ANNUAL REPORT

The Management Committee of Punjab Pension Fund is pleased to present to Government of the Punjab the Annual Report for the year ended 30 June 2013.

FUND SIZE

- A summary of changes in fund size during FY 2012-13 is given in the following table:

Rs. millions (rounded to the nearest million)

	Jul 2012- Jun 2013
Beginning fund size (30th June 2012)	15,605
Add: contribution during the period	-
Less: transfer to Reserve Pension Fund	-
Add: gain/(loss) during the period	2,004
Less: expenses during the period	(24)
Ending fund size	**17,585**

The above numbers exclude unrealized capital gains. Market value of Fund's assets at 30th June 2013 is Rs. 18,822 million. Hence the Fund is carrying unrealized capital gain of Rs. 1,237 million at 30th June 2013.

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 2011		30 June 2012		30 June 2013	
	Amount	%	Amount	%	Amount	%
Pakistan Investment Bonds (PIBs)	8,942	65.2	9,480	60.7	9,560	54.3
Treasury Bills (T-Bills)	1,254	9.1	139	1.0	-	-
Short term bank deposits	3,002	21.9	5,349	34.3	5,928	33.7
National Saving Schemes	-	-	-	-	1,831	10.4
Corporate bonds/Term Finance Certificates (TFCs)	501	3.7	501	3.2	246	1.4
Cash at bank	8	0.1	130	0.8	11	0.1
Other assets*	1	0.0	6	0.0	9	0.1
Total Fund Size	**13,708**	**100.0**	**15,605**	**100.0**	**17,585**	**100.0**

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

- Long-term investments consist of PIBs and TFCs whereas short-term investments consist of T-Bills, National Saving Schemes and bank deposits.

- PPF keeps switching exposure between T-Bills, National Saving Schemes& short-term bank placements in pursuit of higher rates of return.

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FUND'S PERFORMANCE

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

Period	Annualized Return for the period				Long-term Benchmark
	Gross Return	Net Return*	Year End Discount Rate	YoY CPI Inflation	CPI Inflation + 3%
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%
Jul 2008 - Jun 2013 (CAGR)**	13.85%	13.67%	12.14%	11.17%	14.17%

*Net Return means the return after deducting expenses incurred on management of PPF
**CAGR means Compound Annualized Growth Rate

- Inflation rates over the last few years (FY09 to FY12) have beenmuch higher than our long-term inflation expectations of 9%-10% p.a. Interest rates have also been higher than our long-term expectations.

- 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 54.3% of Fund size at the end of June 2013.

- In FY13, CPI Inflation rate has declined sharply and SBP has reduced the policy rate by 3.0% cumulatively (from 12% to 9%). The following graph depicts movement in CPI inflation and changes in discount rate over last two years:

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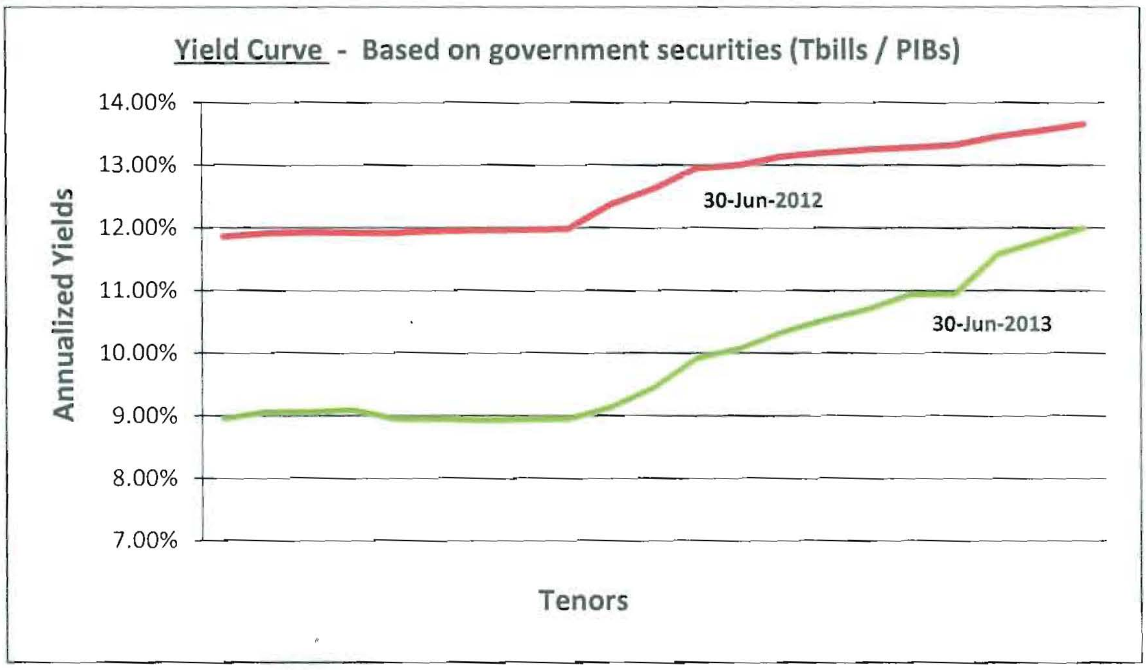
- The investment strategy followed over the past few years i.e. investment in long-term fixed-rate instruments at attractive yields, is now paying off. Despite lower interest rates, the Fund continues to earn an attractive rate of return because of its high yielding portfolio of PIBs.

- The yield curve graph shows the sharp decline in both short & long term interest rates; as a result of 3% cut in discount rate by SBP over the last fiscal year. However, the return of PPF declined by 1.1% in FY13 compared with FY12 which reflects that the strategy of PPF worked in this declining interest rate scenario, and the Fund is able to earn an attractive spread of 6.84%over inflation.



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 provided a more reliable figure, a conservative estimate of the present value of the pension liabilities at 30 June 2013 is Rs. 1,052 billion.

- The market value of PPF assets at 30 June 2013 stood at Rs. 18.8 billion. This translates into a Funding Ratio (Assets / Liabilities) of 1.79%.

- 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 Medium Term Budgetary Framework 2013-15 announced by Government of the Punjab. If the injections of funds stay on course and there are no withdrawals then at the current average rate of return on PPF funds, the projected funding ratio in 2016 will be 2.0%. Thereafter, this ratio is expected to stay in the range of 1.75%-2.25%.However, during FY13the Government made no contribution 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% is ideal.
    - Currently, the Funding Ratio of the pension plan is less than 2% which means that the current level of assets is sufficient to meet less than 2% 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 1052 billion at 30 June 2013. To achieve this magnitude of asset base would require a long-term and sustainable plan of gradual injection of funds into the pension plan.
  - 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 50% 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.

INFLATION

- A summary of a few important measures of inflation during FY 2012-13 is given below:

	YOY Inflation (%)				
	CPI			NFNE[1]	Trimmed[2]
	overall	Food	non-food		
June 2012	11.3	10.3	12.0	11.5	11.1
June 2013	5.8	7.9	4.4	7.8	6.8
12m high	9.6	9.1	10.0	11.3	10.7
12m low	5.1	5.3	4.1	7.8	6.7
12mma[3]	7.4	7.1	7.5	9.6	9.0

[1]NFNE stands for non-food non-energy measure of core inflation
[2]Trimmed Mean measure of core inflation excludes 20% of the items in the CPI basket (10% items showing highest increases in price& 10% items showing lowest increases or negative changes in price)
[3]Twelve month moving average

Source: SBP

- Headline CPI inflation as well as both the measures of core inflation closed the year on lower side. CPI, NFNE and Trimmed Mean inflation all three were lower in June 2013 as compared with June 2012.

INTEREST RATES

- A summary of important interest rates for FY 2012-13 is given below:

	Yields (% p.a.)		
	1-yr T-bill	10-yr PIB	6-m KIBOR
June 2012	11.97	13.31	12.06
June 2013	8.94	10.93	9.09
12m high	11.87	13.06	11.99
12m low	8.94	10.80	9.09
12mma	9.69	11.62	9.82

Source: SBP, Reuters

- SBP reduced the discount rate by 3% from 12% to 9% during the year. The difference between 12-month high and end-of-June rates shows that reduction in discount rate impacted both short-term & long term rates.

OUTLOOK FOR FY 2013-14

Inflation:

- The Government has set inflation target at 8.0% for FY 2013-14. The achievement of the target will be determined by developments on both external as well as on internal front. On external side oil prices & exchange rate will be key determinants, while on domestic side fiscal reforms and crop outlook of key food items will be vital in deciding inflation trend.

- There has been some acceleration in inflation during July and August 2013 as CPI stood at 8.26% and 8.55% respectively during July and August 2013. Due to rising trend in international oil prices and increase in electricity & gas tariff by the Government, there is a risk that annual inflation for FY 2013-14 may close in double digit and surpass the annual target set by the Government.

Interest rates:

- SBP has lowered discount rate by 3% from 12% to 9% during FY13. SBP justified its decision on the basis of lower inflation and the need to revive private sector credit and investment.

- During FY 2013-14 interest rates looks upward as the underlying fundamentals of the economy, including rising inflation, high fiscal deficit, power shortages, rising international oil prices, fragile external account position & exchange rate, suggest that inflation and interest rates may rise.

INVESTMENT STRATEGY

- During the past few years, inflation as well as interest rateshave been quite high.In order to take advantage of high interest rates, Fund's strategy has been mainly to invest at fixed rates of return for longer periods.

- Considering the continuing economic uncertainties, the current strategy is to invest the liquid funds in short-term fixed income instruments and wait for the right opportunity to invest long-term at higher rates.

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 2013 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 are held by 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, 2013 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.

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

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

Place: Lahore
Dated: 27 November 2013

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