

Tightening CPF Investment Scheme (CPFIS) admission criteria for funds - Frequently Asked Questions

New Criteria

1. Why have revised criteria for new funds under CPFIS?

Currently, new funds applying for admission under CPFIS are evaluated based on a number of factors such as the capability of the fund managers, the investment philosophy of the fund, its key decision makers, the appropriateness and quality of its research and analysis, its portfolio construction and implementation, and its past performance.

While this screening mechanism has helped to ensure a minimum standard for the funds under CPFIS, more stringent criteria have been introduced so that funds under CPFIS would better meet the objectives of CPFIS, which is to help members invest for the long-term for financial security in old age. In addition to setting a higher evaluation benchmark based on the current screening mechanism, the Board will also consider the funds' expense ratio. The latter will help lower the investment cost for members over the longer term. Funds submitted for admission under CPFIS should also preferably have a performance track record of at least 3 years as this will allow the Board to better assess whether the funds are able to give consistently good performance against the benchmark.

2. What proportion of funds applying for admission into CPFIS has been successful? What is the target under the revised criteria?

Fund managers would generally assess the quality of their funds using the published CPFIS evaluation criteria before applying for inclusion under CPFIS. Thus far, funds within the top 50 percentile in their global peer group¹ have been successful in their application for admission into CPFIS, and the majority of funds that have applied for admission into CPFIS have been admitted.

New funds will need to meet a higher criterion – i.e. they must be among the top 25 percentile of funds. Going forward, we do not expect a significant change in the success rate of application as managers would continue to assess the quality of their funds against the CPFIS evaluation criteria before application.

3. What are the different evaluation factors under the old and new entry criteria?

New funds will continue to be evaluated according to existing evaluation factors. However, new funds will have to meet a higher benchmark, and henceforth funds admitted to CPFIS will be among the top 25 percentile of funds. In addition, new funds will have to meet an expense ratio criterion pegged at the median of all funds in the same risk class. New funds should preferably also have a track record of at least 3-years.

Supplementary Information

The specific aspects of the investment process that are looked at during the evaluation process for UTs and ILPs include the following:

- a) Investment Philosophy,
- b) Key Decision Makers,
- c) Research and Analysis,
- d) Portfolio Construction,
- e) Implementation/Trading and
- f) Past Performance.

¹ This refers to comparison of funds of similar asset class/strategy on a world-wide basis.

4. Will the funds that have already submitted their applications for inclusion under CPFIS be affected by the revised criteria?

No, the revised criteria will only apply to fund applications received by the Board from 1 February 2006 onwards.

5. What are the reasons for the Board selecting these new criteria?

The new criteria cover issues that the Board is most concerned with, such as quality, consistency of performance relative to peer group and investment costs.

Expense Ratio

1. How are expense ratios computed?

Expense ratios refer to the operating cost of unit trusts and investment-linked insurance products which include investment management fees and other administration costs, expressed as a percentage of the fund's average net assets for a given time period. The expense ratio does not include brokerage costs and various other transaction costs that may also contribute to a fund's total expenses. Expense ratio is commonly used in the industry to compare the cost of funds and forms the biggest component of fund cost. Guidelines on the computation of expense ratio can be found in the Investment Management Association of Singapore (IMAS) website at

http://www.imas.org.sg/cmaweb/attachments/publication/IMAS_Revised_Guidelines_on_Expense_Ratio.pdf

2. Why is the median used as a benchmark in the new expense ratio criterion?

Since new funds should preferably have proven track records and meet the higher evaluation standards, it is reasonable for the Board to also expect these funds to operate more efficiently. Thus, the median is a reasonable benchmark to adopt.

3. Subsequent to inclusion, will a fund whose expense ratio increases be removed from CPFIS?

The expense ratio criterion will only be applied to new funds at the point of application for inclusion under CPFIS for now. The Board will continue to work with the industry to study ways of lowering investment costs.

4. What is the relevant reporting period that fund managers have to indicate in their application for the inclusion of new funds?

It should be the last audited period, and applications should include the last audited expense ratio.

5. Fund sizes have a direct impact on expense ratios. Why did the Board not introduce a new criterion for funds to be of a minimum size to reap economies of scale?

The issue of cost has already been directly addressed under the new expense ratio criterion.

Three-Year track Record

1. Is the preference for new funds with a minimum 3 year track record applied at the fund level or based on the experience of the Fund Management Companies (FMCs)? Also, indexed funds and exchange traded funds (ETFs) are often cited as suitable investment vehicles for the pension portfolio. Given that these are only at the infancy stage of development in Singapore, will the 3 year track record criterion limit the inclusion of such funds?

The preference for a 3 year performance track record is generally applied at the fund level. Currently, the majority (89%) of funds under CPFIS are actively managed. Active fund managers should preferably show a minimum track record so that they can be better assessed whether they are able to give consistently good performance against the benchmark for the specific fund they manage.

In the case of indexed funds or ETFs, the 3 year track record is applied differently. The focus will be on the fund management company's technology or systems and processes that they have established to perform the rebalancing functions to track indexes closely² and their ability to consistently maintain a low cost structure for the index funds they have under management.

² Low tracking error

Existing Funds

1. Will the new criteria be applied to existing funds under CPFIS?

The new criteria will not apply to existing funds. To help members make better informed investment decisions, the Board will, in due course, step up its member education efforts and also avail relevant information on the performance and expense ratios of existing funds

2. Will the new criteria apply to funds that are subject to re-evaluation from 1 February 2006 onwards?

The existing funds will not be subject to re-evaluation unless the Fund Management Companies (FMCs)/funds have undergone material changes in the organisational structure, fund structure or management team.

For re-evaluation cases, the new criteria will apply with effect from 1 February 2006.

3. How does CPFIB currently assess whether funds admitted are still suitable to remain in CPFIS?

When determining if a product is suitable to be under CPFIS, the emphasis so far has been on past performance and the competency of its investment professionals. Re-evaluation will be required for FMCs/Funds that have undergone material changes in the organisational structure, fund structure or management team.

4. What can members do if the funds in which they have already invested do not meet the new standards set by the Board following re-evaluation?

Members who have already invested in such funds can continue to remain invested in the funds, or consider switching to other funds or selling out of the funds if the funds no longer meet their investment objective.

5. The Board mentioned that there will be more member education. What additional information will be released or made available?

The Board will make available more information to help members make better informed investment decisions. Members will be educated on the factors that could impact on funds' performance. They will also soon be

able to make use of an investment calculator to help them project the impact of costs on investment.

The Board has recently launched an online game called *Voyage of Life* in the CPF website. The game aims to educate members about retirement planning through a monopoly-style board game format.

In addition, the Board plans to launch a microsite on unit trusts. The site aims to provide comprehensive information on unit trusts to educate investors.