

Multi-asset solution



Public pension plan delegates asset allocation decisions (within limits)

Client case study



The organization

A metropolitan pension plan serving several hundred current and retired police officers. In total, the Plan oversees the management of roughly \$70 million in pension assets. As with many public plans, the pension's funded status stood at less than 50%, and asset growth to better fund Plan liabilities is a priority for the Board of Directors.

Challenge 1: Resource limitations

The Plan's Board of Directors is comprised of public servants who, while representative of plan beneficiaries, have limits in both investment expertise and in the amount of time they can dedicate to managing the Plan. As a Russell Investments client for more than 25 years, the Board had already delegated manager selection, oversight, and many other aspects of plan administration to Russell Investments. They did not, however feel that their quarterly meeting schedule allowed for the timely implementation of our advice on potentially advantageous asset allocation shifts.

Challenge 2: Increasing complexity

The Board felt strongly that the investment environment had changed since five years prior. Given increased market volatility, economic uncertainty, and the introduction of attractive (but increasingly complex) investment strategies, the Board became convinced that asset class restrictions within their investment policy were further constraining both return-seeking and risk-hedging opportunities.

A strategic solution

After exploring these concerns with the Board, Russell Investments proposed a new framework for managing the Plan's portfolio: a multi-asset strategy. Under this new paradigm, the Board would delegate a degree of control over asset allocation decisions for the majority of the "return-seeking assets" in the portfolio. Russell Investments would then dynamically manage this portfolio on a daily basis to react to market conditions with a level of care and attention that would simply not be possible under the Plan's previous method of management through quarterly meetings.

Two key aspects of the multi-asset solution appealed to the Board:

1. Nimble, real-time implementation. Some of Russell Investments' best investment ideas, and
2. Risk management at the total portfolio level.

Not surprisingly, this recommendation raised a few questions.

The Board's questions about implementing a multi-asset strategy included:



1. How would a multi-asset strategy differ from our current approach?
2. How would fees be impacted?
3. What risk management controls would be put in place?
4. How much transparency/visibility into the Plan's holdings would we have?
5. How would liquidity be affected?
6. How would the new investment portfolio compare to the existing portfolio?



1. How would a multi-asset strategy differ from our current approach?

As a long-term outsourcing client, the Board was already comfortable with the responsibilities previously delegated to Russell Investments: manager monitoring, hiring, firing, and daily management of many aspects of the Plan between quarterly Board meetings. These practices would continue under the proposed multi-asset arrangement, but Russell Investments would also now be given responsibility for shifts between asset classes (within clearly defined boundaries) that would enable our portfolio managers to:

- Act on perceived market opportunities to help improve returns, and
- Adjust the portfolio to help decrease downside risk in times of market stress.

As part of the proposed multi-asset solution, one highly diversified multi-asset fund would replace the Plan's investments in 10 individual funds representing 60% of the Plan's portfolio and would be managed daily by dedicated portfolio managers.

The Board liked this approach for multiple reasons. It matched their thinking that Russell Investments—as the investment expert—was best positioned to make specific allocations to asset classes within their return-seeking portion of the Plan's portfolio. They also liked that our portfolio managers would be able to implement their best thinking in real-time and in response to changing market conditions without the delay of waiting for the next Board meeting.



2. How would fees be impacted?

As plan fiduciaries, the Board was certainly concerned about cost. Implementing the multi-asset strategy, however, proved to cost slightly less than the Plan's current fees.



3. What risk management controls would be put in place?

From a governance perspective, the amount of additional discretion being granted to Russell Investments would be clearly defined within the Plan's investment policy statement: discretionary investment bands would allow Russell Investments 3% leeway in changing the allocation to specific asset classes. Through long experience, the Board was already comfortable with our rigorous internal governance and investment discipline, and these would remain unchanged in the new multi-asset framework. The Board also liked that they would maintain control of their total risk tolerance, and could easily adjust the ratio of return-seeking to capital preservation assets. The Board retained responsibility of strategic oversight for both the Plan and Russell Investments, but effectively hired Russell Investments as a portfolio manager to oversee and optimize—on a daily basis—the majority of the Plan's return-seeking assets.



4. How much transparency/visibility into the Plan's holdings would we have?

The multi-asset solution provides the same daily pricing and reporting transparency as the investment holdings it would replace. This includes transparency into the underlying asset classes, underlying managers, and monthly reporting of underlying securities holdings.



5. How would liquidity be affected?

Portfolio liquidity would not be affected by the multi-asset solution. The proposed multi-asset fund is priced and traded daily. The Board retained control of any opportunistic/less liquid allocations.



6. How would the new investment portfolio compare to the existing portfolio?

For a typical defined benefit plan, the implementation of a multi-asset strategy means:

1. Discretionary investment bands granting Russell Investments 3% leeway in changing the allocation to specific asset classes.
2. An official appointment of Russell Investments as an investment advisor responsible for assisting the Board in the areas of asset allocation, portfolio strategy implementation, performance monitoring and evaluation, and implementation of rebalancing policy.
3. The addition of a new investment policy appendix specifically dedicated to the strategic role of the return-seeking portion of the portfolio, and addressing investment strategies, objectives, monitoring and control.

For this Plan, the biggest change was adjusting their non-U.S. exposure. The Board understood the benefits of having an increased strategic allocation to a broader opportunity set, but they wanted to consider the timing of making an adjustment. Ultimately, they decided that the recent relative underperformance of non-U.S. developed and emerging markets equities combined with then favorable non-U.S. valuations made this an opportune time to bring the portfolio closer to the current global market cap weighting.

Summary

The Board chose to implement the proposed multi-asset solution, seeing it as the next logical step in the evolution of investment outsourcing. Russell Investments had provided the Plan with asset allocation advice and daily plan administration for decades. The Board viewed the multi-asset approach as a more nimble way to marry strategic advice with the daily management of the Plan's portfolio.

Results

By delegating some asset allocation decisions to Russell Investments and adopting a multi-asset approach, the Plan:

- Positioned the portfolio to react to market events in real time, as opposed to once per quarter
- Further diversified the Plan's equity exposure by bringing it in line with the global market cap
- Reduced total Plan fees
- Further engaged investment experts in the daily management of the Plan, allowing the Board to re-focus on strategy and oversight

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Important information

This case study represents a unique situation faced by a metropolitan pension plan seeking to delegate asset allocation decisions due to resource limitations and increasing complexity. Case studies are problem-solving stories. We select a situation that is indicative of problems clients in this category are facing. The recommendations described do not represent a standard strategy or set of recommendations made for all advisory clients with similar issues. Each client has unique requirements, challenges, and constraints, and our advisory solutions are tailored to each client's specific needs. Every client's situation, experience and needs are different, and Russell Investments does not imply that the solution herein is appropriate for any other client.

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