

**AGENDA MANAGEMENT SHEET**

**Name of Committee** Pension Fund Investment Board

**Date of Committee** 31 July 2006

**Report Title** Asset Allocation

**Summary** The report considers options on asset allocation.

**For further information please contact:** Phil Triggs  
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**Would the recommended decision be contrary to the Budget and Policy Framework?** No.

**Background papers** Reports from fund managers

**CONSULTATION ALREADY UNDERTAKEN:-**

Details to be specified

- Other Committees  .....
- Local Member(s)  .....
- Other Elected Members  Cllr Davis, Chair of Pension Fund Board
- Cabinet Member  .....
- Chief Executive  .....
- Legal  Tony Maione
- Finance  David Clarke, Strategic Director of Resources (reporting officer)
- Other Chief Officers  .....
- District Councils  .....
- Health Authority  .....
- Police  .....
- Other Bodies/Individuals  .....

**FINAL DECISION YES**

**SUGGESTED NEXT STEPS:**

Details to be specified

- Further consideration by this Committee  .....
- To Council  .....
- To Cabinet  .....
- To an O & S Committee  .....
- To an Area Committee  .....
- Further Consultation  .....

## Agenda No

# Pension Fund Investment Board 31 July 2006

## Asset Allocation

### Report of the Strategic Director of Resources

#### Recommendation

That the Fund invest a minimum of 5% in each of the alternative asset classes (Hedge Funds and Property), making a 10% allocation to alternatives in total.

#### 1. Introduction

- 1.1 Asset allocation is the distribution of investments across different asset classes such as equities, bonds, property, etc. The asset allocation decision is key in relation to the level of risk that the Fund adopts in respect of its investment objective, namely to achieve a long term return of 1% above a world markets (or other appropriate) benchmark return in order to be at or above a 100% funding level.
- 1.2 The rationale of moving away from the traditional equity and bond asset classes is to create diversification and reduce the impact of individual asset class volatility. Ideally investors would like to see a smooth appreciation of assets over time to help meet their funding objectives.
- 1.3 Throughout this process, the Council has been advised by Mercer Investment Consulting.

#### 2. Current Asset Allocation at 30 June 2006

- 2.1 **Appendix A** shows the current asset allocation at 30 June 2006 and the recommended asset allocation following the move to alternative assets.

#### 3. The Move to Alternative Assets

- 3.1 Having made a decision to commit to Alternative Assets, it is important to ensure that a sufficient proportion of assets is allocated in order to ensure that full diversification can be achieved. It is difficult to argue how allocations of 1 and 2% can have a material impact on diversifying the source of investment returns. In this case, the performance of the overall fund will still be driven by the asset class that makes up the large majority of the assets.

- 3.2 A recent survey of European Pension Schemes conducted by Mercer Investment Consulting indicates that the median allocation to Property and Hedge Funds, where schemes have elected to invest, is just under 7% on both asset classes. The survey asked what future plans pension schemes had in relation to Alternative investments and the trend was to increase allocations further. In relation to Hedge Funds, those schemes that already invested were looking to increase their exposure from 7% to 10%.
- 3.3 Concerning the performance of Hedge Funds, there will be periods when they will under-perform equity markets, given the absolute return strategies that they are seeking to generate. Mercer would continue to advocate that, as part of the process of diversification, Hedge Funds still have a role to play, particularly in a period of falling markets, when their ability to take short positions, should prove positive.
- 3.4 Mercer has highlighted previously that the approach to Hedge Fund and Property investing should be via the Fund of Funds route and, as such, there will be exposure to a large number of individual strategies, thereby diversifying risk further.

#### **4. Recommendation**

- 4.1 It is recommended that the Fund invest a minimum of 5% in each of the alternative asset classes as previously discussed, making a 10% allocation to alternatives in total. This recommendation is based on the fact that a smaller allocation is not likely to have a material impact on the overall performance and therefore it will not create the diversification that is being sought from a move away from equities.
- 4.2 The allocation to alternatives would form part of the 'return seeking' assets, which have traditionally been purely equities.

DAVID CLARKE  
Strategic Director of Resources

Shire Hall  
Warwick  
July 2006

## Warwickshire Pension Fund – Proposed Asset Allocation

Asset Class	Index – Tracker	UK Equity Specialists	Global Equity Specialists	Alternative Assets	Fixed Income	Total
UK Equities	2.00	27.00	3.50			32.50
Overseas Equities	10.00		22.50			32.50
European	7.50		5.50			13.00
North American	1.25		8.50			9.75
Far East/Emerging Markets	1.25		8.50			9.75
Property				5.00		5.00
Hedge Funds				5.00		5.00
UK Corporate Bonds	2.00				8.00	10.00
UK Fixed Interest	2.00				8.00	10.00
UK Index-Linked	5.00					5.00
<b>Total</b>	<b>21.00</b>	<b>27.00</b>	<b>26.00</b>	<b>10.00</b>	<b>16.00</b>	<b>100.00</b>

## Warwickshire Pension Fund – Existing Asset Allocation

Asset Class	Index – Tracker	UK Equity Specialists	Global Equity Specialists	Fixed Income	Total
UK Equities	2.00	32.00	3.50		37.50
Overseas Equities	11.00		26.50		37.50
European	8.50		6.50		15.00
North American	1.25		10.00		11.25
Far East/Emerging Markets	1.25		10.00		11.25
UK Corporate Bonds	2.00			8.00	10.00
UK Fixed Interest	2.00			8.00	10.00
UK Index-Linked	5.00				5.00
<b>Total</b>	<b>22.00</b>	<b>32.00</b>	<b>30.00</b>	<b>16.00</b>	<b>100.00</b>