



Government of the Punjab  
Punjab Pension Fund



Dated: 20 March 2010

MONTHLY REVIEW OF INVESTMENTS

February 2010

FUND SIZE

- A summary of changes in fund size during the current accounting year i.e. 2009-10 is given in the following table:

Rs. millions (rounded to the nearest million)

	Jul 2009 - Feb 2010
Beginning fund size	3,480
Add: contribution during the period	9,000
Less: transfer to Reserve Pension Fund	1,000
Add: gain/(loss) during the period	926
Less: expenses during the period	10
<b>Ending fund size</b>	<b>12,396</b>

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 Sep 2009		31 Dec 2009		28 Feb 2010	
	Amount	%	Amount	%	Amount	%
PIBs	0	0	4,115	33.9	4,458	36.0
T-Bills	0	0	0	0	3,538	28.5
Short term bank deposits	12,670	99.3	7,814	64.3	4,058	32.7
Accrued interest	41	0.3	202	1.7	306	2.5
Cash at bank	49	0.4	22	0.2	27	0.2
Other assets*	(1)	0	2	0	9	0.1
<b>Total Fund Size</b>	<b>12,759</b>		<b>12,155</b>		<b>12,396</b>	

\*Other assets include prepaid expenses for management of PPF and book value of fixed assets (vehicles, computers etc.) of PPF

- PPF is gradually increasing its exposure to long-term fixed-rate investments which are more suitable for the Fund considering the long term nature of pension liabilities. At the end of February 2010 long term PIBs constitute 36% of the Fund size.



# Government of the Punjab

## Punjab Pension Fund



### FUND'S PERFORMANCE

- Time Weighted Return (TWR) earned by PPF until February 2010 is summarized as under:

Period	Annualized Return for the period	
	Gross Return	Net Return*
16 May 2008 (inception) to 30 June 2008	7.00%	6.79%
FY 2008-09	15.21%	15.00%
Jul 2009 - Feb 2010	13.95%	13.78%
Feb 2010	12.15%	12.02%

\*Net Return means the return after deducting expenses incurred on management of PPF

- Despite a gradual shift towards long-term fixed-rate investments (PIBs), the Fund has been invested primarily in short term bank deposits during the current financial year therefore its return has been moving in line with market interest rates.

### REVIEW OF IMPORTANT ECONOMIC & FINANCIAL VARIABLES

#### GDP GROWTH

- Three major segments of the GDP are agriculture, industry and services. Their shares in GDP, growth rates and contributions to the GDP during the last two financial years are summarized in the following table:

	FY 2007-08			FY 2008-09		
	Share in GDP (%)	Growth rate (%)	Contribution to GDP growth (%)	Share in GDP (%)	Growth rate (%)	Contribution to GDP growth (%)
Commodity producing sectors	47	1.4	0.69	46.2	0.2	0.08
Agriculture	21.3	1.1	0.24	21.8	4.7	1.00
Industry	25.7	1.7	0.45	24.3	-3.6	-0.92
Services sector	53	6.6	3.41	53.8	3.6	1.92
Overall GDP	100	4.1	4.10	100	2.0	2.00

Source: Pakistan Economic Survey 2008-09 (published by Ministry of Finance)

- Growth in agriculture sector in FY 2009-10 is likely to be lower than strong growth of 4.7% seen in FY 2008-09.
  - Performance of Kharif crops (April - October 2010) has been weak during FY 2009-10. This is attributable to water shortages at sowing times and decline in area under cultivation of rice and sugarcane because of lower prices received for these crops in the previous Kharif season. Area under cultivation of cotton increased in Kharif FY 2009-10 due to favorable prices in the previous Kharif



## Government of the Punjab Punjab Pension Fund



season but production is expected to remain stagnant at last year's level due to negative developments including higher temperatures and pest attacks.

- Aggressive wheat sowing for Rabi season (November - April 2010) in the wake of better water availability, lower fertilizer prices & stable domestic wheat prices despite a drop in international prices is likely to lead to a bumper wheat crop in Rabi season of FY 2009-10 which may support agriculture growth.
- There has been a sharp deceleration in credit growth for non-farm sectors which may slow down the growth rate of livestock sub-sector.
- Industry consists of the following major segments

	Share in GDP in FY 2008-09 (%)
Mining & Quarrying	2.5
Manufacturing	18.2
Large scale manufacturing	12.1
Construction	2.1
Electricity & gas distribution	1.5
Industry (total)	24.3

Source: Pakistan Economic Survey 2008-09 (published by Ministry of Finance)

Large Scale Manufacturing (LSM) is clearly the biggest of these segments. LSM sector has shown positive growth during the first half of the current financial year. As per the provisional numbers for Quantum Index of Large-scale Manufacturing (QIM) released by Federal Bureau of Statistics (FBS), LSM sector showed a growth of 1.4% during Jul-Dec 2009 over the same period of last year.

- Major sub-sectors showing a decline in production during Jul-Dec 2009 as compared with Jul-Dec 2008 include textiles, food-beverage-tobacco, petroleum products and metal industries.
- Major sub-sectors showing increase in production during Jul-Dec 2009 as compared with Jul-Dec 2008 include pharmaceuticals, cement, leather products, automobiles and fertilizers.
- Future performance of LSM sector crucially depends on availability and cost of energy and credit. Increase in credit off-take by manufacturing sector during the last few months is encouraging for the sector's recovery.
- Services sector has, for many years, consistently outpaced the commodity producing sector (CPS) in terms of contribution to GDP growth and attracting investments. In FY 2009-10, services sector is expected to maintain or surpass the growth rate of 3.6% (contribution of 1.92% to overall GDP growth) achieved by this sector in FY 2008-09.



## Government of the Punjab Punjab Pension Fund



- Recovery in manufacturing sector is expected to support Wholesale and Retail Trade which is the biggest segment within the Services sector - it has one third share in overall output of the Services sector.
- A sharp decline in external trade volume (mainly imports) may adversely affect the Services sector in multiple ways. Decline in imports leads to a slowdown in Wholesale & Retail Trade activities, import-related port/shipping activities and inland transportation of imported goods.
- Strong competition has slowed down growth in Telecom sector. Reduction of federal excise duties & SIM activation charges by the government in the budget of FY 2009-10 and the decision to eliminate regulatory and reduce custom duties on import of mobile sets may help the sector.
- Finance & Insurance sector is expected to perform well on the back of favorable supervisory measures announced by SBP (e.g. higher benefit of forced sale values of collateral while computing provisioning requirements) and strong banking spreads.

### FISCAL MANAGEMENT

- The revised projections issued by the Government for the budget of FY 2009-10 and the actual results for first half of FY 2009-10 are shown in the following table:

Billion rupees

	FY 2009-10 (Proj.)	H1 FY 2009-10 (Jul-Dec 2009)	
		Amount	As % of full yr proj.
<b>Total revenue</b>	<b>2,187</b>	<b>910</b>	<b>42%</b>
Tax	1,600	659	41%
Non-tax	587	251	43%
<b>Total expenditure</b>	<b>2,927</b>	<b>1,313</b>	<b>45%</b>
Current	2,402	1,059	44%
Development	510	239	47%
Unidentified	15	15	100%
<b>Budget deficit</b>	<b>-740</b>	<b>-403</b>	<b>54%</b>
<b>Financing</b>	<b>740</b>	<b>403</b>	<b>54%</b>
External	301	110	37%
Domestic	415	293	71%
Non-bank	240	186	78%
Bank	175	107	61%
Privatization	23	0	0%

Source: Summary of fiscal operations for the period Jul-Dec 2009 (published by Ministry of Finance)



## Government of the Punjab Punjab Pension Fund



- Despite lower expenditures (45% of full year projection), budget deficit has been higher (54% of full year projection) because revenues have been much lower than the projection (42% of full year projection).
- The actual financing mix of the budget deficit has so far been very different from what was envisaged in the projections. External financing has been much lower than expected (37% of full year projection) and, as a consequence, domestic financing has been much higher than expected (71% of full year projection). A continuation of this trend has adverse implications for domestic liquidity and interest rates.

### EXTERNAL ACCOUNT

- Balance of payments during the current financial year has been compared with the balance of payment in the same period of last financial year in the following table:

Billion US \$

	Jul - Jan	
	FY 10	FY 09
<b>Current Account</b>	-2.5	-8.1
Balance on goods & services	-8.3	-11.5
Trade balance	-6.6	-9.1
Imports	17.6	20.4
Exports	10.9	11.4
Services net	-1.7	-2.4
Income net	-1.7	-2.7
Current transfers	7.5	6.1
Remittances	5.2	4.3
<b>Capital and Financial Account</b>	3.6	3.6
Direct Investment	1.1	2.6
Portfolio Investment	-0.3	-0.3
Errors & Omissions	-0.3	0.1
<b>Overall balance</b>	0.8	-4.3

Source: SBP

- Current Account Deficit has been lower during the current financial year on the back of lower imports, lower outflows on account of foreigners' incomes and higher inflows on account of workers' remittances.
- Rising commodity prices (oil etc.) are again increasing the import bill. Domestic economic activity is also improving gradually which is likely to lead to higher imports. Thus, the pressures on the 'balance of trade in goods & services' are far from over.



## Government of the Punjab Punjab Pension Fund



- Mix of inflows related to Capital & Financial Account is also shifting towards lesser investment-related and higher debt-creating inflows. This will put more pressure on country's resources for debt repayments in future.
- Over the next few years, the country needs a combination of higher exports and higher FDI (Foreign Direct Investment) in order to generate foreign exchange to pay for essential imports (crude oil, raw materials, plant & machinery etc.) and to repay the foreign currency loans becoming due. Otherwise, the inability to finance essential imports and repay foreign loans will become a major hurdle in achieving a GDP growth rate of 5% p.a. or more.

### INFLATION

- A summary of inflation rates during the current financial year is given in the following table:

End of month	CPI Inflation (YOY)
July 2009	11.17%
August 2009	10.69%
September 2009	10.12%
October 2009	8.87%
November 2009	10.51%
December 2009	10.52%
January 2010	13.68%
February 2010	13.04%

- Average CPI Inflation has been 11.08% during the current financial year (Jul 09 - Feb 10).
- Inflation went up sharply in Jan 2010. It was mainly contributed by a surge in food and energy prices. Core inflation, measured by excluding food and energy from CPI basket, declined from 10.7% in Dec 2009 to 10.3% in Jan 2010 .
- Major reasons for higher inflation in Jan 2010 included:
  - Increase in administrative prices of energy and key fuels by the government;
  - Depreciation of rupee amidst transfer of oil payments from SBP to interbank market; and
  - Temporary supply shocks to bad weather (fog) in Punjab which created supply shortages of essential food items.
- Despite the surge in CPI Inflation in Jan 2010, it is much lower compared with Jan 2009 when it was recorded at 21%. The long-term trend in CPI Inflation measured by 12-



# Government of the Punjab

## Punjab Pension Fund



month moving average also declined to 13.1% during Jan 2010 as against 13.6% in Dec 2009.

- International commodity prices remained strong during Jan 2010 on account of
  - Supply shortages;
  - Higher demand from emerging economies; and
  - Moderate recovery in advanced economies.
- IMF Commodity Price Index rose by 40.9% on YOY basis (prices compared with same month of previous year) & 3.5% on MOM basis (prices compared with the immediately preceding month) in Jan 2010 compared to 40.3% YOY & -0.5% MOM in Dec 2009. The YOY changes in Price Indices of specific commodities showed
  - high inflation in prices of Metals, Energy and Raw Material;
  - lower inflation in prices of food group; and
  - deflation in prices of fertilizers.

### INTEREST RATES

- A summary of interest rates for the current financial year is given below:

End of month	Yield on 1-yr T-bill (p.a.)	Yield on 10-yr PIB (p.a.)	6-month KIBOR (p.a.)
July 2009	11.83%	11.84%	11.99%
August 2009	12.35%	12.36%	12.56%
September 2009	12.46%	12.47%	12.65%
October 2009	12.57%	12.76%	12.84%
November 2009	12.07%	12.40%	12.41%
December 2009	12.10%	12.62%	12.43%
January 2010	11.95%	12.47%	12.23%
February 2010	12.29%	12.70%	12.43%

Source: SBP, Reuters

- Sharp rise in inflation in January 2010 led to only a modest increase in interest rates. This suggests that the market considers the inflationary pressures to be temporary and does not expect the Central Bank to raise interest rates in the near future.
- In view of the recent upsurge in inflation and continued reliance of the government on domestic borrowing, we expect that, in the upcoming monetary policy decision on 27 March 2010, SBP will keep the discount rate unchanged. We expect the market interest rates to remain close to their current levels.



# Government of the Punjab Punjab Pension Fund



---

---

## FUTURE STRATEGY

- Considering the high interest rates currently prevailing in the market, the strategy is to invest more in long-term fixed-rate instruments. The Investment Sub-Committee (ISC) & the Management Committee (MC) prefer Pakistan Investment Bonds (PIBs) over Defense Saving Certificates (DSCs) because of better liquidity and regular coupon payments in case of the former.
- The ISC's decision to invest up to 5% of Fund size in corporate bonds (Term Finance Certificates or TFCs) has been approved by the MC. We plan to gradually build the TFC portfolio over the next few months.
- There has been no breakthrough in negotiations with commercial banks for long term placement of funds. The banks are generally reluctant to take fixed deposits for periods longer than one year. The matter will be discussed in the next ISC meeting.
- The ISC is yet to make a decision on our recommendation to allocate 10% of Fund size to equity investments. This will also be discussed in the next ISC meeting.

(Aquil Raza Khoja)  
General Manager  
Punjab Pension Fund