

Comparing Mutual Funds- Apples and Oranges

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INTRODUCTION

The Mutual Fund industry is taking off in Nigeria, with rapid growth recorded during 2020. Investors increasingly want to build their savings with professional Mutual Fund managers rather than saving their money in banks.

For all this, however, the aggregate assets under management (AUM) of Nigeria's Mutual Funds are still only 14% the size of its Pension Funds. The industry is at a critical point in its development as it requires several more years of rapid growth to become a true force in Nigeria's financial infrastructure.

In this report we put ourselves in the position of a saver wishing to create a pot of money by investing in Fixed Income funds. And, not unnaturally, our saver wishes to compare the performance of these funds (even though past performance is not necessarily a guide to future performance). Following this line of enquiry we gathered material from the Securities and Exchange Commission, the Fund Managers Association of Nigeria and from the funds themselves.

What we found is that data are not comparable. Performance data for 2020 vary widely, but this is unlikely to be due to the different strategies of the different funds. Rather, it is because different funds report their data differently. This leaves our saver – and all investors – in a difficult position, without the information required to take an informed decision.

In our opinion, this issue needs to be fixed. In many markets around the world, the Morningstar service and the Financial Times Managed Funds service provide accurate and comparable data on thousands of funds, creating confidence and engagement with millions (if not hundreds of millions) of investors. Such a service is required in Nigeria.

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CHOOSING A FIXED INCOME FUND

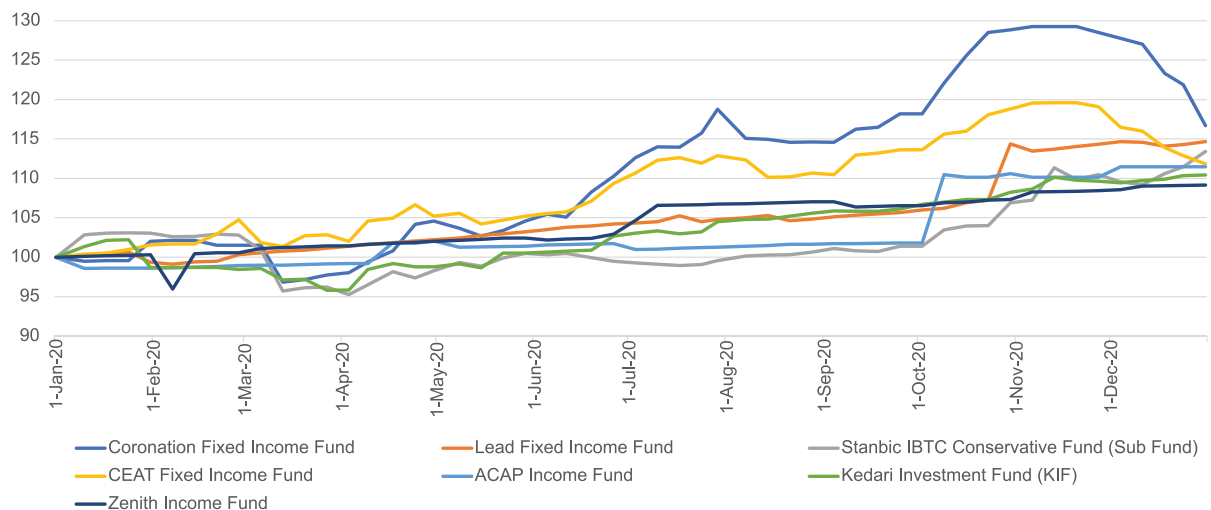
Fund comparison data exists, but it needs improving

In this report we put ourselves in the position of an individual who wishes to invest in a mutual fund in Nigeria. The intention is to save a pot of money for a future expense, and the desire is to see that pot of money grow. There are plenty of funds to choose from, but our saver wants to know which fund managers are the best performers.

We assume that, to begin with, the saver is looking at Fixed Income funds. And we focus on the performance of these funds during 2020, even though past performance is not necessarily a guide to future performance.

And the trouble is, as we shall explain, that it is very difficult to compare Fixed Income funds.

Reported Unit Price (UP) performance in 2020: the Top-7



Source: Securities and Exchange Commission (SEC),
Fund Managers Association of Nigeria (FMAN), Coronation Research

We look at data provided by the Securities and Exchange Commission (SEC) for 17 Naira-denominated Fixed Income funds that were operating and reporting data throughout 2020. These give us Net Asset Value (NAV) data and Unit Price (UP) data weekly. As investors, we are not much interested in the NAV data as these tell us the size of the fund, which is influenced by the level of past subscriptions as well as performance. What interests us is the Unit Price (UP), which tells us the value of our own investment. In particular, we are interested in how UP grows over time, as well as what dividends (or distributions) are paid.

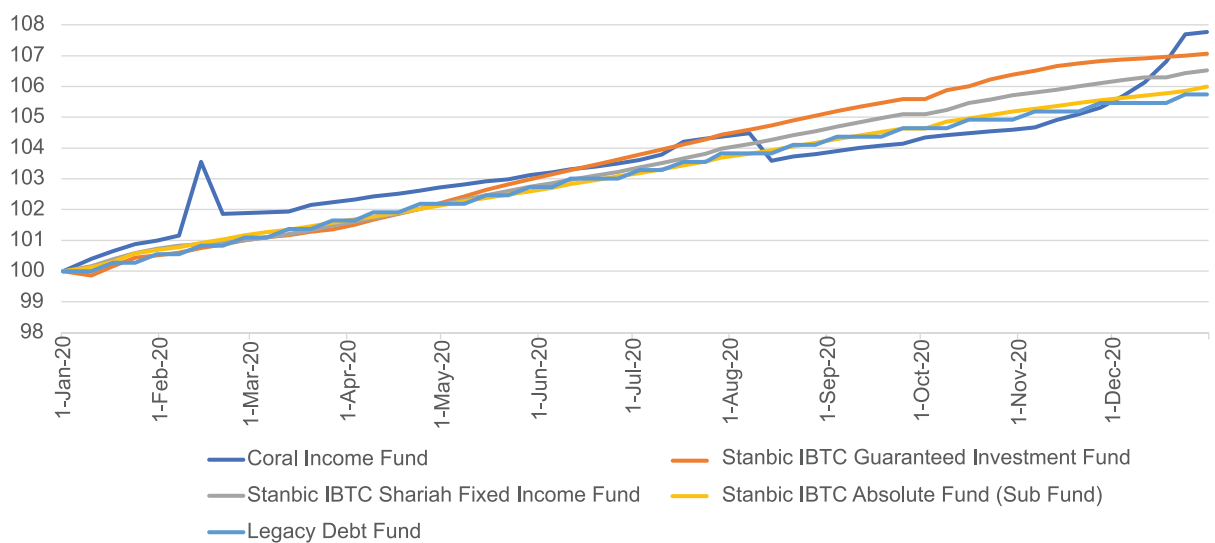
To begin with we select the Top-7 performing funds by Unit Price during 2020, rebasing all data to a value of 100 on 1 January. One might think that we would be happy with this data. After all, our Coronation Fixed Income Fund comes out well from the comparison. But the problem is that the data looks a little implausible. How do some funds return nearly 17.0% when others apparently (emphasis on apparently – we are only looking at Unit Prices) only return in the region of 9.0%? Surely the difference in fund manager performance cannot be as big as this in a single year?

CHOOSING A FIXED INCOME FUND

Unit price data what we have. Does it tell us the whole picture?

The next batch of data further arouses our fears. For when we measure the performance of the Next-5 best-performing Fixed Income funds we find that their performance is within a plausibly narrow range, but well below the performance of the apparently best-performing funds. (Note that the scale on the chart below is 98 to 108, which compares with a scale of 90 to 130 in our first chart.)

Reported Unit Price (UP) performance in 2020: the Next-5

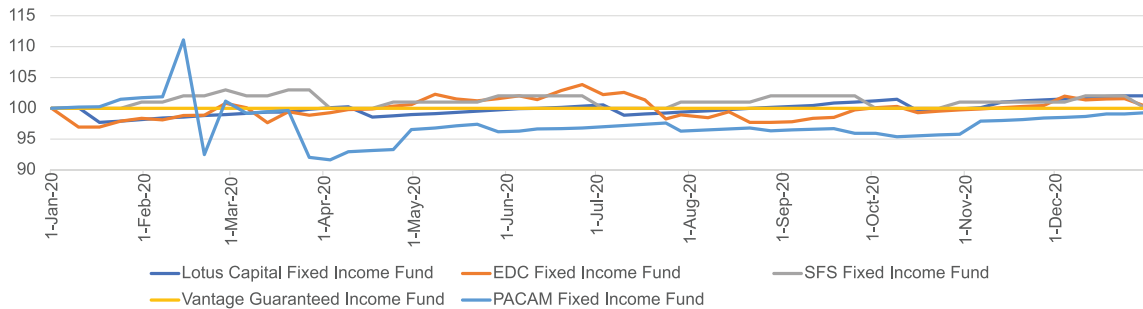


Source: Securities and Exchange Commission (SEC),
Fund Managers Association of Nigeria (FMAN), Coronation Research

And, as if this wasn't enough, the data for the Second Next-5 (i.e. the remainder of our sample) is still less convincing, with some funds apparently showing a negative Unit Price return. (By now, of course, our saver is beginning to realise that a negative UP return is not the same thing as a negative total, i.e. with dividend, return – we will delve into these differences shortly.)

CHOOSING A FIXED INCOME FUND

Reported Unit Price (UP) performance in 2020: the Second Next-5



Source: Securities and Exchange Commission (SEC),
Fund Managers Association of Nigeria (FMAN), Coronation Research

Comparing apples with oranges

Our saver is, by now, questioning the data on Unit Price: not that it is inaccurate (there is no reason to think so), but that different data reflect different measurements. At the very least, we are comparing apples with oranges.

After all, 2020 was a very good year (the best in a decade) for the performance of Naira-denominated bonds. Investors piled cash into a limited stock of Federal Government of Nigeria (FGN) bonds in an unprecedented way; yields crashed and prices rose sharply. If all Fixed Income funds were reporting on a strictly mark-to-market basis (in other words, reporting in their Unit Price the market value of the bonds they hold) then most of them would have reported very strong performance.

Expectations, and next steps

What is our saver going to do? If the expectation was that there is a simple way of comparing the performance of different Fixed Income funds, then this is disappointing. This contrasts with the experience in developed markets where savers have comparable data on fund performance, for literally thousands of funds, at their fingertips. Moreover, the Unit Price is the price at which the saver participates in (buys into, or sells out of) the fund, so having non-comparable Unit Price data makes unclear the value of underlying investments.

On the other hand, at the moment there are no better data in Nigeria. The Unit Price data are what Mutual Funds (legally termed Collective Investment Schemes) are required to submit regularly to the SEC, and this data is used by the Fund Managers Association of Nigeria (FMAN). There is no alternative stream of data.

Therefore, the next logical step is to contact the fund management firms themselves.

COMPARING APPLES WITH ORANGES ... AND MANGOES

The three main sources of discrepancy

To continue our study of the performance of Fixed Income funds we contacted each of the 17 funds and asked for their factsheets and their prospectuses. After several weeks (during last December and January) we gathered some information for almost all of the funds, but it was not a straight forward task. Our efforts went a long way beyond merely examining each fund management company's website: we exchanged emails; we rang fund managers; we visited offices. Our first impression is that information, not to mention up-to-date information, is often difficult to obtain.

Fixed income funds: how they report, dividends and guarantees

FUND NAME	SPONSOR / MANAGER	MARK-TO-MARKET (MTM)?	PAY DIVIDENDS?	CAPITAL PRESERVATION, OR GUARANTY?	FUNDS SIZE NAV, NM	UNIT PRICE PERFORMANCE IN 2020
Coronation Fixed Income Fund	Coronation Asset Management	Yes	Yes	N/a	2,480	16.7%
ACAP Income Fund	Alternative Capital Partners	N/a	Yes	N/a	112	11.5%
CEAT Fixed Income Fund	Capital Express Asset and Trust	Amortised cost	N/a	N/a	558	11.8%
Kedari Investment Fund	Kedari Capital	Yes	N/a	N/a	291	10.5%
Zenith Income Fund	Quantum Zenith	Yes	Yes	N/a	26,376	9.2%
Lead Fixed Income Fund	Lead Asset Management	Yes	Yes	"Capital Preservation"	615	14.7%
Stanbic IBTC Guaranteed Fixed Income Fund	Stanbic IBTC Asset Management	Appears not to	N/a	Yes	35,754	7.1%
Stanbic Shariah Fixed Income Fund	Stanbic IBTC Asset Management	Appears not to	N/a	N/a	11,594	6.5%
Stanbic IBTC Absolute Return Fund	Stanbic IBTC Asset Management	Appears not to	N/a	Yes	36,444	6.0%
Legacy Debt Fund	FCMB Asset Management	No	Yes	N/a	27,371	5.7%
Coral Income Fund	FSDH Asset Management	Appears not to	Income fund	N/a	16,910	7.8%
Stanbic IBTC Conservative Fund	Stanbic IBTC Asset Management	Appears not to	N/a	"Safety of funds"	398	13.4%
Vantage Guaranteed Fixed Income Fund	Investment One Funds Management	Appears not to	Yes	"Pre-stated return"	13,622	0.0%
SFS Fixed Income Fund	SFS Capital Nigeria	No	N/a	"No loss"	5,274	0.0%
Lotus Halal Fixed Income Fund	Lotus Capital	No	Yes	N/a	12,063	2.0%
EDC Nigeria Fixed Income Fund	EDC Fund Management	Yes	Yes	Yes	954	0.4%
PACAM Fixed Income Fund	PAC Asset Management	Appears not to	Yes	N/a	57	-0.7%

Source: SEC, FMAN, Companies, Coronation Research. NB Fund size, NAV, is given for 31 December 2020.

Unit Price performance compares opening and closing Unit Prices in 2020

Having read a mass of prospectuses and factsheets, our preliminary findings are that there are two main sources of discrepancy in how funds report their data, to which we can add a third factor which probably strongly influences how they invest and how they perform.

COMPARING APPLES WITH ORANGES ... AND MANGOES

Using mark-to-market accounting, or other accounting methods.

Some funds use mark-to-market accounting and publish their data accordingly. Mark-to-market simply means recording the price level (usually the bid price) of each holding and recording it as a constituent of a fund's overall NAV and unit price. Other funds, however, use the amortised cost method, whereby the initial value of an investment is recorded at its discounted price, with the discount being added back periodically until redemption. Some funds state that they use market-to-market and amortised cost, which is confusing. In a year of volatile Fixed Income prices, such as 2020, these differences result in big differences in reported performance.

Paying dividends.

Many funds pay dividends. Paying a dividend depresses the Unit Price of the fund. If a fund pays out all its returns above par to its investors, then the Unit Price will never change. We need to find out the history of dividend payments and add them back to the Unit Price performance.

Capital Preservation and Guarantees.

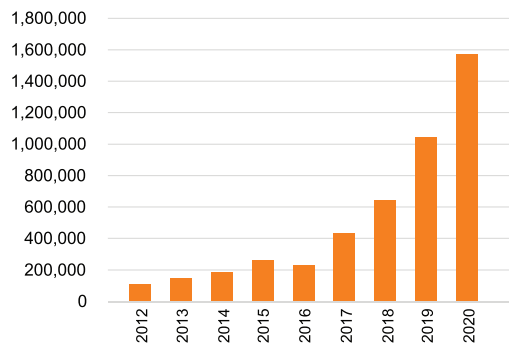
This point is less about accounting and more about fund management style. If a fund sets out not to make any losses, then its returns are likely to reflect T-bill performance more than Fixed Income performance (unless it uses the amortised cost method and only buys Federal Government of Nigeria, FGN, bonds). Such funds therefore may report quite low Unit Price performance even in a year of rapidly rising bond prices.

WHY THIS MATTERS

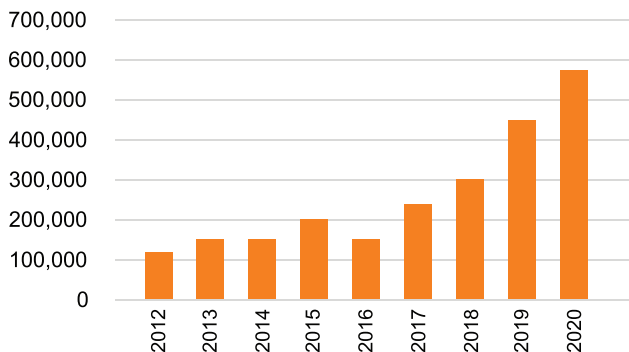
Building confidence into the system

At first sight, the Mutual Fund industry seems to be in good shape. It is growing extremely quickly. Between 2015 and 2020 its total assets under management (AUM) grew by a compound annual growth rate (CAGR) of 43%, or by a CAGR of 23% in inflation-adjusted terms. Very few industries in Nigeria can match this.

Total industry AUM,
nominal Naira millions



Total industry AUM, in 2012
constant prices, Naira millions



Source: SEC, FMAN, National Bureau of Statistics, Coronation Research

And yet growth is no guarantee of future development, in our view. The total AUM of the Mutual Fund industry stood at just under N1.6 trillion (tn) at the end of 2020, but this is just 14% of the size of Nigeria's Pension Fund industry. Moreover, the distribution of funds remains heavily weighted towards a small number of players. This suggests that some fund management companies may not have the asset base, and income flows, to support the development of the industry.

This matters because the cost of harmonising financial reporting across Mutual Funds is likely to be quite high. In particular, the adoption of Global Investment Performance Standards (GIPS) involves an outlay which some small fund managers could find onerous, in our view. Yet, without GIPS, the Nigerian industry could not be considered for inclusion in mainstream global fund comparison services such as Morningstar and the Financial Times Fund Comparison service.

From here to GIPS

At the same time, improvements in reporting fund performance – even if they do not reach GIPS in one step – are likely to increase confidence in the system. As our notional and potential investor in Fixed Income funds found, the current diversity in reporting begs more questions than it answers. So, an agreed framework of harmonising industry-wide reporting, with setting GIPS as the ultimate goal, would go a long way to improving the customer experience, in our view.

A NOTE ON OUR METHODS

Collecting data on funds

Our method in collecting data on funds was to be as fair as possible and to narrow our focus on Fixed Income funds. We have used data published by the Securities and Exchange Commission (SEC) and the Fund Managers Association of Nigeria (FMAN) and used inflation data from the National Bureau of Statistics (NBS) when adjusting data for inflation.

When it comes to dealing with data from the Coronation Asset Management Fixed Income Fund, we treated this data in the same way as all other data under review, i.e. using SEC and FMAN data rather than data from our own company. We note that Coronation Asset Management uses mark-to-market accounting (though not exclusively) in its reporting, and in a year of strong bond market (i.e. price) performance like 2020 we would expect this to translate into good performance in terms of Unit Prices (UP).

Our analysts approached each fund under review with a request for information, factsheets and prospectuses, as potential clients for these funds. We collected as much as possible during December 2020 and January 2021 from sales personnel and offices, via websites, emails, telephone calls and office visits. Therefore, we have created an impression of the customer experience of investing in funds. This report therefore, categorically, is not an exhaustive study of the reporting of the featured funds, nor is it an exhaustive report on the information available from the featured funds.

Readers of this report are asked not to consider the evidence presented on Unit Price (UP) and NAV (NAV) performance as evidence that the performance of any one fund is superior to any other. The purpose of this report is to demonstrate the opposite, namely that current diversity in reporting practices disables any such comparison. This report is not intended to facilitate comparison between funds' performance. Nor does it amount to a recommendation to participate in any of the featured funds.

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Flour Mills of Nigeria	G
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Sell:	The analyst considers the stock overvalued and expects the stock to underperform the Benchmark over the next 12 months or the stated investment horizon.
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	Date	Recommendation	Date	Recommendation	Date	Recommendation	Current price, Naira/s	Target price, Naira/s
Zenith	02-Jan-19	Buy	08-May-19	Buy	08-Jan-20	Buy	21.80	27.50
GT Bank	02-Jan-19	Hold	08-May-19	Hold	08-Jan-20	Buy	31.25	37.50
Access	02-Jan-19	Buy	08-May-19	Buy	08-Jan-20	Buy	10.30	11.25
FBNH	02-Jan-19	Buy	08-May-19	Buy	08-Jan-20	Buy	6.50	12.50
UBA	02-Jan-19	Buy	08-May-19	Buy	08-Jan-20	Buy	8.85	11.50
Stanbic IBTC	02-Jan-19	Buy	08-May-19	Buy	08-Jan-20	Buy	42.50	61.35
Fidelity	02-Jan-19	Buy	08-May-19	Buy	08-Jan-20	Hold	2.02	2.50
Sterling	02-Jan-19	Hold	08-May-19	Hold	08-Jan-20	Hold	2.00	1.90
	Date	Recommendation	Current Price, Naira/s	Target price, Naira/s				
Nestle Nig.	17-May-19	Hold	1,300	1,213.89				
Flour Mills of Nig.	17-May-19	Hold	13.50	18.29				
Unilever Nig.	17-May-19	Hold	29.45	28.39				
PZ Cussons Nig.	17-May-19	Hold	5.90	8.22				

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Buy	66.7%
Sell	0%
Hold	33.3%
Under Review	0%

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