

# Change in store

The ASDA Group Pension Scheme has taken a bold step to boost its investment performance, finds **Alastair O'Dell**

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The ASDA supermarket chain is renowned for its low prices and efficient supply chain management. And these qualities were further reinforced in 1999 when ASDA became a part of the Wal-mart retail empire, a firm notorious for its financial discipline. Within this working environment it is unsurprising that the ASDA trustees should be pioneers in seeking to extract better performance from their pension scheme assets.

The scheme showed only a minimal deficit at the last valuation in April 07 and, according to accounting measure FRS 17 at least the deficit remains modest. But even so, the trustees and pensions manager Steve Jones were interested in increasing the performance of the scheme. So when, in April last year they were reviewing investment managers and considering new ones for their mandates they contacted Cardano, a young firm that was reportedly offering something different. When the firm presented, the trustees were introduced to the idea of delegating not just asset management, but asset allocation as well.

In most schemes trustees and their professional advisers decide the proportion of their assets to allocate to each asset class. Then, for each agreed part of the portfolio, a professional manager (or several)

is selected and performance parameters are set.

It is the initial asset allocation decision that has the greatest impact on overall performance and this decision rests with the only non-financial professionals in the decision making process – the trustees.

Richard Phillips, trustee chairman of the ASDA scheme, compares the situation to a bottle bobbing around in the ocean. “The manager will decide where that bottle lies in the ocean. The trustees make the big decision – asset allocation – that decides whether the tide is coming in or out.”

This is the first major reason that the trustees decided to opt for what some call fiduciary management, but the chosen manager Cardano calls ‘delegated authority’. Says Phillips: “It means experts decide asset allocation policy.”

The second major reason is that a more diverse set of assets and instruments can be employed, and the speed of decisions and execution increases. As with many schemes, first the trustees discuss an investment at a meeting. If it is complicated, they need to take the time to get everyone up to speed before they can decide whether to invest in it. “The trustees thought that we moved reasonably quickly, but because we all had day jobs, decisions could take a month,” says Phillips.

## KNOWLEDGE PAYS

The reasons pension schemes opt for fiduciary mandates are as varied as the eventual contracts: some trustee boards may opt to delegate responsibilities where they feel their expertise is weakest and others where they feel a disproportionate amount of the board’s time is taken up. The ASDA trustees certainly had the expertise to cope with an investment strategy of average complexity, quite possibly more complex than average. However, although this level of knowledge would not be sufficient to run the most complex type of strategy, it is sufficient to oversee an advanced investment approach. The trustees understand the purpose, costs and benefits of financial instruments such as derivatives, and how they fit into an overall strategy. The aim was to use this existing knowledge to increase investment returns through strategies that are not typically available to pension schemes (rather than to get help running a typical strategy).

## SHOPPING AROUND

The process of appointing a fiduciary manager was relatively short, considering how long far less important investment decisions took to complete. Says Jones: “We were originally reviewing our investment consultants as part of a rolling review of providers. Because Cardano had come to our attention



## SCHEME STATISTICS

Members: active 4,985; deferred 6,538; pensioners: 2,535; total 14,058

Annual contributions: £77.6m

Annual investment income: £18.2m

Capital value: £1.1bn

Closed to new members

Open to future accrual

### SUMMARY OF CURRENT INVESTMENTS

Overseas equities: £448.4m

Property: £46.3m

Index linked gilts: £124.9m

Domestic equities: £430.2m

Cash & deposits: £13.7m

Private equity: £19.9m

Currency: £31.3m

in that context, they were on the shortlist of people to see.”

It was in the build up to that meeting that the Cardano executives gave details of the way in which the company operates. Cardano takes



### TRUSTEE PERSPECTIVE



Richard Phillips,  
ASDA trustee chairman

While the ASDA trustees might have delegated some investment decision-making to Cardano the knowledge burden on trustees is not expected to diminish, says Phillips: "I think we will almost require more financial knowledge – because the strategy is going to be more complicated than what we do now. It is a question of understanding instruments, as opposed to the trustees having the ability to go out and deal in them."

Phillips says that Cardano did not want the trustees to relinquish responsibility and wants them to understand the strategies they are following. "We are not just going to blindly give them our money and say get on with it. They explain to us the type of instruments they want to invest in and we then have the opportunity to say if that looks too racy for us."

an all-or-nothing approach to investment strategies – it does not handle individual mandates. Phillips was initially sceptical: "When Steve [Jones] first suggested it to us we thought this is not necessarily something we want to do, but let's take a look." However, after the meeting, the trustees decided they liked the fiduciary management approach and invited further firms to present on that basis. Jones then drew up a shortlist of candidates that the trustees interviewed in summer 2008. From these, two were brought back.

Phillips had some initial

reservations about Cardano as it is a relatively new organisation. However, the trustees were satisfied by outside advice on the investment process, references and the track record of the people heading up the organisation. The trustee board spoke to other trustees that had become customers of Cardano before taking the decision.

Although the trustees were satisfied, would members be uncomfortable with the change in approach? Says Phillips: "We do not have a referendum with members every time we change the investment managers. Even the trustees find the fiduciary

management process complicated. It is quite a mind-blowing exercise. You need to devote days to it – it would be very difficult otherwise." The members will be kept informed by scheme communications and there are member nominated trustees on the board to represent their interests.

The next step was to get the company on board. Says Phillips: "Because we were doing something slightly differently, it was only right that the company was also comfortable with the way we were proposing to handle it."

#### TAKING STOCK

The scheme effectively appointed Cardano to start in November 2008. But even after the due diligence process and agreement, there will be a transitional process. Cardano will have delegated powers over 20 per cent of the scheme's assets and will act as a traditional adviser on the other 80 per cent. However, it is unlikely that they will get fully delegated powers over even the first 20 per cent until the end of February 2009. One of the main hold-ups is waiting for the trustees to complete various training courses to get them up to speed with some of the investment vehicles that they plan to use. And then, says Phillips: "once trustees understand the

issues, we will apply the common sense test."

In the outline transition plan, Cardano will explain the framework they want to operate in, which will be discussed, altered and eventually agreed with the trustees. Cardano will be paid on a performance-related basis. The performance measure will target closing the gap between assets and liabilities. This takes the form of a performance plus contract (such as gilts plus X per cent).

The trustees expect the transition to 100 per cent of assets to take three years but nothing has been set in stone yet – it will depend heavily on Cardano's performance and other factors that will doubtless emerge. Phillips: "It is early days. We have not planned exactly where the deal is going." ■

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