CPF Investment Scheme

Evaluation Criteria for Prospective Fund Management Companies/ Insurance Companies for Inclusion under the CPFIS

The Central Provident Fund Board ("CPFB" or the “Board”) has appointed Mercer (Singapore) Pte Ltd ("Mercer") to assist with due diligence related to the inclusion of Fund Management Companies ("FMCs")/ Insurance Companies ("Insurers"), to manage unit trusts and investment-linked insurance products ("ILPs"), under the Central Provident Fund Investment Scheme ("CPFIS").

The information below, provided by Mercer, is intended to let FMCs/ Insurers gain a better understanding of the criteria applied in the evaluation process.

The due diligence activities may include on-site research meetings with the FMC/ Insurers Singapore-based management team, follow-ups via conference calls, and desktop research. The subjective judgments formed by Mercer in the course of these meetings form an important component of the overall evaluation process.

The evaluation of FMCs and Insurers comprises of two key components:

1. Investment Capabilities

Mercer will supplement the due diligence meeting with the FMCs/ Insurers with existing research of the FMCs/ Insurers on Mercer’s Global Investment Manager Database ("GIMD") and base the assessment of the investment capabilities on that. Specifically, Mercer will make reference to the highest up-to-date ratings on GIMD as a basis for our assessments of investment capabilities. Mercer will also draw on the findings from the due diligence activities with the FMCs/ Insurers.

In the event that there is no up-to-date research (or any research on GIMD), Mercer will work with the candidate FMCs/ Insurers to establish what they consider to be their strongest capability and Mercer will then research this to establish a rating. In this respect, Mercer will evaluate the investment capabilities, based on the four factors framework:

   a. Idea Generation
   Idea generation encompasses everything that the managers do to determine the relative attractiveness of different investments. This may include views on an asset class, country, currency or sector, in addition to individual securities. This indicates Mercer’s assessment of how effective the manager is at generating value-adding investment ideas.

   Mercer will evaluate the manager and develop a clear understanding of how the manager generates investment ideas, what aspects (if any) of this process give it an edge over most other market participants, and what aspects (if any) are weaknesses.

   b. Portfolio Construction
   Portfolio construction refers to the manner in which the manager translates investment ideas into decisions on which investments to include in a portfolio and what weights to give to each of these investments.
Mercer will assess how they take an idea and implement it in an actual portfolio. Mercer will evaluate how effectively the investment ideas generated are translated into weightings within the portfolio, and how well risk is controlled.

Mercer will evaluate if the active positions in the portfolio closely reflect the manager’s investment ideas, and are reasonably well calibrated in relation to each other, as well as how effectively the manager has been able to diversify the active positions in the portfolio.

c. Implementation

Implementation refers to the capabilities surrounding activities that are required to achieve the desired portfolio structure. This indicates how effective Mercer thinks the manager is at minimising the extent to which the value added in the idea generation and portfolio construction stages of the process is given back in the form of implementation costs (including opportunity costs incurred when transactions are not implemented). Costs are both direct and indirect through market impact.

Mercer will assess the ability and the efficiency of the manager in translating investment ideas into the actual portfolio. Mercer pays special attention to capacity issues at this stage.

d. Business Management

Business management refers to the overall stability of the firm, firm resources, and overall operations. This reflects how well Mercer thinks the business and the people who work in it are managed.

Some of the factors considered are the stability and viability of the asset management business of the firm as a whole, as well as the viability of the strategy. The likelihood of key staff retention and how well their interests are aligned with clients is also assessed. Mercer also evaluates how managers are managing their investment firms to understand the economic sustainability of the proposed mandate in the context of the firm.

For Insurers that do not have their own asset management teams, Mercer’s assessment of their investment capabilities would be based on the approach that the Insurers adopt in determining candidate funds for their ILPs to feed into.

2. Operational Risk Assessment

Mercer will issue a questionnaire to the FMCs/ Insurers. Within each operational area, Mercer will ask multiple targeted questions to identify factors, or “flags,” that may give rise to increased operational risks. Mercer will assess the FMCs/ Insurers based on their written responses.

The evaluation methodology is designed to assess the FMCs/ Insurers’ operational risk within each operational area and as a total for each FMC/ Insurer. To that end, Mercer has developed an assessment framework to evaluate the FMCs and the insurers that incorporated the following core factors, which are critical to the safe and soundness of the operations and control environment:

a. Governance and Organisational Structure

The firm’s governance and organisational structure facilitates senior management’s effective oversight over the firm’s activities and promotes investors’ interests. Mercer will
evaluate, for example, the corporate and ownership structure (including committees) within the FMCs/ Insurers, financial strength, delegated authorities and segregation of duties.

b. Human Capital
Human resources and staff competence are important for maintaining institutional history and knowledge of key functions and controls. The areas that Mercer will evaluate include the credit and criminal checks processes in place, staff adequacy, retention and turnover, succession planning and compensation arrangements.

c. Regulation, Compliance and Audit
Regulation, compliance and audit provide the control framework within which a firm operates and invests. Some aspects that Mercer will evaluate include licensing and registrations, regulatory versus firm-wide compliance, litigation and client on-boarding.

d. Risk Control
Mercer will evaluate factors such as how the FMCs/ Insurers deal with operational risk, counterparty risk, control functions and portfolio risk.

e. Technology
Technology, infrastructure, and changes in the management processes provide significant insight into the manner in which an investment management department supports key processes and controls and protects clients in a secure and structured operating environment. Some aspects that Mercer will evaluate include systems security, development, maintenance, level of automation and security around models.

f. Business Continuity and Disaster Recovery Plans
Business continuity and disaster recovery (“BC/DR”) plans represent the organisation’s approach to minimising and managing operational risk created by interrupted access to critical data or services and the opportunity costs should such an event arise. As such, some areas that Mercer will evaluate include assessing the BC/DR plans in place and whether adequate testing is conducted.

g. Transaction Execution
Investment implementation and controls provide the framework and tools for making efficient investments and protecting investor interests during the life cycle of the trade. Some aspects that Mercer will evaluate include trade process, demonstration of trade initiation and execution and trade allocation.

h. Valuation and Administration
Investment administration includes key daily activities supporting investment activities to process transactions, validate assets’ existence and maintain an accurate internal book of records, in accordance with clients’ best interests. Mercer will assess, for example, the process for trade matching and confirmation, cash and position reconciliations, securities pricing, accruals and investor reporting.

i. Third Party Relationships
An organisation may outsource operations or retain external service providers to perform key operational activities. Some aspects that Mercer will evaluate include outsourced functions, selection process, ongoing monitoring and performance monitoring of custodians, banks and other third parties.
In addition to the above two components, assessment will be made of the FMCs/ Insurers’ distribution strategy. Some examples of the factors Mercer assesses are distribution channels and management, market accessibility, training for dealers and servicing standards.

FMCs/ Insurers that score well across all three aspects of investment capabilities, operational risk and distribution strategy will be recommended for inclusion under CPFIS.
Evaluation Criteria for Prospective Products for Inclusion under the CPFIS

The information below is intended to let FMCs/ Insurers gain a better understanding of the criteria applied in the evaluation process for products. This will enable the FMCs/ Insurers to assess whether a product has a reasonable chance of receiving a favourable evaluation before they submit an application for evaluation.

Every product is considered on its own specific merits. There is no preference for a given asset class, style, or type of approach. Our focus is on evaluating whether each candidate investment product has a reasonably high probability of achieving future out-performance relative to its benchmark, where relevant.

The due diligence activities may include on-site research meetings, follow-ups via conference calls, and desktop research with the key decision maker(s), such as the lead portfolio managers, of the products. The research meetings will be undertaken by the Mercer research specialists globally, generally by a researcher in close proximity to where the key decision maker(s) are located. The subjective judgments formed by Mercer in the course of these meetings forms an important component of the overall evaluation process.

Mercer will evaluate the investment philosophy and process, based on the four factors framework:

a. Idea Generation
Idea generation encompasses everything that the managers do to determine the relative attractiveness of different investments. This may include views on an asset class, country, currency or sector, in addition to individual securities. This indicates Mercer’s assessment of how effective the manager is at generating value-adding investment ideas.

Mercer will evaluate the manager and develop a clear understanding of how the manager generates investment ideas, what aspects (if any) of this process give it an edge over most other market participants, and what aspects (if any) are weaknesses.

b. Portfolio Construction
Portfolio construction refers to the manner in which the manager translates investment ideas into decisions on which investments to include in a portfolio and what weights to give to each of these investments.

Mercer will assess how they take an idea and implement it in an actual portfolio. Mercer will evaluate how effectively the investment ideas generated are translated into weightings within the portfolio, and how well risk is controlled.

Mercer will evaluate if the active positions in the portfolio closely reflect the manager’s investment ideas, and are reasonably well calibrated in relation to each other, as well as how effectively the manager has been able to diversify the active positions in the portfolio.

c. Implementation
Implementation refers to the capabilities surrounding activities that are required to achieve the desired portfolio structure. This indicates how effective Mercer thinks the manager is at minimising the extent to which the value added in the idea generation and portfolio construction stages of the process is given back in the form of implementation costs (including opportunity costs incurred when transactions are not implemented). Costs are both direct and indirect through market impact.
Mercer will assess the ability and the efficiency of the manager in translating investment ideas into the actual portfolio. Mercer pays special attention to capacity issues at this stage.

d. Business Management

Business management refers to the overall stability of the firm, firm resources, and overall operations. This reflects how well Mercer thinks the business and the people who work in it are managed.

Some of the factors considered are the stability and viability of the asset management business of the firm as a whole, as well as the viability of the strategy. The likelihood of key staff retention and how well their interests are aligned with clients is also assessed. Mercer also evaluates how managers are managing their investment firms to understand the economic sustainability of the proposed mandate in the context of the firm.

Mercer will recommend products based on the following factors:

1. Mercer’s qualitative assessment (relative to the four factor framework described above)
2. Fees versus peers in the retail universe
3. Performance versus peers in the retail universe

Prior to the due diligence activities, the managers will be required to provide both qualitative and quantitative data, based on the above four factors, on GIMD. For enquires on GIMD, please contact gimdadmin@mercer.com.

In addition, Mercer may issue a questionnaire to the managers, which needs to be completed before the meetings, so that preliminary analysis can be done in preparation for the meetings.
Required Documentation & Notification from FMCs/ Insurers

Note: The following provides the list of information that Mercer would need from the FMCs/ Insurers for evaluation purposes.

FMCs/ Insurers are required to submit to Mercer, via cpfis@mercer.com, the following:

<table>
<thead>
<tr>
<th>Documents</th>
</tr>
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<tbody>
<tr>
<td><strong>1. Investment Capabilities/ Product Evaluation</strong></td>
</tr>
<tr>
<td>- FMCs/ Insurers are required to update the information on GIMD <em>within ten (10) working days from the date the request for evaluation is submitted</em> (or earlier depending on the meeting scheduled).</td>
</tr>
<tr>
<td>- FMCs/Insurers are required to submit the completed questionnaire <em>within ten (10) working days from receiving the questionnaire</em> (or earlier depending on the meeting scheduled).</td>
</tr>
<tr>
<td><strong>2. Operational Risk Assessment</strong></td>
</tr>
<tr>
<td>- FMCs/Insurers are required to submit the completed questionnaire <em>within ten (10) working days from receiving the questionnaire</em>.</td>
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</tbody>
</table>
Note: The following provides the list of information that Mercer would need from the FMCs/Insurers for monitoring purposes.

FMCs/Insurers are required to submit to Mercer, via cpfis@mercer.com, the following:

<table>
<thead>
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<th>Documents</th>
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<tbody>
<tr>
<td><strong>1. Prospectus</strong></td>
</tr>
<tr>
<td>▪ Whenever there is an update to the prospectus, FMCs/Insurers are required to submit the updated prospectus <em>within ten (10) working days</em>.</td>
</tr>
<tr>
<td>▪ If there are no updates to the prospectus, FMCs/Insurers are required to send an email, stating that there are no changes to the prospectus, every half yearly <em>within ten (10) working days from the end of the 6th month</em>.</td>
</tr>
<tr>
<td>▪ FMCs/Insurers are required to start their email subject lines with “Prospectus: &lt;FMCs/Insurers name&gt;”</td>
</tr>
<tr>
<td><strong>2. Notification of any Significant Events</strong></td>
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<tr>
<td>▪ Events such as (but not limited to) changes in the organisational structure/management of the firm, changes to the investment team, philosophy or process in relation to the product on CPFIS, corporate actions, regulatory issues, should be highlighted <em>within ten (10) working days</em>.</td>
</tr>
<tr>
<td>▪ If there are no notifications of any significant events, FMCs/Insurers are required to send an email, stating that there are no updates, every half yearly <em>within ten (10) working days from the end of the 6th month</em>.</td>
</tr>
<tr>
<td>▪ FMCs/Insurers are required to start their email subject lines with “Event: &lt;FMCs/Insurers name&gt; - &lt;Subject Title&gt;”, e.g. “Event: ABC Management – Change in Portfolio Manager for Singapore Bonds”</td>
</tr>
<tr>
<td><strong>3. Monthly Fact Sheets</strong></td>
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<tr>
<td>▪ FMCs/Insurers are required to submit monthly fund fact sheets at the end of each calendar quarter <em>within ten (10) working days from the quarter end</em>. For example, for the quarter ending March 2016, the FMC/Insurer is required to submit the fact sheets for January, February and March 2016 <em>together</em> by 14 April 2016 (10 working days).</td>
</tr>
<tr>
<td>▪ FMCs/Insurers are required to start their email subject lines with “Fact Sheets for &lt;Q# YYYY&gt;: &lt;FMCs/Insurers name&gt;”, e.g. “Fact Sheets for Q1 2016: ABC Management”</td>
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</tbody>
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*Please do not send any marketing messages to cpfis@mercer.com, the mailbox is strictly for the correspondence of the aforementioned documents.*

For enquiries in relation to the evaluation process for inclusion, please contact cpfis@mercer.com.