

**MINUTES OF SEPTEMBER 11, 2014 RETIREMENT BOARD
CITY OF ALEXANDRIA
FIREFIGHTERS AND POLICE OFFICERS PENSION PLAN
DUE DILLIGENCE MEETING**

PRESENT

| <u>Members</u> | <u>Others</u> |
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| Nelsie Birch (Management) | Barry Bryant, Dahab Associates |
| Michael Cross ² Secretary (Fire) | Bryan Capelli, Retirement Specialist |
| Patrick Evans ¹ (Fire) | Shane Cochran, Supplemental Retirement Board |
| Tom Gates ³ Chairman, (Management) | Kadira Coley, Acting Retirement Administrator |
| Jean Kelleher ² (Management) | Brenda D'Sylva, Supplemental Retirement Board |
| Shirl Mammarella ³ (Police, Alternate) | Bill Eger, Supplemental Retirement Board |
| Ed Milner ¹ (Police) | Bob Gilmore, Supplemental Retirement Board |
| Rick Muse ³ (Fire, Alternate) | Arthur Lynch, Retirement Specialist |
| Al Tierney ² (Police) | Nancy McFadden, Supplemental Retirement Board |
| Laura Triggs ³ (Management) | Theresa Nugent, Retirement Specialist |
| | Marietta Robinson, Supplemental Retirement Board |
| | Valarie Wright, Supplemental Retirement Board |
| | Sergey Zelensky, Retirement Specialist |
| | Damon Ficklin, Polen |
| | Jim Haymes, Polen |

Absent:

Jack Browand (Management, Alternate)

Terms: 1/1/2014 – 12/31/2015

¹Purchase of Service Credit Committee

²Technical Corrections and Plan Document Review Committee

³Vendor & Service Provider

CALL TO ORDER

The meeting was called to order at 8:37 AM on September 11, 2014.

In remembrance of the events that occurred on September 11, 2001 the meeting was paused to observe a moment of silence at the time each plane impact.

MEETING RECORD

Mr. Cross made a motion to

Approve the August 14, 2014 minutes.

Ms. Triggs seconded the motion. The motion was unanimously approved (7 – 0).

Mr. Eger & Mr. Milner arrived at 8:40 AM

FINANCIAL REVIEW

Dahab distributed their quarterly report booklet. Mr. Bryant noted the following items:

- 2nd Quarter was an above average quarter for stocks
- Emerging markets did better than domestic markets, Large and mid-cap stocks performed better than small cap stocks
- Bonds also did well.
- Numbers shown in the shadow index may be low because returns for the Cambridge index (private equity) are not available.
- Polen, Herndon and Champlain all underperformed for individual reasons. There was no across the board issue and Mr. Bryant was not alarmed by their underperformance.
- All active managers have underperformed the benchmark since inception.
 - Mr. Bryant noted that our active managers were hired to protect in down markets. He is recommending we wait for a down market and a full market cycle before we evaluate managers or recommend any changes.

Ms. Kelleher arrived at 8:45 AM.

Mr. Bryant provided updates on specific funds.

- Molpus – commitment to timber, Molpus Fund IV for \$3.7 million in 2013. We secured our commitment prior to the first close. No calls have been made at this time. Expect final close in November.
- Hamilton Lane & Private Equity – target allocation to private equity is 5%. Currently at 2.7%. Mr. Bryant reminded the board about vintage year diversification and the process of calls in the early years and distributions in the later years. The average private equity portfolio takes 8 to 10 years to build. Mr. Bryant recommended hearing a presentation from Hamilton Lane and will follow up with them.

Mr. Muse arrived at 9:01 AM.

- PRISA – Mr. Bryant reviewed our real estate allocation and its performance. He noted that the index for real estate differs from other indexes in that it is based on manager returns rather than stock returns. One of issues with this is that many real estate managers use leverage. Mr. Bryant noted that the PRISA investment is one that was inherited from when Prudential managed the assets for the funds.
- PIMCO – Mr. Bryant discussed the management changes at PIMCO. Concern was raised about the fact that 20% of the plan's assets are invested in PIMCO funds. Mr. Bryant noted that PIMCO's performance historically made some negative returns but now seems to be back on track.
 - A board member asked if PIMCO's lead person, Mr. Gross leaves would that affect the monies invested with PIMCO. Mr. Bryant discussed what could happen to our investment with PIMCO if a large percentage of money was withdrawn. He pointed out that the sale would cause prices to drop but believed it would bounce back.
 - Board members asked if we should consider diversifying our bond investment. Mr. Bryant noted that funds of our size and larger may have more than one bond manager. Mr. Bryant felt we could get some specific attention by diversifying with a smaller bond fund. Mr. Bryant also noted that our investment with PIMCO is a Core+ investment which invests in a variety of bonds and gives us diversification over just the Barclays Aggregate. If the board was seeking something comparable we'd have to invest in an all asset manager or split between core and high yield bonds.
 - Mr. Bryant suggested we plan to speak with bond managers two quarters from now.

MANAGER REVIEW – POLEN CAPITAL

Mr. Damon Ficklin and Mr. Jim Haymes of Polen joined the meeting. They began their presentation by reviewing Polen's mission statement. They noted that preservation of assets is stated before growth of assets. They also noted that the statement speaks about protecting the present before enabling the future. Both of these points highlight Polen's philosophy.

Page 2 shows an overview of the firm. Page 3 displays the investment team. Polen noted that 4 new analysts were recently added and are dedicated to their US domestic product.

Page 4 focuses on the firm's investment philosophy. They noted that they focus on 20 high quality companies which has allowed them to grow faster than the market. Polen attempts to choose the best quality companies to decrease the amount of risk assumed. They choose companies with a long-term focus and hold stock for an average of five years. Thus, with the length of holding returns are driven by growth of the selected companies and not by transactions. Polen tends to stay away from companies with debt or leverage.

Page 5 shows the portfolio as of the end of August. Polen noted that their return on total capital (ROTC) was over 26%. Polen's ROTC is more than double their competitors. Page 6 shows the account performance for the City of Alexandria's funds. Polen noted that the City's account performance is in line with their mid-teens target at an average of approximately 14.5%. Note this return did trail the Russell 1000 Growth index which returned approximately 17.00% for the same time period since inception.

Page 7 shows an attribution analysis for the portfolio. The chart of the bottom left highlights the top 5 and bottom 5 performers. Polen noted they don't really have any major detractors. The top detractor is cash and it's a win if cash is the biggest detractor in the portfolio. Page 8 shows the same information on page 7 for the year to date in 2014. Polen noted that the detractors for this period were consumer based stocks. Each company is doing well so they are not concerned about the short term dip in performance.

Mr. Bryant asked if Polen had considered investing some their cash holding into a Russell 1000 index fund. Polen stated that that was not a part of their strategy. Typically their cash holdings are small and lie between 2% and 3%.

Page 9 shows the Barra index which looks at factor return rather than sectors. Polen noted that leverage has done well in the recent market. Polen is under exposed to leverage.

Page 10 shows historical returns relative to the index for different rolling periods. Polen has consistently outperformed in the long term. Polen pointed out some reasons why the index may have outperformed. During the 90s tech bubble low quality companies led the high market returns. Polen does not invest in low quality firms. In 2003 low quality companies also did very well. In 2006 metals drove the market up. And again 2010 through today low quality companies are driving returns.

Polen noted that they do not believe the current market conditions can continue to sustain at the current pace. Their company will stick to their established discipline and will outperform in the down market.

A couple of board members noted that Polen had been hired with the down market in mind. It was noted that when Polen was hired it was known that they would underperform in extreme up markets but also promised to provide downside protection. The Board will re-evaluate Polen's performance following the next down market.

The meeting broke at 10:20 AM and resumed at 10:28 AM.

DAHAB'S CORNER

Risk Article

Mr. Bryant discussed the risk article written by John Bogle. He noted that this article was written before the financial crisis. The article talks about the black swan event aka. the thing that didn't think could happen. Mr. Bryant noted that risk statistics are not perfect. Risk statistics typically use a 1-year measurement period. This is a very short time horizon for investments. He also noted that risk statistics don't account for the black swan event of the thing that has never happened before. Mr. Bryant recommended all board members take the time to read the article.

ADMINISTRATOR'S REPORTS

Regular Investment Reports

No rebalancing was required.

Private Equity

Hamilton Lane Fund II & Fund VII had a distribution since the previous meeting.

Other Items

Education: seminars, conference and training

- The IFEPB's CAPPP training is being offered in DC. Part 1 is September 29-30 and Part 2 is offered October 27-28. Staff apologized for the short amount of time to plan but explained they were just notified of the classes last week. Staff encouraged all trustees who are able to plan to attend one or both of classes. Details about the courses are included in handout 7(b)(i)(1).

Mr. Cross made a motion to

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| Approve the cost of training for any trustee who wants to attend the CAPPP training in DC. |
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Mr. Tierney seconded the motion. The motion was unanimously approved (8 – 0).

- The fall AMRS-VA meeting will occur in October. Board members are encouraged to let Staff know if there are questions they would like Staff to ask or discuss during the conference.

Follow-up Items

- ICMA-RC Allocation Statistics – a PowerPoint presentation from ICMA-RC is included in the packet (handout 7(b)(ii)(2). ICMA-RC will be invited to the November due diligence meeting.
- Election Update – Mr. Ed Milner won the contested election for the Police Officer employee representative. Ms. Mammarella, Mr. Muse and Mr. Evans run uncontested and will continue in their current positions.

COMMITTEE REPORTS

Technical Corrections and Plan Document Review Committee

The committee (Mr. Cross, Ms. Kelleher & Mr. Tierney) has plans to meet to discuss the proposed amendment. The proposal will be brought to a future meeting.

Purchase of Service Credit Committee

No report was given. Committee has plans to meet in the next month.

Vendor & Service Provider Review Committee

The next contract to come up for review is the Dahab contract. The committee will reconvene to see what contracts need to be reviewed.

A trustee asked about the Prudential administration contract. Staff noted that given the transition that has occurred this project has been slowed down.

OLD BUSINESS

Disability Recertification – a draft of the recertification process was distributed after the meeting.

NEW BUSINESS

Asset Allocation Study

Mr. Bryant walked the Board through the model and how it works. He reminded the board that they chose asset classes and ranges of allocation for each asset class. The portfolio is run a bunch of times using different randomly selected investment returns for the S&P 500. Then returns for the other asset classes are chosen based on their correlation to the S&P 500. The model then calculates the mean return, the standard deviation (risk) and the Sharpe ratio (which is measure of efficiency and is a combination of the mean return and risk/standard deviation.)

Mr. Bryant noted that the model is presented in a variety of scenarios 20-year returns, 70-year returns, mean reversion, special scenario with lowered bond returns. Mr. Bryant recommends the Board pay attention the 20-year return. He specifically noted that the 70-year returns have an extremely high return for small cap stocks which can throw the results off.

Mr. Bryant explained the recommended scenarios included in the presentation booklet. Mr. Bryant discussed his concern about potentially being overexposed to equities if we have another year similar to 2008/2009. He is recommending the Board consider the PIMCO All-Asset fund as an alternative investment. He noted that this would be a new concept for Board and would recommend a separate educational on that investment. Mr. Bryant noted that the All-Asset fund is invested in a bunch of assets including international fixed income. The fund is restricted to PIMCO and RAFI investments.

A trustee asked about why real estate is limited to 10%. Mr. Bryant noted that that is just not done in a portfolio of our size. He mentioned that real estate can become extremely illiquid and would only be comfortable going up to 10% of the portfolio.

Staff expressed concern about how the model's returns are forecasted inflated expected future returns. Mr. Bryant said the returns from the model are correct using the historical returns not artificial future forecasted numbers. He noted that some people believe long-term returns will be at this rate in the future. He also noted that the focus should be on the asset allocation mixes and the relationships between the asset classes.

He noted that farmland was highly favored by the model and may be overstated in the current scenarios. He recommended re-running the model taking farmland out of the model. Mr. Bryant will present the updated study to the Board at the interim meeting in October.

NEXT MEETINGS

1. October Meeting – staff will reach out to reschedule the October Interim meeting.
2. Thursday - November 13th at 8:30 AM, Sister Cities 1101, Due Diligence Meeting
3. Thursday – December 11th at 8:30 AM, Sister Cities 1101, Interim Meeting

ADJOURNMENT

The meeting adjourned at 12:50 PM.

HANDOUTS

Distributed to Board members in the Board Packet:

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| Agenda |
| City to Host Moment of Silence in Remembrance of September 11, 2001 [1(a)] |
| Minutes of Prior Meeting [3(a)] |
| Risk Article by John Bogle [6(b)] |
| Monthly Investment & Rebalancing Report [7(a)(i)] |
| Private Equity Cash Flow Report [7(a)(iii)] |
| CAPPP Brochure [7(b)(i)(1)] |
| Administrator's Follow-Up Items List [7(b)(ii)] |
| ICMA-RC PowerPoint – DC plan stats [7(b)(ii)(2)] |

Distributed to Board members at the meeting:

- Dahab's Performance Review Report – June 2014
- Dahab's Deferred Compensation, Defined Contribution & ROTH IRA Performance Review
- Polen Capital Presentation Booklet
- Dahab's Asset Allocation Study – September 2014