



ANNUAL REPORT

The Management Committee of Punjab Pension Fund (PPF) is pleased to present to Government of the Punjab the Annual Report for the year ended 30 June 2014.

FUND SIZE

- A summary of changes in fund size during FY 2013-14 is given in the following table:

Rs. millions (rounded to the nearest million)

	Jul 2013 - Jun 2014
Beginning fund size (30 th June 2013)	17,585
Add: contribution during the period	4,800
Add: earnings during the period	2,198
Less: expenses during the period	(28)
Ending fund size	24,555

The above numbers exclude unrealized capital gains. Market value of Fund's assets at 30th June 2014 is Rs. 24,750 million. Hence the Fund is carrying unrealized capital gain of Rs. 195 million at 30th June 2014.

FUND'S PORTFOLIO

- The Fund's exposures to different investment types are summarized as under:

Amounts: Rs. millions (rounded to the nearest million)

#: as percentage of Total Fund Size

	30 June 2012		30 June 2013		30 June 2014	
	Amount	%	Amount	%	Amount	%
Pakistan Investment Bonds	9,068	58.1	9,145	52.0	16,084	65.5
Corporate bonds/TFCs	489	3.1	237	1.3	593	2.4
Medium-term bank deposits	-	-	-	-	1,000	4.1
Special Savings Account	-	-	1,800	10.2	1,000	4.1
Short-term bank deposits	5,339	34.2	5,800	33.0	4,300	17.5
Treasury Bills (T-Bills)	139	1.0	-	-	493	2.0
Cash at bank	130	0.8	11	0.1	206	0.8
Accrued Markup	434	2.8	583	3.3	867	3.5
Other assets*	6	0.0	9	0.1	12	0.1
Total Fund Size	15,605	100.0	17,585	100.0	24,555	100.0

*Other assets include prepaid operating expenses and book value of fixed assets of PPF.

- Long-term investments consist of Pakistan Investment Bonds (PIBs) and Term Finance Certificates (TFCs), medium-term investments consist of medium-term bank deposits and Special Savings Account and short-term investments consist of short-term bank deposits and Treasury Bills.
- PPF keeps switching exposure between T-Bills and short-term bank placements in pursuit of higher rates of return.



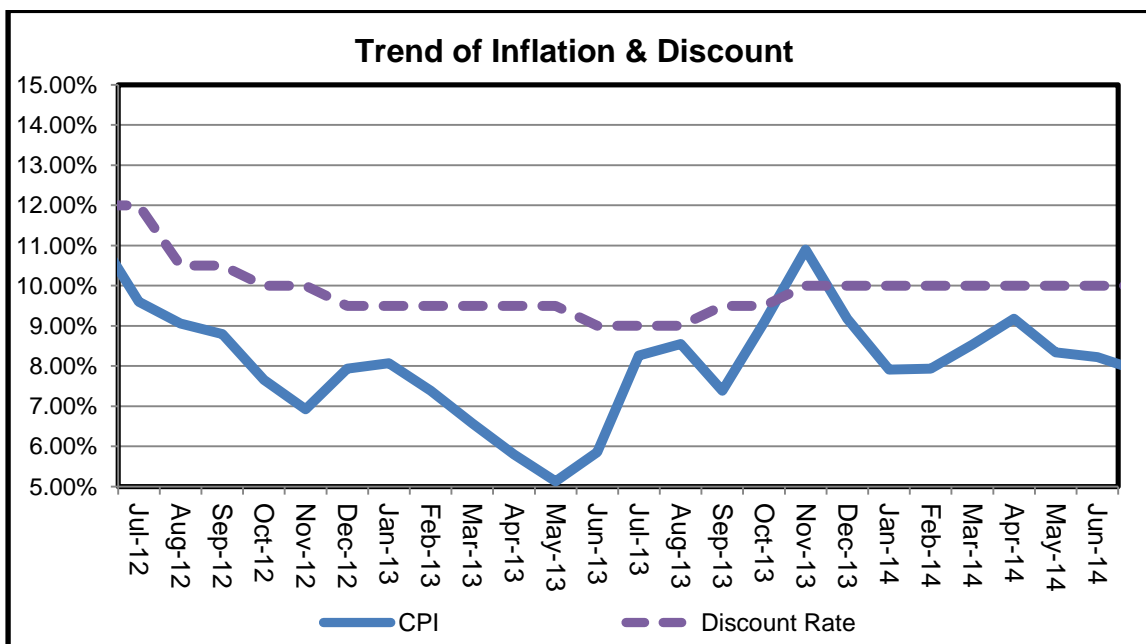
FUND'S PERFORMANCE

- Time Weighted Return (TWR) earned by PPF is summarized as under:

Period	Annualized Return for the period		Year End Discount Rate	YoY CPI Inflation	Long-term Benchmark CPI Inflation + 3%
	Gross Return	Net Return*			
FY 2008-09	15.21%	15.00%	14.00%	13.14%	16.14%
FY 2009-10	13.79%	13.61%	12.50%	12.69%	15.69%
FY 2010-11	13.48%	13.32%	14.00%	13.13%	16.13%
FY 2011-12	13.96%	13.79%	12.00%	11.26%	14.26%
FY 2012-13	12.85%	12.69%	9.00%	5.85%	8.85%
FY 2013-14	12.05%	11.90%	10.00%	8.22%	11.22%
Jul 2008 - Jun 2014 (CAGR)**	13.55%	13.37%	11.90%	10.68%	13.68%

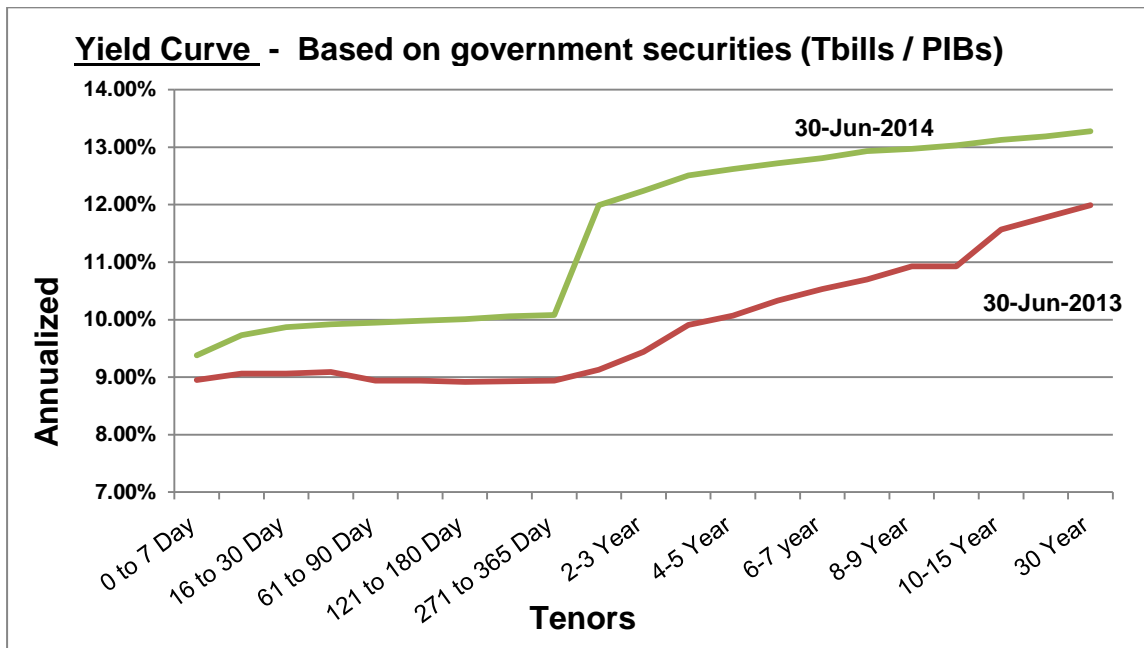
*Net Return means the return after deducting expenses incurred on management of Punjab Pension Fund.
**CAGR means Compound Annualized Growth Rate.

- In order to lock-in higher yields for longer period of time, the Fund has invested a large proportion of its assets in long-term fixed-rate instruments consisting mainly of PIBs. The Fund's exposure to long-term PIBs stands at 65.5% of Fund size at the end of June 2014.
- In FY14, CPI Inflation rate remained under control and closed at a single digit figure. The following graph depicts movement in CPI inflation and changes in discount rate over last two years:





- The investment strategy followed over the past few years i.e. investment in long-term fixed-rate instruments at attractive yields, has paid off. Despite lower inflation and short term interest rates, the Fund continues to earn an attractive rate of return because of its high yielding portfolio of PIBs.
- During FY14, SBP increased its discount rate by 1%; as a result overall yield curve shifted upward. By the end of the year, inflationary pressure eased significantly but continuous demand for borrowing from the Federal Government kept the longer term yields on higher side. The following graph depicts the shift in yield curve during FY14.



GROWTH IN ASSETS vs. LIABILITIES AND FUNDING RATIO

- As per the last Actuarial Assessment Report, the present value of pension liabilities of the Government of the Punjab at 30 June 2010 stood at Rs. 688 billion. Although, a fresh Actuarial Valuation will provide a more reliable figure, a conservative estimate of the present value of the pension liabilities at 30 June 2014 is Rs. 992 billion.
- The market value of PPF assets at 30 June 2014 stood at Rs. 24.8 billion. This translates into a Funding Ratio (Assets / Liabilities) of 2.50%.
- If PPF were envisaged as a fully funded pension plan, the value of its assets would match the value of the total pension liability of the Government of the Punjab, and the Funding Ratio would equal 100%. This would mean that for the accrued pension liabilities, the Government of the Punjab would not have to earmark any budgetary resources because these would be met by PPF from the return on its assets.
- Currently the Government of the Punjab does not have an explicit target for the Funding Ratio. The desired Funding Ratio can be inferred from the projected injections of funds in PPF by the Government as stated in the White Paper to the Budget announced by the Government of the Punjab for the



FY2014-15. If the injections of funds stay on course and there are no withdrawals then with 12% average rate of return on PPF funds, the projected funding ratio in 2019 will be 4.75%. During FY14 the Government made a fresh contribution of Rs. 4.8 billion into the Fund.

- In order to properly manage a pension plan, two things are important.
 - Firstly, the Funding Ratio of the pension plan should be high so that sufficient assets vis-à-vis the liabilities are available. A Funding Ratio of 100% or more is ideal.
 - Currently, the Funding Ratio of the pension plan is 2.5% which means that the current level of assets is sufficient to meet only 2.5% of accrued pension liabilities of the Government of the Punjab.
 - This Funding Ratio is clearly quite low and the government may consider increasing this ratio. To make PPF fully funded would need an asset base of about Rs 992 billion at 30 June 2014. To achieve this magnitude of asset base, a long-term and sustainable plan of gradual injection of funds into the pension plan is required.
 - Secondly, the Fund should preferably make long-term fixed-rate investments whose maturity is as close as possible to the maturity of pension liabilities. With fixed-rate investments the rate of return on the assets of the Fund will be less vulnerable to the fluctuations in the market rate of interest.
 - Considering the importance of long-term fixed-rate investments, PPF has invested more than 65% of its assets in long-term fixed-rate bonds and remains ready to invest further as opportunities to invest long-term at attractive fixed rates arise.

OUTLOOK FOR FY 2014-15

Inflation:

FY15 started with an inflation rate on lower side and CPI declined to historical low of 3.78% on YoY basis during the month of January FY15. Inflation has decelerated due to the sharp decline in global oil prices, global economic slowdown (except US) and soft outlook on commodity prices. Given the reduction in domestic oil prices and its second round impact, such as on transport services, inflation is likely to decrease further going forward. In its latest Monetary Policy announced on 24 January 2015, SBP has revised downwards its forecast range for average CPI inflation to 4.5-5.5 % for FY15, well below the annual target of 8 percent.

Interest rates:

In the last Monetary Policy Statement, announced on 24th January 2015, State Bank of Pakistan (SBP) lowered its policy rate by 100 basis points to 8.5% from 9.5%. The decision of lowering discount rate was justified by SBP on the basis of following:

- i. More than expected slowdown in CPI inflation which stood at 4.3% at Dec-14 end against target of 8.0%; SPB projects average CPI at 4.5 - 5.5% for FY15.
- ii. Improved economic outlook due to expected revival of private sector credit.



- iii. Upward trajectory in Foreign Exchange Reserves as a result of successful completion of fourth and fifth review under IMF's EFF, and issuance of International Sukuks.
- iv. Improved outlook on external balances, especially given the 60% reduction in international oil prices.

As far as remaining part of FY15 is concerned, we expect that there is no serious threat of reversal of inflation. Further, the Balance of Payment situation also seems manageable and SBP reserves are expected to increase further with IMF program on track and expected proceeds from privatization and official flows. We expect that SBP can further reduce its policy rate in the remaining part of FY15.

INVESTMENT STRATEGY

- Since December 2013, the Fund's view on inflation & interest rates changed and it started investing in longer term PIBs. As the inflation remained relatively on lower side, the strategy paid off and higher allocation of PIBs in overall portfolio helped the Fund to post a return higher than its benchmark.
- In September 2014, Yield of PIBs started declining and since then average PIB yields on different tenors have come down by 300-400 basis points. PPF sold out more than 50% of its PIB portfolio, realized the capital gain of Rs. 827 million and switched the exposure into National Saving Schemes in order to hedge the Fund against any further decline in interest rates. Going forward, despite sharp decline in market yields, PPF's portfolio is well in a position to post a decent margin over CPI.

AUDITORS

Government of the Punjab appointed M/S KPMG Taseer Hadi & Co., Chartered Accountants, as auditors of the Fund. The auditors have completed the audit for the year ended 30 June 2014 and have submitted their report to the Management Committee.

TRUSTEE

The Management Committee has appointed M/s Central Depository Company of Pakistan Limited as Trustee of the Fund under Rule 18 of the Punjab Pension Fund Rules 2007. After signing of the Trust Deed custody of all the assets of the Fund rests with the Trustee.

The Trustee in its report has opined that Punjab Pension Fund has in all material respect managed the Trust during the year ended June 30, 2014 in accordance with its Trust Deed and the Governing Laws.

ACKNOWLEDEMENT

The Management Committee takes this opportunity to thank its members for valuable contributions to the Fund.



**Government of the Punjab
Punjab Pension Fund**



The Management Committee also wishes to place on record its appreciation for the hard work and dedication shown by the employees of the Fund.

Place: Lahore

Dated: 03-04-2015

(Mujtaba Shuja-ur-Rahman)
Finance Minister/Chairman,
Punjab Pension Fund