IsDB

البنك الإسلامي للتنمية

Islamic Development Bank

INVESTMENT FOR POVERTY ALLEVIATION

ECONOMIC EMPOWERMENT INVESTMENT POLICY (EEIP)

July 2020

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1. LIST OF ACRONYMS AND ABBREVIATIONS

2SMF	Two-Step Murabaha Financing
APIF	Awqaf Properties Investment Fund
DW	Development Waqf
EED	Economic Empowerment Department
EEIP	Economic Empowerment Investment Policy
EEOMC	Economic Empowerment Operations Management Committee
EFM	External Fund Manager
FCD	Financial Control Department
FPPA	Financial Policies, Planning and Analytics Department
ICIEC	Islamic Cooperation for Insurance of Investment and Export Credit
IsDB	Islamic Development Bank
ISFD	Islamic Solidarity Fund for Development
LD	Legal Department
LDMC	Least Development Member Country
MSMEs	Micro Small and Medium Enterprises
OCR	Ordinary Capital Resources
RMD	Risk Management Department
SC	Shariah Committee
SCU	Shariah Committee Unit
SMART	Specific, Measurable, Achievable, Relevant and Time-bound
SMEs	Small and Medium Enterprises
USD	United States Dollar

2. PREFACE

2.1 MANDATE, NATURE AND PURPOSE OF THIS POLICY

2.1.1 This Economic Empowerment Investment Policy (EEIP) provides guidance on the execution of Economic Empowerment policies and operations. The resources for investments in Economic Empowerment operations are derived from various sources including the Development Waqf of the Islamic Solidarity Fund for Development (The 'ISFD') as well as other sources including OCR and Trust Funds provided by other donors. The Economic Empowerment Portfolio assets managed by IsDB or any external managers on behalf of IsDB shall be governed by this policy and separate agreements signed with the relevant parties. This document aims to provide a policy framework which aids the supervision of the investments. Simultaneously, this policy framework seeks to encapsulate a robust structure for controlling the detailed operational and administrative aspects of the Economic Empowerment Portfolio.

2.1.2 Unlike usual policies that focus on capital markets investments, this policy provides guidance on making Investments for Poverty Alleviation- Investing in the Poor and for the Poor. Unlike making investments in capital market instruments, investments through Economic Empowerment aim to achieve double-bottom line returns. Financial returns will be measured in conjunction with development impact through such investments.

2.1.3 The investment policy also guides how Economic Empowerment Programs, Institutions, Funds and Institutions are processed and through the Economic Empowerment Operations Management Committee by the EDD in collaboration with other units within IsDB leveraging on resources from the ISFD Development Waqf Capital, OCR, ISFD Loans and trust funds managed by IsDB.

2.1.4 Managing a fund is a long-term responsibility given its perpetual nature and long- term role in economic empowerment of the poor. The policy will need to balance the financial returns while ensuring that developmental targets like poverty alleviation and employment creation are met. The EEIP should be reviewed every three years by EED annually to ensure that it continues to be relevant and reflective of the investment climate and opportunities. More frequent reviews shall be undertaken whenever a need arises as when there are material changes in systems, business processes, operating procedures or structural changes in market conditions.

2.1.5 All personnel carrying out Economic Empowerment investment activities should ensure that they comply with the requirements of this policy. The policies outlined in this document are mandatory and must be adhered to by all departments or parties involved in controlling and supporting investment activities related to Economic Empowerment.

2.2 STRUCTURE OF THE ECONOMIC EMPOWERMENT INVESMENT POLICY

2.2.1 This policy defines the objectives of the Economic Empowerment and the means of achieving those objectives, including the responsibilities of stakeholders and guidelines under which the investment activities operate. Specifically, this policy is structured as follows under the following key sections:

- ***Investment Governance*** - This section identifies key personnel, departments and committees involved in the investment process for Economic Empowerment interventions, their responsibilities as well as the delegation of responsibilities related to the management of funds depending on the source of funds (ISFD Development Waqf Capital , OCR, Trust Funds from other donors);
- ***Investment Objectives*** - To describe the expectations of the Economic Empowerment Portfolio (namely, the return objective, time horizon and risk tolerance);
- ***Investment Strategy*** - To describe the investment strategy of the Economic Empowerment Portfolio including the Strategic Asset Allocation;
- ***Investment Performance Management*** - To describe procedures governing the monitoring and evaluation of the investment performance of the Economic Empowerment portfolio at the overall level;
- ***Investment Risk Management -*** To establish a general framework for the risk management of the investment program
- ***Other Policy Matters***

3. INVESTMENT GOVERNANCE

3.0.1 The respective responsibilities of the committees, departments and parties involved in the overseeing and implementation of this policy are as follows:

3.1 KEY COMMITTEES

Board of Directors

3.1.1 The Board of Directors (BoD) has the responsibility for supervising management, providing overall oversight and guidance on the financial and social returns achieved from investments made through ISFD Development Waqf Capital. The BoD has delegated the implementation and on-going monitoring of the investments to the IsDB Preisdent through the Board Resolution number ISFD/BoD/23/2/019/(64)/6. The IsDB BED will review and approve projects that are financed from OCR resources unless the approval authority has been delegated to IsDB President.

Economic Empowerment Operations Management Committee (EEOMC)

3.1.2 The Economic Empowerment Operations Management Committee will manage the operationalization of Economic Empowerment activities deriving on funds from OCR, ISFD income, ISFD Development Waqf Capital and Trust Funds. This includes reviewing, appraising and approval of projects and programs that are guided through this investment policy. The role of the EEOMC is as follows:

- Provide oversight and guidance on the execution of the Economic Empowerment policies, and operations;
- Review and clear Economic Empowerment Department's three-year strategic plans;
- Review and clear Economic Empowerment Department's Annual Work Plans and budgets;
- Review Economic Empowerment Department's performance reports on semi-annual basis;
- To propose and review a fit-for-purpose Investment Policy for Economic Empowerment;
- To review and clear the proposals of new Economic Empowerment Operations for processing investments as per the DOA; and
- To review the financial performance of Economic Empowerment's portfolio and advice on performance enhancement measures.

Shariah Committee

3.1.3 In line with the overall IsDB's investment activities, all investments are guided by rulings of the Shariah Committee (SC) of the IsDB, which composes of leading Shariah scholars. The SC sets the guidelines to ensure that investments are compliant with the Islamic Shariah principles.

3.2 KEY DEPARTMENTS & PARTIES INVOLVED

Islamic Solidarity Fund for Development Unit:

3.2.1 As one of the donors for Economic Empowerment, the ISFD is responsible for the allocation of ISFD funds to EE Projects and managing the approval process with its board of directors whenever required. Its role is pertaining to the management of ISFD resources include the following:

- serve as a focal point for all matters related to ISFD resources;
- obtain approval from the concerned authority;
- conduct supervisory oversight over the investment of Development Waqf capital including EE by the Different Units and Departments managing the capital of the Fund.

Economic Empowerment Department:

3.2.2 The EED is overall responsible as the convener of the EEOMC. Their roles pertaining to the management of ISFD Development Waqf Capital include the following:

- Serve as a focal point and 'Centre of Excellence' for all matters related to Economic Empowerment in IsDB.
- Manages and implements investments relating to Economic Empowerment under the ISFD Development Waqf Capital allocation.
- To provide expertise and support to the ISFD relating to its management of the ISFD Development Waqf Capital.

- Fulfill responsibilities and invest assets as defined in this Policy;
- Recommend investment strategy and strategy implementation (transactions) to EEOMC and President;
- Implementation of investment strategy, including implementing decisions from EEOMC and President;
- Review and recommend investment procedures to EEOMC;
- Review and recommend short-term policy exceptions (guideline breaches) to the Chairman, EEOMC;
- Recommend third-party service providers (EFM, consultant, etc) for Chairman EEOMC's approval;

Financial Policies, Planning & Analytics Department (FPPA) (middle office)

3.2.3 FPPA is the department in charge of OCR financial policies within IsDB. Hence, their roles pertaining to the Economic Empowerment investment policy Include the following:

- Supports the development of investment policy statement of the Fund as long as it is managed internally.
- Monitor compliance of treasury operations with approved limits; report non-compliance to IsDB concerned committee

Risk Management Department (RMD)

3.2.4 The RMD plays an important role in managing the risks of deploying funds managed by IsDB are well-managed. They roles and responsibilities include:

- Review and contribute to changes to this policy
- Review and contribute to investment strategy implementation (transactions)

Shariah Compliance Unit (SCU)

3.2.5 The SCU provides guidance and supervision in ensuring that the transactions made are Shariah-Compliant and are in line with the resolutions of the Shariah Committee.

- Review and clear Shariah guidelines of investment recommendations
- Provide Shariah guidance on the structuring of investment opportunities to be entered
- Recommend external Shariah advisors/consultant

Legal Department (LD)

3.2.6 Helps and advises the business functions on legal related matters

Financial Control Department (FCD)

3.2.7 Responsible for the accounting and reporting of the investment activities (i.e. disbursements, dividends, recording changes in fair value of investments).

3.3 OUTSIDE SERVICE PROVIDERS

External Fund Managers

3.3.1 External Fund Managers (EFMs) may be retained to implement this policy. The EED shall monitor the performance of and supervise all EFMs.

- To qualify for selection by EED, the EFMs will have demonstrated expertise with the type of portfolio in their charge.
- Proven track record in managing relevant portfolio
- The EFMs will be provided explicit written instructions detailing their assignment and will construct and manage the portfolio consistent with this policy.

External Advisor/Investment Consultant

3.3.2 External advisors or investment consultants may be retained to help implement this policy, provide independent input and feedback on various issues, and make recommendations as appropriate.

3.4 DELEGATION OF AUTHORITY

3.4.1 All business relating the implementation of this policy should be governed by the operative DoA of the IsDB.

4. INVESTMENT OBJECTIVES

4.01 The Economic Empowerment initiatives complement IsDB, ISFD and Trust funds mandate to achieve the overall following objectives:

- Fighting poverty & hunger and promoting pro-poor growth;
- Providing financial support to enhance the productive capacity and sustainable means of income generation for the poor;
- Emphasizing human development, especially reducing illiteracy and eradicating diseases/epidemics

4.0.2 Inspired by the concepts of Social Impact Investing through Islamic Finance, The ISFD Development Waqf Capital resources, OCR resources and Trust Fund resources aim to achive both developmental and financial returns on the medium and long term. Below are the main objectives guiding the investments through the implementation of Economic Empowerment initiatives.

4.1 RETURN OBJECTIVE

4.1.1 The investment return objective of the Economic Empowerment programs, initiatives, funds and institutions are to achieve both financial and developmental impact return in the medium and long term.

4.2 FINANCIAL RETURN

Financial Return of the ISFD Development Waqf Capital

4.2.1 The investment objective is to ensure maximum returns to support poverty alleviation while taking mitigating risk measures in ensuring capital protection. The aim is to enhance the developmental impact of deployed funds while ensuring that the financial returns of the funds are not reduced. Hence, for the ISFD Development Waqf Capital the hurdle rate that is expected will be benchmarked the average income earned from the other portfolio of ISFD's cash waqf (2018 actual return is 3.04%). ISFD will share 50% of any income generated beyond the hurdle rate declared each year to initiatives that would enhance the operations of the ISFD Development Waqf capital as specified in the Spending policy. The other 50% will be maintained as income smoothening savings that would be allocated to the ISFD capital preservation account to ensure that in the years that the fund may not achieve the expected returns, the savings will be used provide the adequate returns to ISFD.

4.2.2 Total Return is the sum of all profits and dividends generated and realized or unrealized gains or losses less of all costs, fees and currency exchange fluctuations. The Economic Empowerment Department is proposed as a fund manager of the Economic Empowerment Initiatives of the ISFD Development Waqf capital allocation. Hence, taking 2018 as the benchmark, the target investment return hurdle rate in 2019 is **3.04%.** If the fund achieved **4.04%:**

- 3.04% will be used for ISFD concessional loans to IsDB Member Countries
- 50% will be used to enhance the ISFD Development Waqf Capital allocation operations as per the Spending policy;
- 50% will be saved to ensure that there is sufficient returns to make up any deficit of income in the future through the ISFD capital preservation fund

4.2.3 Each asset class will have a primary benchmark and target allocation. Each asset class is a type of operation aimed at generating a target financial and socio-economic developmental return. The target allocation specified for each asset class will be reviewed and reconfirmed regularly.

4.2.4 There should be active management of the portfolio. EDD is expected to add value and meet target returns as established and in line with the rules and regulations for the Standards of Performance of this Investment Policy. EDD is to pro-actively look out for investment opportunities, within the approved asset class allocation that could enhance the ISFD Development Waqf Capital allocation portfolio.

4.2.5 The fund will only be invested, according to the tenets of Islamic Shariah. Investments can only be made in Shariah-compliant investment products and/or other funds that are Shariah-compliant.

4.2.6 If ISFD require certain investments be made in specific sectors, countries or products, they shall fall outside this policy. These restrictions shall be observed unless they go against Shariah principles or stipulate investing in products that are not Shariah compliant.

Financial Return of OCR and Trust Fund resources

4.2.7 The financial return of OCR resources will be based on existing IsDB pricing policies while the trustee of the fund will determine the annual financial return required.

4.3 DEVELOPMENTAL IMPACT RETURN

4.3.1 Unlike making investments in capital market instruments, investment through Economic Empowerment activities aim to achieve double-bottom line returns. Financial returns will be measured in conjunction with development impact through such investments. The financial returns can be easily measured by the profits earned from the investments made by the fund. Similarly, developmental indicators need to SMART (Specific, Measurable, Achievable, Relevant and Time-bound). The different investment classes and different types of interventions can give rise to different developmental results. However, they should be measured and aggregated into overall results that can be reported by ISFD.

4.3.2 These aggregated or overall development impact has been described in ISFD's Strategic Plan into three main categories based on the three focus areas of Economic Empowerment, Education and Community Development thorough Basic Infrastructure. Details of the developmental indicators can be found in Section 6.2.

4.4 TIME HORIZON

4.4.1 Considering the nature of the Economic Empowerment investments, the tenors of the investments will be set on a medium to long term basis ranging from up to 6 to 20 years depending on investment class. In fact, Long-term responsibilities must never be sacrificed for short-term gain. Care, skill and prudence will be exercised when conducting due diligence when appraising investment opportunities under the Development Waqf allocation. The time horizon for OCR resources will be based on the approved terms and conditions of IsDB while the trustee will determine the nature of investments of their funds.

4.5 RISK TOLERANCE

4.5.1 The Investment risk tolerance for the ISFD Development Waqf Capital allocation portfolio should be diversified to mitigate any concentration risks. Investment authority limits, responsibilities and duties of all concerned stakeholders of the Fund must be observed as specified in the Investment Risk Management Section of this Policy unless approved otherwise by the EEOMC. The Position of the ISFD Development Waqf Capital will be set on a medium to long term basis and expecting to have no more than a 15% chance of the assets yielding a negative return in any given year. Considering the targeted asset classes by the Economic Empowerment Investment Policy, this threshold will be applied to the positions in the equity portfolio as well as non-sovereign backed debt investments.

4.5.2 To withstand any considerable return shortfall in the portfolio, the Economic Empowerment capital will consider the following exposure limits as guiding principle of the Investment Risk Management framework of this Policy as detailed in para 7.1.

5. INVESTMENT STRATEGY

5.1 INVESTMENT STRATEGY OVERVIEW

5.1.1 Investments under this strategy will relate to ISFD Development Waqf capital since OCR and Trust funds allocations are determined by IsDB board and the trustee respectively and is hence not covered under this section. The ISFD Development Waqf capital investments will be made under two main categories- a) Investments that are protected under sovereign guarantee; and b) Investments made through the private sector that are not covered by a sovereign guarantee. Under each investment category, there are several investment classes that target different investment assets. These investment assets will be managed by EDD or external fund managers may be engaged. Each investment class will have different programs and themes that aim to achieve different aspects of poverty alleviation.

5.1.2 The Economic Empowerment Department will play a major role in the management of several assets through the funds, institutions and programs that it is running under the theme of promoting Economic Empowerment. In addition, other relevant units within IsDB that play a significant role in poverty alleviation such as Health and Education will manage respective ISFD programs and implement the programs to meet the expected development objectives and returns based on the target return of the respective investment class. Islamic financial products will be developed with the appropriate pricing to meet the target returns of the respective investment class. This will ensure that the Waqf Development Fund will achieve the overall financial and development returns.

5.2 STRATEGIC ASSET ALLOCATION

5.2.1 The strategy of the ISFD is to obtain good financial returns with the capital invested, protecting the capital while ensuring maximum developmental impact. For example, ISFD currently invests in money markets and capital market instruments to generate a profit which would be used for developmental purposes. Hence, out of the USD 2.7 billion managed, the average actual return from the money markets from 2015 to 2018 is 2.78%. Yet, the development returns in investing in these instruments such as sukuk, stocks and treasury commodity Murabaha are not significant as such investments are targeted to large corporations and not the poor. Hence, while the higher income population will benefit from such transactions, the poor benefits to a much lesser extend giving rise to higher inequality in the country. It is targeted that the investment hurdle rate be benchmarked with the actual returns that are achieved from investments made in the capital markets. This will mean that the expected return is expected net return will be similar to the 3.08% return achieved in 2018. Investments made through Waqf Development will seek to make similar returns.

5.2.2 The strategic allocation of OCR resources will be in line with OCR guidelines and policies. Economic Empowerment Department will work with the various departments in IsDB to ensure that the interventions are coordinated to achieve maximum impact. The financial returns from OCR resources will follow pricing and the terms and conditions set by IsDB board.

Category 1: Sovereign Assets

5.2.3 ISFD typically provides ISFD Loans to LDMC and non-LDMC countries through the income generated from the investments. These Qard Hassan loans are used by IsDB to provide concessional financing to a diverse range of projects. Under the new policy of ISFD, the financing of such interventions should be focused into 3 themes: a) Economic Empowerment; b) Education; and c) Community Development and Social Infrastructure. Under the ISFD Development Waqf model, ISFD capital resources will be utilized to provide not just concessional loans but also non-concessional loans to IsDB Member Countries.

Asset Class 1.1: Non-concessional lines of financing

5.2.4 There are a lot of opportunities to channel funds to reputable financial institutions that can ensure that the funds are utilized in the manner that is being prescribed while guaranteeing a good financial return. The tenors will be designed based on the risk profile of the selected financial institutions and expected returns as well as their capacity to deploy the funds in the most effective manner.

5.2.5 IsDB/ISFD will engage with financial institutions as an agent. The role of the financial institution is to select, appraise MSMEs and utilize the line of financing in a Shariah compliant manner with the end beneficiary. Depending on the identified needs of the end beneficiaries, the line of financing can be structured in a Shariah compliant manner. As part of IsDB mandate to support MSMES through Financial institutions, lines of financing will only be disbursed upon ensuring that the financial institution has the capacity to disburse the funds in a Shariah compliant manner. To satisfy this requirement, the financial institution would need to demonstrate that it has either a) set up a Shariah panel with experts that are experienced and empowered to ensure that the financing provided is Shariah compliant; b) provide an opinion from a recognised Shariah board that the financial product that is being launched is Shariah compliant; or c) demonstrating that the financial product was developed by a consultant that is recognised by IsDB as an expert in Islamic Finance/Microfinance or d) providing the financial product to IsDB to check on its shariah compliance prior to providing its no objection. Lines of finance operations are expected to be less than 6 years including a grace/investment period of up to 18 months.

Asset Class 1.2: Sector Projects

5.2.6 IsDB provides non-concessional financing to IsDB Member Countries to finance developmental projects that are targeted to the poor and provide a sovereign guarantee for such loans. The projects are developed by IsDB Regional Hubs with support Global Practices from the Country Programs Complex. These projects are invested together with a line of finance or activity related to Economic Empowerment. The tenor of such investments are expected to be more long term with investment tenors of up to 20 years similar to the tenors provided by IsDB using its OCR resources.

Category 2: Non-Sovereign Assets

5.2.7 Besides sovereign investments, non-sovereign investments can be made in various asset classes to enhance the financial and developmental impact of ISFD. In line with ISFD's new vision to work with international and domestic NGOs, donors institutions and multilateral institutions, the financial resources of ISFD can be leveraged with its private sector partners to generate a higher impact. It is estimated that by financing non-sovereign assets, ISFD resources can be leveraged through its partners with a factor of 3 to 4 times (as per ISFD Strategic Plan).

Asset Class 2.1: Non-concessional lines of financing

5.2.8 There are a lot of opportunities to channel funds to reputable financial institutions that can ensure that the funds are utilized in the manner that is being prescribed while guaranteeing a good financial return. The tenors that will be designed will be based on the risk profile and expected returns as well as their capacity to deploy the funds in the most effective manner.

5.2.9 IsDB/ISFD will engage with financial institutions as an agent. The role of the financial institution is to appraise MSMEs and utilize the line of financing in a Shariah compliant manner (eg. Murabaha, Ijara etc) with the end beneficiary. Depending on the institution and the identified need, the line of financing can be structured in various means including Restricted Mudaraba, Wakalah and Double Murabaha. As part of IsDB mandate to support Islamic Financial institutions, lines of financing will only be disbursed upon ensuring that the financial institution has the capacity to disburse the funds in a Shariah compliant manner. To satisfy this requirement, the financial institution would need to demonstrate that it has either a) set up a Shariah panel with experts that are experienced and empowered to ensure that the financing provided is Shariah compliant; b) provide an opinion from a recognised Shariah board that the financial product that is being launched is Shariah compliant; or c) demonstrating that the financial product was developed by a consultant that is recognised by IsDB as an expert in Islamic Finance/Microfinance or d) providing the financial product to IsDB to check on its shariah compliance prior to providing its no objection. Lines of finance operations are expected to be less than 3 years including a grace/investment period of up to 6 months.

Asset Class 2.2: Funds Investment (including real estate)

5.2.10 ISFD through implementing units such as EDD may partner with strategic donors and NGOs or real estate funds to set up funds which will be co-invested as a lead or co-lead arranger. The fund manager will ensure that the funds are properly managed and be actively involved in its management and monitoring. It will ensure that the mandate of the funds that are invested are in line with the mandate of that has been agreed. The funds that have been set up can be an open-ended fund or a closed ended fund but the investments made should be for a period of up to 6 years. The investment can be renewed based on good performance of the fund manager who is able to demonstrate the financial and development achievements in the previous fund.

Asset Class 2.3: Equity Investments/Institutions

5.2.11 Direct equity participation can be made for strategic purposes that may fulfil a function beyond the profits that will be generated from the investment. This may include investment in supporting infrastructure companies such as MIS systems, consultancy companies, reputable financial institutions that may contribute to Economic Empowerment beyond distributing dividends. In addition, investments may also be made in real estate or Awqaf properties that may generate revenues for financial institutions or organizations practicing Economic Empowerment.

5.2.12 Financial institutions that have demonstrated a good track record in achieving the investment objectives can be considered for investments with expectation to exit within 10 years. The modes of exists can take various forms including Initial Public Offering, Trade Sale and Put Option to the existing shareholders. In addition, besides pure equity, investments can be made in equity-oriented instruments such as Mudarabah, Musharakah or Diminishing Musharakah. These institutions should provide a concrete proposal on how the funds will be deployed, the profit forecast and the schedule of payments to be made over the project tenor. The feasibility of the financing through value chain investments will be made by prior to approval.

5.3 ALLOCATION OF ASSET CLASSES

5.3.1 Various investment asset classes have been evaluated based on their potential to provide returns, considering the historical rates of return and relative risks associated with each. Over the long-term, the allocation among the various asset classes and the expertise to actively manage the portfolio are the main determinants of the DW Fund's performance. This policy stipulates that all assets should be made in accordance to the specified limits and targets unless specific restrictions are made by the donor funds which must be observed and would fall outside these limits. The following two tables illustrates the asset-mix, limits and targets of the various asset classes for Sovereign and Non-Sovereign investments:

Table 1: Sovereign Investments- Allocation based on Asset Classes

Asset Classes	Type of Investment/ Tenor	Target Allocation (%)	Minimum (%)	Maximum (%)
Non- Concessional Lines of Financing	Up to 6 years	25	20	30
Sector Projects (with components of Economic Empowerment)	Up to 20 years	25	20	30
Overall target allocation for sovereign investments		50	40	60

Table 2: Non-sovereign Investments- Allocation based on Asset Classes

Asset Classes	Type of Investment/ Tenor	Target Allocation (%)	Minimum (%)	Maximum (%)
Non- Concessional Lines of Financing	Up to 6 years	10	5	15
Funds investments (including real estate)	Up to 6 years	25	10	20
Equity investments/ institutions	Up to 10 years	15	10	20
Overall target allocation for non-sovereign investments		50	40	60

5.3.2 As shown in the two tables above, it is expected that about half of the investments will be made in sovereign and non-sovereign investments. The actual asset allocation will be determined based on the optimal allocation within the minimum and maximum ranges provided. Historical performance data will be used as part of the review of the Investment Management Policy when determining the optimal asset allocation targets.

5.3.3 The actual asset allocation policy is expected to have a high likelihood of meeting the objectives as outlined in Section 4 of this Investment Management Policy. The asset allocation ranges established represent a long-term perspective. As such, rapid unanticipated market shifts or changes in economic conditions may cause the asset mix to fall outside this policy range. These divergences should be of a short-term nature and should be reported to the designated authority outlined in Section 3 as part of Governance and Management.

5.3.4 The EEOMC will be responsible for re-balancing aggregate fund assets as guided by Section 5 and ensure that any divergence is as brief as possible. Products will be developed to ensure that the department will have the capacity to deliver them. A 36-month moratorium period (from the date of approval of the Economic Empowerment Investment Policy) to regularize the investment portfolio in accordance with the set thresholds; limits and guidelines.

5.3.5 This EEIP will be reviewed by the EEOMC together with FPPA on a regular basis. Suggested adjustments need to be presented to and approved by the IsDB President whom is empowered by the ISFD board to operationalize the asset allocation of the funds. The IsDB President may also authorize exceptions of application to the limits on a case-by-case, with the endorsement of the EEOMC.

5.4 REBALANCING

5.4.1 This EEIP establishes specific asset allocation targets and ranges. To ensure allocations are consistent with the policy, this section details a systematic re-balancing policy.

5.4.1 Valuation and monitoring of asset classes in relation to their targets will be done monthly and reported to EEOMC. When any asset class is not within its range, shifts will be made to bring the asset classes to within their ranges. ISFD should propose transfers between asset classes.

5.4.2 The target allocation between the asset classes (Table 1 and Table 2) should be achieved by the end of the third year (ie 2023). The EEOMC will continue to monitor the compliance of the rebalancing of the asset classes.

5.4.3 Since the investments are illiquid unlike investments in capital markets, significant efforts will be made to ensure that the allocation in the asset classes are maintained. That is the reason, the estimated variation allowed is set at 5% of the target asset allocation. However, changes may be recommended to the asset allocation based on the available opportunities to the IsDB President for approval. Alternatively, this policy may be revised to reflect the appropriate allocation of asset classes that is more relevant.

5.4.4 Investments made in equity should be maintained within the current targets if possible since due to its illiquid nature, little movement of capital can be made. The EEOMC will decide whether investments within the asset classes need to be sold to return to the policy allocation or if the target ranges need to be widened for a temporary period of time of not more than 6 months.

5.5 SPENDING POLICY

5.5.1 A spending policy utilizes the increase in principal appreciation made possible by a total return investment policy. The Fund recognizes the need for spendable income that will be used to strengthen the monitoring of the ISFD Development Waqf portfolio. The spending policy reflects an objective to distribute as much Total Return as income to ISFD to be used for ISFD loans while protecting the real value of the principle. Some of the types of expenses may include as follows:

- Consultancy expenses
- IT expenses (including MIS)
- Investments in support services
- Project design expenses
- Research and Studies
- Publication and materials
- Promotion and expansion of the Economic Empowerment/Tamkeen model

5.5.2 Consistent with the overall investment objectives, the following policies pertaining to distribution would be followed:

- Fund Management fees will be charged by EDD based on discussions with the respective donors/contributors.
- Target annual distribution rate (net of all costs, fees and currency exchange fluctuations) should be benchmarked at the income generated from other ISFD investment portfolio in money market instruments (hurdle rate).
- The income distributed to ISFD will be done upon the annual declaration of profits of the fund.
- 50% of profits above the hurdle rate should be saved as reserve funds through the ISFD capital preservation fund, unless decided otherwise by the EEOMC to ensure capital preservation as well as ensure that the returns from the ISFD Development Waqf Capital will be maintained as income smoothening savings to ensure that in the years that the fund may not achieve the expected returns, the savings will be used provide the adequate returns to ISFD.

6. INVESTMENT PERFORMANCE MANAGEMENT

6.1 EXPECTED FINANCIAL TARGET RETURN

6.1.1 The performance of the Fund will be reviewed at least annually to determine the continued feasibility of achieving the investment objectives and the appropriateness of the investment policy for achieving these objectives. It is not expected that the allocation policy will change frequently. In particular, short-term changes should not require an adjustment to the maximum commitment levels by asset class as set forth by this investment policy. In consideration of the Fund's goals and objectives, the fund will achieve the target returns (net of all costs, fees and currency exchange fluctuations) on sovereign and non-sovereign investment classes as shown in Tables 3 and 4 below:

Table 3: Sovereign Investments- Target Return

Asset Classes	Type of Investment/ Tenor	Target Allocation (%)	Target Return (%)
Non- Concessional Lines of Financing	Up to 6 years	25	3
Sector Projects (with components of Economic Empowerment)	Up to 20 years	25	3
Overall target allocation for sovereign investments		50	3

Table 4: Non-sovereign Investments- Target Return

Asset Classes	Type of Investment/ Tenor	Target Allocation (%)	Target Return (%)
Non- Concessional Lines of Financing	Up to 6 years	10	3
Funds investments (including real estate)	Up to 6 years	25	5
Equity investments/ institutions	Up to 10 years	15	5
Overall target allocation for non-sovereign investments		50	4.6

6.1.2 Table 3 and Table 4 above shows the expected annual target returns based on the various Asset Classes. Actual pricing of specific operations will defer based on the risk profile of local currency volatility with the aim of achieving the target returns of the respective investment class.

6.1.3 Returns in the above table are stipulated based on hard currency investments. If each Asset Class meets the target specified, the Fund would be expected to generate an Annual Target Return of 3.8% based on the probable scenario (Section 4.1). These performance standards will be compared against returns generated by ISFD from other portfolio investments made in capital markets and the real estate fund (APIF) to determine the performance of Waqf Development investments. The evaluation will be conducted quarterly not only with respect to the performance standards stated above but also the overall qualitative measures with respect to adherence to the Waqf Development Investment Policy. Based on the scenarios below, the fund is expected to achieve a return of 3.60% to 4.00% should the allocation of asset classes and return targets are met.

- **Probable scenario** – based on the above, if all the target allocations and returns are met, the expected return of the fund under this scenario is 3.80%.
- **Conservative Scenario** – If asset allocations which have the lowest return have the largest allocations, the expected return of the fund under this scenario is 3.60%.
- **Aggressive Scenario** – If a more aggressive approach (high allocations in higher return products) is taken while remaining within the policy, the expected return under this scenario is 4.00%.

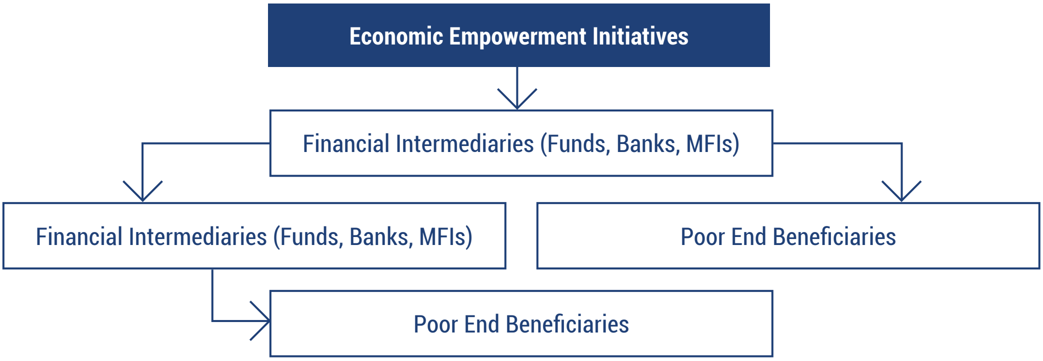
6.2 EXPECTED DEVELOPMENTAL TARGET RETURN

6.2.1 Unlike making investments in capital market instruments, investment through ISFD Development Waqf Capital resources aim to achieve double-bottom line returns. Financial returns will be measured in conjunction with development impact through such investments. The financial returns can be easily measured by the profits earned from the investments made by the fund. Similarly, developmental indicators need to SMART (Specific, Measurable, Achievable, Relevant and Time-bound). The different investment classes and different types of interventions can give rise to different developmental results. However, they should be measured and aggregated into overall results that can be reported by ISFD.

<u>No of Jobs Created for Economic Empowerment</u>

6.2.2 The Number of Jobs Created refers to the number of jobs that are benefitting from the business that receive the funding. It is estimated that for every USD 1,000 line of finance provided to a Microfinance Institution, a job is created while a job is created for every USD 6,000 line of financing provided to an Islamic Bank. To achieve the number of jobs created from Economic Empowerment initiatives, it is important that the job creation indicator is cascaded and measured to the retail financial intermediaries. The different investment classes mentioned above do provide direct investment to the poor. Waqf Development, like other interventions of IsDB typically go through financial intermediaries to make direct investments or indirect investments to other financial institutions as shown in the diagram below.

<u>Diagram 1: Economic Empowerment Inititiatives</u>



6.2.3 Based on the above diagram, the Economic Empowerment Initiatives can invest in a retail financial intermediary that will invest/ finance poor beneficiaries or it may also invest/ finance in a wholesale intermediary that will finance the retail financial intermediary that will have access to the poor end beneficiaries. Hence, the indicators that are measured by the Waqf Development Fund need to be cascaded to the retail financial intermediary to be able to measure the job creation figures.

6.2.4 Job creation figures will be measured through monitoring reports that are provided by retail financial institutions. The retail financial institutions will provide basic information including the following:

- Amount of financing provided to poor end beneficiaries (cumulative)
- Number of loans provided to poor end beneficiaries (cumulative)
- Distribution of types of assets that are being financed
- Distribution of sectors that are being financed

6.2.5 Based on the above figures, analysis on the number of jobs created can be reasonably estimated base on the following formula:

No of jobs created in a particular sector *= Number of loans provided to poor end beneficiaries (cumulative) x proportion of loans financed under the sector x average number of jobs created in the sector*

Total number of jobs created *= Total number of jobs created in all the sectors that are financed combined.*

6.2.7 The alternative means to measure job creation is by surveying every investment to determine the number of people that they have employed on a permanent basis.

6.2.8 In addition to the indicators specified under point 5.2.10, indicators pertaining to the Economic Empowerment value add will also be developed including the following:

Savings generated from choosing Islamic loan compared to conventional loan

- *Cost of conventional loan (principle + interest)- Murabaha selling price*

Percentage of savings generated from choosing Islamic loan compared to conventional loan

- *(Cost of conventional loan (principle + interest)- Murabaha selling price)/ Cost of conventional loan (principle + interest)*

Savings generated from choosing Islamic loan compared to conventional loan contributing to poverty alleviation as a result of direct negotiation

- *(Cost of conventional loan (principle + interest)- Murabaha selling price)/ financing tenor in number of days) / Poverty Line (income per day)*

Savings generated due to negotiation conducted by microfinance institution

- *Initial Spot purchase price – Negotiated purchase price of microfinance institution.*

Percentage of savings generated due to negotiation conducted by microfinance institution

- *(Initial Spot purchase price – Negotiated purchase price of microfinance institution)/ Initial Spot Purchase Price*

Savings generated that is directly contributing to poverty alleviation as a result of direct negotiation

- *(Initial Spot purchase price – Negotiated purchase price of microfinance institution)/ financing tenor in number of days) / Poverty Line (income per day)*

<u>No of Children in School</u>

6.2.9 The number of children in school measures the number of children has been enrolled due to ISFD interventions in constructing schools, providing scholarships to poor children.

6.2.10 Besides the number of students enrolled other indicators, other core sector indicators such as number of teachers and staff hired, number of teachers trained and number of class rooms built or renovated.

<u>No of Livelihoods Improved</u>

6.2.11 The number of livelihoods improved refer to the number of end beneficiaries receiving support from community development initiatives.

6.2.12 Besides the number of people benefitting from the provision of basic good or activities through community development initiatives, other core sector indicators that can be measured include number of community assets created and number of people that receive training.

7. INVESTMENT RISK MANAGEMENT

7.0.1 Considering the specific mandate of the Economic Empowerment portfolio focused on generating both Financial and Developmental Impact return, and due to the long-term horizon of its investments, the Economic Empowerment portfolio is able to withstand investments generating below average market returns as it is the case and the usual global practice for Social and Impact Investment schemes. Hence, the below Risk Framework and Limits detailing the exposure limits and Risk mitigating mechanisms were put in place to minimize any substantial risks associated with investments through the Economic Empowerment portfolio.

7.1 EXPOSURE LIMITS AND RISKS

1.1.1 The following exposure limits (per transaction) and risks must be followed when screening for initiatives must not exceed limits the following percentages.

Table 11: Exposure Risk Limits (per transaction)

Region	Exposure limit
Sovereign	US$ 50 million
Corporates	US$ 10 million
Fund	US$ 30 million or 20% of investee fund size whichever is lower
Financial Institutions	US$30 million or 10% of FI balance sheet size, whichever is lower
Country	Maximum of 15% of economic Empowerment portfolio. RMD headroom will apply for OCR financing.
Region - Africa and Latin America - MENA and Europe - Asia	Maximum 40% of fund size for each region

7.2 MITIGATION OF NON-REPAYMENT RISK

7.2.1 The following mitigation measures including guarantees will be followed to mitigate any non-repayment risks:

- Guarantees from the financial institution itself on non-repayment of loans by beneficiaries
- Financial institutions that act as agent should demonstrate a strong balance sheet and a good track record of repayment to creditors
- Visibility on the portfolio quality
- Letter of comfort from government committing that the government owned financial institution will fulfill all dues
- Third party guarantee funds set up by the government
- Third-party guarantees from other organizations/donors such as KFW, ADB, Silatech etc.

7.2.2 The EEOMC will be monitoring these investments on-ongoing basis and will leverage the EDD to monitor on a live basis the developmental impact on the ground in collaboration with the Executing Agencies and Implementing Partners. Furthermore, these Investments will be mapped and segregated into risk buckets classified by risk exposure and compared to global benchmarks with active adjustments and recalibration measures.

8. IMPLEMENTATION

8.1 STANDARDS FOR SELECTING INVESTMENTS

8.1.1 The EDD shall ensure that it selects safe and excellent Executing Agencies/Financial Institutions as dealflow for financing opportunities and that their growth and viability potential is high. It shall also devise an exit or withdrawal mechanism to derive maximum returns from its investments. Each investee will be thoroughly vetted through a comprehensive due diligence exercise. The standards for selecting investments would include (where applicable):

- study the economic, financial, social and political situation as well as the future trends of the country concerned
- Study the profitability of the financial institution based on the past 3 year audited financial statements
- study the laws and regulations and their effectiveness, especially tax regime, the judiciary and the foreign investment code
- identify the technology and information technology in use
- identify the monetary regime and movement of capital and profits
- Determine the financial and social goals to be achieved
- determine the investment/ financing duration as well as the credit worthiness of the financial institution
- determine investment/ financing risk compared to the projected return and its compatibility with the Fund's investment policy and this includes currency risks and transfer as well as credit and profit rate fluctuations risks
- Shariah compatibility or potential/willingness to be shariah compliant
- Involvement in Agriculture/value chain financing which can be enhanced through Economic Empowerment
- Check the background and expertise of the investment in the investment area concerned, the staff supporting him, the quality of the management, the manager's reputation and market standing in general

8.1.2 In addition to the above standards, IsDB Risk Assessment Criteria will be used as a guide (Annex-I). However, these guidelines will be applied with some flexibility given the likelihood that certain investments will be more social in nature through financial institutions that have the reach and expertise to reach the poor but they may not have the level of financial strength of Islamic Banks. In those circumstances, the appraisal team will highlight the criteria where the financial institution deviates from the RAC in the project documents for deliberation of the EEOMC. The approving authority will provide the needed waivers based on the recommendation of the EEOMC.

8.2 MONITORING

8.2.1 A comprehensive monitoring regime will be maintained for the ISFD. The objectives of the performance monitoring are to:

- Access the actual performance of the implementing agency based on the agreed financial and development results
- Identify issues, problems, risks relating to the implementation of the investment and help the implementing agency overcome the issues
- Upgrade the monitoring mechanisms of the implementing agencies but providing a suite of tools, manuals and IT systems to enable them to better implement the project as well as help them improve the quality of their reporting.
- Monitor milestones based on agreed action plans with the implementing agencies

8.2.2 The performance monitoring regime involves:

- Monthly and quarterly progress reports
- Dynamic reports from the supervision conducted by the Executing Agency
- Annual supervision missions conducted by EDD. At times, more frequent supervision missions may be required especially at the startup stage
- Formal review meetings, board meetings or steering committee meetings where IsDB is represented.
- Ongoing review of issues which may impact the performance of the investment portfolio

8.2.3 The achievement of the developmental objectives is paramount as it is the core objective of the investments in Economic Empowerment. The poor, refugees, youth and women without jobs are all key demographics that will be targeted by the investments. EDD will employ its tools to ensure that the investments are well managed and monitored. Some of the tools include the following:

- **Operations Toolkit:** The Economic Empowerment toolkit provide a guide on how financial institutions not only practice shariah complaint financing but also Economic Empowerment. The toolkit provides a guide on how to conduct an assessment of the organization, development of the strategy, analysis of the value chain and developing products that will economically empower the poor. It also provides a complete manual on how to perform Shariah compliant transactions.

- **Monitoring & Evaluations Toolkit:** This toolkit shows how financial institutions should measure its performance. The performance ratings are divided into three categories. Firstly, financial performance is determined on the basis of a set of financial ratios that measure the profitability and efficiency of the organization. Social indicators are also measured to ensure that the financial institution is treating their poor clients appropriately by applying the Social Performance Management framework developed by the Social Performance Task Force as well as the Client Protection Principles designed by the Smart Campaign. Last but not least, the Value Added Shariah Performance indicators will measure how much money the poor has earned or saved as a result of the intervention done by the financial institution. These indicators the depth of the intervention, measuring how much the financial institution has helped the client come out of poverty.

- 8.2.4 In addition, IT solutions for the monitoring and reporting of investments made from the Waqf Fund resources will be developed to allow for continuous monitoring of the financial and developmental results generated from the Economic Empowerment.

9. OTHER POLICY MATTERS

9.1 SHARIAH COMPLIANCE

9.1.1 As a Shariah compliant financial institution, IsDB and hence the ISFD invest in a Shariah compliant manner.

9.1.2 The Economic Empowerment Portfolio shall be periodically tested for Shariah compliance. Any investment which ceases to be compliant (e.g. due to taking on conventional debt) shall immediately become an exit target unless the ISFD can exercise influence or encourage the investee entity to rectify the situation. In such situations, IsDB shall request the company to provide a timeline (not more than 12 months) for rectification. The requirement for such a timeline shall also be reflected through appropriate clauses in the shareholders' and other relevant agreements for all new investments.

9.2 GUIDELINES FOR INVESTMENT CONSULTANT

9.2.1 EEOMC may elect to engage an independent investment-consulting firm to assist in overseeing the investment activities and performance. The consultant is expected to be proactive in recommending changes in investment strategy, asset allocation, and investment Managers if the situation warrants change. The Consultant's responsibilities are as follow:

- Assisting in the development of investment policies, objectives, and guidelines
- Preparing asset allocation analyses as necessary and recommending asset allocation strategies with respect to the Fund's objectives
- Recommending Fund Managers
- Preparing and presenting performance evaluation reports
- Attending meetings to present evaluation reports no less than semi-annually and at other meetings as requested

- Reviewing contracts and fees for both current and proposed Investment Managers
- Assisting in the rebalancing of asset allocation
- Communicating investment policies and objectives to the financial institutions and monitoring their adherence to such policies and reporting all violations
- Notifying of any significant changes in personnel or ownership of the consulting firm
- Monitoring of financial and social/developmental performance of financial institutions

9.3 CONFLICT OF INTEREST

9.3.1 All persons responsible for investment decisions or who are involved in the management of the Fund of Funds or who are consulting to, or providing any advice whatsoever to EEOMC, shall disclose in writing at the beginning of any discussion or consideration by EEOMC, any relationships, material beneficial ownership, or other material interest(s) which the person has or may reasonably be expected to have, with respect to any investment issue under consideration. EEOMC will require such persons to remove themselves from the decision-making process.

9.3.2 Any members of the EEOMC responsible for investment decisions or who are involved in the management of the Fund shall refuse any remuneration, commission, gift, favor, service or benefit that might influence them in the discharge of their duties, except as disclosed in writing to and agreed upon in writing by IsDB BED. The intent of this provision is to eliminate conflicts of interest between the EEOMC and the Fund. Failure to disclose any material benefit shall be grounds for immediate removal from the EEOMC.

Annex I

Proposed Risk Acceptance Criteria Guidelines for the Economic Empowerment

Asset Class	Risk Acceptance Criteria	
Investments		
Equity	Minimum expected return requirement as per EE Investment Policy	
	Strategic Asset Allocation as per EE Investment Policy	
	Investment horizon 7 to 10 years	
Funds	Minimum expected return requirement as per DW Investment Policy	Satisfactory track record of the Fund Manager for at least 5 years
	Strategic Asset Allocation as per DW Investment Policy	The investment sectors should preferably from defensive sectors like: Education, healthcare, Consumer, Food, Utilities etc
	Investment horizon 7 to 10 years	
	Investment horizon 7 to 10 years	

Asset Class	Risk Acceptance Criteria	
Sovereign		
Sovereign Financing	Availability of country headroom.	To minimize new financing in countries with severe economic vulnerabilities and debt sustainability issue
	Financing after ensuring project readiness and closing of financing gap.	Not to extend non-concessional financing to countries that are likely to be relegated to default rating under High Stressed scenario
	Project inclusion in AWP only after following the established process including preliminary risk review	Maximum limit for a single sovereign project to be capped to USD 50 million.
	Disbursement for projects to follow pro-rata contributions to the extent feasible.	Top 5 and top 10 country exposure not to exceed respectively 40% and 60% of the portfolio
	Not to process additional and supplementary financing for projects without prior risk assessment & inclusion in AWP.	
LoF under Sovereign Guarantee	The LoF recipient bank should possesses good financial strength.	Maximum tenor to be 10 years.
	Maximum outstanding exposure to a bank cannot exceed USD 30 million	
	End beneficiary should be from priority real sector of the country.	

Asset Class	Risk Acceptance Criteria
Non-Sovereign Line of Finance	

Risk Acceptance Criteria- Eligible Entity (LoF bank)

The eligible entity should be a Financial Institution meeting the following criteria:

1. The FI should have:
   i) Minimum 3 years of operational track record
   ii) Maximum 1-year losses in the last 3 Years
   iii) Maximum NPLs 7.5% unless (NPLs – Specific Provision) less than 25%.
   iv) No Major concern on liquidity and capital adequacy
   v) No issue from KYC perspective
   vi) Financial Statements audited by reputable Auditors
   vii) Financial Statements are audited maximum within 6 months from the close of financial year
2. The FI, other than the Leasing Companies, should have a commercial banking license and must be from be systematically important and tier 1 banks of the concerned country.
3. In case the FI is a Leasing Company, it must be from the top tier Leasing companies of the concerned member country with strong track record.
4. The FI should have a minimum Foreign Currency Rating of 'B-' (equivalent to IsDB internal rating of 16)
5. The FI should have local presence with proximity to the End Beneficiary operating area (i.e. a large branch network is beneficial to understand local financing needs and also good online presence).
6. The FI should have strong portfolio monitoring mechanism (to be assessed as part of due-diligence and selection process).
7. Must have a track record of financing SME segment (when End Beneficiary belongs to SME segment); the NPL ratios of the Eligible FI's SME portfolio should be lower than the market average SME NPL average (to be assessed as part of due-diligence and selection process) for the concerned geographical area.
8. The Eligible Entity must have a valid limit assigned by RMD.
9. The eligible financial institution must have its own risk participation in the SME portfolio, which will be benefited from IsDB LoF, to ensure effective monitoring.
10. While it is preferable, to have a commercial bank, which meet the above criteria, as the Eligible Entity for non-sovereign LoF transaction; however, on a case by case basis, three types of Specialized Entities, i.e. government related specialized financial entities, regional financial entities and multilateral financial institutions, may also be considered as long as the Specialized Entity has a credit rating of at least 'BB-' or equivalent and meet the other above noted eligibility criteria which are relevant to it.

<table>
<tr><th>Asset Class</th><th>Risk Acceptance Criteria</th></tr>
<tr><td colspan="2">Risk Acceptance Criteria- Guarantee and Guarantor
Any guarantee instrument to secure DW extended LoF, will need to meet the following Eligibility Criteria
1. The instrument must be an irrevocable, unconditional, unequivocal, legally binding and on demand payment guarantee
2. Non-sovereign guarantor should be a Financial Institution including multilateral development bank with sound financial strength and the following minimum cut-off foreign currency credit rating
i) Financial Institution – 'B' or equivalent
ii) MDB - 'BB' or equivalent
3. The Guarantor should have a track record of issuing guarantee with satisfactory market perception.
4. The rating of the Guarantor should be at least equal or better than the rating of the Eligible Entity.
5. Validity of the guarantee instrument must exceed the full tenor of DW financing by at least 90 days.
6. The Guarantor should not have any KYC or compliance related concern.</td></tr>
<tr><td colspan="2">Risk Acceptance Criteria- Credit Enhancement Instruments
In addition to the Eligible Guarantees, LoF transactions can also be benefitted from various form of Credit Enhancements, like, credit default insurance, LC, SBLC, etc.
1. The instrument should be irrevocable, unequivocal, and on demand payment obligation on the part of its issuer.
2. The insurance policy, covering credit default, which can be invoked without requiring an arbitral award or court order (e.g. NHSO insurance policy) could be considered as an Eligible credit enhancement instrument, to secure DW funded LoF transactions. It is worth noting that before accepting any insurance policy type credit enhancement, Bank should be fully aware of all the associated terms and conditions for receiving payment through invoking an insurance policy before accepting such instrument. It is worth noting that an irrevocable, unconditional and on demand bank guarantee is always preferable over credit enhancement through a credit default insurance coverage (assuming both issuers are of same credit standing), mainly because of certain conditionality attached to the latter (for invoking the instrument).
3. Credit enhancement instrument issuer should have sound financial strength and the following minimum cut-off foreign currency rating
i) Insurance Companies – 'A-' or equivalent
ii) Commercial Banks – 'B' or equivalent
4. Validity of the instrument should exceed the full tenor of DW financing by at least 90 days.
5. The credit enhancement issuer should have
i) Minimum 3 years of operational track record
ii) Maximum 1-year losses in the last 3 Years
iii) No Major concern on liquidity and capital adequacy
iv) No issue from KYC perspective
v) Financial Statements audited by reputable Auditors and are audited maximum within 6 months' close of financial year</td></tr>
</table>

Asset Class	Risk Acceptance Criteria
Risk Acceptance Criteria- Eligible End Beneficiary (for LoF transactions)	
The Eligible End Beneficiary to be benefitted from DW LoF, through the Eligible Entity (LoF Financial Institution), should meet the following minimum criteria: i) End-Beneficiary should be from the priority sector of the country/government ii) Should have solid financial strength with at least three years of operational track record and a viable and realistic business plan (to be assessed by the Eligible Entity) iii) Should have existing banking relationship with the LoF providing bank for at least 3 years with satisfactory performance iv) Should preferably from export-oriented industry v) Should have lower Debt to Equity ratio (preferably not higher than 60:40) vi) Financial statements should be audited by reputed external auditors.	
LoF – Other Criteria	
i) DW non-sovereign LoF portfolio should always maintain a minimum average portfolio rating of 'BB-' or equivalent, which is also in line with the Bank's existing risk guidelines for non-sovereign financing operations portfolio. ii) Door to door tenor of DW non-sovereign LoF facility should not exceed 5 to 7 years. Eligible LoF Financial Institution should be required to utilize DW LoF proceeds to finance a diversified portfolio in such a way that maximum onward financing to a single End-Beneficiary does not exceed 20% of DF financing to the Eligible LoF Financial Institution.	

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