

## Ailing pension fund earns strong return

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Philadelphia poured \$400 million into its public pension fund last year, which was still severely underfunded by 47 percent.

Higher contributions by the city and its employees would be one way to fill the gap.

However, while the fund has its problems, it's also being recognized for improvements resulting in higher market returns — 14.8 percent gross last year, compared to 8.0 percent gross the year prior.

Money Management Letter called the Philadelphia Public Employees Retirement System “an early mover, continually seeking out opportunities for diversification” in crowning it medium-sized public plan of the year. Public pensions nationwide with assets between \$1 billion and \$10 billion were eligible for MML's sixth-annual Public Pension Awards for Excellence.

Both small and large changes were made to improve the city's \$4.3 billion fund over years past, fund consultant Tina Byles Williams said.

“The city has some challenges that have been produced over the last 20 or so years, mainly the underfunding of the plan,” Byles Williams said.

With continued minimum funding and a market return of 8.75 percent, it will take until 2035 for the fund to become fully funded, said Christopher McDonough, chief investment officer for the fund.

Moving the fund from the current 53 percent minimum to 70 percent funding would raise costs \$90 million over fiscal year 2008, according to the city's five-year plan offered by Mayor John F. Street. Such an increase would affect the city's ability to provide funding for other services while continuing tax cuts, the plan said.

“When you are underfunded you have to sort of be a little more creative in trying to close the gap,” Byles Williams said of the changes to the fund since 2004.

Among the larger changes were an increase in allocation to private equity and decrease in allocation to publicly traded equity. Allocation to

U.S. bonds were also decreased and allocation was established in real estate and hedge funds. Global Treasury Inflation-Protected Securities (TIPS), portable alpha and convertible bonds were also introduced into the portfolio to increase returns.

The plan's 14.8 percent return last year included 10.9 percent on portable alpha, 7.3 percent on global TIPS and 12 percent on convertible bonds, MML noted.

“One of the key things for a pension fund is to be diverse across different asset classes,” McDonough said of the changes. “You don't want all of your investments moving in the same direction, at the same time; if there is a downturn the entire portfolio will take a hit.”

The plan was also scoured for passive portfolios — in which the only objective of the manager is to match an index for that particular area — and perennial underperformers, Byles Williams said.

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