REPORT FOR:	**Pension Fund Investment Panel**
Date of Meeting:	27th November 2012
Subject:	Review of the Pension Fund's Investment Strategy
Responsible Officer:	Julie Alderson, Corporate Director of Resources
Exempt:	No.
Enclosures:	Aon Hewitt Report

Section 1 – Summary and Recommendations

The Panel has been considering changes to the investment strategy. At the June 2012 meeting, the Panel asked for more time to consider the proposals. Aon Hewitt has reflected on the June discussion and has prepared a paper setting out their recommendations.

Recommendation:

The Panel is invited to review the options outlined in the Aon Hewitt report and agree a revised investment strategy.

Harrow COUNCIL LONDON

Section 2 – Report

1. The Panel has been debating for some time the appropriate strategic asset allocation for the fund. Training has been provided on a range of investment types that the fund has not previously used. Following the discussion on 25th June 2012, the Panel concluded that more time was required to consider the issues. The investment advisor has reflected on the views expressed in June and has prepared a paper setting out their recommended strategy for the fund. The note below provides a brief recap of the discussion to date. Members may find it useful to review the papers on this issue submitted to the meetings on 12 October 2011, 15 November 2011 and 25 June 2012.

Balance of risk and return

2. The funding level continues to be the main driver of the strategy. At the last valuation the accrued liabilities were 73.5% funded. The subsequent decline in gilt yields has seen the estimated funding level fall to 64% at June 2012. The twin aims of returning to a fully funded status and maintaining the current level of employer contributions requires that the investment strategy focuses mainly on return generation and retains a high allocation to growth assets. Even with such a strategy, the 2013 valuation is expected to require an increase in the level of employer contributions.

3. Aon Hewitt's initial strategy suggestions (October 2011) focused on maximising the probability of achieving full funding rather than maximising expected return and proposed a significant reduction in the equity allocation. The Panel indicated that they wished to maintain at least the current level of returns and invited Aon Hewitt to present alternative suggestions.

Introduction of an absolute return allocation

4. In the last year, training was provided on three types of absolute return mandates that offered the opportunity to achieve an improved balance of return and volatility:

   - Fund of hedge funds
   - Individual hedge funds – long/short and global macro
   - Diversified growth funds

5. The Panel concluded that they were uncomfortable with the complexity, the use of derivatives and the fees involved with hedge funds. No decision was reached at the June meeting on the suitability of diversified growth funds (DGF).

6. The Aon Hewitt paper attached recommends that the equity allocation should be reduced and replaced with an increased allocation to alternatives. Initially this increased allocation would be invested in DGF's (appendix 1). Longer term as opportunities arise, this allocation will be available to fund other alternatives that were approved by the Panel e.g. infrastructure, social housing, absolute return bonds etc. These new asset classes would only be proposed after suitable training.

Implementation of the Revised Strategy

7. Following approval of the investment strategy, an implementation proposal will be brought to the next meeting (January 2013) including the process for appointing any new fund managers and the impact on the existing fund manager mandates. To aid the strategy discussion, the Aon Hewitt paper discusses possible options for reducing the equity allocation. The sale of equities can be achieved by taking a pro-rate reduction of 17% in each mandate, although to minimise governance, a reduction from 3 to 2 active equity managers is suggested. The paper also estimates the costs which will be incurred in the re-organisation.

Financial Implications

8. The Strategic asset allocation of the fund is the most significant driver of future returns and risk and the level of contributions required.

Risk Management Implications

9. Risk included on Directorate risk register? No

10. Separate risk register in place? No

11. Setting risk tolerances and measuring outcomes is central to the strategy.

Equalities implications

12. Was an Equality Impact Assessment carried out? Yes

13. There are no direct equalities implications relating to the pension fund.

Corporate Priorities

14. Corporate Priorities are not applicable to the Pension Fund as it does not have a direct impact on Council resources.

Section 3 - Statutory Officer Clearance

Name: Julie Alderson	√	Chief Financial Officer
Date: 16 November 2012		

Section 4 - Contact Details and Background Papers

Contact: George Bruce (Treasury and Pension Fund Manager)
Tel: 020-8424-1170 / Email: george.bruce@harrow.gov.uk

Background Papers: Papers and training material provided to the PFIP meetings on 12 October 2011, 15 November 2011 and 25 June 2012.

If appropriate, does the report include the following considerations?

1.	Consultation	N/A
2.	Corporate Priorities	N/A

Appendix 1

Recommended Strategic Asset Allocations

Investment Strategy			
	Current Strategy	Current Allocation	Aon Hewitt Proposal
Bonds	**13**	**18**	**13**
Index Linked	2.6	3	3
Corporate	10.4	11	10
Cash	0	4	0
Equities	**71**	**68**	**57**
UK	26	25	25
Global	45	43	32
Property	**10**	**9**	**10**
Alternative	**6**	**5**	**20**
Private equity	3	5	5
Currency	3	0	0
Diversified Growth	0	0	15
Total	100	100	100