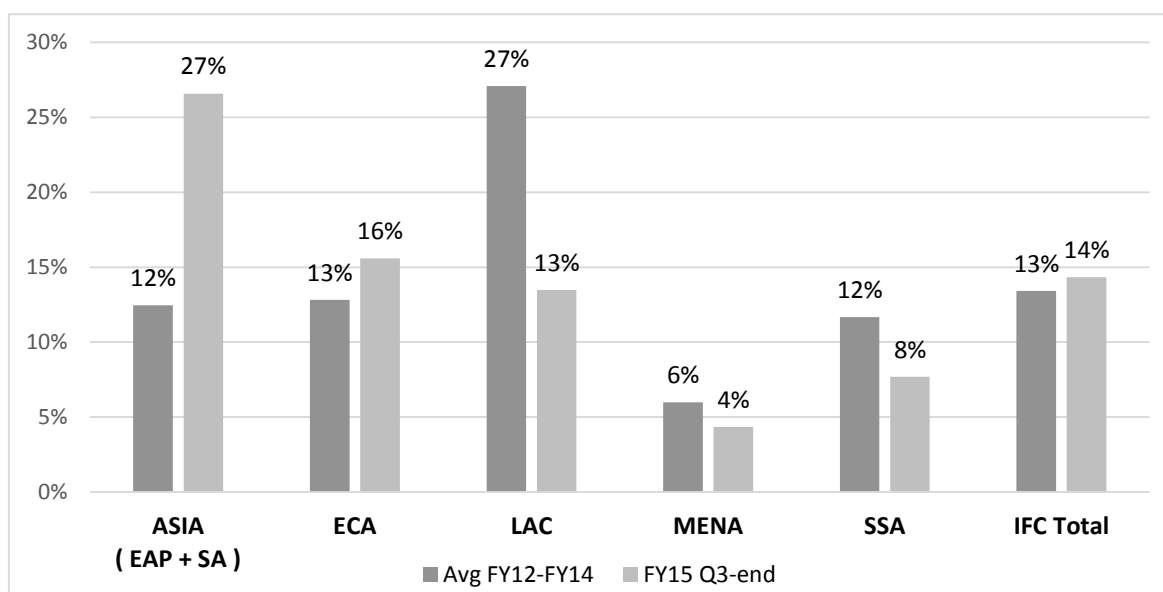
4.11 Despite facing challenging economic conditions during FY15, IFC has managed to generate solid realized cash income during the first three quarters of FY15, generating the second highest cash income through the first three quarters since FY08 (second to record year in FY12). The results are largely driven by strong realized capital gains whilst controlling expenses. The FY15 Q1-Q3 results have also produced the highest Net Loan and Fee revenues in the last 10 fiscal years, further demonstrating the versatility of IFC's portfolio to earn revenues from different sources. Cash Income includes IFC realized income, including realized capital gains, but excludes unrealized drivers, such as write-downs and impacts of exchange rate movements on investments.

Chart 15. Cash Income by Region, FY15 Q3-end



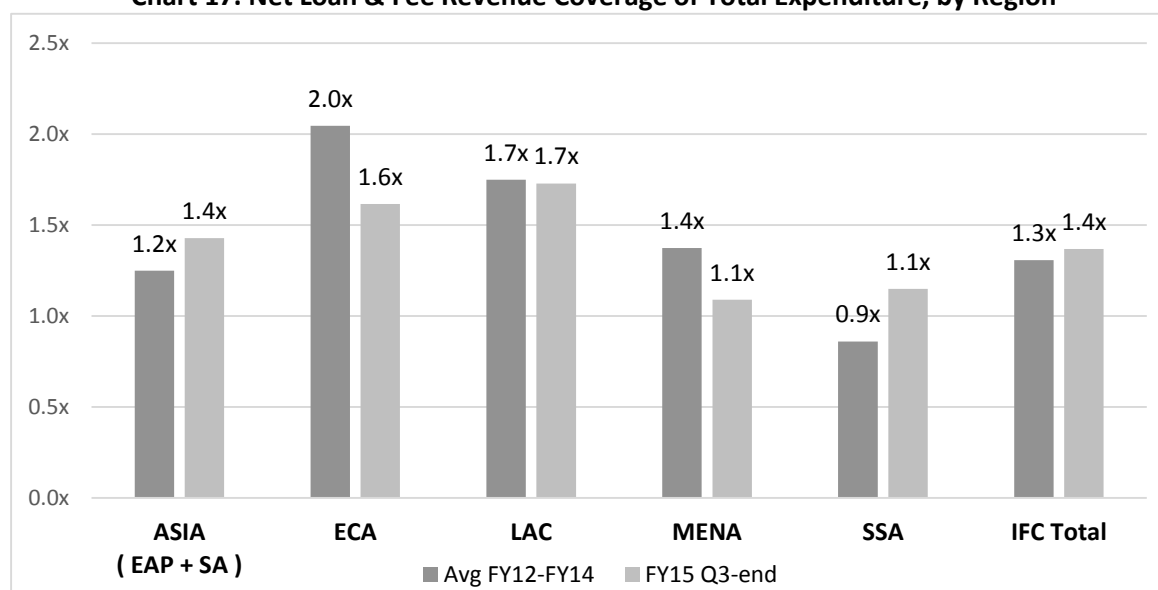
4.12 The exceptional cash income results in FY15 Q1-Q3 in turn has yielded a higher return on invested capital compared to the FY12-FY14 average (even while including the historic FY12 performance). The realized income generated from the portfolio has grown faster than the required capital to support these investments.

Chart 16. Cash Income Return on Average Capital, by Region



4.13 Almost all of IFC's regions have averaged a Net Loan & Fee Revenue Coverage ratio above 1.0x over the last three fiscal years, and the overall IFC ratio for FY15 Q3-end is slightly higher than the three-year average. This coverage ratio measures IFC's continual ability to cover its cost of doing business with stable revenues.

**Chart 17. Net Loan & Fee Revenue Coverage of Total Expenditure, by Region**



## B. ADVISORY SERVICES

4.14 Advisory Services (AS) recognizes three types of revenue: donor contributions, administrative fees on donor contributions, and client contributions. Donor contributions, recognized as revenue at the time they are expended, are leveling off in FY15/16 - in line with total AS Spend, to consolidate reforms and facilitate transition to the new organizational structure. Revenues from clients are expected to continue growing, as IFC's funding model for advice to private firms places growing emphasis on client contributions. Administrative fees on donor contributions remain broadly stable. As a result total revenues are expected to grow beyond FY16, enabling IFC to continue to increase the leverage of its contribution to total Advisory Spend.

## C. TREASURY & SYNDICATED LOANS

4.15 Treasury has made a strong start on its promise to deliver an additional \$1 billion to IFC's net income through FY23. Additional income is expected to be generated through a number of new initiatives:

- (i) Increase in assets under management;
- (ii) Increase in fee income from client and bank counterpart activities;
- (iii) Fee income from Managed Co-Lending Portfolio Program (MCP - program launched in FY14);
- (iv) Additional income from investments in emerging market sovereign debt, bonds issued by sovereign instrumentalities, and corporate bonds (e.g., Brazil, Mexico, China, India); and,
- (v) Potential fees from asset management services provided to third parties.

4.16 Treasury Market Operations invests IFC's net funding surplus and net worth in money markets and fixed income instruments with an emphasis on capital preservation and maintaining a prudent liquidity level. This involves proactive management of IFC's balance sheet with a focus on diversification and risk management.



4.17 In FY15, Treasury portfolios continued to solidly outperform their respective benchmarks. Key generators of excess return have been (i) the collapse of the spread between the yields of IFC's onshore investments in China and off-shore hedges and (ii) spread tightening in international structured products, particularly European securities. For FY15, IFC projects liquid asset net revenue of \$270-320 million.

4.18 The above-mentioned initiatives and the projected increase of IFC's investment portfolio should support the trend of growth in returns.

4.19 Treasury will continue to support the development of capital markets through strategic first time issuances in emerging markets. Treasury will also continue to focus on increasing investor awareness of opportunities offered by socially responsible investment-themed bonds, and promote emerging market corporate bonds in local currencies as an asset class. In addition, Treasury will continue to serve its core mandate to safeguard IFC's financial resources and triple-A credit ratings. Through prudent asset liability, funding, and liquid asset management, Treasury will ensure that IFC has the funds it needs for investing in private sector development, along with sufficient liquidity to guard against global financial uncertainty. Where appropriate, Treasury will ensure close links with IFC's Investment Services (e.g., in cross-vice presidential unit steering groups and the Mobilization and Investor Engagement Steering Group).<sup>6</sup>

4.20 **Forward-looking trends in Syndicated Loans:** Raising and deploying other investors' capital to meet clients' financing needs continues to be a central component of IFC's business model and an increasingly important part of IFC's strategy, primarily because it allows IFC to preserve and fully leverage its limited resources, while maximizing development impact. IFC's Syndicated Loans remain a key component of IFC's overall core mobilization efforts, providing 60% of IFC's total core mobilization raised in FY14 and 72% to-date (as of FY15 Q3). IFC's suite of Syndicated Loans include the traditional "B Loan", Parallel Loans, the MCPP Loan, Structured A-Loan Participation Sales and Unfunded Risk Participations.

4.21 IFC's Syndicated Loan program is also the largest contributor to IFC's service fees, generating revenue of \$27 million in FY14.

4.22 From FY15 onward, IFC will focus on growing the volume of its syndicated loan activities e.g. by expanding the MCPP platform; broadening its co-investor base to include more emerging market (local) banks; and exploring the risk appetite of institutional investors.

## D. ASSET MANAGEMENT COMPANY

4.23 As of March 31, 2015, AMC manages approximately \$8.1 billion across eight funds. AMC's primary source of revenue is the management fees paid by the funds under management. AMC's policy is to charge investors market rates for managing funds. With these revenues, AMC covers its own direct expenses and pays IFC fully for the resources it provides, with the overall objective of making a small net profit. AMC's financial statements are fully consolidated into IFC's, so any net income that AMC makes, net of intra-company eliminations, flows through to IFC's Profit & Loss.

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<sup>6</sup> The Mobilization and Investor Engagement Steering Group provides IFC-wide coverage and connectivity among groups on private equity funds, mutual funds and sovereign wealth funds.

4.24 AMC pays fees to IFC to compensate for the services it provides in developing funds and in providing sourcing, execution and supervision services. AMC pays four types of fees to IFC:

- i) Transaction Fees: Fee based on transaction size (subject to a cap and a floor) which is paid when the transaction is completed and disbursed.
- ii) Supervision Fees: An annual fee paid for each portfolio company. In addition, if upon the agreement of the AMC and IFC, unusual supervision costs are incurred, these will also be reimbursed.
- iii) Fund Development Fees: For each fund launched, a fee based on the total fund size is paid over two years in equal quarterly installments, starting from the quarter after the first close.
- iv) Business Development Fee: For selected funds, a fee to help strengthen resources in regions and sectors to ensure sufficient deal pipeline is generated and portfolio monitoring is effective. This fee is based on the total fund size and is paid over five years in equal installments.

4.25 In addition, AMC-managed funds reimburse IFC for the funds' share of out-of-pocket expenses related to transaction execution and supervision. Where IFC receives mandate fees from the investee company as part of a transaction, the pro rata portion of those fees is netted against expenses reimbursed and/or fees payable by AMC. AMC also makes regular payment to IFC for salaries and benefits of staff seconded to AMC under Services for a Wholly-Owned subsidiary (SWO) and for services provided such as office space and to reimburse IFC for expenses it incurs on behalf of AMC or its funds. In a few situations, AMC may also reimburse IFC for a portion of the compensation of selected IFC staff who spend a majority of their time on AMC-related work.

## V. PROFITABILITY DRIVERS: EXPENSES

5.1 Expenses form the second component of IFC's P&L; they reflect the resources needed to operate and deliver IFC's development mandate. IFC's expense structure reflects its unique business model.

### A. MAJOR EXPENSE DRIVERS

5.2 **Staffing.** Whether providing direct client services, intellectual capital, or a variety of support services, IFC's staff are its greatest asset, and their salaries and benefits account for the largest component of IFC's expenses, at roughly 57% of total resources in the FY15 total resources budget. IFC is continuing its effort to maximize its delivery capacity through more efficient deployment of staff resources, through consolidation and realignment. For example, IFC has introduced global functional talent pools under a single Global Client Services Vice Presidential Unit, that not only allow the organization to tap into global expertise to add value to clients, but also provide flexibility to reallocate staff time to respond to rapidly shifting business priorities. These functional talent pools also enable IFC to provide global career opportunities for staff regardless of point of hire or duty station, which is an essential component of IFC's employment value proposition, particularly for more junior staff. With 59% of IFC's staff based outside of the U.S., it is critical for IFC to continue to provide ongoing career development opportunities for these staff in a cost effective manner.

5.3 As of FY15 Q3, IFC had 3,726 staff, compared with 3,879 staff at the close of FY14. Overall staffing levels have decreased slightly, driven by management's continued oversight of staffing plans across the organization. Instead of automatically replacing exiting staff, IFC has looked primarily at internal redeployment of skills, and limited external recruitments.

5.4 Short-term consultants contributed another roughly 8% toward FY15 total resources budget, largely driven by the Advisory Services model.

5.5 **Shared Services Agreements.** SSAs allow IFC and its counterparts in the World Bank Group to leverage WBG commonalities, specializing and standardizing certain functions for greater efficiency. IFC has entered into a number of SSAs with the IBRD to provide support for its functions. This support ranges from all aspects of IT, Human Resources and External Communications to Finance or General Services, through transaction and administrative expense and compliance activities provided by central units.

5.6 During FY15, the value budgeted for SSAs amounted to \$134.1 million (Table 6); this comprised approximately 14% of the FY15 total administrative budget. The value of services provided by the WBG Integrated Services entities (Human Resources; Leadership, Learning and Innovation Services; IT; and, External Communications) amounted to \$67.3 million or approximately 50% of the total.

5.7 In planning for the FY16 SSAs, IFC instituted new governance procedures in order to better align the services purchased with IFC's business priorities. The Business Planning & Administration Department was assigned as the corporate sponsor for WBG Integrated Services SSAs. In this new role, BP&A also undertook an in depth review of SSAs and engaged closely with IBRD counterparts to better understand the cost drivers. This more focused engagement is anticipated to deliver the net savings reflected in Table 6. In total, the cost for FY16 SSAs is expected to be \$1.1 million less than in FY15 in nominal terms. Going

forward, IFC will monitor SSA results to ensure that the service delivery meets the Key Performance Indicators promised at the outset of the year.

**Table 6. IFC-IBRD Shared Service Agreements (\$, millions, nominal terms)**

Service		World Bank Unit	FY15 Amount	FY16 Estimate	Anticipated Increase/ (Decrease)
1	IT Services	ITS	47.4	48.6	1.2
2	Human Resource Services	HR	10.3	8.8	(1.5)
3	Leadership, Learning and Innovation Services	LLI	1.4	1.3	(0.1)
4	Communication Services	ECR	8.2	8.0	(0.2)
5	Board Services	COGOV	24.2	24.6	0.4
6	Integrity Department Services	INT	3.6	2.0	(1.6)
7	Independent Evaluation Group Services	IEG	7.0	7.0	-
8	Internal Audit Services	IAD	2.3	2.3	-
9	Controllers Services	WFA	3.6	3.4	(0.2)
10	General Services Department Services	GSD	14.7	15.0	0.3
11	Procurement Services	GSD	2.9	3.0	0.1
12	Insurance Services	GSD	2.5	2.6	0.1
13	Business Continuity (BCP) Facility	GSD	0.7	0.8	-
14	Treasury Services	TRE	0.6	0.6	0.1
15	Risk Services	CRO	0.4	0.4	-
16	Ethics, Conflict Resolution and Tribunal Services	EBC	3.0	3.3	0.3
17	Child Care, Legal and Staff Association Services	GSD	1.3	1.3	-
<b>Total</b>			<b>134.1</b>	<b>133.0</b>	<b>(1.1)</b>

5.8 Further details on total resources by cost category may be found in Table 14.

## B. RESOURCE USAGE BY SELECTED STRATEGIC PRIORITIES

5.9 IFC is committed to maximizing development impact while maintaining financial sustainability and focusing on strategic focus areas. For example, IFC places strong emphasis on frontier markets, in particular Fragile and Conflict Situations and other IDA countries while maintaining geographic diversification for financial, risk and development purposes.

5.10 **Investment Operations.** The traditional budget view of spending reflects expenses based on who owns the resources according to the organizational structure. This section translates the spending from who owns the resources into where the resources were deployed. This view captures "cross-collaboration" without transferring resources across departments and ensures resource fungibility, which underlies operational flexibility. Accordingly, the following tables show how the resources were consumed in order to deliver the program, consistent with IFC's continuous effort to focus on its strategic areas.

**Table 7. Total Investment Operations Administrative Expenses + Core Fees, by Region, IDA & FCS**

	FY12	FY13	FY14	FY15Q3
<b>Total IFC (mn)</b>	<b>\$863</b>	<b>\$933</b>	<b>\$975</b>	<b>\$733</b>
Asia	22%	22%	20%	21%
ECA	18%	17%	17%	16%
LAC	19%	20%	22%	22%
MENA	9%	9%	9%	10%
SSA	19%	20%	22%	22%
World	14%	12%	11%	9%

IDA	32%	32%	34%	35%
FCS	6%	7%	7%	6%

**Table 8. Total Committed Portfolio, by Region, IDA & FCS**

	FY12	FY13	FY14	FY15Q3
<b>Total IFC (mn)</b>	<b>\$45,275</b>	<b>\$49,610</b>	<b>\$51,727</b>	<b>\$48,457</b>
Asia	25%	25%	25%	27%
ECA	22%	21%	21%	18%
LAC	22%	21%	21%	22%
MENA	11%	11%	10%	11%
SSA	13%	15%	15%	15%
World	6%	7%	7%	7%

IDA	27%	27%	28%	28%
FCS	4%	3%	3%	3%

% share in IDA and FCS based on countries included in IDA, FCS list at each FY, IDA countries include IDA and IDA blend

5.11 The resources allocated to Africa and MENA increased in absolute amounts as well as in percentage of total expenses (FY12: \$162 million and \$77 million to FY14: \$213 million and \$87 million, respectively) throughout the period. This is also reflected in an increase in their portfolio in absolute amount. While Africa experienced between FY12 and FY14 a compounded annual growth rate (CAGR) of 15% in both expenses and portfolio, MENA presented a 6% CAGR in expenses and 1% in committed portfolio reflecting that, due to political tensions in some of the countries of the regions, the cost of doing business is higher. This trend in expenses and portfolio continued throughout FY15.

5.12 Proportional spending on investment projects in IDA countries rose slightly in FY12-14, while it remained fairly steady in the sub-set of FCS countries over the same period. The percentage of investment portfolio increased in IDA in absolute amounts and relative terms throughout the period FY12-FY14. FCS portfolio decreased in FY13 vs. FY12 but started recovering since then. IDA expenses slightly increased in FY15YTD as a share of IFC's total expenses while portfolio remained the same as a proportion of total committed portfolio. Notably, the portion of IFC spending on FCS investment operations is roughly twice their representation in the IFC portfolio volume; when looking at IDA investments overall, proportional spending still significantly outpaces representation in the portfolio. This resource intensity underscores both IFC's dedication to these populations and the difficult conditions on the ground. IFC operational results continue to reflect its strategic priorities and maintain diversification both from a financial as well as a geographic composition perspective, recognizing the significant development impact that can be achieved in Middle Income Countries as well.

5.13 **Advisory Services.** Following strong growth in recent years, AS spend leveled off in FY15 to consolidate reforms and facilitate transition to the new organizational structure. AS will look to engage with greater selectivity, based on corporate priorities, and increase its development impact. FY15 Q3-end total AS spending was \$240 million and FY15 full year spending is projected at \$370 million. Total AS spending is expected to resume a moderate 2.5% growth in FY16-18. Advisory Program spend is expected to grow more rapidly, nearly 4% over the same period, as a result of new efficiencies from reforms.

5.14 AS Programs have had a strong focus in strategic priority areas of IDA (66% in FY14), FCS (20%) and Climate Change (25%) (see Table 9), and in priority regions (nearly 60% in FY14 in Asia and Sub-Saharan Africa; see Table 10). This emphasis is expected to continue in the coming years.

**Table 9. Advisory Services, Strategic Emphasis Areas, FY12-15 Q3-end (\$, millions and %)**

	<b>FY12</b>	<b>FY13</b>	<b>FY14</b>	<b>FY15 Q3-end</b>
Program Spend	\$197	\$232	\$234	\$138
IDA Share*	66%	65%	66%	64%
FCS Share*	18%	18%	20%	19%
Climate Change Share	16%	24%	25%	23%

\*Projected share of AS program in IDA and FCS based on countries included in approved IDA, FCS List at year of project approval.

**Table 10. Advisory Services, Program Spend by Region, FY12-FY15 Q3-end (\$, millions and %)**

	<b>FY12</b>		<b>FY13</b>		<b>FY14</b>		<b>FY15 Q3-end</b>	
	<b>\$mn</b>	<b>%</b>	<b>\$mn</b>	<b>%</b>	<b>\$mn</b>	<b>%</b>	<b>\$mn</b>	<b>%</b>
Program Spend	197	100	232	100	234	100	138	100
Asia	56	28	73	31	73	31	43	31
ECA	34	17	36	16	39	17	23	17
LAC	21	11	26	11	25	11	16	12
MENA	18	9	20	9	22	9	14	10
SSA	57	29	65	28	63	27	35	25
Global	11	5	12	5	12	5	7	5

## C. UPDATE ON EXPENDITURE REVIEW

5.15 IFC is committed to deliver 18% of total WBG savings in line with the initial estimates. This corresponds to approximately \$71.3 million in gross savings over FY15-18. The Expenditure Review design stage is complete, and IFC is already making progress against all measures currently in implementation. IFC is measuring results based on whether IFC has direct accountability or IFC has input into WBG decision-making but where IFC's gross savings will depend on policy approval and implementation actions at the WBG level. D. Update on Areas for Potentially Increased Resource Intensity in FY15 Budget Paper

5.16 **Environmental, Social & Governance (ESG).** IFC Management identified ESG risk management (including the need for stronger client support) as a particular area for increased resource intensity in FY15 and over the next several years. Under the new Corporate Risk & Sustainability Vice Presidential Unit, the Transactional Risk Solutions department (CRK) laid the foundation for enhanced ESG risk management and increased support to clients in adopting and applying IFC's environmental and social (E&S) Performance Standards. CRK furthered IFC's ESG leadership and ramped up risk management in the following areas, disbursing 96% of CRK-ESG's total allocated administrative budget<sup>7</sup>: enhanced due diligence, intensified supervision and portfolio management, stakeholder engagement and institutional learning, and client support.

5.17 Enhanced due diligence. IFC increased its engagement in delivering comprehensive E&S assessment where clients are faced with complex challenges to the Performance Standards. Examples

<sup>7</sup> Based on Q3 spending projections for FY15.

include intensified support for understanding contextual risks as part of the Ebola crisis response (e.g. Palm Oil in SSA, rubber in Liberia), cumulative impacts in hydropower (Nepal), Myanmar land and legacy review as a first step to a refined due diligence framework for the Myanmar context, and engagement with 14 clients to address security forces issues. Over 20 risk reports were generated assessing country conditions and sector specific issues in 19 countries, including 4 fragile and conflict affected states. Essential tools for due diligence were developed and improved including a customized E&S geographic information platform (GIS) which is being piloted in Mozambique, the transition to a web based mapping system of agriculture commodities related issues (GMAP) with scope for expansion of country-commodity combinations, and the extension of a bio diversity protected areas mapping system (IBAT). Data from these tools, as well as pre-appraisal assessment on labor, are used to inform both appraisal and supervision, and feed into WBG Systematic Country Diagnostics.

5.18 Intensified supervision and portfolio management. In FY15, CRK also augmented its portfolio management with improvements in systems and procedures to our overall monitoring system. Industry specific portfolio reviews have been completed in infrastructure and agribusiness with a new coordination mechanism for handling high risk infrastructure funds, including tracking of high risk sub projects.

5.19 Stakeholder engagement and institutional learning. CRK continues to deepen the dialogue with the Compliance Advisor Ombudsman to incorporate their recommendations as relevant into practice and procedures. In FY15, CRK held 4 deep dives sessions with CAO on the complaint process, dispute resolution, and compliance matters. An inter-departmental working group has been established to guide project teams in addressing CAO cases, and to ensure that lessons learned are reflected throughout the institution. IFC also held workshops with non-governmental organizations on areas of mutual concern. In addition region based training programs targeting high risk sectors, were held in Asia (PE Funds Asia Pacific) and EMENA.

5.20 Client support. In FY15, CRK introduced a system for enhanced client support, helping to manage investment portfolio risk by focusing on clients with Partly Unsatisfactory or Unsatisfactory Environmental & Social performance (Environmental and Social Risk Ratings of 3 or 4), clients in fragile contexts, high risk markets, and strategic/repeat clients. Five financial intermediaries and four direct investment clients have received enhanced ESMS diagnostics to date, with additional diagnostics planned for the rest of the fiscal year. In addition customized assessments and solutions to challenges facing clients in implementation are currently being piloted. This pilot seeks solutions for challenges related to implementation of E&S management systems across a range of themes and industries including wind energy (Jordan, Balkans), energy terminal (Pakistan), hydropower (Pakistan, Nepal), animal welfare (EMENA, Asia), garment industry (Bangladesh), Financial Intermediaries with commodity exposure (Ivory Coast, Liberia), oil palm (Indonesia), infrastructure public private partnerships (PNG and Timor Leste) and fisheries (Djibouti, Solomon Islands). Lessons from experience will inform a ramped up approach in FY16.

5.21 In FY15, more systematic efforts were made to flexibly and quickly deploy senior staff and experienced consultants to respond to emerging high risk situations and offer intensified client support. Examples include support for ESMSs, security forces expertise, labor standards, community engagement and land, life and fire safety requirements, and customized solutions in fragile contexts. With the strategic staffing exercise now complete, an integrated system is in development to learn from and scale up mechanisms tested in FY15.

5.22 In addition, CRK continued to focus on solutions to emerging E&S challenges. Through this work, Mongolia and Vietnam launched environmental and social risk management guidance for the financial sector; three more members joined the Sustainable Banking Network from Kenya, Morocco and Pakistan;

guidance was completed on how to integrate human rights considerations in environmental and social risk management; screening tools were considered for resilience in our infrastructure projects; and IFC joined in global discussions on the valuation of natural capital.

**5.23 Technology.** WBG IT integration continues to bring innovation into many areas of IT, greatly increasing the capabilities to staff. WBG initiatives have also brought critical improvements to IT infrastructure and shared platforms. In FY15, the next step was taken in the implementation of the WBG Federated IT Operating Model, with all IT client service support staff across the WBG were centralized into ITS. This centralization is intended to align the IT vision, culture and service delivery and improve IT service agility, risk management, efficiency, and cost-effectiveness through a scaled and standardized approach.

**5.24** At the same time, IFC's Chief Information Officer continues to advocate IT priorities, coordinate governance, manage business relationships, deliver IFC specific business solutions, and monitor IFC requirements and services across ITS delivery. IFC retains governance over its capital investment program, ensuring that IFC business priorities are served. During FY15, IT made tremendous progress on its ambitious program to accommodate growing business demand for system improvements. Achievements leveraging increased resources in the FY15 budget include the new iPortal processing gateway for investment operations, the new IFC dashboard interactive analytical tool for operational data, the first major upgrade to IFC's loans platform, and the launch of the new Integrated Risk Platform pilot.

**5.25 New Delivery Model.** Timely delivery of quality services is essential to supporting our clients many of whom operate in volatile markets. A team of senior IFC investment and risk professionals conducted a thorough diagnostic to measure IFC's responsiveness to clients. The team found that while IFC's investment process is in line with the industry and other peer institutions, IFC is slower in delivering to clients. The team identified the main reasons to be behavioral and cultural in nature – how staff from different roles and functions work together throughout the investment process. One of the key recommendations is to establish a partnership model between IFC investment and risk functions based on lessons learned from recent successful experiences within EDC and GE Capital.

**5.26** The simplified and interconnected organizational structure that is now in place in the Refocused model is conducive to changing how IFC works internally to deliver to clients. A number of recommendations on project management practices, project segmentation based on risk profile, and parallel instead of sequential execution of process steps are currently being implemented on a pilot basis in the LAC region through the beginning of FY16. The objective of the pilot is to test approaches that would lead to significant increase in responsiveness to clients commensurate with the deal complexity and maintaining IFC's robust standards. We expect to see the greatest improvements in processing times across lower risk and straightforward projects, recognizing that complex and high risk projects require more time. The implementation of the pilot will inform the roll out of successful practices across IFC.

**5.27 Strategic staffing plans.** To ensure that the right people are in the right place to support IFC's operations, IFC conducts an annual workforce planning review to match projected business needs with the needed talent to achieve IFC's business objectives. This review helps managers to evaluate if their staffing structure is adequate to support their evolving business, and allows the organization to identify possible skills gaps and efficiencies. Linking this review with its talent review process, IFC will assess staff for appropriate opportunities such as internal mobility and strategic reassignments to fill identified gaps, before acquiring talent externally.



5.28 While IFC will likely have a decline in staff numbers in FY15, for FY16 IFC's overall workforce is projected to increase slightly as compared to FY14 levels. The Management Team will continue to monitor recruitment very closely to ensure it addresses critical skill gaps and priority areas. IFC intends to grow its business over the next few years, supported by internal measures to improve staff efficiency, as well as targeted external recruitment focused on previously identified gaps including junior talent to better leverage senior staff and senior industry and E&S specialists.

5.29 **Performance Awards.** Awards, incentives and recognition programs can have a significant impact on organizational results when such plans are designed with strategic intent, and where critical components are driving and aligning business goals, results and behaviors. Today, IFC has a portfolio of incentives and recognition programs that reward strong performance and recognize extraordinary team and individual contributions. As the organization strengthens its new delivery model, the awards programs need to have a stronger link among individual, department and corporate goals to incentivize staff to collectively deliver on organizational results. Recognizing and celebrating outstanding individual and/or team achievements, collective delivery towards business priorities, and increasing performance differentiation are among the key features that IFC would like to continue to enhance in its programs.

5.30 In FY14, IFC created a greater alignment between the WBG Corporate Scorecard and IFC's Scorecard, and also strengthened the link between corporate performance and awards pay-outs through the IFC Annual Performance Awards program. For the FY15 performance cycle, key changes include increased focus on fragile states, the expansion of IFC's scorecard awards to operations support units, and greater recognition for client-facing functions, all in support of the strategic alignment of performance goals across individual, department and corporate-wide levels.

## **E. AREAS FOR INCREASED RESOURCE INTENSITY IN FY16**

5.31 **Environmental, Social & Governance.** Building on the foundations laid in FY15, ESG will further adjust its business model and enhance its Environment & Social capacity to effectively support increasingly complex investments and clients who need it most. This will include more hands-on work at client sites where warranted. More specific efforts include: (i) enhance portfolio management, pro-actively manage risk and enhance supervision where needed, (ii) further support strategic clients as well as committed low capacity clients in implementing the Performance Standards, (iii) strengthen due diligence and understanding of systemic and emerging E&S issues as well as contextual risk faced by our clients, (iv) further sustainability leadership and partnerships in the private sector, building on IFC's convening role in strengthening overall authorizing environments and coordination. This includes systematic engagement with the World Bank to support the Bank's safeguards policy reform process.

5.32 With strategic staffing plans complete, the E&S delivery model will continue to deepen, initially bringing on board ten environment and social specialists, and maintaining the high level of leverage and flexibility in E&S deployment globally with a 2:1 ratio of fixed to variable costs (representing the balance between staff and consultants). Building on recommendations from the Business Process Review and findings from the ongoing LAC pilot, CRK will, in addition, make efficiency improvements and seek to increase its portfolio analytics and Monitoring & Evaluation (M&E) capacity in order to better leverage and prioritize resources towards projects and clients.

5.33 IFC will continue to strengthen its engagement with civil society and its ongoing work with the CAO, as well as review findings from the Independent Evaluation Group to inform and improve the effectiveness of its E&S business model including in relation to financial institutions.

5.34 As IFC's business grows in fragile and conflict affected situations, along with increasing emphasis on more complex transformational projects, CRK will need to further deepen E&S client support and work with investment operations to assess risks and support the private sector in managing these risks.

5.35 Knowledge and understanding of the E&S challenges that are likely to face clients is an important part of IFC's value proposition. IFC's experience with clients helps us see common challenges that firms and sectors face regionally and globally, and convene to find solutions that enable business and grow markets in a sustainable way. In FY16, CRK will leverage these internal knowledge opportunities to support IFC's leadership position in the market, bringing IFC's global knowledge and expertise to bear on some of the more difficult E&S challenges facing the private sector. CRK will selectively seek external engagements which can help IFC stay at the forefront of the sustainability issues likely to impact private sector investment, deepen our work with industries in understanding their emerging issues, and leverage IFC's role in the WBG to address the broader contextual environment which is fundamental to the private sector's success and sustainable, shared growth.

5.36 CRK will continue to support engagements with holistic recommendations and expects to be an active participant on Joint Implementation Plan teams. The knowledge we provide through the Systematic Country Diagnostics and Country Partnership Frameworks process and the learning that we take back to our operational context will play an important role in understanding country and sector contexts and shaping WBG strategy.

5.37 **Fragile & Conflict Situations.** IFC is taking a holistic approach in further strengthening its commitment to FCS and staying focused on tackling the most critical challenges while maintaining its prudential responsibilities:

- i) As a clear signal of interventions in this area, the existing FCS Risk Envelope will be significantly enhanced. IFC will introduce measures which enable early guidance and ongoing support directly from senior management for more challenging FCS projects.
- ii) IFC will work to mobilize new pools of risk capital and blended finance instruments to complement existing facilities with the aim of filling key gaps in areas such as infrastructure and encouraging developers and sponsors to bring high impact projects to market in FCS. IFC's contribution to IDA will also be a key area of focus for senior management to ensure that its efforts and resources are most effectively leveraged.
- iii) IFC will seek to boost its project development and upstream work to help expand deal-flow and build client capacity in FCS markets. This will include, for example, ramping up efforts to support building of Environmental, Social and Governance (ESG) capacity for active investment Clients in these markets while acknowledging the significant challenges, work in FCS presents on this front.
- iv) To achieve meaningful impact in FCS, IFC must bring the best of its skills and talents to bear in these markets. IFC will shortly outline measures to: (i) increase awards for compelling staff contributions to FCS operations and portfolio support, (ii) ensure managerial decisions are aligned to facilitate and enable FCS efforts and (iii) allocate additional funds to facilitate Development Assignments, appraisals, external research & analysis and awareness events linked to FCS efforts.

5.38 In addition, over the next few months, IFC will utilize the Business Review process to engage with regional and industry colleagues to deliberate and define the most critical development challenges in FCS markets and focus collective efforts in those areas.

5.39 IFC has also worked alongside the Fragility, Conflict and Violence cross cutting solution area. The FCV group will have even closer synergies as the IFC works to stimulate private sector growth and tackle the barriers to business in difficult environments. The unit also serves as a global hub connecting people working in the discipline across the world with knowledge and resources to help improve development outcomes. At the project level staff with deep working experience in conflict-affected situations helps operational colleagues across core sectors such as governance, social protection, gender, private sector development, financial management.

5.40 **Treasury and Capital Markets Innovation.** Treasury will contribute to IFC's growth and profitability targets in FY16 through the establishment of two regional hubs (London, Singapore) in addition to Washington. The new hubs will position Treasury to meet its objective of generating an additional \$1 billion in income for IFC over the next 10 years while providing services to internal and external clients around the clock. The London hub is expected to be fully operational by August 2015; the Singapore hub by July 2016. Three fully functional hubs will allow Treasury to be "open 24/7" and provide timely responses to IFC clients, IFC's key global financial counterparties, and market opportunities. Concentrating staff in these three locations creates a critical mass of various skillsets, including Client Solutions, Market Operations, and Quantitative Analytics; this means that every major time zone can be fully serviced from at least one hub in real time.

5.41 IFC will also continue to contribute to the development of local capital markets and innovative local currency financing solutions through a three pronged approach:

- i. Direct IFC issuance in selected markets and expansion of the universe of counterparts to raise local currency through derivatives;
- ii. Assist IFC clients in gaining access to local capital markets through anchor investments and credit enhancement of their bond/securitization transactions;
- iii. Continue focus on new capital markets product development to crowd in private investment, such as participations in, and innovative enhancement for, infrastructure project bonds.

5.42 **Performance Awards.** For FY16, in line with driving the delivery of business priorities under the "Refocused IFC", IFC proposes a total performance awards budget, as follows:

- i. A base budget of \$19.6 million, which represents an inflationary increase (aligned with IFC's overall budget increase 2.5%) over the current total awards budget of \$19.1 million; and
- ii. A top-up of \$8.5 million that will be available to IFC contingent on achievement of corporate-wide financial measures, including income and development impact-related metrics to reflect both short and longer-term performance perspectives.

5.43 These budget line items will cover all of the IFC rewards and recognition programs. The top-up amount represents about 40% of the base budget and IFC will only have access to this fund if the corporate performance targets are met. In addition, a few other features will be adopted such as:

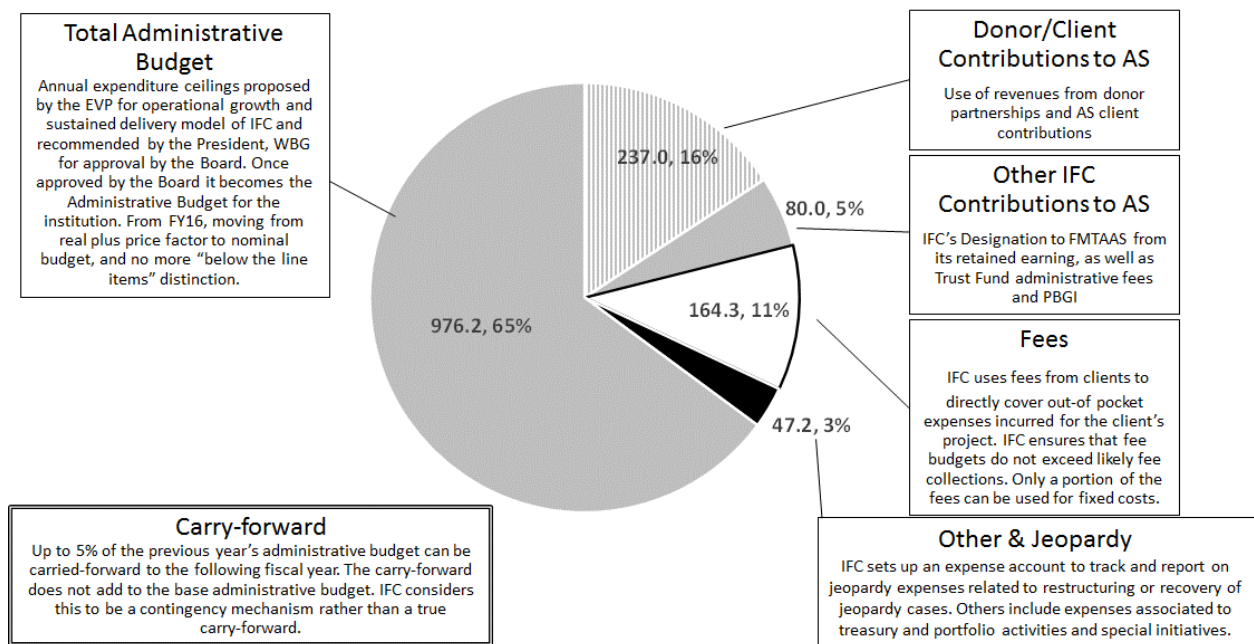
- i. The potential recipients of the top-up budget will be only those departments that have met or exceeded their development scorecard targets;
- ii. In line with building and sustaining a performance culture, performance differentiation will be further emphasized, where awards pay-outs will be more focused on the top performers and outstanding teams; and
- iii. As Fragile States and Conflict Affected Situations represents an urgent development priority for IFC, enhancements on incentives for work on projects in FCS will be adopted.

## VI. IFC'S TOTAL RESOURCES

### A. TOTAL RESOURCES

6.1 IFC's Total Resources represent the full spectrum of expenses needed to deliver IFC's business model. IFC's FY16 proposal for Total Resources sums to \$1.5 billion. The Total Administrative Budget (for which Board approval is sought in Section VII) comprises 65% of the total; the remaining 35% is spread across other sources of funds as summarized in Figure 6 and Table 11. Each component of Total Resources is addressed in the following pages in terms of both sources and uses of funds.

Figure 6. IFC's FY16 Sources of Funds (\$, millions)



6.1 It is important to note that IFC has made three changes in the way the budget is presented to the Board. This has been done to simplify the presentation and to align with the Bank's practice. First, all budget figures are presented in nominal terms to make comparisons across fiscal years easier to understand and better align with the Profit & Loss. The proposal for FY16 thus includes a price increase of 2% to account for anticipated inflation and salary structure increases. The second change is the elimination of 'below the lines items' which formerly distinguished the Regular Administrative Budget (considered fully under control of Management, and the basis for discussion of budget increases) from the Total Administrative Budget which included 'below the line items', namely Board costs, Independent Evaluation Group, and pension contributions. By this change, Management is taking full responsibility for all expense items within IFC's Total Administrative Budget. The third change is to provide the indicative budgets for FY17 and FY18 both for Total Administrative Budget and Total Resources. The indicative budgets for FY17 and FY18 reflect an increase of 2.5% and 3.1% respectively for anticipated inflation and salary structure increases.

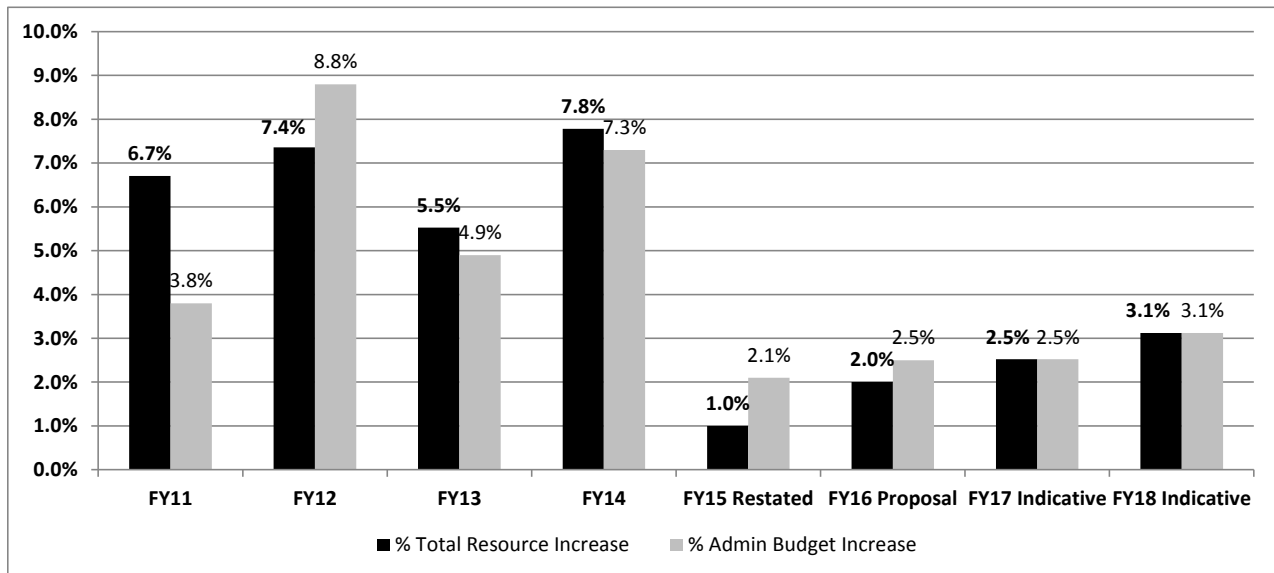
**Table 11. IFC Total Resources, FY14 Actual to FY16 Budget (\$, millions, nominal)**

	FY14 Actuals	FY15 Restated Budget	FY16 Budget	Variance FY16 v FY15
<b>Total Administrative Budget</b>	<b>894.7</b>	<b>952.6</b>	<b>976.2</b>	<b>23.6</b>
<b>IFC Contributions to Advisory Services (other than admin. budget)</b>	<b>87.7</b>	<b>83.7</b>	<b>80.0</b>	<b>(3.7)</b>
Funding Mechanism for Technical Assistance and Advisory Services	67.7	63.0	63.0	-
Others	20.1	20.7	17.0	(3.7)
<b>Donor/Client Contribution to Advisory Services</b>	<b>237.2</b>	<b>244.2</b>	<b>237.0</b>	<b>(7.2)</b>
<b>Expenses associated with IFC's Treasury &amp; Portfolio activities</b>	<b>19.9</b>	<b>20.9</b>	<b>22.0</b>	<b>1.1</b>
<b>Expenses offset by fee income</b>	<b>116.7</b>	<b>148.9</b>	<b>164.3</b>	<b>15.4</b>
Client Fees (includes reimbursables and service fees)	71.8	80.7	87.7	7.0
Treasury / Syndications Programs Fees	4.0	14.2	18.7	4.5
Asset Management Company Fees & Reimbursables	31.1	39.7	44.9	5.2
Donor Trust Funded Investments (DTFI) Fees	9.8	14.3	13.0	(1.3)
<b>Special Initiatives</b>	<b>7.9</b>	<b>12.9</b>	<b>13.2</b>	<b>0.3</b>
<b>Jeopardy Expenses</b>	<b>5.0</b>	<b>12.0</b>	<b>12.0</b>	<b>-</b>
<b>Carry-forward of Unspent Budget from Previous Fiscal Year</b>		<b>46.6</b>	<b>47.6</b>	<b>1.0</b>
<b>IFC's Total Resources (including Carry-forward)</b>	<b>1,369.1</b>	<b>1,521.8</b>	<b>1,552.3</b>	<b>30.4</b>
<b>IFC's Total Resources (excluding Carry-forward)</b>	<b>1,369.1</b>	<b>1,475.2</b>	<b>1,504.7</b>	<b>29.5</b>
<i>o/w</i>				
<b>Investment, Treasury &amp; Support Services</b>	<b>978.1</b>	<b>1,084.3</b>	<b>1,124.7</b>	<b>40.4</b>
<b>Advisory Services</b>	<b>391.0</b>	<b>390.9</b>	<b>380.0</b>	<b>(10.9)</b>

Note: Totals may not add due to rounding.

6.2 Total Resources for FY16 are proposed to increase by \$29.5 million or 2.0% over FY15. The increase by source of funds for FY16 is shown in Table 11. Annual increases from FY11 through FY18 Indicative are shown in Chart 18 for reference. IFC is seeking Board approval for the FY16 increase of \$23.6 million to the Total Administrative Budget in Section VII. The rest of the increase represents expanded use of fees offset by reductions in IFC's Advisory Services business – both from IFC's own Contributions as well as Donor and Client contributions – along with small changes to expenses associated with Treasury and Portfolio activities.

**Chart 18. Nominal Increases to IFC's Total Resources & Administrative Budget, FY11 Budget to FY18 Indicative**



6.3 **Incremental** changes in sources of funds, however, only tells part of IFC's resource story. A functional view of the increase gives a better view of how the budget will support different functions within IFC. As shown below, the proposed increase funds Investment, Treasury, and Support functions, while Advisory Services will see a reduction in available resources. Spending for AS leveled off in FY15 to consolidate reforms and facilitate transition to the new organizational structure. Total AS spending is expected to resume a moderate 2.5% growth in FY16-18. AS program spend is expected to grow more rapidly, nearly 4% over the same period, as a result of new efficiencies from reforms.

**Table 12. FY16 Increase in Total Resources (\$, millions)**

<b>Investment, Treasury &amp; Support</b>	<b>40.4</b>
Inflation	21.7
Administrative expenses (net of inflation)	5.8
Treasury & portfolio activities (net of inflation)	0.7
Client fees (net of inflation)	5.3
Treasury/Syndications Program (net of inflation)	4.3
Asset Management Company (net of inflation)	4.4
Donor Trust Funded Investments fees (net of inflation)	(1.6)
Special Initiatives & Jeopardy (net of inflation)	(0.2)
<b>Advisory Services</b>	<b>(10.9)</b>
Inflation	7.8
IFC Contribution to AS (incl. admin exp.) (net of inflation)	(6.6)
Donor/Client Contribution (net of inflation)	(12.1)
<b>Total Increase</b>	<b>29.5</b>

6.4 Table 13 below provides another view of Total Resources broken down by functional unit. This table illustrates that incremental funding is being deployed to Operations and Enabling Services (net of a decrease for Advisory Services) rather than IG&A or Overheads, with a slight decline in the share consumed by Overheads. Even with the decrease in spending on AS in absolute terms, it will still comprise 29% of IFC's total resources in FY16 compared with 30% in FY15, a relatively insignificant change. It is also important to note that Advisory Services has established and maintains a significant global footprint, with over 650 projects in more than 100 countries, with a strong focus in IDA, FCS and climate change. This business line has achieved continuous improvement in development results (AS Development Effectiveness ratings climbed from 62% in FY10 to 76% in FY14) and consistently strong client satisfaction (91% in FY14).

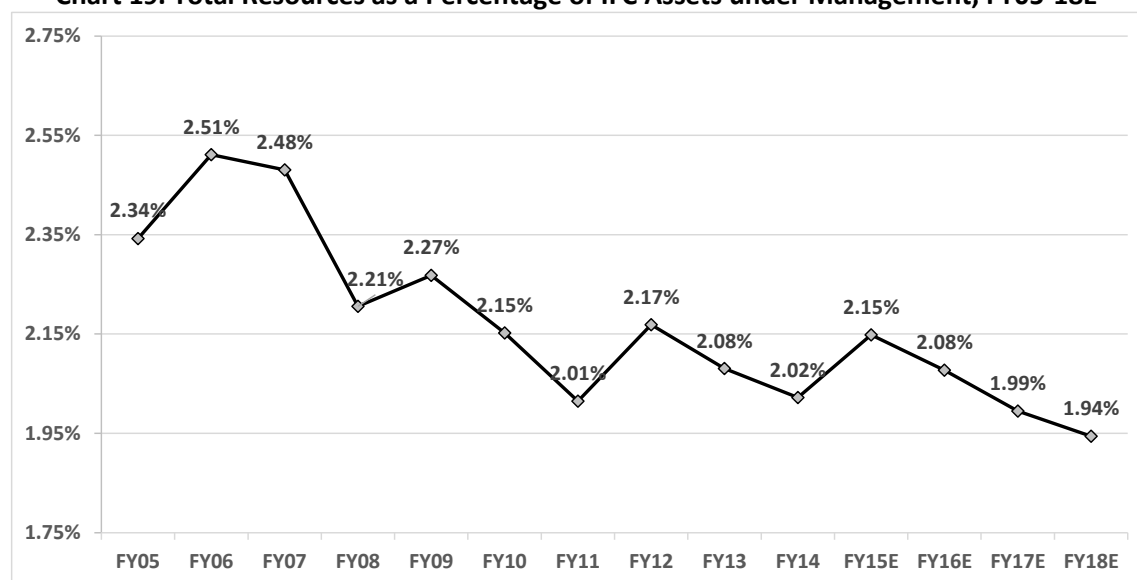
**Table 13. FY16 Funding Envelopes (% of All Units Funding)**

Budget Envelope	FY15		FY16	
% share of All Units Budget Allocation	Administrative Budget	Total Resources	Administrative Budget	Total Resources
Investment Operations	43.6%	35.5%	43.3%	36.9%
Advisory Services	8.1%	30.2%	8.1%	29.0%
<b>Sub-total Operations</b>	<b>51.7%</b>	<b>65.7%</b>	<b>51.3%</b>	<b>65.9%</b>
Treasury/Syndications	2.3%	4.4%	2.4%	4.8%
Corporate Sustainability & Risk	12.9%	8.7%	14.4%	8.9%
<b>Sub-total Operations/Enabling</b>	<b>66.9%</b>	<b>78.8%</b>	<b>68.1%</b>	<b>79.5%</b>
Institutional, Governance and Administration	7.9%	6.2%	8.0%	6.2%
Corporate Overheads*	25.2%	15.0%	24.0%	14.3%
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

\* excluding Pensions and Variable Pay

**6.5 Effective usage of total resources.** Total spending as a percentage of assets under management has steadily decreased over the last several years and is expected to continue this trend as the investment portfolio grows while total resources do not grow at the same pace. IFC has traditionally shown Regular Administrative Budget as a percentage of IFC own account committed portfolio, but IFC is adapting this efficiency measure to reflect the WBG evolution toward budgeting for total resources, including total administrative budget, non-IFC sources of funding for AS, expenses covered by fee revenue, etc. It is also now incorporating AMC mobilization and syndications mobilization along with IFC own account committed portfolio in the measure of assets under management.

**Chart 19. Total Resources as a Percentage of IFC Assets under Management, FY05-18E<sup>8</sup>**



<sup>8</sup> Assets under management includes IFC own account committed portfolio plus AMC mobilization plus Syndications mobilization

6.6 Total expenses as a percentage of IFC own account committed portfolio declined by 12% from 2.98% in FY05 to 2.65% in FY14. The rise in the FY15 estimated ratio results from the substantial decline in committed portfolio largely due to currency fluctuations (and project reflows such as cancellations and prepayments driven by the same fluctuations) rather than a fundamental change in total resources used. The ratio is expected to decline from the FY15 estimate over the next three years, given IFC's projected portfolio growth in FY15-18 and IFC Management's commitment to low nominal total resource utilization over this horizon. IFC Management is comfortable with a medium-term ratio around current levels given the increasing complexity of its investment portfolio and the portfolio management resources that this will require as well. Going forward, IFC will continue to explore the most effective ways of integrating its total business activities into its metrics (e.g., Advisory Services assets under management), resulting in a more holistic view that better captures the drivers of IFC's efficiency.

6.7 Total resources by cost category shows a slight increase in the ratio of fixed to variable expenses. This is driven by increased staff costs, both for salaries and benefits (including variable pay and pensions). The increase for salary reflects a modest increase in headcount, after a significant reduction in FY15, and expected salary increases.

**Table 14. Total Resources by Cost Category, FY14 Actual to FY16 Budget (\$, millions)**

Total Resources	FY14 Actual		FY15 Restated Budget		FY16 Budget	
	\$ m	%	\$ m	%	\$ m	%
<b>Fixed Expenses</b>	914.5	66.8%	994.8	67.4%	1030.0	68.5%
<i>of which</i>						
Staff Salaries and Benefits (including contributions to SRP, SSRP, RSBP)	772.8	56.4%	839.0	56.9%	869.8	57.8%
o/w Salaries	418.6	30.6%	462.0	31.3%	472.0	31.4%
o/w Benefits (including pension & variable pay)	354.2	25.9%	377.0	25.6%	397.8	26.4%
Communications and IT	34.2	2.5%	41.0	2.8%	41.4	2.7%
Depreciation	48.9	3.6%	52.8	3.6%	54.9	3.6%
Equipment and Building	58.6	4.3%	62.0	4.2%	63.9	4.2%
<b>Variable Expenses</b>	454.6	33.2%	480.4	32.6%	474.7	31.5%
<i>of which</i>						
ST Consultants and Temporaries	124.9	9.1%	123.0	8.3%	123.4	8.2%
ET Consultants and Temporaries	0.0	0.0%	0.0	0.0%	0.0	0.0%
Travel Costs	118.0	8.6%	114.0	7.7%	109.9	7.3%
Contractual Services	87.3	6.4%	88.0	6.0%	88.4	5.9%
Services and Support Fees	97.3	7.1%	126.4	8.6%	124.0	8.2%
Other Expenses	27.2	2.0%	29.0	2.0%	29.0	1.9%
<b>Total Resources Expenses</b>	1369.1	100.0%	1475.2	100.0%	1504.7	100.0%

## B. TOTAL ADMINISTRATIVE BUDGET

6.8 While IFC requires all \$1.5 billion of its Total Resources to deliver its business, the Total Administrative Budget is formally approved by the Board per Section VII of this paper. IFC proposes a FY16 Total Administrative Budget of \$976.2 million, a \$23.6 million or 2.5% nominal increase over FY15.



6.9 **Proposed Budget Increase.** For FY16, IFC proposes a 2.5% nominal increase (+\$23.6 million) in the Total Administrative Budget. Since inflation adjustments will absorb \$19.1million of the increase, IFC Management sought savings and efficiencies from the expenditure review, shared services and other sources that could be released for redeployment. This process identified an additional \$20.0 million that could be reinvested towards strategic priorities (of which \$16.2 million representing the portion of the FY16 estimated ER savings impacting the administrative budget). To best support the corporate strategy and maximize impact for clients, IFC Management decided to fund three key areas through reallocation within the FY16 envelope: (i) Variable pay; (ii) Strategic Staffing; and (iii) Strategic priorities.

**Table 15. Total Administrative Budget, FY16 vs. FY15 (\$, millions)**

<b>Total Administrative Budget FY15</b>	<b>952.6</b>
Inflation	19.1
Expenditure Review Savings (Admin)	(16.2)
Incremental Savings from Shared Services and Other	(3.8)
Variable Pay top-up	8.5
Strategic Staffing	11.0
Strategic Priorities	5.0
<b>Variance FY16 vs. FY15</b>	<b>23.6</b>
<b>Total Administrative Budget FY16</b>	<b>976.2</b>

6.10 **Variable Pay.** IFC's variable pay programs have been an important component of IFC's employment value proposition and help drive behaviors in furtherance of corporate goals. Building on the success of existing programs, Management proposes to augment variable pay programs in FY16 with an additional \$8.5 million (see paragraph 5.42). In addition to these increased resources, their eligibility criteria have been refined to further strengthen staff incentives and focus on investment results. IFC will consider paying out awards based on the corporation reaching its FY16 target for allocable income.<sup>9</sup> Once this corporate hurdle is met, further eligibility will take into account the portfolio risk adjusted return on capital/internal rate of return outcomes for those departments which have met development scorecard targets in at least two of the past three years. This approach will replace the previous long-term performance awards program, which had become ineffective given its growing complexity to administer and focus more on individual/project specific rather than collective successes within the organization. Variable pay will be allocated between scorecard/performance awards and Corporate Awards which are

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<sup>9</sup> The FY16 allocable income target is as yet undetermined; it will be used only toward the incremental variable pay component for FY16.

specifically linked to strategic priorities. Within this set, new award categories are being introduced to reflect management, client coverage, and decision making achievements.

**6.11 Strategic Staffing.** IFC strives to optimize its delivery capacity by efficiently deploying staff. Towards this end, IFC introduced global functional talent pools under a single Global Client Services Vice Presidential Unit, which allows the organization to tap into global expertise to add value to clients. This model is predicated on having the right set of specialist skills in the right functions. To help achieve the right skills mix, \$11 million of reallocated resources will be provided to hire new specialists across operations and in key support functions. New hires are expected to result in a slight increase of the organization's headcount through FY16. Almost 40% of the allocation will be dedicated for hiring into the global functional talent pools working on portfolio, advisory, and new business development. The remaining funds will be similarly allocated for other support and analytic roles which address strategic staffing needs.

**6.12 Strategic Priorities.** There are numerous strategic programs which do not involve the recruitment of additional staff but nonetheless benefit from further investment in staff. These include support for the new WBG global mobility framework; measures to encourage and support FCS operations; and enhanced environment and social sustainability support. \$5 million will be allocated to strengthen these key areas of focus.

**6.13** Similar to the Total Resource picture, Table 16 shows a slight shift from variable to fixed costs within the Total Administrative Budget.

**Table 16. Total Administrative Budget by Cost Category (\$, millions)**

Administrative Budget	FY14 Actual		FY15 Restated Budget		FY16 Budget	
	\$ m	%	\$ m	%	\$ m	%
<b>Fixed Expenses</b>	700.1	78.2%	734.9	77.1%	758.6	77.7%
<i>of which</i>						
Staff Salaries and Benefits (including contributions to SRP, SSRP, RSBP)	588.8	65.8%	625.9	65.7%	641.2	65.7%
o/w Salaries	277.9	31.1%	299.6	31.5%	299.6	30.7%
o/w Benefits (including pension & variable pay)	310.9	34.8%	326.3	34.2%	341.6	35.0%
Communications and IT	24.0	2.7%	20.6	2.2%	22.0	2.3%
Depreciation	48.6	5.4%	49.6	5.2%	53.5	5.5%
Equipment and Building	38.6	4.3%	38.8	4.1%	41.9	4.3%
<b>Variable Expenses</b>	194.7	21.8%	217.7	22.9%	217.6	22.3%
<i>of which</i>						
ST Consultants and Temporaries	17.5	2.0%	19.7	2.1%	21.0	2.1%
ET Consultants and Temporaries	0.0	0.0%	0.0	0.0%	0.0	0.0%
Travel Costs	33.8	3.8%	28.2	3.0%	26.5	2.7%
Contractual Services	39.3	4.4%	36.8	3.9%	39.0	4.0%
Services and Support Fees	95.5	10.7%	124.0	13.0%	122.0	12.5%
Other Expenses	8.7	1.0%	9.0	0.9%	9.1	0.9%
<b>Total Administrative Expenses</b>	894.7	100.0%	952.6	100.0%	976.2	100.0%

## C. ADVISORY SERVICES

6.14 **Advisory Services.** It is proposed that IFC contribute \$143 million to AS Spend in FY16, or 37% of total expenditure. The bulk of IFC's contribution in FY16 will be equally divided between FMTAAS (\$63 million) and IFC's Administrative Budget (\$63 million). The remaining \$17 million of IFC's contribution would be sourced from Trust Fund Administrative Fees and part of the Performance Based Grants Initiative used to support AS projects. Donor and client contributions to AS spend are expected to slowly increase from FY16E-18E (see Table 17).

**Table 17. Advisory Services by Funding Source, FY13-18E**

	FY13		FY14		FY15E		FY16E		FY17E		FY18E	
	\$mn	%	\$mn	%	\$mn	%	\$mn	%	\$mn	%	\$mn	%
<b>Donors and Clients</b>	<b>231</b>	<b>59</b>	<b>239</b>	<b>61</b>	<b>235</b>	<b>63</b>	<b>237</b>	<b>63</b>	<b>249</b>	<b>64</b>	<b>259</b>	<b>65</b>
<b>IFC All Sources</b>	<b>161</b>	<b>41</b>	<b>152</b>	<b>39</b>	<b>135</b>	<b>37</b>	<b>143</b>	<b>37</b>	<b>141</b>	<b>36</b>	<b>141</b>	<b>35</b>
FMTAAS	100	26	68	18	55	15	63	16	63	16	63	16
Admin Budget	39	10	63	16	63	17	63	16	63	16	63	16
Other IFC Sources**	22	5	21	5	17	5	17	4	15	4	15	4
<b>Total</b>	<b>392</b>	<b>100</b>	<b>391</b>	<b>100</b>	<b>370</b>	<b>100</b>	<b>380</b>	<b>100</b>	<b>390</b>	<b>100</b>	<b>400</b>	<b>100</b>

\*\*Comprises Trust Fund Administration Fees and some legacy sources tied to specific time-bound initiatives (SME Ventures, Performance Based Grants Initiative).

6.15 IFC Management proposes to set annual spending authority from FMTAAS at \$63 million. Absent further designation of IFC allocable income to FMTAAS, this would reduce the FMTAAS fund balance to \$71 million (see Table 18) by end FY16. The practice has been to designate enough earnings to FMTAAS in order to provide three years of cushion. Management will make a recommendation to the Board on future designations to FMTAAS in the FY15 Net Income Paper.

**Table 18. FMTAAS Designations vs. Annual Spending Authority, FY05-18E (\$, millions)**

	FY05-12	FY13	FY14	FY15E	FY16E	FY17E	FY18E
FMTAAS Designation from FY Earnings	929	80	58	tbc	tbc	tbc	tbc
Re-designation from Performance Based Grants Initiative to FMTAAS	5						
FMTAAS Spend	(715)	(100)	(68)	(55)	(63)	(63)	(63)
Resulting FMTAAS Cushion (Year-end)*	219	199	189	134	71	8	(55)

\*FMTAAS Cushion from FY15 onward without additional designation of Net Income to FMTAAS.

## D. OTHER SOURCES OF FUNDS

6.16 In addition to Total Administrative Budget and Advisory Services, Table 11 shows that IFC's Total Resources comprises numerous sources of funds. These are described in the following paragraphs.

6.17 **Expenses Associated with IFC's Treasury and Portfolio Activities.** IFC incurs expenses directly associated with its market borrowings such as outside legal counsel fees, auditor fees, prospectus printing

costs, and rating agency fees, as well as custody and settlement fees paid to the custodians of IFC's equity and liquid asset portfolio, State Street Bank, Citibank, and external managers. In addition, IFC incurs some minor out-of-pocket costs in relation to business development of its structured and securitized products. Equity transaction costs are not reimbursed by clients due to market practices.

**6.18 Use of Fees.** IFC has a long established practice of using fees from clients to directly cover out-of-pocket expenses incurred for the client's project such as travel, consultants, and outside legal counsel. Similarly, clients pay service fees, privatization fees and mobilization fees for related work associated with their investment projects. IFC generally matches each expense with its fee source before the expense is incurred in order to assess appropriate funding levels and guide spending decisions at the institutional level, as underlined by a recent Internal Audit report. IFC carefully ensures that fee budgets for the upcoming year do not exceed likely fee collections. Up to 40% of service fees can be used for staff costs to provide flexibility to the investment departments. As the remaining fees are used to cover variable costs such as travel, consultants, and outside legal counsel, IFC can expand or contract its activities using fees without changing its permanent cost base. Expenses offset by fee income also include fees from treasury programs, fee from the MCPP program, or fees and reimbursables from the AMC. IFC plans to increase its use of fees to offset expenses by \$15.4 million (10.3%) in FY16 from clients, treasury/syndication and AMC fees/reimbursables.

**6.19 Special Initiatives.** IFC InfraVentures was established in FY08 (IFC/R2007-0275) and renewed in FY13(IFC/R2013-0213/1) to help increase the number of private and public private partnership infrastructure projects in IDA countries and selectively in middle income countries and thereby increase the supply of scarce infrastructure resources to citizens and companies in these countries. Key changes to IFC InfraVentures have been introduced as part of the Board approval of FY13: (i) an increase in the fund's size to \$150 million; (ii) an expansion of the geographic scope to invest selectively into Middle Income Countries, not to exceed 25%; and, (iii) an increase of the maximum exposure to \$8 million per individual project.

**6.20** Through March 2015, IFC InfraVentures has committed to invest a total of \$ 90.4 million in the early-stage development of 36 projects, mostly in IDA countries. Of these projects, 23 projects are still active and, once fully developed, may result in total mobilization of debt and equity in excess of \$7 billion. Amongst others, IFC InfraVentures is contributing or has contributed to the development of:

- i. Three major hydro projects in Nepal with a combined capacity in excess of 1700 MW which will contribute to alleviate the acute shortage of power in the country and create export revenues from power exported to India and possibly Bangladesh;
- ii. A 420 MW hydro project in Cameroon which will add significant generation capacity to the system at a competitive price;
- iii. A 40 MW hydro project and a 33 MW solar project in Mali which will help add much needed renewable power to the country's fossil-fuel dominated electricity system; and,
- iv. A 181 MW hydro power project in Georgia, which achieved financial close in May 2014 with InfraVentures support and will sell electricity domestically in Georgia in winter and export to Turkey in the remainder of the year.

**6.21** IFC InfraVentures is expecting to fully utilize \$5.0m budget allocated in FY15. A nominal increase of 5% is being requested to support InfraVentures' work which has picked up quite strongly this year with a larger pool of projects under development. Board approval is being sought for FY16 budget of \$5.25million for InfraVentures, an increase of \$0.25 million.

6.22 **Jeopardy Expenses.** IFC designates a project as a jeopardy case when the prospects for recovery of IFC's investment are in serious doubt due to expected loan defaults, country/industry considerations, stock market factors, or other factors as determined by the Management Team. The restructuring or recovery of such jeopardy cases often generates significant out-of-pocket expenses (e.g., travel, consultants, auditors, and legal fees). To facilitate the tracking and reporting (and often the reimbursement) of these extraordinary jeopardy expenses, IFC sets up a separate expense account for each jeopardy case. The Board has traditionally recognized jeopardy expenses as being off-budget as in the majority of jeopardy cases, IFC's ultimate recovery on its investments amounts to many times the expenses spent in the recovery process. The proposed ceiling for FY16 is a stable \$12 million, net of recoveries, which should allow sufficient flexibility in the event of stress on IFC's portfolio.

6.23 **Carry-forward.** IFC's current carry-forward mechanism dates to FY99 when the Board approved IFC's adoption of the Bank's 5% carry-forward policy in place at the time. IFC's carry-forward is recalculated each year based on prior-year spending against administrative budget. The carry-forward does not accumulate year-on-year or add to the base administrative budget. Since adoption of the carry-forward mechanism in FY99, IFC has only used it twice: once in FY01 for \$3.5 million during the Argentina crisis and again in FY06 for only \$0.5 million. Thus, IFC prefers to consider this to be a 5% contingency mechanism rather than a true carry-forward.

6.24 IFC's Management Team feels that the 5% contingency mechanism remains the optimal policy even as IFC's budget growth has slowed in the last few years. IFC is committed to only use the contingency in extraordinary circumstances. This practice ensures that IFC's permanent cost base is not increased for temporary needs. IFC Management would inform the Board before using any portion of its 5% contingency to fund special needs such as temporary crisis response activities.

## E. CAPITAL BUDGET

6.25 IFC's capital budget funds Headquarters and Country Office facility needs as well as the investment in Information Technology necessary to support its unique business model. For FY16, the total recommended capital budget is \$140.0 million. This represents an increase of \$56.5 million compared to FY15, with the main drivers of FY16 supporting the evolving World Bank Group real estate strategy.

**Table 19. Capital Budget, FY14-16 (\$, millions)**

	<b>FY14 Budget</b>	<b>FY15 Budget</b>	<b>FY16 Budget</b>
Headquarters Facilities	3.5	7.6	38.5
Country Office Facilities	24.0	21.5	56.5
Information Technology	54.9	53.4	45.0
Contingency	1.5	1.0	-
<b>Total</b>	<b>83.8</b>	<b>83.5</b>	<b>140.0</b>

6.26 **Headquarters Facilities.** The HQ facilities portion of the capital budget is used to fund required building improvements and other work at the F-building. The scope of work planned for FY16 will consist of Restroom Improvements/Renovations throughout the building; Auditorium Improvements including

audio, visual and sound upgrades; Fitness Center Upgrades; F Building Cafeteria – Back of Kitchen/Servery/Catering equipment replacement.

6.27 The HQ Facilities Capital Budget also includes \$33 million in support of the World Bank Group real estate strategy in Washington.

6.28 **Country Office Facilities.** The Country Office facilities budget proposal reflects two major trends: (i) IFC's ongoing decentralization and growth in the field with emphasis on cost efficiency; and (ii) supporting the WBG savings requirements identified as part of the institutional expenditure review, which identifies specific savings from moving towards ownership of larger offices rather than leasing where it can significantly reduce annual administrative expenses.

6.29 IFC's strategic approach to Country Office real estate purchasing has also changed. Where purchasing real estate has been determined by the IFC Management Team as the appropriate course, the focus has shifted to identifying "strata-title" or individual floor ownership arrangements in quality building locations instead of acquiring land and constructing "ground-up" with their inherently higher operating costs.

6.30 By the end of FY15, IFC will have 104 offices in 98 countries supporting over 3,000 individuals in the field. IFC and the World Bank are co-locating country offices when feasible and business needs are supported. Currently, 77 of the 104 offices are co-located. Three to four more offices are expected to co-locate in the next several years. In FY16, no changes are expected in the quantity of IFC country offices.

Options to increase efficiency of field office presence continue to be evaluated in collaboration with the Regional management teams.

6.31 Additionally, IFC Management, consistent with IBRD, is also pursuing other opportunities for savings. Once full reviews and cost benefit analyses are completed and the IFC Management Team approves any actions, more specific information related to capital requirements and administrative budget savings will be provided to the Budget Committee and the Board.

6.32 **Information Technology.** The FY16 Information Technology capital budget proposal of \$45.0 million will fund two categories of investment:

- i) Steady State (\$20.8 million). This category focuses on the established IT needs of the Corporation. These programs ensure the reliability of existing systems by addressing technical obsolescence and facilitating IT capacity growth necessary to accommodate IFC's growth. The FY16 capital budget request includes: enhancements of existing applications with minor business functionalities to keep pace with business needs; replacement of PCs that have reached end of warranty; and improvements to data storage, disaster recovery infrastructure, database platforms, information security infrastructure, telecommunications, and networks for both normal operations and business continuity.
- ii) Systems Development (\$24.2 million). These programs focus on the development of new or enhanced IT solutions to support IFC's lines of business. They include automation of business process changes, as well as the introduction of new business applications along with the modification of existing

applications. Some are new multi-year programs, while others are continuation or completion of programs begun in prior years.

6.33 IFC will also benefit from a number of new WBG-wide IT projects. IFC does not contribute to capital to these initiatives but instead pays for services with SSAs through the administrative Budget once the service or solution is in place.

## **VII. RECOMMENDATIONS**

7.1 IFC Management recommends that the Board resolve to approve the following:

### **A. ADMINISTRATIVE BUDGET AUTHORITY**

- i) A total (nominal) administrative budget for FY16 of \$976.2 million.

### **B. CAPITAL BUDGET AUTHORITY**

- ii) A capital budget for FY16 of \$140.0 million.

### **C. SPECIAL INITIATIVES**

- iii) Authority to spend an additional \$5.25 million for IFC InfraVentures through FY16.