

Vanuatu National Provident Fund Board

Approved Investment Guideline

GOUVERNEMENT DE
LA REPUBLIQUE DE VANUATU

MINISTERE DES FINANCES ET DE
LA GESTION ECONOMIQUE

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GOVERNMENT OF THE REPUBLIC OF
VANUATU

MINISTRY OF FINANCE AND
ECONOMIC MANAGEMENT

PRIVATE MAIL BAG 058, PORT VILA,
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Le Ministre/The Minister

Our/Notre ref:
Your/Votre ref:

26th February, 2007

Mr. Kelip Sandy,
General Manager,
Vanuatu National Provident Fund,
PO Box 420,
PORT VILA.

Dear Mr. Sandy,

Re: VNPF Investment Guideline

Reference to your letter of 12th October, 2006 followed by a meeting on 23rd February, 2007 I am please to advice you that after reviewing the propose Investment Guideline, I hereby approve the propose Guideline as required under VNPF Act (Cap 189 as amended).

I hope the propose changes will serve the propose for which it is intended accordingly.

Yours faithfully,

A handwritten signature in black ink, appearing to read 'Willie Jimmy Tapanga Rarua', written over a horizontal line.

Hon. Willie JIMMY TAPANGA RARUA
Minister of Finance and Economic Management



Cc: To Chairman – VNPF Board
: To Director General - MFEM



RESERVE BANK OF VANUATU

PMB 9062 - EMILE MERCET STREET- PORT VILA - VANUATU
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10 October 2006

Mr. Kelep Sandy
General Manager
Vanuatu National Provident Fund
PO Box 420
Port Vila


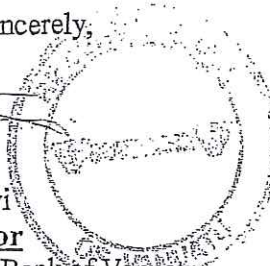


Dear Mr. Sandy,

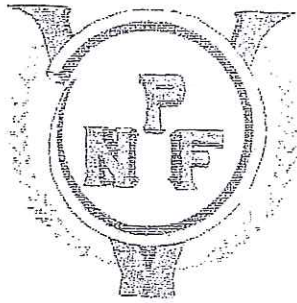
Re: VNPF Investment Guideline

After reviewing your Investment Guideline, I would like to advise you that the Reserve Bank of Vanuatu is content with the changes and the guideline itself. We are looking forward for the Minister of Finance's approval.

Yours sincerely,

Odo Tevi
Governor
Reserve Bank of Vanuatu



VANUATU NATIONAL PROVIDENT FUND

Investment Policy Guidelines

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1.0 Introduction

The Vanuatu National Provident Fund (VNPF/the Fund) is an Accumulation Fund (Defined Contribution Plan). Contributions and interest are credited to a member's account, and the accumulated amount in the member's account forms the benefit payable to the member on retirement or as provided in the VNPF Act (CAP 189, as amended).

This investment policy includes guidelines for asset allocation, funds management, investment performance monitoring and investment performance benchmarks. Throughout this document, all references to members' funds includes both members' funds and the General Reserve. The guidelines have taken into consideration the key provisions of VNPF Act (CAP 189, as amended), and in particular Section 16, in relation to the investment policy of the Fund.

2.0 Objective of the Fund

The overall objective of the Fund is to maximize and protect Provident Fund benefits to all its members, and to provide them with a level of service to which they are entitled. In addition, the Fund may offer other benefits to improve the living standards of all its members, without putting at risk the main purpose of the Fund.

3.0 Purpose of the Investment policy guidelines

The purpose of this policy is to

- define the overall objective of the Fund;
- define the limitations regarding the investment of Fund assets;
- assign responsibilities for investing activities;
- establish a basis for evaluating investment results.

4.0 Investment policies

4.1 While pursuing the outlined objectives, the Fund should display the characteristics of a conservative Fund and pursue a balanced investment portfolio to minimize portfolio risk (volatility of returns) taking into consideration section 16 of the VNPF Act (Cap 189, as amended). This will be achieved through diversification, where the primary objective is to achieve sustainable level of portfolio return within acceptable risk limits. It is recognized that a depressed investment environment may result in a negative return on investments in particular years. This could result in the value of members' accounts falling in any particular year. However, over the medium to long term, the Fund should achieve a positive return on members' funds

4.2 In making decisions on investment strategy, the Board will have regard to the overall circumstances of the Fund, and will comply with all applicable legislative requirements.

4.3 The Fund's investments will be managed with a view to ensuring that the Fund will have sufficient liquidity to meet expected cash flow requirements.

4.4 Investment risk will be limited by appropriate diversification both within and between asset classes

4.5 Board approval will be required for investments of more than 1% of members' funds or Vt10 million (whichever is the lower) in any one asset or security unless otherwise stated.

4.6 Holdings of 10% or more of Members' funds in any one asset or security will be notified to members in the annual report.

4.7 Fund Manager

4.7.1 The Board shall appoint a Funds Manager in accordance with section 16A of the VNPF Act (CAP 189, as amended) who shall be responsible for managing an amount not exceeding 15% of the moneys belonging to the Fund.

4.7.2 The Funds Manager shall manage the moneys in accordance with section 16B of the VNPF Act (CAP 189, as amended).

4.7.3 The terms of the Fund Manager's appointment will be in accordance with sections 16A to 16E of the VNPF Act (CAP 189, as amended).

4.8 The Fund may maintain a General Reserve comprising amounts of investment income not allocated to or earned by the members during the financial year.

4.9 Investment Committee

4.9.1 The Board shall appoint an Investment Committee to assist the Board in evaluating the performance of the Funds' investments. The Investment Committee will participate in the formulation of and execution of investment policy, objectives and guidelines; evaluating Fund Managers; reviewing such Fund Managers over time; measuring and reporting investment performance; and other tasks as deemed appropriate.

4.9.2 The Investment Committee shall consist of five members appointed by the Board of whom at least one may be an independent member with expert knowledge and experience in managing investment funds and portfolios.

4.9.3 The independent member must be a fit and proper person. If he/she, at any time, does not meet the generally accepted criteria for fitness and propriety then he/she is not qualified to be an independent member. The Committee may co-opt for specific areas of expertise necessary to evaluate matters as they arise.

4.10 Exposure to Vanuatu Government assets (including bonds, loans and treasury notes) shall not exceed 40% of members' funds.

4.11 The Fund is prohibited from borrowing except as provided under section 18 of the VNPF Act (Cap 189, as amended).

4.12 Where due to circumstances beyond the control of the Board, the percentages as allocated for a particular asset class is due to be exceeded and in that event, the Board shall inform the Minister in writing explaining the circumstances and reasons for such occurrence.

5.0 Investment strategies

The investment strategies should focus on two primary objectives i.e. to maximise long term fund returns and to manage and control business and investment risks. This strategy inherently requires the Fund to pursue a balanced investment strategy which seeks capital growth over the medium to long term with moderate income streams. The strategies should be within the parameters set out in the VNPF Act (CAP 189, as amended),

6.0 Risks and risk management

The risk management process involves the systematic application of management policies, procedures and practices to the tasks of establishing the context, identifying, analysing, evaluating, treating, monitoring and communicating risks.

The general risk management approach to be adopted by the Fund is as follows:

(i) Diversification

Through diversification, the Fund will reduce the volatility of its investment portfolio by potentially offsetting the losses in one asset class with the gains in another;

The overall return on members' funds will therefore be more stable as the portfolio is less dependent on the return from any single asset class;

(ii) Investment timeframe

The Fund will adopt a long term investment approach for those asset classes that historically experience short term volatility. This reduces the risk of investment losses;

(iii) Review

The Board will regularly monitor and review the Fund's investments against the benchmarks and performance standards outlined further in this document to ensure that the investment profile does not expose the Fund to any unacceptable or avoidable level of risk; and

(iv) Reporting

Regular reporting by the Investment Committee to the Board as outlined in 4.0 Investment Policies will occur to ensure that informed decisions regarding the Fund's investments can be made.

7.0 Liquidity and cash management

To minimise the possibility of a loss occasioned by the sale of an asset or security forced by the need to meet a required payment, the management and staff of the Fund will periodically provide the Investment Committee/Board with an estimate of expected net cash flow. They will notify the Investment Committee/Board in a timely manner to allow sufficient time to build up necessary liquid reserves.

The Investment Committee will provide the Board with forward cash flow estimates as part of its monthly report. Based on these estimates, the Board will determine broad targets for the level of available investment funds that are to be held in cash or cash equivalent forms.

8.0 Asset allocation

All investments undertaken should balance risk against returns. The investment strategies adopted should be pursued in a manner which takes into consideration the right mix of growth and defensive assets (sometimes referred to as income assets) to best suit the needs of the members as well as the requirements of the VNPF Act (CAP 189, as amended).

Growth assets are investment vehicles such as shares and property that are very responsive to market fluctuations. They therefore involve a high degree of risk, but have the potential to provide a higher return.

Defensive assets such as cash and Government Bonds are less susceptible to market fluctuations and are therefore less risky investments. However, with this reduction of risk comes a reduced potential for growth.

A risk profile well suited to VNPF would be low to medium risk levels.

Risk Classification	Minimum Range	Preferred Range (neutral)	Maximum Range
Defensive Assets	20%	60%	70%
Growth Assets	15%	40%	70%

The investment strategy adopted will be to pursue an investment position of 5% or more towards growth assets than income assets to maintain capital stability. The Board of Trustees may move either way within the preferred range by up to 25% in either income or growth assets. However, the Fund is not in a position to immediately shift to Growth assets due to limited on-shore opportunities in these areas and the restrictions on investment in overseas assets.

Portfolio risk will be managed by asset allocation over or below the preferred (neutral) position and the Board of Trustees can take an aggressive or conservative position depending on the economic circumstances prevailing at that time.

Proposed Asset allocation

Asset allocation decisions really serve to define the overall risk of the portfolio. Within the asset allocation framework, there are two structural tiers: -

Sector Ranges

This defines the high and low extremes within which each asset class may move in response to changing economic conditions

Neutral and Benchmark Positions

This defines the average exposure to each asset class assuming that the outlook for each asset class is in balance with the other.

Asset Class	Sector Range Low - High	Neutral Allocation
Cash	5 - 10%	5%
Fixed Interest	15 - 45%	45%
Loans	0 - 15%	10%
Equity	0 - 15%	5%
Property	10 - 40%	25%
Offshore	5 - 15%	10%

8.1 Vanuatu investments

8.1.1 Cash

Defined as liquid assets, call deposits, term deposits and treasury bills with maturity up to 90 days.

Performance measurement benchmark

The average of the cash deposit rate across all domestic banks applicable to an investment of the same amount over the same term during the same period.

Risk Management

- (i) Placement of call and term deposit should only be with RBV licensed financial institutions.
- (ii) Diversification to ensure that the exposure in any one financial institution not to exceed 50% of the cash portfolio.
- (iii) Ongoing assessment of annual reports of approved banks and financial institutions.

8.1.2 Fixed interest

Comprises interest bearing deposits with terms not less than 90 days, government bonds and securities, semi-government securities, and corporate securities.

Performance measure benchmark

Indicator Lending Rate (Ilr) across all domestic banks plus a margin according to risk profile.

Risk Management

- (i) Placement of interest bearing (term) deposit should only be with RBV licensed financial institutions
- (ii) Diversification to ensure that the exposure in any one financial institution not to exceed 50% of the fixed interest portfolio.
- (iii) Ongoing credit assessment.

8.1.3 Loans

Loans with terms beyond 2 years and not more than 15 years.

Indicator Lending Rate (Ilr) across all domestic banks plus a margin according to risk profile.

Risk Management

- (i) Loans to Semi Government and Corporate entities to be secured by primary mortgage against assets owned by the entities. The market value of the secured assets to exceed the loan amount by at least 30%.
- (ii) Borrowers to be able to demonstrate adequate repayment capacity.
- (iii) The Board's engagement in lending activities shall be in accordance with the prudential guidelines of the Reserve Bank of Vanuatu.

8.1.4 Equity

Ordinary or redeemable preference shares.

Performance measure benchmark

Currently there is no Stock Exchange in Vanuatu available to be used as Standard performance measure benchmark. The performance can be measured on the following basis.

- (i) Increase in value on annual independent valuation.
- (ii) The investment demonstrates that based on financial reports and other relevant information, it can produce an average earnings per share of 10% or more including anticipated capital growth over a rolling three year period.

Risk Management

- (i) Diversification between different industry sectors.
- (ii) Require audited financial statements to be provided to the Fund each year by those companies in whom the Fund invests.
- (iii) There shall be a realistic expectation that the investee company will be able to pay out dividends over the term of the investment.
- (iv) There shall be a clear objective for each equity investment covering such aspects as expected return on investment, anticipated period of holding and an exit strategy.
- (v) All equity investments to be approved by the Board and regularly monitored by the Investment Committee to ensure that objectives are being met and to assess the ongoing suitability of the investment with respect of the Fund's overall investment objectives.

8.1.5 Property

Investment in commercial, residential or industrial property for the purposes of generating rental income and potential capital gains.

Performance measure benchmark

Existing investments in property will continue to be managed efficiently and effectively to maximize the rates of return.

Effective from 1st January 2007, new investments in property can only be made if:

- (i) a head lease is signed with the lessee for a minimum lease period of ten years with option for renewal,
- (ii) the net lease rental provides a minimum return of 9% including anticipated capital growth, and
- (iii) the annual rental is adjusted for Vanuatu CPI, general market considerations and the general condition of the building including the cost of maintenance.

Risk Management

- (i) Proper management of all properties owned by the Fund and is administered by a staff of the Fund appointed for proper management of the Fund's Property portfolio with the responsibility for arranging maintenance when required, following up rent payments, etc.,
- (ii) Status of all the properties assessed by professional engineering consultants once every two years,
- (iii) All property investments including the existing property investments are valued once every two years by independent registered valuers.

8.2 Offshore Investments

Offshore (International) investment is for the purpose of risk management, diversification, taking advantages of overseas economic growth and currency hedging.

The Offshore (International) Investments will be made in investments products available in the market through appointed Fund Managers, subject to relevant professional advice. As part of the Contract with the Fund Manager, the Fund Manager shall report on a monthly basis to the Board on the performance of the Fund's investments.

Performance measure benchmark

Real return of 3% as defined in s.16B(5) of the VNPF Act (CAP 189, as amended).

Risk Management

Existing offshore investments will continue to be managed efficiently and effectively to maximize the rates of return.

- (i) Effective from 1st January 2007, new funds invested shall be hedged against Foreign exchange risks. The Fund will utilize professional advice including the Fund Managers' expertise on the hedging techniques.
- (ii) Credit worthiness of potential investments to be assessed prior to investment.

8.3 Prohibited Investments

- (i) VNPF shall not invest in:
 - Any non-income producing assets,
 - Property development companies,
 - Exploration companies, or
 - Start up companies.
- (ii) VNPF shall not lend money directly to a Fund member / Board member or an entity owned or controlled by a Fund member/Board member or Relative of a Fund member /Board member.
- (iii) VNPF shall not provide credit facilities to any company, individual, project or property unless there is a specific strategic or direct benefit to the Fund and its members
- (iv) VNPF will not refinance highly geared companies, properties or projects with equity or debt financing unless there is a specific strategic reason for participating on this basis, such as controlling the provision or continuation of essential services or benefits to members.
- (v) VNPF is not permitted to use derivatives, except for hedging purposes. Before derivatives can be purchased for hedging purposes, the investment committee must inform the Board as to the purpose of the hedging.
- (vi) VNPF shall not finance personal loans including housing loans or staff loans of any kind.

9.0 Divestment strategies

The Fund will consider divestment for the following reason: -

- (i) To rebalance the portfolio
 - To cash out to take advantage of significant capital appreciation
 - To cash up to take advantage of other good investment proposition
- (ii) The investment ceases to pay dividends and there is no expectation of adequate capital gains or recovery of the initial investment in the medium to long term.
- (iii) No capital appreciation or investment income.
- (iv) Predetermined benchmarks are not met.
- (v) Downgrade in profit or outlook for a company that will cause a reduction in value of the investment.
- (vi) A loan becomes non-performing with little or no prospect of full recovery.

10.0 Reporting

The Investment Department of VNPB Board is responsible for the maintenance of appropriate financial and statistical records relating to all Investments and Investment Income of the Fund in accordance with internal procedures and as well as for the safe keeping of all source documents relating to every transaction. The Investment Department is also responsible for the preparation of monthly and annual Investment reports. These reports are to be submitted to the Investment Committee on a timely basis to allow them to prepare their recommendations to the Board of Trustees.

The Investment Report should contain four basic elements:

- (i) Asset Allocation Information – Asset values and asset class percentages versus target allocation and ranges.
- (ii) Investment Performance – Investment returns versus Performance benchmarks.
- (iii) Guideline Compliance – A statement that each portfolio conforms to guidelines of identification and explanation where variances occur.
- (iv) Forward cash flow projections.

11.0 Management

- (i) The General Manager of the VNPB Board will be responsible for the implementation of the investment policy and strategies and arranging for professional advice where relevant.
- (ii) The Board of Trustees is responsible for making investment decisions and approval. Such decisions will be based on Investment Evaluation and recommendations submitted to the Board of Trustees by the General Manager through the Investment Committee on proposed and existing investments.

The Board of Trustees may delegate to the General Manager the responsibility of making investment decisions relating to placing funds in call accounts, term deposits with approved commercial banks, and subscribing to Government Bonds. When delegation is made, the Board will specify an upper limit to the amount which the General Manager is authorized to deal with, without Board approval. This may exceed the limit specified in policy 4.5, particularly in regard to liquid assets.

- (iii) The Funds Manager will provide monthly and annual reports of the Offshore Funds managed as per the agreement entered into with the Board of Trustees.
- (iv) This Investment Policy document shall be reviewed annually by the General Manager and the Board of Trustees, and any changes required or recommended are to be discussed with the appropriate authorities as specified in the VNPF Act (CAP 189, as amended).

12.0 Date of effect and amendments to this policy

In accordance with s16 of the Act (CAP 189, as amended), this policy document comes into effect when approved by order of the Minister for Finance. Any amendments to it must be approved by the Board and the Governor of the Reserve Bank of Vanuatu prior to it being approved by order of the Minister for Finance.

This is a policy guideline and not a procedural guideline