



Safeguarding your retirement benefits

CHALLENGES FACING FUND MANAGERS OF RETIREMENT BENEFITS IN KENYA

Lazarus K. Keizi
Research & Development
Department

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Introduction

The Retirement Benefits Act requires each retirement benefits scheme to seek the services of a registered fund manager. The manager, for the purposes of the Retirement Benefits Act, is a company whose business includes undertaking, pursuant to a contract or other arrangement, the management of the funds and other assets of a scheme fund for purposes of investment; providing consultancy services on the investment of scheme funds; and reporting or disseminating information concerning the assets available for investment of scheme funds. The managers must be licensed by the Retirement Benefits Authority on an annual basis in order to carry out fund management of pension scheme assets. Before pension scheme trustees engage the services of a fund manager, they are required to come up with a prudent investment policy on the investment of the scheme funds, clearly stating the scheme's investment objectives and the benchmarks that will be used to measure the scheme's performance.

The Investment Policy Statement (IPS) development sets forth how the scheme will implement and manage its portfolio and delineates the goals and investment strategy. The IPS goes one step further by clearly defining the specific investments to be included in the portfolio and proposing how and when they should be incorporated. The IPS serves as a guide for the ongoing management of a scheme portfolio, ensuring a common understanding of the strategy and a consistent and focused execution of the scheme plan. The investment process is shown in figure 1.

The objective of the investment policy statement is to maximize the total rate of return through a broadly diversified portfolio in line with the investment guidelines given in the Retirement Benefits Regulations 2000.

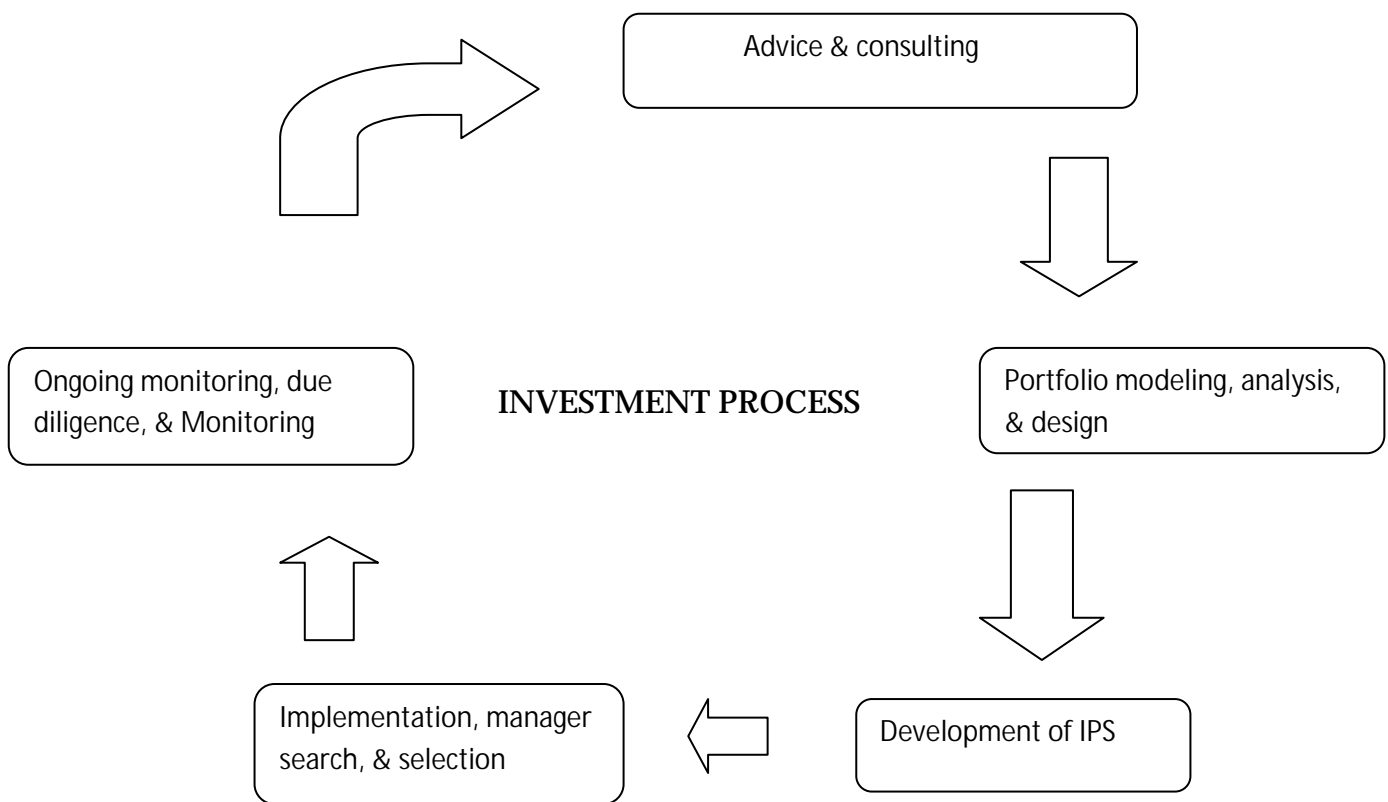


Figure: 1

The survey objectives

In Kenya, there are only sixteen fund managers registered with Retirement Benefits Authority. The survey on Challenges Facing Fund Managers in Kenya was aimed at collecting information and data on the systems in place for various fund managers. The research conducted was also aimed at supporting the Authority's strategic objectives to:

1. Streamline the retirement benefits sector in Kenya by 30th June 2009;
2. Increase the level of coverage by 5% by 30th June 2009;
3. Increase compliance levels to 80% through improved supervision to protect members' benefits by 30th June 2009;
4. Increase benefits replacement rates from 20% to 30% by 30th June 2009; and,
5. Strengthen institutional capacity to continually deliver quality services to stakeholders.

The survey is the first of its kind in the history of the Retirement Benefits Authority and the research findings will be used to recommend policy changes to the

government. The questionnaire was developed to investigate how investment policies are formulated, whether the Act is serving the interests of fund managers well, and the challenges faced by fund managers in investing retirement benefits. In addition to information pertaining to fund management business, respondents were also invited to provide information on the methods used to value bonds and measure investment performance.

The objectives of the survey were to:

1. Establish how the investment policy statement is developed and reviewed
2. Investigate whether the Retirement Benefits Act and Regulations are fulfilling the expectations of the fund managers
3. To get the fund managers views on performance ranking of managers
4. To enumerate the challenges faced by fund managers in the execution of their duties.

The survey methodology

Due to the small number of the fund managers, a census was seen as the only way to reach the majority of the fund managers. A research questionnaire was sent to all the registered fund managers via email for completion and return. **Funds under fund managers' management**

As at December 2007, assets managed by fund managers stood at Ksh182.4 billion compared to Ksh81.3 billion that is under the management of NSSF.

Detailed findings of the survey

The research questionnaire was divided into five sections. Section A was on the company profile.

Population of registered Fund Managers	-	16
Research questionnaires returned	-	14

SECTION B: INFORMATION ON RETIREMENT BENEFITS MANAGEMENT

- 1) Fund Managers participation in the development of an investment policy statement of the scheme
 - a. Initial development of the investment policy - 21.5%
 - b. Setting of the investment targets - 7.1%
 - c. Both (a) & (b) - 71.5%
 - d. Not at all - 0%
- 2) Discussion of investment reports with trustees
 - a. a. Annually - 14%
 - b. b. Bi – annually - 0%

- c. c. Quarterly - 86%
- d. d. Not at all - 0%

3) Participation in the formulation of investment policy statement objectives that guide the investment strategy

- a. a. Yes - 71.4%
- b. b. No - 14.3%
- c. c. When called upon - 14.3%

4) Whether the three year life span of an investment policy is sufficient

- a. a. Yes - 85.7%
- b. b. No - 14.3%

If **No**, what is the sufficient period?

Those that felt it was not sufficient did not have a reason

5) On **Who** is best suited to prepare the investment policy statement for the scheme

- a. The scheme's fund manager - 0%
- b. An independent investment advisor - 21.4%
- c. The trustees with guidance of the schemes' fund manager - 78.6%
- d. The trustees only - 0%

SECTION C: RETIREMENT BENEFITS ACT AND REGULATIONS

6) Whether the Retirement Benefits Act has served the interests of fund manager well

- a. a. Yes - 100%
- b. b. No - 0%

7) If **No** in 11, what is the hindrance?

None had different views about the Act

8) Whether the investment guidelines are necessary

- | | | | |
|----|--------|---|-------|
| a. | a. Yes | - | 71.4% |
| b. | b. No | - | 28.6% |

9) Kindly explain why you believe the investment guidelines are or are not necessary as per your answer.

Several answers were received which include:

For the guidelines

- Protection of the retirement funds

Against the investment guidelines

- No flexibility for fund managers
- Over restrictive
- No encouragement for long term risky assets
- Guidelines already exist in investment policy statement
- Guidelines are arbitrarily set

10) For which asset classes would you propose amendments to the current investment limits?

- Offshore to 50 per cent
- Introduce private equity
- Fixed income maximum to 100 per cent

- Guaranteed funds to follow the investment guidelines as stipulated in the regulations
- 11) Average overall annual investment return for retirement benefits schemes in the past three years
- **Ranges between 10% to 27.52%**
- 12) Method used to calculate the scheme investment performance
- Modified Dietz
 - Time weighted
 - Internal rate of return
 - Unitization system
- 13) Method utilized for valuation of bonds
- Mark to market
 - Face value plus accrued interest
 - Holding to maturity
 - Amortized premium
- 14) Yield curve utilized to determine bond
- KCB weekly yield curve
 - Equity bank yield curve
 - Dyer & Blair one week trade
 - CFC yield curve

SECTION D: RETIREMENT BENEFITS INDUSTRY

- 15) Publishing rankings of fund managers according to their annual return

- | | | |
|--|---|-------|
| a. It is a good idea and should be implemented immediately | - | 46.2% |
| b. It is a good idea but should be implemented in the future | - | 7.7% |
| c. It is a bad idea and should never be implemented | - | 7.7% |
| d. any other (state) | - | 38.4% |

16) Whether the Kenyan Capital Markets offers enough investment products for fund managers

- | | | |
|---------------|---|-------|
| a. Yes | - | 8.3% |
| b. No | - | 91.7% |
| c. Don't Know | - | 0% |

If no what products would you like to see introduced

- Mortgage backed securities
- Property unit trusts
- Traded property funds
- Commodities futures
- Collateralized mortgage obligations
- Hedging products
- Over the counter products
- Convertible securities

SECTION E: CHALLENGES AND RISKS OF INVESTMENT

17) The challenges faced by fund managers in their investment functions

- Lack of liquidity
- Unethical behaviour among stock brokers
- High stock brokerage costs

- Inhibitive regulations
- Little focus on performance
- Limited discretion
- Trustees' limited understanding of risk-return relationship
- Limited investment products

18) Risks faced during fund management duties

- Inflation
- Market volatility
- Political risk
- Competition risk
- Credit risk
- Equity price risk
- Information asymmetry

19) The best way to share information between the Authority and the fund managers

- Seminars and workshops
- Creation of a fund managers association
- Fund managers' conferences
- Brainstorming forums
- Periodical meetings

Conclusion

1. Are Fund Managers aware that the scheme Investment Policy statement is should be formulated by an independent investment advisor?

- The results of the survey indicate that 71.5 per cent of the fund managers are involved in the initial development of the investment policy and setting of the investment targets.

- From these results, it can be concluded that fund managers may not be aware that the Investment policy statement should be formulated by an independent investment advisor.
2. Is the three year life span of an investment policy statement sufficient
- 85.7 per cent of the respondents indicated that the three year life span of an investment policy statement is sufficient. It can therefore be concluded that this period is sufficient.
- Are the investment guidelines in the retirement benefits Regulations necessary?
- Over 70 per cent of the respondents believe that the guidelines are necessary.

Policy recommendation

- i. There is need to enforce the legislation requiring scheme trustees to engage the services of independent investment advisors in the formulation of their investment policy statement.
- ii. The Authority, in collaboration, with fund managers should come up with a standard method for bond valuation. Currently, there is no standard method used.
- iii. Stakeholders in the retirement benefits sector should agree on a standard method of measuring scheme investment performance.
- iv. There is need for the Authority to adopt an acceptable method of sharing information with fund managers. The methods could include Seminars and workshops, liaison with a fund managers association, fund managers' conferences, brainstorming forums and periodical meetings. The forums can be used to share information on the challenges fund managers are facing.
- v. Fund managers should develop good systems to mitigate on the enormous risks they face in their duty as investment managers.

- vi. Scheme Trustees should be trained in risk management in order to oversee the schemes' investments.
- vii. In order to enhance uniformity with the pension industry, there is need for the Authority to consider introducing performance measurement using the international best practice of time weighting.

Annex

RETIREMENT BENEFITS AUTHORITY RESEARCH QUESTIONNAIRE 2007

The Authority seeks to use the information collected from this survey towards development of the retirement benefits industry by finding out the challenges facing the investment managers in investing retirement benefits funds in the country. All responses will be treated with confidence, and only for the above stated purposes. Kindly give clear and candid responses to all questions. Please tick (✓) one, except where indicated.

SECTION A: COMPANY PROFILE

- 1) Company Name : _____
- 2) Type of company: _____

3) Total funds under management Ksh:

4) *Of which* retirement benefits assets Kshs:.....

SECTION B: INFORMATION ON RETIREMENT BENEFITS

5) Pension schemes' trustees are expected to prepare an investment policy statement after every three years. At what stage do you participate in the process?

- a. Initial development of the investment policy
- b. Setting of the investment targets
- c. Both (a) & (b)
- d. Not at all

6) During the three-year term of an investment policy statement, how often do you meet the trustees of the scheme to discuss investment reports?

- a. Annually
- b. Bi – annually
- c. Quarterly
- d. Not at all

7) An investment policy statement has objectives that guide the investment strategy. Do you participate in the formulation of the objectives?

- a. Yes
- b. No
- c. When called upon

8) From your view as an investment manager, do you think the life span of an investment policy of three years is sufficient?

- a. Yes
- b. No

9) If **No**, what is the sufficient period? _____

10) Who do you believe is best suited to prepare the investment policy statement?

- a. The scheme's fund manager
- b. An independent investment advisor
- c. The trustees with guidance of the schemes' fund manager
- d. The trustees only

SECTION C: RETIREMENT BENEFITS ACT AND REGULATIONS

11) Has the Retirement Benefits Act served your interests as a fund manager well?

- a. Yes
- b. No

12) If No in 11, what is the hindrance?

13) The Retirement Benefits Regulations 2000 requires investment guidelines to be observed by fund managers. Do you believe the investment guidelines are necessary?

- a. Yes
- b. No

14) Kindly explain why you believe the investment guidelines are or are not necessary as per your answer in 13.

15) For which asset classes would you propose amendments to the current investment limits?

16) During the last three years, what has been your average overall annual investment return performance for retirement benefits schemes in percentage?

17) What Method do you use to calculate the scheme investment performance that you report to the client?

a)

b)

c)

d)

Other (specify)

18) What method do you utilize to value bonds in your portfolio for purposes of determining values and performance when reporting to your client:

a)

b)

c)

d)

Other (specify)

19) Which Yield curve (if applicable)do you utilize to determine bond valuations for purposes of determining values and performance when reporting to your client:

SECTION D: RETIREMENT BENEFITS INDUSTRY

20) Some industry players have suggested that the Authority should publish rankings of fund managers according to their performance. What is your institution's view?

- a. (a). It is a good idea and should be implemented immediately
 - b. (b). It is a good idea but should be implemented in the future
 - c. (c). It is a bad idea and should never be implemented
 - d. (e). Any other (state)
-
-

21) As a fund manager, do you think the Kenyan Capital Markets offer you enough investment products?

- a. Yes b. No c. Don't Know

if no what products would you like to see introduced?

SECTION E: CHALLENGES AND RISKS OF INVESTMENT

22) As a fund manager of retirement benefits schemes' funds, what challenges do you face in your investment function?

23) In the investment world there are risks. As a fund manager in Kenya, what risks do you face in your fund management duties?

24) What would be the best way to share information between the Authority and the fund managers on the retirement benefits industry?

Thank you for taking time to complete this questionnaire.