

Aligning Resources for Impact: IFC FY15 Budget

Approved by IFC's Board of Directors on June 24, 2014

Released in accordance with IFC's Access to Information Policy

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Glossary

AS	-	Advisory Services
AMC	-	Asset Management Company
CAGR	-	Compound Annual Growth Rate
CBD	-	Central Business District
CCSA	-	Cross-Cutting Solutions Area
CO	-	Country Office
CPF	-	Country Partnership Framework
DSC	-	Deployable Strategic Capital
ECR	-	External and Corporate Relations
ESG	-	Environment, Social and Governance
FCS	-	Fragile and Conflict Situations
FMTAAS	-	Funding Mechanism for Technical Assistance and Advisory Services
FY	-	Fiscal Year
GSD	-	General Services Department
HQ	-	Headquarters
HR	-	Human Resources
IBRD	-	International Bank for Reconstruction and Development
IDA	-	International Development Association
IEG	-	Independent Evaluation Group
IFC	-	International Finance Corporation
IFI	-	International Financial Institution
INR	-	Infrastructure and Natural Resources Industry Group
IS	-	Investment Services
IT	-	Information Technology
LAM	-	Liquid Asset Management
LTF	-	Long-Term Finance
MIGA	-	Multilateral Investment Guarantee Agency
P&L	-	Profit & Loss Statement
PBGI	-	Performance Based Grants Initiative
PPP	-	Public Private Partnership
RAB	-	Regular Administrative Budget
RAROC	-	Risk Adjusted Return on Capital
SCD	-	Systematic Country Diagnostics
SME	-	Small and Medium Enterprise
SSA	-	Shared Services Agreement
STF	-	Short-Term Finance
TAB	-	Total Administrative Budget
VPU	-	Vice Presidential Unit
WBG	-	World Bank Group

Executive Summary

- i) The International Finance Corporation's Fiscal Year 2015 Budget paper sets forth the indicative operational growth and sustainable delivery model for FY15 and seeks Board authorization for the budget required to achieve its contribution to the World Bank Group twin goals. The proposed budget will enable IFC to continue delivering strong development results while reinforcing its financial sustainability by maintaining total resource consumption at a flat real level (0.9% nominal increase).
- ii) An overview of the current financial landscape comprises **Section I** of the report. IFC's diversified operations have provided strong financial returns along with development impact, and these returns have supported the business's growth over several years. Buoyed by this strong foundation, IFC has developed a blue print for improving its operations to serve its clients even better, balancing increasing volume with the ultimate impact on eradicating poverty and boosting shared prosperity.
- iii) **Section II** outlines this plan for client-centered productivity, efficiency and effectiveness, of which "A Refocused IFC" plays a strong part. IFC will continue delivering its world-class investment, advisory and treasury operations while redesigning its structure and processes to engage more extensively with the other institutions in the WBG and to offer deeper partnerships and faster service to its private sector clients.
- iv) The substance of IFC's planned delivery stems from its participation in creating the WBG strategy and was highlighted in the *IFC Road Map FY15-17 and Addendum*. While IFC is undertaking a re-alignment and shifting toward a more transformational, programmatic approach and continually offering innovative products, its fundamental business will not change. At the same time, IFC's important role in the new Systematic Country Diagnostics, Country Partnership Frameworks and Joint Implementation Plans means that IFC will need to maintain flexibility and adapt to emerging strategic priorities on the ground. IFC will also actively participate in the WBG-wide expenditure review; IFC Management currently intends to reinvest all gross savings achieved in FY15 toward its business.
- v) Accordingly, **Section III** identifies the initially intended areas for IFC resource reallocation while acknowledging that, particularly in FY15 as a transition year, it is not possible to determine precise activities, deliverables and resource consumption *ex ante*. The activities preliminarily classified for increased resource intensity include improving environmental and social sustainability risk management, leveraging Information Technology to best support IFC's operations, implementing a new client focused delivery model supporting productivity gains, aligning staff incentives with strategic priorities, and enabling further revenue growth through treasury and capital markets innovation. These priorities will continue to reflect real-time feedback from the IFC Regional and Group Business Reviews, and will be informed by country, industry and corporate strategy discussions.
- vi) **Section IV** builds on the current landscape with planned operational improvements and strategic resource shifts to extrapolate the results on IFC's financial sustainability. This leads to **Section V**, the total administrative budget for Board approval. Even in the midst of a transition year with many multi-faceted changes underway, IFC Management commits to delivering enhanced results with consistent total resources.

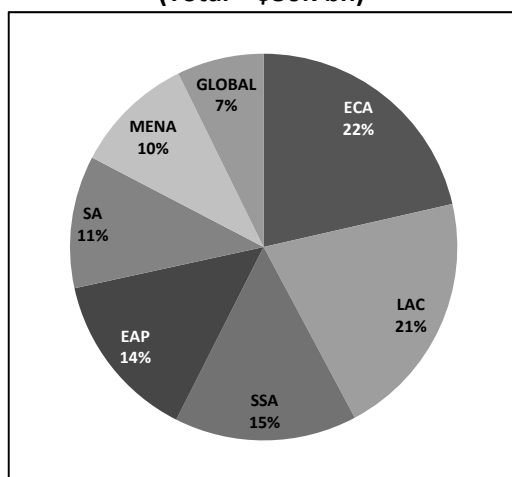
I. Current Financial Landscape

A. INVESTMENT PORTFOLIO OVERVIEW

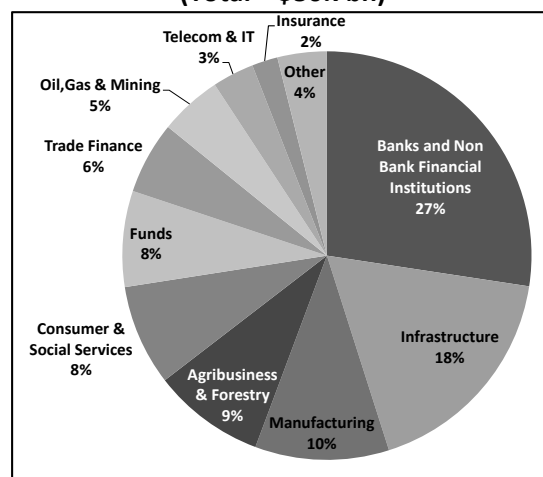
1.1 **Size.** IFC's committed investment portfolio stands at \$50.7 billion as of Fiscal Year 2014 Quarter 3-end, of which 64% in loans, 26% in equity, and 10% in guarantees and risk management products, corresponding to \$15.3 billion in total economic capital. This has been fed by a growing volume of long-term finance new commitments over the past several years, from \$8.2 billion in FY09 to \$11.0 billion in FY13 (and \$6.6 billion as of FY14 Q3). While volume is an ingredient of delivering development impact and ensuring IFC's financial sustainability via investment, it is not IFC's ambition in and of itself but rather one of several means that IFC employs toward achieving the WBG goals of eradicating extreme poverty and boosting shared prosperity. Accordingly, metrics and incentives are shifting from a volume-driven model to an aggregated approach entailing all drivers of financial sustainability and impact.

1.2 **Composition.** Historically, the geographic, industry, and product diversity of IFC's portfolio has supported its reliable performance over the long term. This diversity is reflected in the current committed portfolio as of FY14 Q3-end.

**Chart 1. IFC Portfolio by Region, FY14 Q3-end
(Total = \$50.7bn)**



**Chart 2. IFC Portfolio by Industry, FY14 Q3-end
(Total = \$50.7bn)**



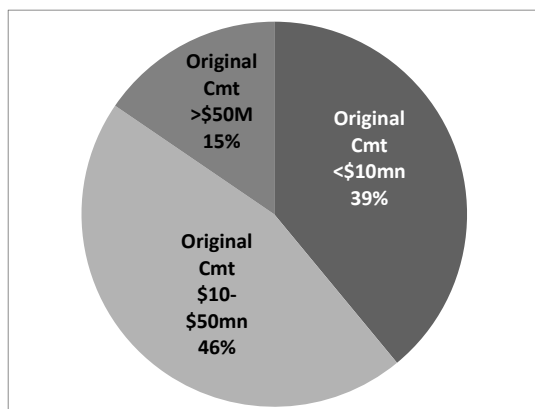
1.3 IFC's diverse portfolio reflects its strategic priorities and also contributes to its financial sustainability. IFC's Infrastructure and Natural Resources industry group provides one example of these benefits.

Box 1. Highlight on IFC's Infrastructure and Natural Resources Industry Group

Infrastructure is both a key strategic priority for IFC (and the entire WBG) and a major contributor to its financial sustainability via both realized equity income and net loan and fee revenue, which has been increasing over time. Most importantly, INR's investments have delivered strong results for IFC's clients, with above-average development effectiveness ratings. IFC's shift toward transformational projects and programs is supported by INR comprising roughly three-quarters of its first tranche of identified transformational engagements. INR expects to maintain its historical track record of contributing to IFC's financial sustainability over the medium to long term. This will include a focused approach on sourcing new quality equity investments and proactively managing existing assets.

1.4 While the average project size of IFC's new commitments has increased from \$24 million in FY09 to \$30 million in FY13, IFC also continues to work with a variety of clients, large and small. In the current committed portfolio, only 15% of projects had an original commitment larger than \$50 million; 39% were smaller than \$10 million. This approach both helps IFC to balance its risk and return and to serve a broader client base for maximum impact. The resource requirements of projects, regardless of size, consider their risk and complexities and differentiate accordingly.

Chart 3. IFC Portfolio by Size of Original Commitment, FY14 Q3-end (# of Projects)



1.5 **Portfolio Quality.** Though IFC's portfolio has held up against recent financial crises and market movements, the nature of its business and underlying financial instruments requires very strong proactive monitoring to ensure its clients are kept in good financial standing throughout. Movements in credit risk ratings of its loan and equities reflect the pace at which financial shocks impact each differently, with changes to equities seen sooner than loans which are distressed at a slower pace. At FY14 Q3-end, average credit risk ratings on its loan and equity portfolios were in line with recent years' trends, with movements generally driven by few large exposures within the fiscal year. Similarly, non-performing loans at FY14 Q3-end showed an increase as a percentage of outstanding portfolio to 5.8%, driven by a single exposure during the quarter. With uncertainties in the economic and market outlook, the re-positioning of its resources to oversee IFC's clients throughout their lifecycle, and particularly during supervision, is critical.

1.6 IFC's investments produce and consume much of IFC's funds, but AS and Treasury operations also play a significant role. Please see further details on sources and uses of funds below.

B. OVERALL SOURCES AND USES OF FUNDS

1.7 **Revenues (Sources of Funds).** Broadly, IFC has four main revenue streams: Investment Services (loan and debt security income and equity income), Fund Management (fees), Liquid Asset Management, and Advisory Services.

1.8 IFC provides a range of financial products and services to its clients. Investment Services product lines include: loans, equity investments, trade finance, loan participations, structured finance, client risk management services, and blended finance. **Investment** revenues come from the returns and fees

associated with these products, such as (i) net interest income, various types of fees, and dividends, all of which are fairly stable and predictable; (ii) realized capital gains, which are more volatile and therefore fairly unpredictable; and (iii) unrealized gains and losses, which are most volatile and unpredictable. IFC's Asset Management Company, a wholly-owned subsidiary managing funds on behalf of third parties, contributes a relatively small but growing income stream to IFC.

1.9 **AMC** invests third-party capital, enabling outside investors to benefit from IFC's expertise in achieving strong equity returns, as well as positive development impact in the countries in which it invests. Investors in funds managed by AMC comprise, besides IFC, sovereign wealth funds, pension funds, multilateral and bilateral development institutions, national development agencies and international financial institutions. AMC helps IFC mobilize additional capital resources for investment in productive private enterprise in developing countries.

1.10 AMC's policy is to charge investors market rates for managing funds (management fees, cost recovery and performance fees). 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 net profit (limited during the investment period, more significant after 6-7 years as and when performance fees are generated by fund results. 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: transaction, supervision, fund development, and business development fees.

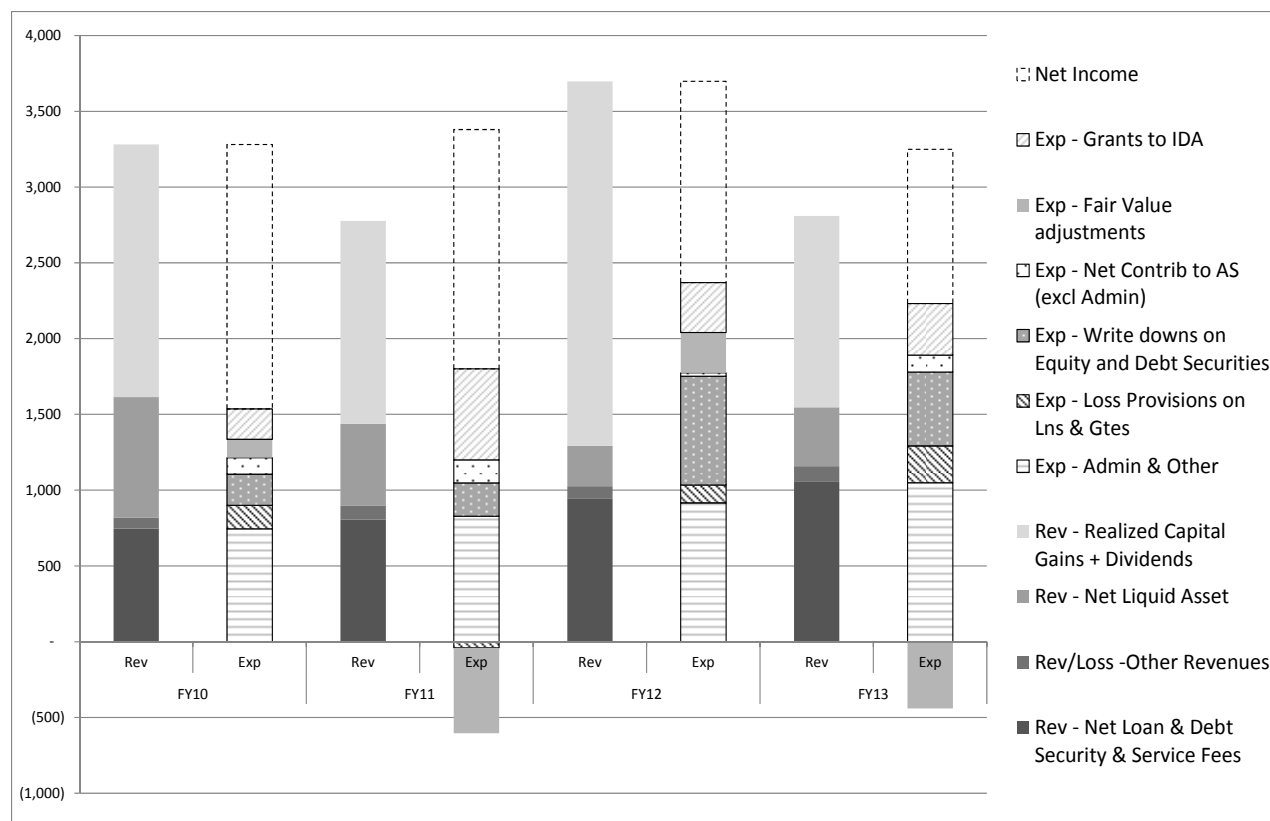
1.11 In addition, AMC-managed funds reimburse IFC for the funds' share of out-of-pocket expenses related to transaction costs, broken deal costs and supervision costs. Where IFC receives mandate fees from the investee company as part of a transaction, the pro rata portion of those fees is netted against expenses reimbursed and/or fees payable by AMC. In addition, AMC makes a regular payment to IFC 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 spending a majority of their time on AMC-related work. AMC's financial statements are fully consolidated into IFC's, so any net income that AMC makes flows through to IFC's Profit & Loss, after eliminating inter-company expenses.

1.12 **Advisory Services** revenues come from donor partnerships and client contributions as well as trust fund administration fees paid by donors. For more details on the funding model for AS, please see paragraph 4.24.

1.13 The objective of **Liquid Asset Management** in IFC's treasury operations is to achieve reasonable returns while maintaining risks to IFC within acceptable levels all the while ensuring that funding for IFC investments is available as needed. IFC's assets are invested in a full range of highly rated financial instruments such as asset-backed securities, US and other government or agency bonds, repos, deposits assets, and mortgage backed securities and derivatives. LAM revenue is dependent on market trends and is therefore relatively volatile.

1.14 **Expenses (Uses of Funds).** A sizeable portion of IFC's expenses, as presented in its income statement, come from basic operations via the administrative budget. Items such as loss provisions, write-downs, and fair value adjustments are also considered expenses; if there is a net release of provisions, reversal of write-downs or positive adjustment to fair value, these items would be considered a negative (or off-setting) expense, contributing positively to IFC's profit. The remaining constitutes IFC's net income for the year. IFC may designate certain amounts to IDA and/or FMTAAS.

Chart 4. IFC Revenue and Expense Categories, FY10-13 (\$mn)



1.15 All of IFC's revenues (and expenses) are equally important in (i) maintaining its financial sustainability and (ii) increasing its capital base to support growing service to and investment in clients. As Chart 4 illustrates, IFC expects its relatively stable loan, debt security and fee revenue (net of funding costs) to cover its administrative and other expenses. Equity revenue generally covers the IDA contributions as well as provides the residual income needed for a sustainable capital base and growth; when equity returns are low; this affects IFC's ability to make designations to IDA and/or FMTAAS.

1.16 For example, in **FY13**, IFC generated \$1,055 million of net loan, debt security and fee revenue that covered \$1,050 million of administrative and other expenses, while the \$389 million of net liquid asset revenue more than covered \$112 million of net IFC contributions to Advisory Services and even absorbed \$243 million of loan loss provisions. Finally, the \$1,193 million in realized capital gains and dividends from equity provided cover for the \$340 million grant to IDA and most of the \$1,018 million in residual profits. The latter added to IFC's capital base, keeping Deployable Strategic Capital strong and hence allowing for increased business volumes.

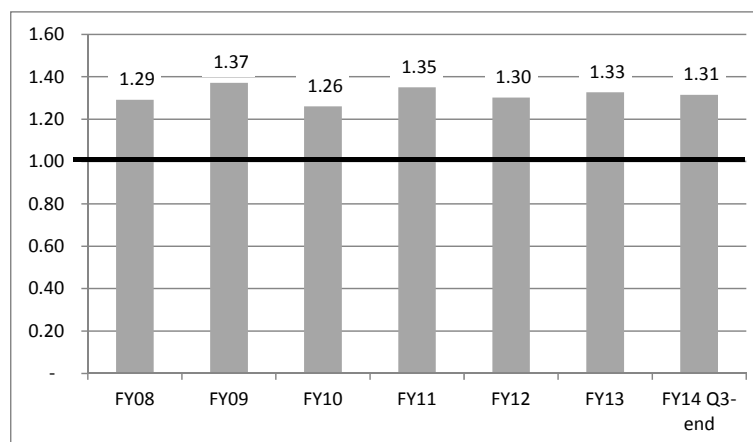
1.17 As Advisory Services aligns with IFC's investment work and becomes an integral part of joint Global Practices, some of these categories may shift, but the underlying structure of fairly stable loan and debt security revenue covering total expenses and more volatile equity revenue comprising the bulk of IFC's net income is expected to continue.

C. PROFITABILITY

1.18 IFC's overall financial sustainability depends on the long-term aggregation of net income as seen above. This net income contributes to IFC's retained earnings, funding operations, building the capital base for increasing investments, and helping maintain IFC's triple-A credit rating. IFC achieved an income before grants to IDA of \$1.35 billion in FY13 and is on track to meet the higher end of the \$0.7-1.3 billion range for FY14 that it projected in the FY14 Business Plan and Budget Paper.

1.19 IFC has several metrics, some used historically, some under evolution, to measure various aspects of its profitability. One investment profitability metric under continual usage is net loan and fee revenue coverage of expenses. Over the past several years, this ratio has hovered around 1.3, showing IFC Investment Operations' ability to cover its costs through its more stable revenue drivers with a healthy buffer.

Chart 5. Net Loan and Fee Revenue Coverage of Total Administrative Expenses Ratio, FY08-FY14 Q3-end



1.20 An overview of IFC's current metric methodology may be found in Section II, and historic trends along with forward-looking discussion may be found in Section IV.

II. Delivering More & Better for Our Clients: Blue Print for Client-centered Productivity, Efficiency & Effectiveness

A. CONTEXT: CLIENT CENTRICITY AND WBG ENGAGEMENT

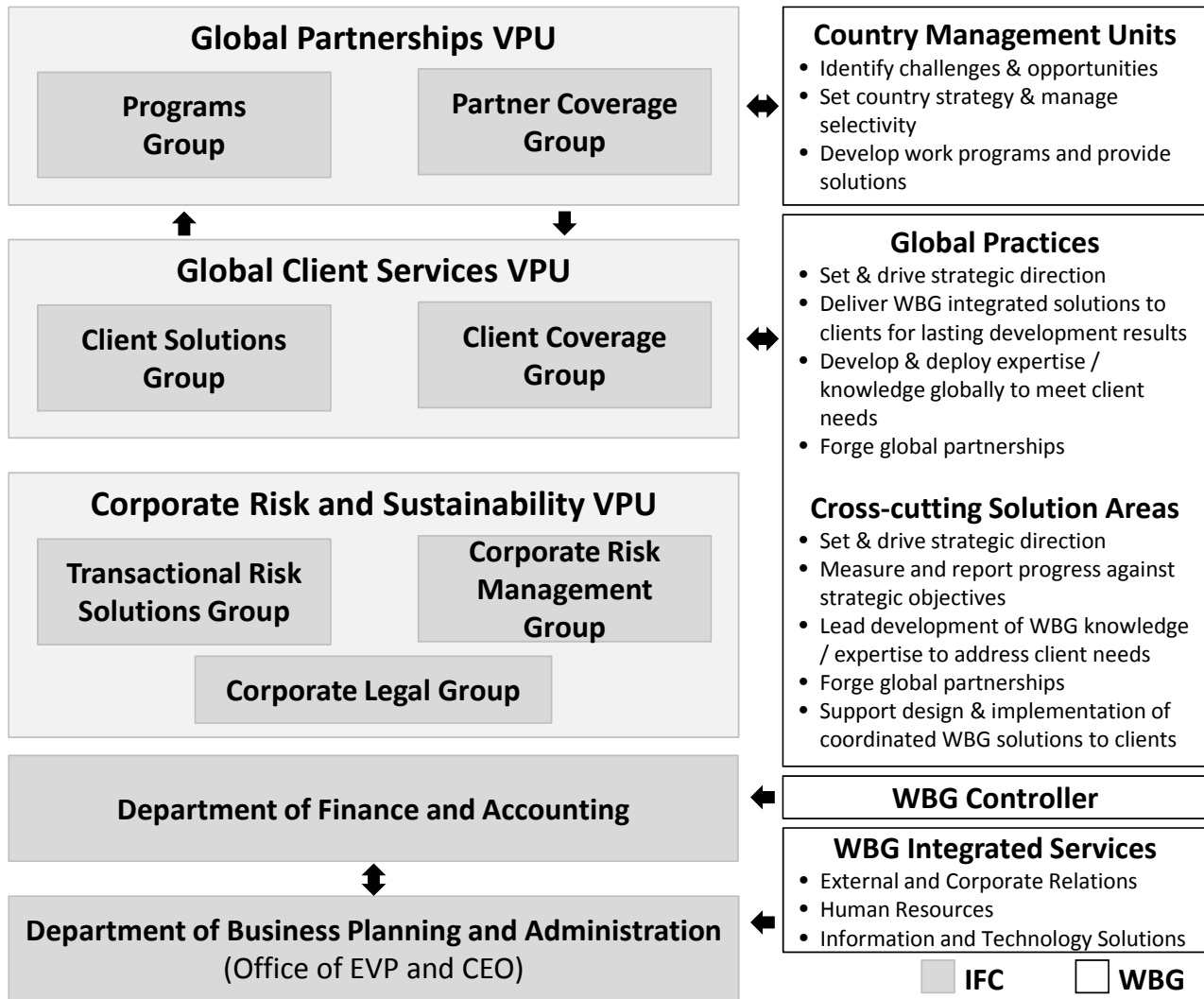
2.1 As the largest private sector multilateral, IFC is well placed to play a key role in implementing the WBG strategy to end extreme poverty and boost shared prosperity. The delivery of a number of ambitious transformational engagements will enable IFC to demonstrate its additionality and achieve greater development impact. However, those engagements will only be possible if IFC also enhances its financial sustainability. IFC will do so by becoming more client-focused and by further leveraging the benefits of one WBG and broader partnerships, as well as by driving improvements in profitability and productivity to maximize impact.

2.2 In FY15, IFC will sequence and prioritize its productivity and efficiency initiatives to enable the recently announced organizational re-alignment. A Refocused IFC aims to strengthen efforts towards client centricity and WBG engagement in leveraging the private sector to address development challenges in the WBG's client countries. IFC Management undertook a holistic review of the entire service delivery model to determine gaps and identify methods of improvement in areas such as organizational structure, governance, processes, talent, and technology. Following this thorough assessment, IFC Management is now beginning to oversee implementation.

B. A REFOCUSED IFC

2.3 Under a refocused delivery framework IFC aims to move from an organizational structure currently designed around regional vice presidential units to a framework founded around partnerships, client services and risk and sustainability, each of which will be covered by a new VPU. Combined, these VPUs will help IFC address higher impact development challenges, supporting the WBG goals of eradicating extreme poverty and improving shared prosperity; holistic, effective solutions will supersede volume and project count as the collective objectives. Chart 6 sets out the new structure in its broader WBG context, described in further detail below.

Chart 6. Refocused IFC Organization



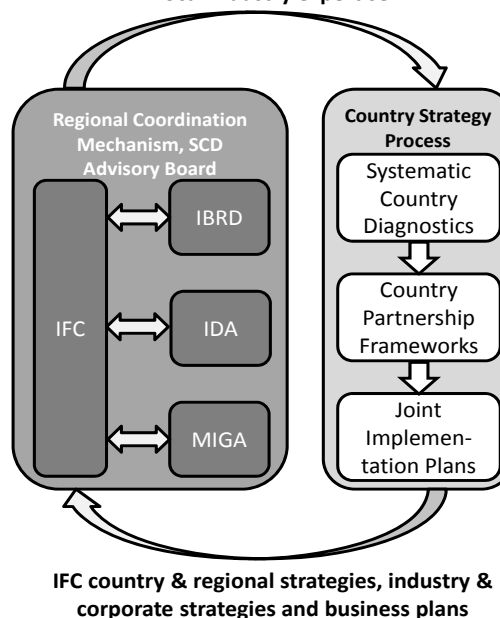
2.4 Global Partnerships. IFC is establishing a Global Partnerships VPU to facilitate smooth interaction with counterparts in the WBG and other development partners, and ensure strong private sector engagement. The VPU will function through two core units:

- a. **Programs Group.** This group is composed of the Regional Programs Unit (including the IFC Regional Program Heads and Leads) and the Global Economics & Strategy Department, which will help IFC form and transmit meaningful inputs on private sector development and private sector solutions for countries' development challenges.
- b. **Partner Coverage Group.** This group will provide active government-linked coverage for IFC and include Partnerships and Trust Funds.

2.5 As expressed in the addendum to the IFC Road Map FY15-17, IFC will lead the private sector aspects of the Systematic Country Diagnostics and Country Partnership Frameworks, with the level of IFC engagement determined by private sector constraints and opportunities in the development of the country in question. IFC's new Global Economics and Strategy Department, headed by a new IFC Chief Economist, will help IFC leadership incorporate the results of its macro-economic analysis on high impact areas for private sector engagement into the SCDs and CPFs, and inform the development of Joint Implementation Plans where most appropriate. Enhancements in IFC's client engagement model – intended to grow IFC's client base, manage its client relationships more effectively, and strengthen its position as trusted advisor – are expected to enable IFC to partner with clients to tackle countries' key development challenges, in line with the SCDs and CPFs.

Chart 7. IFC in the SCD/CPF Process

Private sector development role, global and local industry expertise



2.6 **Global Client Services.** By managing client relationships more actively and adapting its processes and business model where relevant, IFC aims to improve client service and grow its client base. A more structured client coverage model is intended to introduce a more holistic approach to clients, for example to enable early engagement with clients on their strategic and financing initiatives, to seek IFC involvement in a broader range of opportunities and solutions with a given client, to enable better visibility of relevant WBG resources, and to strengthen the bridge between the new business and portfolio functions. While the WBG Global Practices will have varying levels of institutional integration behind the scenes, they will serve as holistic implementing agents for all externally-facing solutions to clients, whether public or private sector. To this end, IFC is establishing a new Global Client Services VPU that encompasses investments, advice, and client relationships. This VPU consists of:

- a. The Client Solutions Group. This group will provide investment and advisory services through three industry groups and a cross-cutting advisory solutions group. All investment staff will be part of a global industry, based in HQ or in a region. Advisory staff not integrated within Global Practices will join industry groups, or become part of a single Cross-Cutting Advisory Solutions unit.
- b. The Client Coverage Group. This group will provide full-time dedicated coverage of a large group of former, current and/or prospective private sector clients. Investment staff in industry groups will continue to develop business from all other clients.

2.7 One of the co-VPs of the new Global Client Services VPU will drive IFC's operations in Fragile & Conflict Situations. These countries remain an urgent development priority, and IFC continues to bring greater focus across the organization to its FCS engagements, in collaboration with other WBG institutions.

2.8 IFC is adopting a more structured approach to serving clients and renewing focus on delivering solutions across departments. In the second half of FY14, an initial group of Client Leaders – a small team of IFC senior staff – assumed full-time responsibility for IFC's relationships with senior management at a

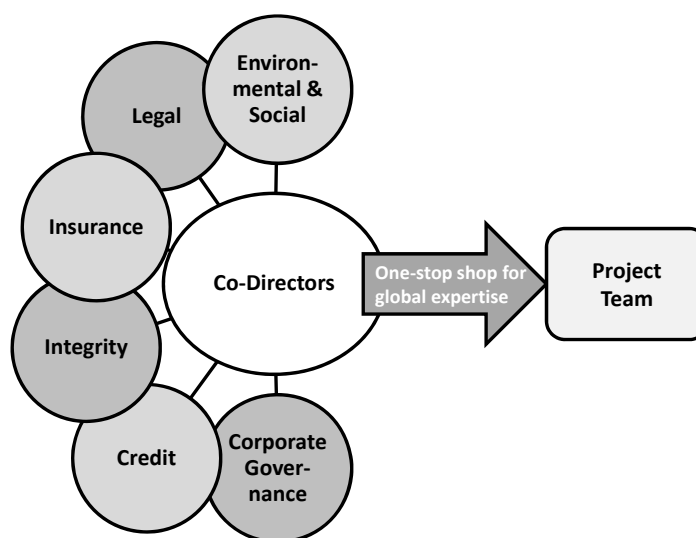
number of actual and potential IFC clients. Importantly, these senior staff are no longer required to spend time managing staff or budgets; they are entirely dedicated to client interactions.

2.9 Client Leaders focus their efforts on senior executives, developing long-term relationships and expanding the scope of IFC's dialogue and solutions. Each Client Leader covers 15-20 former, current and/or prospective clients of various sizes in areas that reflect his or her strengths and expertise, or where IFC currently has gaps. They span all regions and encompass a wide range of sectors including global strategic priorities sectors such as infrastructure, agribusiness, and financial services. Each Client Leader represents the full range of WBG products and services, with the goals of delivering holistic solutions and generating greater results. All client relationships are oriented toward generating greater development impact and financial results.

2.10 An initial phase will cover a small subset of IFC's client base (approximately 150 parent companies and their 350 subsidiaries, compared with roughly 8,000 companies with which IFC has an investment and/or advisory active project). As the refocus progresses, additional staff within operations departments will assume similar full-time client relationship roles for additional sets of clients.

2.11 IFC aims to provide better service to its internal clients. As illustrated in Chart 8, under a simplified Corporate interface, Co-Directors will provide one tool for doing so, offering a one-stop shop for project teams to fill their corporate support needs.

Chart 8. Simplified Corporate Interface for Project Teams



2.12 **IFC Advisory Services in the new WBG.** Over recent years, IFC Management has been pursuing a series of bold reforms to strengthen the impact and effectiveness of Advisory Services. The AS reforms have contributed to continuous improvement in development results (Development Effectiveness ratings climbed from 62% in FY10 to 76% in FY13) and consistently strong client satisfaction (90% in FY13). They have also contributed to improved efficiency as well as progress in building a more financially sustainable funding model.

2.13 To take AS to the next level, IFC Management has decided to strengthen client focus and impact by bringing AS together with relevant WBG Global Practices and with IFC Investment Services. The current four AS business lines are being reorganized as follows:

- a. Investment Climate will become an integral part of the WBG Trade and Competitiveness Global Practice.
- b. The part of Access to Finance that focuses on market development and enabling environment work will join the WBG Finance and Markets Global Practice, while the part that works with individual firms will join IFC investment services as part of IFC's Financial Institutions Group.
- c. Public Private Partnerships will remain a core IFC offering, working closely with the WBG global practices and IFC industry departments, including through the new WBG Cross-Cutting Solutions Area for PPPs.
- d. Sustainable Business Advisory alternative considerations are currently being discussed.

2.14 To facilitate transition to the new structure, IFC Management will fund AS staff moving to WBG Global Practices during at least FY15. During FY15, the AS funding model will be jointly reviewed to take account of factors such as:

- a. AS with individual firms undertaken with IFC industry departments are expected to be provided on an increasingly commercial basis over time.
- b. AS on broader market development and enabling environment issues undertaken with WBG Global Practices should have new opportunities to leverage IBRD/IDA lending instruments. There will also be opportunities to harmonize pricing policies for advisory work for the WBG as a whole and to achieve greater efficiencies and coordination through various joint arrangements.

2.15 **Corporate Risk & Sustainability.** IFC is creating a new Corporate Risk & Sustainability VPU that unifies transaction enabling services. The VPU consists of three units:

- a. Transactional Risk Solutions Group. This will include all transaction-enabling services (Legal, Environmental & Social, Investment Credit, Integrity Risk, Insurance, and Corporate Governance). This will strengthen IFC's risk judgments and simplify the transaction approval process for staff.
- b. Corporate Risk Management Group. This will include all macro and micro risk functions related to pricing, rating, and evaluation; risk reporting; and stress testing and monitoring. This will consolidate IFC's view and approach to risk management.
- c. Corporate Legal Group. This will consist of the compliance, conflict of interest, and legal practices.

2.16 This new structure will enable IFC to view all of its projects from an integrated risk perspective. By enabling central oversight of both financial and non-financial risk at both the transaction and corporate levels, IFC will be able to promote the highest standards consistent with its brand and ensure that it sets the global standards to which other multilaterals will aspire.

2.17 As part of the refocusing effort around the three new VPUs described above, IFC is also streamlining processes to enable more efficient decision-making. Each VPU will have a cross-VPU Steering Group, and IFC Management Team's role as the Corporate Risk Committee will be unified. As a first step toward a refined investment approval process, the Corporate Risk & Sustainability Steering Group will absorb the role of the current Corporate Operations Committee/Regional Operations Committees.

2.18 In parallel, IFC will expand the ability of IFC managers to approve investment projects through delegation so as to improve its responsiveness to clients, simplify processes for staff and empower management at all levels. Currently, thirty-five managers have delegated authority to approve Tier I investments. As a result, staff can more easily obtain approval of their projects through managers with relevant delegated authority, which simplifies their work and achieves quicker and more streamlined decision making, benefitting IFC's clients.

2.19 **Business Planning and Administration.** The Business Planning & Administration Department, with support from the Finance and Accounting Department as well as WBG Integrated Services, will be in charge of driving initiatives that have cross-departmental applications and further support real-time re-allocation of staff and resources, internal communication, training, knowledge, governance, and management reporting.

2.20 IFC's Finance and Accounting Department will ensure that available resources are allocated to fund the entire work program including a growing portion that will be delivered by the WBG as a whole. Starting in FY15, part of IFC's budget will directly fund IFC staff reporting to Global Practices and Cross Cutting Areas. This budget allocation will be adjusted as business needs evolve.

Box 2. World Bank Group Controller

The WBG Controller position was announced in February 2014. This newly created position will further advance synergies and sharing of best practices among the Controller functions across the WBG institutions. The WBG Controller's functions will contribute significantly to the integrated services model thereby increasing collaboration and reducing overlaps across the WBG. The role will also enable more proactive, timely, effective, and efficient services and actively support the implementation of the new WBG strategy.

2.21 **Staffing.** IFC had 3,977 staff at FY14 Q3-end and is projected to end the fiscal year at about the same level. Year-to-date, IFC had 268 hires and 169 exits. Moreover, 138 staff transferred from the IFC to the WBG-integrated ITS, ECR and HRD units. When discounting these inter-institutional transfers, staffing growth would have been 2.3% year-to-date, below the average annual 3.8% growth in the five prior years.

2.22 IFC's senior management continues to centrally manage external hiring through the employment control framework implemented in early March 2014, which was adopted WBG-wide (VP approval for filling any vacancy internally, and IFC EVP approval for selecting any external candidate if no suitable internal candidate is available).

2.23 These controls along with a specific focus on staff re-allocation help ensure that hiring remains aligned with strategic priorities and resources are utilized in the most optimum way. A general decrease in new hires within FY14 to-date is seen already compared to the prior fiscal year with an average 30 new hires per month YTD, with continued expectations of slow-down compared with 40 new hires per month in FY13. FY14 to-date exits have remained at similar levels to those in FY13 with about 19 exits per month.

2.24 **Award Programs.** In alignment with its strategic priorities, the IFC awards programs continue to provide the directional incentive to drive results for clients and promote greater effectiveness across the organization. Today, IFC has an array of incentives and reward and recognition programs that have evolved over time to address business priorities, reward top performance, and recognize extraordinary individual and team efforts. Specifically, IFC's portfolio of awards programs serves the following purposes: (i) reinforce the link between the achievement of goals and rewards; (ii) provide the necessary tools to reward for various types of performance, whether at the individual, team and/or specific project level; (iii) differentiate for top performers; (iv) incentivize, recognize and reward performance over multiple time periods (ranging from less than 1 year to 3-8 years); and, (v) partially close the gap between the market pay levels and staff pay levels, specifically for investment and core finance functions.

2.25 As IFC renews its focus, the current programs need to evolve further to ensure alignment with the new strategic direction, and to incentivize work in priority areas such as FCS or work across organizational units, including across the WBG.

2.26 An IFC Incentives Working Group is reviewing IFC's variable-pay/awards programs with a view to setting a holistic framework across the various programs. It will make recommendations to be implemented for the FY14 performance cycle. This working group will also be looking at greater performance and functional differentiation. New and/or modified reward and recognition programs (monetary and non-monetary) are being explored.

2.27 IFC's experience in linking results with incentives is also being leveraged across the WBG. Specifically, IFC has utilized scorecard results as an integral component of its Annual Performance Award program. In FY14, IFC introduced a new approach to scorecards by adding a direct link between department and corporate performance in incentive programs to encourage staff to collectively deliver on corporate results and support one another across organizations. The lessons learned will be evaluated for further adjustments in FY15, including strengthening the link with the WBG Corporate Scorecard. This will inform IFC's scorecard in FY15 and beyond.

2.28 With the introduction of the new Global Practices it is also critical to ensure appropriate incentives to motivate and reward collaboration, not only across the global practices and cross-cutting solution areas, but also between IFC and World Bank units. Hence, the IFC Incentives Working Group is coordinating very closely with a cross-organizational task force on results and incentives.

2.29 **WBG integrated delivery model.** In FY13, HR, Corporate Relations and IT functions were chosen as quick wins for integration as there was significant overlap between the World Bank and IFC in these areas. The following provides an update from IFC's perspective on results to date. Integration, which took place in FY14, has been and will continue to be a learning process. IFC will work with its counterparts to make improvements as warranted.

2.30 Box 3 provides examples of early successes.

Box 3. World Bank Group Integrated Services Experience with IT, HR, and ECR

IT. The information and technology units of the WBG were integrated at the beginning of FY14 to create a Group-wide information and technology organization. Services provided to IFC by IBRD were agreed and documented in shared services agreements put in place at the beginning of the fiscal year; this was followed by quarterly monitoring of the service quality, deliverables, and client feedback. This SSA monitoring framework covering 66 services and 51 capital projects has to-date proven valuable, and continues to be monitored to ensure that expected scope, performance levels, and pricing are clear and that services are being delivered as agreed. WBG IT integration has brought innovation in many areas of IT greatly increasing the capabilities to staff. Cloud-based solutions such as File, Synch and Share, Client Relationship Management, improved analytics, better devices, and more mobile-enabled transactions bring increased productivity to a busy and mobile workforce. Integration also allows IFC to focus on business specific applications of new technologies such as data visualization and Client Relationship Management to support IFC's client-centric business strategy. Under the integrated model, IFC retained a Chief Information Officer to advocate IT priorities, coordinate governance, manage the business relationship, manage IFC specific business solutions and unique needs, and monitor service levels on behalf of IFC and its constituents; IFC also retained governance over its capital investment program, ensuring that IFC business priorities are served. Finally, IFC's IT department remained responsible for delivering IFC-specific services and solutions. IFC expects to simplify some processes and make other improvements during FY15 as all parties learn along the way.

HR. In the course of the WBG integration of HR, a new WBG-wide HR governance and delivery model has been developed which, among other things, introduced a WBG People and Leadership Committee, building on the experience with the IFC PLC, and clarified the roles and accountabilities of HR Business Partners, Centers of Expertise, and Shared Services. To guide the WBG HR integration, a consolidated list of top FY14 priorities and core services were produced for each HR Center of Expertise and Shared Services, and helped in creating a WBG HR FY14 work program and Memorandum of Understanding, which in turn was used in developing FY14 business objectives and SSAs between IFC and WBG HR. Overall, the Group-wide integration has and continues to deepen the understanding of HR policies, practices, and governance in IBRD, IFC and MIGA, and help in identifying internal best practices. Organizationally integrating WBG HR staff and sharing information, for instance through frequent town hall-style events and a newsletter, allowed knowledge and experience to flow more easily. Best practices identified have been informing initiatives like strengthening staff planning, expanding within-grade progression, sharpening HR-related scorecard indicators, and establishing one-WBG performance management. Standardizing the recruitment function, centralizing global mobility program management, aligning leadership and learning programs, and creating a centralized transaction processing team in Chennai have been geared towards improving effectiveness and efficiency. The work to build common HR practices into business strategy, plans and processes will continue, as will efforts to clarify roles and responsibilities, and improve SSA administration.

ECR. On July 1, 2013, an integrated communications function was established for the WBG—the External and Corporate Relations VPU. ECR has made significant progress in reaching across institutional boundaries to generate more effective communications that advance WBG goals while attending closely to the needs of each institution. Significant progress was made in four specific areas: (i) **Reputation Risk:** Communications staff across the WBG collaborated closely to manage reputation risks pooling individual talents and expertise—with respect to media and social media, Civil Society Organizations, and government affairs—to develop effective strategic communications plan; (ii) **Brand Management:** In FY14, a WBG visual identity was introduced to enable the institutions to speak with one voice about their shared goals of ending poverty and boosting shared prosperity. This initiative will help leverage the collective strengths of the WBG institutions while reinforcing their individual brands; (iii) **Web and Social Media:** The World Bank already has a highly effective web and social media operation. Those capabilities are now being deployed across the WBG, raising the profile of individual institutions through cross-promotion. IFC is benefiting from ECR's integrated social media crisis-monitoring program; and, (iv) **Content and Messaging:** WBG communications staff members collaborate across institutions to produce high-quality multimedia and editorial content. IFC, as a result, no longer uses external vendors to produce videos. Where appropriate, content is being integrated for the internal and external websites of WBG institutions, and for key publications such as annual reports.

2.31 Shared services agreements. 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, HR and External Communications to Finance or General Services, through transaction and administrative expense and compliance activities provided by central units.

2.32 During FY14, the value of SSAs amounted to \$106.6 million (Table 1). The value of services provided by the WBG Integrated Services entities (HR, IT and ECR) amounted to \$55.2 million or approximately 52% of the total. The preliminary review and discussion of the value of SSA services to be agreed upon for FY15 is expected to increase primarily due to IFC being allocated a significantly higher share of Board costs. In addition, the SSA for Integrity Department Services is being renegotiated taking into consideration a more reflective basis of cost sharing and therefore the FY15 estimate remains similar to FY14 for the time being.

Table 1. IFC-IBRD Shared Services Agreements (\$mn)

	Service	World Bank Unit	FY14 Amount	FY15 Estimate before Price Increase	Anticipated Increase
1	IT Services	ITS	40.0	45.0	5.0
2	Board Services	COGOV	18.3	23.8	5.5
3	General Services Department Services	GSD	12.1	12.5	0.4
4	Human Resource Services	HR	7.9	8.9	1.0
5	Communication Services	ECR	7.3	7.5	0.2
6	Independent Evaluation Group Services	IEG	7.0	6.8	-
7	Controllers Services	CTR	3.9	4.0	0.1
8	Integrity Department Services*	INT	3.6	3.6	-
9	Insurance Services	GSD	2.5	2.5	-
10	Internal Audit Services	IAD	2.2	2.2	-
11	Business Continuity (BCP) Facility	GSD	0.7	0.7	-
12	Treasury Services	TRE	0.7	0.7	-
13	Risk Services	CRO	0.4	0.4	-
14	Country Office Security **	GSD	-		
Total			106.6	118.6	12.2

*Basis of cost reimbursement being renegotiated for FY15

**New SSA for FY15; reimbursement amount not yet determined

2.33 The WBG's emphasis on efficiency and synergies between its institutions, coupled with the recent creation of the WBG Controllers unit, is expected to lead to new activities, processes and procedures being identified during FY15 for inclusion in the shared services approach.

C. MEASURING RESULTS

2.34 IFC is developing new metrics for monitoring and measuring success that reflect client focus and financial sustainability and that align with WBG/IFC Scorecards as well as an improved framework to understand development impact. The monitoring of productivity and efficiency in order to understand the optimal mix of resources for strategic and sustainable investment output remains at the forefront of IFC Management priorities. IFC continues to examine how to maximize effective new business delivery as well as monitor an evolving and complex portfolio, while utilizing resources effectively and efficiently.

2.35 **New metrics.** Metrics will play a critical role allowing IFC Management to monitor performance and change behavior as part of the new Client Service model. They will be carefully developed and reviewed as needed, for implementation effective in FY15. New internal metrics will also consider relevant external benchmarks as a means to continue holding IFC to high standards in charting the path forward. IFC is refining how it measures results beyond transactional and volume targets. Beyond informing decisions, IFC Management is carefully considering how metrics will be able to influence staff behavior further toward common goals and objectives for the long term. In addition, IFC's results measurement

framework will focus more closely on understanding impact of our interventions, primarily through job and economic growth effects, while maintaining our leadership role in this area.

2.36 Metrics will be focused on client responsiveness, relationships and impact. Priority will be shifted away from volume and project count. The new metrics will be based on the following guiding principles:

- a. Initially, metrics will not be used to set targets/goals but as a means for continuous improvement
- b. Metrics used for internal IFC management will be consistent with metrics reported to external stakeholders (including the Board)
- c. Metrics will only cascade down to department/unit/project levels when it makes sense
- d. Metrics with a horizon greater than one fiscal year will be tested as part of this program
- e. Metrics will be adjusted as new tracking and reporting tools become available
- f. Selected metrics will be easy to calculate and available to IFC Management and client service teams in order to begin changing mindsets and behaviors

2.37 IFC has started the process of reconciling the WBG's, President Delivery Unit's, and IFC's own evolving results measurement frameworks so that all are aligned. Metrics will need to be consistent across scorecards, with appropriate selections based on lines of sight to impact and ultimate usage. Table 2 provides a few profitability and productivity metrics under consideration given the focus of this paper; the final metrics will comprehensively cover IFC's results and performance including such provisional topics as growth, inclusiveness, sustainability and resilience, development outcomes, client feedback, alignment with strategy, working as one WBG, operational delivery for clients, financial sustainability, and managing talent. The selection and adoption of a new results framework may require significant time, but IFC is committed to developing and using a scorecard that is both strategic and practical.

Table 2. Sample Profitability and Productivity Metrics under Consideration

		Timing		Frequency		Usage	
	Sample metrics	Ex ante	Ex post	Per annum	Multi year	Strategic planning	Portfolio mgmt.
IFC overall	Controllable income	✓	✓	✓		✓	✓
Operations	Total resource / Assets under management		✓	✓	✓		✓
Investments	Net loan and fee revenue coverage of total expenses	✓	✓	✓		✓	✓
Loans	Risk adjusted return on capital (RAROC)		✓	✓		✓	✓
Equity	Sharpe ratio		✓		✓	✓	✓

2.38 **Changes to IFC's Results Measurement Framework.**¹ Changes to IFC's Results Measurement Framework, which are to be presented shortly, have a greater focus on understanding impact, and on improving the articulation of how planned operations will lead to intended results. The framework will also be aligned with the WBG strategy and scorecard. Please see the IFC FY15-17 Road Map Addendum for the principles underlying the current plan. The following key changes are proposed:

¹ IFC will inform Board Committee on Development Effectiveness (CODE) of the detail of these changes on July 2, 2014, seeking guidance on its approach going forward.

- a. IFC's overall impact: Deepen understanding of the impact of IFC's interventions mainly through job and economic growth effects, including the impact of Global Industry Departments' key projects/programs in strategic priority areas. For example: assess indirect job effects in selected automotive sector transactions, estimate an economic multiplier for power projects, and estimate the job effects of SME finance.
- b. Country level results: Build joint results measurement frameworks for Country Partnership Frameworks, with WB/MIGA.
- c. Raising the unit of analysis from transaction to Strategic Program results (e.g. transformational engagements): Support teams in measuring, monitoring and evaluating results of these engagements and their underlying component projects using a common results framework for the program.
- d. Technology as a tool: Streamline monitoring and significantly ramp up the use of monitoring data and evaluative evidence, systematically, to add value to clients.

2.39 IFC is unable to determine at this time the resource implications of these changes.

2.40 IFC has made great progress in instilling a culture and foundation around profitability to ensure business decisions are made with expectations on financial returns to help sustain IFC's capital base. In recent years, IFC embedded profitability targets within Management and staff objectives and developed tools to best measure its predictable and volatile drivers for ex-post and ex-ante analyses in the most effective way. Additional changes to create focus on profitability drivers on an annual and/or multi-year basis are currently being explored further. Such distinction will allow for management and measurement of results influenced by new business activities versus current portfolio decisions. Section IV provides results on current measures which are used by IFC Management and Operations.

III. Strategic Reallocations

3.1 Understanding the need to maintain flat real total resources (+0.9% nominal increase) in FY15, IFC Management has investigated and continues to explore ways of freeing existing resources for reallocation to areas of increased emphasis. “A Refocused IFC” will provide some room for movement through productivity and efficiency gains. IFC’s participation in the WBG Expenditure Review will also produce gross savings, which IFC will track for reinvestment in the business over the next three years, and IFC Management has identified further areas for reduction or elimination. Finally, IFC’s involvement in the WBG Global Footprint exercise, while not resulting in short-term savings, should lay the groundwork for future savings. IFC Management will carefully manage resource utilization across the new organizational structure throughout the fiscal year in order to sufficiently fund strategic priorities such as transformational engagements; the new delivery model; improved environmental and social sustainability risk management; IT; staff skills; innovation; and enhanced treasury and capital markets innovation.

A. ESTIMATED GROSS SAVINGS FROM THE EXPENDITURE REVIEW

3.2 At the 2013 Annual Meetings, the Board of Governors endorsed a new Finance and Risk Framework in support of the new WBG strategy, setting a \$400 million savings target to be achieved by FY17. The objective of the WBG Expenditure Review is to bring about a significant reduction in the WBG’s cost base while maintaining its capacity to more efficiently deliver high-impact solutions and services to its clients, enabling achievement of the WBG twin goals.

3.3 While the initial Expenditure Review analysis has estimated that roughly 18% of total gross savings for the WBG could be attributed to IFC, the teams are in the process of validating measure-by-measure the impact on IFC’s cost basis of the proposed changes.

3.4 IFC will track savings against the Expenditure Review initiatives, reporting progress (or lack thereof) and adjust accordingly, as some savings could be realized sooner based on implementation plans.

B. GLOBAL FOOTPRINT

3.5 IFC’s emphasis on global presence and global expertise remains steadfast, and it carefully considers the costs associated with decentralization. “A Refocused IFC” will remain an IFC with strong traction in the field, working to bring integrated solutions to clients of all sizes.

3.6 As part of the Expenditure Review, IFC’s Facilities Management team worked with the IBRD General Services Department to jointly review office co-locations among the WBG institutions. This approach identified that IFC and the World Bank are currently co-located in 75 countries, with plans to co-locate within the next 2 years in six more countries. This will raise the total of IFC co-located offices to approximately 72%. Following on the WBG decision to co-locate offices where possible, IFC and the World Bank will continue to discuss co-location where it is practicable and where the costs to both institutions are not prohibitive. The synergies in the WBG operations delivery models will clearly support such moves between the organizations.

3.7 Additionally, IFC and the World Bank will be looking to finalize the Global Real Estate Strategy, which is expected to lead to savings in the reduction of rental expenses through the purchase and/or construction of country offices. Based on such buy vs. lease reviews, especially where office rents are extremely high, 9-10 country offices have been identified by IFC and the World Bank that merit more

detailed review to confirm possible savings. In some cases, the governments have already been contacted to discuss the possibility of free land being provided to the WBG for construction. IFC will continue to work with the World Bank to look at country offices where the effectiveness of the location will support the new delivery model. For offices where the new model is not effectively supported, IFC will consider closing and moving activities to other offices as appropriate. Clearly any such decisions will have to consider implications of closure versus required travel to compensate for the new distance.

C. AREAS FOR INCREASED RESOURCE CONCENTRATION AND/OR REINVESTMENT OF EXPENDITURE

REVIEW GROSS SAVINGS

3.8 As outlined in the addendum to the IFC FY15-17 Road Map, IFC's historic and recent performance suggest that the medium- to long-term development results and financial returns of reinvesting any gross savings would far outweigh the near-term capital benefits of reducing the total expenditures identified as potential gross savings, especially considering the benefits of IFC's robust third-party mobilization. However, as more granular details emerge about the type and extent of measures selected (and their proportional impact on IFC), IFC Management will carefully track savings and will continue to re-evaluate the benefits of reducing total expenditures versus reallocating savings and strategically accelerating its growth and impact.

3.9 Currently, IFC Management plans to re-allocate all gross savings resulting from efficiency gains and cost saving initiatives in four main areas: environmental, social and governance risk; technology; refocused delivery model; and, incentives. Two additional areas (Treasury and capital markets innovation; Asset Management Company) are also identified as areas for growth, and which are expected to generate additional income for IFC. Ultimately, some shifts in resources will be contingent on the type and magnitude of savings achieved via the Expenditure Review and/or internal productivity improvements.

3.10 **Environmental, Social & Governance Risk Management.** While IFC is enhancing its entire strategic risk framework, IFC Management has identified ESG risk management and client engagement as a particular area for increased resource intensity in FY15 and over the next several years. Under the new Corporate Risk & Sustainability VPU, ESG will continue to work primarily at the firm level to directly support clients in adopting and applying IFC's environmental and social Performance Standards, and strengthening their corporate governance practices. As IFC works to increase its support to clients in fragile and conflict situations and through transformational operations, ESG issues facing clients will be more complex, requiring best-in-class ESG risk management. Lessons learned from recent operational experience and Compliance Advisor/Ombudsman findings demonstrate the importance of providing integrated ESG services to clients, increasing the understanding of the contextual risks that clients face in successfully implementing the Performance Standards, and ensuring that IFC stays on top of current and emerging issues. Examples of such issues include stakeholder engagement, conflicts, and tensions around land and water, supply chain issues, deployment of security forces, and ESG management in financial institutions.

3.11 Within the new IFC organizational structure, ESG will remain a core function and a center of excellence on sustainability, serving IFC and its clients, and further strengthening its leadership role on ESG among the financial institutions working with the private sector. In this regard, there are several ways in which IFC can strengthen client engagement on the ESG front to achieve better risk management and sustainability outcomes. These include:

- a. More comprehensive environmental and social assessment processes that include understanding the country and sector issues that might impede clients in implementing the Performance Standards or present implementation risks that are out of clients' control and represent reputation risks for IFC;
- b. Intensified supervision in priority, high risk situations and for clients with limited capacity in high risk contexts, developed and managed in a more structured region-based portfolio management function; and,
- c. The ability to flexibly and quickly deploy experienced teams of staff and consultants to respond to emerging high risk situations and offer intensified client support.

3.12 An important element of this scenario is to enable effective engagement of IFC in transformational projects, with robust attention to the sectorial and thematic areas outlined above. This would also entail strengthened coordination and collaboration across the WBG as relevant to identifying ESG issues and how to solve them, and intensified internal skill development on ESG sustainability within IFC. While leveraging the work of IFC through external consultants, this would also involve the creation of new staff positions, many of which are likely to be externally recruited given the current unavailability of relevant skills and expertise within the WBG.

3.13 Further IFC leadership in sustainability would have two broad objectives: (i) a more proactive and strategic approach to supporting clients' ability to implement IFC's Performance Standards, and (ii) a stronger leadership position for IFC in sustainability and the private sector, including external partnerships focused on innovation, solutions to emerging issues, and reaching groups of firms. These objectives would strengthen the linkage and synergies between what IFC contributes and learns from its operational engagement and IFC's global partnerships and thought leadership. Strengthening IFC's leadership role in the private sector would involve engaging in broader strategic partnerships aimed at improved coordination around policy requirements; leveraging IFC's convening role by building broader market support and consistency through financial institutions, groups of firms, and industry associations; and innovating around emerging issues such as natural capital, biodiversity, and business and human rights. There is strong demand among clients and in the market more broadly for IFC leadership in these and other emerging areas of interest.

3.14 **Technology.** Savings expected from IT initiatives will be reinvested within IT to accommodate growing business demand for system improvements (which will translate into higher depreciation, maintenance charges, and project administration costs). IT will provide enabling solutions that specifically support IFC's strategy, including: (i) client relationship management tools to leverage quality partner data, make information more accessible and improve client service; (ii) flexible systems to allow for quick introduction of new products to grow IFC's business and to allow differentiated approaches by clients, products and industries; and (iii) alignment of development, financial, investment and advisory data, along with new credit tools and consolidated risk reporting for improved decision-making and risk management. Efficiencies will be improved through: (i) modernization of fragmented operational data and streamlined processing for investment operations; (ii) mobile solutions including online approvals and cloud-based file sharing; and (iii) higher quality infrastructure and country office bandwidth with improved system response. The increased costs associated with these activities will mainly be seen through depreciation, maintenance and support, and IT project administration.

3.15 **IFC's new delivery model.** IFC plans to reinvest savings from Norms for Management as stated in the Expenditure Review section of the paper to fund the deepening and broadening of IFC's partnerships and client relationships. To this effect, IFC is adopting a more structured approach to serving clients by

expanding the scope of its dialogue and engagement with clients through the offering of a comprehensive suite of WBG products and services.

3.16 IFC Annual and Long-Term Performance Award Programs. IFC continues to use its portfolio of integrated non-salary monetary award programs in creating a performance-based culture. The programs reward corporate projects, teams and individuals based on outcomes and initiatives which have a significant and lasting impact for the IFC and its clients. In FY15, IFC awards and incentives will be realigned to help drive behavior towards increased performance, client engagement and collaboration across organizational boundaries. The recommended FY15 budget will restore the IFC awards to the FY11 original budget as a percent of the IFC wage bill. Following interest from the Human Resources Committee of the Board regarding IFC awards and incentives, a briefing for Executive Directors and Executive Director Advisors is being organized for FY15 Q1.

3.17 Treasury and Capital Markets Innovation. While any additional resources for Treasury operations would be supported by increased Treasury revenue rather than gross savings or productivity gains, IFC Management would like to highlight the rationale for intensifying this area as well. The Treasury Client Solutions team is already providing IFC's clients with local currency, risk management and structured credit solution, generating fee and interest income and promoting development outcomes. Treasury and capital markets innovation will expand under the new client focused structure, and Treasury capital market solutions will be a part of the core business offering to IFC clients.

3.18 Over the past two years, Treasury has put its client solution staff in several of IFC's larger country offices (Dakar, Senegal; Hong Kong SAR, China; Moscow, Russian Federation; and, Johannesburg, South Africa) to be closer to clients and investment staff. This has proven to be extremely valuable. In pursuit of offering clients IFC's full Treasury capabilities in their respective time zones, IFC will establish a Treasury presence first in a European financial center and subsequently in an Asian financial center. These Treasury centers will replicate all the functions of their HQ counterpart, including liquid assets and cash management, funding, client risk management, structured finance solutions, and other treasury client solutions. The centers will have their own profit & loss for better accountability and will allow deeper engagement with clients, offering real time solutions and support to operations. IFC Management is considering the costs of Treasury and Capital Markets innovation and will provide an update to the Board.

3.19 Asset Management Company. Further growth of the AMC platform continues to be a strategic priority and an additional source of income for IFC.

D. REGIONAL AND GROUP BUSINESS REVIEWS

3.20 Beginning in FY14, IFC has undertaken a new practice, in the form of Regional Business Reviews, to report internally on current and expected opportunities as well as risks across its regions. These discussions allow IFC Management and operational teams to elaborate on market developments, portfolio results and profitability, WBG high impact opportunities, transformational engagements, and other matters on a periodic basis. Similarly, effective April 2014, the WBG has implemented a Group Business Review to discuss issues and progress toward collective business and financial objectives. Through this forum and other means, IFC plans to report and discuss progress on its operations and financial results across regions and industries with its Board on a quarterly basis.

IV. Financial Sustainability Outlook

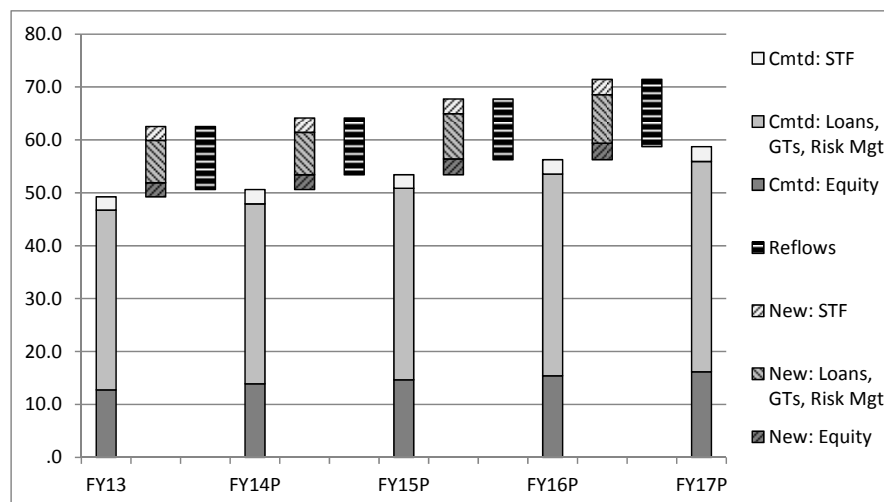
4.1 Financial Sustainability is defined as IFC's ongoing ability to accomplish its mission by generating and maintaining sufficient financial resources through business activities and resulting profitability.

A. PIPELINE AND PORTFOLIO: INVESTMENT AND ADVISORY

4.2 **Investment pipeline and portfolio.** As set out in the Road Map, IFC is committed to delivering an additional long-term finance program of up to \$11.8-12.8 billion through its own account by FY17, while mobilizing an additional \$6.4-7.4 billion by the same period. Measurement of trade finance commitments, a large proportion of IFC's short-term finance business, will shift from accumulative commitments to average outstanding portfolio in FY15. This will impact total volume as historically calculated, including with regard to IDA and FCS countries.

4.3 While future growth rates are relatively lower than historic results, the size of IFC's investment pipeline is not in itself a reflection of either IFC's commitment or ambition. While volume remains critical, results achieved through volume in the form of financial results and development impact are of utmost importance.

Chart 9. Pipeline & Portfolio Projections, FY14P-FY17P (\$bn)



4.4 IFC's committed investment portfolio has been growing at an average rate of about 12% per annum over the last 10 years, reaching \$50 billion at the end of FY13. It is projected to reach \$60 billion at the end of FY17, at a compounded annual growth rate of 5%. The decrease in projected portfolio growth is in part attributable to the need to manage growth of the own account portfolio with limited capital availability as well as the emphasis on mobilizing third party capital, and focusing resources on transformational projects, in which significant impact may be achieved with lower volume over time.

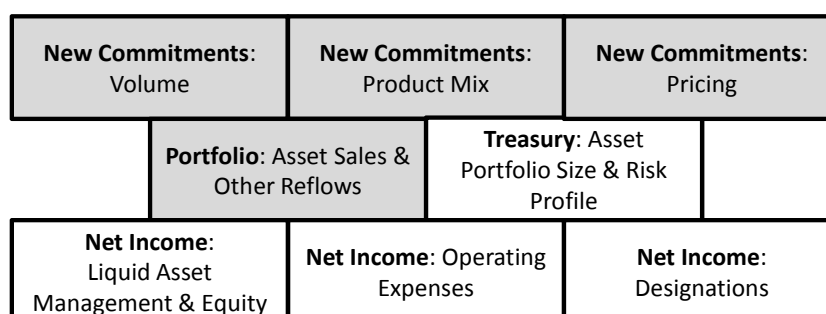
4.5 IFC will exercise selectivity through its focus on sectors where impact can be greatest, including infrastructure (particularly energy and extractives), agribusiness and the food supply chain (with a focus on integrated cross-sector solutions), health and education, and financial markets (providing access to

finance, including through partnering with intermediaries and ramping up local capital markets programs). It will continue to emphasize the cross-cutting themes of jobs, climate change, gender, and public-private partnerships as appropriate.

4.6 IFC will continue to pay particular attention to: Sub-Saharan Africa, which has the most countries with a high incidence of poverty, with the aim of making Sub-Saharan Africa the largest IFC program by FY17; South Asia (including Afghanistan and Pakistan), which accounts for the largest number of the world's extreme poor; the Middle East and North Africa, with a focus on jobs for disadvantaged youth and women; and FCS and other challenging IDA countries that pose unique development challenges. In Middle Income Countries where 70% of the global extreme poor reside, including a large population living in urban areas, IFC will focus on innovation, inclusion, frontier regions, climate change and South-South. In IDA countries, where IFC continues to have a focus, it is also exploring innovative ways to work with other institutions in the WBG, such as the possibility of leveraging some of the IDA17 replenishment funding in order to catalyze additional private sector investment and increase our impact on growth and job creation.

4.7 **Deployable strategic capital.** Focused, selective and smarter long-term financing has to be underpinned with the right level of risk capital to create sustainable financial results. Such long term benefits should also exert a stabilizing countercyclical impact for IFC's clients. IFC's capital adequacy measured through its DSC stood at 8% at the end of FY13. IFC projects DSC over a three-year period to ensure that there is enough capital to implement the strategy. IFC is highly attentive to the importance of capital management and of maintaining the highest rating standards.

Chart 10. Measures Impacting Deployable Strategic Capital



4.8 As noted in the Road Map Addendum, IFC expects DSC to remain positive to FY17, taking into account the increase in transformational projects as well as the increased exposure to FCS. Further discussion of IFC's DSC projection, range and concentration analysis will be presented in the FY14 Financial Risk Management paper.

4.9 Advisory business plan and budget. Following strong growth in recent years, total AS spend is planned to slow in FY15 to help consolidate reforms and facilitate transition to the new organizational structure. Program spend is expected to continue to grow, however, as a result of new efficiencies from working more closely with Global Practices and with IFC Industry Departments. Planned total AS spend and total AS program in FY15 are presented in Table 3.

Table 3. Advisory Services, Total Spend & Total Program, FY12-15P (\$mn)

	FY12	FY13	FY14E	FY15P
Total Spend	365	392	400**	390
Total Program*	197	232	238	242

*Comprises direct spend on client-facing projects, and excludes spend on non-client facing projects (e.g., knowledge management) as well as Program Management & Support and General & Administrative expenses.

**\$400 million estimated spend at year-end per the FY14 Q3 Performance Report to the Board vs. a plan of \$417.5 million.

4.10 AS has had a strong emphasis on IDA, FCS and climate change for several years. This emphasis is expected to continue under the new organizational arrangements, although specific targets will need to be confirmed with relevant WBG Global Practices and IFC Industry Departments as part of new integrated strategies and business plans. The FY15 projected program shares are presented in Table 4.

Table 4. Advisory Services, Strategic Emphasis Areas, FY12-15P (\$mn)

	FY12	FY13	FY14E	FY15P
Program	197	232	238	242
IDA Share	65%	65%	64%	>60%
FCS Share*	18%	18%	19%	19%
Climate Change Share	16%	24%	25%	25%

*Projected share of AS program in FCS based on list of countries included in WB FCS list at January 2014.

B. FY15-17 PROFITABILITY DRIVERS

Table 5. Historic Income, FY09-13 (\$mn)

	FY09	FY10	FY11	FY12	FY13
Loan & fee revenue (net) ¹	694	677	719	883	954
Treasury revenue (net)	331	796	542	267	389
Dividends ²	318	292	289	288	262
Advisory Services gross-up	-	-	-	269	239
Other revenue ³	120	142	177	143	196
Controllable revenue	1,463	1,907	1,727	1,850	2,040
Total expenses (including Advisory Services)	(764)	(853)	(981)	(1,207)	(1,401)
Controllable income	699	1,054	746	643	639
Realized capital gains ⁴	1,057	1,375	1,050	2,117	1,001
Realized Income	1,756	2,429	1,796	2,760	1,640
Loan loss provision	(438)	(155)	40	(117)	(243)
Write-downs ⁵	(1,066)	(206)	(220)	(719)	(487)
Fair Value adjustments and other unrealized gains (losses) ⁶	47	(122)	563	(266)	440
Income before grants to IDA	299	1,946	2,179	1,658	1,350
Grants to IDA	(450)	(200)	(600)	(330)	(340)
Less Loss (gain) Attributable to Non-controlling Interests	-	-	-	-	8
NET INCOME (LOSS)	(151)	1,746	1,579	1,328	1,018

¹ Interest income from loans and "loan-like" debt securities; financial and commitment fees net of funding cost;

² Dividend income on equity investments and "equity-like" debt securities;

³ Custody fees; service fees and other revenues;

⁴ Loans, equities and debt securities sales, realized gains on non-monetary exchanges and realized gains (losses) on derivatives;

⁵ Write-downs and "equity-like" debt securities;

⁶ Unrealized gains (losses) on loans accounted for at fair value under the Fair Value Option; unrealized gains (losses) on equity investments; Unrealized (losses) gains on debt securities accounted for at fair value under the Fair Value Option ("loan-like" and "equity-like" debt securities); unrealized gains and losses on non-trading financial instruments accounted for at fair value; unrealized gains (losses) on market borrowings; and foreign currency transaction gains on non-trading activities.

4.11 Forward-looking trends in Equity. The timing and amount of realized capital gains are extremely difficult to predict with accuracy. 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. IFC's Corporate Equity Department provided a technical briefing on the equity sales process to the Board in May 2014.

4.12 Forward-looking trends in loans. The outlook for loan income is determined through assumptions on future commitment growth, the rate of disbursement, and pricing (spreads and market rates). As noted in Section I, IFC generally looks to its stable net loan and fee revenue to cover its total administrative expenses. Historically, the average ratio of net loan and fee revenue coverage to total administrative expenses has been in excess of 1.3, providing a comfortable buffer. IFC Management expects this trend to continue.

4.13 Risk Adjusted Return on Capital. Measuring performance on loans and guarantees via non-performing loans and provisions is important to understand and manage current as well as future

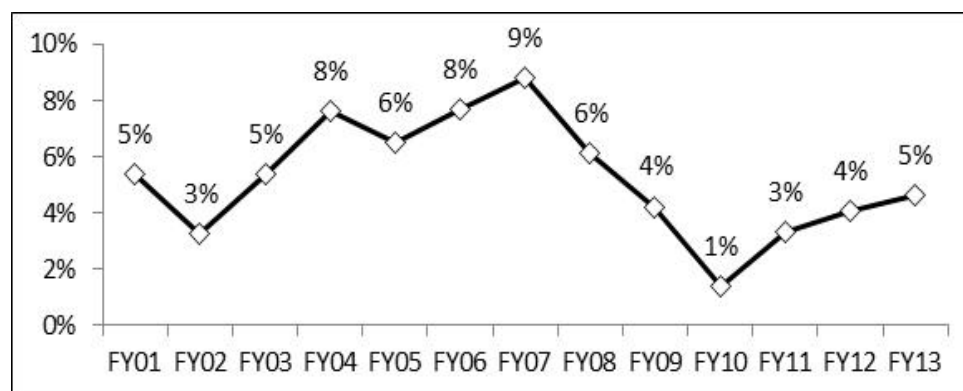
deterioration. One risk-adjusted profitability metric is the industry standard “Risk-Adjusted Return on Capital” or RAROC. As a forward-looking measure of risk-adjusted performance, RAROC represents IFC’s best estimate of the cycle-average return on the capital invested in the loan portfolio. The formula for RAROC is similar to the calculation of return on equity but includes an adjustment for expected losses in the numerator and economic capital in the denominator:

Equation 1. Risk Adjusted Return on Capital

$$\text{RAROC} = \frac{\text{Interest Income} + \text{Fees} - \text{Borrowing Costs} - \text{Operating Expenses} - \text{Expected Loss}}{\text{Economic Capital}}$$

4.14 IFC’s RAROC for senior and quasi-equity loans was 5% in FY13, in line with long-term average. This represents an increase from RAROC between 1% and 2% in FY10. Between FY01 and FY13, IFC’s loan RAROC ranged from 1% to 9%.

Chart 11. IFC Risk Adjusted Return on Capital, FY01-13, Loans & Guarantees



4.15 Over the long run, RAROC on the loan portfolio is one of the key drivers of IFC's sustainable rate of growth (along with equity returns). The return on the capital invested in loans, equity products and liquid assets drives the growth in Total Resources Available (through retained earnings), which in turn defines the sustainable rate of growth in Total Resources Required (through portfolio growth and shifts in product mix). While RAROC is not forecast for future years, it is a useful tool for examining portfolio trends and informing *ex ante* decision making on new loans. A more detailed discussion of risk-adjusted profitability and sustainable growth is to be found in the upcoming FY14 report on Financial Risk Management.

4.16 **Forward-looking trends in Syndications.** IFC’s syndicated lending program is the largest contributor to IFC’s service fees and core mobilization, generating revenue of \$28 million in syndication and administration fees from borrowers in FY13 on new syndicated commitments of \$3.1 billion and a portfolio of \$14.3 billion. IFC’s syndicated lending program has mobilized over \$46 billion from more than 500 financial institutions for over 1,000 projects since its inception in 1957.

4.17 As the loan market has evolved over time, so have IFC’s syndicated lending products and investor base. The program has traditionally arranged co-financing from commercial banks through the B-Loan product. In FY08, as a response to the financial crisis, IFC broadened its investor base to International Financial Institutions and local commercial banks through the development of the Parallel loan product. IFC negotiated a Master Cooperation Agreement with IFIs to ensure the new product could be implemented efficiently (currently 19 IFIs signatories). In FY11, IFC further developed partnerships with

insurance companies that provide unconditional guarantees on a portion of individual IFC A-Loans through a product called Unfunded Risk Participation.

4.18 In FY14, IFC is engaging with institutional investors to co-invest with IFC on a delegated basis through a new product called the Managed Co-Lending Portfolio Program. This investor type can provide the volume and long tenors that IFC's clients require. MCPP will not only increase fees from borrowers through an increased syndications volume, but IFC also charges fees to the investor to manage the funds.

4.19 **Forward-looking trends in Treasury.** Treasury expects to increase its contribution to IFC's net income over the next several years by rolling out a number of new initiatives, namely:

- a. Adding new asset classes (e.g., investing in Emerging Market Corporate Bonds, China's Interbank Bond Market, Indian Government Bond Market);
- b. Increasing the size of assets under management;
- c. Integrating its funding and investment activities to capture investment opportunities during the year; and,
- d. Achieving the lowest possible funding costs and ensuring continued market access through a more opportunistic and diversified approach (US retail market, Equity Linker).

4.20 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 as well as maintaining a prudent liquidity level. Under the three tiered investment approach introduced in FY09, Treasury follows an active management approach focusing on diversification and favorable risk adjusted outperformance.

4.21 In FY14 Treasury portfolios continued to solidly outperform their respective benchmarks. The risk-adjusted return potential increased during the year through the addition of Chinese government bonds and Emerging Market Corporate Bonds to the portfolio. In addition, the funding and investment programs have been more integrated, allowing IFC to capture attractive investment opportunities during the year. Overall, the portfolio continues to be well-positioned.

4.22 New initiatives as well as the projected increase of the portfolio will enhance the returns on a sustainable basis. Some of IFC's invested portfolios have seen a substantial increase in valuation, and further upside potential is somewhat limited. The new initiatives will most likely more than compensate for lower projected returns in the rest of the portfolio.

4.23 In addition, Treasury will continue to support the development of capital markets through first time issuances in selective emerging markets, increasing awareness of socially responsible investments through issuance of SRI-themed bonds and promoting Emerging Market Corporate Bonds in local currencies as an asset class. Treasury will continue to serve its core mandate to safeguard IFC's financial resources and triple-A credit ratings. Through prudent asset liability management, funding management, and liquid asset management, Treasury will continue to ensure that IFC has the funds it needs to invest in the private sector of developing countries and at the same time ensure it has sufficient liquidity to navigate the uncertain financial markets. Overall, Treasury activities will involve closer links with IFC's Investment Services (e.g., in cross-VPU steering groups and the Institutional Investors Engagement Group), yielding better client coverage.

4.24 **Advisory Services sustainable funding model and IFC contribution in FY15.** 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 (Table 6). A key part of recent and

ongoing AS reforms has been to further strengthen the sustainability of the AS funding model while providing integrated investment and advisory development solutions, yielding better value for IFC's clients and better returns for IFC. For example, recent analysis by the World Bank's Development Economics team indicates that IFC's internal rate of return is, on average, five percentage points higher for its equity investments when AS is part of IFC's engagements with these clients. FY14 highlights of the evolving AS funding model include:

- a. **FMTAAS mainstreaming.** As approved as part of IFC's FY12 Business Plan & Budget, IFC Management has been working to partially mainstream 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, involving \$20 million, with claims on FMTAAS reduced accordingly.
- b. **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. During FY14, staff received additional guidance and training to strengthen consistency in applying the policy.
- c. **Donor contributions.** Robust donor commitments continue, including new partnerships with Goldman Sachs Foundation and Hungary's Export-Import Bank.
- d. **AS financial management systems and processes.** In FY14, IFC rolled out the first phase of the new AS Financial Management System, in partnership with the World Bank, which will significantly enhance IFC's ability to monitor and report on AS business.

4.25 Consistent with the sustainable funding strategy and the proposed consolidation of AS spending as part of the reorganization, it is proposed that IFC contribute \$143 million to AS in FY15, or 37% of projected total AS spend. Following implementation of the second phase of FMTAAS mainstreaming, the bulk of IFC's contribution in FY15 will be almost equally divided between FMTAAS (\$63 million) and IFC's Administrative Budget (\$59 million). The remaining \$21 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 (see Table 6).

Table 6. Advisory Services Leveraging and Mainstreaming IFC's Contribution, FY12-15P

	FY12		FY13		FY14E		FY15P	
	\$mn	%	\$mn	%	\$mn	%	\$mn	%
Donors and Clients	207	57	231	59	244	61	247	63
Donors (estimated)	181	50	203	52	212	53	211	54
Clients (estimated)	26	7	28	7	32	8	36	9
IFC All Sources	158	43	161	41	156	39	143	37
FMTAAS	95*	26	100*	26	73	18	63	16
Admin Budget	40	11	39	10	60	15	59	15
Other IFC Sources**	23	6	22	5	23	6	21	6
Total	365	100	392	100	400	100	390	100

*Includes amortization of accounting credit resulting from transition adjustment made in FY12. This transition adjustment is expected to be amortized by the end of FY15.

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

Note: Recent and on-going financial management system enhancements will enable better delineation between donors and clients funds.

V. FY15 IFC Budget

A. NEW IFC BUDGETING PROCESS

5.1 IFC Management approached the FY15 planning cycle with three goals: (i) maintain and improve IFC's ability to deliver value to its clients; (ii) cap total resource usage at a flat real rate, leveraging Expenditure Review savings and other productivity gains to free resources for reallocation; and, (iii) make the planning process itself more efficient.

5.2 Historically, IFC's strategy process has been followed by detailed, department-level budget requests for both mainstream activities and special initiatives, building from a base case of the previous year's adjusted budget. This consumed a great amount of time from staff members across the organization and was followed by prolonged IFC Management meetings to discuss the trade-offs involved in each request. While this enabled a high degree of bottom-up input, re-allocations tended to be incremental and did not bear out the administrative costs of the exercise.

5.3 FY15 looks to be a transitional year with changes both to organizational structure and delivery models. In particular, the new SCD/CPF/Joint Implementation Process and IFC's evolving role in it will require an unprecedented amount of flexibility and continual deliberation. As such, IFC Management decided to utilize the departments' strategy submissions to inform centralized decisions about broader resource allocation without the previous intermediate step. This considered approach will ensure that basic operations are funded while enabling the new structure to take hold and preserving the ability to shift resources as country strategies and conditions on the ground unfold throughout the year.

5.4 Going forward, the WBG institutions will work together increasingly closely throughout the planning and budgeting process, including aligning treatment of 'below the line' budget items. Budget preparation for FY16 will see a more efficient, generalized nominal approach across all institutions while maintaining their respective strengths and addressing their unique business models.

B. TOTAL ADMINISTRATIVE BUDGET

5.5 Within the flat \$1.46 billion envelope (real) of Total Resources, IFC's Management proposes a Total Administrative Budget of \$939.3 million (\$952.6 million on nominal basis), shown in Table 7, for approval in Section VI of this paper. This amount represents a \$6.3 million (0.7%) real increase and a \$19.6 million (2.1%) nominal increase over the FY14 TAB of \$933.0 million. The proposed FY15 real budget reflects no increase in Regular Administrative Budget. Rather, the TAB real increase is largely comprised of an additional \$5.5 million to IFC's Corporate Secretariat & Board, which reflects a new ratio for calculating each WBG institution's share of the Board costs, net of estimated Expenditure Review savings. The TAB real increase also includes \$1.0 million more for IFC's Contributions to Staff Retirement Plans, which is driven by increased headcount. Although TAB is proposed to increase by \$6.3 million on real basis, this increase will be offset by reductions in planned resource use by Advisory Services (see Table 11). IFC's considerable efforts to manage costs and reallocate in various areas will allow it to accommodate these unavoidable cost increases in TAB without increasing its total resource usage on a real basis (See Table 10).

Table 7. Total Administrative Budget (\$mn)

	FY13 Actuals	FY14 Restated Budget*	FY15 Real Budget	FY15 Nominal Budget	Real \$ Δ Over FY14	% Δ Over FY14	Nominal \$ Δ Over FY14	% Δ Over FY14
Regular Administrative Budget**	692.8	751.6	751.6	761.9	0.0	0.0%	10.2	1.4%
Corporate Secretariat & Board	19.5	18.3	23.8	24.2	5.5	30.1%	5.9	32.4%
Independent Evaluations Group (IEG)	6.5	7.0	6.8	6.9	-0.2	-3.0%	-0.1	-1.3%
Contributions to Staff Retirement Plans	123.8	156.0	157.0	159.6	1.0	0.6%	3.6	2.3%
Subtotal 'Below the Line'	149.8	181.3	187.6	190.7	6.3	3.5%	9.4	5.2%
Total Administrative Budget	842.6	933.0	939.3	952.6	6.3	0.7%	19.6	2.1%

*Including FY14 Partial FMTAAS Mainstreaming Phase II of \$20.5 million

**Totals may not add due to rounding.

5.6 Regular Administrative Budget. RAB is the benchmark used to measure discretionary budget growth as it excludes “Below the Line” items that are deemed not under the direct control of IFC Management. IFC proposes to keep RAB flat at \$751.6 million in real terms (+1.4% in nominal terms). However, it is important to note that the flat real budget does reflect strategic reallocation of potential RAB-related savings.

5.7 Budget versus spending. Prudent financial management requires IFC to maintain a safety margin between the Board-authorized budget and IFC’s actual level of spending. Without this margin, unexpected cost swings could cause IFC to inadvertently overspend its annual budget. To ensure against this possibility, IFC Management aims to keep spending below IFC’s total spending authority, which comprises the administrative budget plus the carry-forward from previous year’s underspending. In FY14, spending continues to be closely monitored and is expected to be in a range of 97-99% of the administrative budget and 92-94% of total spending authority (administrative budget plus 5% carry-forward).

5.8 Administrative Budget by Cost Category. Table 8 provides the indicative breakdown of the administrative budget by cost category. Budgets are fungible and subject to analysis and strategic reallocation throughout the fiscal year, so the actual composition of spending by cost category may vary. The FY15 budget is, therefore, an estimated breakdown that will be analyzed and amended as necessary in early FY15, when complete cost data for FY14 is available. The estimate changes the balance between fixed (76%) and variable costs (24%) by only 1% within the regular administrative budget through focused cost management. Similarly, the relative share of each cost category is expected to change in FY15, with staff costs accounting for 61% of the regular administrative budget.

Table 8. Administrative Budget by Cost Category (\$mn)

	FY13		FY14		FY15			
	Actual Expenses	As % of RAB	Restated Budget*	As % of RAB	Real Admin. Budget	As % of RAB	Nominal Admin. Budget	As % of RAB
Fixed Expenses	537.5	78%	565.4	75%	570.2	76%	578.1	76%
of which:								
Staff Salaries and Benefits	427.3	62%	459.3	61%	459.2	61%	466.3	61%
Communications and IT	29.3	4%	22.1	3%	23.1	3%	23.4	3%
Depreciation	44.2	6%	46.1	6%	49.6	7%	49.6	7%
Equipment and Building	36.7	5%	37.9	5%	38.3	5%	38.8	5%
Variable Expenses	155.3	22%	186.2	25%	181.4	24%	183.8	24%
of which:								
ST. Consultants and Temps.	17.0	2%	20.7	3%	19.8	3%	20.1	3%
Travel Costs	38.6	6%	41.1	5%	33.1	4%	33.5	4%
Representation, Hospitality and Food	1.3	0%	1.6	0%	1.6	0%	1.6	0%
Contractual & Other Expenses**	98.4	14%	122.8	16%	126.9	17%	128.6	17%
Regular Administrative Expenses (RAB)	692.8	100%	751.6	100%	751.6	100%	761.9	100%
Other Expense Items:	149.8		181.3		187.6		190.7	
Independent Evaluation	6.5		7.0		6.8		6.9	
Corporate Secretariat & Board	19.5		18.3		23.8		24.2	
Contribution to SRP, SSRP, & RSBP	123.8		156.0		157.0		159.6	
Total Administrative Expenses (TAB)***	842.6		933.0		939.3		952.6	

* FY14 restated budget after Partial FMTAAS Mainstreaming Phase II and WBGIS transfers

** Contractual & Other Expenses include service and support fees

***Totals may not add due to rounding

5.9 Table 9 9 provides further details of the RAB staff cost component. The budget for total staff cost is expected to stay flat from FY14 to FY15 in real terms and increase by 1.5% in nominal terms. The budget for HQ salary cost is expected to decrease by 3.2% in real terms in FY15 while the Country Office component is expected to increase by 7.1% in real terms, reflecting the focus on selective new hiring in the field, and the full year impact of the transfer of staff to WBG Integrated Services.

Table 9. Staff Costs (\$mn)

	FY13 Actual	FY14 Restated Budget*	FY15 Real Budget	FY15 Nominal Budget
Headquarters Staff	208.6	225.6	218.3	223.2
Country Office Staff	68.4	71.6	76.7	76.4
Benefits	150.9	162.1	164.2	166.7
Total Salary & Benefits	427.9	459.3	459.2	466.3

*FY14 restated budget after Partial FMTAAS Mainstreaming Phase II and WBGIS transfers

C. TOTAL RESOURCES NEEDED FOR FY15

5.10 IFC's financial sustainability imperative (see Section IV) supports its alignment with the WBG institutions in incorporating all types and sources of spending (i.e., not just TAB) into its budget discussion; WBG Chief Financial Officer Bertrand Badré is leading this shift. The FY15 \$1.46 billion Total Resources (real) baseline is composed of \$0.94 billion in TAB for which IFC is seeking Board approval plus \$0.52 billion in other sources of funds (donor funding, FMTAAS, client fees, etc.) which IFC plans to use as an extension of resources needed to fulfill its strategic objectives. The increase in TAB, spending against client fees, and other categories for FY15 will be offset by reductions in planned resource use by Advisory Services.

Table 10. IFC's Total Resources (\$mn)

	FY13 Actuals	FY14 Restated Budget	FY15 Budget Real	FY15 Budget Nominal	Variance Nominal FY15 v FY14
Total Administrative Budget	842.6	933.0	939.3	952.6	19.6
<i>o/w Regular Administrative Budget</i>	<i>692.8</i>	<i>751.6</i>	<i>751.6</i>	<i>761.9</i>	<i>10.2</i>
<i>o/w 'Below the Line Items'</i>	<i>149.8</i>	<i>181.3</i>	<i>187.6</i>	<i>190.7</i>	<i>9.4</i>
IFC Contributions to Advisory Services (other than admin. budget)	122.4	97.6	83.7	83.7	(13.9)
Funding Mechanism for Technical Assistance and Advisory Services	100.4	73.4	63.0	63.0	(10.4)
Performance Based Grants Initiative	10.5	11.5	10.0	10.0	(1.5)
IFC SME Ventures -Advisory Services	0.8	0.5	0.5	0.5	-
Trust Fund Administrative Fees	10.7	12.2	10.2	10.2	(2.0)
Donor/Client Contribution to Advisory Services	229.5	260.8	247.2	247.2	(13.6)
Expenses associated with IFC's Treasury & Portfolio activities	16.3	16.9	20.9	20.9	4.0
Borrowing Expenses	2.9	2.8	2.8	2.8	-
Custody and Settlement Costs	10.4	10.5	14.0	14.0	3.5
Structured and Securitized Products	0.2	0.2	0.2	0.2	-
Equity Transaction Costs	2.7	3.4	3.9	3.9	0.5
Expenses offset by fee income	109.0	130.5	147.7	147.7	17.3
Client Fee (includes reimbursables and service fees)	70.5	80.7	80.7	80.7	-
Privatization Fees	1.8	-	-	-	-
Syndicated Loan Management	3.7	4.3	4.4	4.4	0.1
Managed Co-Lending Portfolio Program	-	-	2.4	2.4	2.4
Treasury & Capital Markets Innovation Programs	-	-	7.5	7.5	7.5
Asset Management Company Fees	16.7	22.7	23.5	23.5	0.9
Asset Management Company Reimbursable	10.0	11.9	16.2	16.2	4.3
The Climate Change Program	-	0.6	0.7	0.7	0.1
Global Agriculture and Food Security Program	1.5	2.3	2.3	2.3	(0.0)
Global SME Financing	-	0.8	1.1	1.1	0.3
Women Entrepreneurs Opportunity Facility	-	-	0.8	0.8	0.8
GEF Earth and Catalyst Fund	-	0.1	0.1	0.1	-
Climate Investment Funds	-	1.2	1.1	1.1	(0.1)
Special Initiatives	7.9	9.9	9.9	9.9	(0.1)
Infra Ventures	4.2	5.0	5.0	5.0	-
IFC Post-2012 Carbon Facility	0.0	1.0	0.6	0.6	(0.5)
PBGI-Access to Infrastructure	0.2	-	-	-	-
IFC SME Ventures - Grants	2.7	3.1	3.5	3.5	0.4
Environmental/Social Mediation and Conflict Resolution	0.8	0.8	0.8	0.8	-
Jeopardy Expenses	4.1	12.0	12.0	12.0	-
Carry-forward of Unspent Budget from Previous Fiscal Year	-	42.5	46.6	46.6	4.1
IFC's Total Resources (including Carry-forward)	1,331.8	1,503.2	1,507.3	1,520.6	17.5
IFC's Total Resources (excluding Carry-forward)	1,331.8	1,460.6	1,460.6	1,474.0	13.3
<i>o/w</i>					
Investment, Treasury & Support Services	789.5	861.8	883.0	892.3	30.5
Advisory Services	392.5	417.5	390.0	390.9	(26.6)
"Below the Line (Corp. Sec. , IEG, Staff retirement Plans)"	149.8	181.3	187.6	190.7	9.4

Totals may not add due to rounding

5.11 **Advisory Services.** As indicated in paragraph 4.25, IFC Management proposes to set FMTAAS annual spending authority at \$63 million in FY15. Absent further designation of IFC Net Income to FMTAAS, this would reduce the FMTAAS fund balance to \$63 million (see Table 11). IFC Management will make a recommendation to the Board on future designations to FMTAAS in the FY14 Net Income Allocation Paper.

Table 11. FMTAAS Designations vs. Annual Spending Authority, FY05-15P (\$mn)

	FY05-11	FY12	FY13	FY14E	FY15P
FMTAAS Designation from Prior FY Earnings	860	69	80	-	tbc
Re-designation from PBGI to FMTAAS	5	-	-	-	-
FMTAAS Spending	(648)	(67)*	(100)	(73)	(63)
Resulting FMTAAS Cushion (Year-end)	217	219	199	126	63**

*FY12 FMTAAS spend includes a credit of \$27 million resulting from a change in accounting policy. This transition adjustment is expected to be amortized by the end of FY15.

**FMTAAS Cushion of \$63 million at end of FY15 would result in the absence of any designation of FY14 Net Income to FMTAAS.

5.12 **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.

5.13 **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.

5.14 IFC plans to increase its use of fees to offset expenses by \$17.3 million (13%) in FY15, including extending the use of fees to two new programs in FY15: (i) the Managed Co-Lending Portfolio Program, and (ii) Treasury and Capital Markets Innovation. Combined, these account for 57% of the FY15 expected fee usage increase. The entire increase will be offset by a countervailing decrease in spending on Advisory Services.

5.15 **Special Initiatives.** IFC is not requesting additional budget for any new special initiatives in FY15, but it does plan to continue funding four existing special initiatives (IFC InfraVentures, IFC SME Ventures - Grants, IFC Post-2012 Carbon Facility, and Environmental/Social Mediation and Conflict Resolution). InfraVentures, which represents the majority of that with \$5.0 million, was established in FY08 and

renewed in FY13 to help increase the number of private and PPP 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.

5.16 Through end of March 2014, IFC InfraVentures has invested \$63.6m representing 26 project development investments in IDA countries. In the first half of FY14, IFC InfraVentures committed two projects, a hydropower project in Cameroon (the largest IFC InfraVentures commitment to date) and a hydropower project in Nepal (IFC InfraVentures' first \$1.0 billion project and second investment in Nepal). IFC InfraVentures program is actively engaged in project development activities, with a strong pipeline in various stages. IFC InfraVentures spending for FY14 is estimated to be modestly below FY14 budget of \$5.0 million due to delay in new hires for the program. IFC InfraVentures spending for FY15 is estimated at \$5.0 million, for which Board approval is being sought.

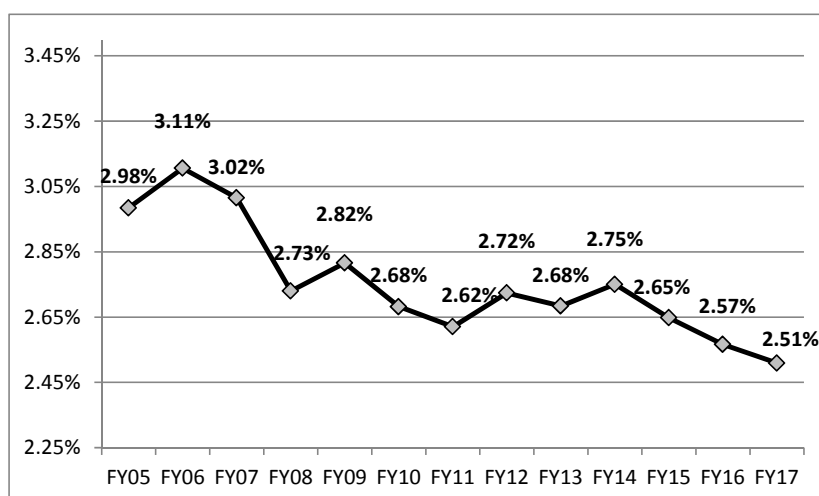
5.17 **Jeopardy Expenses.** IFC designates a project as a jeopardy case when the prospects for recovery of IFC's investment are in serious doubt due to expected loan defaults, country/industry considerations, stock market factors, or other factors as determined by the Management Team. The restructuring 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 FY15 is a stable \$12 million, which should allow sufficient flexibility in the event of stress on IFC's portfolio.

5.18 **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 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.

5.19 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.

5.20 **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 remain flat in real terms (increasing only by 0.9% with the price factor). IFC has traditionally shown RAB as a percentage of committed IFC own account 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, and expenses covered by fee revenue, as well as "below-the-line" items.

Chart 12. Total Resources as a percentage of IFC Own Account Committed Portfolio, FY05-17P



5.21 Total expenses as a percentage of IFC own account committed portfolio declined by 16% from 2.98% in FY05 to 2.68% in FY13, and are expected to decline further over the next three years, given IFC's projected portfolio growth in FY15-17 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. It should be noted that this ratio is over-stated as the numerator takes Advisory Services expenses into consideration and the denominator does not account for the assets under IFC's management from (i) third-party investment mobilization or (ii) the Advisory portfolio, parts of which are increasingly integrated into IFC's reorganized delivery model. Going forward, IFC will explore the most effective ways of integrating these amounts into its metrics, resulting in a more holistic view that better captures IFC's efficiency.

D. CAPITAL BUDGET

5.22 IFC's capital budget funds HQ and Country Office facility needs as well as the investment in Information Technology necessary to support its unique business model. For FY15, the total recommended capital budget is \$83.5 million.

Table 12. FY15 Capital Budget (\$mn)

	FY13 Budget	FY14 Budget	FY15 Budget
Headquarters Facilities	4.9	3.5	7.6
Country Office Facilities	25.4	24.0	21.5
Information Technology	57.6	54.9	53.4
Contingency	1.5	1.5	1.0
Total	89.4	83.8	83.5

5.23 **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 FY15 will support organizational realignments while continuing the annual capital improvements required to keep an aging building functioning well and properly maintained. Included are critical improvements such as the replacement of the HQ building's automatic transfer switches and emergency power data center cooling system. Other notable projects are the space re-alignment due to the new organizational structure project, F-building restroom improvements, and the F-building lobby and atrium redesign to provide a more efficient use of the space. Capital investments in the F-building continue to include energy conservation measures which reduce energy and water consumption to maintain LEED PLATINUM² certification.

5.24 **Country Office Facilities.** The CO facilities budget proposal reflects IFC's continued decentralization with emphasis on cost efficiency. By the end of FY14, IFC will have 106 offices in 98 countries supporting over 2,800 individuals in the field. IFC and the World Bank are co-locating country offices wherever feasible; 75 of the 106 offices will be co-located with an estimated 4-6 more to co-locate in the next 3-5 years. As IFC's field presence has grown, new offices have been added and others have been closed to ensure that the location of staff in the field maximizes contact with and support for IFC's clients.

5.25 The new IFC building in Accra, Ghana was completed and occupied by both IFC and World Bank staff in July, 2013. Previously approved, a major project is under way to design and build a new IFC office in Dakar, Senegal at a total cost of \$22.6 million (of which \$3.0 million is proposed to be funded with a FY15 budget). The proposed overall FY15 capital budget of \$21.5 million will fund work on approximately 12 country offices. No capital is requested yet in relation to the "Buy versus Lease" opportunities identified as part of the Expenditure Review. By the end of FY15, IFC expects to have 105 offices in 99 countries, 78 of which will be co-located.

5.26 **Information Technology.** The FY15 Information Technology capital budget proposal of \$53.4 million will fund needed improvements in IFC's technology platforms to provide foundational value-added systems and data management supporting greater development impact, client focus, and productivity. The adoption of up-to-date technologies is critical to meeting the needs of a more global, mobile staff with high expectations that technology should enable them to be more productive. Mobile, cloud, data management, and social technologies help them stay connected with co-workers and clients, find the information that they need to be effective, and generally transform how they do business.

5.27 The proposed FY15 capital budget would fund two categories of investment:

- a. **Steady State (\$23.1 million).** This category focuses on IFC's established IT needs. These programs ensure the reliability of existing systems by addressing technical obsolescence and facilitating IT capacity growth necessary to accommodate IFC's operations growth. The FY15 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

² LEED (Leadership in Energy and Environmental Design) is an internationally recognized certification program that provides third-party verification that a building is designed and built using strategies aimed at reducing environmental impact and improving energy efficiency. LEED PLATINUM is recognized as the highest levels of LEED certification and is a substantial achievement for a building not originally designed with sustainable operations in mind.

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.

- b. **Systems Development (\$30.3 million).** These programs focus on the development of new or enhanced IT solutions to support IFC's business segments. They include automation of business process changes and the introduction of new business applications along with the modification of existing applications. Some are new multi-year programs, while others are the continuation or completion of programs begun in prior years. The programs to be funded in FY15 include:
- i. **Investment Operations.** Implementation of the "iPortal" – IFC's new, modern workspace for investment operations; integration with Global Practice Groups; additional funding for the new Short-Term Finance platform for managing existing and planned products; enhancements to portfolio valuation systems to improve efficiency and data quality; replacement of the disclosure portal with a more robust and scalable technology platform; and, new integrated interfaces for microfinance.
 - ii. **Advisory Services.** Integration with Global Practice Groups; new system to manage the Trust Fund pipeline and enhancements for transaction processing; and, additional funding for advanced analytics and reporting.
 - iii. **Finance and Treasury.** Financial collateral management that integrates into IFC investment, portfolio, and risk operations; automation of manual top-level accounting processes for financial reporting; automation of trade entry from Bloomberg and trade matching; additional funding for ongoing upgrades to treasury systems; new system to manage equity participation; and, improved transaction processing and reporting for donor trust fund investments.
 - iv. **Legal.** Holistic renewal of technology solutions used to manage the work of the legal practice areas.
 - v. **Risk Management.** The new Integrated Credit Risk Platform and consolidated risk reporting.
 - vi. **Information Management and Delivery.** Implementation of data structures and warehouses required to optimize data movement across IFC systems and provide robust reporting and analytics about IFC's partners, projects, and results.
 - vii. **Corporate.** Implementation of document management capabilities for all IFC records (currently only available for investment services records); and integrated technology solutions to capture and maintain partner data with improved data quality.

5.28 In addition to the above, IFC will 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. Initiatives include a new email system, a new client relationship management platform, replacement of aging cash systems, SAP financials renewal, new HR systems for recruitment and talent management, and upgrades to identity, credential, and access management.

VI. Recommendations

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

A. ADMINISTRATIVE BUDGET AUTHORITY

- i) A total administrative budget for FY15 of \$952.6 million.

B. CAPITAL BUDGET AUTHORITY

- ii) A capital budget for FY15 of \$83.5 million.

C. SPECIAL INITIATIVES

- iii) Authority to spend an additional \$5.0 million for IFC InfraVentures through FY15.

Annex 1. Indicative Volume Projections

Table 13. Long-Term Finance and Mobilization New Commitment Volume Projections, FY11-17P (\$bn)

	FY11A	FY12A	FY13A	FY14P	FY15P	FY16P	FY17P	CAGR FY14P-17P
Long-Term Finance	7.5	9.2	11	10.6 - 11.6	10.3 - 11.3	11.0 - 12.0	11.8 - 12.8	3 - 4%
Mobilization	6.5	4.9	6.5	5.2 - 6.2	5.6 - 6.6	6.1 - 7.1	6.4 - 7.4	6 - 7%
Total (LTF + Mobilization)	14.0	14.1	17.5	15.8 - 17.8	15.9 - 17.9	17.1 - 19.1	18.2 - 20.2	4 - 5%

Note: Mobilization does not include IFC-MIGA mobilization

Table 14. Short-Term Finance Volume Projections, FY11-17P (\$bn)

	FY11A	FY12A	FY13A	FY14P	FY15P	FY16P	FY17P	CAGR FY14P-17P
Average Outstandings	1.9	2.5	2.7	2.5 - 2.7	2.6 - 2.8	2.7 - 2.9	2.8 - 3.0	3 - 4%
Commitment Volume	4.7	6.2	7.3	6.3 - 7.3	6.6 - 7.6	6.9 - 7.9	7.1 - 8.1	3 - 4%

Annex 2. Adjustment for Price Increase

Each fiscal year, IFC Management proposes a nominal US dollar budget that includes an adjustment for price changes based on external price movements. The budget price adjustment covers the effects of external price increases/decreases on IFC's total administrative expenses. Following extensive discussions between the Board and IBRD/IDA Management to maintain a more accurate value of the World Bank's budget, both in US dollar and non-US dollar currencies, revisions to the price factor methodology were approved by the Board for IBRD/IDA (*R2009-0050 Price Adjustment to the World Bank Administrative Budget, April 1, 2009*). Subsequently, in June 2009, the Board approved the adoption of the same price factor for IFC (*IFC/R2009-0126/3*). Thus, IFC uses the same methodology as the World Bank; the resulting budget price adjustment is different for each institution, reflecting differences in cost structures for IFC and the World Bank.

This methodology derives a composite price adjustment factor from the following components:

- Apply the Washington appointed staff structural salary adjustment for Washington appointed staff salaries and salary related costs;
- Apply country office specific structural salary adjustments to their respective country office salary costs;
- Apply country-specific Consumer Price Index to their respective country office non-salary costs;
- Apply exchange rate adjustment to non-US dollar based costs; and,
- Apply US-Consumer Price Index to US dollar based non-salary costs.

For FY15, the overall budget price adjustment is 1.5%. The budget price adjustment results in an increase of \$10.8 million (excluding budget price adjustment of \$2.6 million for contribution to Staff Retirement Plans). The budget price adjustment is the weighted average of the adjustment for the factors mentioned above, excluding depreciation. The weights represent the respective share of these costs in the total administrative budget. The calculation of these constituent factors is explained in Table 15.

Table 15. Price Factor Adjustment Components

Component	Price Adjustment Factor	Weight	Description
Washington appointed staff salaries and salary-related costs	2.3%	42%	Based on IFC Management's recommendation; see <i>2014 Review of Staff Compensation for the World Bank Group</i> (paper number being assigned)
Country office specific structural salary adjustments to country office salaries and salary-related costs	4.8%*	12%	Based on the 2014 set of adjustments; see <i>2014 Review of Staff Compensation for the World Bank Group</i> (paper number being assigned)
Country-specific CPI to country office specific non-salary costs	5.4%*	10%	Based on the 2013 annual increase reported in the <i>IMF World Economic Outlook, April 2014</i>
Exchange rate adjustment to non-USD based costs	(5.2)%	22%**	Based on USD equivalent of local currency expenditures using the most recent twelve month average rates (April 2013 - March 2014) and comparing it to the USD equivalent of local currency expenditures using the prior twelve month average rates (April 2012 - March 2013)
US-CPI to USD based non-salary costs	1.5%	36%	Based on the US-CPI average forecast of 2014 and 2015 annual increases reported the <i>IMF World Economic Outlook, April 2014</i>

*Before applying the exchange rate adjustment

**Exclude from total to avoid double-counting weight of non-US dollar components

In terms of implementation, IFC Management will make a detailed analysis by fiscal year-end on how to fairly make the allocations to managing units for the price increase to maintain purchasing power.