

Considering the alternatives

PETER DAVY TALKS TO MARTIN ROTH, HEAD OF ASSET MANAGEMENT AT PENSIONS KASSE MANOR ABOUT ASSET STRATEGIES AND THE FUND'S ALTERNATIVES PORTFOLIO

Martin Roth is head of asset management at Pensionskasse MANOR, the pension fund of Switzerland's biggest department store chain. "We are a Swiss Debenhams or Macy's," he says.

It has around 8,800 active employees in the fund, two thirds of them female, and about 3,900 retirees. With assets of CHF 1.7 billion, the technical coverage ratio is 112 per cent. The fund is one of those that has made a deliberate break with Swiss bonds.

Tell me about your asset strategy?

We have just revised it, and have done so quite regularly in the last five years because of the challenging environment. Our new asset allocation as of 1 January 2016 is around 10 per cent in bonds, much lower than the average Swiss pension fund; our equity portion is about 33 per cent – more or less the same as others; similarly, we have 26 per cent in real estate; and a large part in alternatives.

What prompted the move out of bonds?

We started strongly reducing our exposure to bonds about four years ago, when we had around a 30 per cent allocation. The decision was mainly due to the asymmetric risk-return profile of them. If you look at asset allocation models, bonds may still have the lowest risk, but on the other hand the risk is not symmetric. The risk of having a very low or even negative yield in bonds is far higher than the possibility of achieving the return of 2.8 per cent we need to hold our coverage ratio steady.

What does the alternatives portfolio look like?

The main part is hedge funds, where we have 11 per cent. Two thirds of that is a stress-absorbing portfolio with exposure to macro managers, commodity managers, relative value and CTA managers. Only a third is mainly directional – mostly equity long short. We have no credits in the portfolio and the correlation to the bond portfolio is very low.

The rest of the portfolio is made up of private equity, with 3.5 per cent, where we try to achieve a premium of around 3 per cent per annum over the public markets, and also infrastructure, where we tend to invest more in the brownfield area; the goal is to be a bond proxy and generate cash flows, rather than realise capital gains.

What are the returns expected to look like compared to bonds?

Swiss bonds are currently yielding zero and we require them to return 3 per cent, so we would like to gain at least a premium of 200 to 400 basis points compared to Swiss bonds.

Are you worried by the extra risk?

It's something we looked at closely, but we didn't really increase the overall portfolio risk by a massive amount. If we had increased the equity portion significantly – as some other pension funds have done – the story might be different.

Even so, one has to take particular care about the liquidity of those investments. The liquidity of the portfolio was one of the main guidelines during the portfolio construction and manager selection. It was also one of the reasons the private equity allocation did not increase.

Would you expect other funds to follow your example?

It is difficult to say. We are a family-run business, and the board has an entrepreneurial approach to managing money. If you look at government-linked pension funds and those of listed companies, they tend to be less progressive. They are often focused on issues such as the impact of the fund on the company balance sheet or the reputational risk.

Will all this be enough to ensure an adequate funding ratio?

The required return is 2.8 per cent, but with our asset allocation model the expected return is 2.3 per cent, so there is still 0.5 per cent missing. Consequently, we are also in the process of working on the liability side, whether that is increasing the retirement age or reducing the conversion ratio. You need a balance; you cannot have a liability side where you need to earn 2.8 per cent and an asset side that brings in only 2.3 per cent.

Even though your technical funding ratio is 112 per cent?

Yes, that's typical for Switzerland. If we were to discount at the market rate we would be below 100. The technical discount rate is not something that makes the Swiss pension system very transparent. ■