

Pension Fund Association for
Local Government Officials

Fiscal Year 2018

Review of Operations

Employees' Pension Insurance Benefit
Adjustment Fund



地方公務員共済組合連合会

Pension Fund Association for Local Government Officials

Table of Contents

<u>Fiscal Year 2018 Investment Results (Overview)</u>	3
--	----------

Section 1 Administration and Investment of Funds in FY2018

1. Investment results	
(1) Asset mix	5
(2) Investment return	5
(3) Excess return	6
(4) Investment income	7
(5) Value of assets	7
(6) Fees	8
2. Risk management	
(1) Approach to risk management	9
(2) Risk management efforts	9
(3) Status of risk management (Overall assets)	11
3. Contribution analysis of excess return by asset and status of risk management	12
4. Alternative assets	16
5. Stewardship activities	19
6. Selection and management of entrusted investment management institutions, etc. (traditional assets)	29

Section 2 Business and Fund Management of Association

1. Establishment	31
2. Major operations	32
3. Organization	
(1) Governing Council	32
(2) Fund Management Committee of Pension Fund Association for Local Government Officials	33
(3) Executives and Secretariat	35
(4) Meetings	35
(5) Governance structure	36

4. Investment of funds	
(1) Mechanisms	37
(2) Basic approach to investment	37

[DISCLAIMER] When there are any discrepancies between the original Japanese version and the English translation version, the original Japanese version shall prevail.

[Abbreviations]

Local Public Service Mutual Aid Associations: Collectively means the Mutual Aid Association of Prefectural Government Personnel, the Japan Mutual Aid Association of Public School Teachers, the Japan Police Personnel Mutual Aid Association, the Mutual Benefit Association for Tokyo Metropolitan Government Employees, the National Federation of Mutual Aid Associations for Municipal Personnel and the Pension Fund Association for Local Government Officials.

Member associations: Collectively means the Mutual Aid Association of Prefectural Government Personnel, the Japan Mutual Aid Association of Public School Teachers, the Japan Police Personnel Mutual Aid Association, the Mutual Benefit Association for Tokyo Metropolitan Government Employees and the National Federation of Mutual Aid Associations for Municipal Personnel.

National Federation: National Federation of Mutual Aid Associations for Municipal Personnel

Association: Pension Fund Association for Local Government Officials

KKR: Federation of National Public Service Personnel Mutual Aid Associations

PMAC: Promotion and Mutual Aid Corporation for Private Schools of Japan

GPIF: Government Pension Investment Fund

EPI Act: Employees' Pension Insurance Act (Act No. 115 of 1954)

Local Public Officers, etc. Mutual Aid Association Act: Local Public Officers, etc. Mutual Aid Association Act (Act No. 152 of 1962)

Order for Enforcement of Local Public Officers, etc. Mutual Aid Association Act: Order for Enforcement of Local Public Officers, etc. Mutual Aid Association Act (Cabinet Order No. 352 of 1962)

Regulation for Enforcement of Local Public Officers, etc. Mutual Aid Association Act: Regulation for Enforcement of Local Public Officers, etc. Mutual Aid Association Act (Ministerial Order of Ministry of Home Affairs No. 20 of 1962)

Implementation Procedures for Local Public Officers, etc. Mutual Aid Association Act: Implementation Procedures for Local Public Officers, etc. Mutual Aid Association Act (Ministerial Order of Prime Minister's Office, Ministry of Education, Science and Culture and Ministry of Home Affairs No. 1 of 1962)

Fiscal Year 2018 Investment Results (Overview)



Investment return: **+1.23%**



Investment income: **+¥139.7 billion**



Value of investment assets:
(As of the end of March 2019)

¥11,319.7 billion

As pension investment funds are intended for long-term investment, the investment status must be judged from the long-term perspective.

As investment income is based on the market value as of the end of each term, it should be kept in mind that it includes valuation gains/losses, which means it may change depending on market movements.

◆ Long-Term Status of Investments (last 15 years)

- Cumulative investment income*:

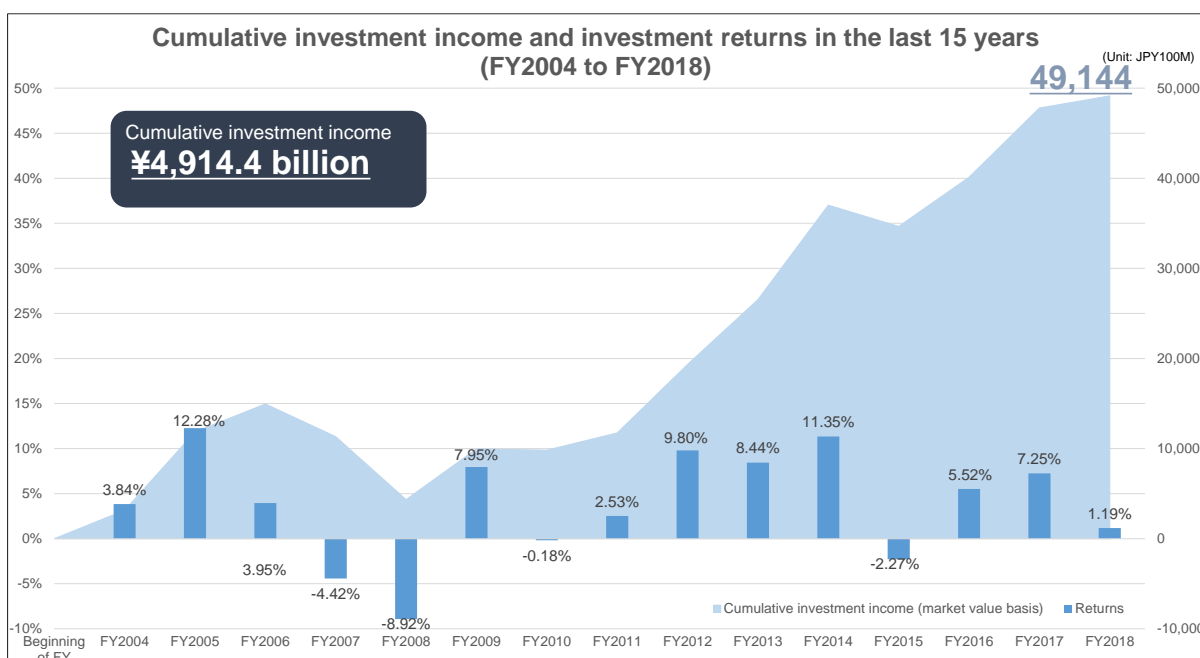
¥4,914.4 billion (Note 1)

- The average investment return (after deduction of fees):

3.72% (Note 2)

The real investment return **exceeded the investment return required from the perspective of pension finance.**

(See ① and ② in the table below.)



<Changes in the real investment return concerning funds>

		FY2004	FY2005	FY2006	FY2007	FY2008	FY2009	FY2010	FY2011	FY2012	FY2013	FY2014	FY2015	FY2016	FY2017	FY2018	Average of 15 years
Results	Nominal investment return	3.84%	12.28%	3.95%	-4.42%	-8.92%	7.95%	-0.18%	2.53%	9.80%	8.44%	11.35%	-2.27%	5.52%	7.25%	1.19%	3.72%
	(Note 3) Nominal wage growth rate	-0.20%	-0.17%	0.01%	-0.07%	-0.26%	-4.06%	0.68%	-0.21%	0.21%	0.13%	0.99%	0.50%	0.03%	0.41%	0.95%	-0.08%
	Real investment return ①	4.05%	12.47%	3.94%	-4.36%	-8.68%	12.52%	-0.85%	2.74%	9.57%	8.30%	10.26%	-2.75%	5.49%	6.81%	0.24%	3.80%
Assumptions for actuarial calculation	Nominal investment return	1.69%	1.81%	2.21%	2.51%	3.00%	1.47%	1.78%	1.92%	2.03%	2.23%	1.34%	1.88%	2.17%	2.57%	3.08%	2.11%
	Nominal wage growth rate	0.60%	1.30%	2.00%	2.30%	2.70%	0.05%	3.41%	2.66%	2.81%	2.60%	1.00%	2.47%	2.52%	3.56%	3.73%	2.24%
	(Note 4) Real investment return ②	1.08%	0.50%	0.21%	0.21%	0.29%	1.42%	-1.58%	-0.72%	-0.76%	-0.36%	0.34%	-0.59%	-0.35%	-0.99%	-0.65%	-0.13%
①-②		2.96%	11.97%	3.73%	-4.56%	-8.98%	11.10%	0.72%	3.46%	10.33%	8.66%	9.92%	-2.16%	5.84%	7.80%	0.89%	3.93%

(Note 1) The figures for income in and before the first half of fiscal year 2015 are estimates calculated by multiplying the value of income of the Long-term Benefit Fund in each fiscal year by the proportion of Employees' Pension Insurance Benefit Adjustment Fund at the time of the final allocation.

(Note 2) The nominal investment return for the whole of fiscal year 2015 cannot be calculated because the integration of employee pension plans was implemented during the year (October 2015), so it was mechanically estimated, as a reference figure, based on the nominal investment returns in the first half (Long-term Benefit Fund) and in the second half (Employees' Pension Insurance Benefit Adjustment Fund).

(Note 3) The figures for the nominal wage growth rate were cited from the Report on Investment of Investment Funds in FY2014 (September 2015, Ministry of Health, Labour and Welfare). The figures for fiscal year 2015 and later are those provided by the Ministry of Health, Labour and Welfare for Type 1 insured persons under employees' pension insurance as defined under the EPI Act after the revision made through Act No. 63 of 2012.

(Note 4) The figures for the real investment return used for actuarial calculations were cited from the Report on Investment of Investment Funds in FY2014. The figures for fiscal year 2015 and later were cited from the 2014 Actuarial Valuation (June 2014, Ministry of Health, Labour and Welfare).

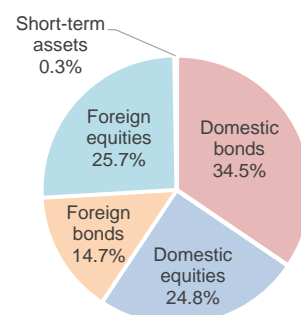
1 Investment results

(1) Asset mix

The asset mix changed as follows as a result of market value fluctuations and rebalancing, among other factors.

	End of FY2017	FY2018				Benchmark Portfolio
		End of Q1	End of Q2	End of Q3	End of FY	
Domestic bonds	35.9	35.1	33.6	36.5	34.5	35.0
Domestic equities	27.3	26.3	26.9	24.4	24.8	25.0
Foreign bonds	14.2	14.4	14.1	15.1	14.7	15.0
Foreign equities	21.9	24.0	24.9	23.9	25.7	25.0
Short-term assets	0.7	0.2	0.4	0.1	0.3	-
Total	100.0	100.0	100.0	100.0	100.0	100.0

Composition by Investment Asset Class (as of end of FY2018)



(Note 1) Deviation tolerances from the benchmark portfolio are $\pm 15\%$ for domestic bonds, $\pm 14\%$ for domestic equities, $\pm 6\%$ for foreign bonds and $\pm 12\%$ for domestic equities.

(Note 2) Due to rounding, the total sum of individual figures may not necessarily add up to 100%.

(Note 3) Short-term assets held by each fund were classified into relevant asset classes in principle.

(Note 4) The ratio of alternative assets to the total amount of funds is 0.5% (the upper limit is 5%).

(2) Investment return

The modified total returns came to 1.23% due to rises in foreign equity markets, among other factors.

	FY2018				
	Q1	Q2	Q3	Q4	FY total
Modified total returns	1.51	3.20	-8.82	5.99	1.23

	FY2018				
	Q1	Q2	Q3	Q4	FY total
Time-weighted return	1.52	3.21	-8.84	6.00	1.25
Domestic bonds	0.18	-0.69	1.02	0.97	1.47
Domestic equities	0.72	5.92	-17.95	7.79	-5.65
Foreign bonds	0.79	1.54	-2.53	2.92	2.67
Foreign equities	5.09	7.01	-15.77	13.85	7.85
Short-term assets	0.00	0.00	0.00	0.00	0.00

	FY2018				
	Q1	Q2	Q3	Q4	FY total
Realized return (book value basis)	1.15	0.86	0.42	0.71	3.14

(Note 1) The return in each quarter is the period rate.

(Note 2) The modified total return and time-weighted return represent the figures before the deduction of fees.

(Note 3) The realized return (book value basis) represents the figure after the deduction of fees.

(3) Excess return

The return (market value basis) for overall assets was 1.25%, while the excess return over the benchmark was -0.88%.

The excess return due to the asset allocation factor was -0.52% because of the adverse effects of overweighting in domestic equities, for which the benchmark return was negative compared with the benchmark return for overall assets, and

underweighting in foreign equities, for which the benchmark return was positive compared with the benchmark return for overall assets.

The excess return due to the individual asset factor was -0.39%, mainly because the returns on domestic bonds as well as domestic and foreign equities (market value basis) were lower than the benchmark returns.

	Domestic bonds	Domestic equities	Foreign bonds	Foreign equities	Overall assets
Return (market value)	1.47%	-5.65%	2.67%	7.85%	1.25%
Benchmark return	1.89%	-5.04%	2.46%	8.33%	2.12%
Excess Return	-0.43%	-0.61%	0.21%	-0.48%	-0.88%

(Note 1) Unless otherwise specified, the return (market value basis) refers to the time-weighted return. (The same shall apply hereinafter.)

(Note 2) The benchmark return for overall assets is calculated by weight-averaging the benchmark returns for individual asset classes based on the shares in the asset mix of the benchmark portfolio.

	Asset allocation factor ①	Individual asset factor ②	Other factor (including errors) ③	①+②+③
Domestic bonds	-0.07%	-0.15%	0.01%	-0.21%
Domestic equities	-0.20%	-0.16%	0.00%	-0.36%
Foreign bonds	-0.02%	0.03%	0.00%	0.02%
Foreign equities	-0.20%	-0.11%	0.01%	-0.29%
Short-term assets	-0.03%	0.00%	0.00%	-0.03%
Total	-0.52%	-0.39%	0.03%	-0.88%

(i) Asset allocation factor: A factor that is attributable to the difference in terms of the asset mix between the benchmark portfolio, which is the standard for the calculation of the composite benchmark, and the actual portfolio.

(ii) Individual asset factor: A factor that is attributable to the difference between the actual and benchmark returns concerning each asset class, which may arise depending on the level of investment expertise.

(iii) Other factor (including errors): A factor combining elements of the asset allocation and individual asset factors and calculation errors.

(4) Investment income

Investment income (market value basis) was ¥139.7 billion.

(Unit: JPY100M)

	FY2018				
	Q1	Q2	Q3	Q4	FY total
Investment income (market value basis)	1,701	3,657	-10,378	6,416	1,397
Domestic bonds	71	-276	398	374	567
Domestic equities	240	1,769	-5,681	2,032	-1,641
Foreign bonds	128	251	-420	473	432
Foreign equities	1,261	1,914	-4,675	3,538	2,038
Short-term assets	0	0	0	0	0

(Unit: JPY100M)

	FY2018				
	Q1	Q2	Q3	Q4	FY total
Realized income (book value basis)	1,125	842	420	704	3,091

(Note 1) The investment income (market value basis) represents the income before the deduction of fees.

(Note 2) The investment income (market value basis) represents the realized income (book value basis) adjusted for the effects of changes in valuation gains/losses based on market value.

(Note 3) Realized income (book value basis) represents the sum of trading profits/losses and interest and dividend income, etc. after the deduction of fees.

(Note 4) Due to rounding, the total sum of individual figures may not necessarily add up to the FY total.

(5) Value of assets

Value of investment assets (market value basis) was ¥11,319.7 billion.

(Unit: JPY100M)

	End of FY2017			FY2018											
				End of Q1			End of Q2			End of Q3			End of FY		
	Book value	Market value	Valuation gains/losses	Book value	Market value	Valuation gains/losses	Book value	Market value	Valuation gains/losses	Book value	Market value	Valuation gains/losses	Book value	Market value	Valuation gains/losses
Domestic bonds	39,207	40,342	1,135	38,776	39,912	1,137	38,821	39,550	729	37,914	38,985	1,071	37,831	39,062	1,231
Domestic equities	23,721	30,642	6,921	23,309	29,893	6,584	23,512	31,675	8,163	23,936	26,096	2,160	24,285	28,109	3,824
Foreign bonds	16,247	15,976	-271	16,390	16,304	-86	16,527	16,609	83	16,613	16,190	-423	16,796	16,664	-132
Foreign equities	17,480	24,545	7,065	19,244	27,307	8,063	19,509	29,221	9,711	20,649	25,546	4,897	20,883	29,067	8,185
Short-term assets	740	740	0	186	186	0	499	499	0	92	92	0	294	294	0
Total	97,394	112,246	14,851	97,905	113,602	15,697	98,868	117,554	18,686	99,202	106,908	7,705	100,089	113,197	13,108

Allocation changes of each asset class as a result of rebalancing

(Unit: JPY100M)

	Domestic bonds	Domestic equities	Foreign bonds	Foreign equities
Amount of funds allocated/withdrawn	-1,839	-873	262	2,500

(Note) The amount of funds allocated or withdrawn is the amount of cash balance (cash-in and cash-out) other than investment income.

(6) Fees

The amount of fees totaled ¥4.9 billion. The fee rate relative to the value of investment assets came to 0.04%.

Regarding entrusted investments, the Association has introduced a fee rate table in which the fee rate declines in proportion to the value of investment assets, and an incentive fee system (the upper limit is set on fee rate) for active investment.

(Unit: JPY100M, %)

	FY2018	
	Fee	Fee rate
Domestic bonds	8	0.02
Domestic equities	19	0.07
Foreign bonds	6	0.04
Foreign equities	16	0.06
Overall assets	49	0.04

(Note 1) Fees include management fees and custodian fees related to entrusted investment.

(Note 2) Fee rate = fee amount/month-end market value average balance

(Note 3) The month-end market value average balance for the overall assets includes short-term assets.

2 Risk management

(1) Approach to risk management

Generally speaking, "risk" refers to the "possibility of an incident that could have a negative impact on an organization's goals and objectives." In the field of asset investment, interest rate risk, price fluctuation risk, credit risk, liquidity risk and other factors are viewed as "risks" in some cases, while the possibility that the required yield cannot be ensured may be viewed as a "risk" in other cases.

Therefore, for asset investment, it is important to consider various risks commensurate with investment from a long-term perspective.

The Association appropriately implements

risk management concerning investment in accordance with the implementation policy for risk management concerning investment of the Employees' Pension Insurance Benefit Adjustment Fund in consideration of the following points: that investment of funds should be made safely and efficiently from a long-term perspective; that diversified investments should be maintained in principle; and that the relationship between all Local Public Service Mutual Aid Associations' liabilities and the funds in the future should be taken into consideration.

Implementation policy for risk management concerning investment of the Employees' Pension Insurance Benefit Adjustment Fund (excerpt)

1 Basic approach concerning risk management

The Pension Fund Association for Local Government Officials ("Association") appropriately conducts risk management related to the investment of adjustment funds in light of the following matters.

- (1) Manage adjustment funds safely and efficiently from a long-term perspective.
- (2) Develop a benchmark portfolio based on the principle of managing adjustment funds through appropriate diversification across multiple asset classes with different risk/return profiles and other characteristics (hereinafter referred to as "diversified investment") and manage the funds based thereon.
- (3) Manage adjustment funds in consideration of the relationship between all Local Public Service Mutual Aid Associations' liabilities related to employees' pension insurance operations and the funds in the future.

(2) Risk management efforts

■ Management of the deviation of the asset mix

Investment based on the benchmark portfolio requires the management of various risk factors. Therefore, in order to secure profits in line with the benchmark portfolio from the long-term

perspective, it is important, in particular, to manage the degree of deviation of the asset mix of the actual portfolio from that of the benchmark portfolio.

Specifically, as the asset mix constantly changes due to asset price fluctuations, the Association keeps track of the status of the deviation of the asset mix of its actual portfolio from that of the benchmark portfolio and manages the actual portfolio so as to keep the degree of deviation within a certain range (deviation tolerance) for overall assets. In this way, the Association checks whether or not

there are problems such as a deviation from the benchmark portfolio in excess of the deviation tolerance. In addition, flexible investment is made within the deviation tolerance in line with an investment policy formulated through deliberation at a meeting of experts. In this regard, the Association confirms that the existing deviation is in line with the investment policy.

■Monitoring of market risk, etc.

The Association monitors downside risks by using the value at risk approach, which measures the maximum foreseeable amount of losses, and stress tests, which conduct simulations assuming the application of certain shocks to markets.

As it also uses active investment in its investment of funds, the Association seeks to earn an excess return over the benchmark by

diversifying investment strategies and investment issues within each asset class.

Therefore, the Association monitors the status of market risk (price volatility risk, etc. in each asset market), credit risk (default risk), etc. with respect to each asset class, mainly from the viewpoint of difference from the benchmark for each asset class.

■Management of entrusted investment management institutions, etc.

The Association manages liquidity risk (risk that purchasing and selling assets will become difficult due to a decline in trading volume) from the viewpoint of revising asset allocations (rebalancing) and smooth conversion of assets into cash. In addition, as the Association entrusts the operation of some investment-related activities to external institutions, it

monitors the status of management (status of risk management and asset administration) of the institutions to which it entrusts asset management or asset administration (entrusted investment management institutions and asset administration institutions), from the viewpoint of smooth operation by individual institutions.

■Reporting on the status of risk management and improvement measures implemented

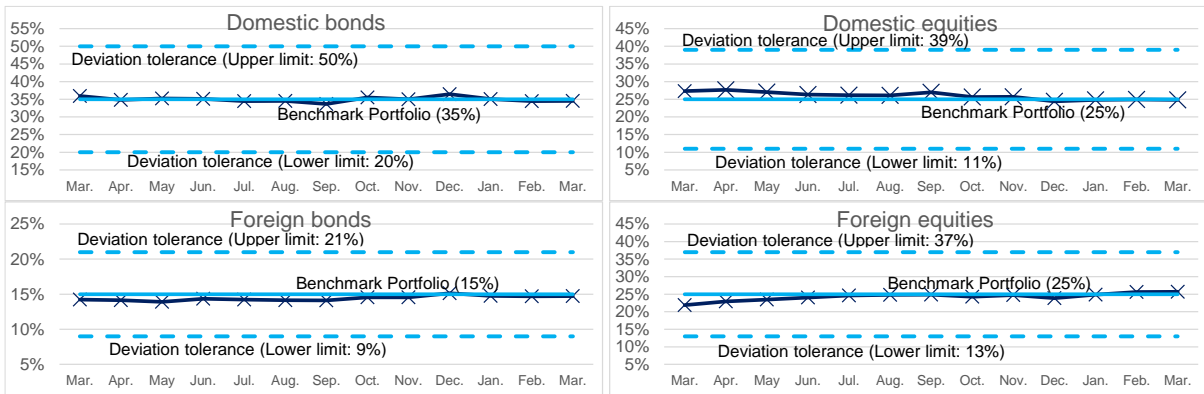
The Association reports on the status of risk management and improvement measures implemented to the Investment Risk Management Committee, the Fund Management Committee of Pension Fund Association for Local Government Officials and the Governing Council.

(3) Status of risk management (Overall assets)

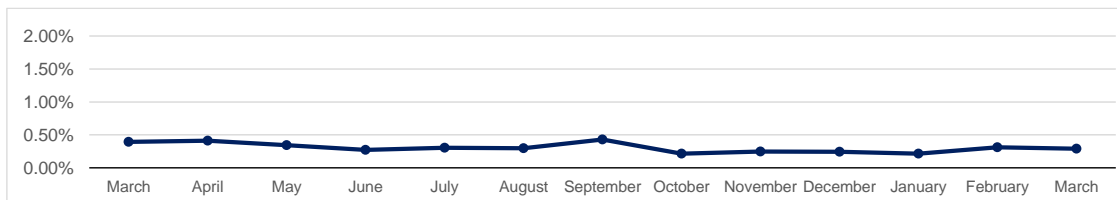
The shares in the asset mix concerning all asset classes—domestic bonds, domestic equities, foreign bonds and foreign equities—stayed within the deviation tolerance.

The estimated tracking error concerning overall assets did not show significant movements and remained stable.

【Changes in the asset mix】



【Changes in the estimated tracking error concerning overall assets】



(Note) The estimated tracking error concerning overall assets represents the tracking error concerning the benchmark portfolio (composite benchmark).

3 Contribution analysis of excess return by asset and status of risk management

(1) Domestic bonds

■ Contribution analysis of the excess return

By factor, the excess return of -0.43% on domestic bonds can be broken down as follows: fund factor: -0.43%; benchmark factor: 0.00%; other factors: 0.01%.

Regarding the fund factor, NOMURA-BPI (Active) and currency-hedged foreign bonds included among non-benchmark funds made positive contributions when foreign interest rates dropped steeply. However, the excess

return from domestic bonds was negative because the rate of price increase due to the interest rate drop was small compared with the benchmark as a result of shorter duration in mandatory investments compared with the benchmark and also because inflation-indexed government bonds were negatively affected by a rise in real interest rates due to a drop in the expected inflation rate.

Return (market value) ①	Benchmark ②	Excess Return ①-②	Fund factor	Benchmark factor	Other factor
1.47%	1.89%	- 0.43%	- 0.43%	0.00%	0.01%

【Contribution analysis of the excess return by the manager benchmark, etc.】

	Mandatory investment, etc.	Inflation-indexed government bond	Nomura BPI Overall (Passive)	Nomura BPI Overall (Active)	Nomura BPI Overall (Enhanced)	Non-benchmark (Active)	Domestic real property, etc.	Total
Fund factor	- 0.41%	- 0.10%	- 0.00%	0.04%	0.01%	0.03%	0.01%	- 0.43%
Benchmark factor			0.00%	0.00%	0.00%			0.00%

(Note 1) The fund factor is a factor attributable to the difference between the return for an individual fund and the return for the manager benchmark.

The percentage ratio is calculated in consideration of the average total market value of an individual fund.

Concerning mandatory investments, etc. and non-benchmark funds, a factor attributable to the difference between the return for an individual fund and the return for the policy benchmark is calculated as the fund factor for reference because the manager benchmark has not been set.

(Note 2) The benchmark factor is a factor attributable to the difference between the return for the manager benchmark and the return for the benchmark (NOMURA-BPI Overall).

The percentage ratio is calculated in consideration of the average total market value of an individual fund.

(Note 3) "Other factors" are factors attributable to calculation errors, asset transfer, etc.

(2) Domestic equities

■ Contribution analysis of the excess return

By factor, the excess return of -0.61% on domestic equities can be broken down as follows: fund factor: -0.62%; benchmark factor: 0.05%; other factors: -0.04%.

Regarding the benchmark factor, in the phase of stock price decline, positive contributions came from funds with reduced downside risk benchmarked against MSCI Japan Minimum Volatility (Active) and Japan Minimum Volatility Index (Active), which invest in low-

volatility issues. On the other hand, regarding the fund factor, market-specific funds investing in growth funds included in TOPIX (Active) and growth-oriented funds made negative contributions, as growth stocks weakened amid concerns over the deterioration of domestic companies' earnings due to wariness about a global economic slowdown. As a result, the excess return from domestic equities was negative.

Return (market value) ①	Benchmark ②	Excess Return ①-②	Fund factor	Benchmark factor	Other factor
- 5.65%	- 5.04%	- 0.61%	- 0.62%	0.05%	- 0.04%

【Contribution analysis of the excess return by the manager benchmark, etc.】

	TOPIX (Passive)	JPX400 (Passive)	MSCI JAPAN (Passive)	Russell/Nomura Prime (Passive)	TOPIX (Active)	TOPIX Mid400 (Active)	FTSE GWA Japan (Active)	FTSE RAFI Japan 350 QSR (Active)
Fund factor	0.07%	0.00%	0.00%	0.00%	- 0.61%	0.03%	0.00%	0.00%
Benchmark factor	0.00%	0.02%	0.02%	0.00%	0.00%	- 0.00%	0.01%	0.00%

	MSCI Japan Minimum Volatility (Active)	Russell/Nomura Small (Active)	S&P Japan Small Cap Index (Active)	SNAM Sustainability Index (Active)	Japan Minimum Volatility Index (Active)	Non-benchmark (Active)	Domestic PE	Total
Fund factor	- 0.00%	0.02%	- 0.02%	0.00%	- 0.00%	- 0.10%	- 0.00%	- 0.62%
Benchmark factor	0.06%	- 0.07%	- 0.02%	- 0.00%	0.02%			0.05%

(Note 1) The fund factor is a factor attributable to the difference between the return for an individual fund and the return for the manager benchmark.

The percentage ratio is calculated in consideration of the average total market value of an individual fund.

Concerning non-benchmark funds, a factor attributable to the difference between the return for an individual fund and the return for the policy benchmark was calculated as the fund factor for reference because the manager benchmark has not been set.

(Note 2) The benchmark factor is a factor attributable to the difference between the return for the manager benchmark and the return for the policy benchmark (TOPIX (with dividends)).

The percentage ratio is calculated in consideration of the average total market value of an individual fund.

(Note 3) "Other factors" are factors attributable to calculation errors, asset transfer, etc.

(3) Foreign bonds

■ Contribution analysis of the excess return

By factor, the excess return of 0.21% on foreign bonds can be broken down as follows: fund factor: 0.10%; benchmark factor: 0.13%; other factors: -0.02%.

Regarding the fund factor, positive contributions came from the FTSE World Government Bond Index (Passive), whose income from lending was positive, and stable income from facility operation of overseas infrastructure. Regarding the benchmark factor,

amid the dollar's appreciation against the yen and the euro's depreciation against the yen, positive contributions came from Barclays aggregate (Active), which was overweight in U.S. assets and underweight in European assets compared with the benchmark, and from overseas real properties (NFI-ODCE fund index), which is comprised exclusively of U.S. assets. As a result, the excess return from foreign bonds was positive.

Return (market value) ①	Benchmark ②	Excess Return ①-②	Fund factor	Benchmark factor	Other factor
2.67%	2.46%	0.21%	0.10%	0.13%	- 0.02%

【Contribution analysis of the excess return by the manager benchmark, etc.】

	FTSE World Government Bond Index (Passive)	FTSE World Government Bond Index (Active)	Barclays aggregate (Active)	Nomura RAFI (Active)	Overseas real properties (NFI-ODCE fund index)	Overseas infrastructure	Total
Fund factor	0.06%	- 0.00%	0.01%	0.00%	0.00%	0.03%	0.10%
Benchmark factor	0.00%	0.00%	0.07%	- 0.01%	0.07%		0.13%

(Note 1) The fund factor is a factor attributable to the difference between the return for an individual fund and the return for the manager benchmark. The percentage ratio is calculated in consideration of the average total market value of an individual fund.

(Note 2) The benchmark factor is a factor attributable to the difference between the return for the manager benchmark and the return for the policy benchmark (FTSE World Government Bond Index (excluding Japan; without currency hedging, yen-based)). The percentage ratio is calculated in consideration of the average total market value of an individual fund.

(Note 3) "Other factors" are factors attributable to calculation errors, asset transfer, etc.

(4) Foreign equities

■ Contribution analysis of the excess return

By factor, the excess return of -0.48% on foreign equities can be broken down as follows: fund factor: -0.42%; benchmark factor: 0.01%; other factors: -0.07%.

Regarding the fund factor, as defensive issues, regardless of valuation, were selected due to concerns over global recession, negative contributions came from value-oriented funds

benchmarked against MSCI-ACWI (Active), which were making investments mainly from the valuation perspective, and from market-specific funds benchmarked against MSCI-KOKUSAI (Active), whose issue selection was unfavorable. As a result, the excess return from foreign equities was negative.

Return (market value) ①	Benchmark ②	Excess Return ①-②	Fund factor	Benchmark factor	Other factor
7.85%	8.33%	- 0.48%	- 0.42%	0.01%	- 0.07%

【Contribution analysis of the excess return by the manager benchmark, etc.】

	MSCI-ACWI (Passive)	MSCI-ACWI (Active)	MSCI-KOKUSAI (Active)	MSCI-Emerging (Active)	Foreign PE	Total
Fund factor	- 0.09%	- 0.17%	- 0.17%	0.00%	- 0.00%	- 0.42%
Benchmark factor	0.00%	0.00%	0.13%	- 0.12%		0.01%

(Note 1) The fund factor is a factor attributable to the difference between the return for an individual fund and the return for the manager benchmark.
 The percentage ratio is calculated in consideration of the average total market value of an individual fund.

(Note 2) The benchmark factor is a factor attributable to the difference between the return for the manager benchmark and the return for the policy benchmark (MSCI-ACWI).

The percentage ratio is calculated in consideration of the average total market value of an individual fund.

(Note 3) "Other factors" are factors attributable to calculation errors, asset transfer, etc.

4 Alternative assets

(1) Objectives of investment

■ Improving investment efficiency through diversified investment

As the sources of returns for alternative assets are different from the sources for traditional assets, alternative assets are suitable for diversified investment. Alternative assets can be classified into real estate, infrastructure, PE (private equity), PD (private debt) and bank loans, among other asset classes. Regarding

real estate, for example, the return trend varies from usage to usage and from region to region. Therefore, the Association raises investment efficiency through diversified investment by allocating assets in such a way that they are not concentrated in specific classes, regions or sectors.

■ Earning liquidity premiums

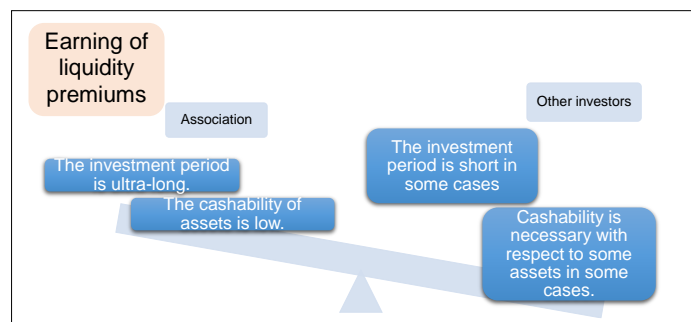
Generally speaking, while the liquidity (cashability) of investment stakes in alternative assets is low, a premium that compensate for the low liquidity is added to the return.

Generally, investors other than public pension funds may need to secure a certain degree of liquidity for their investment assets because of

reasons such as a short period of investment. However, the Association is relatively free from the liquidity-related constraint because of its ultra-long-term investment period.

Therefore, by investing in alternative assets, the Association enjoys premiums in exchange for accepting low liquidity.

【Liquidity-related constraint】



■ Measures taken to respond to inflation and interest rate rises

Generally speaking, bond prices drop when interest rates rise. However, in the case of real estate and infrastructure, income for investment assets also change in tandem with an interest rate rise. As a result, the impact of an interest rate rise on asset prices is not so direct as the impact in the case of bonds. For some overseas

infrastructure assets, facility usage fees, which correspond to sales, are linked to inflation, which means that sales increase if inflation rises. Therefore, some alternative assets help to curb interest rate rise risk and inflation risk (an asset price decline due to an interest rate rise or inflation).

(2) Fund selection

■ Introduction of an asset manager registration system

An Asset Manager Registration System is a system whereby the Association accepts entries from entrusted investment management institutions for investment funds on an ongoing basis for the purpose of selecting investment funds and concluding contracts and evaluates and selects investment funds on an ongoing basis. In July 2015, the Association introduced

an Asset Manager Registration System for Alternative Investments and started receiving entries with respect to investment funds investing in real estate and infrastructure assets.

Subsequently, the Association added PE in June 2016 and PD and bank loans in July 2018 to the scope of eligible investment instruments.

■ Selection of investment funds

Among the investment funds registered, the Association carefully selected investment funds that were expected to deliver long-term returns and provide the diversified investment effect and conforming to the investment policies and selection criteria related to the investment strategy. As of the end of fiscal year 2018, based on a comprehensive evaluation from both quantitative and qualitative aspects, the

Association decided to adopt a total of 19 funds, and started the investment in 14 funds.

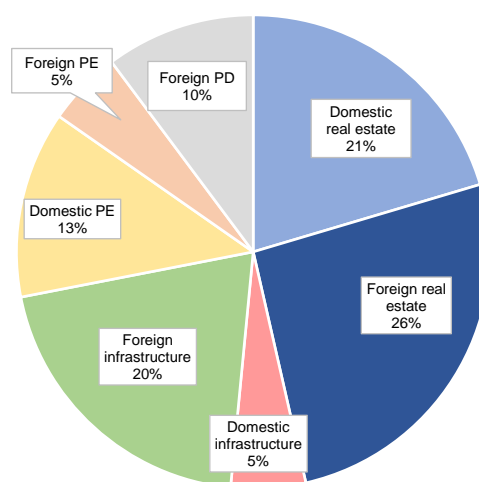
In the future, to seize opportunities for investing in superior investment funds likely to contribute to diversified investment of the funds, the Association will continue to evaluate the investment funds entered and make selection.

【Number of funds adopted】

Investment fund	Number of funds adopted
Domestic real estate	3
Foreign real estate	4
Domestic infrastructure	1
Foreign infrastructure	4
Domestic PE	4
Foreign PE	1
Foreign PD	2
Total	19

*As of the end of FY2018

【Asset mix】



*Commitment basis as of the end of FY2018

■ Monitoring of funds

With respect to the monitoring of alternative assets, it is difficult to manage risks only in light of indicators based on price changes (e.g., standard deviation and tracking error) because, unlike in the case of listed assets, price formation does not occur on a daily basis.

Therefore, the monitoring of real estate and infrastructure assets is conducted mainly through the evaluation of returns and market value of assets based on reports from entrusted investment management institutions. The

monitoring of PE assets is conducted mainly with respect to the implementation of measures to increase enterprise value and the actual status of investment management institutions' investment systems. The Association conducts periodic monitoring on a fund-by-fund basis. If unusual signs are detected, it checks with entrusted investment management institutions on the cause and planned countermeasures and requests them to make improvements as necessary.

【Example of risk management】

【Real estate and infrastructure】

- Status of diversification regarding trading of assets and holding of assets
- Trend in income for assets (e.g., operation rate)
- Trend in evaluated market value
- Changes in the leverage level (dependence on borrowings)

【PE】

- Status of progress in investment
- Status of diversification of investment instruments
- Status of investment candidate assets
- Management status of investee companies
- Progress in implementation of measures to increase investee companies' enterprise value

5 Stewardship activities

(1) Stewardship responsibilities

"Stewardship activities" refers to the activities of institutional investors to increase medium to long-term investment returns for their clients and beneficiaries by encouraging improvements in corporate value and sustainable growth of investee companies through means such as engagement (i.e. constructive "purposeful dialogue" based on a deep understanding concerning the investee companies, their business environment, and other factors).

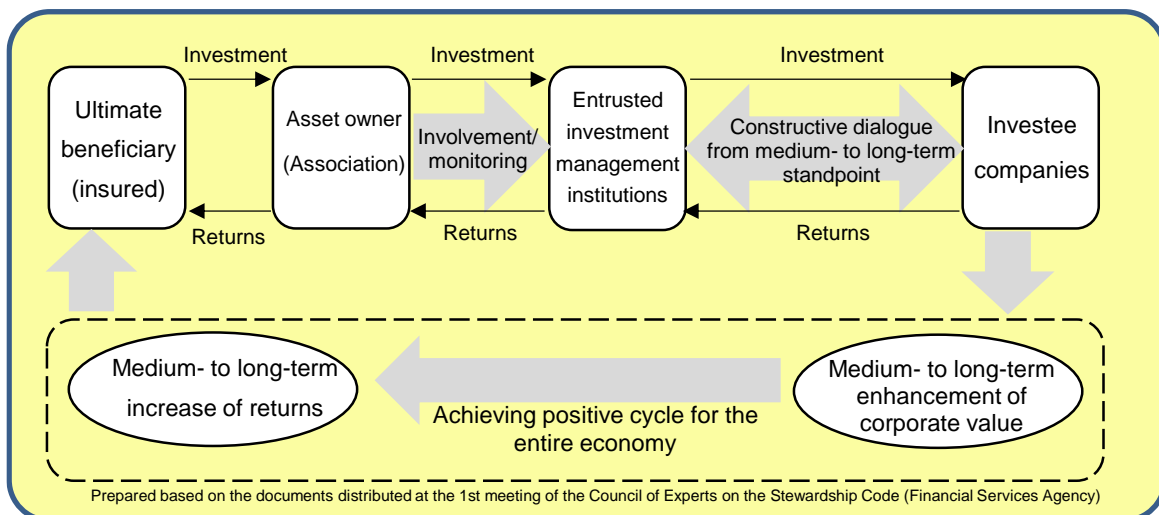
Stewardship activities include the exercise of shareholders' voting rights, engagement, and ESG investment.

The Association is required to fulfill its fiduciary responsibility of increasing the value of its assets for the insured over the long term

and social responsibility as a public pension fund. In this connection, as the means to seek medium- to long-term enhancement of corporate value and sustainable growth of investee companies, the Association has been proactively committed to effective stewardship activities.

In addition, the Association entrusts investment management institutions ("entrusted investment management institutions") to make investments in companies. The Association believes that conducting the stewardship activities through these entrusted investment management institutions is effective for fulfilling the stewardship responsibility as they have more opportunities to access investee companies and have in-depth insight on corporate management.

[Stewardship Activities]



Based on this idea, the Association established the "Corporate Governance Principles of Pension Fund Association for Local Government Officials" and the "Guidelines for Exercising Shareholders' Voting Rights (Domestic Equities)" (hereinafter referred to as "Guidelines for Domestic Equities") in 2004 and the "Guidelines for Exercising Shareholders' Voting Rights (Foreign Equities)" (hereinafter referred to as "Guidelines for Foreign Equities") in 2016. These guidelines and principles specify that the Association should conduct stewardship activity based on them when it has concluded contracts with

entrusted investment management institutions.

In addition, the principles concerning funds specify how the Association should fulfill its stewardship responsibilities.

Moreover, in May 2014, the Association signed up to Japan's Stewardship Code, and in November 2017, the Association made its approach to stewardship activity clearer than before following the revision of the Stewardship Code.

The Association has started investing in ESG fund in February 2010, and has entrusted investment in four ESG funds concerning domestic stocks.

[Chronology of the Association's stewardship activity]

Year	Activities
FY2004	- Established the Corporate Governance Principles of Pension Fund Association for Local Government Officials. - Established the Guidelines for Exercising Shareholders' Voting Rights. Instructed entrusted investment management institutions to exercise voting rights in line with the Guidelines.
FY2009	- Newly adopted one ESG fund concerning domestic stocks.
FY2014	- Signed up to Japan's Stewardship Code. - Newly added another ESG fund concerning domestic stocks.
FY2015	- Established the Administration and Investment Policy and the Basic Policy in association with the unification of pension systems. Specified measures to fulfill the stewardship responsibilities. - Newly added two ESG funds concerning domestic stocks.
FY2016	- Established the Guidelines for Exercising Shareholders' Voting Rights (Foreign Equities). Instructed entrusted investment management institutions to exercise voting rights in line with the Guidelines.
FY2017	- Signed up to Japan's Stewardship Code (Revised Version).

(2) Monitoring of entrusted investment management institutions

For each fiscal year, the Association has been monitoring the stewardship activities of the entrusted investment management institution of domestic equities so as to ensure the compliance with the Association's abovementioned policies, while focusing on the "quality" of stewardship efforts. The Association receives reports concerning stewardship activity from and holds interviews with the entrusted investment management institution.

In addition, following the start of the exercise of voting rights concerning foreign equities in

FY2016, the Association received reports on stewardship activity concerning foreign equities in FY2017 and conducted hearings in FY2018.

On April 25, 2018, the Association held briefing meetings on the direction of the Association's stewardship activity for investment management institutions entrusted with domestic and foreign stock investment in FY2018 and explained the matters which the Association considers important in relation to stewardship activities (see below).

Matters which the Association considers important in relation to stewardship activities

[Exercise of voting rights]

- (i) Compliance with the Association's guidelines for exercising shareholders' voting rights**
- (ii) Exercise of voting rights suited to the circumstances of companies**

[Exercise of voting rights/engagement]

- **Exercise of voting rights and engagement in an integrated manner**

[Engagement]

- (i) Engagement aimed at enhancing the corporate value and sustainable growth of companies**
- (ii) Details of engagement**
- (iii) Effectiveness of processes (e.g. PDCA cycle)**

In July 2018, the Association requested 23 investment management institutions entrusted with domestic stock investment and 15 investment management institutions entrusted with foreign stock investment to submit reports on stewardship activities of FY2017. Based on

the reports submitted, the Association held interviews focused on the matters which the Association considers important in relation to stewardship activities (from November 19 to December 20, 2018).

(3) Results of the exercise of voting rights (domestic equities)

Regarding the Employees' Pension Insurance Benefit Adjustment Fund, the Association exercised voting rights through the 23 investment management institutions entrusted with domestic stock investment (43 funds in total), with respect to a total of 15,617 companies which settled accounts between April 2017 and March 31, 2018. The number of proposals for which voting rights were exercised was 52,631.

Of the 52,631 proposals, 12,592 (including 1,585 shareholder proposals) were voted

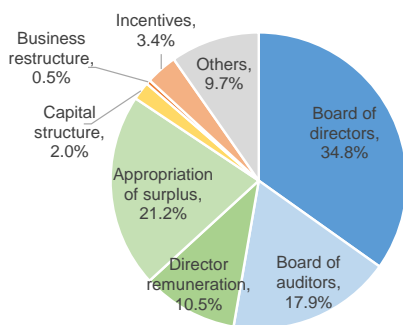
against, translating into a vote-against rate of 23.9% (almost the same level as that of the previous year). The vote-against rate concerning company proposals was 21.6% (up 1.2 points from the previous year).

The vote-against rate came to 40.2% (down 0.6 points) concerning proposals related to the board of directors/directors, 15.0% (up 1.6 points) concerning proposals related to the board of auditors/auditors and 19.4% (up 4.1 points) concerning proposals related to director remuneration, etc.

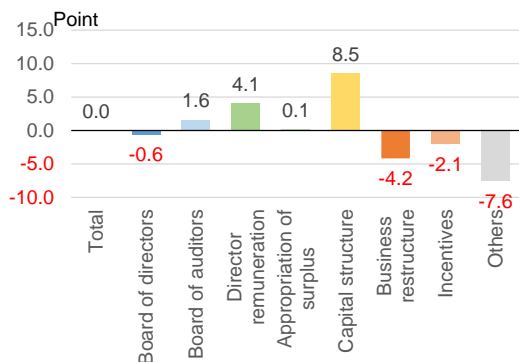
Voting activity (Companies with accounting settlement between April 2017 and March 2018)

Proposal Subject	Total	Composition	Vote for		Vote against		Vote-against rate in the previous year
				Rate		Rate	
Total	52,631	100%	40,039	76.1%	12,592	23.9%	23.9%
c.f. Company Proposal	50,900	96.7%	39,893	78.4%	11,007	21.6%	20.4%
c.f. Shareholder Proposal	1,731	3.3%	146	8.4%	1,585	91.6%	94.2%
By Subject	52,631	100%	40,039	76.1%	12,592	23.9%	23.9%
Board of Directors/Directors	18,333	34.8%	10,954	59.8%	7,379	40.2%	40.9%
Board of Auditors/Auditors	9,417	17.9%	8,008	85.0%	1,409	15.0%	13.3%
Director Remuneration, etc.	5,514	10.5%	4,444	80.6%	1,070	19.4%	15.3%
Appropriation of Surplus	11,136	21.2%	10,599	95.2%	537	4.8%	4.7%
Capital Structure	1,050	2.0%	661	63.0%	389	37.0%	28.5%
Takeover Defense Measures	398	0.8%	25	6.3%	373	93.7%	88.5%
Capital Increase or Reduction	32	0.1%	31	97%	1	3.1%	0.0%
Third Party Allotment of Shares	24	0.0%	20	83.3%	4	16.7%	19.2%
Acquisition of Own Shares	9	0.0%	5	55.6%	4	44%	100.0%
Business Restructure	251	0.5%	245	97.6%	6	2.4%	6.6%
Incentives Improvement for Executives	1,813	3.4%	1,436	79.2%	377	20.8%	22.9%
Other proposals	5,117	9.7%	3,692	72.2%	1,425	27.8%	35.5%

Share by proposal subject



Changes in the vote-against rate (compared with the previous year)

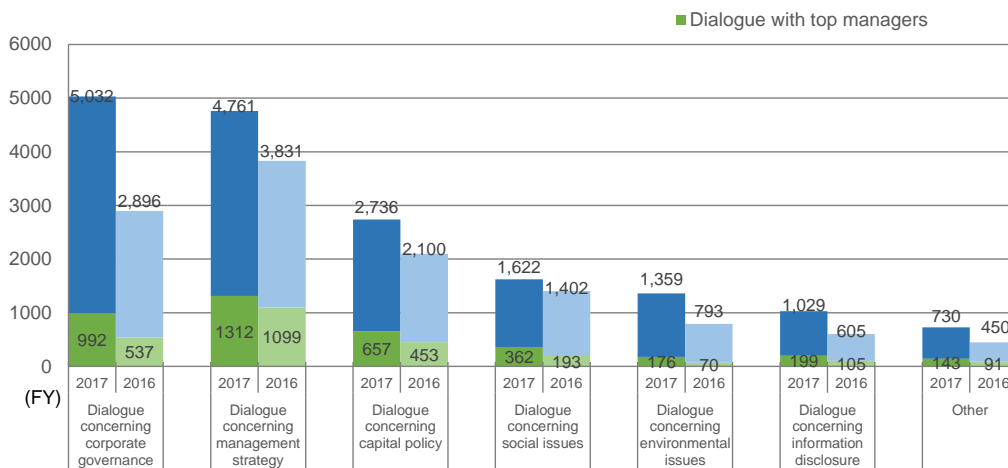


(4) Results of engagement activities (domestic equities)

Regarding the Employees' Pension Insurance Benefit Adjustment Fund, in FY2017, the Association implemented engagement with a total of 6,323 companies through 23 investment management institutions (a total of 43 funds) to which domestic stock investment was entrusted. The number of cases of dialogue was 17,269 (up 43.0% from the previous year).

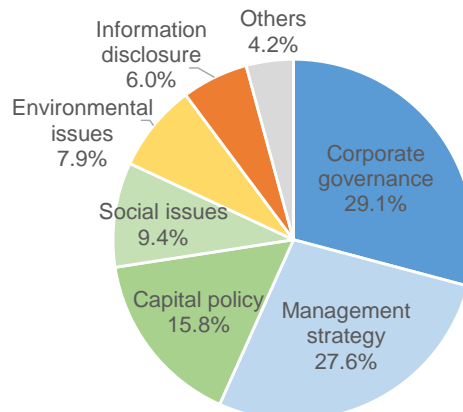
While some entrusted investment management institutions increased engagement staff, others focused on engagement related to environmental issues, social issues and corporate governance against the backdrop of increased attention on these issues by companies. As a result, the number of cases of engagement increased significantly.

**Number of cases of engagement (including overlaps)
From April 2017 to March 2018**



*The standard for counting the number of cases of engagement varies from entrusted investment management institution to entrusted investment management institution.

Share by dialogue item



(5) Results of the exercise of voting rights (foreign equities)

Regarding the Employees' Pension Insurance Benefit Adjustment Fund, the Association exercised voting rights through the 15 investment management institutions entrusted with foreign stock investment (18 funds in total), with respect to a total of 7,379 companies which settled accounts between April 2017 and March 31, 2018. The number of proposals for which voting rights were exercised was 51,995.

Of the 51,995 proposals, 5,853 (including

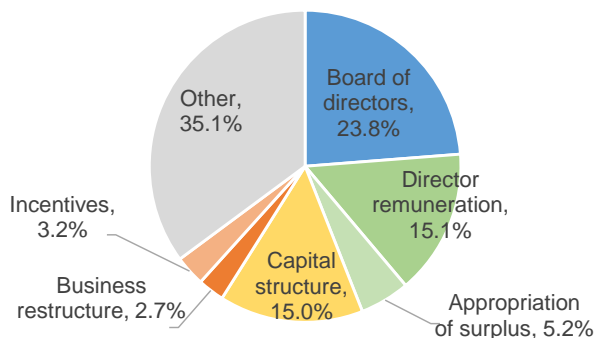
1,388 shareholder proposals) were voted against, translating into a vote-against rate of 11.3% (up 0.7 points from the previous year). The vote-against rate concerning company proposals was 9.1% (up 1.0 point).

The vote-against rate came to 11.6% (up 0.5 points) concerning proposals related to the board of directors/directors and 9.9% (down 0.2 points) concerning proposals related to director remuneration.

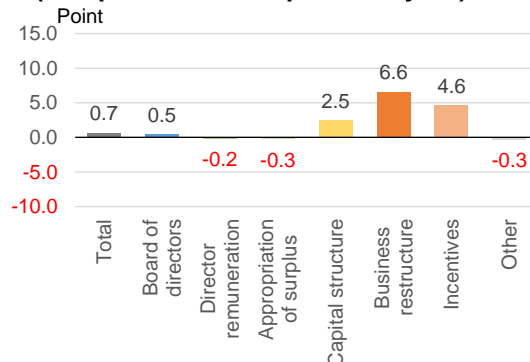
Voting activity (Companies with accounting settlement between April 2017 and March 2018)

Proposal Subject	Total	Composition	Vote for		Vote against		Vote-against rate in the previous year
				Rate		Rate	
Total	51,995	100%	46,142	88.7%	5,853	11.3%	10.6%
c.f. Company Proposal	48,809	93.9%	44,344	90.9%	4,465	9.1%	8.2%
c.f. Shareholder Proposal	3,186	6.1%	1,798	56.4%	1,388	43.6%	49.7%
By Subject	51,995	100%	46,142	88.7%	5,853	11.3%	10.6%
Board of Directors/Directors	12,355	23.8%	10,918	88.4%	1,437	11.6%	11.2%
Director Remuneration, etc.	7,835	15.1%	7,061	90.1%	774	9.9%	10.0%
Appropriation of Surplus	2,691	5.2%	2,667	99.1%	24	0.9%	1.1%
Capital Structure	7,777	15.0%	6,614	85.0%	1,163	15.0%	12.4%
Takeover Defense Measures	384	0.7%	363	94.5%	21	5.5%	9.0%
Capital Increase or Reduction	3,299	6.3%	2,640	80%	659	20.0%	19.3%
Third Party Allotment of Shares	663	1.3%	590	89.0%	73	11.0%	1.0%
Acquisition of Own Shares	1,812	3.5%	1,700	93.8%	112	6%	3.5%
Business Restructure	1,429	2.7%	1,242	86.9%	187	13.1%	6.5%
Incentives Improvement for Executives	1,640	3.2%	1,308	79.8%	332	20.2%	15.6%
Other proposals	18,268	35.1%	16,332	89.4%	1,936	10.6%	10.9%

Share by proposal subject



Changes in the vote-against rate (compared with the previous year)

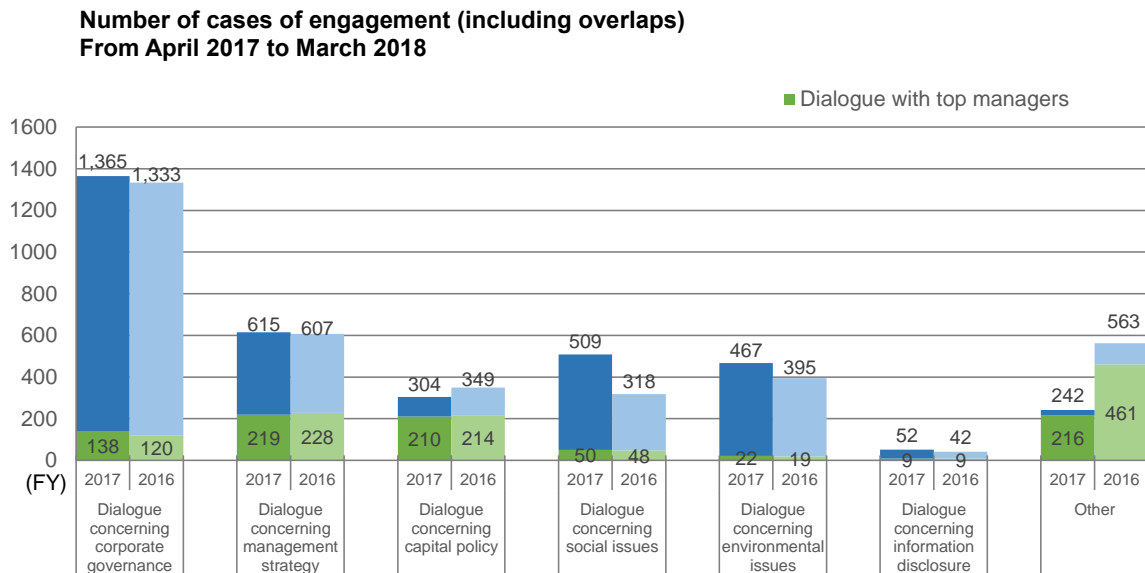


* From the viewpoints of constraints related to the exercise of voting rights and additional cost burden, the exercise of voting rights is limited to 18 countries (the United States, Canada, the United Kingdom, Ireland, Australia, New Zealand, Singapore, Hong Kong, Chile, the Czech Republic, Indonesia, Mexico, the Philippines, South Africa, Taiwan, Thailand, Pakistan and China A Stock). (The underlined country and stock were newly added in April 2018 to the scope of foreign investments for which voting rights may be exercised.)

(6) Results of engagement activities (foreign equities)

Regarding the Employees' Pension Insurance Benefit Adjustment Fund, in FY2017, the Association implemented engagement with a total of 1,326 companies through 15 investment management institutions (a total of 18 funds) to which foreign stock investment was entrusted. The number of cases of dialogue was 3,554 (down 1.5% from the previous year).

While some entrusted investment management institutions increased engagement staff or strengthened engagement related to environmental issues, others more strictly defined engagement. As a result, the number of cases of engagement declined slightly.



*The standard for counting the number of cases of engagement varies from entrusted investment management institution to entrusted investment management institution.

Share by dialogue item



(7) ESG investment

■ ESG investment initiative

As the Association invests pension funds over the long term, it is rational to aim to maximize the long-term return by paying attention not only to short-term business performance when making investment but also to factors related to sustainability, including ESG.

The Association believes that it can simultaneously fulfill the fiduciary responsibility of increasing the value of stocks for the insured persons over the long term and the social responsibility as a public pension fund by seeking to increase the investment return through the sustainable growth of investee

companies and the enhancement of shareholder value and by encouraging efforts to resolve social challenges, such as environmental, human rights and employment issues.

The Association started investing in ESG funds in February 2010. Based on interviews with entrusted investment management institutions, the Association has confirmed that around 90% of existing active funds give consideration to ESG elements and that ESG elements are mainly used as a supplemental judgement factor for stock selection.

【ESG investment (as of the end of FY2018)】

Number of funds	Total market value
4	50.9 billion yen

■ Approach to ESG investment

Of the ESG-related four funds adopted by the Association, three fall into the ESG integration category and one falls into the engagement category.

ESG integration refers to an investment approach that gives consideration to the ESG elements in the process of selecting stocks from the investment universe for possible inclusion in the portfolio. The examples of specific approaches to ESG investment are as follows:

- An entrusted investment management institution uses an external organization to select stocks relatively highly evaluated in terms of ESG within each industry as components of the investment universe. Fund managers select stocks from the universe based on evaluation conducted from two viewpoints—the stock price level and whether the companies' ESG initiatives are likely to lead to earnings growth. The portfolio is comprised mainly of stocks highly evaluated by fund managers in terms of ESG.
- Analysts evaluate stocks under research in terms of their fundamentals and ESG performance. The ESG evaluation is a combination of basic evaluation based on third-party information obtained from external ESG evaluation organizations and analysts' evaluation based on qualitative information obtained through dialogue. A score table is prepared with scores given with respect to detailed items concerning the ESG elements. Fund managers integrate the fundamentals evaluation and the ESG evaluation and select stocks in such a way that the deviation value of each of the items concerning the ESG elements in the whole portfolio is higher than 50.

- An entrusted investment management institution has adopted a smart beta strategy under which its funds track an index internally developed based on the combination of the ESG evaluation and the stock price evaluation. The entrusted investment management institution uses an external organization to recognize companies whose ESG performance exceed a certain level as components of the index. Asset weight allocation is determined by adding to the basic weight (a uniform weight for all stocks: 60% of the overall weight) a weight calculated on the basis of an ESG adjusted stock price (40%), which is a stock price multiplied by a co-efficient reflecting the ESG evaluation.

Engagement refers to objective-oriented constructive dialogue based on in-depth understanding of investee companies and their operating environment. The examples of specific approaches to ESG investment are as follows:

- After picking stocks with high quality in terms of ROIC (return on invested capital), an entrusted investment management institution makes stock selection from among them in light of factors such as the room for improvement of competitiveness and the viability of the dialogue effect, aiming to increase corporate value through cooperative engagement from the view point of ESG.

The approach to ESG varies from fund to fund. However, through interviews with entrusted investment management institutions, the Association learned that they make efforts to identify the ESG elements concerning individual funds and use ESG as a reference for stock selection. In this way, they are reducing the risk of corporate value being undermined and are promoting investment in companies whose corporate value is expected to increase in the medium to long term.

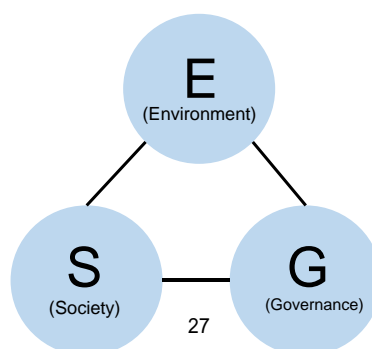
■ Performance of ESG investment

Entrusted investment management institutions are making investments through various approaches based not only on ESG evaluation but also on stock price evaluation with respect to individual funds adopted by the Association. The earning of excess return over the policy benchmark (the TOPIX index including dividends) differs from fund to fund and from year to year.

There is not yet an established consensus on whether the ESG approach leads to an excess return. The method of analyzing the relationship

of ESG evaluation and engagement with investment performance varies across entrusted investment management institutions with respect to funds adopted by the Association.

The Association plans to continue ESG initiatives such as evaluating the effectiveness and usefulness of ESG investment according to the investment horizon by cooperating with entrusted investment management institutions in checking how the ESG elements are contributing to the investment performance.



(8) Future initiatives

The Association will continue to actively conduct stewardship activity in order to simultaneously fulfill the fiduciary and social responsibilities.

■ Implementation of effective monitoring of entrusted investment management institutions

The Association will continue to make sure that entrusted investment management institutions' stewardship activity is consistent with the Association's policy and will conduct monitoring with emphasis placed on the "quality" of initiatives in terms of whether entrusted investment management institutions are implementing engagement with investee companies and are exercising voting rights in an effective manner and whether they are encouraging the companies to ensure effective corporate governance.

■ Dialogue with entrusted investment management institutions and accumulation of knowledge within the Association

From the viewpoint of continuously enhancing the effectiveness of stewardship activity, the Association conducts dialogue with entrusted investment management institutions about matters of priority and accumulates knowledge concerning stewardship activity.

■ Review of the approach to engagement

From the viewpoint of enhancing the effectiveness and sustainability of engagement conducted by entrusted investment management institutions, the Association continues to study what kind of engagement it should require while examining national trends and monitoring entrusted investment management institutions.

■ Revision of the corporate governance principles, etc.

The Association will revise the Corporate Governance Principles of Pension Fund Association for Local Government Officials, the Guidelines for Exercising Shareholders' Voting Rights (Domestic Equities) and the Guidelines for Exercising Shareholders' Voting Rights (Foreign Equities) as necessary while taking into consideration revisions of laws, regulations and codes and changes in the social situation.

■ Collaboration with other public pension funds, etc.

The Association will make appropriate judgment on matters related to dialogue with investee companies and stewardship activity. As part of its efforts to enhance the effectiveness and efficiency of stewardship activity, the Association will also exchange opinions with its member associations and other public pension funds, among other activities.

6

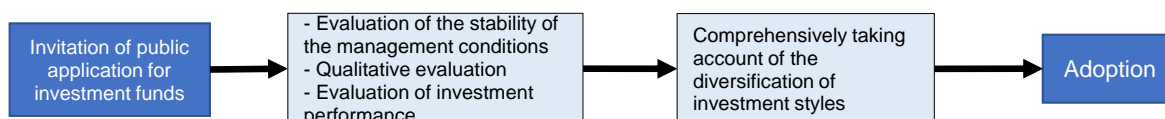
Selection and management of entrusted investment management institutions, etc. (traditional assets)

■ Approach to selection

In accordance with the criteria prescribed by policies including the Basic Policy for Employees' Pension Insurance Benefit Adjustment Fund, the Association makes the selection by comprehensively taking account of the diversification of investment styles across its entire portfolio and other factors based on the benchmark portfolio, after conducting the evaluation of the stability of the applicant institutions' management conditions (capital amount, financial position, number of employees, customer base, etc.) and the qualitative evaluation of the applicant institutions' investment philosophy, investment methodology,

investment structure, compliance system, etc.

In light of the purpose of the selection, the Association also conducts the evaluation as to whether or not the applicant institutions have achieved good investment performance over a period of time longer than the prescribed duration and the evaluation as to whether the proposed investment funds meet the needs and whether a good return can be expected based on comparison of investment methodologies and analysis of the risk profiles, levels and trends using long-term risk data concerning the portfolio (various factors).



■ Asset Manager Registration System

An Asset Manager Registration System, which started in July 2015 with respect to alternative investments, has also been introduced with respect to traditional assets. The

Association started accepting entries with respect to domestic bonds in 2016 and with respect to foreign equities in 2018.

■ Administration and evaluation of entrusted investment management institutions

The Association receives monthly reports on the investment status and quarterly reports on the overview of investment results, future investment policy and other matters from entrusted investment management institutions. In addition, the Association conducts a detailed

interview annually concerning the overview of investment results, future investment policy and other matters and also implements monitoring through visits to entrusted investment management institutions.

Furthermore, the Association annually conducts a comprehensive evaluation combining quantitative and qualitative evaluation by asset and by investment category (e.g., domestic equity market type and foreign equity growth type).

Qualitative evaluation is intended to evaluate the current and future status of the fulfilling of the expected role from a long-term perspective and to examine “whether the fund is expected to deliver a higher return than the target in a stable manner” and “whether the investment process which represents the advantage of the fund in earning an excess return has been sufficiently functioning in light of the market environment” and “whether the process will continue to function in the future.” The focus of attention in the analysis is on investment teams’ skills

(investment experience, staffing strength and stability of the employee turnover) and the effectiveness of the investment process (whether the process is functioning as proclaimed and presence or absence of reproductivity, reasonableness and flexibility).

Quantitative evaluation mainly assesses the actual excess return compared with the target excess return, the information ratio (the tracking error in the case of passive investment), and the cost performance (the excess return earned relative to fees).

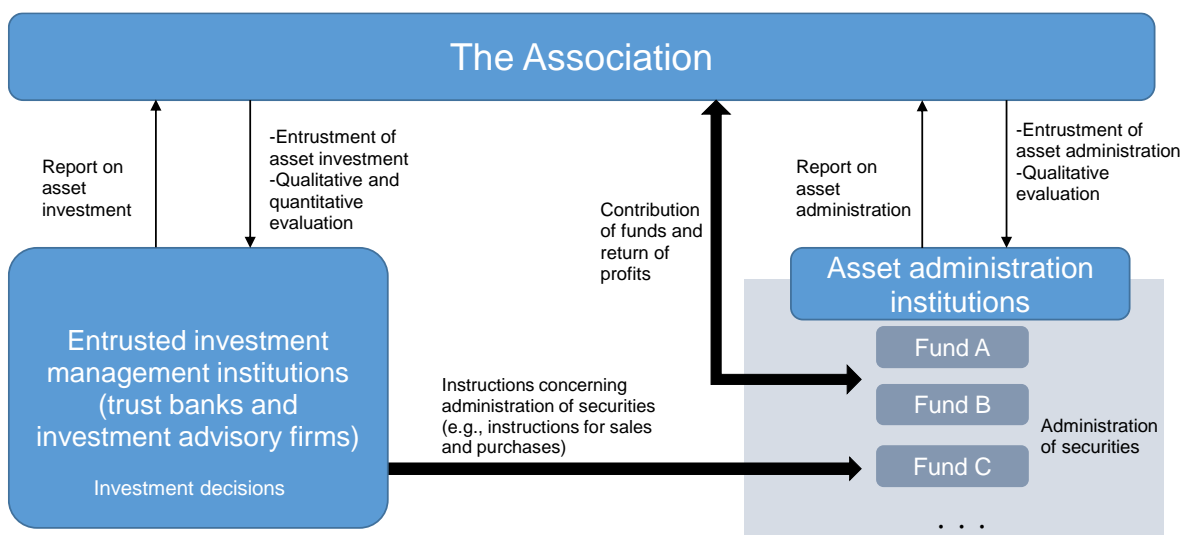
The Association allocates funds in a consistent manner across the entire portfolio in consideration of not only the results of comprehensive evaluation but also the balance of strategy categories in each asset class and the balance of funds in each category.

■ Administration and evaluation of asset administration institutions

The Association provides an incentive or gives a reminder for asset administration institutions as appropriate by providing feedback on the results of qualitative evaluation of their asset administration status and by

transferring funds from one institution to another depending on the results in order to ensure appropriate administration by asset administration institutions.

【Relationships with entrusted investment management institutions and asset administration institutions】

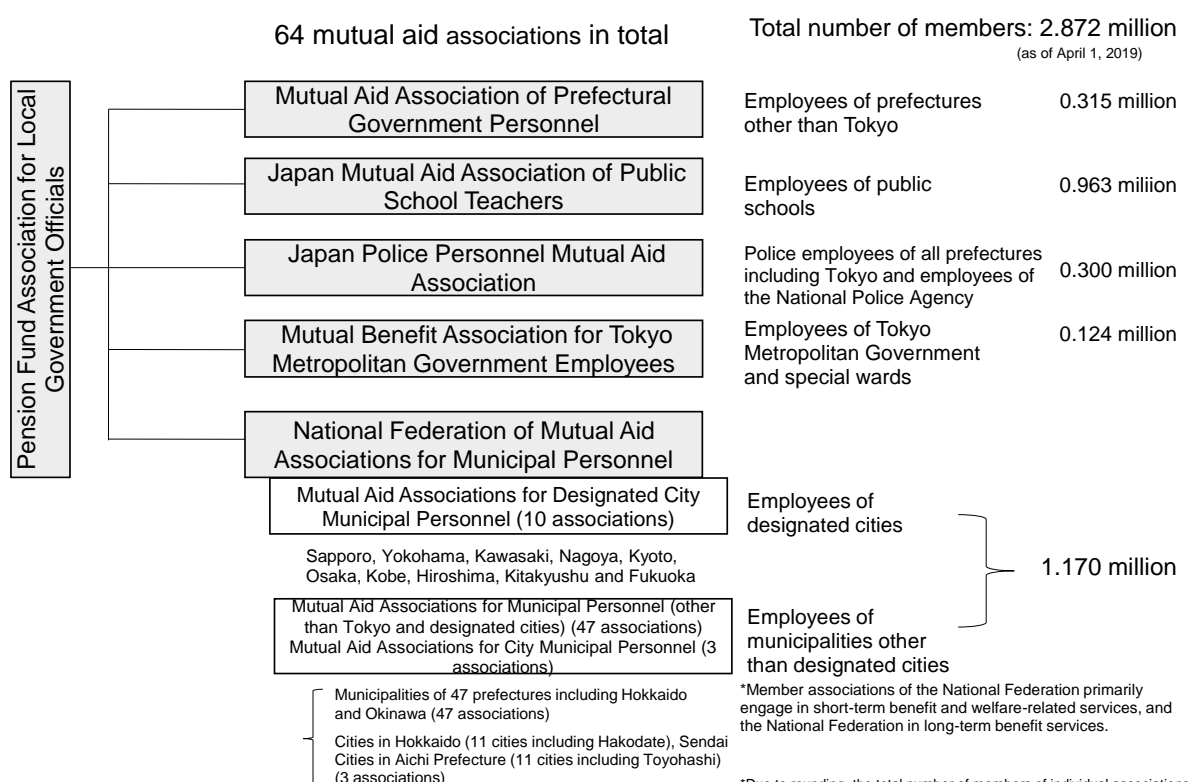


1 Establishment

Article 43 of the Local Public Service Act provides "A mutual aid system shall be implemented in order to provide appropriate benefits in cases of employees' illness, injury, childbirth, involuntary leave, calamity, retirement, disability or death, or their dependents' illness, injury, child birth, death or calamity." Based on this provision, the Local Public Officers, etc. Mutual Aid Association Act has been enacted.

The pension fund system for local government officials was established in December 1962 as a system to comprehensively manage the long-term benefits program, short-term benefits program and welfare services program for local government employees and their families, for the purpose of providing mutual aid for local government employees.

The Pension Fund Association for Local Government Officials was established on April 1, 1984, in order to stabilize the foundation of pension finance by integrating the pension funding units and to ensure appropriate and smooth management of operations related to long-term benefits of mutual aid associations so that sound management of the pension system can be maintained. The Japan Mutual Aid Association of Public School Teachers and the Japan Police Personnel Mutual Aid Association became members in April 1990, and the Association has become a federation comprising all local public service mutual aid associations (64 associations as of April 1, 2019) and the National Federation of Mutual Aid Associations for Municipal Personnel.



2 Major operations

The Association conducts the following operations in order to maintain sound management of pension systems related to local government officials.

- Administration and investment of funds
- Investment of surplus funds entrusted by mutual aid associations
- Provision of technical and professional knowledge and reference materials related to operations concerning long-term benefits of mutual aid associations
- Exchange of information and communication and coordination with the implementing organizations prescribed under the EPI Act
- Matters concerning contributions and grants related to employees' pension insurance. Payment of National Pension contributions.
- Calculation of the following items related to retirement and other pension benefits: the entitlement rate, the standard interest rate, the present value rates of lifetime pensions and fixed-term pensions, and the ratio of the standard monthly remuneration to premiums and the ratio of the standard term-end allowances, etc. to premiums
- Handling of matters related to payment to and receipt from the KKR of fiscal adjustment contributions
- Exchange of information related to special levies of nursing care insurance premiums, etc. from pension benefits
- Operations intended to achieve other objectives (e.g., administrative works related to the aggregation of pension coverage periods in Japan and other countries)

3 Organization

(1) Governing Council

Members of the Governing Council are appointed by the Minister of Internal Affairs and Communications from among association members. The Minister of Internal Affairs and Communications must appoint members from among individuals who possess broad knowledge concerning matters pertaining to the operations of the Local Public Service Mutual Aid Associations. In this case, half of all members must be representatives of members of individual mutual aid associations.

Revision of the articles of incorporation, the

formulation and revision of the rules of operations, annual business plans, budgets and account settlement, disposal of important assets and assumption of significant debt are subject to deliberation by the Governing Council.

Meanwhile, the Governing Council is empowered to investigate and deliberate important matters pertaining to the operations of the Association upon request from the President and to present proposals to the President with respect to the matters for which the need to do so is recognized.

(2) Fund Management Committee of Pension Fund Association for Local Government Officials

■Outline of Fund Management Committee of Pension Fund Association for Local Government Officials

To study expert matters pertaining to the administration and investment of funds based on the Basic Policy for Employees' Pension Insurance Benefit Adjustment Fund, the Association has established the Fund Management Committee of Pension Fund Association for Local Government Officials, which is comprised of individuals who possess academic knowledge or practical experience in

areas such as economics, finance, and fund management (the "Fund Management Committee").

The Fund Management Committee can express its opinions on important matters upon request from the President concerning expert matters related to the administration and investment of each fund.

■List of Fund Management Committee Members (As of April 2019)

Hidetaka Kawakita	Kyoto University, Professor Emeritus
Konosuke Kita	Russell Investments Japan Co., Ltd. Executive Consultant/Director, Consulting
Hisae Sato	Chief Investment Officer, NISSAN MOTOR, LTD.
Yoshiko Takayama	J-Eurus IR Co., Ltd. Managing Director
Hitoshi Takehara	Professor, Waseda Business School (Graduate School of Business and Finance)
Kazuyo Hachisuka	Executive Senior Vice President, Japan Economic Research Institute Inc.
Chairperson Takaaki Wakasugi	Executive Director, Michigan University-Mitsui Life Financial Research Center

■Matters for deliberation and report by the Fund Management Committee

Deliberation matters	Reporting matters
<ul style="list-style-type: none"> • Matters concerning formulation and revision of the basic policy • Matters concerning formulation and revision of risk management implementation policy • Matters concerning formulation and revision of investment policy for new investment instruments • Matters concerning formulation and revision of flexible investment policies • Matters concerning formulation and revision of the selection criteria for entrusted investment management institutions, etc. • Matters concerning the revision, etc. of the Corporate Governance Principles and the Guidelines for Exercising Shareholders' Voting Rights Matters • Other expert matters concerning the administration and investment of each adjustment fund 	<ul style="list-style-type: none"> • Investment performance • Status of risk management • Investment status of new investment instruments • Status of selections of entrusted investment management institutions, etc. • Status of stewardship activities • Status of training and nurturing of expert personnel • Other matters required by the committee concerning the administration and investment of each adjustment fund

■ Past Meetings of the Fund Management Committee

Meeting number	Meeting date	Main theme
27th Meeting	June 19, 2018	<ul style="list-style-type: none"> • Changes in the basic policy • Expansion of eligible investment instruments (addition of private debt and bank loans) and clarification of the treatment of strategy related to real estate and infrastructure investment • Revision of the manager structure concerning traditional assets • Review of Operations reports concerning administration and investment of individual funds in FY2017 • Status of risk management of individual funds in FY2017 • Examination of the benchmark portfolio of the Annuity Retirement Benefit Fund • Status of asset allocation in FY2018 (April-May)
28th Meeting	November 9, 2018	<ul style="list-style-type: none"> • Status of manager entries with respect to domestic bonds and foreign equities • Status of manager entries with respect to private debt and bank loans, and policy for selection of products • Status of asset allocation in FY2018 (April-October) • Status of investment of individual funds in the first and second quarters of FY2018 • Status of risk management of individual funds in the first and second quarters of FY2018 • Actuarial valuation concerning the Annuity Retirement Benefit Adjustment Fund
29th Meeting	February 25, 2019	<ul style="list-style-type: none"> • Study on the revision of the benchmark portfolio of the Annuity Retirement Benefit Adjustment Fund • Status of investment of individual funds in the third quarter of FY2018 • Status of risk management of individual funds in the third quarter of FY2018 • Status of asset allocation in FY2018 (April-January)
30th Meeting	March 20, 2019	<ul style="list-style-type: none"> • Examination of the benchmark portfolio of the Employees' Pension Insurance Benefit Adjustment Fund • Examination of the benchmark portfolio of the Transitional Long-term Benefit Adjustment Fund • Annual Stewardship Activity Report FY2018 • Revision of the Corporate Governance Principles and the Guidelines for Exercising Shareholders' Voting Rights • Investment policy for FY2019 • Status of investment in alternative assets

(3) Executives and Secretariat

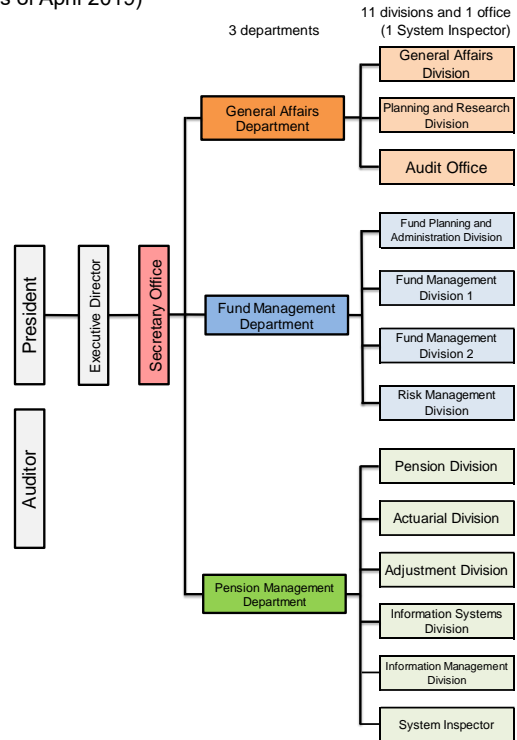
■ Executives

The Association is required to appoint the President, eight executive directors and three auditors. The President, two of the executive directors, and one of the auditors must serve on a full-time basis.

■ Secretariat

The Association's Secretariat is comprised of three departments, 11 divisions (there is also a system inspector outside the divisions), and one office, as is shown in the figure on the right. The prescribed number of employees at the Secretariat is 76.

(As of April 2019)



(4) Meetings

■ Asset Management Committee

The Association has established the Asset Management Committee, which is chaired by a full-time executive director responsible for fund management, in order to conduct preliminary deliberation when the President makes important decisions concerning the management of status of investment by the Local Public Service Mutual Aid Associations as well as the

management and investment of funds by the Association.

In principle, the Committee shall hold a regular weekly meeting and shall also meet as necessary. The chairperson shall promptly report to the President on the status of discussions at the Committee.

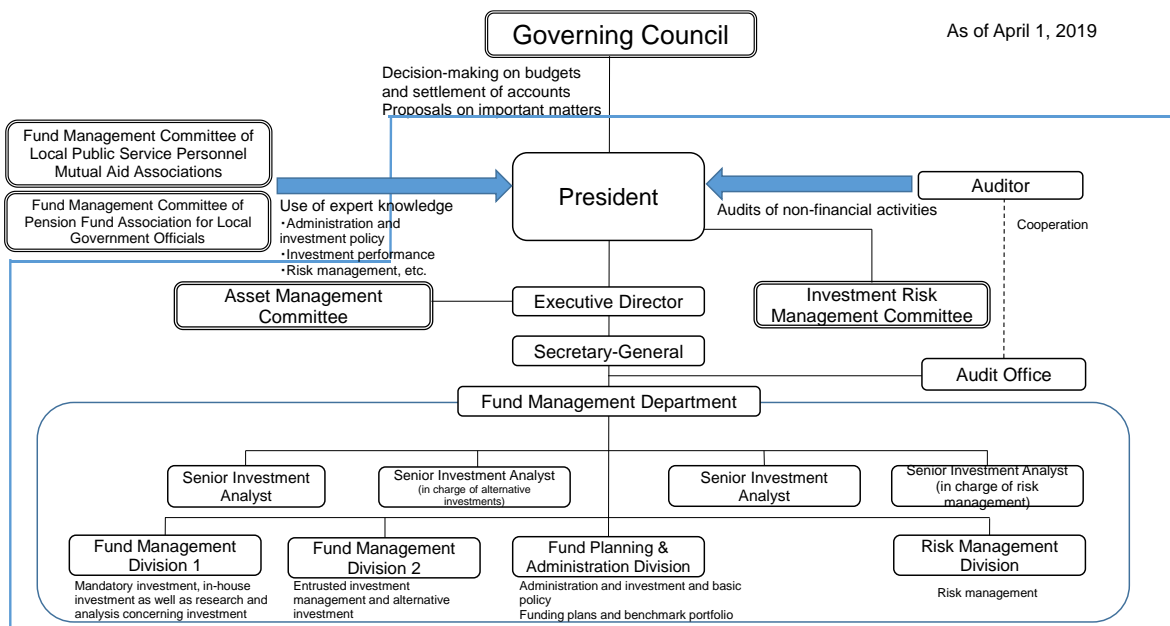
■ Investment Risk Management Committee

The Association has established the Investment Risk Management Committee, which is chaired by the President, in order to deliberate matters pertaining to the risk management of investment of funds so that the risk management can be appropriately conducted.

this committee is under the direct control of the President in order to ensure mutual checks and balances between the risk management side and the investment side. In principle, the Investment Risk Management Committee shall hold a regular quarterly meeting and shall also meet as necessary.

Unlike the Asset Management Committee,

(5) Governance structure



4 Investment of funds

(1) Mechanisms

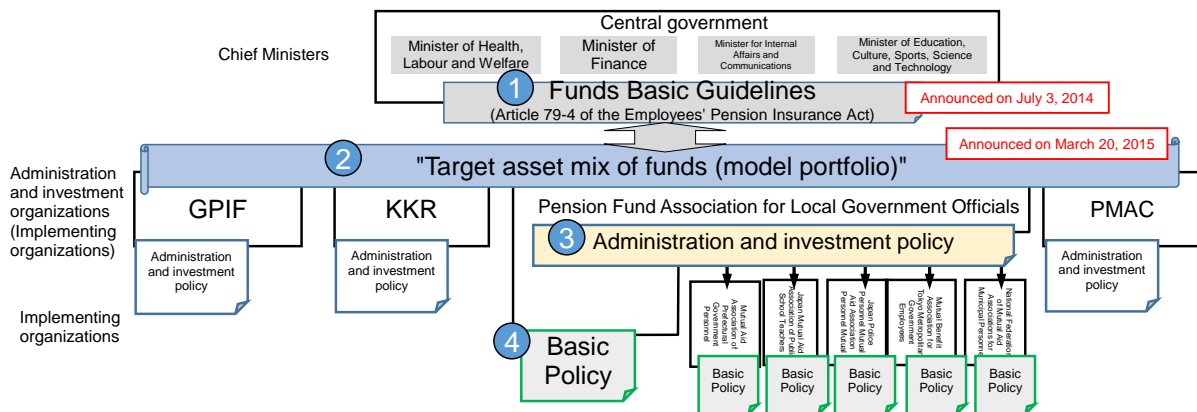
First, the chief ministers, namely the Minister of Health, Labour and Welfare, the Minister of Finance, the Minister for Internal Affairs and Communications, and the Minister of Education, Culture, Sports, Science and Technology, jointly formulate the Basic Guidelines for Ensuring Safe and Efficient Administration and Investment of Funds from a Long-Term Perspective (hereinafter referred to as the "Funds Basic Guidelines") as an overall framework. (①)

Next, the administration and investment

organizations (the GPIF, the KKR, the Association, and the PMAC) jointly formulate the target asset mix of funds (model portfolio) based on the Funds Basic Guidelines. (②)

The Association formulates the administration and investment policy subject to approval from the Minister of Internal Affairs and Communications (③) and individual implementing organizations formulate basic policies in accordance with the administration and investment policy. (④)

【Mechanism of fund investment after the integration】



(2) Basic approach to investment

■ Basic policy

Investment shall be made for the purpose of contributing to the stable management of the Employees' Pension Insurance operations into the future by investing safely and efficiently from a long-term perspective for the benefits of individuals covered by Employees' Pension Insurance.

In the management of funds, investments shall be made in a way that ensures appropriate diversification across multiple assets with

different risk/return profiles and other characteristics.

To ensure the required real return on investments of the funds (meaning the investment return less the nominal wage increase) at the minimum risk, a benchmark portfolio shall be established and appropriately managed and efforts shall be made to secure the benchmark return for each asset class, including over the long term.

