INVESTMENT

Being Agile In An Uncertain Economy

BY: **RYAN SILVA**

Reprinted with permission from:

BENEFITS AND PENSIONS
MONITOR

April 2019 Issue

Being Agile In An Uncertain Economy

BY: **RYAN SILVA**

It is no secret that the geo-political climate is changing. Key events such as Brexit, trade wars between global super powers, and shifting power dynamics across different regions have impacted the global economy.

The Eurasia Group's 'Top Risks For 2019' report summarized the global turbulence by saying, "Consider the trajectories of all the current geopolitical dynamics that matter. Start with the big ones. The strength of political institutions in the U.S. and other advanced industrial economies. The transatlantic relationship. U.S.-China. The state of the EU. NATO. The G20. The G7. The WTO. Russia and the Kremlin. Russia and its neighbours. Regional power politics in the Middle East. Or in Asia, for that matter. Every single one of these is trending negatively – every single one – and most in a way that hasn't been in evidence since World War II."

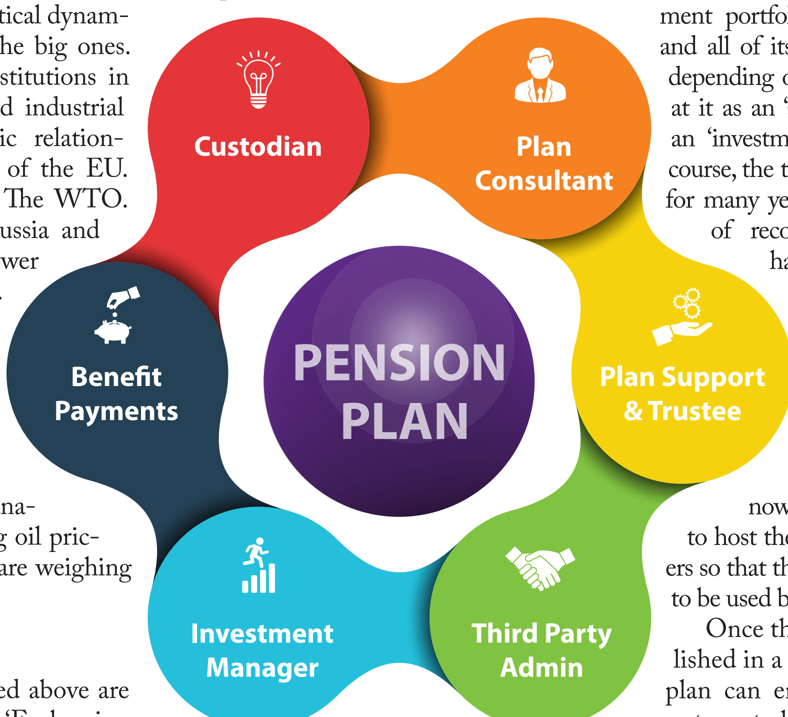
Meanwhile at home, Canada-China relations, declining oil prices, and higher interest rates are weighing on the economy.

Key Obstacle

The sentiments mentioned above are consistent with findings in 'Embracing Change,' a survey of over 100 Canadian defined benefit pension plans conducted by RBC Investor & Treasury Services where respondents indicated that economic and geopolitical uncertainty is one of their top three challenges over the next 12 months. Given that the key responsibility of any pension plan is to align its liabilities with its assets, economic uncertainty is a key obstacle because it can cause the gap between the plan's assets and its liabilities to widen which can be a significant challenge for the sponsor of the pension plan.

Pension returns have shown that plans are not immune to the ongoing political and economic changes. However, they must also endeavour to protect the economic interests of their members. But how?

Being agile is the key. In an ever-shifting environment that continues to be uncertain, pension plan managers must move quickly to assess and react quickly to the changes that are occurring in order to ensure the plans are operating at optimum levels.



Pension plans can 'move quickly' by ensuring they have an investment structure that can adjust quickly. That means having a connected and optimized data flow between all investment partners; from the custodian to the investment consultant to the actuary to the investment managers. Regardless if these functions are performed internally or externally, it is crucial that a pension plan ensures all of its partners are working off the same base of information, in the best interest of the pension plan.

This can be achieved by leveraging the technology provided by the partners so all of the pension plan's data is located in one central location which ensures that all parties involved are working on and communicating off the same set of data. Appropriate authorizations must be in place for different data sets. However, it is imperative that everyone has access to and is working off the same source to generate a successful outcome.

The data set, in this case, is the investment portfolio. The investment portfolio and all of its activity take different forms depending on the audience. You can look at it as an 'accounting book of record' or an 'investment book of record,' and, of course, the timing of the data. Custodians, for many years, were viewed as the 'book of record.' However, as portfolios have evolved and pension plans hold investments in different forms in different locations, the consolidation and aggregation of the data can often lead to significant inefficiencies for the pension plan. The pension plan can now look to leverage the custodian to host the data from each of its providers so that there is one true 'book of record' to be used by all of the parties involved.

Once the complete data set is established in a central location, the pension plan can ensure it drives the relevant partners to have a holistic understanding of what is required to meet the investment goals of the plan as it is laid out in the investment policy. As an example, the plan's investment committee should have a regular review of the investment manager's performance. Based on this review, once the committee decides to either increase the allocation to a manager that is performing well, or remove a poorly performing investment manager, the sooner that information cascades through the process and the investment committee's decision can be executed.

Plans also need to be able 'move easily.' This means that the governance and procedures required to allow the organization to move easily, while mitigating for all the appropriate risks, are in place.

For example, the Pensions Benefits Act of Ontario states:

"Funding and governance policies

(5) The documents that create and support a pension plan shall include the funding policy of the pension plan and the governance policy of the pension plan. 2017, c. 34, Sched. 33, s. 2 (4).

Same, existing pension plans

(6) The administrator of a pension plan that applied for registration before the day subsection 2 (4) of Schedule 33 to the Stronger, Fairer Ontario Act (Budget Measures), 2017 comes into force shall, within the prescribed time, file with the Superintendent a funding policy of the pension plan and a governance policy of the pension plan. 2017, c. 34, Sched. 33, s. 2 (4).

Note: On a day to be named by proclamation of the Lieutenant Governor, subsection 10 (6) of the Act is amended by striking out "Superintendent" and substituting "Chief Executive Officer." (See: 2018, c. 8, Sched. 23, s. 2)

Same, requirements

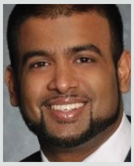
(7) A funding policy of a pension plan and a governance policy of a pension plan must satisfy such requirements and contain such information as may be prescribed, and must be reviewed in accordance with the regulations. 2017, c. 34, Sched. 33, s. 2 (4)."

Good Governance

In addition, while the Pension Benefits Standards Act (PBSA) ensures that a governance policy exists, it does not prescribe the specifics of the policy and good governance is rooted in structure and transparency between the sponsor, the plan, and each of the plan's partners, as stated above.

In order to avoid slowing down the decision-making process, the pension plan must be mindful of hiring partners who can deliver transparency easily and quickly so that the investment governance structure that oversees the investment policy, investment management (including performance measurement), information technology, and accounting can function with ease.

In a rapidly changing economy, organizations must be able to maximize the value of their data because the effectiveness of the pension plan's execution can either mute or magnify the impact of the economic volatility upon its portfolio. Maximizing the value of data comes down to how quickly and easily the pension plan can use the appropriate data at the appropriate time while taking advantage of the significant opportunities for them to increase their agility by creating the appropriate governance structure and optimizing the data flow between partners. **BPM**



Ryan Silva *is director, pensions and insurance segments, global client coverage, RBC Investor & Treasury Services.*

ryan.silva@rbc.com