

Bureau of Labor Fund, Ministry of Labor

Investment Policy Statement of National Pension Insurance Fund

Approved by Ministry of Health and Welfare, 2015.08.26.

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PREFACE

“National Pension Insurance Fund” is superintended by Ministry of Health and Welfare. The matters related to premium receiving and benefit payments are commissioned to Bureau of Labor Insurance, Ministry of Labor; the matters related to investment are commissioned to Bureau of Labor Funds (BLF), Ministry of Labor; the matters related to supervision are mandated to National Pension Supervisory Committee, Ministry of Health and Welfare.

The investment of the Fund is in the charge of BLF. BLF comprises 5 Divisions and 4 administrative offices. Besides, BLF sets up Investment Strategy Panel and Risk Management Panel in charge of significant issues about investment and risk management.

I . PURPOSE

The practice of investment should follow basic principles founded by the Investment Policy Statement (IPS) and related regulations. We also expect the investment can achieve our goal by affirming investment purpose and beliefs, instituting basic policy, establishing regulation principles, legislating external regulation and internal rules.

II . PERIODICAL REVIEW

The IPS regulates basic investment principles. In addition to annually regular review, BLF will submit the modified version to Ministry of Health and Welfare for investment purpose and beliefs alteration, drastic market fluctuation, significant variation of cash flow pattern, etc.

INVESTMENT GUILDLINES

I . PURPOSE AND OBJECTIVE

The investment purpose is to protect beneficiaries' interest according to related regulation and through drafting of short, mid and long term plan, as well as to achieve the objective of sustainable operation.

II . BELIEFS

(I) Long-term-horizon Investment

- 1.Taking into account of the beneficiaries of long-term generations.
- 2.Maintaining the soundness and sustainability of the Fund.
- 3.Reducing the influence of short-term fluctuation through diversifying investment.
- 4.Subsuming Socially Responsible Investment (SRI).

(II)Manage and assume reasonable risk

- 1.Pondering on multi-faceted risks and instituting related policy, regulation, management and control rules in order to manage risks.
- 2.Legislating applicable restriction or regulation toward different risk-exposing assets and varied risk-tolerant Funds.
- 3.Exploiting definite strategies and techniques as well as the reciprocation of active and passive investment to increase long-term value of the Fund.
- 4.Weighing the status of politics and economy as well as the demand-supply uncertainty of natural resources in order to avert the effect from fluctuation of long-term trend toward portfolio return.

(III) Engage in effective monitoring and management

1. Ensuring the long-term rights and interests of BLF, beneficiaries, invested institutions, external investment entities and custodians.
2. Adopting effective performance measurement and risk control.
3. Keeping the consistency of the regulation toward external investment entities.

(IV) Explicit investment objective and return target

1. Setting up annual and mid-and-long term target performance.
2. Considering the equilibrium between return and risk.
3. Adopting explicit performance benchmark for external investment entities.

(V) Assets allocation strategy is a decisive factor for risk-return equilibrium

1. Contemplating the relation between varied risk factors and return, as well as diversifying investment.
2. Meditating the attribute, cash flow pattern and capital scale of the Fund in order to increase its return.
3. Reviewing the appropriateness of assets allocation when facing significant alteration of risk-return relation.

(VI) Reasonable management and operation cost

1. Deliberating the equilibrium between risk premium and operation cost.
2. Providing appropriate incentive to encourage external investment entities in order to increase long-term benefit of the Fund.
3. Duly utilizing investment scale to reach the objective of enhancing return, saving cost and reducing operation complexity.

III. THE PROCEDURE OF INVESTMENT DECISION

(I)Legislate investment policy and regulation

Investment policy and regulation should be enacted and modified as the occurring of significant alteration of investment strategies, beliefs and organization.

(II)Draft annual investment plan

“Annual assets allocation and investment plan” should be drafted prior to the beginning of every year. It should be presented to the Investment Strategy Panel, and submitted to the National Pension Supervisory Committee.

(III)Compose investment programs

Investment programs should be composed for every asset according to their characteristics. In terms of external-managed investment, investment entities should proceed with investing in accordance with the plans or researches following regular procedure.

IV. ASSETS ALLOCATION

(I)Set up investment proportion and range

- 1.Assets proportion target and range should be set up according to characteristics, position, attribute and regulations of the Fund.
- 2.Establishing different restrictions according to risk tolerance for assets which bearing higher market risk.

(II)Assess multi-faceted factors

- 1.Deliberating macro-economy, capital market outlook, stock and bond prospect during assets allocation process.
- 2.Pondering investment cost, expected return, volatility and correlation.
- 3.Subsuming the following factors in assets allocation: attribute of the Fund, net cash flow variation and risk tolerance.

(III)Implement assets allocation policy and plan

- 1.Gauging market status of respective assets to avoid that each asset position exceeds decided allocation policy and plan. Facing the extraordinary fluctuation of market, it's required to consider cost and liquidity in order to restore to allocation range timely.
- 2.Incorporating rebalance strategy by using central allocation target as foundation and max-min range as buffering.

(IV)Contemplate risk tolerance of the Fund

The risk tolerance of the Fund should be contemplated in assets allocation process. It depends on the cash flow pattern and attribute of the Fund. Risk budgets should be included when drafting annual plan.

V. RISK MANAGEMENT

BLF constitutes risk management division for monitoring risk and establishing control mechanism.

(I)Manage risk rather than eliminate it

Return is the outcome of risk taking. Instead of eliminating risk, the purpose of risk management is to seek for the equilibrium between risk-return and ensure that taking extra risk can get commensurate return.

(II)Institute management mechanism and procedure

Utilizing information system and adopting appropriate control measures to build up risk management mechanism.

(III)Set up risk limit and budget

The Fund should have sufficient elasticity to achieve return target under reasonable risk. The most applicable assets allocation and risk budget are obtained by utilizing allocation system for simulation through referring to the selected benchmarks, estimating return rate, gauging future trend as well as setting assets weighting and range according to current position and market capacity.

(IV)Stress test

Risk management division should carry out stress test periodically aiming at significant historic economy and finance events in order to estimate risk exposure and endurance in extreme condition.

(V)Constitute procedure to cope with ultra vires transactions

In the case of ultra vires transactions, it's necessary to be obedient to related regulation and commission contracts including notice, recognition of controversial issues, process, report, etc.

(VI) Legislate criteria of derivatives investment

Each investment division should enhance security, liquidity, profitability, or reduce risk when engaging in derivatives transactions. It's also necessary to conform to the essence of long-term steady operation. In the case of hedge purpose, total contract value of derivatives should not exceed total value of corresponding securities. Besides, derivatives trading cannot increase total financial leverage in the case of non-hedge purpose.

(VII) Establish comprehensive risk consciousness and regulation

Risk Management Panel and Risk Management Division should assist other departments to establish risk consciousness, as well as frame out operation procedure, internal control and risk management regulation.

VI. INVESTMENT EXECUTION

(I) Criteria for trading counterparties and intermediaries selection

The selected trading counterparties and intermediaries including brokers and dealers should be qualified for certain criteria such as credit rating and capital adequacy.

(II) Social responsibility

It's necessary to take social responsibility into consideration when choosing invested companies, it will be elaborately interpreted in next chapter.

(III) Best execution

It should be taken into consideration of fee, tax, amassed/scattered ordering cost and best efficiency for trading execution.

(IV) Assessable and reasonable benchmark

Investments should be provided with open market price, or evaluation by third party, or internal evaluation. It also should have reasonable benchmark to measure the performance.

(V) Independent custodians

The custody of assets should be administered by independent institutions for internal-managed or external-managed investments.

(VI) Security lending

It should be regulated when engaging in security lending. It's also necessary to follow the regulation of TWSE (Taiwan Stock Exchange) and GTSM (GreTai Security Market) for domestic security lending. In the case of overseas security lending, it's also necessary to regulate items about the qualification of intermediaries, collaterals, maintenance ratio. Moreover, the intermediaries should provide report about lending profit, quantity, market value, collateral ratio, expense, etc.

(VII) Regulation for external investment entities and custodians

BLF can arrange for external-management investment within the limit of ratio and amount in annual investment plan. The external investment entities or custodians should be selected through open tender process and also be reviewed periodically.

(VIII)Criteria toward external consultants

There should be criteria for the selection of investment and legal consultants. Commissioned investment consultant should provide recommendation proposal aiming at potential or existing external investment entities' staff and investment process. Commissioned legal consultants should provide legal recommendation or opinion statement according to the requirement of BLF.

(IX)Regulation for the disobedience of investment restriction

In the case of disobedience of investment restriction for the reason of market fluctuation, it should be settled during certain period of time. Facing the need of postponement or incapability of settlement, it's necessary to obtain approval from authorized superintendent. In the case of disobedience of investment restriction without paying attention, it should be settled promptly as well as submitting complete report and precaution measures to authorized superintendent. It's also necessary to obtain approval from authorized superintendent for postponement.

(X)Accounting and assets appraisal

Fund assets appraisal should follow government accounting regulation and Financial Reporting Standards according to investment characteristics.

VII. SOCIALLY RESPONSIBLE INVESTMENT

Socially Responsible Investment (SRI) refers to the conception that

it will get benefit for investment return as well as the whole society, environment and economy when considering the aspect of society, employees' benefit, human rights and environment in the investment process. We hereby set up SRI policy under the prerequisite of increasing return, and adopt related strategy gradually according to the developing stage of SRI. It will increase the benefit of the insured persons and encourage corporations to fulfill social responsibility, therefore attain win-win situation.

We take into account of environment, society, corporate governance, information disclosure in domestic investment. We also adopt investable and representable SRI indexes for domestic external-managed investment. Moreover, domestic external investment entities are requested to incorporate SRI into "Request for Service Proposal" for the selection reference. For the corporations seriously violating social responsibility, BLF will not invest or increase investment in them.

For the companies that BLF carries significant value of shares against total value of outstanding shares (or total net value of stock holding of the Fund), when they involve in major events relating to employees' benefit, environment protection and corporate governance, we will urge them to pay attention by shareholder activism such as converse, official letter, attending stockholders meeting and voting. Besides, we also interpret the definition and regulation of Corporate Social Responsibility (CSR) and SRI in our website. Furthermore, we will periodically announce the percentage of equity investments that meet public standard of CSR.

VIII. INFORMATION DISCLOSURE

Referring to the benefit of beneficiaries, BLF should disclose investment information to the public. BLF have been abiding by the resolution of imperative periodical disclosure items of government pension and insurance fund through negotiation between ruling and opposition party in the time of examining 2012 Central Government General Budget on 2012.12.14 in Legislative Yuan, ROC. The disclosure items include total amount of the Fund, investment performance, assets allocation, performance statistics report of domestic / overseas internal – managed / external – management investment. Besides, we also irregularly disclose information or press release referred to major events related to Fund investment in order to let the public grasp the picture of the Fund.

IX. ETHICS

(I)Internal staff

Interests conflict should be regulated for staff behavior in investment process including forbiddance of insider trading, canvass or lobby, social intercourse, etc.

(II)External entities and their staff

Commissioned institutions and their staff should abide by the ethics regulation of government, professional association and their own companies. They also bear the obligation for compensation when encountering the violation of above ethics regulation resulting in

damage of the Fund's benefit.

X. ASSETS AND BENCHMARK

The standards of assets classification are determined by the specific characteristics of assets and sufficient distinction from other assets including return, risk, correlation, asset scale, liquidity, etc.

The purpose of selecting benchmark is to provide long-term investment target. The benchmarks should be provided with investability, measurability, representability and clarity. The definition and benchmark for each asset are as follows:

(I) Domestic deposit

1. Definition : Taiwan-dollar (TWD) deposits saving in local banks.
2. Benchmark : One year large-amount average deposit interest rate from large banks.

(II) Domestic debt security

1. Definition : TWD-denominated debt securities including:
 - (1) Short-term commercial paper.
 - (2) Money market fund.
 - (3) Bond : Including government bonds, financial institution bonds, corporate bonds, and other bonds, as well as lending transactions and derivatives.
2. Benchmark :
 - (1) Short-term commercial paper : 30-day domestic commercial

paper average interest rate.

(2) Money market fund : 30-day domestic commercial paper average interest rate.

(3) Bond :

① Government bond : Yield of 10-year domestic government bonds.

② Financial institution bond : Yield of 7-year A-credit-rating financial institution bonds.

③ Corporate bond : Yield of 5-year A-credit-rating corporate bonds.

④ Other bond : Appropriate benchmark.

(III) Domestic equity security

1. Definition : TWD-denominated securities with the trait of directly or indirectly possessing stockholder's equity, as well as lending transaction and derivatives.

2. Benchmark : "Taiwan Stock Exchange Capitalization Weighted Stock Index" or appropriate benchmark.

(IV) Domestic alternative investment

1. Definition : TWD-denominated investments not belong to deposit, debt security or equity security.

2. Benchmark : Appropriate benchmark according to realistic environment.

(V) Overseas debt security

1. Definition : Non-TWD-denominated securities with the trait of debt, including foreign currencies, lending transaction and derivatives.

2.Benchmark : Barclays Capital Global Aggregate Bond Index or appropriate indexes.

(VI)Overseas equity security

1.Definition : Non-TWD-denominated securities with the trait of directly or indirectly possessing stockholder's equity, as well as lending transaction and derivatives.

2.Benchmark : MSCI AC World Index or appropriate indexes.

(VII)Overseas alternative investment

1.Definition : Non-TWD-denominated investment not belonging to deposits, debt securities or equity securities.

(1)Property and land : Including overseas real estate, infrastructure, real estate trust investment, property trust beneficiary certificates, as well as other securitized products and derivatives.

(2)commodity : Including overseas precious metals, energy resources, natural resources, as well as securitized products and derivatives.

(3)Others

2.Benchmark : FTSE EPRA/NAREIT Index 、Dow Jones Brookfield Global Infrastructure Index or other appropriate indexes.

INVESTMENT POLICY

According to the Fund's attribute and cash flow pattern, risk tolerance are divided into five levels such as high, middle-high, middle, middle-low, low. Investment target and strategy limitations are set according to risk tolerance and fluidity requirement. Generally speaking, risk tolerance of defined-contribution Funds is divided into high or middle-high; the one in defined-benefit Funds is divided into middle, middle-low or low according to their net cash inflow(>0, =0, <0). "National Pension Insurance Fund" belongs to defined-benefit scheme. It's in the early developing stage, and therefore the cash inflow outnumber outflow. Consequently, the risk tolerance is classified as "middle".

(I)Introduction

"National Pension Program" was launched in 2008.10.1. It targets the insured registered in ROC whose age are over 25 and under 65 except for those have already participated in Labor Insurance, Farmer's Health Insurance, Civil Servant and Teacher Insurance and Military Personnel Insurance. National Pension Program offer three types of annuity payments including the " Old-Age Pension", "Disability Pension" and "Survivors Pension", as well as two types of lump sum benefits including the "Maternity Benefit" and "Funeral Benefit". All insured persons who have paid the premium in a timely manner are eligible to receive the relevant pension benefit or lump sum payment for the following conditions: giving birth, physically or mentally disabled (degree "severe" or above), passing away, attaining the age of 65. The purpose is to protect the basic economic safety of the insured persons or their surviving dependents. Among the benefits above, "Old-Age Pension" adopts defined-benefit system.

BLF proceeds with investing according to related regulations including “Regulations for Management, Utilization and Supervision of the National Pension Insurance Fund”, “Operation Directions for Management and Utilization of the National Pension Insurance Fund”, etc.

(II)Mission and targets

- 1.Fundamental mission : The missions is to increase long-term performance, mitigate the pressure of increasing insurance premium by premises such as fulfilling the royal obligation of administrator, upholding steady operation and advocating long-term horizon investment.
- 2.Risk tolerance target : Periodically tracking funding ratio; pursuing maximum return under endurable medium risk.
- 3.Liquidity target : Maintaining sufficient medium liquidity in order to meet the gap between premium revenue and payments for each year.

(III)Mid and long term return target

The mid and long term return target of the Fund is that 5-year-average real return rate exceeds corresponding period of 2-year-deposit-interest-rate of “Bank of Taiwan” plus annual growth rate of consumer price index. Simultaneously, the growth/decline of Fund, and contents of actuarial report will be referred to.

(IV)Strategies

Following the above-mentioned overall policy such as assets

allocation and risk management, the specific investment strategies for the Fund are as follows:

1. Asset allocation : Diversification of investment and risk is the principle of assets allocation. We construct efficient portfolio in accordance with financial condition of beneficiaries, global economy situation, market outlook, investment target, revenue-expenditure status, etc.
2. Internal-managed and external-managed investment : Investments are handled by both internal-managed and external-managed modes. Domestic equity securities are mainly handled by internal-managed mode.
3. Active and passive investment : The investments are handled by both active and passive modes.