NAFA
NBP Fullerton Asset Management Limited
(Formerly National Fullerton Asset Management Limited)

Managing Employees' Funds / Endowments

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Trustees carry a fiduciary responsibility of managing employees' funds and endowments, as their decisions impact a large number of people. Traditionally such money in Pakistan has been invested in banks and national savings schemes. However, with the present inflation rate hovering around 15%, and bank deposits and savings schemes offering less than the inflation rate, the real return on such investments is negative. The Pakistani stock market has historically (last 30 years) provided a return of about 18% per year, but it is also very volatile over shorter time periods.

Our advice to the Trustees of Employee Funds / Endowments is to diversify their investments among the four major asset classes: Money Markets (bank deposits and Treasury bills), Fixed Income (TFCs and PIBs), Capital Protected strategies and the Stock Market. The allocation among these asset classes will depend upon the target return and risk appetite of the beneficiaries. If the Target Return is 12%-13%, then this can be achieved by simply investing in bank deposits and Treasury Bills. However, if the Target return is say 15% then some exposure to at least capital protected strategies will be required.

It is important that the performance of each asset class be compared against the relevant benchmark so that one is not comparing apples with oranges. A suitable benchmark for Money Market is the 3-month Treasury Bills rate, which is presently around 12.87% p.a.. For Fixed Income and Capital Protected strategy, 6-month KIBOR is an appropriate benchmark, which is presently around 13.6% p.a. For equities the relevant benchmark is the KSE-100 Index. If the Asset Manager beats the respective benchmark, he or she has done the job well, and vice versa.

The objective of the Capital Protected Strategy is to earn a higher return than bank deposits. This strategy allows the investor to benefit from the growth of the stock market, while protecting the capital of the investor. NAFA has back-tested this strategy over the last 15 years based on investments in Pakistan's capital markets. The Strategy has provided a return of 19% per annum, which is even better than the stock market with a much lower volatility than that of the stock market. NAFA is presently managing several portfolios based on this strategy.

Investing in bank deposits and Treasury Bills can be done in-house by the Trustees of Employees' Funds / Endowments. However, managing Fixed Income, Capital Protected Strategies and Equities require extensive time and a special expertise that may not be available in-house. Therefore, it is advisable to out-source such investments to Asset Managers. Again, there are two ways of doing so. First, employees' funds can be invested in mutual funds managed by various asset management companies. Second, an Asset Management Company can manage a special portfolio for the employees' funds based on specific guidelines agreed with the Trustees.

Asset Managers should be chosen by the Trustees based on the Sponsor's reputation, quality of management, performance of funds, and rating of the Asset Manager. It is very important that the Trustees diversify their investments among 4-5 Asset Managers in order to reduce their risk. Different Asset Managers use different investment strategies. An investment strategy may be very successful in a certain period and may not be in another period. Thus, an Asset Manager may perform very well in one year, and poorly the next year. Investing is all about timing – the proper time to buy an investment and the proper time to sell. The timing can be good in one instance and poor in another. Therefore, using several asset managers can help reduce this timing risk.