

We wish you a Happy and Prosperous New Year

Pakistan inflation is more than 20% pa, for the first time after FY 1975

Possible effect on retirement funds

Officials project 22% inflation in Fiscal Year 2009, ending 30 June 2009. In FY 2010, they project 13%, reducing to 9.5 % in FY 2011.

To respond to inflation, interest rates have increased, under the lead of the State Bank. As we write, the secondary market yield on 10 year Pakistan Investment Bonds has gone up to 16.60% pa, compared with 10.39% a year ago. Yields on National Savings Schemes have also increased sharply. The yield on 3 year Special Savings Certificates (SSC's) was 9.17 % pa on 1 Jan 2008, and is now 14.53%.

The floor imposed on share prices was removed on 15 Dec 2008, about 3 months after it was imposed. As we write, share prices have fallen below that floor. Earnings and dividend yields at current prices are high. But it is impossible to say where the share market will be in three months, or three years. Funds have some interesting investment decisions to make!

In the immediate future, salaries may rise at more than the rates of investment returns. Negative real yields affect costs of Defined Benefit schemes. In Defined Contribution schemes, the effect will fall on members.

We have been here before. In FY's 1974 and 1975, official inflation rates were 30.40% and 27.03% respectively. But inflation fell to 10.90% in FY 1976. The situation corrected itself, and retirement Funds survived and prospered in the next 30 years.

We Pakistanis are resilient, and Inshallah we will also overcome present problems. But we do wish that our resilience is not tested so often.

You can out-source Provident, Pension and Gratuity Fund administration to us

You can read balances on the internet.

A growing number of Provident, Pension and Gratuity Funds have out-sourced administration to us. We have a team dedicated to this work, with many years' experience.

We can (a) maintain your Fund's and individual employees' accounts and records; (b) answer your queries about balances at end of service, or for withdrawals (from Provident Funds only) (c) prepare Funds' accounts for submission to your auditors, including the distribution of investment income under Provident Funds and DC Pension schemes.

We have now web-enabled our records. Persons designated by you can be given pass-words, to read balances at any time on the internet. Your individual employees can read their own password protected accounts, if you authorise them.

The advantage to you as an Employer or Trustee is that you take advantage of our experience and personnel, instead of having to maintain in-house capability. It is cost-efficient, and frees you to focus on your own business.

To explore this, please talk to our colleague Irfan Ali, FIA, FPSA, Consulting Actuary.
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Three increases during 2008 in National Savings Yields

Yields on SSC's, 10 year Bahbood Certificates and Pensioners' Benefit Accounts (BC/PBA's), and other NS schemes (but not Defence Certificates) were increased thrice in 2008. The Table gives details for SSC's and BC/PBA's.

Investment date →	5/6/06 to 23/06/08	24/6/08 to 30/9/08	1/10/08 to 30/11/08	1/12/08 to now
SSC's	9.17	11.25	13.00	14.53
BC/PBA	11.64	13.56	15.00	16.80

These are simple average yields % per annum.

22% inflation is like 103% income tax on Bahhood and Pensioners' Accounts

Inflation is cruelly re-distributive, favouring some classes at the expense of others. People on low and/or fixed incomes are badly affected.

Persons over 60, and all widows, can buy Bahhood Certificates. Government, defence and semi-government pensioners can invest in Pensioners' Benefits Accounts. The maximum investment in each is Rs 3 million.

The yield of 16.80% is paid monthly, and is mathematically equal to 18.16% pa. At 22% inflation, the real yield net of inflation becomes **minus** 3% pa. 22% inflation operates like income tax of 103%.

But if they survive for 10 years, investors may have the last laugh, as the next section shows.

Is it wise for Government to issue 10 year BC's/PBA's at 16.8 % pa?

The Akhtar & Hasan Letter of Aug 2008 said "Fixed return investments are a gamble on future inflation. If inflation goes down, the lender gains and the borrower loses."

Is it wise for Government to issue 10 year BC's/PBA's at 16.8% pa payable monthly, mathematically equal to 18.16% pa ?

If inflation falls to 9.5% pa, as forecast, then Government will pay a real yield of 7.9% pa.

During the 10 years ended FY 2008, inflation averaged 6.15% pa. If this is repeated,

Government will end up paying a real return of 11.3% pa. This would burden public finances.

For the average Pakistani, especially a retiree, a low real yield of 3% pa or thereabouts under index-linked government securities would be better than risking unpredictable, widely fluctuating, and perhaps negative real yields.

This would also be much less risky for Government. But it depends on public confidence in the Consumer Price Index.

Two new Turkish insurance systems

Two major new systems, TRAMER and TARSIM, were introduced in Turkey.

High fraud and loss rates, and fierce premium competition, made it hard to make a profit on Motor Third Party Liability business. TRAMER was set up in 2004. It centralises all information relating to this line. As a result, the percentage of un-insured vehicles reduced to 24% from 35-40%, and fraudulent proposals and claims have been reduced. TRAMER proved un-expectedly successful, so non-compulsory motor insurance has now been included.

Agricultural Insurance is too risky for insurance companies to undertake, so government support was inevitable. TARSIM, set up under a 2005 law, is a pool for this line. Government pays half the premium, and provides reinsurance support where the market is not sufficient. As a result, catastrophic risks like hail, storm and frost are now covered.

("Turkinsurance", Oct 2008, sponsored by Milli Re)

Christopher Columbus was the first economist

How so? Because when he set off, he did not know where he was going. When he arrived, he did not know where he had reached.

And government paid for his entire trip.