



NATIONAL PENSION COMMISSION

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CIRCULAR

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To: All Licensed Pension Fund Operators

Subject: Requirements on Performance Management and Provisioning for Expected Credit Losses (ECL)

- 1.1 The Commission has observed the need for Pension Fund Operators to measure and report on the performance of pension fund assets under their management using approved benchmarks. It has also observed the need for the standardization of Expected Credit Loss (ECL) computation in the pension industry in line with the International Financial Reporting Council (IFRS) 9 standards.
- 1.2 The objective of this Circular is to guide Pension Fund Operators on the approved benchmarks for performance measurement and reporting as well as provide a uniform methodology for calculating ECL.
- 1.3 The Following shall serve to guide PFA/CPFA in Fund Performance Management and Provisioning for ECL:

2.0 Performance Management

2.1 Performance Measurement

The performance of pension fund assets is to be measured against set benchmarks. The recommended benchmarks for each Asset Class are as stated below:

- **Quoted Equities** – NGX Pension Broad Index
- **FGN Bonds** – Bloomberg Nigeria (BNGRI) Index
- **Sub-National Bonds with ISPOs** – BNGRI + 150BPS
- **Sub-National Bonds without ISPOs** – BNGRI + 200BPS
- **Corporate Bonds** – BNGRI + (150 - 200BPS)
- **Eurobonds** – Global Aggregate Bond Index (GABI)
- **Domestic Money Market** – 364 days Weighted Average Treasury Bills Rate (WATBR)
- **Corporate Infrastructure Bonds** – 10-Year FGN Bond yield + 150 basis points
- **Infrastructure Fund** – 3-year average CPI plus 150 bps & Composite Index for Infrastructure Fund in Africa
- **Private Equity** – NGX Growth Index + 300bps
- **Real Estate Investment Trust** – 1-year average CPI
- **Real Estate (Direct)**- 1-year average CPI plus 200bps

2.2 PFAs/CPFAs are at liberty to identify and adopt alternative benchmarks other than the ones listed in Clause 2.1 above so far as they meet the following minimum requirements:

- (i) The constituents of the Benchmark are investible.
- (ii) All the constituents meet the minimum eligibility requirements as contained in the Regulation on Investment of Pension Fund Assets.
- (iii) The process of constitution/rebalancing is known and transparent.

(iv) The constituents should be dynamic and evolving to accommodate future changes.

(v) It should be constructed in a manner that allows for accurate and consistent measurement of performance over time.

2.3 PFAs shall seek prior approval of the Commission before adopting an alternative benchmark.

3.0 Performance Attribution Analysis

3.1 PFAs/CPFAs are expected to conduct an attribution analysis to evaluate the performance of investment portfolios by analyzing the sources of return and identifying the factors that contributed to the Fund's overall performance.

3.2 A report on this attribution analysis shall be submitted to the Commission before the end of the second month after the year-end on each calendar year.

4.0 Performance Appraisal

In addition to a pension fund's performance measurement and attribution, the Commission would appraise PFAs' individual fund performance using performance measurement tools that meet its requirements such as Sharpe ratio, Information ratio, Jensen's alpha, Treynor ratio etc.

5.0 Reporting Requirements

i. The PFA shall make full disclosure of all assets and liabilities under management in the valuation report in line with IFRS 7 and forward to the Commission daily.

ii. A standard reporting template shall be made available to Pension Operators in due course.

6.0 Expected Credit Loss (ECL) Provision

- i. PFAs shall ensure that there is adequate provision for ECL for all fixed income instruments valued at amortized cost in line with IFRS 9 on General Rules for the Standardization of ECL in the Pension Industry.
- ii. Where debt securities held by the pension fund managers are subject to a significant risk of non-payment, delay in payment or payment in smaller amount, the PFA shall value such debt securities at the lower cost or net realizable value, with appropriate provision made for any resulting diminution in value.
- iii. Valuation of Pension Fund Assets for periodic accounting purposes must be done on business days.

7.0 General Rules for the Standardization of ECL in the Pension Industry

S/N	Parameter	General Rule
1	Determination of Default and Recovery rates	PFAs to adopt the S&P mapping, which specifies what the local credit rating for Naira-denominated instruments mapped to the S&P international credit rating and apply the corresponding Default and Recovery rates
2	Credit Ratings for dual-rated bonds i.e.	<p>a. Where an instrument has a dual credit rating, the lower of the ratings should apply, in line with Section 5.1.8 of the Regulation on the Investment of Pension Fund Assets and Prudence Concept.</p> <p>b. In this instance, where the lower credit rating is local, the corresponding International Default and Recovery rates should be applied.</p> <p>c. Where the international credit rating is lower, the associated default and</p>

S/N	Parameter	General Rule
		recovery rates should be directly applied.
3	Determination of Probability of Default for foreign currency denominated sovereign Instruments	For foreign currency-denominated instruments issued by FGN, the default rate estimate is similar to corporate bonds, therefore the international credit rating applicable to Sovereign shall be applied to the S&P corresponding default rate.
4	Determination of Probability of Default for local currency denominated sovereign Instruments	For FGN local currency-denominated instruments, the highest credit rating in a rating band e.g. AAA shall be mapped to a AAA in an international rating scale. Therefore, FGN instruments shall have a default rate of a triple-A international credit rating.
5	ECL provision for Corporate bonds	The lower credit rating of the instrument should be mapped to the international equivalent credit rating in line with Section 5.1.8 of the Regulation on the Investment of Pension Fund Assets.
6	ECL Provision for money market instruments	The lower credit rating of the issuer/instrument should be mapped to the international equivalent credit rating in line with Section 5.1.8 of the Regulation on the Investment of Pension Fund Assets.
7	Determination of ECL provision where there is an indication the credit rating of an instrument/issuer may be downgraded or an indication of distress with the issuer	<p>Apply a lower credit rating, commensurate to the perceived risks and peculiarities for ECL computation until an official credit rating is assigned by a rating agency.</p> <p>In this instance, map the lower credit rating based on perceived risks and peculiarities of the instrument/issuer to the corresponding international credit rating as contained in the S&P mapping</p>
8	Determination of ECL provision where an existing instrument/issuer credit rating	Make whole Life Credit Loss

S/N	Parameter	General Rule
	falls or is expected to fall below the investment grade.	
9	Write Back of ECL provisions	Writeback of ECL provisions is made daily over 12 months where an entity recognizes a 12-month ECL or over the life of the instrument where lifetime ECL was made based on a significant increase in credit risk.

8.0 Please note that this Circular takes effect from 1 January 2024.

8.1 PFAs/CPFAs are required to put in place the required policies, processes and IT system recalibration to ensure a smooth take-off and timely reporting.

9.0 All enquiries on this Circular should be directed to:

Head, Investment Supervision Department

National Pension Commission

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