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Investment & Actuarial Consulting,  
Controlling and Research. [www.ppcmetrics.ch](http://www.ppcmetrics.ch)



## Investment Consulting

# Investing in Alternatives – What Are Swiss Pension Funds Considering?

**EPFIF**

Some of the graphs/pictures are not available online

**PPCmetrics AG**

Dr. Diego Liechti, Senior Investment Consultant

Zürich, June 15, 2017



# Structure Of My Talk

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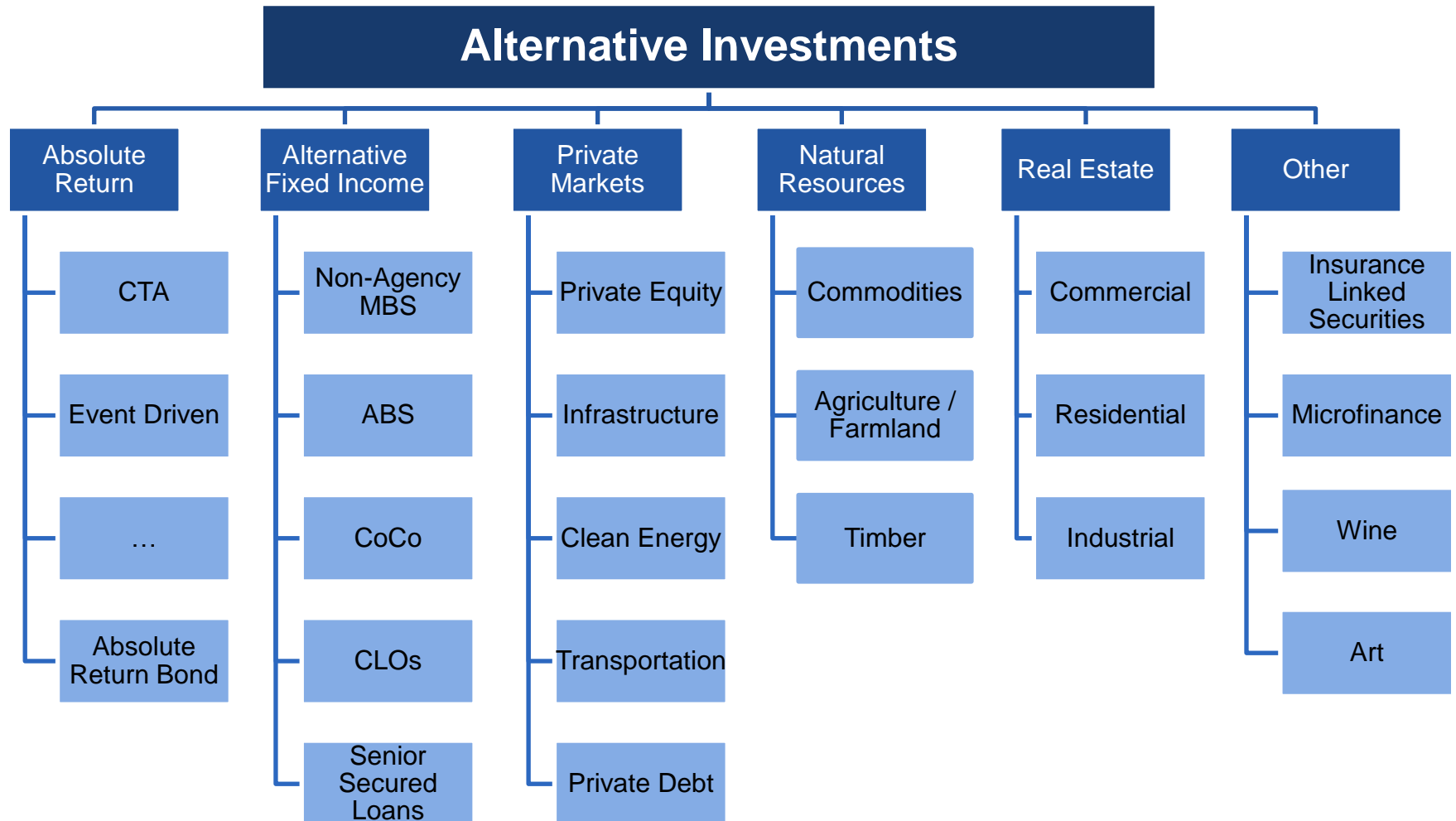
- Introduction
- The «Menu»
- What Are Swiss Pension Funds Doing?
- A Look Abroad: Yale Endowment
- What Are Swiss Pension Funds Considering?
- Questions To Be Answered Before Investing
- Take-Aways

An alternative investment is an asset that is **not one of the conventional investment types**, such as stocks, bonds and cash. Most alternative investment assets are **held by institutional investors** or accredited, high-net-worth individuals because of the **complex natures** and **limited regulations** of the investments.

Source: <http://www.investopedia.com>

- What are typical alternative investments?
- How do pension funds invest? What are they considering?
- How should you evaluate them?

# The «Menu» Overview

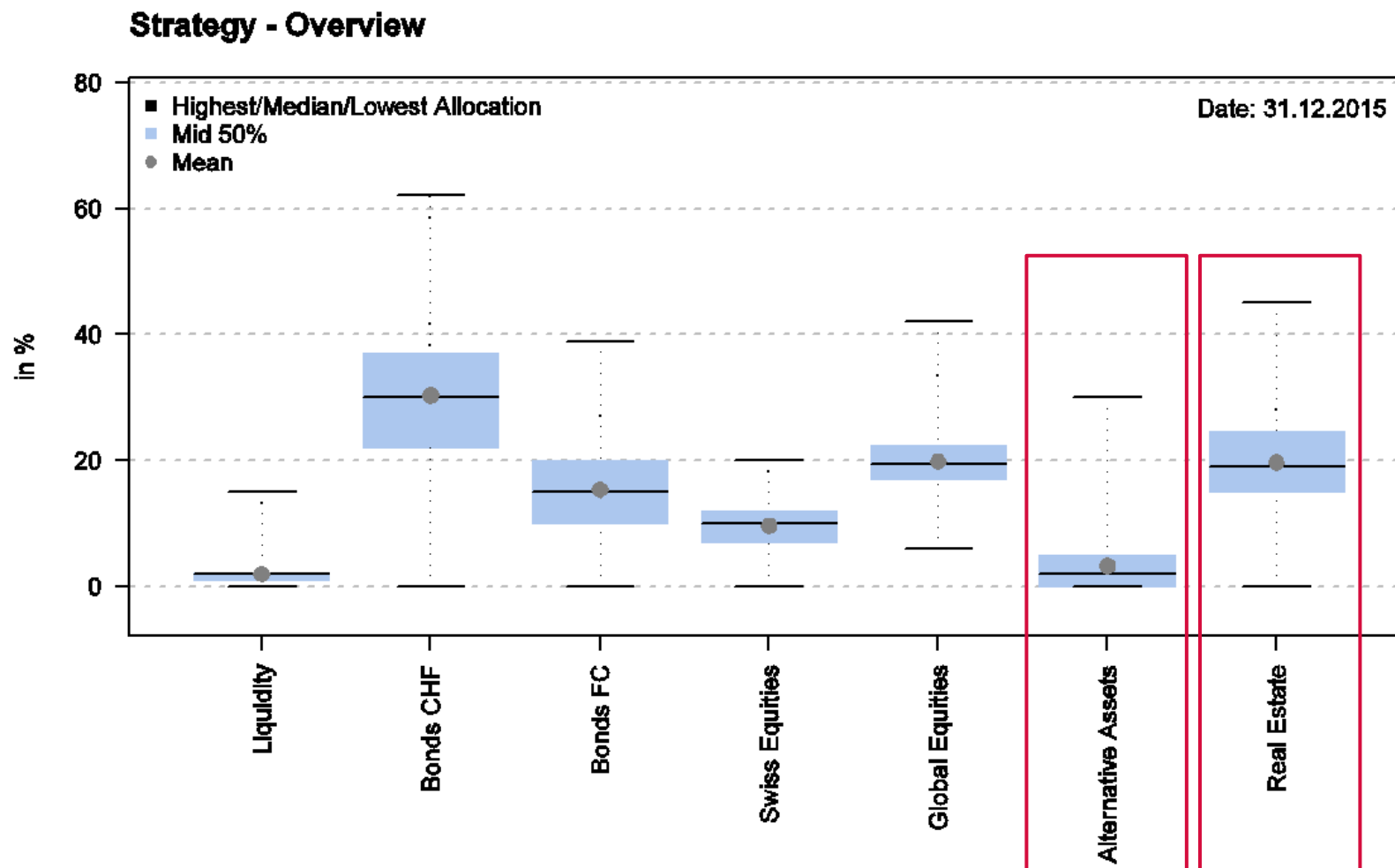


# The «Menu» Growth Story

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# What Are Swiss Pension Funds Doing?

## Diversity In Asset Allocation?

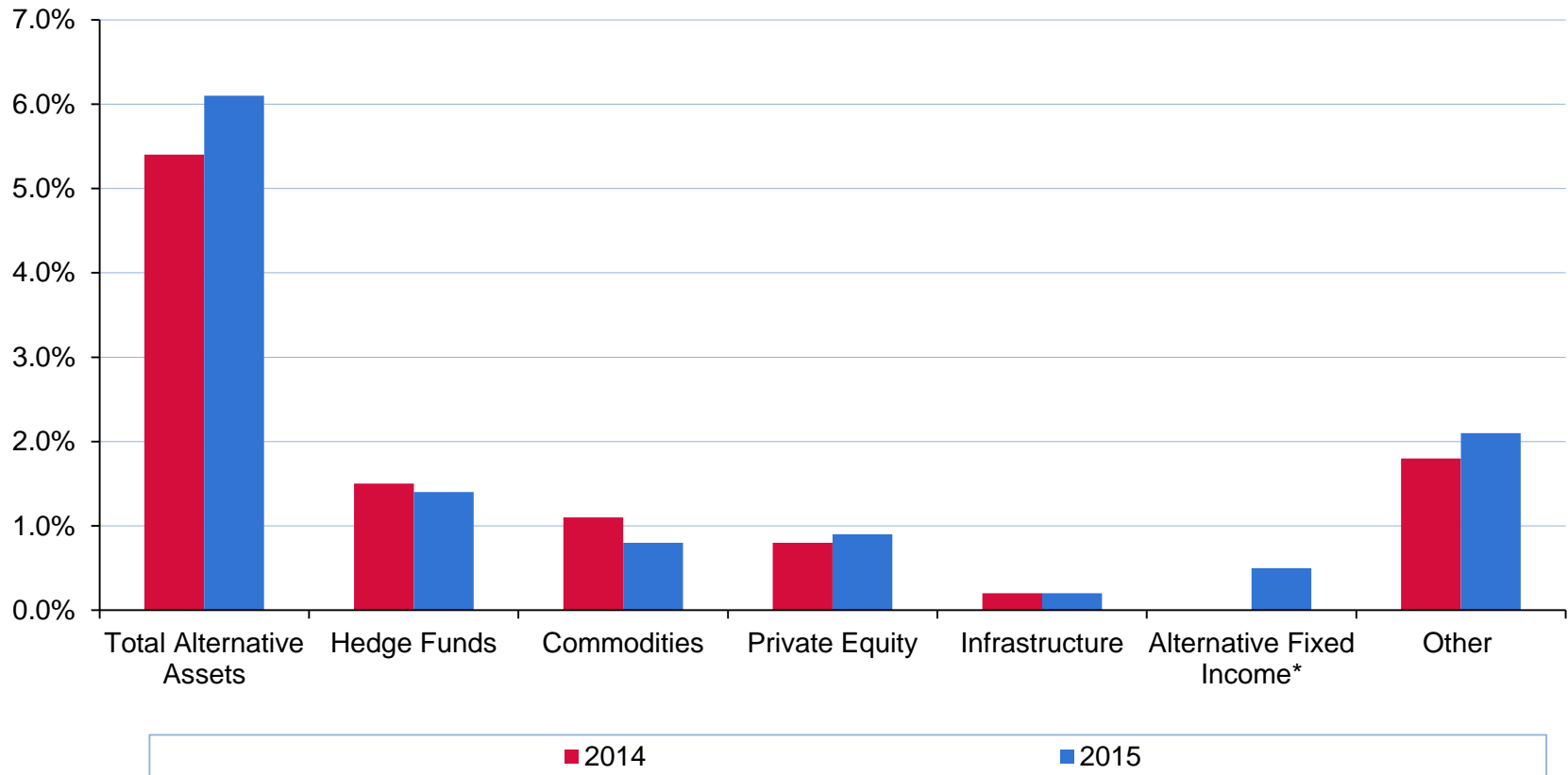


© PPCmetrics AG Number of pension funds: 157 / Pension fund assets according to art. 44 BVV 2 as at end of period in m of CHF: 301'478

# What Are Swiss Pension Funds Doing?

## Alternative Asset Allocation

### Alternative Assets according to Strategy



\* No data before 2015

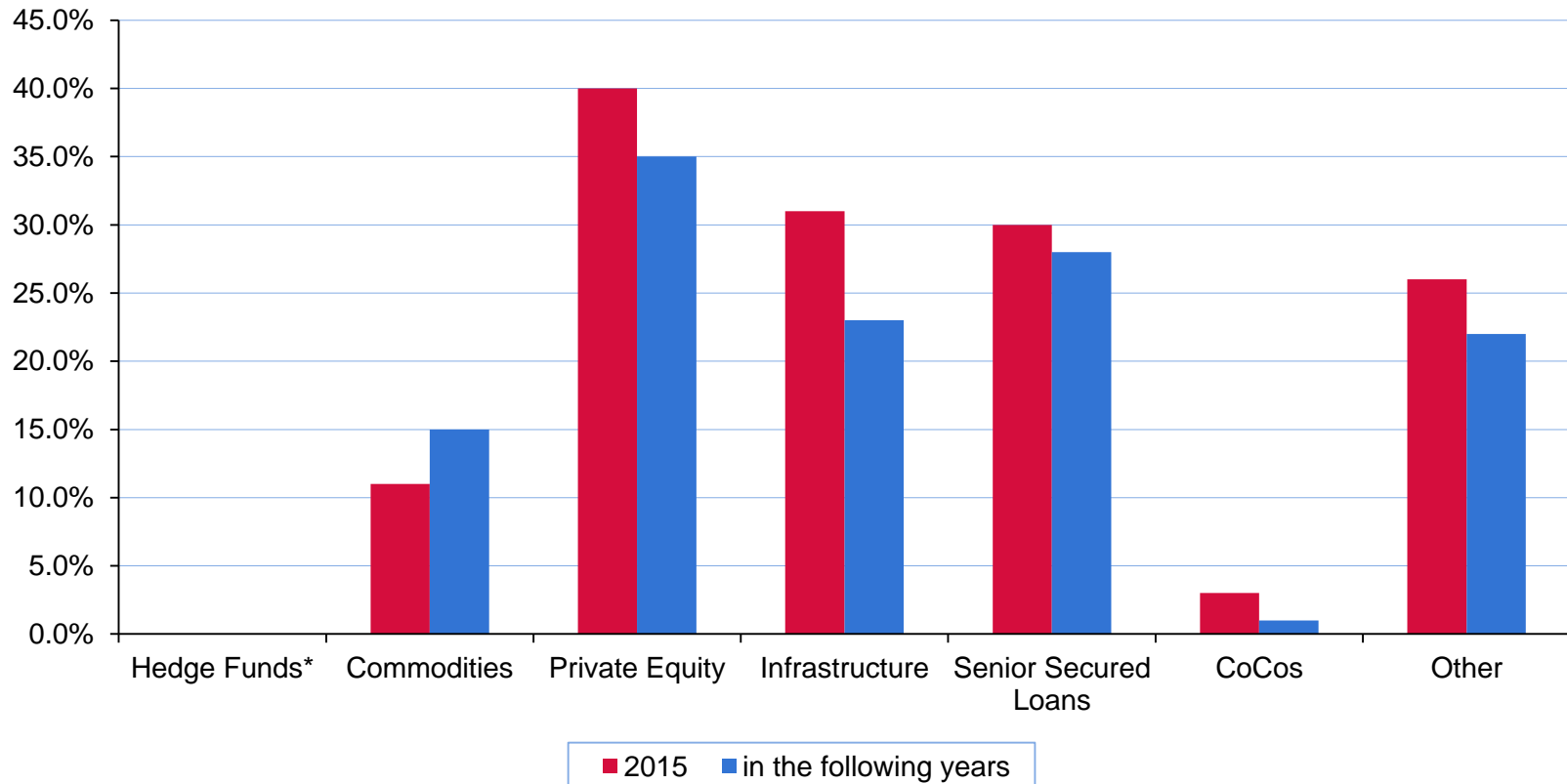
Source: Swisssanto Pensionskassenstudie 2016



# What Are Swiss Pension Funds Doing?

## What Type Will Be Increased?

### What kind of alternative assets will be increased?



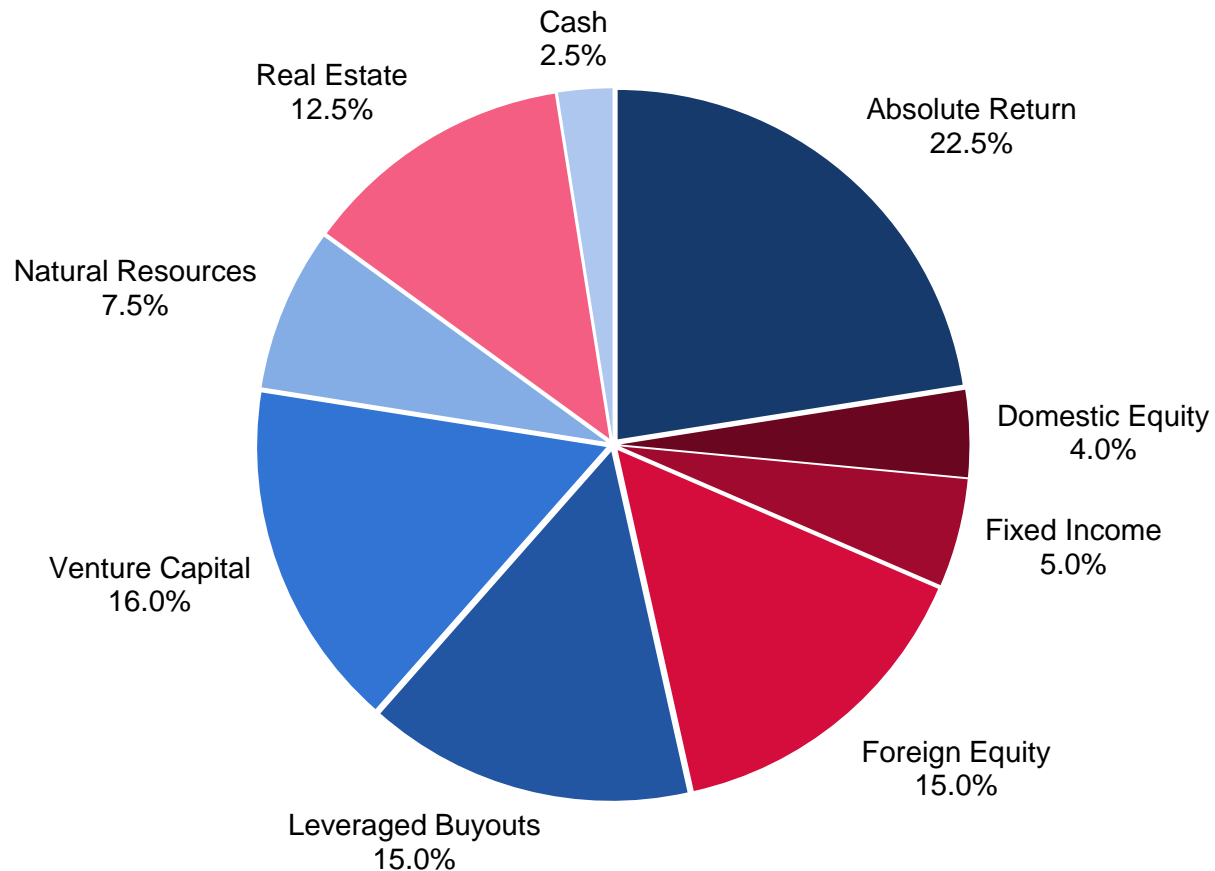
\* No systematic mentioning

Source: Swissscanto Pensionskassenstudie 2016

# A Look Abroad

## The Yale Endowment: Target Allocation

### The Yale Endowments' 2016 target allocation



Source: Yale

## The Yale Endowment: What About Swensen's Personal Philosophy?

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According to **unconventional success: A fundamental approach to personal investment**:

- Construct a portfolio with to the following **6 asset classes**: Domestic Equities, U.S. Treasury Bonds, Inflation Linked Bonds, Foreign Developed Country Equity, Emerging Market Equity and Real Estate
- **Rebalance regularly**
- In the **absence of confidence in a market-beating strategy**, invest in **low-cost index funds**.

**How does this fit with Yale's strategic asset allocation?**

# A Look Abroad

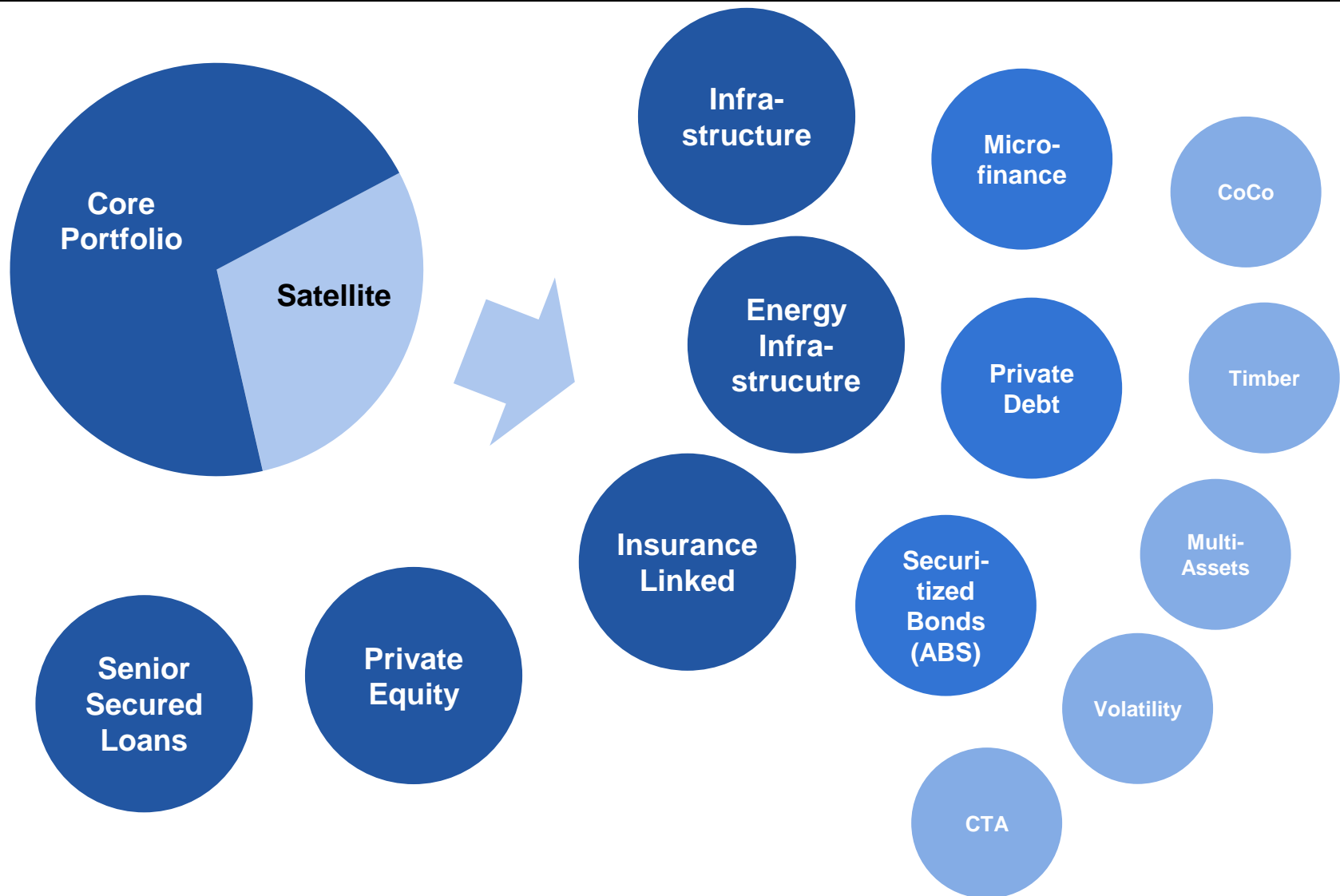
## The Yale Endowment: Performance Attribution

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**Added Value of Alternative Assets?**

# What Are Swiss Pension Funds Considering?

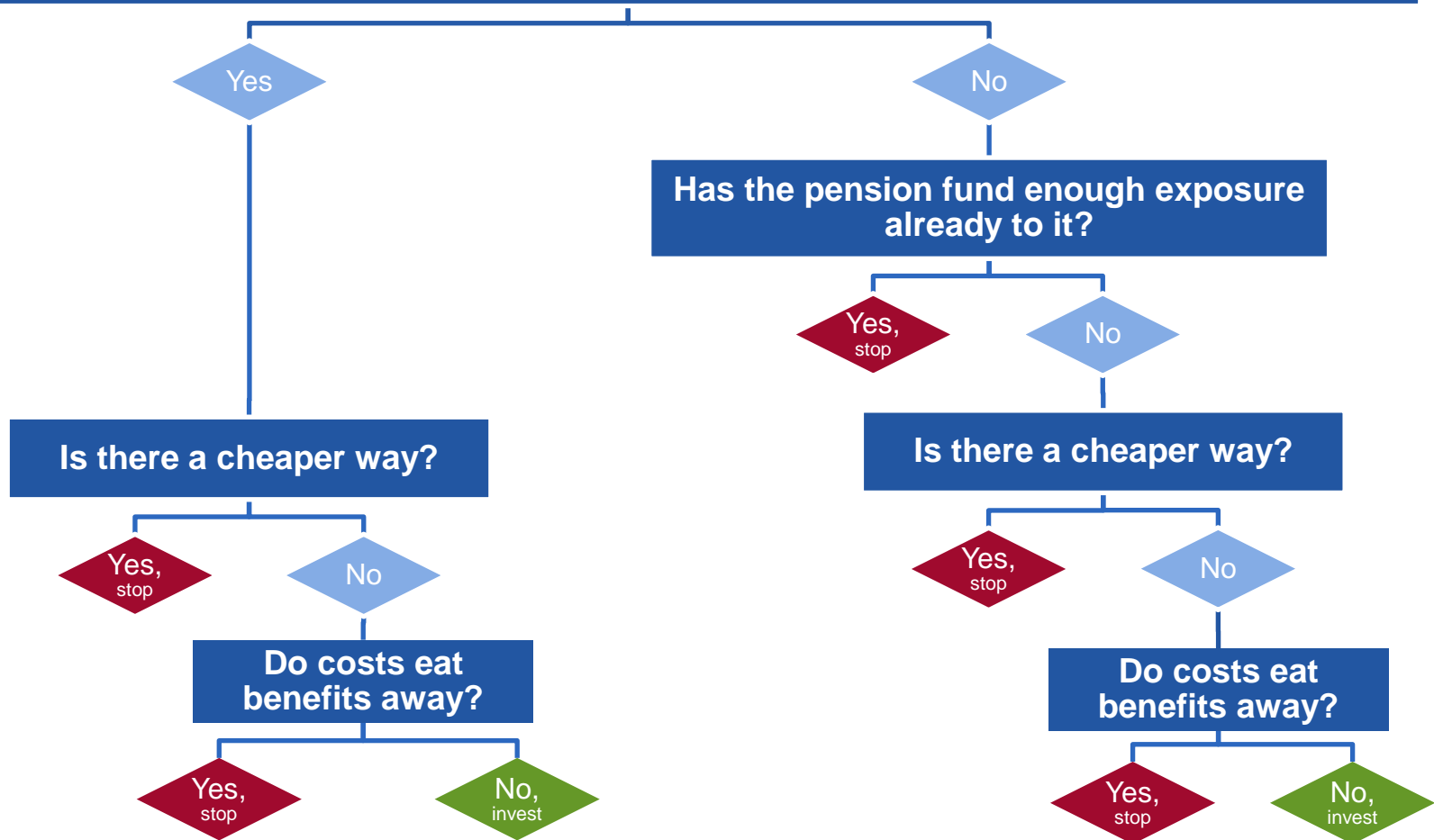
## «Hot Topics»



# What Are Swiss Pension Funds Considering?

## Questions To Be Answered: General Approach

Is the risk premium / «alpha» unique in the asset allocation of the pension fund?





# What Are Swiss Pension Funds Considering?

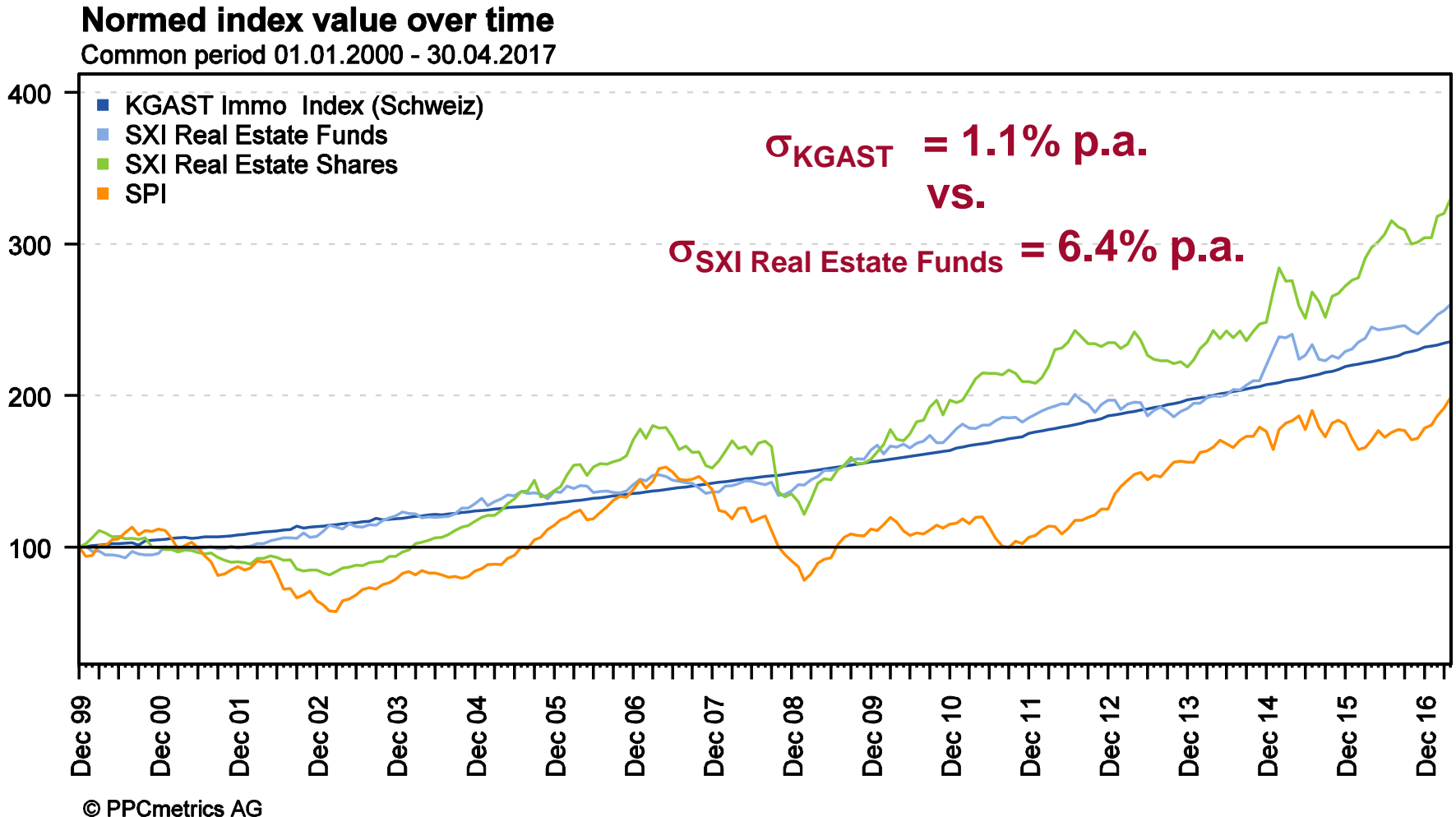
## Questions To Be Answered: Example Private Equity

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- Private Equity returns can be **decomposed into**:
  - **Equity Risk Premium**
  - **Small Cap Risk Premium**
  - **Illiquidity Premium**
  - **«Alpha» (?)**
- Does the pension fund have **enough exposure to those premia**?
  - Is there already exposure to small cap equity, private debt, (unlisted) real estate, ... ? Is there an alpha?
- Can the pension fund invest in the asset class in **an efficient way**?
  - Management fee, costs from operational set-up, or monitoring

# What Are Swiss Pension Funds Considering?

## Watch Out: Illiquidity (1)



# What Are Swiss Pension Funds Considering?

## Watch Out: Illiquidity (2)

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**Performance  
measurement and  
benchmarking**

**Less flexibility  
(tactics!)**

**Legacy for  
successor**

**Patience and  
long breath**

**Problems with  
rebalancing**

**Run for illiquid  
investments reduces  
premium**

**Measurement problems  
(i.e., returns, volatility,  
correlations)**

# What Are Swiss Pension Funds Considering?

## Watch Out: Problem Of Self-Selection

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e.g., IRR Marketing

# What Are Swiss Pension Funds Considering?

## Watch Out: Fee Structure

- **Example: Catch-up in Private Equity**

- Return of 12% p.a. (after management fee)
- Carried interest 20% after a hurdle rate of 8%

	100% Catch-up		No Catch-up	
	LPs	GP	LPs	GP
First 8%	8%		8%	
Next 2%		2%	1.6%	0.4%
Remaining 2%	1.6%	0.4%	1.6%	0.4%
<b>Total</b>	<b>9.6%</b>	<b>2.4%</b>	<b>11.2%</b>	<b>0.8%</b>

- **Fees can be much higher depending on «small» details such as a catch-up. <sup>1</sup>**

\* In this example roughly 60%, assuming a management fee of 2%

# Take-Aways

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1. There are **many alternative investments** worth considering.
2. Evaluation of alternatives should be done **with care**.
3. Be critical and **avoid major pitfalls**.
4. And remember Swensen's advice as well as:

Boring assets provide better risk-adjusted returns than speculative peers. One explanation is the lottery ticket story. ... another explanation is the leverage aversion.

Antti Ilmanen

Source: Journal of Investment Consulting





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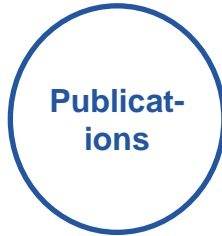
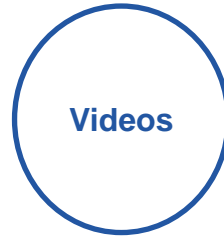
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