Q&A

How Tampa's Fire and Police Pension Meets Return Target and Stays 95% Funded

Harold J. Bowen, III, President, CEO and CIO of Bowen, Hanes & Co.

- The Tampa Fire and Police Pension Fund, managed by Bowen, Hanes & Co., returned 13.2 percent in the year ended Sept. 30, 2016
- The fund has an investment return assumption of 8.5 percent and is 95 percent funded
- The fund is focused on long-term performance and avoids riskier assets like hedge funds and private equity

Bowen spoke with Amanda Albright on June 1. Comments have been edited and condensed for clarity.

Q: Many public pension funds have struggled to meet their investment return assumptions. Your fund has a return target of 8.5 percent but has managed to stay well-funded. What are you doing differently?

A: Tampa is unique in a variety of ways. Foremost, we've managed every penny for 43 years. My father forged the relationship in 1974 when the fund was around $12 million. Assets are now approaching $2 billion. I know I'm biased but I would argue it's probably the most successful municipal fund in the history of municipal fund management — not only from an investment return standpoint but just in terms of being funded and the prudent way the fund's been run from an administrative standpoint. It's an exceptionally run city.

I don't know of another plan in the country that employs the Tampa model. What I'm talking about primarily is the fact that Tampa only has one manager, and the board allows us to take a really high-quality long-term investment approach.

Q: Where do you think other pension funds go wrong?

A: The core issue with these other funds is there is an entity involved there, an investment consultant, who comes in and becomes the key player in terms of investment strategy. Investment consultants decide they're going to have a stable of money managers. For a $1 billion fund, typically you'll have 20 or 30 money managers. You'll have every discipline under the sun — small-cap, large-cap, value, growth, foreign, fixed income, private equity, hedge funds — and it all flows from modern portfolio management theory that you need to be diversified. In theory, it might look very good and sophisticated. But in practice, oftentimes it leads to mediocre performance.

Tampa has never done that — Tampa does not have an investment consultant with a stable of money managers that are constantly being changed and evaluated on a quarterly basis.

Q: How are you seeing public pensions change their strategy?

A: You're seeing a big move toward passive investing or index investing. Municipal funds like Calpers and a host of others are deciding that, particularly on the stock side, they need to do much more passive investing. A lot of them are giving up on hedge funds because of the fees and the lackluster returns.

Q: What's your biggest concern in the market?

A: The Federal Reserve seems hell bent on normalizing interest rates. But the inflation data is moving against them, and the biggest risk right now to the market is that they could normalize rates too quickly based on an artificially distorted unemployment rate.

If you look at the labor force participation rate and you look at the employment-population ratio, those have just really trended down since the financial crisis and since the mid-2000s. The unemployment rate is really not what they should be focused on. I think they should be focused on price stability.

It's the inflation data that worries me, we still have not slayed these deflationary demons. I would hate to see a situation where they invert the yield curve. To me, that's the biggest danger.

Q: Where are you finding value?

A: Europe is attractive right now relative to the U.S. The global investment community is underweight European stocks and I think that's going to change. You're having some of the political uncertainty dissipate in Europe and you're having a pick up in economic activity, especially in manufacturing, which will feed into higher GDP growth. What we look at is these really high-quality, globally-oriented companies, like a Siemens or ABB.

On the American side, we're range-bound until we get clarity on the monetary policy and fiscal policy front.

Q: What solutions do you see for the public pension funding crisis?

A: What will help is if we get the economy growing again — if we get to 3 or 4 percent. That's going to really help.

I think this is a dangerous time to focus on bonds. I think a lot of these municipalities need to re-allocate their portfolios towards stocks. If you have a municipal fund that has 25 to 35 percent in fixed income, you can lose an enormous amount of money if we have a bear market in bonds. I just don't see where the money's going to be made in the bond market. Funds also need to move away from high-fee active managers and more towards passive investing.

Probably the end result is what you're seeing in Houston, where they've proposed issuing bonds to help fund the gap. There's going to be a reduction in benefits. There's going to be a balanced approach in terms of spreading the misery.