STRATEGIC ASSET ALLIANCE
THE INSURANCE INVESTMENT SPECIALIST

Investment Seminar for Gov't Risk Pools: Sample Case Study "Strategic Asset Allocation – Limited Opportunity?"

Introduction

Tess was new to the risk pooling business although she'd held various underwriting and claims positions during her young career at large, well-known commercial carriers. Per her recruitment discussions with the executive director, her new role was associate executive director with the clear career path of learning the business and leading the risk pool within ten years.

Tess's weakest area was investments and the executive director asked her to "dig in" and become familiar with the investment portfolio and how it was constructed to support the goals and objectives of the pool.

Background

Since its inception, the pool was a successful risk transfer mechanism for the workers' compensation needs across the state's municipalities, both large and small. Conservative management and actuarial practices helped propel the pool's net position to nearly $100M as of 12/31/2017 allowing the pool greater flexibility in supporting its members.

With the goal of always trying to price risk adequately, the pool's focus on underwriting has served it well. Investments have always taken a back seat to underwriting and the current portfolio was 90% high quality fixed income (70% of which were U.S. Gov/Agency) and 10% U.S. Total Equity Market. At 12/31/2017, the equity allocation represented approximately 22% of net position (a much more conservative position relative to P&C commercial market statistics).

As Tess researched, she compared a recent rebalancing study to the pool's investment portfolio and a thought struck her – disconnection. While implementation may be more difficult with certain asset classes, nothing in the state regulations precluded the pool from investing in any of the asset classes posed within these two intriguing items; however, the investment policy allows only U.S. equities.

Through her AGRIP connection, Tess was also able to locate and review an investment portfolio peer analysis for several larger pools which also supported her thoughts of disconnection relative to current asset allocation themes and approaches. On median, nearly 81% of the peer group's investments that were not high-quality fixed income were U.S. equities. It appeared to be too high based on her intuition.

Upcoming Board Meeting

The Board meeting was six weeks away and the executive director asked Tess to lead the review of investments and coordinate with the pool's advisors as needed. While the Board was expecting the standard agenda, Tess approached the executive director, and wanted to pose a few strategic questions for the Board and advisors to consider:

1. As a globally-connected millennial, Tess wondered why the pool would limit the investment policy only to U.S. equities. She felt intuitively that the current asset allocation had a large opportunity cost? Agree/Disagree?

2. With strong operating cash flow, why do we have 70% of high quality fixed income allocated to U.S. Gov/Agency?

3. Some of the investments recommended within the most recent optimization, propose a radical departure from the current allocation. Are these reasonable options? Why? Why not?

4. Tess believes the pool can support up to 50% of its net position allocated to higher returning assets. Do you agree/disagree?