Finding the right level

Founded in 1961, Inarcassa began life as the state-run pension fund for Italian Architects and Engineers. It was privatised in 1995 and its revolutionary approach to restructuring its asset management department since has seen it remain at the helm of Italy's pension fund system and a worthy winner of several IPE Awards, not least this year's country award for Italy.

A SPECIAL TOUCH

So what exactly has Inarcassa done to overhaul its asset management so successfully? "Our investment process basically been shifted from balanced mandates to specialised mandates over seven years ago," the scheme explains.

At the centre of the Inarcassa investment process is a diversified strategic asset allocation (SAA) policy which is based on asset classes that can be defined by the most representative, transparent and replicable indexes. To complement the SAA, Inarcassa has also adopted a tactical asset allocation policy to take care of currency hedging and the exposure to different currencies its investments incur. "This takes the form of a currency overlay model which is implemented by our new depositary bank," the fund says.

To increase portfolio diversification and improve its efficiency and robustness, Inarcassa implements a top- down methodology to define its asset allocation and determine the type of specialised investments it needs to make.

LEVELLING OUT

This is done at several levels. First there is the asset class level. Inarcassa says its current SAA contains six asset classes: fixed-income; equities; real estate; inflation-linked bonds; alternatives, and cash. These are split into 13 sub-classes that form the second level. Third, specialist classes have been introduced to split the sub-classes further at the next level. An example of this is Inarcassa's recent introduction of specialist infrastructure investments as part of its private equity sub-class, which is part of the alternatives main class.

Implementing and maintaining such a diversified approach is, however, not easy, but Inarcassa claims to have found the solution. "To maximise efficiency, transparency and monitoring, we have chosen to invest through specialised instruments, such as mandates, funds, exchange traded funds, direct investments, and so on, both for the active management and passive management areas."

For most of the asset classes Inarcassa invests in, it uses a core-satellite approach, with the core constructed in the main from passive, low-commission vehicles such as exchange-traded funds, passive asset managers, futures and investible indices. Alternatively, it invests directly through its finance department which uses a best execution policy pitting the various brokers against each other.

ACTIVE VERSUS PASSIVE

For the more efficient markets, such as US bonds, US equities and European equities, much of the portfolio will be beta-driven and thus managed passively. For the more inefficient markets, however, Inarcassa says it prefers active management as this generates greater alpha. Examples include emerging market equities, emerging market debt, and high-yield bonds.

But the philosophy doesn't end there. Inarcassa is determined to find the best vehicles for its wide range of mandates and investments. "For the passive management, for example, we run searches to find the best tools to use and then within the tools themselves, the best-in-class. So we ask ourselves questions like: are US equities best managed through exchange traded funds for their liquidity or trusts because they offer lower fees?" Inarcassa explains. Similarly, it will look at which index is best. According to Inarcassa, the S&P500 is renowned for its long history while the Russell 1000 makes use of a wider basket of potential investments. Once it answers these questions, it can determine what it feels is the best in class for its investment strategy and objectives.

For its active mandates, Inarcassa says it runs searches through the dedicated teams in its finance department with the support of its adviser, MangustaRisk. "The short list of managers is then drafted by a second adviser whom we appoint according to their area of expertise. It could be in hedge funds, equities, bonds, US focused, European focused. It depends on what we are looking for," it adds. Once this phase of the selection has been completed, a final due diligence phase and interviews are then conducted directly by the scheme's finance department and MangustaRisk.

In the past 18 months, Inarcassa says it has focused on creating a private equity portfolio through various specialised funds representing different areas of the private equity spectrum.

ON TARGET

Inarcassa says its recent activity has seen it almost reach its strategic target with close to 30% of its alternative class now invested in private equity, which represents close to 4.5% of its overall portfolio. "Half of the committed assets have been called and we expect to start redeeming in five years."

Being the pension fund for architects and engineers means Inarcassa can be confident about its investments through private equity in infrastructure – the market its members work in. "As such, we have allocated 50% of our private equity portfolio to infrastructure funds in the US and Europe. We are considering Asia in the future and we created and control 6% of F2i, the third largest infrastructure fund in the world with €2.5bn of equity and €10bn of debt," it boasts. "We sit on the board of directors alongside the other partners, including the partially state-owned Cassa Depositi e Prestiti, Unicredito Italiano, Banca Intesa, Lehman Brothers, Merrill Lynch and eight other banking foundations," it adds. Fine company indeed.

inarCASSA

Name of fund
Inarcassa

Type of fund
Professional

Date established
1961

Fund structure
Defined benefit

Members
Active 131,095
Retirees 11,756
Deferred 3,674

Capital value of fund (€m)
31 Dec 2006 3,772
31 Dec 2005 3,357
31 Dec 2004 2,976

Investment return (%)
2006 4.12
2005 4.56
2004 4.99

Five-year rolling investment return (%)
2002–06 21
2001–05 19
2000–04 20

Highlights and achievements

A CAREFULLY PLANNED AND EXECUTED investment strategy is sure to reap rewards but being bold could bring in that touch more. Inarcassa can claim to be a master of both.

Pigeon-holing each and every investment according to different levels of assets class and sub-class allows the scheme to remain fully in control of the various risk each mandate creates. It also permits it to streamline its allocation and asset management process.

But with the backing of the state removed, finding that bit extra is now crucial. Conscious of the industry it represents and the boldness of its work, Inarcassa has adopted some of that boldness itself and opted for a sustained investment programme in private equity infrastructure and engineering where few others would dare go.

IPE AWARDS 2007