

**Item No. 9: Diversification of investments in Exchange Traded Fund (ETF) under category (iv) i.e. investment in Equity and related investments of Investment Pattern 2015.**

1. The Government of India vide notification no. S.O. 1071 (E) dated 23rd April, 2015 had notified Investment Pattern for investments of Central Board, EPF. Category (iv) of said Pattern provides minimum 5% and upto 15% investment in Equity and Related Investment. Sub-Category (c) of said Category (iv) provides investment in “Exchange Traded Funds (ETFs) / Index Funds regulated by the Securities and Exchange Board of India that replicate the portfolio of either BSE SENSEX Index or NSE Nifty 50 Index”. Accordingly, the investments are being made in Exchange Traded funds (ETFs) based on Nifty 50 and SENSEX indices as prescribed in the Pattern of Investment.
2. An agenda items on “Diversification of investments in Exchange Traded Fund (ETF) under category (iv) i.e. investment in Equity and related investments of Investment Pattern 2015” was placed in 220th Central Board of Trustees’ EPF meeting held on 21st February 2018, wherein the Central Board had suggested that the summary of the Consultant furnished in the agenda item was not complete and the matter will be further examined in Consultation with the Consultant. (Agenda & Minutes enclosed as **Annexure-9A**).
3. In pursuance to the direction of Central Board, the matter has been re-examined by M/s CRISIL, the Consultant of EPFO. In order to summarize the findings, CRISIL has carried out the ranking of these indices using an approach similar to that used by CRISIL to carry out ranking of equity mutual funds which are published in the public domain on a quarterly basis. Ranking of the above said indices is based on the following parameters for the period December 16, 2005 to March 28, 2018:
  - a) **Mean return (55% weight)**

Mean return is the average of the 5 year annualised returns calculated on a daily basis.
  - b) **Volatility (25% weight)**

Volatility is the standard deviation of the 5 year annualised returns.
  - c) **Industry Concentration (10% weight)**

Industry concentration measures the risk arising out of improper diversification in terms of industry level exposure. Diversity score is used as the parameter to measure industry concentration. It is calculated as the square root of the sum of squares of the percentage exposure in the portfolio. Lower the diversity score, lower the concentration.
  - d) **Company Concentration (5% weight)**

Company concentration measures the risk arising out of improper diversification in terms of stock level exposure. Diversity score is used as the parameter to measure company concentration. It is calculated as the square root of the sum of squares of the percentage exposure in the portfolio. Lower the diversity score, lower the concentration.

**e) Liquidity (5% weight)**

Liquidity is a measure of the ease with which the portfolio can be liquidated. Impact cost of the portfolio is used as the parameter to measure the liquidity. Impact cost of the portfolio is calculated as the weighted average of impact cost of individual stocks in the portfolio as obtained from the BSE. Lower the impact cost, greater is the liquidity.

4. For the above ranking parameters, values have been computed as under:-

**Table 1 - Parameter values**

Index	Mean return	Volatility	Company Concentration	Industry Concentration	Liquidity
Nifty 50	10.48%	4.38%	20.31	35.70	0.0217
Nifty Next 50	14.62%	6.59%	16.08	30.40	0.0445
S&P BSE SENSEX	10.50%	4.59%	23.74	39.81	0.0204
S&P BSE SENSEX Next 50	12.95%	5.32%	15.20	27.92	0.0423
S&P BSE MidCap Select Index	15.49%	6.95%	18.96	26.70	0.0450

5. Based on the parametric values, scoring has been done on a scale of 0 to 100, the best scoring getting 100% and all others scaled accordingly. The parametric score and composite rank is as under:-

**Table 2 - Parametric score and composite rank**

Scoring (scale of 0% to 100%) and ranking							
Parameter ->	Mean return	Volatility	Company Concentration	Industry Concentration	Liquidity	Weighted score	Rank
Weight ->	55%	25%	5%	10%	5%		
S&P BSE MidCap Select Index	100.00%	62.98%	80.15%	100.00%	45.40%	87.02%	1
Nifty Next 50	94.41%	66.45%	94.52%	87.84%	45.88%	84.34%	2
S&P BSE SENSEX Next 50	83.58%	82.25%	100.00%	95.65%	48.21%	83.51%	3
Nifty 50	67.66%	100.00%	74.84%	74.80%	93.90%	78.13%	4

6. All the three Indices being considered for diversification S&P BSE MidCap Select Index, S&P BSE SENSEX Next 50 and Nifty Next 50 fares better in the composite weighted score and rank than Nifty 50 and S&P BSE SENSEX. We may accordingly select all the three S&P BSE MidCap Select Index, S&P BSE SENSEX Next 50 and Nifty Next 50 for investment in their Exchange Traded Fund.
7. Further as mentioned in Para 1 above, category (iv) (c) of Pattern of Investment states that *'Exchange Traded Funds /Index Funds regulated by the SEBI that replicates the portfolio of either BSE SENSEX or NSE Nifty 50 Index'*. Thus the Pattern of Investment notified by the Central Government has to be suitably amended to include other than Nifty 50 and Sensex Indices.
8. Accordingly the existing clause (iv) (c) may be substituted in line with existing clause (iv) (b) as under: *"Exchange Traded Funds (ETF)/Index Funds regulated by the Securities and Exchange Board of India, which replicate the portfolios which have all their investment in shares of body corporates listed on BSE or NSE and also satisfies the conditions mentioned in clause (iv) (a) (i) and (ii) of this Investment Pattern."* This amendment in the Investment Pattern shall enable investment by EPFO in the equity index ETF beyond Nifty 50 and Sensex ETF.
9. Further in the 220<sup>th</sup> meeting the Central Board on 21<sup>st</sup> Feb, 2018 it was also decided that training needs to be organized at PDNASS on ETF for all the Central Board members. Accordingly a training programme was organized on Exchange Traded Funds (ETFs) on 16<sup>th</sup> March, 2018.
10. The above said agenda is being placed in the 139<sup>th</sup> FIAC meeting held on 25.06.2018. The recommendation of the Committee will be placed before the Board on table.

**Proposal:**                      **Para 6, 7 and 8 of the above item is placed before the CBT for its approval.**

**Item No. 11: Diversification of investments in Exchange Traded Fund (ETF) under category (iv) i.e. investment in Equity and related Investments of Investment Pattern 2015.**

The Government of India vide notification no. S.O. 1071 (E) dated 23<sup>rd</sup> April, 2015 had notified Investment Pattern for investments of Central Board, EPF. Category (iv) of said Pattern provides minimum 5% and upto 15% investment in Equity and Related Investment. Sub-Category (c) of said Category (iv) provides investment in "Exchange Traded Funds (ETFs) / Index Funds regulated by the Securities and Exchange Board of India that replicate the portfolio of either BSE SENSEX Index or NSE Nifty 50 Index". Accordingly, the investments are being made in Exchange Traded funds (ETFs) based on Nifty 50 and SENSEX indices as prescribed in the Pattern of Investment.

2. The Expert Group constituted by FIAC to examine alternate strategies for investments in ETF in its report suggested alternate ETFs investment other than Nifty 50 and SENSEX in order to optimise return with minimum risk. The Expert group among other things also suggested that indices such as Nifty Next 50, S&P BSE Midcap Select or other indices can be considered provided the Index constituents are within top 100 stocks by market capitalization at the time of final selection of indices.

3. The suggestions of India Index Services and Products Ltd (NSE) and Asia Index Private Limited (BSE) were again sought recently on the possible indices within the top 100 companies by market capitalisation. In response, S&P, BSE vide email dated 12.07.2017 (**Annexure-11A**) and NSE vide mail dated 13.07.2017 (**Annexure-11B**) furnished suggestions on alternate strategies for investments in ETFs. Inputs received from BSE & NSE were forwarded to the Consultant for comments.

4. The Consultant of EPFO, M/s. CRISIL Ltd provided comments on the inputs received from BSE & NSE on alternative strategies for EPFO's investment in ETF. The Consultant has furnished its comments (**Annexure-11C**), which includes a comparative analysis of the following indices:

- I. S&P BSE Midcap Select Index
- II. S&P BSE SENSEX Next 50
- III. S&P BSE SENSEX
- IV. Nifty Next 50
- V. Nifty 50.

5. The Consultant has highlighted following key points/messages:

- I. Diversification: Addition of stocks beyond Nifty 50 and S&P BSE SENSEX would improve overall portfolio diversification in terms of company as well as sector exposure.
- II. Returns: Returns of S&P BSE MidCap Select, S&P BSE SENSEX Next 50 and Nifty Next 50 indices are higher in comparison to that of S&P BSE SENSEX and Nifty 50 over the trailing periods of 1 year, 3 years and 5 years.
- III. Market risk: S&P BSE MidCap Select, S&P BSE SENSEX Next 50 and Nifty Next 50 indices have higher volatility in comparison to that of S&P BSE SENSEX and Nifty 50 over the trailing periods of 1 year, 3 year & 5 Years.
- IV. Returns adjusted for risk: S&P BSE MidCap Select, S&P BSE SENSEX Next 50 and Nifty Next 50 indices have delivered higher return per unit of risk (volatility) in compare to that of S&P BSE SENSEX and Nifty 50 on the basis of rolling returns for ten-year holding periods.
- V. Maximum Drawdown and impact cost: S&P BSE MidCap Select, S&P SENSEX Next 50 and Nifty Next 50 indices have relatively higher drawdown and impact cost in comparison to S&P BSE SENSEX and Nifty 50.

- VI. Concentration risk: S&P BSE MidCap Select, S&P BSE SENSEX Next 50 and Nifty Next 50 are more diversified compared to Nifty 50 and S&P BSE SENSEX.
6. After examine the comments/comparative analysis furnished by the Consultant, it can be concluded that Nifty Next 50 and S&P BSE SENSEX Next 50 can be considered for investment by EPFO as a means for diversification. S&P BSE MidCap Select index may not be considered as it has maximum downside risk in the worst return period moreover it also has higher portfolio concentration in comparison to next 50 indices.
7. As mentioned in Para 1 above, category (iv) (c) of Pattern of Investment mentions that Exchange Traded Funds /Index Funds regulated by the SEBI that replicates the portfolio of either BSE SENSEX or NSE Nifty 50 Index. Accordingly these new indices will have to be included in the Pattern of Investment notified by the Central Government after its approval by the Central Board.
8. The item was placed before the FIAC and the members after deliberation recommended it for consideration of the Central Board.

**Proposal: The item is placed before the Central Board for its approval.**

Shri Ashok Singh said that in view of the fact that the balance in administrative account has been reducing over the years, it would not be prudent to keep on reducing the rate of administrative charges. The employers' representatives S/Shri Ravi Wig, Vijay Padate, G.P. Srivastava and Sushanta Sen welcomed the proposal and observed that EPFO has enough surplus in administrative account to meet the envisaged expenditure by the EPFO in future. CPFC intervened and informed that even if the rate of administrative charge is reduced income in administrative account is expected to increase in the long term as the number of subscribers is projected to increase. Secretary, L&E referred that there is already a surplus of more than Rs. 20,000 crores in this account which is sufficient to sustain any eventuality.

The Board approved the proposal as contained in the agenda.

**Item No. 6: Cumulative performance evaluation for the period July, 2015 to June, 2017.**

The Board took note of the information placed before it.

**Item No. 7: Revised Estimates for the year 2017-18 and Budget Estimates for the year 2018-19 for EPFO and Schemes administered by EPFO.**

The following discrepancies/typing mistakes were pointed out:-

- (a) Shri A. D. Nagpal said that there is a discrepancy in the figures of Revenue Expenditure under Budget Estimate for 2018-19 furnished in the Budget Book.
- (b) EPF contribution is printed as 8128937.42 instead of 81289.37 on page 01 of the Budget Book.

Shri Manish Gupta, FA & CAO said that the discrepancies pointed out will be rectified.

The Board approved the proposal as contained in the agenda.

**Item No. 8: Realization of capital gains from investment in ETF (EPF Scheme).**

The Board approved the proposal as contained in the agenda.

**Item No. 9: CBLO borrowing transactions by the Portfolio Managers during the period 01.04.2017 to 31.12.2017.**

The Board took note of the information placed before it.

**Item No. 10: Performance Evaluation of Custodian of EPFO securities, M/s Standard Chartered Bank (SCB) for the period 01.04.2016 to 31.03.2017.**

The Board took note of the information placed before it.

**Item No. 11: Diversification of investments in Exchange Traded Fund (ETF) under category (iv) i.e. investment in Equity and related Investments of Investment Pattern 2015.**

Shri Arun Goel, Addl. Secretary and Financial Advisor said that the summary of the Consultant's comments as furnished in the agenda item is not complete. Shri Virjesh Upadhyaya stated that a training needs to be organised at PDNASS on ETF. The Vice Chairperson said that the matter will be further examined in consultation with the Consultant.

The item was deferred.

**Item No. 12: Inadequate supply of corporate issuances in the Category (ii) of the New Investment Notification No. S.O. 1071 E dated 23, April 2015 of Ministry of Labour and Employment.**

The Board was apprised that an order has been received from the Government where the minimum limit in the Category (ii) of the New Investment Notification was reduced from 35 to 20 percent. The Board took note of it.

**Item No. 13: Centralised Payment System through single Nodal Bank using NPCI.**

Shri Ashok Singh & Shri A. K. Padmanabhan said that FIAC should consider and take decision on this issue. CPFC clarified that the matter has been discussed in the FIAC on 21-02-2018 and the minutes of the FIAC meeting have been placed on the table. The recommendation of the FIAC was noted by the Board.

**Item No. 14: Recommendations of rate of interest to be credited to EPF members' accounts for the year 2017-18.**

All employees' representatives requested that the rate of interest should be kept at the previous year's rate of 8.65%. After deliberations, it was decided to recommend the rate of interest of 8.55% for the EPF balances in 2017-18.

**Item No. 15: Approval of revised transfer policy for Group 'A' Officers in EPFO.**

It was informed that the original agenda item titled above, placed in the first agenda booklet was withdrawn. Instead, another item titled "Amendment to the Transfer Policy for Commissioners Cadre in EPFO" was placed at Serial no. 15, in the second booklet before the Board, wherein CBT was requested to approve the amendment to para 4.21 of Transfer Policy for Commissioners Cadre in EPFO. The Board approved the same.

**Item No. 16: Delegation of powers for granting permission to visit foreign countries by officials of Central Board.**

The Board approved the proposal as contained in the agenda.

**Item No. 17: Introduction of non-functional grades in respect of Lower Division Clerk (LDC), Stenographer and Upper Division Clerk (UDC) for promotion to subsequent cadres.**

Dr. Sanjeeva Reddy said that while adopting rules of DoP&T, the autonomy given to EPFO under EPF & MP Act should be kept in mind.