SSNIT INVESTMENTS SERIES

ELEVENTH EDITION

INTRODUCTION

In this edition of the SSNIT Investments Series, we continue with the discussion on the International Social Security Association (ISSA) Guidelines on investment of social security funds as introduced in the tenth edition.

A sound investment structure is essential for the effective functioning of any social security institution. It ensures an appropriate division of operational and oversight responsibilities as well as the suitability and accountability of the persons involved. ISSA has therefore, structured the guidelines to ensure all aspects of the investment process are covered. The structure is made up of guidelines that are key to the following; investment governance principles, investment governance structures, common investment processes and processes specific to internal and external investment management.

There are thirty-three guidelines of which seventeen relevant to the SSNIT scheme, because it has an internal investment management unit, will be discussed in this and subsequent editions. The guidelines are grouped according to how particular elements of the process should be applied. The format for the presentation of the guidelines are as follows:

Guideline: This is stated as clearly as possible.

Structure: This suggests the structure for investment governance that will support the application of the guideline and also facilitate the promotion of the underlying investment principle.

Mechanism: A guideline could be implemented in several ways hence a number of mechanisms are suggested for its application in the member institution. This is to ensure there are appropriate controls, processes, communication & incentives which encourage good decision-making, proper and timely execution as well as regular review and assessment of the guideline.

The overall goal is to ensure member institutions do the right things and do things right.

THE GUIDELINES – INVESTMENT GOVERNANCE PRINCIPLES

The guidelines under the Investment Governance Principles, cover the underlying structure, mechanism and processes required in the investment of reserve funds. These principles form the initial building blocks of an investment governance process. They set down the investment beliefs as well as the missions and goals which underlie any investment process. The principles are expected to be reviewed regularly to ensure that, the ensuing investment process correctly reflects the structure and mechanism in place.

Guideline – 1: Investment Beliefs

Strong investment beliefs that command institution-wide support, are aligned with objectives and inform all investment decision-making, are agreed and documented.

Investment is essentially about making judgements and decisions in the present, typically with reference to the past so as to cope with or exploit an uncertain future. Investors do this by using their underlying beliefs about how the world works. The quality of those underlying beliefs is a major determinant of success in investment. Investment beliefs reflect the views on the overall investment goal of the fund and governance areas as well as beliefs on alpha (portfolio return) and beta (portfolio volatility) which will drive the investment approach and strategy.

Structure

- A well-thought-through set of investment beliefs is clearly articulated, documented and agreed at all levels of the decision-making process. In order to assist the investment committee to order priorities, beliefs which may be contradictory are ordered according to the importance or an amount of conviction is placed on each one.
- The investment beliefs are consistently applied in all relevant areas of the decision-making process.
- The investment philosophy and process are framed with reference to the institutions' skills, resources and processes.

Mechanism

- It is necessary for the board, management and investment committee to have a clear understanding of the impact of theory on practice and formulate beliefs supported by evidence and research.
- High-level investment beliefs are then articulated by the board, management and investment committee about;
    a. Asset class and security pricing including "fair" prices of investment opportunities, the reasons for the occurrence of mis-pricing and the degree to which mis-pricing is a systematic fact of life;
    b. The investing institutions' ability to exploit its comparative advantage in such identified opportunities;
    c. How the investing institution might develop and integrate these beliefs into its investment strategy; and
    d. What these strategies (portfolio return and volatility) can produce in terms of value addition and risk, both individually and together across the whole portfolio.
- A layered or "nested" investment belief system is then articulated from the board through management and the investment committee to the investment units to guide ongoing management of the investments.

CONCLUSION

It is evident that, without a good set of investment beliefs, a pension fund might end up with a strategy that would not be appropriate for its members, given the fund objectives and the risk profile. Clear beliefs prevent a fund from switching from one strategy to another hence changing the portfolio more often than necessary resulting in high transaction costs and lower net investment return. With documented investment beliefs, trustees and their investment managers can make informed decisions, instead of simply joining the herd.

APPLICATION OF GUIDELINE - 1 BY THE TRUST

The Trust's Investment beliefs are agreed and documented in its Investment Policy and Guidelines approved by the Board of Trustees for implementation by Management and the investing departments. The objective is to invest the Scheme's assets in a responsible and prudent manner to ensure that, there would be adequate funds to pay benefits to members and their survivors in the short to long-term.

The next edition of the SSNIT Investment Series will focus on Guideline 2 – Investment mission and goals.