

REPORT FOR: Pension Fund Committee

Date of Meeting: 25th June 2013

Subject: Equity Training and Beliefs

Responsible Officer: Simon George, Director of Finance and Assurance

Exempt: No.

Enclosures: .Aon Hewitt training material

Section 1 – Summary and Recommendations

With the completion of the strategic asset allocation review, this paper focuses on the equity component and discusses the options for structuring an equity portfolio. The purpose is to agree a basis for further training and the development of more precise proposals that reflect the Committee's views.

Recommendation:

None. The Committee views will be noted and used to develop future training and detailed proposals.

Section 2 – Report

1. With the completion of the strategic asset allocation review it is appropriate to consider the structure and composition of each asset class to ensure that the fund is achieving the best balance of return and risk and to test whether the assets are being managed in accordance with the Committee's investment beliefs. Listed equities represent 62% of the strategy and are a good place to start this process.
2. Currently, the portfolio is managed by 4 fund managers, with 42% UK passive (1 manager) and 58% global active (3 managers). The current arrangements were put in place in 2009.
3. The attached paper from Aon Hewitt considers the current structure and the factors that should be considered when structuring an equity portfolio. The paper is not intended to offer solutions but to facilitate a debate on the beliefs, assumptions and forecasts that should influence the equity portfolio construction. In doing so, we can test whether the current structure chimes with the Committees beliefs and expectations and represents the optimum way to manage equities.
4. The factors that the Committee will be asked to consider when going through the training material include:
 - a) Geographic allocations
 - The rationale for a specific UK equity allocation given that currency risks can be managed with hedges. With most UK equity earnings deriving from overseas and UK equity returns expected to trail overseas equities, they don't appear to be a better match for our pension fund liabilities.
 - The UK represents around 10% of the global equity market, yet the current allocation is 42%.
 - Emerging markets generate most economic growth and represent most of the global population, but little more than 10% of the stock market indices. Do expectations of wealth rebalancing justify a higher / explicit allocation to emerging markets?
 - b) Active / passive
 - Do active managers exist who can reliability add value after costs?
 - In all or only some markets?
 - If so, can the Committee identify and monitor these relationships? Evidence from WM has been that active management does not **on average** deliver superior returns to LGPS.
 - Are others better placed to identify and monitor active managers on our behalf e.g. delegated manager selection?
 - Are alternatives to market capitalisation based indices a basis for passive management? Although historic performance of alternative indexation is superior to traditional passive, the reasons are often unclear and the ability to predict future returns uncertain.

c) Mandate structure

- Which styles of active management work best e.g. low risk highly diversified core through to concentrated / benchmark unconstrained portfolios?
5. At this stage, the Committee's views on the questions / options raised are sought. In some cases, more training will be required before any decisions can be made e.g. alternative passive benchmarks. Hopefully, the Committee will at least talk through the framework on page 19 of the Aon report. The views of the Committee will be used to develop more precise proposals and training for the September meeting. Suggested topics for future training topics include:
- Alternative passive methodologies
 - The case for a targeted emerging market exposure
 - Fiduciary / delegated management

Financial Implications

6. The equity structure will have a significant impact on ability to meet and exceed the returns required to restore full funding.

Risk Management Implications

7. Risk included on Directorate risk register? No
8. Separate risk register in place? No
9. Setting risk tolerances and measuring outcomes is central to the strategy.

Equalities implications

10. Was an Equality Impact Assessment carried out? Yes
11. There are no direct equalities implications relating to the pension fund.

Corporate Priorities

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

Legal Implications

13. The report has been reviewed by Legal Department and comments received are incorporated into the report.

Section 3 - Statutory Officer Clearance

Name: Simon George	<input checked="" type="checkbox"/>	Chief Financial Officer
Date: 10 June 2013		
Name: Matthew Adams	<input checked="" type="checkbox"/>	Monitoring Officer
Date: 10 June 2013		

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 relating to investment strategy provided to the PFIP meetings on 8 January 2013 and at various meetings in 2011 and 2012.

If appropriate, does the report include the following considerations?

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