



Institute of Actuaries of India

Investment approaches adopted by Indian Provident Fund trusts

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Indian Actuarial Profession
Serving the Cause of Public Interest

Agenda



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- ❖ Guidelines for Trust investment
 - ❑ Process
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Key Facts about PF Trust investments



- 3221 exempted PF Trusts in India v/s 7.4 Lacs un-exempted establishments (0.4%)
- ~ 5.65 Million employees are members of exempted PF trusts v/s 83 Million in un-exempted establishment (6.8%)
- INR 14,458 Cr. Contributed by exempted trusts in 2012-13 v/s INR 45,798 Cr. by un-exempted organizations (31.5%)
- INR 2,02,114 Cr. total investments in respect of exempted establishments
- INR 22,693 Cr. invested in 2012-13 itself by exempted establishments

Thus, all the more need for professional outlook towards PF investments in Trusts and sound governance framework

Source: EPFO Annual Report 2012-13

Guidelines for Trust investment - Process



- Investments to be held till maturity unless the ratings drop below investment grade (Below 'A-')
- Incremental investments to adhere to prescribed pattern by 31st March of every year
- If securities fall below investment grade, permission to be sought from Regulator (EPFO) for liquidation
- Written permission to be sought from Regulator for liquidation of assets due to any bulk settlements (e.g. VRS)

Guidelines for Trust investment – Asset Allocation



| No. | Category of Investments | Allocation | |
|-----|--|-------------|-----------|
| I | Central Government Securities or Mutual Funds dedicatedly investing in G-Secs | Minimum 25% | Up to 85% |
| II | Securities issued by State Governments (State Development Loans) or Securities fully and unconditionally guaranteed by Central/ State Governments | Minimum 15% | Up to 75% |
| III | Bonds issued by PSU's or PSU Banks including Term Deposit Receipts | Maximum 30% | |
| IV | Any of the above categories as per Trustees' preference | Up to 30% | |
| V | Up to 1/3 rd of earmarked investment in Category IV in private sector bonds/ securities which have investment grade ratings from at least 2 rating agencies | Maximum 10% | |

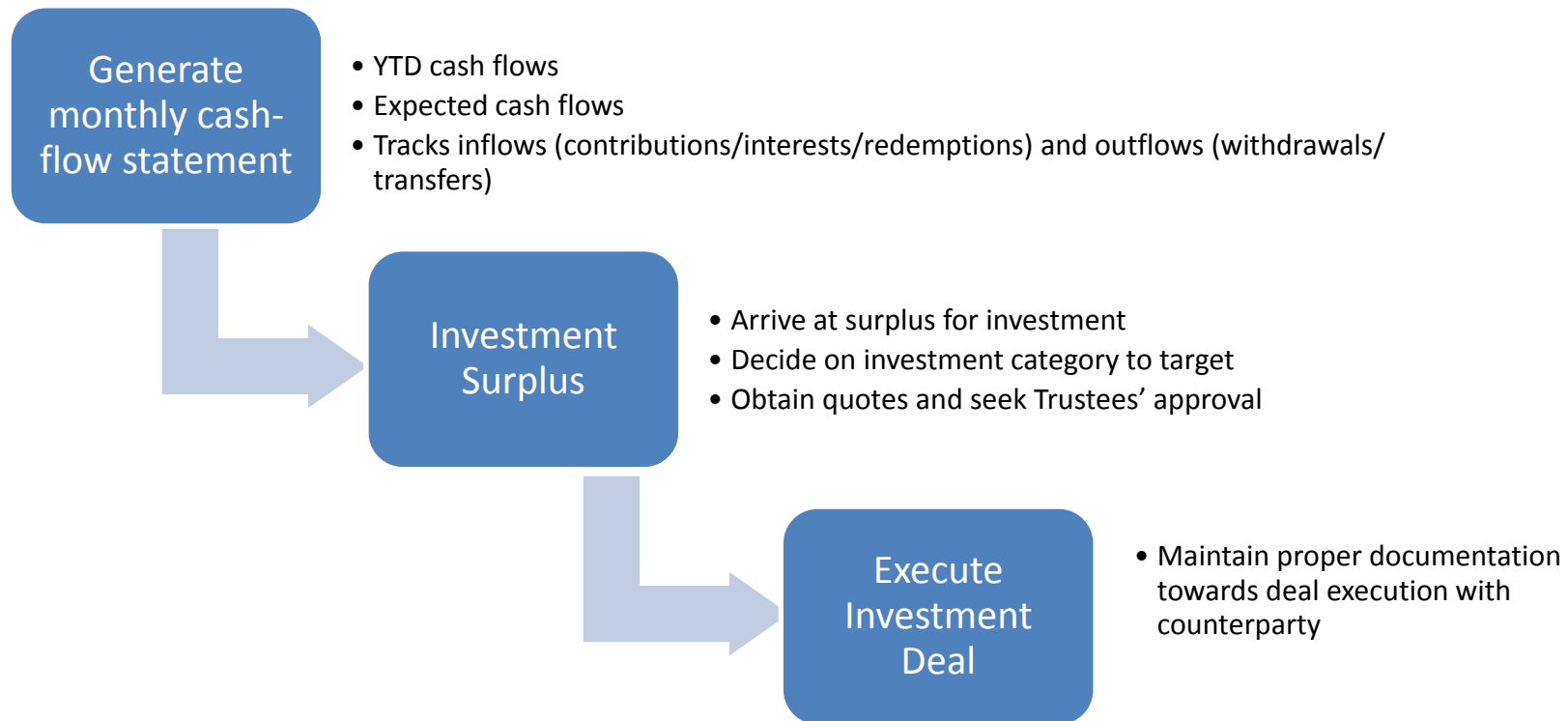
Source: Labour Ministry Notification dated 9th July 2003

PF Investment Objectives

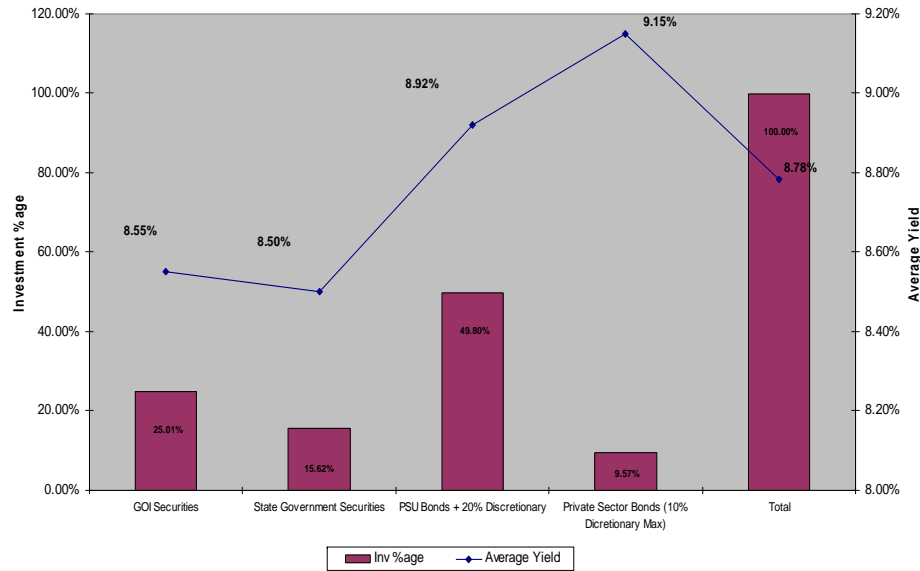


1. Safety & capital preservation
2. Return-maximization
3. Exposure diversification
4. Speedy investment of funds
5. Minimize asset-liability mismatch

Process followed by Organizations managing PF funds professionally



Portfolio Analysis – Annual Investment Split as per guidelines

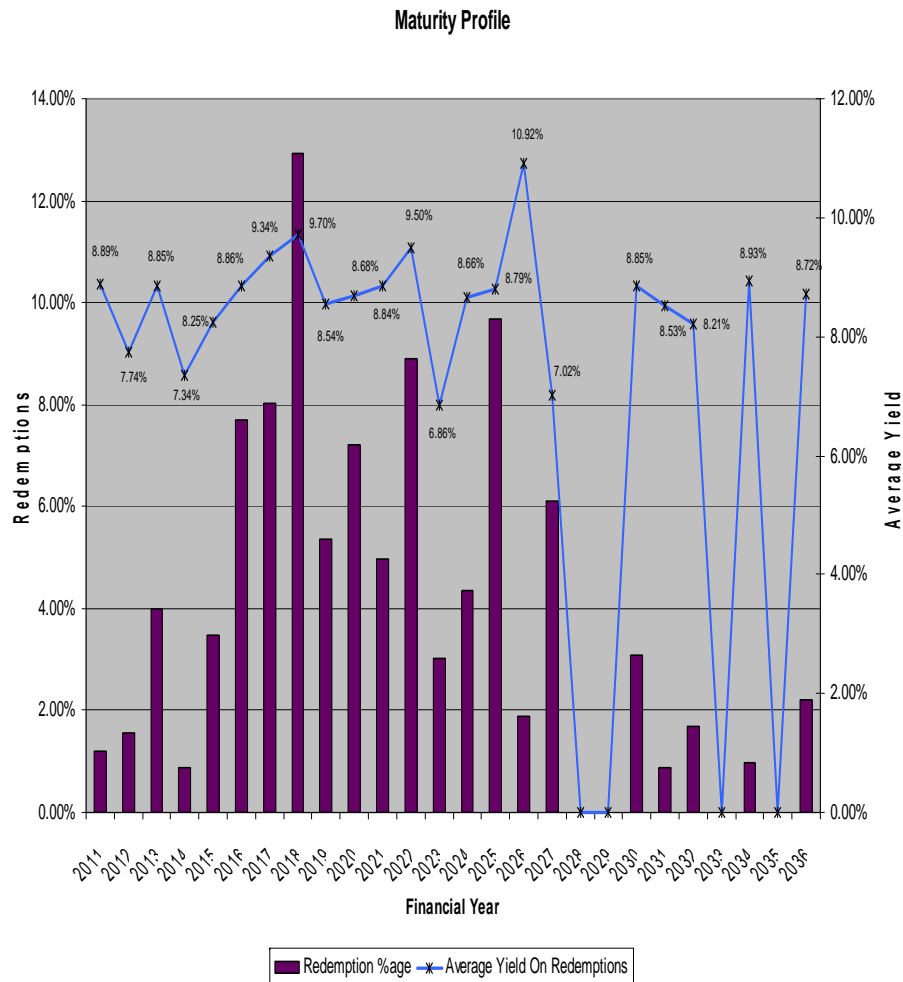


Insights on:

- Annual Compliance
- Average Yield achieved

| Investment Category | Inv %age | Investments | Average Yield |
|--|----------------|-----------------------|---------------|
| GOI Securities | 25.01% | 31,978,830.00 | 8.55% |
| State Government Securities | 15.62% | 19,970,750.00 | 8.50% |
| PSU Bonds + 20% Discretionary | 49.80% | 63,859,450.00 | 8.92% |
| Private Sector Bonds (10% Discretionary Max) | 9.57% | 12,232,700.00 | 9.15% |
| Total | 100.00% | 128,041,730.00 | 8.78% |

Portfolio Analysis – Maturity Profile



- Determines reinvestment risk or gains when greater proportion of high-yielding bonds mature in depressed interest rate scenario, leads to reinvestment loss and vice versa
- Determines relative holding period of bonds with varying risk profile
- Determines the level of annual earnings when premium is written off in the year of redemption
- Determines the extent of cost-efficiency of asset-liability management
 - When outflows are funded through current contributions in a rising interest rate scenario, it increases opportunity cost
 - When assets are liquidated to meet outflows, it exposes the fund to interest rate risk

However,

- It is difficult to predict normal attrition in a young work force (where average age and past service is lower), therefore avoid ALM
- For a matured work force (where average age and past service is higher), limited ALM is advisable

Portfolio Analysis – Yield Attribution & Residual Term

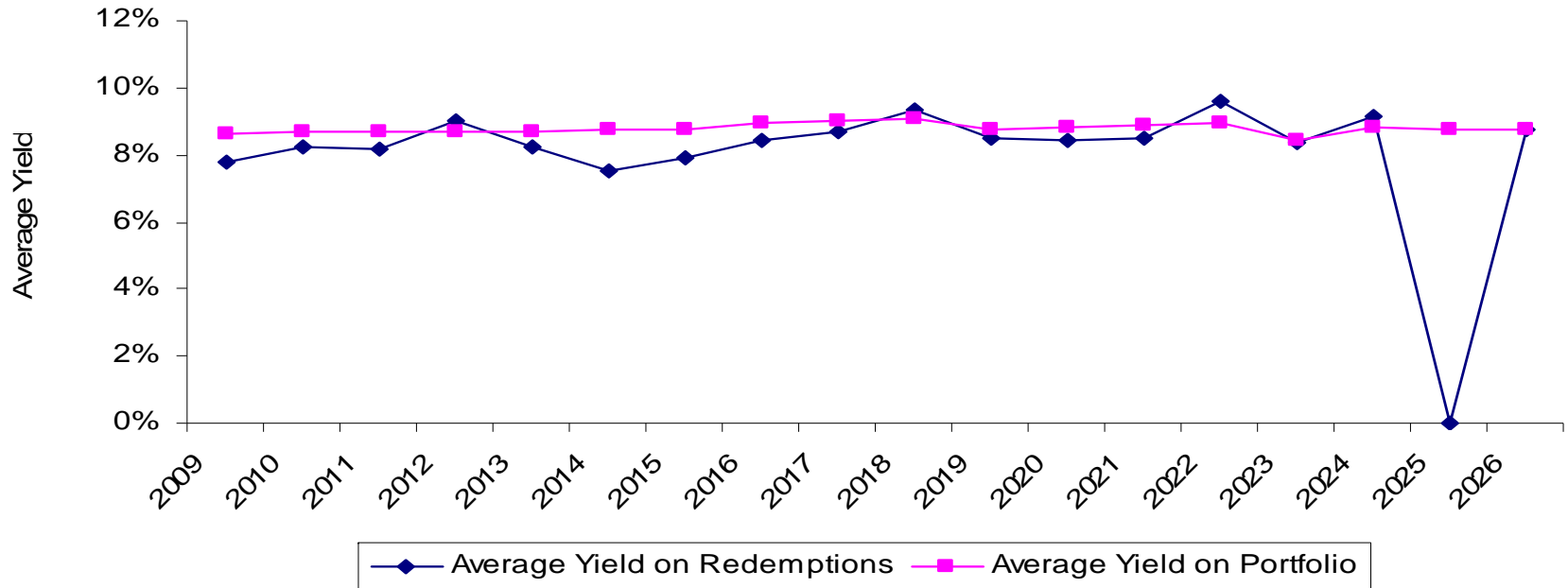


| Yield Range | | Proportion of Corpus | Residual Term in Years |
|-------------|--------|----------------------|------------------------|
| 5.00% | 5.99% | 1.21% | 11.12 |
| 6.00% | 6.99% | 5.14% | 15.70 |
| 7.00% | 7.99% | 7.25% | 8.64 |
| 8.00% | 8.99% | 48.43% | 11.01 |
| 9.00% | 9.99% | 25.87% | 9.84 |
| 10.00% | 10.99% | 8.03% | 8.93 |
| 11.00% | 11.99% | 2.51% | 10.54 |
| 12.00% | 12.99% | 1.56% | 7.69 |

Insights on:

- Proportion of corpus in each yield range and residual term of the same

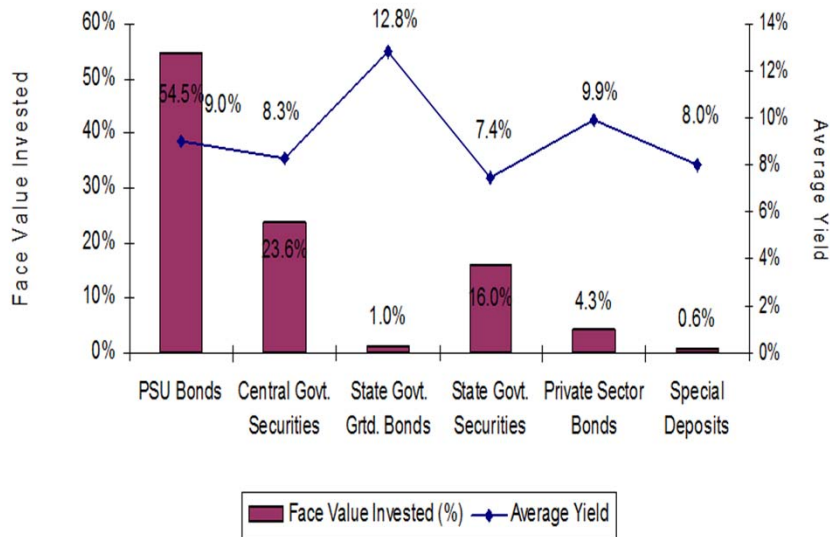
Portfolio Analysis – Impact of redemption on portfolio yields



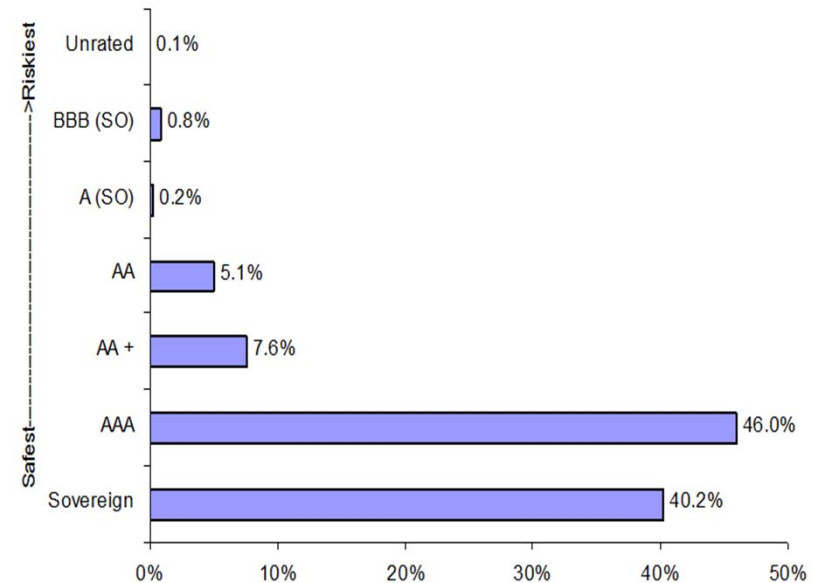
Insights on:

- Change in average yield on portfolio v/s average yield on redemptions

Portfolio Analysis – Exposure Profile Study



Portfolio Composition



Ratings Exposure

Why analyze exposure profile?

- Determines the level of credit risk
- Determines sustainability of returns
- Determines the possibility of cost devolvement on to the company
- Helps initiate corrective actions and policy formulation

Best Practices followed in the industry



- Shift the contribution date to the 1st or to the 1st week
- Increase frequency of investments to twice a month
- Sell low-yielding bonds to meet excess outflows
 - Post regulatory approvals and post thorough analysis of impact on returns & cost to company



Thank You