POLICE & FIRE PENSION INVESTMENT BOARD

April 12, 2016

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
Guy Pinkman – Fire Electee
Matt Franken – Police Electee

Members Absent: Jeremy Gegg – Fire Electee

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:
Meeting minutes for November 12, 2015
Watershed Preliminary Monthly Performance March 31, 2016
Watershed Core Fixed Income Manager Search.

Doug McDaniel calls the meeting to order at 2 pm. He asks members to review the minute of the last meeting for a vote at the next meeting. He provides an update on the Citizen Review Committee sharing that they have submitted a few benefit changes to the plan actuary for cost estimates.

Gerry Finnegan asks the date of their next meeting.

Doug McDaniel answers April 21 4 pm in the Mayor's Conference Room. He asks Steve Niemeyer to report on his recent conference.

Steve Niemeyer reports that there were many different perspectives on the future of the markets. He lists negative discussed and those included debt levels increasing and the potential for default increasing. The positives included job growth. The current bull market is the 2nd longest and the 2nd strongest and therefore concern exists regarding its cycle ending. China growth rate is slowing. Private Equity valuations are getting high. Conference attendees discussed the need for boards to be more forward looking, planning for different significant market scenarios in advance and advocating giving authority to act to those in a position to do so. Major threats to public pensions were seen as lower returns and increased longevity.

Doug McDaniel thanks Steve and asks Dale Connors to present.

Dale refers to the Watershed Preliminary Monthly Performance March 31, 2016. Major benchmark returns are shown on page 1 with many noted as negative for the 12 months ending March 31, 2016, the worst being MLPs, commodities and emerging market equity. Fixed Income High Yield was also negative. A representative from the Principal Bond fund will make a short presentation at the May meeting. A comparison of target vs. actual allocation is discussed with graphs and tables. Next discussed are individual investment cashflows and a performance for several time periods from 1 month to 10 years. Assets finish 2015 at $201M. Finally a Fee schedule per investment and in total, 0.58%, is displayed.

The rest of the presentation regarding Fixed Income.

Currently Fixed Income comprises 20% of the portfolio:

LSBDX Loomis Sayles Bond Instl	$13,473,743
PMSFIT Pioneer Multi-Sector Fixed Income Trust	$13,996,620
FBNRX Templeton Global Bond R6	$13,682,739

Loomis Sayles Bond Instl and the Pioneer Multi-Sector Fixed Income Trust are non-core styles that invest a significant portion of their portfolios in non-investment grade (high yield) and non-dollar (non-US) denominated securities. Both bond managers have about 30% in high yield investments.

Pioneer is less credit focused than Loomis in that the manager also adjusts duration and curve positioning, as well as utilizes non-$ instruments.

Templeton Global Bond invests primarily in sovereign debt, like Treasury bonds of non-US countries. It does not invest in US bonds. Often sovereign debt is not AAA grade, like US Treasury debt.

None of these funds is considered a core bond fund.

The pension's current Fixed Income structure lends itself to a comparison with, and is benchmarked in the Investment Policy to the Barclay's US Universal Index - an index of global bonds including high yield/non-investment grade bonds. Most pensions seek to compare to the Barclay's Aggregate index – an index of US denominated investment grade bonds that contains neither foreign bonds nor high yield bonds.

Bond indexing is not technically feasible because an investor cannot buy the bundle of bonds in the index, as an entire bond issue may be held by investors and not for sale. Bond index funds will underperform their index because of fees.

Referring to the Watershed Core Fixed Income Manager Search. The document details commingled bond funds from three firms: Barrow Hanly Mewhinney and Strauss (BHMS), J.P. Morgan, and Prudential. An update to the document is that the JP Morgan fee is 0.0375%. Fees are less than the non-core managers used currently because core funds management is less complex and less expensive to manage. All funds offer daily liquidity. Other data were Assets Under Management, organization and background, investment staff.

Guy Pinkman asks about business continuity in case listed staff leave the firm.

Dale Connors answers with an explanation involving specific staff and locations. He continues with a presentation on each firm's process, philosophy and process, portfolio construction, holdings, portfolio metrics. BHMS has a relatively concentrated portfolio with 198 holdings compared to 1053 for JPM and 1359 for Pru.

Gerry Finnegan asks if issuer, coupon and maturity differences constitute a holding.

Dale Connors answers yes and continues with other metrics, maturity profile compared to the index. Here JPM held relative equal amount in various maturity ranges, with BHMS and Pru closely matching the index.

Credit quality: JPM can use CMBS as a substitute for Treasuries to get a yield advantage. However, sector exposures per firm show all three currently closely follow the index.

Regional exposure, returns were all very close with JPM slightly higher, Standard deviation: JPM slightly lower, tracking error: Pru is lowest.

Sharpe Ratio: JPMorgan's low volatility results in a better Sharpe Ratio than BHMS and Pru, but all are very good.

Information Ratio relates to tracking error and return. Low tracking error and high return result in a high information ratio. Due in part to low tracking error Pru has highest information ratio.

Risk/return quadrant graphs for various time periods show JPM slightly lower S.D. and slightly higher return.

Up/Down capture for various time periods show BHMS with slightly more upside capture and JPM with significantly less downside capture.

Becky Ferguson praises JP Morgan's bond management.

Matt Franken states he observed Templeton losing money faster than Loomis.

Becky Ferguson and Dale discuss Templeton as a good fund that is completely non-US dollar, as a currency fund, which does not hedge, is being whipsawed by currency exchange rates.

Paul Lutomski asks if next month the Board would look at selling Templeton and reinvesting in equities.

Dale Connors responds affirmative and clarifies all or some of Templeton and reinvestment could include other than equities. He states a preview of the next meeting is asset allocation comparing on a 10 and 20 year expectation basis, because they are so different. That he has only used 20 years previously, but want to show the 10 year because it is so different.

Mark Westphalen states his concern that if fixed income is expected to earn 2% the remaining assets must earn a lot to have the entire portfolio earn 7.5% and the Board discusses that a slightly lower credit quality, or lesser fixed income allocation, could enhance the overall return.

Dale explains that the Fixed Income class is the only part of the portfolio with a negative correlation to equity, and that is needed. He states his intent to discuss distressed debt to be ready if the time comes to consider that type of investment. He was successful with this strategy in 2009 and feels that is the best way to ern higher returns in fixed income.

Becky Ferguson affirms that a fixed income component is important in a down equity market.

Dale Connors states for index funds REITS have been included within the finance sector, but this summer will be its own sector, and therefore required to be held in many indexes, and therefore will behave differently – either less of more volatile. He states he is comfortable with the fixed income sector being conservative and the remainder less conservative.

Doug McDaniel calls for a motion to approve or deny the Watershed recommendation.

Becky Ferguson makes a motion to sell all shares of the Loomis Sayles Bond fund and reinvest all proceeds in the commingled JP Morgan bond fund.

Steve Hubka seconds the motion.

The Board discusses the amount (~$13.4M) the turnover ratio of JPM and use of derivatives such as futures and options, but they do buy CMBS (none of the three use future and options).

At the end of discussion Doug calls for a vote.

All members vote approval.

Dale states the liquidation of the dividend portfolio is taking longer than expected because the dividend reinvestment program (DRIP) needed to be turned off. Discussion that a discount broker was contacted but could sell fractional shares, US Bank could not sell fractional shares, Smith Hayes was contacted and agreed to sell the fractional shares for a fee equal to what US Bank would have charged.

Doug asks if the Board has any new business. There being none the meeting is adjourned.