

**MINUTES OF NOVEMBER 12, 2015 RETIREMENT BOARD
CITY OF ALEXANDRIA
FIREFIGHTERS AND POLICE OFFICERS PENSION PLAN
DUE DILIGENCE MEETING**

PRESENT:

<u>Members</u>	<u>Others</u>
Jack Browand (Management)	Barry Bryant, Dahab Associates
Jean Kelleher, Secretary ² (Management)	Noraine Buttar, Special Asst. to City Manager
Shirl Mammarella ³ (Police, Alternate)	Bryan Capelli, Retirement Specialist
Ed Milner ¹ (Police)	Kadira Coley, Retirement Administrator
Rick Muse, (Fire, Alternate)	Charles Curia Supplemental Board
Al Tierney ² (Police)	Robert Gilmore, Supplemental Board
Laura Triggs, ³ (Management)	Arthur Lynch, Retirement Specialist
Christina Zechman Brown (Management, Alternate)	Theresa Nugent, Retirement Specialist
	Marietta Robinson, Supplemental Board
	Eric Sabol, PRISA
	Michael Stewart, Deputy Director Finance
	Sergey Zelensky, Retirement Specialist

Absent:

Michael Cross ² Chairman (Fire)

Patrick Evans ¹ (Fire)

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 8:41 AM on Thursday, November 12, 2015.

Introductions were made and Ms. Noraine Buttar, Special Assistant to the City Manager was introduced to the board. As part of her rotation she may be attending the board meetings.

MEETING RECORD

Mr. Tierney made a motion to:

Approve the October 8, 2015 minutes.

Ms. Mammarella seconded the motion. The motion was unanimously approved (5 – 0).

FINANCIAL REVIEW

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

- Overall this was a bad quarter for the market.
- GDP was disappointingly low at 1.5% for the 3rd quarter. This has raised concerns about the economy faltering.
- The jobs report numbers were low but better than previous quarter.
- Most of ground that was lost in the 3rd quarter has been gained back already in October.
- The third quarter is the worst quarter for domestic equities in the past 6 years
- Driven by concerns about China – filtered into their stock market
- Wall Street goes on “vacation” in August. The markets experienced a lot of panic without the “value” buyers available.
- Domestic equities were down across the board. Large Cap performed better than small cap and growth outperformed value stocks. Developed foreign stocks down 10%, while emerging markets were down 18%. Emerging Markets are commodity driven which drove down market.
- Fixed income rates went down because of panic despite the fact that everyone is expecting rates to rise. There was a flight to longer term stable fixed income.

Ms. Kelleher arrived at 8:48 AM.

Manager Performance Summary (page 10)

- Composite return is -6.1% in quarter; in the 87th percentile (vs other public funds); shadow index is -6.2%
 - Polen had a great quarter in 1st percentile
 - NewSouth had a great quarter in the 19th percentile
 - PRISA was up 4.9% versus index at 3.7%
 - Herndon & Champlain below benchmark
- Asset allocation – main determination of relative return – we are higher weighted in mid-cap and small-cap and lower allocation to bonds. Plan’s portfolio is risk oriented portfolio and positioned to do better in up markets.

Investment Manager Discussions

Herndon

- Herndon hurt by sector allocation within their portfolio
- Herndon has been a long standing problem, Firefighters and Police Officers Pension Board had previously passed a motion to allocate a portion of their large cap value funds to an index fund.
- Based on current and past performance Mr. Bryant is recommending that the Board take action to move all large cap value money from Herndon to the an index fund.
- A trustee asked why Mr. Bryant is recommending a transition away from Herndon today.
 - Mr. Bryant noted that Herndon’s performance has continued to lag the benchmark and given their investments he does not see them being able to make up the lost ground.
 - Mr. Bryant noted the board has two choices if the Board decides to move forward with moving the money from Herndon: leave the money in the index fund for the near future or put the money in the index fund temporarily and begin interviewing other large cap value managers.
 - Trustees noted that in the future they would like to see the most up to date information on a manager when Mr. Bryan is recommending a change or adjustment.

- Mr. Bryant offered to include in “pre-lims” in the quarterly booklets. The trustees were not interested pre-lims but rather wanted to see all available information for fund managers.

Manager Allocation and Target Summary (page 9)

- Champlain has a number of stocks that did not perform well but Mr. Bryant recommends the Plan to stick with their stock choices
- PIMCO fixed income is not in longer duration bonds. Rather they are positioned for the FED to raise interest rates. Thus they did not have great performance this quarter.

Manager Performance (page 10 & 11)

- Mr. Bryant noted that page 10 show performance gross of fees. Page 11 is a new addition to the quarterly report and shows the performance net of fees. Mr. Bryant noted that the quarterly books now also added index summary on page 12.

Mr. Bryant noted that his staff is working on including PIMCO to risk metrics on page 14.

Active vs. Passive

- The board had a brief discussion about active versus passive.
- Mr. Bryant emphasized that he would recommend reviewing the board’s intention to continue with active management or moving to passive management next fall to coincide with an approximate 5-year market cycle for the majority of the plan’s investments.
- Mr. Bryant discussed investable indexes. He noted that the board cannot purchase the timber, real estate or private equity index.
- He noted that theory that there is not a lot of money to be made in active management. If the board decides to go passive then the focus becomes on asset allocation and alternatives.

Page 7 – Performance Summary

- This page is intended to show how the plan is doing at asset subclass level. Since one manager in most classes becomes a repeat of manager summary
- Mr. Bryant recommended collapsing the chart into asset classes – domestic equities, foreign equities, real assets, fixed income & diversified assets. Displayed an example of the recommended chart from OPEB report.
- The Board gave Mr. Bryant approval to make this change to the chart.

REAL ESTATE

Mr. Bryant presented an education on investing in real estate. He spoke from Dahab’s handout “Investing in Real Estate”.

- 3-types of real estate investments: Core, Value Add and Opportunistic
 - Board has a decision to make:
 - Could choose to go with PRISA or another firm
 - PRISA I=Core, PRISA II= Value add; PRISA III is a bit further than value added
- Why do we invest in real estate? handout – page 2
 - Introduction – offer bond-like property. Greater appreciation than bonds, offers inflation protection.
 - Bond substitute but not a perfect substitute.

- Liquidity issues. – Real estate was illiquid for 4 to 6 quarters following 2008. Fees are higher than bonds
 - Not highly correlated to stocks and bonds
 - Offer protection in rising interest rate environment
- Real Estate Variations
 - REIT – RE investment trust, traded like stock, daily liquidity. Acts like a stock
 - Import distinction is public vs private, private REIT do not move like the stock mkt and acts more bond like
 - Risk level is important – most risky real estate investments do not act like bonds
- Property types – industrial, multi-family, office and retail, hotel & self-storage
 - Things to ask about during manager presentation: what is your property, why and how do you move between them?
- Leasing periods (page 8) – think of lease similar to duration in bonds
- Risk & return – page 9 – standard deviation variability of return is a measure of risk. Should require more return for more volatility.
- Real Estate Investment Styles (page 10)
 - Core
 - Up to 25% leverage
 - 6 gateway markets
 - Leased 90% to 95%
 - Value Add
 - Up to 50% leverage
 - 80% leased
 - Goal to make improvements and to increase occupancy
 - At 90 to 95% occupancy sell to core investment
 - Opportunistic
 - 70% leverage
 - Build from bottom up
 - Higher number of risks
 - Responsible for purchasing of land, attaining permits

Core real estate may currently be overvalued. Money poured in after 2008 and cue to get in were over 2 years.

Mr. Stewart arrived at 9:53AM.

- Historical Returns (page 13)
 - Average returns have been between 5 & 10%. The past 20 years returns have been 9.06%.
- Correlations (page 14)
 - Chart shows correlation to S&P 500. Items in our portfolio that have the lowest correlation are fixed income and, timber and real estate.
- Summary – when listening to PRISA presentation listen for:
 - Differences between funds I, II & III
 - Amount of leverage
 - How funds are positioned – geographically and sector type

Staff clarified that PRISA's presentation today is to fulfil our regular manager due diligence. Additionally, the Board has approved an increased asset allocation to real estate and the Board has the option of putting this additional money into PRISA or finding another real estate manager.

Mr. Bryant was asked if there is an advantage to staying with PRISA or going with another manager. Mr. Bryant noted that PRISA has done well for the fund and that he would recommend staying with PRISA for simplicity sake. He clarified that there is not the risk of duplication (like you may have if you have multiple large cap managers).

Staff noted that the Victory Center (which the City has a monetary interest in) is an investment in PRISA II. It was recommended that we have the City Attorney's office opine on if there is any risk of conflict of interest in investing in PRISA II.

PRISA, Eric Sabol, Assistant Vice President

- Real Estate Market Overview
 - 6-property types: apartments, office, warehouse, retail, hotel & storage
 - Invest in all 6-types gives a diverse portfolio
- Goal to reduce amount of leverage/debt in portfolio
 - PRISA I – policy limit to 30%; current rate 20%
 - PRISA II – policy limit to 40%; current rate mid to upper 20%
 - Leverage allows PRISA to buy more assets, magnifies returns on the upside and downside.
 - Benchmark leverage is 20 to 25%.
- Reviewed historical returns by fund. Supplemental since inception returns at 14.31%. Noted that the plan entered after the 2008 real estate crisis.
 - PRISA I investment returns are expected to be between 7.5% and 9.5%
 - PRISA II investment returns are expected to be between 8.5% and 11%
- PRISA overview - \$20 billion fund in existence since 1970 that focuses on the 6 core real estate markets.
 - PRISA team located in four offices across the US
 - Page 18 – snapshot – discussion focused on diversification. Mr. Sabol noted that the fund has a “coastal focus” – 33% in west coast. On the coast it is harder to acquire land paired with higher job growth which makes the coast a more attractive option.
 - PRISA I is 93% core, 7% non-core. The allocation to non-core gives the fund flexibility.
- Performance (page 19)
 - PRISA returns compared to the NCREIF-OCE has outperformed in the 1, 3, & 5 year periods. Slight underperformance in the 10 year period.
- Occupancy & Income Growth – average property leased status is at 92.2%. This represents an improvement from 91.3% last year.
- Strategic Markets (page 22)
 - Major exposure on the coasts (Southern California & San Francisco) & Washington DC and New York Metro.
 - A trustee asked how a major earthquake in California would affect the fund. Mr. Sabol noted that it would affect PRISA as well as all of America. PRISA does have insurance and claims would have to be filed.
- Core Assets – Mr. Sabol discussed a handful of the funds core asset investments. (pages 23 & 24)
- Non-Core Assets – development (build on it) and repositioning (fix up existing building)

- PRISA is investment manager – not developers. If any development is done it is done by an expert in land development.
- Mr. Sabol walked the Board through a number of investments in PRISA I including 500 8th St Washington, DC, Cupertino Gateway & block 300 in Portland, OR.
- Mr. Sabol reviewed the investment strategy, outlook and objectives. He noted the focus on urban markets.
- There was a brief discussion on the LEED Certification (environmentally friendly). Anything PRISA develops will be LEED certified. Mr. Sabol noted that the LEED certification would not drive pricing as it is becoming more of an industry standard.
- PRISA is a \$2 billion cue. Existing or new clients are in the cue that is about 6 quarters. There is no obligation to drawdown the cue so PRISA will not overpay for an asset to reduce their cue. PRISA I is always open. Once you are first in line you are fully committed.
- PRISA II will open for a small period of time. Once the goal commitment is reached the fund will be closed. Then the PRISA will drawdown that commitment. PRISA II works this way because of the type of investment. Once in the all investor are drawn down on a pro-rata basis. Expect PRISA II to be opened in the near future.
- PRISA I non-binding cue. PRISA II is a contractual agreement.
- Why would PRISA sell an asset?
 - Typical holding times: PRISA I is about 10 years; PRISA II is 5 to 7 years
 - PRISA I would sell assets without a lot of upside or in case of hotel – requires a minor renovation so they ask if they want to invest the money in the renovation.
 - There is an asset manager at each investment to make a recommendation to the portfolio team about hold or sell involvement.
- PRISA investment allows the funds to take out quarterly dividends. The fund is currently reinvesting those quarterly disbursements.
- Mr. Sabol briefly covered PRISA III. Long term return target is 11.0% to 14.0%. PRISA III is a value-add fund. Functions similar to PRISA II in that it opens from time to time and then stops. 40% core 7 60% non-core with lots of development. Average holding is about 3 years. Average leverage for the portfolio is 65%.

Mr. Sabol left at 11:11 AM.

Mr. Bryant made the recommendation to have Staff work with PRISA to get into the cue for PRISA I.

Ms. Mammarella made a motion to:

Have Staff work with PRISA to get into the cue for PRISA I in the amount of the increased allocation per the new asset allocation study.

Mr. Tierney seconded the motion. The motion was unanimously approved (7 – 0).

The Board had a discussion about whether they wanted to hear from other real estate managers. The discussion focused on the cues to get into PRISA I and II and similar managers and whether the Board wanted to invest in Core or Core plus. Some trustees thought that we should stay in PRISA I because it is a more conservative investment and it is meant to be a bond substitute.

It was clarified that if the money could not be invested for the next 6 to 8 quarters it would remain in fixed income until it could be invested.

There was a discussion about leverage and how it affects the real estate investment. Mr. Bryant referred back to page 16 of Dahab's presentation which shows a grid about the impact of various interest rate environments.

The Supplemental Retirement Board made the decision to have Dahab perform a search for Core + investments. This Board decided they would stay in a core real estate investment with PRISA.

Calendar 2016

- A survey was distributed in advance of the meeting and based on the results it seems that the current meeting structure will continue to work for most members. Interim meetings will continue to be held on the 2nd Thursday and due diligence meetings will also be held on the 2nd Thursday of the month jointly with the Supplemental Retirement Board. Staff will create the updated calendar and distribute it at a future meeting.

Mr. Bryant left at 11:37 AM.

ADMINISTRATOR'S REPORTS

Regular Investment Reports

Staff recommended rebalancing the disability trust.

Mr. Tierney made a motion to:

Rebalance the fund as recommended: decrease PIMCO by \$500k and increase Glovista by \$150k and Brandes by \$350k.

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

Cash Flows Reports

Reports are included in the Board Packet. (Hamilton Lane & Molpus)

Staff called attention to the large call from Molpus which has now called 44% of the original commitment.

Other Items

Education

- AMRS-VA – Staff has included some notes from the October 2015 meeting. Attendees to the AMRS-VA conference included Mr. Capelli, Ms. Coley, Mr. Curia, Mr. Gilmore, Ms. Vagnoni and Ms. Wright.
- ICMA-RC follow-up
 - ICMA-RC provided an update to their previous presentation. Details are included in the PowerPoint presentation in the board packet.
 - Included in the presentation was a comparison on the City of Alexandria to other similar jurisdictions. It was noted that as a percentage of invested monies the City had the lowest percentage at 1.53% as compared to 2.5% to 3.1%.
 - It was suggested that Staff and ICMA-RC review the education provided to participants who are taking loans.
- Manager Staffing Updates
 - Staff provided details in the packet on the staffing transition at Hancock.

COMMITTEE REPORTS

Technical Corrections and Plan Document Review Committee

No report was given.

Vendor & Service Provider Review Committee

No report was given.

OLD BUSINESS

None.

NEW BUSINESS

None.

NEXT MEETINGS

1. Thursday – December 10th at 8:30 AM, Sister Cities 1101, Interim Meeting

ADJOURNMENT

The meeting adjourned at 11:50 AM.

HANDOUTS

Distributed to Board members in the Board Packet:

Agenda
Minutes of Prior Meeting [1(a)]
Potential 2016 Meeting Dates [4]
Monthly Investment & Rebalancing Report [5(a)(i)]
Private Equity Cash Flow Report [5(a)(iii)]
Timber Cash Flow Report [5(a)(v)]
AMRS-VA Fall 2015 Meeting Notes [5(b)(i)(1)]
457 Loan Details from ICMA-RC [5(b)(ii)(1)]
Hancock – Management Changes [5(b)(iii)(1)]
FP – Disability Certification Letter [8(a)]
FP – Investment Policy Statement [8(b)]
Asset Allocation Changes

Distributed to Board members at the meeting:

- Dahab Performance Review September 2015 (Specific to your plan)
- Dahab’s Deferred Compensation, Defined Contribution & ROTH IRA Performance Review
- Dahab’s Investing in Real Estate
- PRISA Real Estate Presentation Booklet