Clare College Endowment

Investment Philosophy and Long Term Asset Allocation

The College is a permanently endowed charity. It therefore aims to preserve and if possible improve the real value of the College's endowment and the income from it over time. This is to ensure that future generations of beneficiaries receive the same benefits as the current generation of beneficiaries.

There are three critical principles that underlie the College's investment approach:

- As a permanently endowed charity the College adopts a very long-term time horizon when making investments. The natural investments for the College to hold are titles to real assets since these assets should preserve their real value over time. The Investments Committee therefore has a preference for equity 'and equity-like assets'.
- To maximise long-term risk adjusted returns it is important to maintain a well-diversified portfolio of assets within the endowment.
- Superior long-term investment performance requires a sound philosophy but also requires low management and transaction costs. The Investments Committee only recommends investments into funds where the fees charged by the fund manager are justified by the expected risk adjusted returns from that manager and asset class. The Investments Committee therefore has a preference for investments into index funds which involve very low management costs.

The Investments Committee believes that there is evidence that over the long-term, shares not only provide protection against the ravages of inflation, but also provide a higher return than other financial assets such as bonds or cash on deposit. Hence, the long-term investment targets set for the endowment have a relatively high weighting toward equities.

It is also thought that the long-term risk adjusted returns on real assets such as equities and property will tend to be similar; and that there is a clear benefit in holding both, since neither their capital values nor their income streams (rent and dividends respectively) move together over medium-term periods of five to ten years. A more diversified portfolio that contains both shares and property will therefore be less risky than one exclusively invested in either. The Investments Committee has chosen a long-term target allocation for the endowment fund with the following target weights:

	Endowment	Acceptable Range
Quoted Equities	70%	50-80%
Property in the UK	25%	20-30%
Alternative Assets	5%	0-10%
Cash	0%	0-20%

A similar approach to risk reduction has led the Investments Committee to invest both in UK shares and in those of other countries because dividend and capital values in different stock markets do not rise and fall in unison in the long-term. The Investments Committee has chosen a target equity allocation with the following geographical spread:

Geographic Region	%	Acceptable Range	MSCI ACWI Index
North America	35	25-40	55.8
UK	25	20-30	7.1
Europe excluding UK	15	12-18	15.7
Japan	10	7-13	7.9
Pacific excluding Japan	3	0 - 5	3.8
Emerging markets	12	8-16	9.7

The geographic target allocation has been set with reference to the relative market capitalisation of each region. In addition to the long term target allocation, an 'acceptable range' has been established for each region which helps to ensure that a policy of regular rebalancing is enforced. The target allocation over-weights the UK, compared with the relative size of the UK stock market. This is because exchange rates can vary greatly and a rise in the real value of sterling might place a strain on the income from the non-UK components of the endowment. Accordingly, we target a higher allocation to UK assets than relative market capitalization might suggest. Similarly, the target allocation under-weights North America since the market capitalisation weight to North America is 56% and such a high weight to North American equity it would make it difficult for the College to maintain an appropriately diversified portfolio.

The underlying foreign currency risk for equities is not explicitly hedged unless there is a specific tactical case for taking a position, not least because it is difficult to identify the underlying currency exposure for many multinational companies. Academic research, notably by Dimson Marsh & Staunton, also shows that foreign currency returns contribute little to real global equity returns over long-run periods to a sterling investor. The Investments Committee therefore believes that it is not sensible to attempt to hedge the currency risk since there is a cost in doing so. All cash is held in sterling unless there is a specific tactical case to do otherwise.

Investment Management

The Investments Committee makes recommendations on asset allocation decisions to the Finance Committee for the main endowment and the 2048 Fund. It has chosen to adopt an external manager model that relies on low cost index funds to gain market exposure and only considers actively managed funds when the management fees will be more than justified by the anticipated risk adjusted returns. Superior investment performance requires a sound philosophy with consistent execution and relatively low investment management and transaction costs.

For the direct property investments within the investment portfolio the College takes external advice on individual properties (the current adviser is Bidwells). In addition to the direct property investments the College also invests in two actively managed property investment funds. Investments are made into alternative investment products such as Private Equity, Venture Capital and Hedge Funds when the expected risk adjusted net returns from such funds, after all fees, is similar or superior to those from equities. Tactically the allocation to alternative investments will change over time with reference to the expected risk adjusted return from the asset class relative to the expected returns available from property and equities.

Endowment Drawdown

At the heart of the College's financial strategy is the 'spending rule' which provides the fiscal discipline for the endowment, setting a compromise between two competing objectives. The first objective is to release a substantial level of income to cover operational expenditure in a stable stream, since large fluctuations are difficult to accommodate in the College's activities. The second objective is to protect the value of the endowment assets against inflation. The College's spending rule attempts to meet these two objectives by using a long term spending rate of 3.5% of the average value of the endowment over the three previous financial years.

Current Asset Allocation

The asset allocation as at 30 September 2015 was as follows:

	Endowment	2048 Fund
Quoted Equities	59%	76%
Private Equity	2%	-
Property in the UK	27%	11%
Fixed Interest	3%	-
Cash	9%	13%

The current asset allocation is set with reference to the long term strategic allocation targets but the asset weightings are tactically changed overtime. Asset class valuation data is the principal driver behind the tactical changes which are made within the acceptable ranges that have been established for the endowment. The cash and fixed interest weights are an outcome of the other tactical allocation decisions that are made by the Investment Committee.