MINUTES OF MAY 11, 2011 RETIREMENT BOARD
CITY OF ALEXANDRIA FIREFIGHTERS AND POLICE OFFICERS PENSION PLAN
SPECIAL MANAGER SELECTION MEETING

PRESENT

Members	Others
Michael Cross, Chairman [2,4]	Jonathan Bauman, CFA American Century
Shirl Mammarella (Alternate) [2, 3]	Steven Bland, Retirement Administrator
Morgan Routt [3]	James Bland, University of Wyoming
Al Tierney [4]	Barry Bryant, Dahab Associates
Laura Triggs [2, 3]	Arthur Lynch, Retirement Specialist
	Theresa Nugent, Pension Communication Specialist
	Paul Marshall, CFA Atlanta Capital
	Ellen DiNicola, America Century
	Kathleen Ognibene
	James Skesavage Jr., Atlanta Capital
	John West, Research Affiliates

Committee Membership
[1]Buyback Committee
[2]Technical Correction Committee
[3]Training Opportunities Committee
[4]Vendor & Service Provider Committee

CALL TO ORDER

The meeting was called to order at 1:00 PM on May 11, 2011.

MINUTES

Meeting minutes will be deferred until a meeting with greater attendance.

EDUCATIONAL SESSION: RESARCH AFFILIATES

Mr. Bryant discussed the RAFI firm, its founder, and credentials.

Mr. West highlighted the materials in the package he distributed and then focused on the one main handout used in his presentation

Mr. West believes the 8.0% that many pension plans assume they will earn is not attainable. Staff asked the timeframe for the projection. Mr. West said ten to twenty years. The bulk of the presentation is to discuss the gap between the expected return assumed in actuarial valuations, annual statements, etc. and what he believes is a reasonable expectation.

Slide three demonstrates returns on ten year bonds over a ten year period is essentially the same as the initial rate of the bond. Reinvestment has little impact on total return. Current yields are historically low so future returns are expected to be modest.

Slides five and six break down historical equity returns into components and suggest future equity returns will be modest. Staff agrees with the direction of future returns but questions the magnitude. For example, over time lower growth in equities would lead to a higher return from dividend. There is a modest buffering effect in the scenario described.

Slide seven shows the price to earnings ratio for 130 years. The current ratio is above average.

The graph on slide eight shows return on the vertical and initial price to earnings ratio on the horizontal. The current market's P/E ratio suggests future returns will be modest, possibly 3% per annum.

Mr. Bryant asked the reason for the change. Mr. West said the starting point of the Ibbotson study had a dividend yield of 4 ½%. The current dividend yield is 2%. Mr. West said companies are making silly acquisitions. Staff added companies were buying shares at market tops.

Slide twelve suggests three paths to improvement: considering other asset classes, managers providing alpha (which is zero sum), and actively managing the asset mix. Mr. Bryant asked if this was Tactical Asset Allocation? Mr. West said yes.

Ms. Mammarella ask how slide thirteen was different from the asset allocation Dahab Associates had recently performed for the plan. Mr. West said his numbers were from Ibbotson. Mr. Bryant said the asset allocation used the most recent 20 years, the 70 years, and return to mean scenario.

Mr. West briefly talked about the Fundamental Indexation ideas and product and then focused on a long-short product. Slide eighteen shows returns for a major capital weighted index, and then tweaks the index composition based on a series of factors. In all cases the 1984-2010 returns are higher for the alternative weightings than for the capitalization weighted.

Mr. West said the system had been back-tested a number of years, but that it had been live for six full years. In these six years the fundamental index had beaten the capitalization weighted index.

Mr. Bryant had said the knock was this was the value effect (vs. growth), the small cap effect (versus large cap), and "contra trading."

Slide twenty one demonstrates the long short fund focuses on the differences between the capitalization weighted and fundamental weighted indices. The go long the Fundamental overweights and short the underweights. They are market neutral in dollar terms of overweights and underweights. Staff asked if the beta was zero or if there was any market exposure, small though it may be. Mr. West said there may be some beta and market exposure, yes, it would be small. In answering the question he referenced page 38.

Mr. Tierney asked about the relationship between the S&P 500 and the long/short fund. In general, the long short fund does well in a sluggish, sideways, or dowanwards market. The S&P 500 will do better in a bull market.

Staff asked if this is an absolute return fund. Mr. West said yes. Mr. Bryant said there were five types of assets: equities, fixed income, real assets, tactical asset allocation, and absolute return.

Slide twenty three showed results. Staff asked if they were net or gross. Mr. West said they were net.

RFP – MANAGER SEARCH LARGE CAP GROWTH

Mr. West left at 2:00 PM.

Mr. Bryant gave a quick summary of the RFP process, writing the RFP, posting it, allowing a sufficient time for vendors to respond, and the process of whittling down the candidates. The Board was satisfied the process is independent, objective, and meets due diligence standards.

Mr. Bryant provided an overview of the candidates. American Century has the highest portfolio turnover, the largest portfolio, the largest company, and the least Tracking error. Polen Capital is on the opposite end of the spectrum. Atlanta Capital is somewhere in between.

Mr. Bryant then referred to page 5 of his summary book and reviewed more statistical differences.

Ellen DiNicola and Jonathan Bauman of American Century introduced themselves.

They distributed a booklet *American Century Investments Large Cap Growth*. Ms. DeNicola provided background for the firm (page 3) and said there were no regulatory actions against the firm.

Page 4: the peer rankings are strong.

Page 5: the firm's view of growth is to focus on improvement of prospects, not an absolute level, but of relative improvement. They are bottom up fundamental oriented. The bulk of their success is from stock picking and not macroeconomic bets.

Page 6, there have been no changes in the investment team firm for six years.

Mr. Cross asked about the senior portfolio manager having twenty nine years of experience. Would he be around longer? This is not an ageist question, but a very relevant issue of succession, continuity, and performance attribution. Mr. Woodhams is 52 and plans on remaining at the firm for years to come. Also, all key employees have stock in the company and are incentivized for long term performance.

Page 9: In evaluating securities they monitor revisions in earnings estimates. They evaluate metrics for the company rather than per share price. They feel the market may be slow in recognizing the impact of a change. They develop an investment thesis for each company and then use it for purchase, monitoring, and selling companies.

They discussed Apple computer. Mr. Bryant asked what they liked, disliked about Apple, what could go right and what could go wrong. Mr. Bauman said the introduction of new products was the key. He provided an update on the I pad and I phone.

Page 11: They discussed risk using Exxon as an example. Risks come from specific stock selections. Risks come from sector underweights and overweights are minimized. Pages eighteen through twenty demonstrate how they address risk.

Staff believes their taking minimal risks will lead to benchmark returns with active management fees.

Mr. Tierney asked if 82% turnover means all the holdings will be gone within a year. Mr. Bauman said they sell just over a half in a year plus some of those that are kept might be reduced in weighting.

Page 14: There has been one lead manager the entire period.

Mr. Cross said the mandate would be $18 million from the Fire & Police Plan. Would that be small for them? Their minimum is ten million dollars. Their largest customer is the Lockheed Martin pension plan.

Pricing would be on combined accounts. If the Supplemental Retirement Plan and retiree medical and life insurance trust fund were also to select this company the fees would be based on the combined accounts and economies of scale shared by all.

Style drift was discussed. Mr. Bauman said the S&P 500 was dominated by a handful of large companies such as Exxon Mobil and Apple Computer. The average capitalization of their holdings was similar to that of the index.

ATLANTA CAPITAL

Mr. Skesavage introduced the team and distributed a booklet, *Atlanta Capital Investment Managers*. They reported the average plan retains a manager for six years. They average twelve years with their clients.

Mr. Marshall said they meet their objectives by having high quality, discipline (no small cap and no value stocks), and diversification (all sectors except utilities and one other). They look for consistency of earnings over long periods of time and risk adjusted returns.

Page 5: They integrate analysts into the hierarchy. They meet daily at 8:30. They profess to be nimble. The list of credentials and college degrees is impressive.

Ms. Ognebene said she did not see any women employees in the booklet.

Page 8: They believe they focus on the right questions which enables them to build scenarios for upside and downside potential.

They are conservative in that no holdings exceed five percent of the portfolio. They use the S&P 500 as their benchmark.

Page 12: They discussed Apple computer. Mr. Bryant asked what they liked, disliked about Apple, what could go right and what could go wrong. They believe earnings could grow above 20% annually. The I-phone is the key, especially internationally. They feel I-pads are commodities. International growth could move and margins can be as much as 60%. An issue is Steve Job's health.

The Focus Fund is not a sector fund, and not aggressive. Mr. Tierney asked if they ever got below twenty holdings. They had never been below 25 and sometimes as many as 29. They discussed their sell discipline.

Page 14: The upside capture is 120+% and the downside 93%.

Staff asked about barriers to entry. It is easier to see barriers to entry in old line businesses, but with rapid technological changes how do they foresee changes that might knock down barriers to entry? Someone like Apple spends huge sums on R&D.

POLEN CAPITAL

Stan Moss, CFA CPA introduced himself, Dan Davidowitz, CFA, and Polen Capital. David Polen has been running the firm for 20 plus years. They have held less than 100 equities over the last 22 years.

Mr. Tierney asked for examples of Public accounts. Quite a few were named. The average holding is in the portfolio for five years. There is a very high standard for getting into the portfolio. They seek a sustainable competitive advantage, low debt, and a high returns on equity and capital.

Staff complimented the Downside Capture Ratios listed on page 2. While the values are quite admirable the values are getting closer to 1.00. Mr. Davidowitz said this is a period of higher correlations to the entire market than normal. As correlations revert to historical levels he expects the downside capture ratio to decline.

Page 3: The 2003 – 2007 is the only five-year period of under-performance.

Page 4: They have performed well when the markets have a good decade (1990s) or bad (2000s).

Page 5 - 6: The holding period is five years on average. They constantly ask, “What will things look like in five years?” If they do not look good there is no hesitation to sell. They seek a high return on equity, earnings growth, expanding margins, low debt, and free cash flow.

Page 7: They paid for a survey (research) of Varian customers. They pay up for quality.

Ms. Ognibene asked about diversity amongst the workforce. They employ thirteen and soon that will be fifteen. They had three women but one left to raise a child.

Mr. Cross referred to page twenty of the Dahab book. It appeared the number of clients is decreasing. Mr. Davidowitz explained these were small wrap accounts and the Assets under management is increasing.

Mr. Cross said one million dollars of errors and omissions insurance was small.

They have overweighted healthcare and technology. They have no materials/commodities related equities. They are entirely bottom up.

They discussed Apple computer. Mr. Bryant asked what they liked, disliked about Apple, what could go right and what could go wrong. The I-phone is a game changer. Incremental sales are much more profitable as margins are very high. What might go wrong with Apple Computer? The Apple eco-system would have to have serious setback.

Mr. Bryant said 2003-2007 was a tough time, they did well in 2008. In 2009 he would have expected a quality growth company to do well in a rally led by low quality companies. Mr. Davidowitz agreed that part of the 2009 rally was lead by junky companies, but that some was led by top flight companies. Some of their old line companies like Coke held up well, so they were sold for some great bargains in Amazon, Visa, and Apple. Also, they invested their cash near the bottom of the market.

Ms. Triggs made a motion to go into executive session.

Mister Chairman, I move that the Fire Fighters and Police Pension Plan Board convene in closed executive session at this time, pursuant to Section 2.2-3711(A)(7) of the Code of Virginia, for the purpose of consulting with legal counsel and briefing by staff with respect to specific legal matters regarding a potential claim arising out of the administration of the pension plan.

Mr. Tierney seconded the motion.

The motion was unanimously approved (5-0).

There was a motion by Ms. Triggs:

Mister Chairman, I move that the Fire Fighters and Police Pension Board

reconvene in open session.

Mr. Tierney seconded the motion.

All members read the following language and agreed:

WHEREAS, the Alexandria City Fire Fighters and Police Pension Plan Board has this 13th day of June, 2005, recessed into closed executive session pursuant to a motion made and adopted in accordance with the Virginia Freedom of Information Act; and

WHEREAS, § 2.2-3712 of the Code of Virginia requires a certification by the Board that such closed executive session was conducted in accordance with Virginia law;

NOW, THEREFORE, BE IT RESOLVED that the Board does hereby certify that, to the best of each member's knowledge, only public business matters that were identified in the motion by which the closed executive session was convened, and that are lawfully exempted by the Freedom of Information Act from the Act's open meeting requirements, were heard, discussed or considered by the board during the closed executive session.

The motion was unanimously approved

Mr. Tierney made a motion to:

Select Polen Capital Management to manage the fund's large cap growth allocation subject to a contract review by the City Attorney and finalization of the fees by Mr. Bryant and staff.

Ms. Triggs seconded the motion. The motion was unanimously approved 5 – 0.

Ms. Mammarella made a motion to:

Adjourn

Ms. Triggs seconded the motion. The motion was unanimously approved 5 – 0.

NEXT MEETING

The next meeting is Thursday June 9, 2011. This is a special meeting for manager selection.

ADJOURNMENT

Ms. Mammarella made a motion for:

The meeting to adjourn.

Ms. Triggs seconded the motion. The motion passed (5-0). The meeting adjourned at 4:00 P.M.

HANDOUTS

Distributed in advance to Board members

1) Agenda
2) Large Cap Growth Manager Search, Dahab Associates

Distributed during the meeting:

3) *Research Affiliates Fundamental Index Capital Markets View & RAFI Global Long/Short*
4) *American Century Investments Large Cap Growth.*
5) *Atlanta Capital Investment Managers*
6) Polen Capital