

Investment Policy Statement

Employees' Provident Fund

1. Purpose of the Investment Policy Statement

This Investment Policy Statement (IPS) sets forth the process that Employees' Provident Fund has adopted to make investment related decisions with respect to assets of the Fund in compliance with the standards of fiduciary conduct prescribed in the Employees' Provident Fund Act No 15 of 1958 (the EPF Act). The policy identifies the investment goals and objectives of the Fund and sets out decision-making processes for selecting investments. The Investment Policy Statement will be used as the basis for making investment decisions of the Fund and will itself be reviewed and approved from time to time by the Monetary Board of the Central Bank of Sri Lanka.

2. Employees' Provident Fund

The Employees' Provident Fund, hereinafter referred to as "EPF" or "the Fund", has been established under the Employees' Provident Fund Act, No.15 of 1958 (the EPF Act) as a mandatory defined contributory retirement benefit scheme which covers the private sector and semi-government sector employees. As per the EPF Act, the Commissioner of Labour is vested with the powers to administer the Fund while the Monetary Board (MB) of the Central Bank of Sri Lanka (CBSL) is assigned to manage the Fund as its custodian. Powers and duties of the MB in relation to the Fund have been laid down in Section 5 of the EPF Act.

3. Management of the Fund

3.1 The Monetary Board

The EPF Act empowers MB to receive contributions and all other sums collected under the EPF Act, maintain a general account in respect of the Fund and individual member accounts, invest the moneys of the Fund, charge the expenses incurred in carrying out its duties under the provisions of the Act on the income

of the investment and pay retirement benefits to eligible members or their legal heirs when such benefits are claimed.

Section 5(1) (e) of the EPF Act states that “*the Monetary Board*” may invest the moneys of the Fund as are not immediately required for the purposes of this Act in such securities as the Board may consider fit and may sell such securities.” Accordingly, MB has the discretion to invest in securities, which include the following and not limited to Government Securities e.g.: Treasury bonds, Treasury bills, Rupee loans, and other securities issued by the Sovereign State and Local Government Authorities, shares and debt instruments issued by private corporates, which are considered fit by MB.

3.2 Investment Committee

The Monetary Board has established the Investment Committee (IC) to provide guidance to the EPF Department in line with the strategic directions given by MB and review and monitor the performance of EPF investments in relation to the prevailing and future domestic and global market conditions. Accordingly, IC takes investment and asset allocation decisions within the guidelines stipulated in the IPS and the strategic directions provided by MB to meet risk and return considerations of EPF.

IC consists of the Deputy Governor (Chairman) and Assistant Governor who oversee the EPF Department, the Superintendent of EPF and Additional Superintendent/s and Deputy Superintendent of EPF in charge of Fund management Division (FMD). A staff officer from FMD serves as the Secretary to IC.

4. Investment Policy approved by the MB

4.1 Investment Objective

The investment objective of the Fund is to provide reasonable and sustainable returns to its members while minimizing the risk and ensuring the safety and growth of the Fund. According to Section 14(1) of the EPF Act, the Fund has a statutory obligation to pay a minimum rate of 2.5 per cent per annum on year end balances lying to the credit of member accounts.

4.2 Risk-Return and Maturity Profile of EPF Investments

Investments are made with the objective of maximizing returns having regard to the risks associated with such investments. Further, as the average period of member contribution is above 20 years, the investment horizon also can have a similar time frame. Consequently, the IC will be expected to take a long term view in making investment decisions while maintaining adequate liquidity of assets to meet the liquidity requirements of the Fund. As the investments are made with a long term view, short term volatilities in the market would have a less impact as compared to an investor with a short term time horizon. Accordingly, EPF investments will be made to take advantage of long term developments of the market. Hence, EPF should not be unduly affected or become vulnerable for short term volatilities in the market. However, in view of avoiding or minimizing the losses, the IC may also consider selling some securities at a loss, if it considers that such a strategy is the most appropriate in the particular circumstances. Nevertheless, the IC will need to ensure an appropriate balance in the investment portfolio by allocating funds between different maturity periods ranging from overnight Re-purchase agreements to long term investments with 20-30 year maturity. It will also manage the portfolio in a manner in which risk will be distributed across the sectors, different types of instruments and among a wide spectrum of asset classes. The IC would also be expected to make sure that

adequate systems and procedures are in place to identify, mitigate and manage risks associated with EPF investments.

4.3 Asset Allocation

MB may provide the IC the necessary guidance from time to time, in relation to the composition of securities, the maturity structure of the portfolio and risk-return profile of the investment portfolio. In accordance with such guidance, the IC would assess the market conditions and investment climate prevailing at the time of investment, having regard to age composition of members, taking a long term view of returns and risks associated with individual investments and asset portfolio. Accordingly, an investment strategy will be put in place by the IC to make the changes desirable with regard to asset allocation in view of the investment objective stated above.

(a) Macro Economic Considerations

In view of achieving the investment objective of EPF all its funds at present are to be invested within Sri Lanka. However, with the gradual reduction of fiscal deficit in the medium to long term, the EPF may face a challenging environment to find suitable investment avenues for its funds. Such a situation is likely to challenge the existing investment policy of the Fund, which is highly concentrated on government securities.

In that context, since the growing capital market would result in a higher demand for funds from the private sector in the domestic market, the growth of both the equity and corporate debt markets would, in the medium to long term, provide new opportunities for investments of the Fund.

In order to benefit from these emerging opportunities, while enhancing the availability of resources for economic activities of the private sector, the Fund would also be expected to focus on diversifying its investments into new areas

which would provide higher returns even if such funds may attract a slightly elevated level of risk, in order to meet the investment and return objectives of the Fund.

(b) Investment Strategy

The EPF will take a long term view of both the local and global market conditions and pursue innovative and diversified fund management strategies to enhance its returns in a declining interest rate environment while ensuring the safety and growth of the Fund. These strategies would include, but not limited to

- **Investments in fixed income government securities**, with short, medium and long term maturities to ensure high returns, liquidity considerations, growth and safety of the Fund.
- **Investments on equities** in different sectors to ensure long term growth and income to the Fund.
- **Investments on debt securities** such as corporate debentures, trust certificates and commercial paper to earn higher income and to be a partner in developing the debt securities market which would in return benefit the Fund.
- **Investments in capital intensive projects and housing market.** In view of minimizing the risk of concentration of investments on limited sectors, the IC will be expected to consider the developments of the emerging market environment. In many successful countries in achieving high economic growth, pension funds have played an important role in developing capital and housing markets, both of which are required for sustainable economic growth by way of supplying long term funds/liquidity to those markets. Hence, EPF would also allocate an appropriate percentage of its Funds for such investments and would endeavour to popularize capital and housing markets, which would be to the ultimate benefit of the EPF members.

- **Investments in special purpose vehicles.** The EPF will also be expected to consider the establishment of a few special purpose vehicles (SPVs) that would specialize in management of investments based on different risk appetites and allocate funds for such SPVs so that those could undertake investments in selected investment instruments.
- **Investment in foreign assets.** EPF does not yet have exposure to the foreign exchange markets or foreign assets. However in the future, the Fund will be expected to explore alternative investment opportunities and therefore, shall train the required personnel so that they would be equipped with the skills necessary to face the emerging challenges in regard to foreign investment as well.

5. Periodic Review of the Investment Policy Statement

The MB shall review the IPS from time to time in view of changing economic conditions and growth of investment opportunities. Changes would be made to the extent to which such changes are in the interest of the Fund's members or required as a matter of law, prudence or advantage. However, such changes would be evolutionary and designed essentially for the long term, although short term events in the financial markets may also be considered if it is deemed necessary or useful.