ASIAN INFRASTRUCTURE
INVESTMENT BANK

DIRECTIVE ON ASSET LIABILITY MANAGEMENT

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Summary of Content: Establishes rules, processes, and responsibilities with the Bank to facilitate the application of the ALM Policy and Financial and Risk Management Policy.

Related Documents: ALM Policy, Financial and Risk Management Policy, Directive on the Treasury Investment Portfolio, Guideline on the Treasury Investment Portfolio, Directive on The Risk Appetite Framework

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DIRECTIVE ON ASSET LIABILITY MANAGEMENT

1. OVERRIDING OBJECTIVE

1.1. This Directive establishes rules and directions to ensure that the identification, measurement, management and monitoring of bank-wide asset liability management (**ALM**) risks are undertaken in accordance with the Asset Liability Management Policy (**ALM Policy**) and Financial and Risk Management Policy by the Bank's personnel.

1.2. The ALM Policy establishes a framework for the sound asset and liability management in the Asian Infrastructure Investment Bank (**AIIB** or the **Bank**).

1.3. For the purposes of this Directive, ALM risks include, but are not limited to, all the risks defined in this Directive. The Directive shall also apply to any other risks reasonably considered to be part of ALM under prevailing industry practices or evolving regulatory expectations, even if not explicitly stated herein.

1.4. The exercise and interpretation of this Directive shall seek to give effect to this overriding objective.

2. DEFINITIONS

The terms, acronyms, and abbreviations used in this Directive shall have the meanings set forth below:

2.1 "**AIIB**" or "the **Bank**" has the meaning as defined in Section 1.2 of this Directive.

2.2 "**ALM**" has the meaning as defined in Section 1.1 of this Directive.

2.3 "**ALM Policy**" has the meaning as defined in Section 1.1 of this Directive.

2.4 "**Asset and Liability Management Committee**" or "**ALCO**" means the Asset and Liability Management Committee of the Bank.

2.5 "**Concentration Risk**" means exposures that may arise within or across different risk categories throughout an institution with the potential to produce: (i) losses large enough to threaten the institution's health or ability to maintain its core operations; or (ii) a material change in the Bank's risk profile.

2.6 "**Credit Rating Agencies**" or "**CRAs**" means credit rating agencies.

2.7 "**Debt Redemption Limit**" has the meaning as defined in the ALM Policy.

2.8 "**Early Warning Indicators"** or **"EWIs"** means the early warning indicators of potential stress-monitoring market conditions and counterparty behaviors.

2.9 “**Economic Value of Equity**” or “**EVE**” means the difference between the present value of the Bank’s assets minus the present value of liabilities. The change in EVE or “ΔEVE” means the difference between the EVE estimated with stressed discount factors under various scenarios, minus the EVE estimated with the discount factors as of the reporting date.

2.10 “**Funding Concentration Risk**” means the risk that the Bank’s funding structure is excessively dependent on a limited number of sources, making it vulnerable to a single event or a single factor, such as a significant and sudden withdrawal of funds or inadequate access to new funding.

2.11 “**High Quality Liquid Asset**” or “**HQLA**” means an asset that can be easily and immediately converted into cash at little or no loss of value.

2.12 “**Intraday liquidity**” means the funds which can be accessed during the business day, usually to enable banks to make payments in real time.

2.13 “**Intraday liquidity risk**” means the risk that a bank fails to manage its intraday liquidity effectively, which could leave it unable to meet a payment obligation at the time expected, thereby affecting its own liquidity position and that of other parties.

2.14 “**Investment Operations**” means the Investment Operations Department of the Bank.

2.15 “**KPIs**” or “**Key Performance Indicators**” has the meaning as defined in the Risk Appetite Framework.

2.16 “**KRIs**” or “**Key Risk Indicators**” has the meaning as defined in the Risk Appetite Framework.

2.17 “**Liquidity Contingency Plan” or “LCP”** means the Bank’s strategy for handling a liquidity crisis. It describes procedures for managing cash flow shortfalls in stress situations.

2.18 **“LCR”** means Liquidity Coverage Ratio.

2.19 “**Liquidity Stress Testing**” means a financial assessment that evaluates an institution’s ability to meet its cash flow obligations, particularly during adverse economic conditions or unexpected events.

2.20 “**Long-Term Financial Projection”** or **“LTFP**” means a forward-looking estimate of the Bank’s financial performance over an extended time period.

2.21 **“Model Risk”** has the meaning as defined in the Directive on Model Risk Management.

2.22 "**Net Interest Income**" or "**NII**" means the difference between total interest income and total interest expenses, over a specific time horizon and taking into account hedging. The change in NII, or "ΔNII" means the difference between the NII estimated with stressed interest rates under various scenarios, minus the NII estimated with the interest rates as of the reporting date.

2.23 "**Office of the Treasurer**" or "**TRE**" means The Office of the Treasurer of the Bank.

2.24 "**RAF**" means the Risk Appetite Framework

2.25 "**Risk Committee**" or "**RC**" means the Risk Committee of the Bank.

2.26 "**RMD**" means the Risk Management Department of the Bank.

2.27 "**Treasury Investment Portfolio**" has the meaning as defined in the Directive on the Treasury Investment Portfolio.

3. SCOPE OF APPLICATION

3.1. This Directive applies to Bank Personnel.

4. GOVERNANCE

4.1 General Principles

A. The Office of the Treasurer and the Risk Management Department shall collaborate to define and mutually agree upon the ALM risk measurement methodologies which are the basis for calculating Key Risk Indicators (**KRIs**) pertaining to ALM risks.

B. Any new methodologies, metrics, or limits introduced by either TRE or RMD for the measurement, management and monitoring of ALM risks, as well as any changes to such existing methodologies, metrics or limits, shall, at a minimum, be discussed with the ALCO.

C. Any changes to the established ALM KRIs, including changes to associated methodologies for calculating such KRIs, shall be mutually agreed by TRE and RMD and not be implemented prior to such an agreement.

D. TRE may propose new metrics or limits that are not classified as KRIs or Key Performance Indicators (KPIs) under the Directive on Risk Appetite Framework (RAF). Such proposals shall adhere to the principle outlined in Section 4.1.B of this Directive and shall not conflict with any existing KRIs or KPIs as defined in the RAF.

E. Should an agreement on KRIs/KPIs between TRE and RMD not be reached, the matter will be referred to the RC for final resolution.

4.2 Roles and Responsibilities Pertaining to Asset and Liability Management

A. The Chief Financial Officer shall:

i. Oversee the strategies and activities in relation to balance sheet management.
ii. Review the Bank's KPIs/KRIs pertaining to ALM risks.
iii. Approve strategies to manage liquidity levels in accordance with the risk appetite and to ensure that the Bank maintains sufficient liquidity.
iv. Approve strategies to manage ALM risks in accordance with the Risk Appetite Framework.
v. Approve ALM limits that are not KPIs/KRIs, including but not limited to equity duration limit (bands) for the overall balance sheet and for individual fixed income portfolios.
vi. Approve the Bank's Long-Term Financial Projection at the recommendation of ALCO.
vii. Approve the Liquidity Contingency Plan.

B. The Chief Risk Officer shall:

i. Approve the Bank's Level 3 KPIs/KRIs in line with the RAF as pertaining to ALM risks.
ii. Approve the Bank's Liquidity Stress Testing methodologies and assumptions.
iii. Approve the validation of the methodologies and rules adopted to measure and assess ALM KPIs/KRIs.

C. The Asset and Liability Management Committee and the Risk Committee shall exercise their duties in accordance with their respective terms of reference.

D. The Office of the Treasurer shall:

i. Act as the first line of defense and provide strategic and analytical support to management on ALM matters.
ii. Identify, measure, monitor and manage ALM risks associated with the Bank's business with the objective of maintaining sufficient liquidity, protecting the Bank's earnings and the economic value of its balance sheet, and report related matters to ALCO.
iii. Ensure that the Bank's ALM risk profile is within the Bank's risk appetite and limits.
iv. Set up the LTFP model to forecast the Bank's balance sheet and income statement over a long-term horizon (i.e. 1 year to 10+ years), with input from relevant departments as endorsed by the ALCO.

E. The Risk Management Department shall:

i. Act as the second line of defense and identify, measure and monitor ALM risks in line with the Bank's risk appetite and report on ALM risks to the RC and to the Board of Directors.

ii. Ensure the implementation of the Bank's risk management framework, in accordance with the Bank's policies, directives, instructions and guidelines.
iii. Ensure the existing KPI and KRI frameworks, assumptions, models and methodologies are appropriate, fit for purpose, and in line with the Bank's risk appetite, and, if necessary, propose new KPIs and KRIs taking into account the Bank's balance sheet evolution and complexity, and any emerging risks.
iv. Monitor ALM KRIs/KPIs limit compliance.
v. Assess and validate the key assumptions, models, methodologies, results and limitations of the ALM risk KRIs/KPIs.

F. The Office of the Controller (CTL) shall:

i. Perform centralized accounting treatment for treasury and investment operation businesses.
ii. Produce management reporting for the sources and uses of funds across the Bank.
iii. Provide breakdown of balance sheet and income statements to TRE to set the initial positions of the balance sheet and year-to-date revenues and expenses of the income statement.

5. LIQUIDITY RISK MANAGEMENT AND REPORTING

5.1 Contractual maturity mismatch

A. TRE shall assess liquidity risk by analyzing the contractual maturity mismatch profile, which provides insights into the extent of the Bank's reliance on maturity transformation under existing contractual arrangements.

B. TRE shall report contractual maturity mismatch profile to the ALCO on at least a quarterly basis.

5.2 Concentration of funding

A. TRE shall establish an adequate funding strategy that provides effective diversification in the sources and tenors of funding.

B. TRE shall maintain an ongoing presence in its chosen funding markets and strong relationships with funds providers to promote effective diversification of funding sources.

C. TRE shall identify the main factors that affect its ability to raise funds and monitor those factors closely to ensure that estimates of fund-raising capacity remain valid.

D. Debt redemption concentration shall be managed by TRE in accordance with the Debt Redemption Limit set in the ALM Policy.

E. TRE shall identify and build strong relationships with current and potential investors and diversify its investor base to reduce Funding Concentration Risk.

5.3 Available liquid assets

A. The Bank's liquid assets shall be centrally managed in the Treasury Investment Portfolio.

B. TRE shall manage the Bank's liquid assets according to the Directive on the Treasury Investment Portfolio, its related Instruction and Guideline, and in line with the Bank's Risk Appetite Framework.

C. RMD shall define High-Quality Liquid Assets for internal liquidity metrics.

5.4 Collateral Management

A. TRE shall actively monitor the Bank's collateral positions, differentiating between encumbered and unencumbered assets.

5.5 Liquidity risk metrics management

A. RMD shall conduct Liquidity Stress Testing based on AIIB's stress testing methodology to identify potential liquidity strain and to ensure that current exposures remain in accordance with the Bank's established liquidity risk tolerance.

B. RMD shall report Liquidity Stress Testing assumptions and results to the RC quarterly.

C. RMD shall share the LCR and Liquidity Stress Testing results with TRE for inclusion in the ALCO update.

D. TRE shall maintain an adequate stock of liquid assets to ensure a level of coverage that meets both the internal liquidity requirements as well as the appropriate targets for liquidity assessments by the Credit Rating Agencies (CRAs)[1] to support the Bank's triple-A credit rating.

E. TRE shall monitor such metrics and report to the ALCO at least on a quarterly basis. In calculating the metrics, all positions across all currencies shall be aggregated.

F. RMD shall monitor internal liquidity KRIs (LCR, Liquidity Stress Testing, 3-Year Liquidity) and KPIs, and report to RC on at least a quarterly basis.

5.6 Funding management

A. TRE shall design the annual borrowing program to meet the amount of borrowings required during the year in order to facilitate balance sheet growth and reach the target level of liquidity by the following year end.

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[1] Unless otherwise stated, the term CRAs refers to the international leading credit rating agencies, Standard & Poor's (S&P), Moody's, and Fitch.

B. TRE shall monitor the utilization of the annual borrowing program and report to the ALCO on a monthly basis.

5.7 Intraday liquidity management

A. TRE shall monitor its intraday liquidity positions and risks to meet payment and settlement obligations on a timely basis and thus contribute to the smooth functioning of payment and settlement systems.

B. If the Bank chooses to rely on correspondents or custodians to conduct payment and settlement activities, TRE shall ensure that this arrangement allows it to meet obligations in a timely manner and to manage its intraday liquidity risks under a variety of circumstances.

C. TRE shall have the capacity to measure expected daily gross liquidity inflows and outflows.

D. TRE shall arrange to acquire sufficient intraday funding to meet its intraday objectives, where applicable.

E. TRE shall be prepared to deal with unexpected disruptions to its intraday liquidity flows.

5.8 Early Warning Indicators (EWIs) and Liquidity Contingency Plan (LCP)

A. TRE shall utilize EWIs to identify the emergence of increased risk or vulnerabilities in its liquidity position or funding needs.

B. EWIs shall be appropriate, comprehensive and regularly reviewed against the prevailing and emerging liquidity stress indicators that are relevant to the Bank, aligned with the Bank’s balance sheet development and growth.

C. TRE shall have a formal liquidity contingency plan that clearly sets out the strategies for addressing liquidity shortfalls in emergency situations. An LCP shall outline processes to manage a range of stress environments and establish clear lines of responsibility.

D. LCP’s design, plans and procedures should be closely integrated with the TREs operations as per the Directive on Treasury investment Portfolio.

6. INTEREST RATE RISK MANAGEMENT AND REPORTING

6.1 Interest rate repricing gap

A. Interest rate repricing gap analysis shall be undertaken by examining details of interest sensitive assets and liabilities to establish when they will next reprice, i.e., be subject to a change in interest rate, and then tabulating those which reprice within set time buckets.

B. TRE shall report interest rate repricing gap to ALCO on at least a quarterly basis.

C. RMD shall ensure that the repricing assumptions for interest rate risk measurement are appropriate and aligned with the product characteristics and the balance sheet complexity.

6.2 Scenario analysis

A. TRE shall perform the analysis of the change in net interest income (∆NII) and change in economic value of equity (∆EVE) under various scenarios to evaluate the impact of interest rate changes on both the Bank's earnings and its economic value.

B. TRE shall report the results to ALCO on at least a quarterly basis.

C. RMD shall monitor EVE and NII KRIs, and report to RC on at least a quarterly basis.

6.3 Duration

A. TRE shall conduct duration analysis for the balance sheet and for specific portfolios.

B. TRE shall manage duration within limits and/or targets set by the CFO and report the result to ALCO on a quarterly basis.

6.4 Refinancing risk monitoring and management

A. Refinancing risk involves the risk that debt will have to be refinanced at an unusually high cost or cannot be rolled over at all. This risk is primarily presented in funding non-sovereign operation[2].

B. To manage and mitigate the refinancing risk, TRE shall:
   i. diversify its financing sources and investor base;
   ii. diversify debt maturities to avoid Concentration Risk;
   iii. lengthen average maturity of debt where appropriate;
   iv. implement any other action as determined by ALCO.

C. TRE shall monitor such refinancing risk for nonsovereign-backed financing from both an economic value and earnings perspective. The result shall be reported to ALCO on at least a quarterly basis.

7. CURRENCY RISK MANAGEMENT

[2] Refinancing risk also resides in legacy sovereign fixed spread product which has been suspended as of April 15, 2021.

7.1 The Bank's principal currency risk management objective is to protect its capital from currency transactions and translation risks due to fluctuations in currency exchange rates.

7.2 The Bank shall manage its own exposure to currency exchange rates while giving its clients the flexibility to choose from a set of currencies approved for lending.

7.3 Currency risk is minimized through normal business activities, and any residual risk exposure shall be managed within limits established by RMD and/or TRE.

7.4 TRE shall monitor the currency risk exposure and report to the ALCO on at least a quarterly basis.

7.5 RMD shall monitor currency risk KPIs and KRIs, and report to RC on at least quarterly basis.

8. NEW PRODUCTS

8.1 ALM risks of any new products shall be identified and measured with the support of, and information provided by, all relevant Bank's Business Units in a timely manner.

8.2 TRE and RMD shall have access to all relevant data, including, but not limited to market data, product data, and any other information required for identification and measurement of ALM risks of new products.

8.3 TRE and RMD shall agree on the ALM risk assumptions for each new product. Such assumptions shall also be reviewed by ALCO.

8.4 ALM risks of new products shall also be subject to the overall Bank's operational readiness assessment for onboarding of new products.

9. USE OF LONG-TERM FINANCIAL PROJECTION

9.1 Long-term financial projection involves projecting future assets, liabilities, revenues, expenses, and key factors that have a financial impact on the Bank. Understanding long-term trends and potential risk factors that may impact overall financial sustainability allows the Bank to proactively address these issues.

9.2 TRE shall establish a robust LTFP model under a going-concern basis to support long-term financial planning and sustainability.

9.3 All relevant departments shall be responsible for providing timely and accurate assumptions and inputs to TRE in accordance with the responsibilities and timeline agreed by ALCO, and TRE shall report the key assumptions and results to ALCO on at least a quarterly basis.

9.4 RMD shall review and validate LTFP model assumptions, methodologies, and results according to its Model Risk related policies.

10. REVIEW

This Directive shall be reviewed at least every two years and/or if there are any material changes.

11. IMPLEMENTATION

The Chief Financial Officer and Chief Risk Officer shall introduce, if necessary, any related Instruction or Guideline to ensure the effective implementation of this Directive. The Chief Financial Officer and the Chief Risk Officer shall provide necessary support for the application and implementation of this Directive.

12. APPLICATION AND WAIVER

The President shall make all final decisions regarding the application of this Directive, including whether to grant a waiver thereof, in accordance with Section 4.8 of the Directive on the Internal Legal Framework.