

FMA, Reuters launch bond index

RECORDER REPORT

KARACHI: Financial Markets Association of Pakistan (FMA) and Reuters Pakistan Ltd, under the initiative of State Bank of Pakistan, have announced introduction of Pakistan Government Bond Index (PGBI) from February 21, 2005.

FMA and Reuters would provide two indices for the market participants: 1) Total Return Index; and 2) Clean Price Index.

The release of the Association said that total Return Index calculates price performance and income paid, assuming that the coupon is reinvested back in the portfolio, while the Clean Price Index tracks daily price performance of the market.

In addition, a modified duration calculation of the portfolio provides a risk measure. The indices are composed of selected liquid government bond issues chosen by the Technical Committee of FMA. The indices will be calculated daily for the settlement day of the market. The validated closing market prices for selected bond issues will be sourced from the Primary Dealers. For this purpose a Bond Fixing Page (PKBF) has been established on Reuters. The use of market prices will reduce bias in calculating the Index. In essence, the index will be priced by the market for the market.

The used methodology for index

calculation is in conformity with the standardized rules of European Federation of Financial Analysts Societies—European Bond Commission and ISMA. The adopted methodology is already in use by prominent Bond Indices like EFFAS Indices, ISMA Indices, FTSE Bond indices, iBoxx Indices and is also being used in several emerging and developed economies—India, Thailand, Taiwan, Turkey, Hong Kong etc.

The unique features of Pakistan Govt Bond Index (PGBI), which distinguishes it from existing indices, are:

1. Representative: The index is constructed with the consultation of State Bank and the Market participants and is managed by a neutral third party (Reuters). In essence, the index would be a true representative of the market.

2. Replicable and Investable: The index would include only those securities in which an investor can deal at a short notice, i.e. liquid issues. Firm prices should exist for all constituent bonds.

3. Reliable and Accurate: Index calculation should accurately reflect the actual changes in the value of the portfolio consisting of the index securities.

4. Timely updating: Index values are made available on the same day so that managers can measure per-

formance immediately, and make timely adjustments to investment strategy.

5. Flexibility: The index is flexible to accommodate the needs of individual portfolio managers.

6. Transparent: Investment managers know which securities are included in the index and how it is constructed.

Objectives & Applications of Pakistan Govt. Bond Index (PGBI): The creation of Pakistan Govt. Bond Index will serve to provide; i) Track Daily Price Performance of the Market; ii) Track Total Returns for Fixed Income Investment, iii) Track Historical Performance & Volatility; iv) Provide Risk Measures & Transparency, v) Investment managers can measure their performance by using these indices PGBI as a reliable tool; and vi) The PGBI forms an excellent benchmark to measure the performance of the emerging fixed income mutual fund markets.

Thus, Pakistan Emerging Bond Index will assist both Local & Global investors and Fund Managers in their Asset Allocation strategies and help to track return of the portfolio over period of time. FMAP was assigned the project ownership of exploring and developing the proposed Pakistan Government Bond Index