USAID-Funded Economic Governance II Project

NATIONAL BOARD OF PENSIONS INVESTMENT POLICY INSTRUCTIONS

PREPARED FOR:

NATIONAL BOARD OF PENSIONS GOVERNING BOARD

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There are many Investment Policy documents for United States government entities on the web, as well as papers on the subject. Arguably, the United States has the most comprehensive pension investment corporate governance laws and policies. The Employee Income Retirement Security Act (ERISA) and other more recent regulations serve as the basis for the construction of the document.

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NATONAL BOARD OF PENSIONS
INVESTMENT POLICY INSTRUCITONS

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1. CORPORATE GOVERNANCE AND INVESTMENT POLICY

Article 11 of Law #69/2007 amends the Unified Pension Law #27/2006 Article 18 by providing the authority for the National Board of Pensions (NBP) Board to invest both employer and employee contributions a the rates of 12% and 7% of salary respectively. This document is intended to satisfy the mandate found in Article 11, Third Paragraph, which states that the NBP Board (Board) shall “determine its members, tasks, work flow and money investment”. The first step in pursuing this authority and satisfying the mandate is to develop an overall NBP Investment Policy.

New concepts and responsibilities are introduced as the result of the mandate. An effective NBP Investment Policy must recognize the broad concept of corporate governance, as well as the Board responsibilities as fiduciary and prudent investor.

The NBP is not per se a corporation. However, it will have both revenue (investment income) and expenses. With the right Board and management execution, the NBP can be a self-sustaining or independent entity. To become such, the NBP must develop a sound corporate governance structure. A corporate governance structure starts with the top, the NBP Board. If the NBP Board establishes a good functioning structure for itself, consisting of comprehensive policies, procedures, and systems to control and manage the NBP activities dedicated to the active employees, pensioners and beneficiaries, then the Board will be in a position to push their structure to each NBP organizational level.

The Investment Policy is a critical component of the corporate governance structure necessary for a self-sustaining organization. The Board responsibilities of fiduciary and prudent investor are necessary pre-requisites to a sound Investment Policy.

With respect to the operations of the NBP, the Board has a fiduciary relationship. By undertaking to act for and on behalf of the active employees, pensioners and beneficiaries with respect to investing their contributions, ensuring that the NBP is adequately funded, the NBP Board has assumed a relationship of trust and confidence. The Board must therefore act solely in the interest of those groups, in the matters affecting investment of their contributions as well as all other NBP duties and responsibilities mandated by the law.

As prudent investor, the NBP does not guarantee superior or even good investment results. It is the process that the NBP establishes through a comprehensive Investment Policy and ensuring its compliance which matters. It is better to incur a modest return with an established Investment Policy, than a superior return without one. So, for the NBP to be a prudent investor, they must establish and follow a process. If the process followed in making investment decisions is prudent (based on what is known and not known at that time), then the decisions being made are prudent, regardless of subsequent results

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2 INVESTMENT POLICY OBJECTIVES

2. INVESTMENT POLICY OBJECTIVES

OVERVIEW

The NBP Board is organized and authorized to conduct the business of the NBP solely in the best interests of the active employees, pensioners and beneficiaries. With respect to the investment of employer and employee contributions, the Board assumes the role of "fiduciary" and "prudent investor" with respect to the NBP investment assets.

The ultimate obligation of the NBP is to provide retirement benefits to active employees, pensioners and beneficiaries. With respect to investments, as fiduciary, the NBP must always act in the best interests of the active employees, pensioners, and beneficiaries. All Board decisions must be made from the perspective of that obligation. The best interests of the Government of Iraq (GOI), the Ministry of Finance (MoF), participating State Owned Enterprises (SOE), participating private employers or other such entities or individuals shall be made subordinate to the interest of the active employees, pensioners and beneficiaries.

The Board as fiduciary shall have the authority to delegate investment management and other functions to third parties. While the Board can delegate functions, particularly investment management (discussed later), they cannot delegate or surrender their fiduciary status. Board oversight of delegated functions remains a fiduciary responsibility.

The Board shall: have authority over the NBP's entire investment portfolio. That portfolio will include, but may not limited to the investment of:

- Employer Contributions
- Employee Contributions
- Gains from liquidated Investments made in accordance with this Policy
- Other Cash or Investments provided to the NBP by the GOI, MoF, or the Central Bank of Iraq (CBI) from time-to-time.

The Board or prudent investor considers an entire investment portfolio when determining the prudence of an individual investment. As such, the prudent investor shall not be held liable for individual investment losses, so long as the investment, whether made by the Board or an engaged investment manager, at the time of acquisition, is consistent with the overall NBP Investment Policy objectives and no fiduciary breach of duty has occurred.

The consequences of prudent investor status require that the Board ensure that investment diversification is explicitly required. Further, no category or type of investment is deemed inherently imprudent.

Instead, of specifically categorizing an investment as imprudent, suitability with respect to the NBP obligation as fiduciary shall govern. As a result, real property investments in limited partnerships, derivatives, futures, and similar investment vehicles, are not per se considered imprudent.

With the suitability as a test, Board is encouraged, to develop greater flexibility in overall portfolio management. , Notwithstanding, speculation and outright risk taking is not sanctioned by the prudent investor status, and the Board remains subject to criticism and possible liability

The obligation of the Board is to provide for the active employees, pensioners and beneficiaries pursuant to the Law #27/2006 and its amendments. The Investment Policy shall establish an investment goal that is measurable. Accordingly, the Board shall establish the following objectives:

1. Real Return Objectives (RRO) that will:

   i. Keep contribution rates reasonably level over long periods of time absent changes in actuarial assumptions.

   ii. Maintain contribution rates consistent with historical levels ranging from 8% to 12% of covered payroll subject to and recognizing that changes made in the law or actuarial assumptions will affect contribution rates.

2. Asset Allocation Policy

   Satisfy the RRO while minimizing the impact of the fund's volatility on the contribution rate. Secondary considerations include, but are not limited to, the expected rate of return for each asset class, the expected risk of each asset class, the correlation between rates of return among the asset classes, and the investment objectives and risk constraints of the fund.

3. Monitor costs associated with efficient:

   i. Implementation of the asset allocation through the use of internal and external resources (managers, brokers, analysts, etc.).
   ii. Operation of the entire NBP organization so as to minimize the use of investment gains or GOI subsidies

REAL RETURN OBJECTIVE:

In accordance with Article 30, Second Paragraph "B", of Law #69/2007, actuarial studies shall begin "after the first three years from the date this Law enters into force". The results of those studies will produce information from which the Board can develop a reasonable actuarial assumption that will provide a compound rate of return necessary to meet the NBP benefit obligations, while maintaining the contribution rates of 12% and 7% respectively for employers and employees.

Until the results of the actuarial study are available, and based on international best practices and various experts, the NBP has estimated that the portfolio should generate a compound annual real return on invested assets of 5.0 percent per annum--less expenses--in order for the NBP to accumulate the assets needed to meet benefit obligations while at the same time maintaining a level contribution rate.

3 INVESTMENT POLICY AND LIMITATIONS

3. INVESTMENT POLICY AND LIMITATIONS

BOARD AUTHORIZING PROVISIONS

The NBP shall have the authority to invest and re-invest employer and employee contributions for the purpose of increasing the value of the Fund's assets to pay retirement, beneficiary, and disability payments to current and future beneficiaries in accordance with the Law as amended from time to time.

At the recommendation of the NBP Chairman, the Board shall submit for approval to the MoF a list of competent portfolio managers who shall be engaged to execute an investment strategy consistent with this Investment Policy, in accordance with their particular strategies as presented to the NBP at the time of engagement. Contained in the list shall be a portfolio manager who will be designated as Lead Investment Manager (Lead). The Lead portfolio manager shall be responsible for establishing the individual investment targets for each manager, consistent with the Asset and Sub-Asset Allocation Policy mix noted in this document.

The Lead manager shall provide input to the NBP board at their direction, including attendance at Board meetings, no less frequently than quarterly. The Lead shall have no Board voting capacity.

The Portfolio managers are engaged for no longer than three years, although they serve at the discretion of the NBP Board, and may be terminated should investment results prove unsatisfactory based on their strategy and the international benchmarks for such (Value, Growth, Income, Sector, etc.), or non-compliance with any of the provisions of this Investment Policy. The criteria the NBP board shall consider with respect to engaging any portfolio manager, shall include but not be limited to their:

1. Ability to provide detailed firm history, including investment philosophy, approach, and results, clients, locations, and at least two recent firm audited financial statements.

2. Representation that firm is operating in good standing with regulators and clients, with no material, pending, or concluded legal actions.

3. Organization as bank, insurance company, brokerage, or other such financial institution with authority to conduct investment management business

With respect to voting proxies or exercising ownership rights related to the financial instruments in which the investment managers have invested, upon the approval of the Board, the Chairman shall direct the lead investment manager to develop a proxy policy that is solely in the best interests of the active employees, pensioners and beneficiaries. The lead investment manager shall be responsible for communicating the proxy voting policy to the engaged managers, and to monitor its compliance. The proxy policy shall be reviewed annually as part of the overall Board investment management review of performance, target returns, etc.

Each individual manager shall report the results of their investment work quarterly. The report will include a comprehensive accounting of the portfolio, including fees, from the beginning of the period through the close. Annually, each manager shall prepare a report for the past year which consolidates the information of the year, as well as any proposed changes to the core strategy for the coming year(s). At the direction of the Chairman, the portfolio managers may be required to present their annual report to the Board, the MoF, etc., in person.

Annually, at the direction of the Board shall request audited financial statements from the engaged managers. These statements will cover the NBP portfolios assigned to each engaged manager, and the statement scope will include the operational and financial controls in place at by engaged managers either through their own organizations or as delegated (custodial relationships, etc.).

Consistent with the concepts of liability driven investment, and other investment approaches as may be identified from time to time, the NBP shall rely on the periodic (no less frequent than every three years) actuarial valuations of the pension liabilities to establish target rates of return (RRO noted above) for the entire invested portfolio. The RRO shall be reevaluated in light of changing investment circumstances, no less frequently than annually.

Consistent with its obligation as fiduciary to delegate certain functions, the Board has engaged a Lead. The Lead has been delegated the responsibility for establishing the strategic (sub-asset class) allocation of the portfolio within broad bands approved by the Board. The broad bands serve as a guideline about what maximums in any one asset category are permitted at any one time. Those maximums are:

70% Equities
70% Bonds
50% Short Term Investments(Cash, Commercial Paper, etc.)
20% Foreign Exchange
10% Miscellaneous (Options, Futures, Shorts, Derivatives, Securities Lending)
05% Real Estate or Real Estate Investment Trusts (REITs)

The Lead will make strategic allocation decisions away from the policy benchmark weight subject to approval from the Board, or any consultant it may engage through similar delegations of power, providing the Lead obtain certification that the change is in compliance with the Board's Investment Policy.

Based on a variety of considerations, the Board has selected the strategic (sub-asset class) allocation bands that are allowable. These ranges are outlined in the table shown below. In addition, this table outlines the benchmark weights which will be used to measure performance. A general review of all components of this table will be completed and, with the results reported by the Lead to the Board, no less frequently than annually.

Asset Class	Sub-Asset Class Range	Policy Benchmark Maximum	Policy Benchmark Index
EQUITY		**70.00%**	
Domestic/Middle East	15% - 40%	27.50%	
Hedged	0% - 10%	5.00%	
International	5% - 70%	15.00%	MSCI EAFE
Emerging Markets	0% - 5%	2.50%	MSCI EMF
BONDS		**70.00%**	
Core Fixed Income	0% - 30%	10.00%	
High Yield	0% - 20%	5.00%	
Market Neutral	0% - 20%	5.00%	
ALTERNATIVES		**10.00%**	
Commodities	0% - 5%	0%	
Derivatives	0% - 5%	0%	
Foreign Currency	0% - 5%		
REAL ESTATE	0% - 5%	5.00%	

The overall portfolio strategy should ensure that apart from the opportunity to rebalance on a periodic basis--but no less frequent than annually-- the total invested assets in any one class or sub-class do not exceed the percentages above.

In addition, all ratable investments (bonds, commercial paper, etc.) should be within the highest decile based on third party ratings (Moody's, Standard and Poor's, etc.).

For investments made within Iraq, no investment exceeding 20% of the total equity value should be made in any publicly traded entity or private procurement.

Investments in single entities or bonds made outside of Iraq should be limited to no more than 5% of the total entity equity or authorized outstanding shares at the time of the investment transaction.

Should the long-term investment strategy require a prudent allocation of assets internationally, those investments must be made in highly liquid, publicly traded markets and countries with single country risk no greater than 20% of the total outstanding NBP portfolio.

Periodically, but no less frequently than annually as mentioned above, asset rebalancing of the invested portfolio shall occur to ensure that the above asset class maximum investment restrictions are not exceeded. This will be done in conjunction with the investment results and recommendation of timings provided by the engaged portfolio managers.

COMPONENTS OF INVESTMENT RETURN:

Investment return is comprised of two components known as "beta" and "alpha." Beta return is the return generated from exposure to the policy sub-classes as identified in the above table. Beta return is thought of as the market return for the sub-class in question and is identified by the Policy Benchmark Index. Alpha return is generated as a result of manager skill or investment decisions made that add or detract value relative to the Policy Benchmark Index. The following paragraphs define each component's respective role within the portfolio.

Beta Exposures:

The policy weights outlined in the above table represent policy exposures to various markets we have defined as sub-asset classes. It is also appropriate to think of these sub-asset classes as exposure to the beta component of the return equation. What follows are descriptions of each sub-asset class, their purpose in the overall portfolio, and more specifically, the types of investments that would be expected to be made within the sub-asset class according to a mutual understanding between the investment management group (staff) and the Board.

Public Equity

Domestic Middle East Region Equity: This sub-asset class seeks to provide a combination of long-term capital appreciation and dividend income that is expected to exceed the rate of inflation. It is expected that investments in this class will perform well during periods of rising economic growth and/or falling inflation. Investments in this sub-asset class may include a variety of Iraqi stock investments with varying characteristics related to market capitalization and investment style. While the Board may not find sufficient investible Iraqi equities to create a domestic equity portfolio, the characteristics sought from such investments would include large-cap, mid-cap, small-cap, and micro-cap stocks, and value and growth stocks. Investments could also be made in specific sectors of the overall market such as technology, energy, or real estate investment trusts (REITs). Short selling is expected in this sub-asset class from time to time to rebalance the overall fund. Note: To the extent that the characteristics described above are absent from domestic Iraqi markets, international equity focused within the Middle East Region shall be sought.

Hedged Equity: This sub-asset class provides diversification to the total portfolio and strives to reduce volatility within the total fund by targeting a .beta factor to an identified benchmark equity market such as that of the U.S.

International Developed Equity: International Developed Equity seeks to provide long-term capital appreciation and dividend income that in aggregate are expected to exceed the rate of inflation. Investments in this category will be made through a diverse group of strategies varying in size, investment style, and exposure to opportunities in a large group of developed countries. It is expected that investments in this sub-asset class will perform well during periods of rising economic growth and/or falling inflation Characteristics of this sub-asset class include large-cap, mid-cap, small-cap, and micro-cap stocks, and value and growth stocks. Investments may also be made in specific sectors of the overall non-Iraqi/Middle East Region markets such as technology or energy as examples. Managers could be hired with a global focus or for specific country exposures. An example of the latter would be a Japan-only manager. This sub-asset class will be invested predominantly in equities that make up the Morgan Stanley Capital International (MSCI) Europe, Australia and Far East (EAFE) Index, however, from there may be minor investments in countries outside of EAFE. Short selling is expected in this sub-asset class from time to time to rebalance the overall fund.

Emerging Market Equity: This sub-asset class seeks to provide long-term capital appreciation in excess of inflation primarily through investments in countries outside of those included in the MSCI EAFE Index. Because of the higher growth rates in these countries, higher returns are expected. Investments may range in size (large, mid, small, and micro-cap stocks) and style (growth and value) and be both long and short.

Public Debt

Core Fixed Income: The core fixed income portfolio is designed to provide a source of current income and to reduce overall fund volatility. In addition, it is expected that investments in this category would perform well in periods of falling inflation. Investments within this category may include Iraqi treasuries, and other instruments issued by the GOI from time to time and international investment grade securities. Shorting is expected in this portfolio from time to time as necessary to rebalance the overall fund

High Yield Bonds: This sub-asset class seeks to provide capital appreciation within the portfolio through investment in below investment grade debt instruments and debt considered to be "opportunistic" in nature. Generally, it is expected that securities in this asset class will be in "current pay" status with superior coupon cash flow because of the lower credit quality bias. Investments in this portfolio may include non-investment grade debt of any issuing country which meets the criteria above.

Market Neutral: This sub-asset class provides diversification to the total portfolio and strives to reduce total fund volatility. That this sub-asset class has been positioned within public debt is not that all of its exposure will be to debt instruments, but, more importantly, that it will be expected to have lower volatility (standard deviation) and similar returns over long periods of time to other public debt investments. This area will include investments in a group of skill-based managers using a variety of strategies to produce acceptable absolute returns as established by the Lead. At any given point in time, the number of managers and types of investments and strategies used may include the entire universe of available investment options. In addition, a variety of marketable alternative strategies may be utilized within this sub-asset class including, but not limited to hedged equity, convertible arbitrage, event driven, relative value, global fixed income/currencies, managed futures, and commodities.

Alternatives

Distressed Debt: This sub-asset class provides additional diversification to the total fund and is expected to provide equity-like returns. Investments include debt instruments of primarily international companies which may be publicly traded or privately held that are financially distressed and are either in bankruptcy or likely candidates for bankruptcy. Typical holdings are senior and subordinated debt instruments and bank loans. Equity exposure is acceptable in this sub-asset class as debt positions are often converted to equity during the bankruptcy reorganization process.

Commodities: This sub-asset class is expected to provide meaningful diversification to the overall fund as it has exhibited a zero to slightly negative correlation to traditional assets (i.e. stocks and bonds). This sub-asset class is also expected to provide superior returns during periods of unexpected inflation. Investments in this category might include a variety of derivative instruments including futures, total return swaps, options, and forward contracts, as this is how most commodities exposure is obtained. It is also possible that this category might include limited partnerships and/or commodity trading advisors (CTAs) who seek exposure to various types of commodities and commodity-related investments, including oil, gas, and other energy investments.

Private Equity: This sub-asset class is expected to provide high real returns over long periods of time while providing additional diversification to the fund even though it is understood that the diversification benefit is likely due to the lack of market pricing on these investments as opposed to a "true" diversification characteristic of these investments. Investments in this category are expected to be very illiquid and long-term in nature. Investments in this category include corporate buyout, venture capital, and opportunistic/special situations. These opportunities may be identified domestically or on a global basis.

Real Estate: This sub-asset class primarily serves as a hedge against general price inflation and would also be expected to provide a relatively high level of income. Real estate investments are expected to provide diversification to the overall fund. Investments may include real estate investment trusts (REITS), opportunistic real estate funds, direct real estate holdings, and mezzanine debt investments.

Allowable Investments in all Sub-Asset Classes (Beta Exposures):

As it pertains to the above referenced sub-asset classes within the NBP portfolio, beta exposure may be gained through investments in derivative instruments including, but not limited to futures, forward contracts, swaps, and options per the terms of each manager's specific governing documents and in accordance with the limitations outlined in this governance policy under "Limitations". In addition to derivative instruments, leverage may be utilized in the implementation of these sub-asset classes in accordance with each manager's specific governing documents and in keeping with the investment limitations outlined in this policy. Additional investments which are allowed include exchange traded funds (ETFs), warrants, rights, convertible bonds, and preferred stock. Currency hedges may also be used for non-dollar exposures within each respective asset class as outlined in each manager's governing document. Long/short investment strategies may also be employed per the terms of the Investment Limitations defined in this governance policy, however, from a beta perspective the predominance of long/short strategies would be expected to exist within the hedged equity and market neutral sub-classes.

In addition to the instruments outlined in the paragraph above, for every sub-asset class, a variety of investment structures may be utilized depending on the nature of a particular investment. Per the terms of the investment limitations outlined in this policy, these structures may include mutual funds, partnerships, limited liability companies, trusts, fund-of funds, and separately managed accounts in which assets may be held by an external custodian who is selected and monitored by the external manager or general partner.

Alpha Strategies:

A variety of implementation strategies may be used in capturing alpha (skill-based manager returns) within the portfolio. These strategies include both traditional active management strategies and marketable alternative market neutral strategies. Marketable alternative strategies may be used as long as both the NBP Board and Lead are convinced that these strategies exhibit little to no market exposure. The use of investment instruments available to these managers is broad, covering a variety of investment types and strategies across numerous asset classes. In making implementation decisions related to the alpha component of the portfolio, staff may utilize any and all investment tools so long as they are defined in each manager's governing documents and are carried out in accordance with the Investment Limitations spelled out in this policy.

LIMITATIONS

Pursuant to its authority fiduciary and prudent investor authority, the Board pledges that it will not:

1. Operate the investment program without an Investment Implementation Policy approved by the Lead that is consistent with this Investment Policy and outlines the detail of how the overall investment program will be implemented and monitored.

2. Violate fiduciary requirements, conditions, and limitations.

3. Allow the Lead to invest the assets of the NBP in a manner that is inconsistent with the asset allocation mix and any strategic (within class) allocation of the portfolio as approved by the Board and set forth herein.

4. Fail to have the Lead perform an asset allocation/liability study at least every 3 years and to report the results of that study to the Board.

5. Fail to have the Lead evaluate the asset allocation mix and any strategic (with-in class) allocation of the portfolio annually and have the Lead report the results of that evaluation to the Board.

6. Fail to have the Lead provide quarterly investment performance reports to the Board that show performance of the total fund and all underlying asset classes based on the benchmarks set forth in this Chapter (Chapter 3) of the Investment Policy.

7. Permit the Lead to hire outside service providers (securities lending managers, specialty consultants, the master custodian, and external money managers, including but not limited to external money managers who may be structured as a public or private entity in the form of a partnership, limited liability company, trust, separately managed account, commingled account, or some other form of operational structure in which assets may be held by an external custodian selected and monitored by the external manager) unless the Board agrees in writing to the proposed hiring action by the Lead.

   In the event of a hiring, the Lead shall follow a process that is based on a competitive Request for Proposal (RFP) with established selection criteria unless under the circumstances it is not prudent to do so. In the event of a hiring, the Lead shall also: i) document the proposed action by describing the decision-making process, expectations, and rationale for the decision, ii) within 14 days after the hiring decision is made, prepare a letter of notification to the Board informing them of the action taken, the process, and the rationale for the decision including a justification if the Lead did not follow an RFP process, and iii) enter into a written contract with the new outside service provider on a form that has been reviewed by either DG Legal Affairs, or the DG MoF Legal Affairs.

8. Permit the Lead to terminate an outside service provider as described, unless the Lead agrees in writing to the proposed termination action and the Board certifies that the

proposed termination is in compliance with the Board's Investment Policy. In the event of termination, the Board and the Lead must agree and the underlying reason for the proposed termination action must be documented and shared with the Board as soon as is practical.

9. Fail to have the Lead monitor the performance of and hold due diligence meetings with all outside service providers at least semi-annually unless the Lead provides prior notice to the Board of his intention to meet less often than semi-annually.

10. Permit the Lead to alter the strategic (with-in class) allocation of the portfolio within broad bands approved by the Board unless the Lead receives approval from the Board, and the Board Director certifies that the change is in compliance with the Board's policy.

11. Permit the Lead to manage assets internally at NBP unless approval from the Board has been received prior to implementing any portfolio within the internal investment program.

12. Fail to have the Lead monitor the performance of any NBP internal investment program that may exist from time to time.

13. Fail to have the Lead perform semi-annual due diligence meetings of any NBP internally managed portfolios and report the results of those meetings to the Board.

14. Fail to notify the Board in writing in the event a member of the internal NBP investment staff has materially underperformed against an applicable investment benchmark or has been terminated as a result of underperformance or potentially unlawful actions.

15. Fail to provide an annual report by an external consultant which evaluates the implementation costs of the investment program.

16. Allow the Lead to make investments that are economically or socially targeted (ETIs or STIs), Islamic investment portfolios excepted. For purposes of definition, ETIs or STIs are investments that are selected for the economic and social benefits they create in addition to the investment return to the employee benefit plan investor. The following criteria, applicable to any investment, will also be applied to investments that might be classified as ETIs or STIs:

    - The fiduciary principles of prudence and exclusive interest of participants will not be abrogated or modified in order to increase the attractiveness of ETIs or STIs.
    - There will be no concession on rate of return. This means there will be no hidden subsidies and that the classic "efficient frontier" test is applicable: a commensurate unit of return will be received for each unit of risk incurred.
    - All participation should be voluntary on the part of the System and should not stem from a legal or policy mandate.
    - Each ETI or STI will be evaluated using an integral, objective process -- that is, each will be meticulously analyzed solely on its own risk/return characteristics. No weight will be given to redeeming social interests.
    - The System will participate only if at least one other comparable investor is participating.
    - When evaluating an investment, appropriate consideration must be given to the role that the investment or investment course of action plays (in terms of diversification, liquidity, risk and return) with respect to the entire Investment Portfolio of the System. Consideration should also be given to alternative

investments with similar risks available to the System. The Board believes this set of investment criteria is in full compliance with Section 105.688. RSMo.

17. Fail to have the Lead operate without a rebalancing policy that requires the LEad to examine and comply with the broad asset allocation mix on a monthly basis using the most cost efficient method that is reasonably possible unless under the circumstances it is not possible or prudent to do so in which case the Lead shall provide written notice and explanation to the Board within a reasonable period of time.

18. Allow the Lead to use leverage in the fund except where a specific external service provider has been given written authorization to utilize leverage by the Board and Lead, subject to written guidelines describing its use within the manager's governing contract. The use of futures to rebalance the fund and the use of futures for the equitization of cash within portfolios is not considered to be leverage.

19. Allow the Lead to use derivative securities and synthetic products including futures, options, swaps, and forward contracts (and/or combinations of these instruments), and pooled, mutual or segregated funds that employ derivative and synthetic products except where a specific external service provider has been given written authorization to use derivative securities and synthetic products by the Board and Lead subject to written guidelines describing their use within the manager's governing contract.

20. Allow the Lead to engage in short sales in the fund except where a specific external service provider has been given written authorization to engage in short sales by the Board and Lead, subject to written guidelines describing their use within the manager's governing contract.

21. Fail to establish policies for securities lending, proxy voting, soft dollar usage, and brokerage commissions that ensure that the interests of the system are adequately protected.

22. Allow Board members, the Lead, engaged investment managers, and service providers, to engage in personal securities transactions:

    - Based on information about a company that is both material and nonpublic (also known as "insider trading"),
    - Timed to take advantage of non- public information that would favorably affect that person's personal securities transaction (also known as "front running").

    (The CIO shall provide each outside service provider managing assets on behalf of MOSERS with annual notice of the foregoing trading limitations with direction to contact either the Chief Counsel or the Internal Auditor in the event the manager has questions or concerns.)

23. Permit the NBP assets to be commingled with the assets of the GOI and thereby subject to creditor liens or other claims upon the GOI.

4 INVESTMENT PERFORMANCE MESUREMENT

4. INVESTMENT PERFORMANCE MEASUREMENT

The NBP success in achieving the RRO can only be evaluated over long time periods. The reason for the long-term focus on this objective is to preclude the temptation to overreact to events in the marketplace that have no relevance in long-term asset/liability management and the fiduciary responsibilities to the active employees and pensioners and beneficiaries. The resulting dilemma is the conflicting need to evaluate investment policy implementation decisions over shorter time frames while maintaining the longer-term focus necessary to manage and measure the fund's performance relative to the RRO.

To address this problem, the Board has established the following categories to measure performance:

1. Board Policy Decisions
2. Lead Decisions
    a. Strategy Decisions
    b. Implementation Decisions

BOARD DECISIONS

The value added through Board Policy decisions is measured by the difference between the Policy Benchmark return and the Required Rate of Return Objective (defined as Real Return Objective + Inflation). This difference captures the value added by the Board through their broad policy asset allocation decisions relative to the required rate of return objective necessary to meet the actuarial assumptions. A Policy Benchmark return greater than the Required Rate of Return Objective reflects value added through Board decisions. A Policy Benchmark return less than the Required Rate of Return Objective reflects losses or shortfalls in performance in funding the liabilities of the system. These policy decisions are measured over long periods of time.

LEAD DECISIONS

There are two components to the Lead decisions that are monitored by the Board on an ongoing basis:

Strategy Decisions:
Strategy Decisions are sub asset class asset allocation choices made by the Lead, with approval from the Board or its designated consultant to deviate from the Policy Benchmark weights and a certification from the NBP that the proposed deviation is in compliance with the NBP Investment Policy. The value added through these decisions to overweight and/or underweight these sub-asset classes is measured by the difference between the Strategy Benchmark return and the Policy Benchmark return. This difference captures the value added by the Lead through sub asset class strategic decisions relative to the Board's broad policy allocation decisions. A Strategy Benchmark return greater than the Policy Benchmark return reflects value added through the with-in class allocation decisions. A Strategy Benchmark return less than the Policy Benchmark return reflects losses to the fund's performance based upon strategy decisions. Strategy decisions should be measured over all periods of time.

Implementation Decisions:
Implementation Decisions are money manager selection choices made by the Lead with the approval of the Board or its designated consultant and a certification by the NBP Board that the proposed manager selection choices are in compliance with the Board's Investment Policy. The value added through these manager selection

decisions is measured by the difference between the Actual Portfolio return and the Strategy Benchmark return. This difference captures the value added through these manager hiring decisions. An Actual Portfolio return greater than the Strategy Benchmark return reflects value added through these manager selection decisions. An Actual Portfolio return less than the Strategy Benchmark return reflects losses to the fund's performance based upon implementation decisions. Implementation decisions should be measured over all periods of time.

5 MISCELLANEOUS POLICY CONSIDERATIONS

5. MISCELLANEOUS POLICY CONSIDERATIONS

The creation of a trust and the selection of an institutional trustee (bank, investment management firm, brokerage, etc.) are necessary requirements of NBP Investment Policy. While not directly related to Investment Policy, the NBP, as fiduciary, must ensure that the NBP assets are fully segregated from GOI, State Owned Enterprises (SOEs), and participating private employer assets, and held in a trust.

NBP invested assets are not subject to creditor claims, and stand apart from the assets of the GOI, SOEs, or private employers. The withheld contributions of both employer and employee become separate from the assets of the GOI, SOEs, or participating private employers the moment they are paid. Any other payments made by those or other entities on behalf of the Trust become assets of the Trust when received by the Trustee or custodian. After the point of payment of contributions or monies from other entities, they shall become property of the NBP Trust.

Until such time as Iraq has an active trust business, with trust laws, global custody mechanisms, and the ability to convey and monitor trust powers granted to suitable institutions, the Board shall create a Trust, using an institutional trustee in a location of its choosing. If the Board is unable to find a suitable location, the Dubai International Financial Center (DFIC) shall be the default situs of the Trust. The DFIC “Trust Law of 2005” as amended, provides the necessary asset protections described above.

X APPENDICES

X. APPENDICES

Appendix A –Investment Glossary

وحدة قياس عائد الاستثمار **Alpha** is a risk-adjusted measure of the so-called active return on an investment. It is a common measure of assessing an active manager's performance as it is the return in excess of a benchmark index. Note that the term "active return" refers to the return over a specified benchmark (e.g. the S&P500), whereas "excess return" refers specifically to the return over the risk-free rate. It is a common error to confound these two terms, and the reader is cautioned to make a careful distinction between them when studying or discussing investments.

The difference between the fair and actually expected rates of return on a stock is called the stock's alpha.

دفعات سنوية حولية **Annuity**: where an insurance company promises to pay an income for life in exchange for a lump sum.

Asset: type of investment, normally divided into four classes - shares, property, fixed-interest securities and cash.

تخصيص او توزيع الاصول **Asset Allocation** An investment strategy intended to reduce the volatility and risk of loss of an individual`s holdings by assigning the holdings to several different types of asset classes, such as stocks, bonds, mutual funds, preLeadus metals and real estate. Asset allocation is considered the main determinant of portfolio performance. The term can also apply to spreading assets across different regional and national markets.

فئات الموجودات **Asset Classes** The various types of investments, such as stocks, bonds, currencies and commodities that are available for investment by individuals or portfolio managers.

متوسط العائد السنوي **Average Annual Return** The average yearly profit (or loss) from an investment calculated over a period of years. Average annual return is often confused with "compound annual return. (Please see **Compound Annual Return**.)

النقاط الاساسية **Basis Points** is the smallest measure of the yield paid by a bond or note. One basis point is equal to 0.0 1% (one-one hundredth of a percent) of yield. If a bond`s yield moves from 9.5 percent to 10.5 percent, that would be a move of 100 basis points. Investment management fees are often quoted in basis points. For example, an investment manager might charge an annual fee of 50 bps (1/2 of 1%) on the assets managed). If an investment manager does well, the assets he manages will grow and so will his fee.

مقياس التقلبات المالية **Beta** is measure of volatility and risk which reflects the degree to which the price of a security or portfolio tends to rise or fall with the market. The higher the beta, the higher is the volatility.

سوق نزولية **Bear Market** is a period of declining stock prices.

سهم او سند صادر **Blue Chip** is a stock of the largest, most well-established companies. Also referred to as large-capitalization stocks, blue chip stocks are generally considered strong, growing companies with market values of in the range of $1 billion or more. Most blue chips pay dividends, and are considered to be the most stable, least risky stocks on the market.

سند دين **Bond**: can refer to a corporate bond issued by a company or a government agency (Government, directorate, city) to borrow money from investors via the stock

Bond Quality The safety of principal and dependability of interest payments of a bond. Quality depends on the financial soundness of the issuer. The lower the quality, the higher the interest rate an issuer must pay to attract investors.

القيمة الدفترية **Book Value** The assessed value of a company`s assets. ("Book value per share," which is frequently used in assessing the potential value of a company`s stock, is defined as the per-share assessed value of a company`s assets.

اسلوب استثمار بدا من القاعدة **Bottom-Up Approach** Stock market investment approach in which the emphasis is on analyzing individual stocks rather than broad economic trends. Bottom-Up Analysis is the opposite of top-down analysis. Analysts try to identify stocks that are undervalued or have strong growth potential. It is far more popular than the top-down approach. (Also see **Top-Down Analysis**.)

الشراء للايجار **Buy-to-Let:** the purchase of a residential property to let for investment purposes.

Capital Growth: increase in the capital value of an investment as reflected in a higher selling price.

وديعة **Deposit**: another name for cash.

Derivatives: a term for futures, options and warrants

Distribution Bond: investment bonds issued by insurance companies which invest in a mixture of shares and fixed interest securities.

ارباح الاسهم **Dividends:** the income from shares paid out of company profits.

Dollar Cost Averaging - An investment strategy to invest an identical dollar (currency) amount at set time intervals. For example, investing $100 each month in a mutual fund assumes dollar cost averaging. This strategy results in you purchases more shares when the price is low and fewer when prices are higher (because the same dollars buy more shares when the price is lower and vice versa).

Dow Theory: A theory which says the market is in an upward trend if one of its averages (industrial or transportation) advances above a previous important high, it is accompanied or followed by a similar advance in the other. The theory also says that when both averages dip below previous important lows, it's regarded as an indicator of a downward trend.

حق الملكية/ السهم **Equities**: another name for shares or stocks.

سعر الصرف **Exchange Rate** The price at which the currency of one country can be converted into another`s. For instance the exchange rate between the U.S. dollar and the Japanese yen is about 1 to 105 ($1 = 105 yen).

حماية سعر الصرف **Exchange Rate Protection** An investment strategy designed to keep an investor from losing money on international investments due to fluctuations in the exchange rate. For instance, an American investing in British stocks could buy put options on British pounds (to sell at a pre-set price) as an exchange rate hedge just

Fiduciary: In Anglo Saxon Law, an individual who is bound in a legal relationship between two or more parties (most commonly a "fiduciary" or "trustee" and a "principal" or "beneficiary") . In English common law a fiduciary is arguably the most important concept within the portion of the legal system known as equity. In the United Kingdom, the *Judicature Acts* merged the courts of Equity (historically based in England's Court of Chancery) with the courts of common law, and as a result the concept of fiduciary duty also became usable in common law courts.

> “ A fiduciary is someone who has undertaken to act for and on behalf of another in a particular matter in circumstances which give rise to a relationship of trust and confidence. ”

A fiduciary duty is the highest standard of care at either equity or law. The NBP can be viewed as a fiduciary, with each individual member possessing a fiduciary relationship with respect to the NBP as an entity. As such, each member shall be expected to be loyally serve those to whom he owes the duty (Pensioners/Beneficiaries and Active Employees): he must not put his personal interests before the duty, and must not profit from his position as a fiduciary, unless the principal consents. The fiduciary relationship is highlighted by good faith, loyalty, and trust, and the word itself originally comes from the Latin *fides*, meaning faith, and *fiducia*. When a fiduciary duty is imposed, equity requires a stricter standard of behavior than the comparable tortious duty of care at common law. It is said the fiduciary has a duty not to be in a situation where personal interests and fiduciary duty conflict, a duty not to be in a situation where his fiduciary duty conflicts with another fiduciary duty, and a duty not to profit from his fiduciary position without express knowledge and consent. A fiduciary cannot have a conflict of interest. It has been said that fiduciaries must conduct themselves "at a level higher than that of a common individual.

فائدة ثابتة Fixed Interest: a guaranteed rate of interest paid for the term of the investment.

صندوق Fund: a general term to described collective investments, such as unit and investment trusts or mutual funds. Funds pool the investments of smaller investors to invest in portfolios of shares, fixed- interest securities or other assets.

محفظة مختلطة الاهداف Growth-Income Portfolio is a collection of growth stocks based on a stock market investment approach in which the emphasis is on identifying stocks with superior long-term earnings and stock growth potential. Opposite of a value-oriented strategy in which analysts look for undervalued stocks. (Also see **Value-Income Portfolio.)**

سهم متنامي القيمة Growth Stock is a stock of a small to mid-capitalization company that is expanding rapidly. Growth stocks offer the greatest long-term appreciation potential, but are also the most volatile and vulnerable to changing business conditions.

سندات مضمونة Guaranteed Bond: a lump sum investment that provides a fixed level of income normally over a period of one to five years and a return of capital at the end of the term.

Liability Driven Investment Strategy (LDI) is an investment strategy of a company based on its risk tolerance, the company's ethics and the target return. The target return is usually linked to an index or combination of indices of the sector or any other like S&P 500. This is called the benchmark-driven investment strategy. Especially in the long-term investments, like pension fund, the benchmark-driven is no longer appreciated. Now the buzzword is LDI. The investment target of the fund is no longer linked to any external index, but to the liability of the fund, which is evaluated by the actuaries. In case of pension fund, it will be the present value of the benefits payable to the employees and pensioners, attached with a probability of those payments made.

A pension fund following an LDI focuses on the pension-fund assets in the context of the promises made to employees and pensioners (known as liabilities). This is in contrast to an approach which focuses purely on the asset side of the pension fund balance sheet. Typical LDI strategies involve hedging, in whole or in part, the fund's exposure to changes in interest rates and inflation. These risks can erode a pension scheme's ability to keep their promises to members. Historically, bonds were used as a partial hedge for these interest rate risks but the recent growth in LDI has focused on using swaps and other derivatives. These offer significant additional flexibility and capital efficiency compared to bonds.
LDI investment strategies have recently come to prominence in the UK and US largely as the result of country regulatory body requirement that companies post the funding position of a pension fund on the corporate sponsor's balance sheet.

نظرية المحفظة الاستثمارية الحديثة Modern Portfolio Theory Investment asset allocation theory developed by 20th Century investment analysts and researchers that stresses diversification in order to reduce risk and increase long-term performance. Key assumptions of the theory are that investors prefer higher returns to lower, less risk to more, and that they have long-term time horizons. Under the theory, by adding a relatively risky, high-return asset to a portfolio, you can not only increase the expected return, you also decrease the risk.

السياسة النقدية Monetary Policy is the **g**overnmental policy regulating the supply of money in the economy. For instance, in a weak economy, the government might stimulate growth by extending more credit to the banking industry. That action serves to increase the amount of money in circulation, which bolsters the economy. By the same token, the government can temper an overheating economy by reducing the money supply through bank credit restrictions.

صندوق السوق النقدية Money Market Fund is a mutual fund that invests in high quality, short-term debt instruments such as Treasury bills or certificates of deposit. Money market fund investors earn a steady stream of interest income that varies with short-term interest rates. Generally investors may cash out at anytime.

ادوات السوق النقدية Money Market Instrument A short-term, low-risk security such as commercial paper, Government Treasury bills, certificates of deposit and bankers` acceptances

شركة مودي لخدمات المستثمرين **Moody`s Investor Service** A company that rates the quality of bonds issued by corporations and governments. The rating system includes a number of fine gradation between the safest "investment grade" bonds and the riskiest "high yield" or "junk" bonds.

شركة استثمار مفتوحة الراسمال Open-Ended Investment Companies: OEICSA are funds that are similar to unit trusts with only one price at which they are bought and sold.

محفظة استثمارية Portfolio: The collection of all investments held by in a fund or managed by an investment manager. This collection can include stocks, bonds, real estate, mutual funds, etc.

Redemption Yield: the return on fixed-interest securities taking into account interest paid and any capital gain or loss at maturity.

مردود، عائد Return: The income or capital growth earned by your savings.

مخاطرة Risk: the likelihood that the value of your investment could fall.

سهم Share: a part-ownership of a company.

سهم، عائد **Stock** represents a share of ownership in a corporation. Stocks and Equities are often used to refer to the same thing.

مخاطر نظامية Systematic Risk Also known as "market risk," it refers to the risk attached to the overall market, rather than to an individual stock or bond. When an entire national bond or stock market rises or falls, most of the individual securities in that market tend to rise and fall with the market. (Also see **Unsystematic Risk.)**

اجل/ مدة سريان Term: describes the period of investment - short term is typically one to five years, medium term is five to ten, and long term is ten years or more

المدخل النزولي للاستثمار Top-Down Approach Stock market investment approach in which the emphasis is on economic trends rather than individual stocks. This investment approach is the opposite of bottom-up analysis. Analysts attempt to identify industries or geographic regions with the greatest potential for gain, and then invest in stocks of those categories. (Also see B**ottom-Up Analysis.)**

العائد الكلي Total Return is the combined income (dividends, interest, etc.) and capital growth earned by your savings.

مخاطر غير منتظمة Unsystematic Risk The risk attached to a particular security, independent of the movement of the market (as opposed to "systematic risk" or "market risk, " which refers to the risks attached to the movements of the overall market). For instance, bad earnings news may cause a stock`s price to fall even on a day when the overall market i s moving up. (Also see **Systematic Risk.)**

Value-Income Portfolio is a collection of stocks using the market investment approach in which the emphasis is on identifying undervalued stocks -- those that may have been knocked down in price by the market further than they should have been. Value-oriented investors try to buy those stocks when they appear to be poised for a rebound. (Also see **Growth-Income Portfolio**.)

سعر فائدة متغير Variable Rate: an interest rate that fluctuates.

عائد او غلة **Yield:** annual income from an investment in percentage terms.