POLICE & FIRE PENSION INVESTMENT BOARD

August 13, 2015

Summary Minutes

The information in these meeting minutes is intended to assist Police and Fire Pension members in understanding the activities of the Investment Board. The information is not intended to provide investment or financial advice to any individual or organization and should not be relied upon for that purpose. While we attempt to keep the content accurate we cannot guarantee that all information is current, accurate or complete.

Members present: Doug McDaniel – Human Resources Director (Board Chairman)
Steve Hubka – Finance Director
Mark Westphalen – Mayoral/Council Appointment
Gerry Finnegan – Mayoral/Council Appointment
Becky Ferguson – Mayoral/Council Appointment
Steve Niemeyer – Police Electee
Jeremy Gegg – Fire Electee
Guy Pinkman – Fire Electee
Matt Franken – Police Electee

Members Absent: None

A quorum is any five Board members.

Human Resources
Staff: Paul Lutomski – Police and Fire Pension Officer

Others present: Dale Connors – Watershed Investment Consulting

Unless otherwise noted, meeting materials were provided to Investment Board members in electronic format, or printed format, a few days preceding the meeting for their advance consideration. Printed copies of the materials were provided at the time of the meeting.

Documents:
Watershed Quarterly Investment Analysis June 30, 2015
Meeting minutes for February 12, 2015
Meeting minutes for May 14, 2015

Doug McDaniel calls the meeting to order at 2 pm. He asks for a motion to approve or amend the minutes of the February 12, 2015 and May 14, 2015 meetings.

Mark Westphalen moves to approve the February 12, 2015 minutes.
Jeremy Gegg seconds the motion.
All members vote to approve.

Paul Lutomski asks for an amendment to the May 14, 2015 minutes to the correct the date of the meeting written on the minutes. Steve Hubka asks for an amendment to indicate he was present.

Jeremy Gegg makes a motion to approve with the amendments.
Matthew Franken seconds the motion.

All members vote to approve.

Doug McDaniel asks those recently attending conferences to present.

Guy Pinkman states he attended the Opal Financial Emerging Managers conference in Chicago. The format was to meet individual managers one-on-one in rapid succession. He stated the managers were not necessarily managing investments from emerging markets nor starting their first fund, but rather mostly private equity managers that had prior fund experiences working on their gaining commitments for their next fund. He did not recommend any of the investments.

Matt Franken attended the Opal Financial Public Funds East conference in Newport, Rhode Island. He stated a discussion on education occurred and suggested we offer educational sessions for members especially regarding pre-retirement. Other topics included annual manager reviews; hedge fund fee reduction by pension funds working together may be an anti-trust violation; China may be overvalued, they are moving from an economy of production to one of consumption that cannot be maintained; demand for real estate retail and office is decreasing. He asks if the plan has any real estate investment in China.

Dale Connors states the VOYA manager invests in China, but we will look at real estate options later today.

He states that the return expectation for FY 2014-15 contains a possibility that it may be flat.

The Markets Review tab: A lot of negatives. Most are due to dollar strength. The local market may have been positive, but converted to dollars the return declined. Reviews market figures for S&P and EAFE. Europe is starting to come out the a double dip recession. Markets tend to lead economic activity. Rates are starting to go up. Meaning bonds decline in value. Longer maturity bonds are more affected. Our two domestic bond managers are corporate focused. Hedge funds up more than US Stocks or bonds. Real estate has been the big winner. MLPs are tied to energy and energy has been down. Our target is 7.5%. Managers are underperforming the policy index.

Total Fund tab: Page 11 volatility has been reduced. Cashflow on Page 12 discussed. Page 13 policy target discussed. JPMorgan is expected to finalize sale of Alternative Property Fund soon. Page 17 graph; 3 and 5, exceed 7.5% target, but not the 10 year return. The 1 year policy index is in the 2nd percentile compred to competitors, but the manager under performance, total fund, is in the 70th percentile, so we need to keep working on the managers. Page 18 discusses listed sectors. US Equity mentioned as lower return because to MLP and infrastructure. The real estate index is NCREIF, but we have REITS, so we will look at changing the index to include REITS.

Paul D. Lutomski asks if an index fund exists for NCREIF.

Dale Connors answers that there is no investible index for NCREIF.

Equity tab: Begins discussing managers. Board Managed Dividend Fund is not performing as well as others. Tortoise is doing well on a relative basis, but on an absolute basis returns are bad. They buy mostly MLPs of pipelines. Revenues are stable, but contract re-negotiation expectations have caused the price to decline. It appears China's demand for oil is going to decrease and even though the US does not export much to China the demand for oil my remain lower.

Mark Westphalen comments that there are more influences on US oil and MLPs than China.

Dale Connors agrees and advocates a wait and see attitude for now. If prices stay here Tortoise is a 7% yield.

Gerry Finnegan asks for more description regarding China's influence on the world market.

Dale Connors states Wall Street did not expect the Chinese currency devaluation and does not know what to expect. This move implies China is trying to increase manufacturing and exports by devaluing their currency and that oil demand should increase if that is the case.

Dale continues manager discussion.

Fixed income tab: Loomis Sayles has split rated and high yield bonds. Split rated bonds are rated differently by S&P and Moody's. If a bond is moved to investment grade there is a price increase. That is not working right now. Pioneer is similar, but more active in adjusting duration lower to avoid decline caused by interest rate increase. We will work on that in the next meeting.

Other bond manager, Templeton global, buy only government bonds, and mostly non-US bonds. They were hurt because their gains in bonds were offset by currency losses.

We have lowered position in bonds and may suggest more lowering if rates continue to decrease.

Alternatives tab: Blackstone hedge fund of funds is doing well. Real estate managers discussed. VOYA is sub-advised by CBRE. VOYA invests in global REITS. They are a good manager in a bad sector of the market. Rreef is a core manger. We advised increasing and you have done that. Rreef has purchased existing office and industrial. Those are cyclical. Residential is not cyclical. Most managers are increasing cyclical holdings. Office takes 3 years to build so having them when they are in demand allows for increasing rents. Industrial is in demand by Amazon and FedEx type businesses. PRISA is a value added manager. They buy and improve, or build, lease them out, and then sell. The JP Morgan Alternative Property Fund is down to one building. Tenaska is an energy limited partnership and has a negative return. 2007 year fund, typically 10-15 years to finish.

Be aware that the fiscal year ending August 31 is going to be one of the worst in recent history. That affects the demand for contributions and the GASB calculations. The fund is performing well on a relative basis but the markets have not returned well.

Dale Connors presents the Equity Portfolio Structure Review. Relative valuations indicate it may be time to lessen US Equity overweighting as compared to foreign equity. US dollar is very strong relative to other currencies, so an investment made with foreign currency will increase if the US dollar decreases. Current equity portfolio is underweight large cap. Also, mid and small cap are relatively expensive compared to large cap. As the economy expands, growth stocks outperform value stocks.

Recommendation
Sell Baron Growth Fund (mid-cap growth US equity). This is approx. 2.5% of portfolio or $5 M.
Sell Vanguard Total Stock Market Index Fund so holdings decrease 5% to 25% of the portfolio, approx. $10 M.
Buy equal amounts of non-US large cap equity of existing EuroPacific Growth Fund and Oakmark International Fund.

Doug McDaniel asks for a motion.

Gerry Finnegan moves to approve the recommendation.

Mark Westphalen seconds the motion.

Doug McDaniel asks if there is any discussion.

Mark Westphalen asks if an index is available.

Dale Connors answers there is a Vanguard Developed Market index, it has a low expense ratio, but did not recommend it because both of the active managers have consistently outperformed the index and EuroPacific Growth has a low expense ratio.

Gerry Finnegan states his bias toward index funds is derived from most of the markets can be efficiently indexed, but the micro-cap domestic stocks, distressed companies, and emerging markets can not, and we are talking about such a space and have no problem with active managers in this space.

Becky Ferguson agrees that recent research supports active managers can add alpha in this space.

Doug McDaniel calls for a vote.

All members vote in favor.

Becky Ferguson excuses herself from the meeting as it is running long and she has another meeting.

The next topic is the REIT Manager Search. Dale Connors refers members to page 103 of the Quarterly Investment Analysis as it shows all real estate of the plan and presents the REIT Manager Search document. Dale explains REITs (Real Estate Investment Trust) own stock in companies that own real estate. He lists the four final candidates and introduces the basics of each manager. Three are three active managers and one index.

The next pages list each manager account format, items such as fees, minimum investments, assets under management. The detailed information on each manager including organization, staff, philosophy and process, and portfolio construction is presented. All active managers are described as providing good and consistent returns relative to the index and index fund is described as tracking the index closely for low cost. Diversification, turnover, average market cap, dividend yield. Trailing returns for 1,3,5,7 and 10 years compared to benchmark, calendar returns for last 10 years. Risk-reward 3, 5, 7, and 10 years. Risk statistics Trailing Std Dev., Trailing Sharpe Ratio, Trailing Tracking Error, Up/Down capture 7 years agains benchmark MSCI US REIT FGR USD. Prefer US over global because US is more developed, stable and higher returns. Prefer risk performance of Principal or CenterSquare, but notes that any manager in this list would be good and that several clients own the index.

Board discusses.

Paul Lutomski states VOYA is $9 M.

Steve Neimeyer makes a motion to sell VOYA and buy either Principal or CenterSquare.

Paul Lutomski states $11 M would get the plan closer to the 15% target real estate allocation.

Dale offers that Principal is 10 bp less expensive than CenterSquare. CenterSquare is a little more value add, Principal more concentrated.

Guy Pinkman makes a motion to invest $11 M with Principal.

Steve Neimeyer seconds the motion.

All members vote in favor.

Dale states he and Paul are working to lower expenses to the fund. He states the plan is switching Pioneer vehicles to a less expense one that is a commingled investment trust.

We will look at fixed income at the next meeting.

Doug McDaniel asks if anyone has new business. There being none the meeting concludes at 3:35.