Division(s): N/A

PENSION FUND COMMITTEE – 25 JUNE 2010

REVIEW OF THE STATEMENT OF INVESTMENT PRINCIPLES

Report by Head of Finance & Procurement

Introduction

1. The Fund publishes its Statement of Investment Principles (SIP) in the Annual Report each year. The SIP is usually amended for any changes that have taken place during the year.

2. The Government has published a revised set of investment regulations, the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009. In accordance with regulation 12 of the Regulations, an administering authority must, after consultation with such persons as it considers appropriate, prepare, maintain and publish a written statement of the principles governing its decisions about the investment of fund money. The statement must cover its policy on—

   (a) the types of investment to be held;

   (b) the balance between different types of investments;

   (c) risk, including the ways in which risks are to be measured and managed;

   (d) the expected return on investments;

   (e) the realisation of investments;

   (f) the extent (if at all) to which social, environmental or ethical considerations are taken into account in the selection, retention and realisation of investments;

   (g) the exercise of the rights (including voting rights) attaching to investments, if the authority has any such policy; and

   (h) stock lending.

3. As a consequence of the change to the regulations, and the fact that the SIP had not been reviewed for a few years, a complete revision of the SIP has taken place in conjunction with Peter Davies.

Outcome from the Review

4. The revised SIP is attached at Annex 1. A large part of the review was structural, making the statement more logical in the way it was set out. There have been a few additions, although these were things that had previously been agreed by committee or statements of fact where inclusion was deemed helpful.

5. There are few additions or changes to policy that need to be specifically highlighted and agreed:

   Investment Objectives – these were not explicit within the SIP previously. It is suggested that they should be fairly simple statements as follows:

   - To achieve a 100% funding level;
   - To ensure there are sufficient liquid resources available to meet the Fund's current liabilities and investment commitments; and
   - For the overall fund to outperform the benchmark by 1.3% per annum over a rolling three year period.

   The latter objective was not previously stated explicitly but is derived from the agreed targets set for the Fund Managers and the agreed strategic asset allocation.

   Fundamental Review – the previous policy was to undertake a fundamental review of the Fund's investments once in the life of the Council. It seems that an appropriate time to undertake the review is when the outcome from the valuation is known, so that due regard can be made of the investment return required to meet liabilities, and the level of investment risk that is appropriate given the nature of the liabilities. As a consequence the revised SIP changes the policy so that a fundamental review is undertaken once every three years following the valuation.

6. The revised SIP complies with the guidance given by the Secretary of State.

RECOMMENDATION

7. **The Committee is RECOMMENDED to approve the revised Statement of Investment Principles set out in Annex 1.**

PAUL GERRISH
Head of Finance & Procurement

Background papers:	LGPS (Management & Investment of Funds) Regulations 2009
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ANNEX 1

Statement of Investment Principles

1 Introduction

Oxfordshire County Council has drawn up this Statement of Investment Principles to comply with the requirements of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009. The Authority has consulted its actuary and independent financial adviser in preparing this statement.
Investment policy falls into two parts: strategic management and day-to-day management. The strategic management of the assets is the responsibility of the Authority and is driven by its investment objectives set out below. Day-to-day management of the assets is delegated to investment managers as described in the management of the assets section below.

2 Overall Responsibility

The County Council is the designated statutory body responsible for administering the Oxfordshire Pension Fund on behalf of the constituent Scheduled and Admitted Bodies. The Council is responsible for setting investment policy, appointing suitable persons to implement that policy and carrying out regular reviews and monitoring of investments.

The review and monitoring of investment performance and fund administration is delegated to the County Council's Pension Fund Committee. The Assistant Chief Executive & Chief Finance Officer has delegated powers for investing the Oxfordshire Pension Fund in accordance with the policies determined by the Pension Fund Committee. The Committee is comprised of seven County Councillors plus two District Council representatives. A beneficiaries' representative attends Committee meetings as a non-voting member.
The Committee meets quarterly and is advised by the Assistant Chief Executive & Chief Finance Officer and the Fund's Independent Financial Adviser. The Committee members are not trustees, although they have similar responsibilities.

3 Investment Objectives and Strategy

Investment Objectives

The investment objectives are:
1. to achieve a 100% funding level;
2. to ensure there are sufficient liquid resources available to meet the Fund's current liabilities and investment commitments;
3. for the overall Fund to outperform the benchmark, set out in the next section, by 1.3% per annum over a rolling three-year period.

In looking to deliver these objectives the Committee will take into account the fact that the Fund is immature with the cash received from employer and employee contributions exceeding the cash required to pay benefits and the costs of administering the Fund. This enables the Committee to take a long term view.

Risk

There are several risks to which any pension fund is exposed. The overriding risk is a deterioration of the funding level of the Fund. This could be caused by the differential movement of markets within the global economy or investment managers performing poorly and not achieving their target rate of return, or even their benchmark return.

To mitigate such risks, the following strategy has been adopted:

- retaining a proportion of investments in bonds to reflect potential changes in liabilities;
- investing a proportion of the fund passively to limit the impact of poor performance by investment managers;
- diversification of investments, including investing in alternative assets with a low degree of correlation;
- use of a number of different investment managers to spread the risk of poor performance.
- diversification of investment styles, e.g. growth and value

Investment managers are required to implement appropriate risk management measures and to operate in such a way that the possibility of undershooting the performance target is kept within acceptable limits. The managers report on portfolio risk each quarter.

Strategic asset allocation

In September 2009 the Pension Fund Committee agreed a customised benchmark for the strategic allocation of assets. This is set out in the table below:

Asset Class	Target asset allocation %	Range %
UK Equities		
- passively managed	10	
- actively managed	21	
Total UK Equities	31	29 – 33
Overseas Equities	32	30 – 34
Total Equities	**63**	
UK Gilts	3	
Index Linked Gilts	5	
Overseas Bonds	2	
Corporate Bonds	6	
Total Bonds & Index Linked	**16**	**14 - 18**

Property	8	5 – 9
Private Equity	10	6 – 11
Hedge Funds	3	2 – 4
Cash	0	0 – 5
Total Other Assets	**21**	
Total All Assets	**100**	

4 Management of the Assets

Following a fundamental review of the management of the Fund's assets in 2003, the Committee decided to switch from investment managers with a balanced mandate to a specialist management structure. As part of this review the Committee, advised by the Independent Financial Adviser, took over responsibility for strategic asset allocation. Once every three years, following the actuarial valuation, there is a fundamental review of how the assets are managed. The last such review was undertaken in November 2007.

The assets are currently managed as set out in the following table.

Asset Class	Investment Manager	Benchmark	Annual Target #
UK Equities	Baillie Gifford Legal & General	FTSE Actuaries All-Share FTSE 100	+1.25% Passive
Overseas Equities	UBS Global Asset Management	Various FTSE geographical indices	+1.0%
Global Equities	Alliance Bernstein	FTSE All World	+ 3.0%
Bonds & Index Linked - UK Gilts - Index Linked - Corporate bonds - Overseas bonds	Legal & General	 FTSE A All Gilts Stocks FTSE A Over 5 year IBoxx Sterling Non-Gilts JPMorgan Global Govt (ex UK) traded bond	+ 0.4%
Property	UBS Global Asset Management	IPD UK All Balanced Funds Index weighted average	+1.0%

Private Equity - Quoted Inv. Trusts - Limited Partnerships	 Peter Davies Adams Street Partners Group	FTSE smaller companies (including investment trusts)	+ 1.0%
Hedge Funds	UBS Wealth Management	3 month Libor	+ 3.0%
Cash	Internal	3 month Libor	-

\# Target performance is based on rolling 3-year periods

Legal & General have been given control ranges for each of the four sub categories of bonds & index linked. UBS Global Asset Management have been given control ranges for overseas equities relating to investment in their Global Pooled Fund and emerging markets. These ranges have been drawn up to ensure the Fund's investments remain well diversified.

Restrictions on Investment

The investment managers are prohibited from holding investments not defined as 'investments' in the LGPS (Management and Investment of Funds) Regulations 2009. Use of derivatives and currency hedging is permitted within pre-agreed limits. Underwriting is permitted, provided that the underlying stock is suitable on investment grounds and complies with existing investment criteria.

The regulations limit the powers of the Council to invest. The key restrictions are:

- not more than 10% (15%) of the Fund may be invested in unlisted securities of companies;
- not more than 10% of the Fund may be held in any single holding;
- not more than 10% of the Fund may be held as a deposit in any single bank, institution or person;
- not more than 2% (5%) of the Fund may be contributed to a single partnership
- not more than 5% (15%) of the Fund may be contributed to partnerships in total.
- not more than 10% of the Fund may be deposited or loaned to local authorities

Where figures are quoted in brackets, the Council could increase its limit as long as certain conditions are met. The Council has not decided to exercise this power at this time.

Realisation of Investments

Investment managers are required to maintain portfolios which consist of assets that are readily realisable. Any investment within an in-house or pooled fund which is not readily tradable requires specific approval. It is recognised that investment in Limited Partnership private equity funds are long term investments and as such are not readily realisable.

Monitoring and review

The individual manager's performance, current activity and transactions are monitored quarterly by the Pension Fund Committee. Investment management performance of the Fund is reviewed annually upon receipt of the annual report prepared by WM Performance Services.

5 Social, Environmental & Ethically Responsible Investment

The Council's principal concern is to invest in the **best financial interests** of the Fund's employing bodies and beneficiaries. Its Investment Managers are given performance objectives accordingly. However, the Council requires its Investment Managers to monitor and assess the social, environmental and ethical considerations, which may impact on the reputation of a particular company when selecting and retaining investments, and to engage with companies on these issues where appropriate. The Council believes that the operation of such a policy will ensure the sustainability of a company's earnings and hence its merits as an investment; it will also assess the company's sensitivity to its various stakeholders.

The Investment Managers report at quarterly intervals on the selection, retention and realisation of investments on the Council's behalf. These Report/Review Meetings provide an opportunity for the Council to influence the Investment Manager's choice of investments but the Council is careful to preserve the Investment Manager's autonomy in pursuit of their given performance. The Council will use meetings to identify Investment Manager's adherence to the policy and to ask Investment Managers to report regularly on any engagement undertaken.

6 Exercise of Rights attached to Investments

The Council takes an interest in the way the companies in which it has made investments manage their affairs. It will always exercise its voting rights to promote and support good corporate governance and socially responsible corporate behaviour.

In practice its Investment Managers are delegated authority to exercise voting rights in respect of the Council's holdings. They have been instructed to vote in accordance with the guidance set by RiskMetric Group. However, in exceptional circumstances managers may vote differently to the RiskMetric Group guidance, if in their judgement this would be in the best interests of the fund. Where managers take a contrary view to the RiskMetric Group they must obtain permission from officers to vote differently and officers must report this to the Pension Fund Committee.

Investment Managers are required to report quarterly on action taken. The Council, through its Investment Managers, may act with other pension funds to influence corporate behaviour and, apart from the exercise of voting rights in concert with others, may make direct representation to the boards of companies through its Investment Managers in concert with others, on issues of social responsibility.

7 Custody & Stock Lending

Custodian services are provided by BNY Mellon. In accordance with normal practice, the Scheme's share certificates are registered in the name of the custodian's own nominee company with designation for the Scheme. Officers receive and review internal control reports produced by the custodian. The custodian regularly reconciles their records with the investment manager records, providing a regular report to officers which they in turn review.

The custodian holds the majority of the Fund's assets. Exceptions include some pooled funds, held by the relevant investment manager's custodian, hedge fund assets and a working cash balance, which is held by the County Council and invested in the wholesale money market.

The Council allows the custodian to lend stock and share the proceeds with the Council. This is done to generate income for the Fund and to minimise the cost of custody. To minimise risk of loss the counter party is required to provide suitable collateral to the custodian.

8 Compliance

The Council will monitor compliance with this statement annually. In particular it will obtain written confirmation from the investment managers that they exercised their powers of investment with a view to giving effect to the principles contained in the Statement so far as is reasonably practicable. The Council undertakes to advise the investment managers promptly and in writing of any material change to the Statement.

The Pension Fund Committee has assessed itself against the updated Principles of Pension Fund Investment in June 2010 and is broadly compliant. This statement also complies with the guidance given by the Secretary of State.

9 Review of this Statement

The Council will review this Statement in response to any material changes to any aspect of the Fund, its liabilities, finances and its attitude to risk, which has a bearing on its stated investment objectives. A formal review of the strategic asset allocation will be undertaken annually. In addition the Council will undertake a strategic review of this Statement every three years to coincide with the actuarial valuation.