

# EXTERNAL FUND MANAGERS (Public Markets)

Since GIC's inception in 1981, we focused on developing an internal capability to invest the Government's reserves. At the same time, we also awarded investment mandates to external fund managers with expertise which complements and augments our own capabilities. External managers have played a significant role in the Government's portfolio, managing at times up to 20% of the portfolio.

Allocating funds to external managers has three strategic benefits. It diversifies the Government's portfolio, expands the investment opportunities available and deepens our understanding of financial markets.

For the funds under external management, we adopt an active investing approach, under which investment managers seek to outperform public market benchmark indices rather than just matching their performance, as in passive investing. We have built long-term relationships with our external managers, some of whom we have invested with for many years. These partnerships have helped us to gain insights into high-quality investment ideas and research, as well as industry best practices in the areas of investments and operations.

## THE VALUE OF EXTERNAL MANAGERS

When we first started out, because of our relative inexperience, we invested with external managers to benefit from their experience, expertise and understanding of the financial markets.

**We view our external managers as partners** Our external managers must share our core investment philosophy that taking a long-term perspective enables an investor to earn superior risk-adjusted returns. We look for external managers who can maximize a portfolio's total market value over market cycles while controlling the interim risks.

**Our external managers complement GIC's internal capabilities in their respective asset classes** As GIC has upgraded our internal management capabilities, the role of external managers has become more nuanced. In general, we apply the principle of best sourcing, where we appoint external managers in equities and fixed income only if they augment the overall performance of the Government's portfolio. External managers have to justify their management fees by delivering superior performance net of fees. Additionally, some of our external managers operate in niche markets or employ an investment style or strategy beyond GIC's current capabilities.

GIC remains fully accountable for the overall performance of our external managers. We ensure that the risks they take are properly diversified and managed, and fall within the parameters set by the Government for GIC. We evaluate the risks involved in externally managed portfolios together with those that are managed internally.

Our external managers bring other benefits. They share their market and investment insights with GIC. These

insights benefit our macroeconomic forecasts and asset allocation research and sometimes challenge our own investment beliefs. Through our external managers, we have expanded our network of contacts, giving both GIC and our client an important source of knowledge and experience.

Sometimes our external managers refer co-investment deals to our investment teams. They also keep us informed about best practices and norms in areas such as risk management, trade operations and settlements, compliance and monitoring.

## DEDICATED IN-HOUSE TEAM TO MANAGE EXTERNAL MANAGERS

The External Managers Department is responsible for appointing and managing external managers in public markets. Two separate, independent divisions within the department handle the investment and compliance/operations aspects of the portfolio under external management.

Within the investment division, different teams cover the wide range of strategies offered by external managers. Each team is fully responsible for all aspects of appointing and managing an external manager including sourcing of the manager, investment due diligence, post-investment monitoring and review. The senior members of the investment teams have extensive portfolio management experience. This has enabled them to gain a deeper understanding of how a particular strategy drives returns and hence leads to a better analysis of investment risks.

The compliance/operations division is responsible for the operational aspects of the mandates awarded by the department. The team works with the external managers, the investment division and other corporate services departments in GIC to conduct independent operational due diligence reviews on each mandate. Such reviews are undertaken prior to the appointment of a new external manager and/or the award of a new mandate as well as on an ongoing basis.

### INVESTMENT PROCESS

Managing our externally-managed portfolio entails a four-stage process: Strategy research and manager sourcing; manager review and due diligence; portfolio construction; and portfolio monitoring and risk management.

#### Strategy Research and Manager Sourcing

We start by identifying a specific investment thesis that we wish to pursue. This could be as broadly-focused as a regional mandate (for example, investing in Emerging Asia stocks) or as narrowly-focused as a specific market mispricing we wish to exploit. After researching the investment thesis, we shortlist and meet with the external managers who have expertise in these specific areas. Many contacts are obtained from our wide-ranging dialogue with market participants, including referrals from our market network and internal team.

#### Manager Review and Due Diligence

Before an investment is made, we carry out extensive investment and operational due diligence on the manager. As part of the investment due diligence process, we conduct both quantitative and qualitative evaluations. We evaluate factors such as the external manager's track record; its performance relative to its peers; its compatibility with our existing portfolio and our assessment of the manager's team, investment process and attention to risk control. We go through an equally exhaustive operational due diligence process before awarding an investment mandate to the external manager. Some of the factors include the investment structure, internal controls in the operations and pricing procedures.

**Portfolio Construction** Our goal in portfolio construction is to achieve a balanced portfolio that maximizes returns over the medium term while minimizing the risk of severe capital loss in periods of extreme market stress. Expected returns and risks are interconnected, so constructing the externally-managed portfolio requires good judgment to balance a variety of risks. Our allocation to different strategies is formulated through a clear understanding of the risks and returns inherent in each strategy.

#### Portfolio Monitoring and Risk Management

We monitor our external managers closely, through regular update calls and meetings. We take a long-term view when assessing managers. In addition to consistent good performance, we look for a steady application of their investment philosophy and process throughout market cycles. At the overall portfolio level, we review the aggregate portfolio risk and return characteristics and market exposures. We also review the portfolio strategy allocations and the attractiveness of specific investment themes.

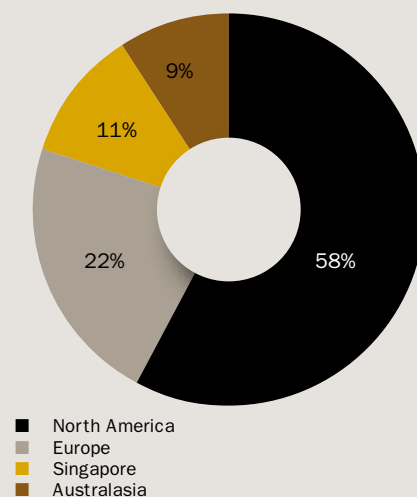
### CONCLUSION

While we have honed investing capabilities within GIC over the years, we have always benefited by learning from our peers and partners in the industry. We have built strong connections with our panel of external managers. They will continue to be a valuable source of not only returns, but also market views and understanding of industry best practices.

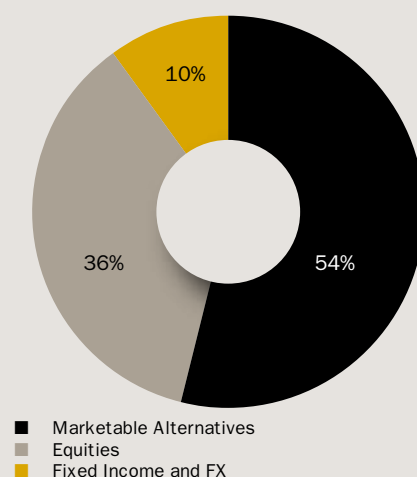
Although external managers can provide strong and diversified returns, outsourcing part of the Government's portfolio inevitably adds further complexity to the overall portfolio. Therefore, we will continue to construct our externally-managed portfolio with a clear understanding of the benefits of using external managers, while paying close attention to risks.

Our approach to external management has evolved in step with our internal capabilities and needs. We continue to seek good managers who can complement our strengths and add value to the structure and performance of the Government's portfolio.

WHERE OUR EXTERNAL MANAGERS ARE BASED



NUMBER OF EXTERNAL MANDATES BY ASSET CLASSES



BREAKDOWN BY LENGTH OF EXTERNAL MANDATES

