

Global Investment Performance Standards (GIPS) will open doors to international capital flows

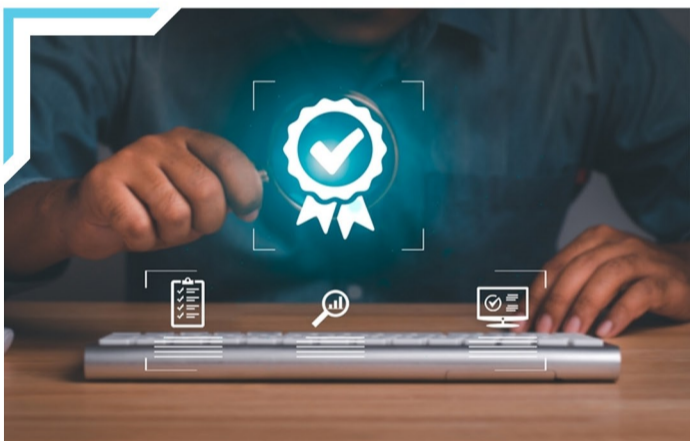
Coronation leading charge for mark-to-market mutual fund valuation

The adoption of Global Investment Performance Standards (GIPS), including mark-to-market accounting of traded securities, will enable Nigerian mutual funds to feature on international fund comparison sites. Supported by reliable and globally comparable performance data, Nigerian mutual funds will attract global investment, positioning mutual funds as the country's default destination for discretionary savings.

A decade ago, a large number of international funds invested in Nigeria, run by money managers out of the United Kingdom and other European markets, South Africa, the United States and Singapore. The existence of these funds made it possible for ordinary investors to participate in Nigerian capital markets. When the oil price crashed in 2015, sparking a recession in 2016, the performance of these funds also collapsed. Most funds shrunk in size, merged, and some were simply wound up.

The result is that for several years now "international investors, including individual savers, have found it difficult to participate in funds invested in Nigeria as their number and size have dwindled," reports Guy Czartoryski, Head of Research at Coronation Asset Management.

Nigeria's more recent challenges aside, over recent decades the global fund management and investment world has also moved on. Especially in the wake of the 2008 global financial crisis, regulators around the world have applied much more stringent compliance standards to the global mutual fund industry. To remain active in global capital markets mutual funds, asset managers and advisors have been forced to keep up with global best practice. This always means adopting GIPS. The result is that, today, "independent financial advisors don't want to be seen to be recommending funds that are not GIPS-compliant and approved," says Czartoryski.



To enable credible global fund comparison services like Morningstar, Yodelar and the Financial Times Funds Comparison Service to include Nigerian mutual funds on their platforms Nigeria needs to adopt GIPS. GIPS adoption will dramatically increase international and local investment in the country's asset management industry "increasing the range and ability of savings instruments available to global savers, including Nigerians living abroad," says Czartoryski.

GIPS require "the correct evaluation of mutual funds, showing clear linkage between the prices of their assets and value," adds Czartoryski. Unfortunately for Nigeria, it is currently impossible to calculate, let alone accurately compare, the value of most of the country's mutual funds because there is no universally applied method of valuing these funds. Furthermore, some funds pay dividends and offer various forms of guarantee while others don't. "All these variations in valuation complicate comparisons," reports Czartoryski.

Yet by far the most confusing aspect of this picture - and the Nigerian mutual fund industry's biggest barrier to global capital market participation - says Czartoryski is "the use of both market-to-market and amortised cost accounting"

In an age where the whole world has broadly adopted mark-to-market fund evaluation, moving away from the previously popular amortisation method, Nigeria remains an outlier, "forfeiting the global capital flows that would transform Nigeria from a country that saves in banks to a country that saves through much more rewarding mutual funds," says Czartoryski.

In brief, the amortised valuation method provides a theoretical projection of fund value based on the metrics of each fund's underlying securities at the time of their purchase. The mark-to-market valuation method reports a fund's fluctuating value based on the current values of its underlying securities in the market.

Amortised valuation remains popular in Nigeria, especially amongst fund managers, as it makes it easier to sell funds. From the start, the amortised method shows predictable returns over time,

even if in practice these returns are not always achieved, and certainly not consistently. Mark-to-market valuation, however, without claiming the ability to predict returns over time, provides a more accurate, real-time, valuation of funds.

Since the value of underlying securities are influenced by prevailing market interest rates as well as other variables like inflation, by regularly reporting fluctuations in the multiple metrics that determine fund value, "the mark-to-market method describes real value much more accurately as value shifts over time," reports Czartoryski.

Despite Nigeria's ambivalence in valuation approaches, the global asset management industry, as well as legislators the world over, have decided - in both practice and legislation - that the only way to compare fund managers' performance is for all funds to mark-to-market their positions as GIPS demand.

Ghana recently reminded fund managers to enforce mark-to-market rules, giving extensive guidance as to the benefits of mark-to-market and adherence with international standards. At least one Ghanaian fund manager responded by giving clients the mark-to-market value of holdings as well their amortised value.

"Our own Securities and Exchange Commission (SEC) rules clearly favour mark-to-market fund evaluation," observes Czartoryski. While implementation is currently patchy it is likely only a matter of time before either the regulator, market forces, or a combination of the two ensure broad-based compliance.

Mark-to-market is the only way to avoid surprises when fund holders come to sell their holdings.

Over the long term, adoption of mark-to-market accounting and GIPS is a pre-requisite to "building trust in mutual funds as reliable and safe wealth preservation and growth tools that every Nigerian should feel confident using," says Czartoryski.

Currently, the absence of uniform mark-to-market valuation across the Nigerian asset management industry is an obstacle to competition.

Fund managers using the amortised accounting method will report steadily increasing values to the fund's unit holders. Fund managers following the mark-to-market valuation method will report fluctuating values to the funds' unit holders, though the cash flows provided by the underlying securities are no different. While the mark-to-market method will more accurately reflect the value of the fund in real time, using the different values reported by both methods makes genuine comparison impossible, "crippling the consumer's ability to accurately judge value and performance," explains Czartoryski.

Amortised valuation also increases risk.

Since amortised accounting doesn't guarantee investors the unit values it generates in all circumstances, amortised prices can exceed what the market is able to realise, increasing risk for investors in addition to creating the potential for broader systemic risk.

Coronation's decision to lead the conversation on Nigeria's adoption of mark-to-market mutual fund valuation currently reflects a higher order of client service and ethical commitment to corporate responsibility. Certainly, Nigeria's Association of Corporate and Individual Investment Advisors, ably headed by Mr. Akin Adeniyi, applies mark-to-market valuation to the funds that this important independent body assesses. Similarly, "Coronation will be offering international investors GIPS-compliant Nigerian funds domiciled and regulated in Nigeria," reports Czartoryski.



Most importantly however, in picking up the baton for mark-to-market mutual fund valuation and broad GIPS adherence, Coronation is seeking to empower ordinary Nigerians with accurate and reliable tools to assess and compare the value of mutual funds. In addition to expanding the range and effectiveness of saving instruments available in the country, "the adoption of GIPS and mark-to-market fund valuation will also open Nigeria's mutual fund industry for global investment, significantly increasing the depth and capability of our capital markets," concludes Czartoryski.

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