

Bespoke Portfolios
In 10 C ticks, 10 Minutes, 1/10th Cost

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Post Covid-19 Recommendations to SWFs

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SWFs to Revisit Mission Statement

The Mission Statement also called "philosophy of the fund" helps managers understand their mandate. BUT this in itself is no predictor of mission fulfillment.

The Mission Statement is a document describing the basic principles and core values of the fund as well as its general entrusted mission.

* To achieve a long-term investment return on the financial reserves, providing an alternative to oil reserves, which would enable future generations to face the uncertainties ahead with greater confidence while meeting the principal objective of the fund's establishment.*

Ethical Guidelines include:

- Integrity
- Transparency
- Accountability
- Leadership
- Guidance
- Knowledge
- Due Diligence
- Decision Making
- Commitment and Teamwork
- Risk and Resilience
- Stakeholder Engagement
- Strategic Focus
- Active Ownership

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SWFs to Re-examine Charter

The SWF legal status is key since it impacts the fund's formation, performance, liability between actors and applicable law. With many effects of the Covid-19 still to unfold, previous legal status may no longer be relevant. A revision in legal status should consider Santiago Principles to promote transparency, accountability, ensure transparency and foster accountability, ensure transparency and foster accountability.

SWF legal status is an important document that:

- Establishes the Fund
- Indicates the date of its foundation
- Whether it is a government agency, private company, or trust
- Describe the functions of the fund
- Determines liability arising from the management of the fund
- Specifies the legal jurisdiction of the fund
- Specifies the legal status of the fund

Name	Applicable Law	Principles
ADIA (Abu Dhabi Investment Authority)	Specific Mandate	Follow the Royal Family Principles
Norway Government Pension Fund	Public Law, Amendment Act	Follow the guideline described in its mandate
Singapore Investment Corporation	Singapore Companies Act	Commercial Principles in light with Government Guidance
China Investment Corporation	Specific Mandate	Commercial Principles
China Investment Corporation	Specific Mandate	Commercial Principles in light with Government Guidance
Alaska Permanent Fund	State Law	Follow commercial principles
Korea Investment Corporation	Korea Investment Corporation Act	Follow the guideline described in its mandate
Malaysia National BHD	Company Act	Commercial Principles

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SWFs to Revisit Objectives

Most should generate introspection on topics of investment of "excess" reserves, the level of future risk and more important spill-over implication for macro-economic policies.

New Objectives?	Best practices	Why?
Stabilize macroeconomic fundamentals	Shield the domestic economy against volatility in global markets of critical value Gather knowledge in specific areas	To reduce dependency on commodity exports
Support Industrial or Monetary Policy	Smooth short and medium term fluctuations	To support the level of the local currency
Optimize Risk-return	Generate substantial profits Diversification of the economy	To move away from conventional reserve management as undertaken by Central Banks to maximize profits
Create Wealth for Future Generations		To anticipate the impact of unfavorable demographics
Set aside Savings		Fear of crisis and need for a flexible investment strategy
Support Domestic/Regional Industries	Support and secure domestic / regional industries to create jobs, wealth...	To restructure and encourage industries / infrastructure
Support Social Objectives		Leasing mechanism

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SWFs to Re-examine Established Investment Guidelines

For most SWFs existing investment processes need an overhaul. This includes both administrative rules managers must comply with, and the policy they must adopt to invest and manage assets.

Guidelines need to be revised to securely save Fund's assets and to increase value through effective investment management

Guidelines specificities

- Compliance Code to prepare Investment Policy
- Re-visit existing
- Preparation within the legal framework of the Status
- Submission to the Board and to the Governmental entity responsible for the fund
- Approval through a voting session

It is common to include specific guidelines for external managers. Usually, they prohibit them from various investment such as:

- Share ownership in companies who a principal business involves gambling or liquor and adult entertainment or meet ESG goals.
- Participation in private placements and venture capitalization.
- Investing in a issuer issue in excess of 5% of the portfolio at the time of the purchase... etc.

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New guidelines to constitute the framework through which investment policy is drawn

Guidelines must specify key elements of the investment policy

- The foreign currency composition of investment portfolio
- The forecast volume of investment portfolio
- The portion of investment portfolio assigned to external managers
- The external managers' investment horizon
- The credit risk limits
- The forecast return
- The benchmark determination process

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SWFs to Re-examine Established Investment Process

Existing investment processes need an overhaul. This includes reflecting changes (downgrades) in country ratings and lists of permitted investment.

Permitted Investment

- Deposits in central, commercial banks and other financial institutions
- State Securities (bonds) issued by governments of countries which have pre-specified long-term country rating
- Securities issued by financial institutions that have State specified long-term country rating
- State agencies and government of countries which have pre-specified long-term country rating
- Securities and bonds issued by international (supranational) institutions
- Debt issued in the form of securities by central banks and other financial institutions which have pre-specified long-term country rating
- Securities issued by corporations and financial institutions which have pre-specified long-term country rating

Restricted Investment

- Currency and other derivatives
- Real estate and other investments

Permitted/Restricted investment depend on the policy implemented and should vary with time

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SWFs to Improve Monitoring and Reporting Functions

During Covid-19 period, inadequate proactive investment monitoring resulted in weak local calls with redemption restrictions, lockups, and LP inertia resulted in SWF wealth destruction, hindering routine GP reporting, with LP fiduciary responsibility for active monitoring, rebates/losses.

Monitoring

- Portfolio managed by external managers ("SPM") should be monitored on a regular basis to ensure investment objectives and guidelines are actively observed
- To assess performance and risks, various measures should be taken to make sure EPMs are on the right path or to sanction them if not.

Reporting

- External managers should report on a regular basis but also proceed to a high level notification of any events which may affect their investment capabilities or the value of the portfolio

Internal Manager

- Change in management
- Significant change in the financial position
- Change in the business direction
- Change in key officers
- Change in key individuals responsible for investment management
- Breach of laws or regulations
- Material errors, omission, false statements

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SWFs to Re-examine Manager Investment Mandates

Clear lines of responsibility to be re-defined to frame and supervise both internal and external managers' investment activities.

"Owner"	"Manager"	"External Manager"
<ul style="list-style-type: none"> Overall responsibility Strategic asset allocation Risk limits Evaluate operational management 	<ul style="list-style-type: none"> Carry out investment strategy Risk management Accounting and reporting Offer advice to the owner on strategic investment decisions 	<ul style="list-style-type: none"> Follow the strategy Daily, monthly, quarterly report

Revisit distinction between internal and external managers

Internal Manager

Benefits include centralized control of assets, ensuring effective coordination across managers and portfolio

Avoid additional cost for setting up a team for monitoring external managers critical to ensure professional management

In-house expertise than can allow additional portfolios to be managed internally and can provide financial market expertise to other Government entities, including the Central Bank, MOF, etc.

External Manager

Benefits include professionalism – asset managers bring breadth of experience and efficiency; transfer of knowledge; outside credibility and transparency in benchmarking returns

Value Add

Ensures diversification by asset class, geographic, market, sector and management style and potential for alpha generation

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SWFs to Re-examine External Manager Selection Criteria

SWFs usually opt for a mix of internal and external managers. During and post Covid-19, even closer attention must be paid to the external manager selection process and management arrangements.

Criteria for choosing external managers	Management Arrangements
<ul style="list-style-type: none"> Competence / Fundamental and technical expertise Resources and capabilities/availability and dedication Track record of risk management and performance Investment philosophy Complexity of investment strategy Asset under management / Number of institutional clients Coordination with execution of monetary policy Costs Control 	<ul style="list-style-type: none"> Scope of action, Timeframe, Amount under management Restrictions Other functions: <ul style="list-style-type: none"> Investment advisory: asset allocation, portfolio construction, review and analysis of asset classes Legal advisory: legal advice relating to the investment of entrusted assets Tax advisory: tax advice relating to the investment of entrusted assets Transition management in place to smooth consequences on portfolio of change in managers

Decision for selecting external managers should be derived from the objectives set for the Fund

The best selection process requires transparency, objectivity and should be competitive

Some SWFs have very specific criteria. External Managers shall have a credit rating of not less than AAA, or at least 5 year positive experience in management of assets not less than \$1 bn

*** determined according to the benchmark and to objectives assigned to an external manager

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SWFs to Re-examine External Manager Monitoring

During Covid-19 period, External Fund Managers should be continuously monitored even more than ever.

Monitoring	Reporting
<ul style="list-style-type: none"> Portfolio managed by external managers (EFM) should be monitored on a regular basis to ensure investment objectives and guidelines are strictly observed To assess performance and risks, various measures could be taken to make sure EFMs are on the right track or to sanction them if not 	<ul style="list-style-type: none"> External managers should report on a regular basis but also proceed to immediate notification of any event which may affect their investment strategy or the investment portfolio Change in investment strategy Change in the investment portfolio Change in key personnel Change in the investment philosophy or investment objectives Breach of laws or regulations Material omissions, false statements (...)

Preparation of Control Reports

Regular Portfolio Review

Comprehensive Analysis of existing EFMs and of internal managers

Warning Letters to Underperformers & meetings

Portfolio repositioning through a transition manager

Daily Review - Trading
 Monthly Review - Performance Review
 Quarterly Review - Portfolio Review
 Annual Review - Portfolio Review, Manager Review, Investment Policy Review

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SWFs to Revisit Role of the Benchmark

We provided inputs to CFA Institute Global Investment Performance Standards during comment period to arrive at Guidance Statement on Benchmarks. We summarize the key takeaways below.

Benchmarks should be used to measure the effectiveness of investment strategy at three levels

Fund Level	Class Level	Manager Level
Included within the legal status or the mission statement	Included in the investment policy	Included within the management arrangement

Select indices to meet criteria

Relevance	Comprehensiveness	Objectivity	Stability but Flexibility	Replicability
Track record and ease of interpretation	Ability to capture all opportunities and measure the performance of the investment	Clear and objective criteria should be used to determine the benchmark, and the investment manager should be able to anticipate and agree on changes in its composition	An index should be flexible enough to be able to change composition and all changes should be easily understood and predictable	Total returns should be replicable and must be fair to investment managers who are measured against the index

Additional	Expenses Minimization	Openness
Provide a clear way of measuring the performance of the investment	Expenses related to withholding tax, as sleeping, and transactions incurred, should not be excessive	The markets and segments included in an index should not contain significant barriers to entry

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SWFs to Re-examine Post Covid-19 Benefits & Concerns

We recently provided policy inputs to policy makers. Here are some takeaways, that can be extrapolated for the wider population of government investment funds.

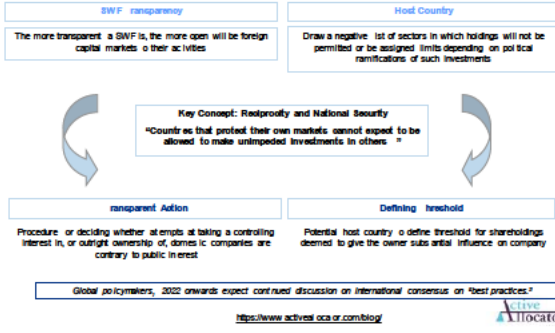
Potential Benefits	Potential Concerns / Risks
<ol style="list-style-type: none"> Enhances revenues and potentially improves yields on reserves Preserves current wealth for future generations Funds Social Security / Pension Funds Diversifies investments Focus on long-term investments Provides on-going budget support Supports infrastructure projects Supports national champions Takes advantage of market opportunities Acquires stakes in well-run companies Develops internal expertise 	<ol style="list-style-type: none"> Decline in political support Fund loses money, who is responsible? Funds could be used for domestic infrastructure, education, housing, health care, etc. given revenue shortfalls Use of earnings Funds needed at later date by Central Bank or MOF Political ramifications for investments Impact of investment in industries Unclear objectives post Covid-19 Stray in execution of mandate

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Recipient Host Government Reaction to Shape SWF Investment Evolution

Santiago Principles to promote improved governance, foster accountability, ensure transparency and instill prudent investment practices.



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SWF Investment to Re-Examine Post Covid-19 Implications of Macro-Economic, Fiscal & Monetary Policy

- Invested Offshore
 - Funds would be "sterilized"
 - No direct impact on domestic economy
 - Higher returns can reduce cost of sterilization to central bank
- Invested Domestic
 - Potential Impact on
 - Domestic demand
 - Exchange rate
 - Inflation
 - Money Supply
- Policy Debate
 - SWF will itself generate a public debt
 - Investment of "excess" reserves
 - Mission
 - Objectives
 - Level of risk
 - Lead to spill-over implications for macro-economic policies

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SWFs to Improve Risk Management Function

Investment Risks	Operational Risks
<p>(a) adopting an appropriate risk profile that is commensurate with the return objective and time horizon of the fund. That risk profile is defined after analysis of the prospective risk and characteristics of each asset class in which the fund might invest;</p> <p>(b) avoiding concentration of risk and ensuring adequate diversification between and within asset classes;</p> <p>(c) careful selection and monitoring of managers to ensure sufficient confidence in each manager warrant the allocation of activities to them;</p> <p>(d) monitoring the composition of the portfolio managed to ensure there are no unintended biases arising from the investment strategy;</p> <p>(e) careful use of derivatives and managing of both market and counterparty risk;</p> <p>(f) careful use of benchmarks being used, and underlying assumptions being made, to make sure they reflect accurately the owner's risk appetite</p>	<p>Operational risks are financial loss due to management, employee or unauthorized use of techniques and/or financial products.</p> <p>(a) engaging an independent global custodian to separate the investment function (undertaken by the investment managers) from the transaction settlement, recording and reporting of investment activities (undertaken by the localodian);</p> <p>(b) requiring investment managers and the custodian to provide the head of the fund with third party covenants or assurances against these events;</p> <p>(c) ensuring that the fund has in place insurance arrangements to cover claims in those events; and</p> <p>(d) ensuring that the fund has in place, and regularly confirm the existence and efficiency of, internal policies and controls to address those risks;</p> <p>(e) establishing a system of compliance reporting by investment managers and the custodian to the head of the fund;</p> <p>(f) establishing an Audit Committee of the board, with responsibility for recognising and controlling operational risk; and</p> <p>(g) establishing an effective business continuity plan in conjunction with the custodian.</p>

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SWFs to Revisit Build Inhouse or Outsource Decisions



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