Statement of Investment Principles

Introduction

Hampshire County Council is the administering authority for the Hampshire Pension Fund, which covers employees of the County Council, two city (unitary) councils, 11 district councils, and 318 other scheduled and admission bodies. The total number of contributors is 57,815 and there are 59,857 deferred members and 36,519 pensioners.

The Local Government Pension Scheme (Management and Investment of Funds) (Amendment) Regulations 2009 require pension fund administering authorities to prepare and review, from time to time, a written statement setting out the investment policy for their Fund.

This Statement of Investment Principles has been drafted to comply with these regulations.

Types of investments to be held

The Fund can be invested in shares, bonds and other investments to limits defined in Schedule 1 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009.

The main limits are:

- no more than 10% of each portfolio can be invested in any individual holding

- no more than 25% of the Fund can be invested in each manager's in-house unit trusts.

The expected return on investments

The overall objectives when investing the Fund are:

- to achieve a 100% funding level, which means that all current and future Fund liabilities (pensions and other benefits) can be met in full for the foreseeable future
- to maintain a stable employers' contribution level, with a long-term target of around 200% of the average employees' contributions set for the actuary.

- The Fund's actuary, Aon Hewitt advised that the Pension Fund should set a target to achieve a long-term return 2.3% a year above a low-risk portfolio. A low-risk portfolio is defined as a portfolio invested 95% in index-linked gilts and 5% in fixed-interest gilts.

Spread of investments

The Joint Pension Fund Panel and Board agreed a specialist investment management structure in 2011, with the aim of achieving the Pension Fund's overall long-term target return without exposing the Fund to excessive risk. Following the review in 2014, the long-term asset allocation was set as shown in the following table.

Investment sector	Management style	% of Fund
Equities	- Passive	14.0
	- Low-risk active	14.0
	- High-performance active	26.0
Global bonds	Active	5.0
UK index-linked bonds	Passive	21.0
UK Property	Direct and indirect	10.0
Alternative investments	- Private equity and other	5.0
	- Infrastructure*	1.5
	- Hedge Funds	3.5
Total		**100.0**

* an additional 3.5% is available for infrastructure investments if suitable opportunities can be found.

2014 Investment Strategy Review

The completion of the actuarial valuation of the Pension Fund at 31 March 2013 by the Fund Actuary provided an updated view of the Pension Fund's liabilities and the level of investment returns necessary to meet those liabilities in the future, including the recovery of the deficit. This provided an appropriate opportunity to review the Pension Fund's investment strategy in the light of the results from the actuarial valuation.

The Pension Fund's previous investment strategy was providing the level of return required by the assumptions used in the actuarial valuation at March 2013. From that position, it was then considered whether any changes should be made to the asset allocation which would maintain or improve the level of expected return whilst reducing the level of risk.

The final investment strategy agreed increased the allocation to infrastructure and removed the tactical asset portfolio.

The increase in the allocation for infrastructure reflects the recent focus on the desirability of pension funds investing in infrastructure assets. Infrastructure can provide the Pension Fund with risk-adjusted returns that are reliable, index-linked, stable and long-term. In the short-term however, there may be a lack of appropriate infrastructure funds available for investment at suitable prices. The current level of demand by pension funds for infrastructure has driven up the prices for such funds.

The increased target for infrastructure may take a number of years to reach but acknowledging this now enables the Pension Fund to take advantage of whatever suitable opportunities arise in the future without being restricted by the need to change the investment strategy.

Realisation of investments

Managers are asked to avoid unnecessary sales and purchases of stocks, which incur transaction costs. They must regard all sales and purchases of stocks as being in the Fund's financial interests; that is, they will either improve the return or limit excessive risk.

Transaction costs are monitored closely and reported to the Joint Pension Fund Panel and Board once a year.

Managers of equity and bond portfolios are asked not to invest in stocks that are not readily realisable (capable of being turned into cash).

The Fund's cash can be invested for periods of up to two years in order to access higher investment returns in the current low interest rate environment.

Social, environmental and ethical considerations

The Hampshire Pension Fund has an overriding fiduciary duty in law to invest Fund monies to achieve the best possible financial return for the Fund consistent with an acceptable level of risk.

However, the Fund recognises that companies can enhance their long-term performance and increase their financial returns by adopting positive social, environmental and ethical principles in planning and running their activities.

The Fund has delegated to the external investment managers responsibility for taking social, environmental and ethical considerations into account when assessing the financial potential and suitability of investments.

Each investment manager is asked to work actively with companies to promote forward-looking social, environmental and ethical standards. This should not, however, deflect from the primary objective of achieving the best possible financial return for the Fund, in accordance with the Fund's fiduciary duty.

Exercise of rights attaching to investments

Managers have been instructed to exercise the Fund's responsibility to vote on company resolutions wherever possible.

They have also been instructed to intervene in companies that are failing and thus jeopardising the Fund's interests, by voting or by contacting company management directly.
The Fund believes that if companies comply with the principles of the UK Corporate Governance Code published by the Financial Reporting Council, this can be an

important factor in helping them succeed; but the Fund also accepts the need for a flexible approach that is in the common long-term interests of shareholders, company employees and consumers. The Fund's managers should cast their votes with this in mind.

In particular, the Fund's managers should cast their votes to ensure that:

- executive directors are subject to re-election at least annually
- executive directors' salaries are set by a remuneration committee consisting of a majority of independent non-executive directors, who should make independent reports to shareholders
- arrangements for external audit are under the control of an audit committee consisting of a majority of independent non-executive directors, with clear terms of reference – these should include a duty to ensure that managers closely control the level of non-audit work given to auditors, and should not significantly exceed their audit-related fee unless there are, in any manager's opinion, special circumstances to justify it
- in the managers' opinion, no embarrassment is caused to the Fund in relation to its beneficiaries, Hampshire residents, or the general principles of the UK Corporate Governance Code.

If managers do not follow these guidelines, they must report to the Panel and Board explaining why.

Custody

JP Morgan Chase has been appointed as the Fund's independent global custodian with effect from 1 August 2013 for a 5 year period ending on 31 July 2018, subject to satisfactory performance, with the option to extend the contract for a further 5 years.

Stock lending

Since 2006, the Fund has been part of its custodian's stock lending programme, whereby stocks (mainly equities) held by the Fund are loaned to third parties in return for a fee that helps the Fund meet its funding objectives.

In accordance with Schedule 1 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009, lending restrictions have been placed on JP Morgan to ensure that the proportion of Fund assets that are available to be lent at any time will not exceed 25% of the total market value of Fund assets.

To acknowledge the risks in stock lending, collateral is provided of at least 105% of the market value of the borrowed stock, unless the borrowed stock and collateral are denominated in the same currency, then a collateral level of 102% will apply. The collateral arrangements were tested in September 2008, when, within a few days, the Fund's custodian recovered stock on loan to Lehman Bros at the time of its collapse.

Although the Fund temporarily suspended stock lending in September 2008 as a result of the financial crisis, the Joint Pension Fund Panel and Board agreed that this should be reinstated from December 2009 as market conditions had normalised.

Overall, the Panel and Board considers that the income from stock lending benefits the Fund and that the risks are understood and well managed. The Director of Corporate Resources will continue to monitor the risks and, as in the case of the Lehman Bros collapse, would be able to instruct JP Morgan to suspend the programme with immediate effect.

Review of the Statement of Investment Principles

This Statement of Investment Principles is subject to review at any time by the Director of Corporate Resources, who will report to the Joint Pension Fund Panel and Board accordingly, seeking approval for any changes.

The six principles for the management of defined benefit schemes – compliance

Effective decision-making

The County Council has delegated responsibility for managing and administering the Fund to its Joint Pension Fund Panel and Board.

Panel and Board members and County Council officers can attend workshops and seminars on investment and pensions.
Detailed investment decisions are delegated to fund managers. Advice on asset allocation is sought from the actuary and other consultants as necessary.
The Director of Corporate Resources provides Panel and Board members with full briefings on investment and pensions. The Panel and Board also takes advice on investment from its independent adviser.

There is no power under LGPS regulations to pay Panel and Board members for pension fund work. A business plan, which includes a training plan, has been prepared.

The Fund's contract for actuarial and other advice is open to competitive tender periodically. Following a retender process at the end of 2014, Aon Hewitt was appointed Fund actuary from January 2015 for a period of 4 years.

Investment managers are asked for advice, and new approaches are developed in partnership with them.

Little use is made of other advisers, as the Finance function within Corporate Services has enough expertise. If external advice or consultancy is required, a procurement process will be followed according to the value of the work as set out in the County Council's Standing Orders policy.

Clear objectives

The Fund's objectives are set out clearly in this Statement of Investment Principles.

All mandates have clear objectives and timescales for performance assessment.

Acceptable levels of risk vary according to the nature of each manager's mandate, and are effectively determined by the agreed targets and timescales for performance assessment.

There are no soft commission arrangements.

The Fund's overall target return and the managers' individual targets are set out clearly in this Statement of Investment Principles and in the Annex.

Risk and liabilities

Advice from the actuary and other sources was used to determine the strategic asset allocation introduced from 1 January 2007 and the revisions made in 2011 and 2014, which should enable the Fund to meet its liabilities and maintain stable employers' contribution rates.

Advice was also sought to draw up the benchmarks and constraints within which the fund managers must work.

Performance assessment

Reviews of the managers' performance take place at quarterly intervals, either by the Joint Pension Fund Panel and Board or officers.

There is no formal system for reviewing the performance of Joint Pension Fund Panel and Board members.

Responsible ownership

The Fund's policies on voting rights and engagement are set out clearly in this Statement of Investment Principles.

Transparency and reporting

This Statement of Investment Principles covers all areas as proposed by the Myners Committee and subsequently confirmed by the Government.

The results of the Joint Pension Fund Panel and Board's performance monitoring exercises are published in the annual report for the Fund.

An updated Statement of Investment Principles is published and made available to scheme employers within three months of the Joint Pension Fund Panel and Board approving any significant amendment.

December 2016

Annex Investment management arrangements

	Benchmark	Annual target performance gross/net of fees
Low-risk active UK equities		
Schroder Investment Management	FTSE All Share	+1.25% gross
High-performance global equities		
Acadian Asset Management	MSCI World Index	+1.5-2.5% gross
Baillie Gifford	MSCI ACWI	+1.5-2.5% gross
Newton Investment Management	MSCI ACWI	+1.5-2.5% gross
Standard Life	MSCI ACWI	+1.5-2.5% gross
Active global bonds		
Western Asset Management	Barclays Capital Global Aggregate Bonds Index	+1.5% gross
Passive UK index-linked bonds		
Legal & General	FT British Government Over Five Years Index-Linked Gilts Index	
State Street Global Advisors	As above	
Passive global equities		
State Street Global Advisors	FTSE All World Equity Index	
Passive UK equities		
State Street Global Advisors	FTSE All Share Index	
UK property		
CBRE Global Investors	Retail Price Index (RPI)	+4.5% net
European property		
Aberdeen Property Investors	Eurozone Harmonised Index of Consumer Prices (HICP)	+5% net
Alternative Investments advisers		
GCM Grosvenor		+7.5% to +10.0% net (base)
Aberdeen Asset Management		+9.0% to +11.5% net (local)
Morgan Stanley		+5.5% to +8.0% net (local)

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