

# EXPLANATORY MEMO

## PHILIPPINE DOLLAR BOND INDEX FUND

The **PHILIPPINE DOLLAR BOND INDEX FUND** is a foreign currency long-term bond Unit Investment Trust Fund established under the authority of the Bangko Sentral ng Pilipinas ("BSP"). The following is a summary of the Fund's Plan Rules and Regulations ("Plan Rules") and the terms and conditions governing the investments in the Fund:

### 1 Trustee

Bank of the Philippine Islands through the Asset Management and Trust Group

### 2 Fund Features

Name of the Fund:	<b>Philippine Dollar Bond Index Fund</b>
Fund Classification:	Long-term Bond Fund
Base Currency:	U.S. Dollar
Launch Date:	December 31, 2006
Minimum Investment Amount:	USD 500
Minimum Transaction Amount:	USD 200
Trust Fee	0.25% p.a.
Dealing	Daily up to 12:00 PM
Custodian Bank	HSBC
External Auditor	Isla Lipana & Co

### 3 Investment policy

#### 3.1. Investment Objective

The Fund intends to achieve for its investment returns that closely track the total return of a US Dollar-denominated index, the JPMorgan Asia Credit Index – Philippines, before fees and taxes, by investing in Philippine sovereign and corporate credits.

#### 3.2. Allowable Investments

Philippine Dollar Bond Index Fund may invest in the following:

- Primarily long term tradable fixed-income instruments issued or guaranteed by the Philippine government or the BSP; tradable fixed-income instruments issued by financial institutions or private corporations; exchange-listed securities; marketable instruments that are traded in an organized exchange; loans traded in an organized market; and, such other tradable investment outlets/ categories as the BSP may allow.
- Tradable fixed-income securities issued, underwritten, or otherwise dealt by BPI and/or any of its subsidiaries, affiliates, their successors-in-interest or assignees, their directors, officers, stockholders, and related interest, and any of their trust and fund managed accounts, under such terms and conditions as the Trustee may deem to be in the best interest of the Fund
- Collective investment vehicles managed by reputable fund managers the investment objectives and policies of which are generally consistent with those of the Fund, subject to then existing BSP regulations.
- The principal investments of the Fund will be in fixed-income instruments denominated in, but are not limited to, the following major currencies: U.S. Dollar, Euro, British Pound, Canadian Dollar, Australian Dollar, Swiss Franc, Danish Kroner, and Japanese Yen.
- Bank deposits and such other investments allowed under regulations issued by the BSP.

3.2 For all transactions with related parties or entities, the Trustee of the Fund shall be transparent at all times and maintain an audit trail. The Trustee shall observe the principle of best execution and no purchase/sale shall be made with related counterparties without considering at least two (2) competitive quotes from other sources

3.3 The exposure to a single issue shall not exceed fifteen percent (15%) of the market value of the Fund, provided, that this limitation shall not apply to securities issued or guaranteed by investment grade sovereigns or supranationals, as well as non-risk assets as defined by the BSP.

3.4. A list of existing and prospective investments outlets which shall be updated quarterly shall be made available to all Participants. Upon request, a copy of such list shall be furnished such interested Participant/s.

### 4. Disclosure on Profiling process

The objective of a Client Suitability Assessment (CSA) is to profile the risk-return orientation of the investor and the result is used as basis to recommend various classes of UITFs. The CSA shall be subject to review every three (3) years. Should there be any change in the investor/s' personal/financial circumstances or preferences prior to three years, he/she should immediately request the UITF Marketing person for a new profiling process and changes be made immediately to the investment in UITF, as applicable.

### 5. Qualified Participants

Participation in the Fund shall be open to all persons with legal capacity to enter into contracts. Acceptance of Participants shall be subject to the rules or procedures established by the Trustee which it deems advantageous or to the best interest of the Fund. The Fund is suitable for investors with a moderately conservative risk profile and those with short-term liquidity requirements.

### 6. Subscription and Redemption of Units of Participation

Participation shall always be through participation units and each unit shall have uniform rights or privileges as any other unit. Admission or redemption of units of participation in the Fund, including fractions thereof, shall be based on the applicable NAVPU for the day. The NAVPU shall be based on the prevailing market value of underlying investments at any relevant time. Admission and/or notice of redemption received by the Trustee on or before the cut-off time shall be considered as transaction for the day. However, admission/notice of redemption received after the cut-off time shall be considered as transaction for the next applicable banking day. Upon initial participation, the Participating Trust Agreement shall be made available to the Participant. A Confirmation of Participation or Transaction Advice shall be provided to the Participant for subsequent transactions.

### 7. Settlement of Contributions and Redemption

Contributions and redemptions received on or before the cut-off time are settled at the end of the trading day.

### 8. Suspension of Subscriptions and Redemptions

BPI Asset Management may temporarily suspend calculation of the NAV/NAVPU of the Fund, as well as admission to and redemption from the Fund, if it is unable to determine the NAVPU of the Fund due to any fortuitous event, such as fire, natural calamity, public disorder, or national emergency affecting the financial

The Participation in the Fund is a trust product, NOT a bank deposit or an obligation of, or guaranteed, nor issued, nor insured by the Bank of the Philippine Islands or its affiliates or subsidiaries and therefore are not insured or governed by the Philippine Deposit Insurance Corporation (PDIC). Any income and loss arising from market fluctuations and price volatility of the securities held by the fund, even if invested in government securities, is for the account of the investor. As such the fund is not capital protected and may not be suitable for clients seeking preservation of capital. Historical performance when presented is purely for reference purposes and not a guarantee of similar future results.

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market resulting in the suspension of trading and consequently, the absence of available market prices of securities/instruments.

### 9. Allocation and Distribution of Income

Participants shall be entitled to income, profits and losses with respect to its participation in the Fund on a pro rata and pari passu basis depending upon the number of units held by each Participant. The actual distribution or realization of income shall take place every time a redemption of units is made, to the extent of the number of units redeemed.

### 10. Valuation

The NAV shall be the summation of the market value of each investment of the Fund, less taxes, fees, and other qualified expenses as defined herein. The determination of the market value of the investments of the Fund shall be in accordance with existing BSP rules and regulations on marking to market valuation of investment instruments.

### 11. Amendments

The Plan Rules of the Fund may be amended from time to time by the resolution of the Trust Committee, which authority was delegated by the Board of the Directors of the Bank of the Philippine Islands. Participants shall be immediately notified of such amendments and those who are not in conformity with the amendments made shall be allowed to withdraw their participations within 30 calendar days after the amendments are approved or such longer period as may be fixed by BPI Asset Management.

### 12. Trust Fee, other expenses and Taxes

In consideration of BPI Asset Management's services, trust fees shall be collected from the Fund in the amount indicated in the Fund Features which shall be accrued daily and shall be payable monthly in arrears.

BPI Asset Management may charge special expenses if the same are necessary to preserve or enhance the value of the Fund. Such special expenses shall be payable to the pertinent third party/ies covered by separate contract/s, and disclosed to participants.

### 13. Annual External Audit

An external audit of the Fund shall be conducted annually after the close of each fiscal year by an independent auditor acceptable to BSP. A notice shall be sent to the Participants that the report is available, and upon request, a copy of such report shall be furnished such Participant/s, without charge.

### 14. Termination

The Fund may be terminated by resolution of the Board of Directors of the Bank of the Philippine Islands. Following the approval of the termination of the Fund but at least 30 business days prior to the actual termination, BPI Asset Management shall provide notice of the termination to the remaining participants.

### 15. Risk disclosure

Below are the relevant risks that the Fund may be subject to. Some or all of these risks may adversely affect the Fund's NAVPU, return on investment, and/or its ability to meet its investment objectives:

- 15.1 Market Risk - the risk that movement in the financial markets will adversely affect the investments of the Fund. The markets will fluctuate based on many factors, such as the state of the economy, current events, corporate earnings, interest rate movements.
- 15.2 Interest Rate Risk -the risk that the value of the portfolio will decline as interest rates rise. Bond prices are inversely related to interest rates. As interest rates increase, bond prices decrease.
- 15.3 Liquidity Risk - the risk that the investments of the Fund cannot be sold or converted into cash within a reasonable time or in instances where sale or conversion is possible but not at a fair price.
- 15.4 Credit Risk - the risk that the bond issuer may not be able to pay its debt upon interest payments and maturity
- 15.5 Inflation Risk - the risk the return of your investments will not keep pace with the increase in consumer prices.
- 15.6 Currency Risk - the risk that fluctuations in the exchange rate between the US dollar and a foreign currency may decrease the value the Fund's investments.
- 15.7 Tracking Error Risk- Risk that returns may deviate from the index due to fees, expenses, liquidity of the market and changes in the index and regulatory policies.
- 15.8 Concentration of the index in certain issues-The Fund's investments maybe concentrated in securities of a single or several issuers as a result of tracking the index.
- 15.9 Changes in the composition of the index- An investor's investment will generally reflect the index as its constituents change and not necessarily the way it is comprised at the time of actual investment.

### 16. Risk Management and Hedging Policy

For the general and collective interest of the Fund's Participants, the Trustee is authorized to adopt an external or internal risk management and hedging strategy and a more definitive policy guideline based on generally accepted risk management principles, and duly approved by the Trust Committee.

The Fund may avail itself of instruments solely for the purpose of hedging risk exposures of the existing investments of the Fund, provided, that, these are accounted for in accordance with existing BSP guidelines, as well as the Trustee's risk management and hedging policies duly approved by the Trust Committee, and disclosed to the Participants. The Fund may use financial derivatives to hedge the portfolio against market and credit risk. The volatility of the Fund's investments is managed using the principles of Value-at-Risk (VAR). VAR is a measure of the portfolio's maximum potential loss.

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