ASSET LIABILITY MANAGEMENT POLICY
DECEMBER 9, 2024

1. Introduction

1.1. This Asset Liability Management (ALM) Policy establishes a framework for the sound management of ALM in the Asian Infrastructure Investment Bank (AIIB or the Bank).

1.2. The purpose of the ALM Policy is to define the principles for prudent management of the Bank's assets, liabilities and equity, and to identify and manage resultant risks, while ensuring income stability.

2. Definition of Terms

As used in the Policy, the following terms have the meanings set forth below:

2.1. "**ALM**" means Asset Liability Management.
2.2. "**AIIB**" or "**the Bank**" means the Asian Infrastructure Investment Bank.
2.3. "**Equity**" means the total of Paid-in Capital, Reserves and Retained Earnings.
2.4. "**Basis Risk**" means the risk arising from impact of relative changes in interest rates for financial instruments that have similar tenors but are priced using different interest rate indices.
2.5. **"Currency Risk"** means the risk of loss arising when assets or liabilities are denominated in a non-US Dollar currency and the price of that currency fluctuates against the US Dollar. Currency Risk may arise from non-USD assets, including margin income, direct equity and equity fund investments, or any other non-USD assets for which hedging may not be feasible.
2.6. **"Debt Redemption Limit"** means the maximum amount of long-term debt redemptions as a percentage of current outstanding long-term debt principal that may occur over a rolling 12-month period.
2.7. "**Duration**" means the measure of the sensitivity of the value of an asset or liability to a change in interest rates, expressed in years.
2.8. "**Exposure**" arises when there is a change in the value of an asset or liability without an instrument on the balance sheet that would generate an offsetting change in value.
2.9. "**Gap Risk**" means the risk that arises from the term structure of interest sensitive positions on the balance sheet.
2.10. "**Hedging**" means a risk management strategy that involves taking a position in a financial instrument that can change in value to offset the changes in value from other assets or liabilities.

2.11. "**Interest Rate Risk**" means the risk that occurs when the value of assets or liabilities changes with the fluctuation of interest rates. Interest Rate Risk comprises Gap Risk, Basis Risk and Optionality Risk.

2.12. "**Long-term Debt"** means borrowing with an original maturity date of more than one year from the date of borrowing.

2.13. "**Liquidity Risk**" means the risk that the Bank is unable to pay its obligations due to cash flow mismatches between assets and liabilities while concurrently lacking the ability to liquefy assets expeditiously without material loss in value.

2.14. "**Optionality**" means the right, but not the obligation to alter the nature of cash flows of an asset or liability, which could be either behavioral (e.g., prepayment) or contractual (e.g., interest rate caps or floors specified in loan term sheets).

2.15. "**Optionality Risk**" means the risk that arises from option derivative positions or optionality embedded in a bank's assets, liabilities and/or off-balance sheet items.

2.16. "**President**" means the President of AIIB.

2.17. "**Refinance Risk**" means the margin compression that may arise when spreads on the Bank's issuances widen at roll over, while the spreads on existing loans remain locked-in. This may result in a potential impact to the Bank's earnings and economic value from potential changes in funding costs.

2.18. "**Short-term Borrowing**" means borrowing with an original maturity date of no more than one year from the date of borrowing.

2.19. **"Treasury"** means The Office of the Treasurer.

3. Asset Liability Management at AIIB

3.1. The objectives of AIIB's ALM approach are to:

(a) provide for the Bank's liquidity needs at all times, while maintaining the necessary resources to satisfy the requirements of credit rating agencies; and

(b) limit potential market risk losses by keeping the Bank's exposures under various allocated market risk limits, while prudently managing interest income to ensure income stability.

3.2. To achieve these objectives, the ALM Policy adheres to the following principles:

3.2.1. **Management of Funding Sources.** Treasury is responsible for supporting the Bank's operations by ensuring the availability of sufficient funding to meet the Bank's business needs. To meet this objective as well as to promote effective risk management, AIIB manages its funding sources as follows:

(a) **Borrowings**. AIIB diversifies its borrowings to provide flexibility and cost-effectiveness in funding. Rate-sensitive liabilities shall be deemed to fund rate-sensitive assets, thus reducing the exposure to volatility of rates and mitigating interest rate risks.

(b) **Equity**. Assets with no outright maturity schedule such as equity and equity fund investments, and other assets for which hedging may not be feasible, shall be deemed funded by equity. Treasury will manage any remaining funding sources appropriately, with due consideration given to the objectives of the ALM.

3.2.2. **Liquidity Risk.** The Bank shall manage Liquidity Risk to ensure its ability to meet cash flow obligations, guided by the following core principles:

(a) The Bank shall maintain sufficient liquid assets to cover maturing liabilities, client disbursements and operational cash requirements.

(b) The Bank shall maintain a diversified funding base comprising various currencies, tenors and investors.

(c) In addition to business-as-usual scenarios in which the Bank shall maintain a liquidity buffer to meet unforeseen disbursements and potential future funding conditions, the Bank shall also anticipate funding needs under stress scenarios and ensure the availability of funds even under extreme stress events.

(d) The Bank shall manage assets in the Treasury Investment Portfolio with the overall objective of achieving relatively low market value volatility and ensuring sufficient liquidity across the entire portfolio, especially in times of stress.

(e) The Bank may fund assets with liabilities of a shorter maturity or with mismatched timing of cash flows.

(f) To prevent debt redemption concentrations, the Bank shall maintain a Debt Redemption Limit of 30%.

(g) The Bank may use short-term borrowings, such as commercial paper or repurchase agreements, to meet interim cash flow requirements or to invest in short-term assets.

3.2.3. **Interest Rate Risk**. The Bank shall manage Interest Rate Risk to mitigate Gap Risk, Basis Risk and Optionality Risk according to the following principles:

(a) Rate sensitive risks shall be managed by the Bank utilizing interest rate derivatives to hedge the exposures to the desired basis.

(b) Asset terms that create market exposures from Optionality may be either hedged on a back-to-back basis or offered in a manner that transfers the cost of the market risk to the borrower.

(c) Any unhedged risks shall be centrally managed by Treasury, adhering to established risk limits.

3.2.4. **Currency Risk.** The Bank shall manage Currency Risk according to the following principles:

(a) AIIB's functional currency is the US Dollar (USD). The Bank may offer loans and other development-related assets denominated in currencies other than USD whenever it has the means to adequately operate in those currencies and manage risks unique to the relevant products.

(b) To minimize Currency Risk, the Bank shall match its assets in any one currency with borrowing obligations in the same currency (after derivative activities). In cases where non-USD funding through bond issuances or swaps may not be feasible, the assets could also be funded by equity and remain unhedged, within established limits to control such unhedged exposures.

3.2.5. **Refinance Risk**. Refinance Risk shall be managed according to the following principles:

(a) Loans shall be priced at a premium designed to absorb periods where funding costs may be high at the time of refinancing.
(b) In order to understand the level of Refinance Risk, the Bank shall monitor both the economic value and earnings impact arising from such risk. The risk shall be managed within endorsed thresholds.

3.2.6. **Use of Financial Derivatives**. The use by the Bank of derivatives as an integral part of its ALM activities shall be governed by the following principles:
(a) As a matter of sound business and financial practice, the Bank may use financial derivatives as outlined in the General Investment and Financial Derivative Authority to hedge the balance sheet and/or portfolio and manage cash flow, Interest Rate Risk and Currency Risk.
(b) The Bank shall monitor derivatives by:
(i) Measuring the value of the instrument on a regular basis (monthly, at a minimum);
(ii) Disclosing the market value of derivative instruments at least annually in the notes to the Bank's financial statements; and
(iii) Segregating the execution and monitoring activities between business units and supporting units.

4. Limits and Controls

4.1. **Limits**. The Bank's risk appetite provides for ALM risk to be incurred, provided that the Bank maintains prudent boundaries around the potential impact of market changes on both earnings and capital. These boundaries are expressed as Key Risk Indicators (KRI) to be reported to the Board of Directors and specified in the Risk Appetite Statement (RAS).

4.2. **Controls.** This ALM Policy requires an effective system of internal controls for market and liquidity risks. Such controls shall ensure the following:
(a) Implementation of
(i) appropriate limits and enforcement on risk taking;
(ii) adequate systems and standards for identifying, measuring, monitoring and evaluating risk;
(iii) standards for valuing positions and measuring performance;
(iv) a comprehensive and timely ALM risk reporting process in conjunction with ALM review process; and
(v) a strong adherence to established controls.
(b) Clear lines of authority and responsibility for the management and control of ALM risks.

5. Review of Policy

The ALM Policy shall be reviewed by the Bank at least once every three years. Interim reviews may be conducted within the stipulated period of three years if deemed necessary.

6. Implementation

The President shall ensure the implementation and observance of this ALM Policy.