



Agenda Item 8a

April 15, 2013

ITEM NAME: Cost Effectiveness

PROGRAM: Total Fund

ITEM TYPE: Business Plan/Roadmap – Information

EXECUTIVE SUMMARY

This agenda item provides an overview of the Investment Office (INVO) Roadmap Strategic Objective -Cost Effectiveness. The topics include an analysis of INVO's cost drivers and cost structure vs. peers. It also reports on INVO's expense trends and key cost savings and financial reporting accomplishments.

STRATEGIC PLAN

This agenda item supports the Strategic Plan goal to improve long-term pension and health benefit sustainability.

BACKGROUND

Cost Effectiveness is one of the INVO Roadmap strategic objectives. INVO aims to enhance cost effectiveness of the investment program to improve net returns on assets.

ANALYSIS

Each year, the Investment Office participates in the CEM Benchmarking survey which analyzes our costs against a customized peer group comprised of both US and Global pension investment organizations.

The total cost reported to CEM for Calendar year 2011 to manage the CalPERS portfolio was 53.5 basis points. The CEM analysis concludes the Investment Office is cost-advantaged compared to its peers, due to:

- Internal management of public assets
- Passive management of equities
- Lesser use of fund-of-funds than peers

The Investment Office strategy has been to deliver more value for cost by pursuing the following efforts:

- Reduce the reliance on external consultants and advisors, especially for key control and portfolio monitoring functions

- Transition assets from external managers to internal management when it is possible to build internal capabilities
- Reduce external management fees paid

The total cost to manage the CalPERS portfolio for Fiscal year 2011-12 was approximately \$1.1 billion; 89% of these costs were attributable to fees paid to external investment managers. Total cost to manage the portfolio decreased by \$182 million. Excluding performance fees, which are very volatile, the cost to manage the portfolio decreased by \$63 million.

The reduction in costs has enabled INVO to fund an increase in staffing to:

- Internalize core, high-value functions that were previously outsourced
- Establish critical control functions that previously did not exist (e.g. Investment Risk Management and Investment Compliance)
- Transition assets to internal management and reduce fees

INVO is also partnering with Fiscal to develop the necessary management reporting and budgetary tools to properly control total investment costs and provide the Board with comprehensive reporting of the total costs to manage the portfolio.

ATTACHMENTS

Attachment 1 – Cost Effectiveness PowerPoint presentation

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