PERFORMANCE OF NATIONAL PENSION SCHEME

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Abstract

With the changing social and economic environment, making one's future secure by way of pension provides great relief to retired persons and helps them live a financially secure and dignified life after retirement. Proper financial planning adds the quality of life in the years to come and if the person further provides for healthcare he can add years to his life. Pension in India has traditionally been based on financing through employer and employee participation. Majority of the population is not covered by any formal pension scheme, as the coverage in employee pension schemes has been restricted to only 1 the organized sector. Only about 12% of the working population in India is covered by some form of retirement benefit schemes. That means 88% of population still does not have access to any form of retirement planning and has to rely on their own earnings or traditional and informal methods of old age income security such as the joint family system. National Pension Scheme is introduced by the Government of India, aiming to lead a comfortable life after retirement. The National Pension scheme is extended to all the citizens of India. The scheme is governed and monitored by an established autonomous body PFRDA set by the Government of India. Very few people are aware the National Pension Scheme, not much of them showed interest. To understand the performance of the National Pension Scheme fund offered by various companies are taken for study.

Key words: NPS, Tier – I, Tier- II, Equity, Corporate Bonds

Introduction

The National Pension Scheme is a government sponsored pension system which was launched in January 2004, for the employees of the government. The NPS is a voluntary contribution pension system administered and regulated by the PFRDA (Pension Fund Regulatory and Development Authority) by passing an Act of the Parliament of India. NPS was initiated for the government employees with the decision of the Government of India to stop defined benefit pensions for the employees who joined after 1 January 2004, and it was opened for all citizens of India in 2009 including self- employed professional and others in unorganized sectors on voluntary basis. The objective of the NPS is to create pensioned society in India.

National Pension Scheme is the cheapest market linked retirement plan, which is easily accessible, low cost, tax-efficient and flexible retirement savings account. The employer can also contribute for the social security/welfare of the individual. NPS is designed on Defined contribution basis where in the subscriber contributes to his account, accumulated wealth depends on the contributions made and the income generated from investments of such wealth. The greater the value of the contributions made, the greater the investments achieved, the longer the term over which the fund accumulates and the lower the charges deducted, the larger would be the eventual benefit of the accumulated pension wealth likely to be.

Contribution + Investment Growth – Charges = Accumulated Pension Wealth

There are two types of NPS Accounts

i. Tier – I Account : It is a basic pension account with limitations on withdrawal. Before attaining the age of 60 years of age, only 20% of the contribution can be withdrawn while the rest of the 80% has to be used for buying annuity from a life insurer. After attaining the age of retirement also, 60% contribution can be withdrawn and the rest 40% again has to be used to purchase annuity from approved life insurers. This account is available from 1st May 2009.

ii. Tier- II Account: It is a voluntary savings option from which a person can withdraw money without limits. This account is available from 1st December 2009.

Minimum contribution requirement	Tier – I	Tier - II
Minimum contribution at the time of account opening	Rs.500/-	Rs.1,000
Minimum amount per contribution	Rs.500	Rs.250
Minimum Account Balance at the end of FY	6000	2000
Minimum number of contributions in a year	01 per year	01 per year

Tax benefit to employee:

Individuals who are employed and contributing to NPS would enjoy tax benefits on their own contributions as well as their employer's contribution as under: -

(a) Employee's own contribution - Eligible for tax deduction up to 10% of Salary (Basic + DA) under Section 80 CCD(1) within the overall ceiling of Rs. 1 lac under Sec 80 CCE.

(b) Employer's contribution – The employee is eligible for tax deduction up to 10% of Salary (Basic + DA) contributed by employer under Sec 80 CCC(2) over and above the limit of Rs. 1 lac provided under Sec 80 CCE.

Tax benefit for self-employed: Eligible for tax deduction up to 10 % of gross income under Sec 80 CCD (1) with in the overall ceiling of Rs. 1 lakh under Sec 80 CCE.

Pension Fund Managers

The funds contributed by the Subscribers are invested by the PFRDA registered Pension Fund Managers (PFM's) as per the investment guidelines provided by PFRDA. The investment guidelines are framed in such a manner that there is minimal impact on the subscribers contributions even if there is a market downturn by a judicious mix of investment instruments like Government securities, corporate bonds and equities. At present there are 8 Pension Fund Managers (PFM's) who manage the subscriber funds at the option of the subscriber. At present, Subscriber has option to select any one of the following 8 pension funds:

- ICICI Prudential Pension Fund
- LIC Pension Fund
- Kotak Mahindra Pension Fund
- Reliance Capital Pension Fund
- SBI Pension Fund
- UTI Retirement Solutions Pension Fund
- HDFC Pension Management Company
- DSP Blackrock Pension Fund Managers

Since registration of PFMs is an ongoing process, this list will be updated from time to time.

Choice of Investment :

NPS allows two approaches to invest in the account.

1. Active Choice: Individual Funds: Unlike traditional investment products, NPS offers the flexibility to design your own portfolio depending on the risk appetite of the investor. The investor can design portfolio by allocating funds among the following four asset classes.

1. Alternative Infrastructure Fund (A)
2. Corporate Debt (C) - "Medium Return – Medium Risk"
3. Equity (E) – "High Return – High Risk"
4. Government Securities (G) - " Low Return – Low Risk"

2. **Auto Choice: Lifecycle Fund :** In this type of scheme preference, the Scheme Setup (scheme as well as allocation ratio) will be determined by the system based upon the age of the Subscriber at the time of registration.

A Subscriber who wants to automatically reduce exposure to more risky investment options as he / she gets older, Auto Choice is the best option. As age increases, the individual's exposure to Equity and Corporate Debt tends to decrease. Depending upon the risk appetite of investor, there are three different options available within 'Auto Choice' - Conservative, Moderate and Aggressive.

Conservative Fund: This Life cycle fund provides a cap of 25% of the total assets for Equity investment.

Moderate Fund: This Life cycle fund provides a cap of 50% of the total assets for Equity investment.

Aggressive Fund: This Life cycle fund provides a cap of 75% of the total assets for Equity investment.

NPS Lite: The NPS Lite is designed with the intention to secure the future of the people who are economically and financially not well to do with effect from April 1st 2010. It has developed on a low charge structure. The people forming part of this low income groups will be represented through their organizations known as " Aggregators" who would facilitate in subscriber registration, transfer of pension contributions and subscriber maintenance functions. Subscribers in the age group of 18 to 60 can join NPS – Lite through the aggregator and contribute till the age of 60.

Objective of the Study : To know about the National Pension Scheme and to understand the performance of the National Pension Schemes offered by Pension Fund Managers. To identify the best pension Scheme fund .

Tools of Analysis: The tools used for the analysis are Cumulative returns from 3 months to 3 years, Returns and Standard deviation, Sharpe Ratio.

Sharpe ratio is a measure of risk-adjusted return of a Scheme. It is calculated as the excess portfolio return over the risk-free rate relative to its standard deviation. The higher the Sharpe ratio, the better it is.

$$S_p = \frac{r_p - r_f}{\sigma_p}.$$

Here

r_p = portfolio rate of return

r_f = risk free rate of return

σ_p = standard deviation.

Limitations of the Study:

The limitations of the study were the study was done on the NPS with Category E (Equity) and C (Corporate Debt).

The data was secondary data taken from NPS statistics as on Feb 1st 2018.

The data was represented in terms of percentage.

Analysis:

Table : 1 National Pension Scheme Cumulative Returns Equity Tier –I

(%)

Scheme	1Month	3Months	6 Month	1Year	3 Years
HDFC	3.06	5.61	8.70	28.89	9.79
ICICI	4.01	6.87	9.77	27.37	9.05
Kotak	2.05	5.34	9.91	27.98	9.76
LIC	3.28	5.20	9.52	25.49	8.37
Reliance	3.03	4.62	8.66	28.06	8.79
SBI	3.55	6.03	9.05	26.84	9.20
UTI	3.23	6.46	10.38	28.75	10.24

Table : 2 National Pension Scheme Cumulative Returns Equity Tier – II

(%)

Scheme	1Month	3 Months	6Months	1 Year	3 Year
HDFC	3.10	5.71	8.81	29.26	10.37

ICICI Prudential	3.94	6.82	9.76	27.35	9.0
Kotak	1.99	5.28	9.82	27.90	9.73
LIC	2.57	3.95	8.73	23.97	8.55
Reliance Capital	3.05	4.67	8.66	28.35	8.87
SBI	3.60	6.12	9.20	27.10	9.21
UTI Retirement Solutions	3.84	6.98	10.38	29.33	10.15

Table :3 NPS Cumulative Returns Corporate Debt Tier – II (%)

Scheme	1 Month	3 Months	6 Months	1 Year	3 Year
HDFC	0.05	-0.02	0.89	4.95	9.43
ICICI Prudential	0.24	-0.06	0.83	4.89	9.30
Kotak	0.15	-0.17	0.42	4.42	8.87
LIC	-0.05	-0.46	0.05	3.94	9.51
Reliance Capital	0.24	0.08	0.94	5.44	8.96
SBI	0.18	-0.11	0.81	4.74	8.81
UTI Retirement Solutions	0.19	-0.13	0.76	4.77	8.68

Table :4 NPS Cumulative Returns Corporate Debt Tier - I

Scheme	1 Month	3 Months	6 Months	1 Year	3 Year
HDFC	0.05	-0.05	0.74	4.95	9.08
ICICI Prudential	0.29	-0.01	0.93	4.94	9.44
Kotak	0.27	0.07	0.60	4.59	9.19
LIC	0.29	-0.01	0.93	4.94	9.44
Reliance Capital	0.28	0.15	1.06	5.01	9.01
SBI	0.21	-0.09	0.74	4.81	8.81
UTI Retirement Solutions	0.19	-0.26	0.62	4.69	8.85

Table :4 Risk- Return, Sharpe Ratio of the Equity Tier –I and Tier -II

Scheme	Tier- I		Tier -II		Sharpe Ratio	
	Returns	Std Deviation	Return	Std. Deviation	Tier -I	Tier- II
HDFC	3.33	2.33	3.46	2.32	1.43	1.46
ICICI Prudential	3.08	2.55	3.35	2.29	1.21	1.21
Kotak	3.46	2.32	3.08	2.55	1.49	1.49
LIC	2.95	2.31	2.85	2.25	1.27	1.27
Reliance Capital	3.2	2.45	3.21	2.43	1.33	0.32
SBI	3.15	2.32	3.02	2.23	1.35	1.35
UTI Retirement Solutions	3.24	2.44	3.25	2.45	1.33	1.33

Table :5 Risk- Return, Sharpe Ratio of the Corporate Debt Tier –I and Tier -II

Scheme	Tier- I		Tier -II		Sharpe Ratio	
	Returns	Std. Deviation	Return	Std. Deviation	Tier -I	Tier- II
HDFC	0.73	0.99	0.73	1.01	0.72	0.72
ICICI Prudential	1.71	0.99	0.71	1.01	0.71	0.69
Kotak	0.65	1.16	0.66	1.14	0.56	0.58
LIC	0.64	1.11	0.61	1.16	0.57	0.53
Reliance Capital	0.73	0.99	0.8	0.98	0.73	0.81
SBI	0.68	1.08	0.69	1.16	0.63	0.64
UTI Retirement Solutions	0.68	1.04	0.69	1.01	0.65	0.69

All the NPS – E (Tire – I and Tier –II) offered by SBI, LIC, UTI, ICICI, Reliance, Kotak & HDFC gives a positive return compared with the risk free rate of return (i.e., bank rate) for the first year, the variation in the return between the companies are very close. The highest is HDFC got the return of 28.89% and the lowest is 25.49% by LIC, for the one-year period.

All the NPS – C (Tier –I and Tier –II) offered by the pension fund managers most of the fund are generating negative returns for 1 month and 3 months period. The returns generated by this funds are less than the NPS –E category.

The Kotak NPS –E Tier – I is offering highest return of 3.46% and for Tier- II ICICI With 3.35% . For NPS – C Tier –I ICICI prudential is having highest return of 1.71% and for Tier-II SBI and LIC is offering highest return of 1.16%.

The Sharpe performance Index for NPS- E and C for all companies are giving positive index for the one year period.

Conclusion: Though it was thrown open to the public eight years ago, investors started showing interest in the National Pension System (NPS) only two years ago. Almost 80% of the 4.39 lakh voluntary subscribers joined the scheme only in the past two years. Also, 75% of the 5.85 lakh corporate sector investors joined NPS in the past four years. Clearly, these investors have been attracted to the NPS by the tax benefits offered on the scheme. Four years ago, it was announced that up to 10% of the basic salary put in the NPS on behalf of the individual would be tax free. The benefit under Sec 80CCD(2d) led to a jump in the corporate NPS registrations. The number of subscribers shot up 83% from 1.43 lakh in 2012-13 to 2.62 lakh in 2013-14.

Then two years ago, the government announced an additional tax deduction of Rs 50,000 under Sec 80CCD(1b). The number of voluntary contributors shot up 148% from 86,774 in 2014-15 to 2.15 lakh in 2015-16. It turned into a deluge after the 2016 Budget made 40% of the NPS corpus tax free, with the number of subscribers in the unorganized sector more than doubling to 4.39 lakh in 2016-17. In the present budget 2018, 40 percent of the total amount payable to the National Pension System (NPS) subscriber on closure of his account or on his opting out in case of non-employee subscribers. The tax benefit for non-salaried individuals will now be at par with salaried.

These numbers are as encouraging as they are worrying. They indicate that tax savings, and not the product features, define the flow of investments in India. This is also the reason why investors blindly buy low-yield life insurance policies every year, unmindful of the poor returns earned from these plans.

The tax benefits have generated a lot of interest in the NPS. But many investors are not able to decide which pension fund they should invest in. The problem is further compounded by the fact that the NPS investments are spread across 2-3 fund classes. A conservative investor would put 20% in stocks, 30% in corporate bonds and 50% in gilts. A balanced allocation would put 33.3% in each of the three classes of funds while an aggressive investor would invest the maximum 50% in the equity fund, 30% in corporate bonds and 20% in gilts.

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