DEPARTMENT OF CITY CLERK

CITY HALL

AUGUST 26, 2010

The Board of Investment Commissioners meets this day at 2:30 o'clock P.M., in The Conference Room, Third Floor, City Hall.

PRESENT: Vice-Chairman Bruce Miller, Finance Director; Stephen T. Napolitano, City Treasurer; Aaron Simon and Ted Mocarski– 4.

ABSENT: Mayor David N. Cicilline, Councilman John Igliozzi, and Myrth York – 3.

Also present are Eric Bertonazzi, Wainwright Investment Counsel LLC; Jeffrey D. Fabrizio, Wainwright Investment Counsel LLC; Kenneth Chiavarini, Assistant City Solicitor, Law Department; Michael A. Boyd, Jr., Chairman of Executive Committee, Forest Investment Management LLC; Lori L. Hagen, Second Deputy City Clerk and Kimberly DiScullio, Assistant Clerk.

(Subsequently, Ms. York joins the meeting)

I INVESTMENT PERFORMANCE ANALYSIS

1.) Recent Performance Estimate

2.) Portfolio Structure and Performance Summary: Asset Class

3.) Manager Performance: Benchmark vs. Manager Analysis

A.) US Equity Managers
B.) International Equity Manager
C.) Fixed Income Managers

II DISCUSSION RELATIVE TO THE DEXTER DONATION FUND AND OTHER TRUST ACCOUNTS INCLUDING THE CASH BALANCE OF THE FUNDS

III DISCUSSION RELATIVE TO THE MOTLEY RICE PORTFOLIO MONITORING REPORT

IV DISCUSSION AND /OR DECISION RELATIVE TO CHANGE IN ASSET ALLOCATION

V PRESENTATION BY FOREST INVESTMENTS

MR. MILLER: We're going to go out of order on the agenda so if we could defer to Forest Investments to begin their presentation.

MR. BOYD: Wonderful. Thank you very much.

MR. BERTONAZZI: In keeping with our standard practice, we have Forest here today. On your flash report you can see them down under the hedge fund column. They run a convertible arbitrage strategy for us and reporting to our standard procedure. We would like to give them about five minutes to refresh you on who they are, where they are, that type of thing, then give them around twenty minutes or so to go over their strategy and show you the numbers and the ideas they're thinking about, and what they'd like to tell you, and then save five or ten minute for questions with sort of a half an hour target. So please, Michael, go ahead.

MR. BOYD: Well, thank you. My name if Michael Boyd, my associate Tamara Rabaceroni is here with me today. We're a convertible arbitrage hedge fund located down in Old Greenwich, Connecticut. We were founded in 1992. Our strategy is that of an absolute term structured type strategy. We are at certain times in the investment cycle a bond equivalent, or at other times we are an equity equivalent depending on the pricing structure of the convertible bond market at that time. As of last month's end, we have approximately $300 million dollars under management, and of that $300 million dollars we have a total of sixty five clients and the majority of those assets are institutional type assets. I'm the chairman of the company. I've been with the company now for eighteen years. I'm the founder of the company. John McDonald, who is our chief operating officer, has been with the company for twelve years. Scott Watson, chief investment officer, has been with the company now for eleven years. Jingyan Wang, our portfolio manager and quantitative theorist, has been with us for nine, and Robert Weaver, our director of resources, has been with us now for eight. So it's a team that's been together now for along time. We're been through some tough markets as everybody knows over the most recent timeframe, and we have in total in the firm fifteen individuals of which ten to eleven are invested and involved in the actual investment process itself. An absolute return strategy is one where a reasonable degree of consistency we perform through thick and thin. For example, since the firm has been founded, actually the first year of 1993 is the first year's returns. We have produced slightly under 10% compounded rate of return on an annual basis. It hasn't come in an easy stream. Some years we've been down to a 1% rate of return and in other years we've been up to a 20% rate of return. Actually we've had two losing years, 1994 when our main fund was started, it started in September I think, that year we were down slightly, it wasn't a full year. In 2008 we were down. We were down 27.8% in this fund and the following year we were up 52%. So, between 2008 and 2009 a dollar given to us on January 1, 2008 was up about 5% approximately on those two years, each year. So it's a strategy, and just to talk about the problems that we had because for me to be an arbitrage manager and be down 28% is like the machine goes into tilt. That's really hard, I mean, how do you lose 28%. Well, we all know what kind of a year 2008 was, but what was particularly hurtful and damaging to the convertible strategies in that year was the fact that we had government intervention in our markets, which prevented us and that was in the September period. I mean, half of the stool in which we support ourselves is the short side of the market, so that really hurt us. At the same time that was happening, you can make all the assumptions you want about risk assessments or not, but you got to make some assumptions based on the sun coming up tomorrow and one of the assumptions contributing to the sun coming up tomorrow is that the banking system is going to be there for you to supply credit with somewhat of a leverage strategy and to supply the credit for that leverage. Well, all that credit was pulled from us. So, shorts were prevented, credit was withdrawn from those and then banks were just closing all of their prime brokerage operations and so thank God we were smart enough to have a number of plan brokers, thank God we had a number of alternative financing sources, which we're able to call up on during that period of time. So, yes, we were down 28% in 2008, but in 2009 we bought back when the market stabilized. Today, when we do a stress test of our portfolios we look back and say okay, fine, how do we get funding, if funding is pulled and is that such a weird question to think about today and the answer is, I don't think so. So, we have extended our funding to foreign banks as well as domestic banks. So, we are funding through J.P. Morgan and Citibank. We're funding through the Royal Bank of Canada and we're funding now through UBS in Boston. So, some of the funding sources are different like the Royal Bank of Canada. It's a different, it's a European style funding methodology and that is based on the treasury market and that should be very stable for us. So, as an absolute return strategy I inserted that deviation from my presentation to show you that yes, we went into a big loss and it was through very specific factors that happened. We do global convertible arbitrage. We're not just convertible arbitrage in a domestic market. We are also in Europe and in fact currently now the portfolio is structured about 95% domestic U.S. and about 5% foreign, 4% of that is Western Europe and the other 1% is in the Asia Pacific. The Asia Pacific region is becoming a bigger market and as that market grows and matures, I think it will overtake the U.S. market. At one point in time Japan was a dominant world player in the market, back in the early 90s. The U.S. convertible market, well I should say the global convertible market is about four hundred billion right now. In the early 90s, Japan was over half a trillion just itself besides Europe and the United States. I think I can see China, Singapore, Hong Kong becoming major growers. Australia is becoming a bigger issue with convertibles. So, I think the global convertible market is a growing market particularly as the world becomes much more globalized. We pursue our strategy through three legs. We research, we model and we trade. We have our own proprietary research models, our research methodologies, we develop our own proprietary trading models with all the assumptions that run mainly based on creating the wrong models and then we trade based on that. It's a repeatable process as you can see. The returns are year in and year out. Eighteen years in business and basically one real losing year on a twelve month basis. Our process is definitely a disciplined one, and as I said, is repeatable. We're a bottom up research person and our strength is in really analyzing the balance sheets of the investments we make. This is a credit strategy. Years ago if anybody had asked me do you trust Standard and Poor's the answer is no. Standard and Poor's and Moody's and Fitch to us were always a problem and the reasoning why is because our research is always much more timely. It showed the problems in the company prior to it ever happening and when you think about some of the bankruptcies that occurred during 2008 and to have the agencies come out and downgrade them after they're bankrupt is such a joke, but because the way Wall Street is structured you have to say that you use the investment grading's of Moody's or Standard and Poor's, but we really rate the companies ourselves and often times what Standard and Poor's would say is an investment grade company we disclude and that's part of the edge. I mean the idea is to be evident. The bond market is a smarter player then the equity market is, because the guys in the bond market do their research on the financial fundamentals, they read the footnotes. The equity stories are great and we do that. We do our own equity analysis, but the strength of the firm is primarily on the credit side of the firm. Modeling is proprietary and I can go into it. It's very quantitative and oriented and it works, it works for us. Risk control is the key. As I started to talk about, earlier in 2008, you can do risk control all you want. I mean we have investment managers that come in and require us to supply them a stress test. What happens if interest rates go up this amount, what happens if stocks go down to that amount, and you do that, you do that in various combinations, stocks are going up, interest rates are going up and vice versa and you come up with an average outcome of potential scenarios. It's what we call scenario analysis. We do that on a daily basis and what we've done and even prior to starting the firm in 1982, I've been managing this kind of a strategy since the late 60s. I was doing it before it became even hedge funds. I was doing it for Goldman Sachs and I was doing it for Dean Witter. So, I have analysis going back in various stressors like the '73-'74 bare market and the '87 bear market. The '87 bear market was one of our most profitable years. It's not in our tract record because I wasn't at this firm at that point in time, but the point is you can do stressors all you want. How does anybody ever stress out like what happened in 2008 and so when we go through our portfolio we ask ourselves, okay, guys like I talked about the various kinds of funding's. We make sure we have the funding, so I think if 2008 occurred again there are various things that we can do. If they prevented shorts we could operate it and if they withdrew funding like they did in 2008, the major banks, we would still be able to operate and once again decision making in situations like 2008 it's only experience. It's gray hairs on the desk of guys who have been doing, oh girls and guys doing this kind of a strategy in various periods and that kind of intelligence and to experience is what hopefully helps you come out of the problem. Our investment process, it starts with computer screens showing some kind of potential possibility in the name. We then do the credit analysis in that name, we incorporate that trade into a certain kind of structured trade and we determine whether or not it fits into our current portfolio at the time. You don't want to get too weighted like the portfolio currently is disrupted by. We're in technology, we're in industrials, we're in healthcare and we're in energy and that's the main construction of the portfolio right now, high twenties to mid teens for all of that. The top ten positions in the portfolio equal about 56% of the portfolio. When you give money to a manager you really don't know if they're as good as they say they are. What helps show that you are as good as you hold yourself out to be is the track record and part of gaining the tract record through particularly a very trying period of time like the last ten years is to really be doing the work, to know the problems are going to pop up. Often times, you think you're in clear waters, sailing is nice and then all of a sudden this score comes up and the ships un-riding. And 2005 was the perfect example of that for our market, the convertible market. We thought we were okay, but it wasn't okay, things happened and the convertible market that year structural problems and we came out of it very, very nicely and a lot of that has to do with knowing your companies. The credit analysis and knowing the kind of a trade that you have will stand up under real stress. In 2008, when all of this was happening, we looked in our portfolio and we had investment grade double A pieces of paper in a portfolio, two year paper never yielding 10%. We said that the worst that happens is if we had to is we would cover all of our shorts and the average yield of the portfolio at that point in time is something like about fourteen or fifteen percent and you'd be standing there with a portfolio yielding that kind percentage, and what you hope for is than what's the duration of the portfolio. Well, let's say it was an average of four years. If it was an average four year portfolio, you're unwind portfolio within four years and that was not a very difficult decision if we had to make it. We didn't have to make it, thank God, because the government finally came back and said, you could short and then the banks came back and they provided financing, but if the worst actually did happen we would have been okay. All the money would be return to all of our clients. It was very interesting during that screaming nutty period of time, people put gates in hedge funds. One of the things people concerned themselves about was, I can't get at my money, we never put a gate on it. If a person put in a redemption, and believe me they did, we gave them the money and we went back and said, listen, the worst that happens is they close the markers and it looked like there might have been a market holiday during that period of time. We would be sitting there and collecting a nice income and that's where you want to be. I mean, we have a number of retired people and this is a retirement plan you're talking about. It's not a bad position to be in if you're at that point in time. So, unlike stocks, I mean, yields and stocks if you're in good stocks that pay dividends that might have yielded like 2% or 3%, but you were in bonds that were at a very short time to pay off. Like the Yantin bonds that we had and the Jensine bonds they were one and a half and two year paper, but we're gong to be paying off and those are some of our big positions.

MR. BERTONAZZI: Can I interrupt and ask to make sure that we have enough time, on page ten we have your track record, which you've been sort of referencing but the folks can see it and they also know or they'll know in a moment we called up and we have through the 24th of this month you made another 1%, so you're sort of up seventy basis points or something year-to-date, but if they look on page ten they will see what you've been referencing about how bad it was in 2008, what the returns were, how big the rebound was in 2009 and we're now positive and we've made back all of those losses, plus you're now through July and into August we're basically flat, we're up a little and they see that and they also see you know lately credit spreads and credit has actually been performing but stocks have been getting clobbered and treasury rates are plunging and the double dip is on the minds of everybody again because if you jump and fast forward to where we are now and give your firm's ideas as to what's happening now, what you're seeing in the near future, how your positioned, how much risk you're taking and that that type of thing, so to ensure the board has enough time to hear your current thoughts as well.

MR. BOYD: As we left the office this morning the account is up a little over 1% of the month, we're still not positive on the year. The Standard and Poor's is down about six, the Dow is down about five and the NASDAQ is down about seven. Treasury bonds is sort of what's happened in the last few days with the ten year, the ten year got down as low as 240 and 242 yesterday. You can read a lot of things about the deflation and the environment. I'll give you two scenarios.

Scenario one, deflationary environment stocks get blocked. All right. Where do we stand? Credit analysis, the names that we're in, the long market value versus the short market value we do well, in that environment we do really well. In fact, we do really well. Your rates of return are going to go into double digits in that environment okay. The other environment, if you stretch yourself out they say, okay, possible double dip. Deflationary looked at things, than money comes. You can pump money as much as you want, you got to get people to use it. The velocity of money has to start increasing before you get inflation. If you happen to get people to use the money and we do come into an inflation, it's a questions of what part of the market and stocks you're in. Bonds we know get clobbered. It's a question of how you deal with your bonds. So, we have a bond portion and we have an equity portion. You have to structure your portfolio and stocks in a certain way. You have to be in the energy sector and you have to be in heavy industrial, you have to be in hard asset kind of companies. So, we would swing our portfolio into hard asset kind of companies, not that you're not there already, but you wouldn't have this big position intact. If you have a big position in tact you wouldn't have such a big position in healthcare. You'd have it mostly in minerals and energies and hard asset industrials. Then on your bond side, you would hedge out your bond risk and that's what we would do anyway. Right now we're running lighter hedges. In an environment like that you'd run heavy hedges, so how should we do in a highly inflationary environment, we should be able to keep up and beat the rate of inflation. My last inflationary period that I can really experiment and give you the rates of return on, they're not in this, but in the 70s the strategy did very well. I was doing it for Peabody and Golden Sachs in the 70s and we have nice rates of return, its proprietary capital but we had nice rates of return in this strategy during the 70s. In 1981 when the overnight rate went to 15% and the ten year was trading at about, it came out at about 14%, oh I don't have a rate of return here for anyone, we made money in 1981. We made money in 1982 and we really started to make nice money is ’82, ’83, ‘84 and ’85, and the reason I say that is because the convertible bond market during the rate of inflation what happens is that the bonds that they issued, the coupons get higher and higher and higher. You started to see that over the last couple of years. You’re getting two and three and four percent coupons now and that’s the reason why this is really called a convertible interest arbitrage strategy, because we can arbitrage the interest rates, so they’re equivalent at that point in time. Because we’re in such a low interest rate environment right now, the standstill carry on the portfolio is lower, but in the 70s my standstill carry on the portfolio is in the teens. Standstill, overnight rate of return everyday being clocked out was in the 10% to 12% range. So, in an inflationary environment this is a great strategy if done right. It has to be done right and in a deflationary strategy and that’s how we’re structured right now we will really do well. We’ll do very well.

MR. BERTONAZZI: So, if we have a doubled edge will we get into some type of liquidity trap or we get into some sort of real deflationary environment and predict higher returns.

MR. BOYD: Yes.

MR. BERTONAZZI: What about if we’re somewhere in between, given the way the portfolio is structured now, what sort of returns profile would you predict?

MR. BOYD: Six to eight percent in that range.

MR. BERTONAZZI: Then your prediction is to fall further to get the structure for more the risk of deflation and a real slowdown in the economy.

MR. BOYD: Right now we use a lot of research. One of the research services we use is Ned Davis Research, they’re very, very good for some of their economic statistical analysis and what we’re showing is that we’re not necessarily going into a double dip, but the risk is increasing on a month-to-month basis and so we’re structured for that. In fact, there’s way to construct a portfolio of convertibles. You can barbell it or you can weight it on one side. We are very heavily hedged on deep in the money convertibles so that if the stock market really gets hit, what will happen is the stocks will come down and convertibles will come into where they're bonds and that's where the rates of returns are going to come from. So, we're more heavily right now than where we would be if we thought that the market was gong to have a nice round up. If we felt that we were looking at clear sailing in the stock market we wouldn't be as heavily hedged as we are right now and because of the way we're structured we're not gong to get hurt. We will participate.

MR. BERTONAZZI: I have another question. Jumping around a little bit, but I'm sorry. Assets have come back lately of course with a very strong performance, but still on the lower end of recent history, can you tell the board how the firm is right now even a level of assets, vis-á-vis the number of professionals, your team is stable, you predict it to be stable that type of thing.

MR. BOYD: We had been up to about a billion or so coming into 2008. We had a multi-strategy approach, and in 2008 we shut a lot of that down before the real problems started. We sent two hundred and some odd million back to clients, $235 million was back to clients because we stopped the strategies that money was associated to and we concentrated on convertibles. So, the convertible market decreased in size, money was pulled out of it by institutional investors. Why? I don't know why, but they did. So, we decreased the size of the firm, we were at forty some odd people, now we are down to fourteen and change looking to hire another person. We're well capitalized. The partners have their personal capital in the firm. So, we could go on for years, our breakeven level on operating the firm, paying everybody is about asset level right now. So, we're not touching our own capital. What we're trying to do now is structure the firm in a marketing effort to go out and raise institutional capital primarily in the long term investors, folks like yourself who have long term viewpoints. Some institutional investors want to get rates of return that are just not achievable and you come into them with rates of return that are bond like. I mean here we are, we're 10% rate-of-return for eighteen years and people should be happy with that, but they're not. Don't ask me why, they're not. I mean you have a hard time selling people on convertible arbitrage and it's the granddaddy hedging strategy and I don't understand why people don't put money into it. I've been doing this for a lot of years and I still don't understand it. Everybody should have money in the strategy and it proves itself year in and year out, but we should be able to raise money and we hope to.

MR. BERTONAZZI: Any other questions? Thanks a lot guys, we appreciate it, it was very helpful.

VICE-CHAIRMAN MILLER: All right, why don't you get into Investment Performance Analysis.

MR. BERTONAZZI: Sure. Thanks everyone. If you look at your flash I will give you a quick update. If you've been watching the TV in recent weeks the markets have been down pretty substantially. You can see that the S&P was down 4½% almost month-to-date and this is through the 24th. We've actually probably made some money in the last couple of days. We're down 3% month-to-date putting us down 1% year-to-date through August 24th compared to the market for some comparisons. Like I say, given what happen yesterday I would said we're close to flat year-to-date right now and the market is down 4% coming into today. With that said, markets have been in sell off mode in recent weeks. As I asked Michael to discuss that's why I know you're probably looking at it wondering about it, I wanted you to hear his views. What's been happening? Unemployment has remained stubbornly high, unemployment claims have been coming in until this morning a little bit worse than expected. So, we're seeking signs of weakness, the rebound, the rate in which the economy was rebounding as slow as the market. So it slowed enough to get folks to wonder, jeez, is it going to slow all the way back into another recession. I don't think that's going to happen. I think the odds don't favor that. It could happen, but I don't think the odds favor it. I think the most likely outcome is sluggish growth. Slow growth and as a matter of fact slow enough to not feel very good. Slow enough to keep the unemployment rate high, to keep states and localities budgets tough, to keep the unemployment rate up around where it is right now maybe go up a little bit before it goes back down and that type of thing. So, we're in sort of this very sluggish period. The Federal Reserve you may have seen there was some news the other day, it has decided to take a middle ground between tightening, which is where they were leaning towards. They had stopped the emergency programs, they had stopped pumping money into the system and they actually in recent months have begun thinking about undoing what they had done. Very recently in response to this weakness they kind of did a middle ground and said well, we're not going to expand our balance sheet and buy more mortgage back securities and things like that, but we will keep it from shrinking on its own. So, instead of letting it shrink, which is a form of tightening, we're going to keep it where it was. There is a big meeting out in Jacksonville, Wyoming right now where all of the talking heads and professionals are trying to figure out what to do next right now. There might be some more actions taken at the federal level in terms of additional stimulus or something like that or tax breaks whose knows. There are all kinds of things on the table right now. The thing to take away is there is a lot of uncertainty right now and you're seeing it in the markets and you're seeing in in your portfolio. What I will tell you is, is our bonds are doing very well. As you can see Loomis is up 8% year-to-date. That's a very strong year for fixed income especially that we're only in August right now. So, at that rate we would be looking at something like 12% or 13% for the year, which would be very strong. So, that's something I wanted to point out. You can see our equity mangers are all now down somewhere between 3% to 4% year-to-date. Although it's a little better now they probably made a percent yesterday or something like that. Our international bond manager is up 4%. Our hedge funds are helping us this year. You can see they're all up somewhere between 1% and 5% year-to-date and that's helping us. So, bonds and hedge funds helping us, equity is hurting us beating the markets very nicely, a lot of uncertainty and perhaps more actions on the monetary side from the Federal Reserve and on the fiscal side who knows. The elections are coming up, God knows what that means, what's going to happen or now happen, a lot of uncertainly right now and we're seeing it in the portfolio. Any questions about individual managers, strategies or that type of thing.

MR. MOCARSKI: I'm just curious, the names you have on this sheet right here and all the other managers you're managing for other clients too. Any names that just stand out as great performers on this sheet?

MR. BERTONAZZI: Year-to-date or over the longer term.

MR. MOCARSKI: Either.

MR. BERTONAZZI: Over the longer term Brandes has been unbelievable in this plan just destroying the benchmark really adding a lot of value even though they're down 7% year-to-date, a lot of European exposure, a lot of Asian exposure. Of course, that's what we hired them to do. The European exposure is one of the reasons they're down more than others. They are unhedged. Their currency is not hedged so when the dollar strengthens that's bad for us and when it weakens that's good for us and you know the dollar has been going up and down. It's been strengthening lately that's another reason why we're down. Very strong over the long run, Boston Partners small cap value has been very strong over the long run. Loomis has been solid over the long run, I wouldn't say great, but doing fine beating the benchmark adding value. Renaissance was a weaker performer in the last couple of years that's been outperforming lately. So, weakened over the intermediate past, strong in the very recent period and I'm happy to see that. Quellos our strategic fund to funds is adding value up 3% year-to-date. They have been doing very well lately. I would say that Mellon and Columbia have been about average lately, not great, but now bad, nothing to get excited about either way.

MR. MOCARSKI: In last month's presentation their strategy, their approach it just kind of left me scratching my head.

MR. BERTONAZZI: They're beating the benchmark in the long run. They've beat the benchmark, but recently they've been quite choppy up and down. So, that's why we had them come in. We have had them on the watch list in previous times and they may be back on it again, but nonetheless they have added value over the long run. So, the portfolio is doing okay relatively speaking. I promise you, you will be doing very well relative to your peers again, but honestly my guess is if we took a snapshot right now we're probably down thirty basis points year-to-date. So, here we are in August and essentially nothing has happened this year. Could that turn around and be up 5% or 10% year-to-date by the end of the year, it could. Could it be down 5% or 10% by the end of the year, it could. My own guess is that I am very optimistic, but I will tell you anything can happen in the next several months. The portfolio is structured currently to protect you in that case and that's where our recent discussions have been. Asset allocation, which you have some in front of you, although last time we didn't have a quorum, should I move into that Bruce?

VICE-CHAIRMAN MILLER: Sure, go ahead.

MR. BERTONAZZI: If you look at the handouts that I've given you, we've given you a bunch and I apologize, but there was really no way else I can answer all of our tasks before you.

MR. MOCARSKI: The question I have is when you say current 3% to 4% bonds that's the current plan, that's not our actual today?

MR. BERTONAZZI: Yes. That was our current target and we are never there except for maybe right when the city makes their contribution once a year and then we immediately month after month after month burn it down to pay the benefits. Lately, it has been running at $6 million dollars a month. So, every month just about there is a little bit, but every month on average lately you can see it in your cash flows. You see this handout here, I can jump to that and answer that question. This shows you the withdrawals from the portfolio on a monthly basis, we went back to 2005 to give you an idea of how it looks and then you can compare it to the contributions that get the portfolio. Now, the city contributes more than is on the page. Some of the money the city gives goes directly to the beneficiaries and never gets in the portfolio. So they're given more than is on this page. However, you can see what comes in versus what goes out and if you turn to the second page you can see that we're bouncing around five million to six million. If you look back in 2009, every month we took out six million and the city made a contribution of 33½ and ten million and a larger contribution the year before. So far it's given seven million, and it will be I'm sure preparing to get another contribution in the not too distant future within the next couple of months. The reason why we're not at the 34% or whatever the target is, is because of that page and what you see. So, we reallocate once a year to bring us back up and if let's say in a February, March or April time period, which would be six months since the previous contribution and yet maybe six months before the next contribution, if the portfolio gets out of line in the past we have taken money from equity and put it to the bond manger to get our target back in a force of range. You can see right now we are quite low. Our fixed income is a low of about 22% of the portfolio. Within a matter of weeks, four weeks, six weeks, eight weeks, if history is any guide we will have a very large contribution from the city and we will be able to replenish our bond manger up to the target again. That is assuming we keep that target, which is sort of the next portion of the discussion and that was this board asked us to do some work and consider asset allocation that is you may recall. We used to have a 25% target on the portfolio for fixed income and as a function of 2008 and the increased volatility we reran our asset allocation and this board decided to take that target the fixed income allocation up to 34% and lower risk. Now, we have some lower risk stuff over in hedge funds and things like that. With that said, we decided to take the fixed income target out of the 34% and reduce risk, which we did. I also said at two or three previous meetings ago, jeez, is that the best allocation for the long run. Should we leave it there, should be reduce it, should we go back to where we were, should we increase our risk because one of the things I had said was is that in times of stress this higher fixed income allocation will help us. In longer periods assuming we have some average times in the future within the next fifteen to twenty years, over the longer periods of time the lower risk portfolio is going to generate a longer return. Therefore, those very strong rankings, which you have in front of you, I brought them for you per a request. If you see this page we have your rankings in the State Street Universe, which I will go over with you again very quickly because it's pertinent to this discussion. These are the rankings that State Street puts together. Now, you will see in the footnotes and in the data there are 131 public plans in this universe, in which you are one and we are comparing you to. If you add up all the assets and all of the 131 plans in this universe as of March 31st you have over $1 trillion dollars in the universe, it's a big universe. It's very large. It's a lot of big plans. You're actually one of the smaller plans in this universe and if you look at you returns on your rankings over these times periods, five, seven and ten years, you will see how you rank compared to them. Now, the seven year number is the one that I've been asked to focus on in recent times because that happens to coincide to the Mayor's term. So, since he's been the chairman of your board what have the numbers been? You can see your rankings have put you in the top 3% over that seven year timeframe. From March 31, 2003 to March 31, 2010, a time period which encompasses the greatest financial crisis in our history, you see that we're in the top 3% with a gross return of 9.9% per year over that time period. So, that timeframe you have beaten your 8.5% actuarial return. One of the reasons was the posture of the portfolio, the 25% target. Now, we've lowered that risk profile and we've increased our fixed income. So, one of the thing I was saying is that if we have average times over the next seven or ten years you're not going to be in the top three and top 7% I predict. I predict you will be lower and that's because we have a lower risk portfolio, which will in average times generate a lower risk and a lower return. If we have bad times you will do better because the rankings will be higher. If we have average times, I think you will be a little lower, if we have very good times I think you will be a good bit lower in your rankings. So, the work we've put together for you today in the context where our portfolio is now, where you rankings have been. On the other page it shows you how well you've done against the state. That is another task that was given and I was pleased to tell how well we have done, and Mayor Cicilline requested this versus the State of Rhode Island. If you look at that, what we've done is we went back ten years and we showed you what your return has been per year versus what the State of Rhode Island's return has been per year. We give you the debits and the compound rates of return. This we brought for a meeting a two ago. So, year-to-date you can see seven years annualized through April 30th, the return has been 160 basis points greater per year then the State of Rhode Island and over ten years it's been fifty basis points greater per year then the state. Those are net returns reported and those numbers are reported by the state to us. So, you see your rankings, you see how you've done against the state, you see the structure of you portfolio now and what might happen in average times, bad times or good times. Therefore, we put this work in front of you today and that is some asset allocation thinking and if you look at that page you will see the middle column is the current structure with our 34% target for fixed income. We entitled it that to remind you that's where we are currently and what our data show our assumptions about the very long future ten years, twenty and thirty years not this year or next year. They're very long time periods. We think if you all have that type of portfolio 8.75% is a reasonable return to expect over that very long timeframe with a standard deviation. The S&P would do around 9% or so with a much higher standard deviation and much higher risk. That's what the very long term numbers show. If we were to reduce the bond portfolio from thirty four down to twenty nine, we're showing a 9% return with a slightly higher standard deviation. You might say, jeez, Eric 25 basis points, it doesn't sound like a lot, but we've provided you some numbers with the other handouts to look at, which shows that if you made a quarter of a point or half a point difference in a portfolio as large as this over the years that's many million dollars going forward. That can be tens of millions of dollars over the longer timeframe. Another way to look at it more importantly when you get the human nature of just the way people reasonably act. We generated another thing to think about to help you understand that difference in what changing these portfolios might make in any one period instead of over the very long term and that's what this page is. It's titled City of Providence ERS 2008 Calendar Year Return Back Test at the Manger Level. So, what we showed you here was had we held the 29% allocation to bonds instead of the 25% allocation to bonds we had as a target in 2008. Instead of losing 25.3% like we did in 2008, we would have lost 22%. We would have lost 3.3% less. It still wouldn't have felt good, but that's another $10 million dollars that we would have had that we didn't have at that time. So, what we're trying to show you here is, is that these changes thought they might look small for the long term number, when times get crazy and scary your portfolio will behave noticeably different with these 4% to 5% moves in fixed income to equity reduction of risk and that type of thing. So, we could structure a portfolio if we want to or instead of losing what the S&P lost in 2008, which was 38%. Instead of losing 25%, we could structure one that would lose 10%, 12% or 15%, which would still feel quite a lot, but they are far less than the equity markets and even far less than we actually experience. The flip side of that is of course when the rebound comes like in 2009 we make a whole lot less and over the long run assuming the world doesn't blow up or a mediator strikes or something like that when these numbers average out and they will, it might take a long time for that to happen. It might be five years, it might be ten years or it might be twenty years, but when that happens we will make less. So, it's really a risk management decision, a comfort level that this board has to think about. I mean these numbers can show you the implications of your choices and we're trying to give them several ways to think about it. Average returns, standard deviations, risks, actual back tests and back times and that type of thing. You know our draw downs, you know our liquidity needs, you know the funding status of the plan and the city's state of finances and that type of thing. All that feeds into your decision as to the profile we want to have, the risk you want to take and then we can discuss and tell you what we think the implications of your choices are, but I would stress its choice and I don't know if anyone is better than the other, it's just your choice. The risk profile you want to have and how you deal with your constituencies and explain these things. Luckily in the last seven to ten years you can explain very good things to them about your relative performance and how much you beat the market by and how you have done versus your peers. I don't know that may be total comfort in 2008 that we experience. So, what Jeff and I are trying to do is giving you this view point and having you gain an understanding of your choice set. See the data, see the burn rate on the portfolio and see what the implications are and to help you make your choice.

MR. SIMON: What are we supposed to be doing as a committee, because there's a funding deficit? We can't fix it alone here. Obviously, it has to be an investment strategy. You know we're going to 29%, 25% to 20% that's not going to fix the problem. So, is our goal to not be part of fixing the problem, whatsoever, because in that case you err towards being more conservative. Or, if we're supposed to at least try to contribute towards fixing the problem albeit in a small amount then maybe that pushes us towards 29% proposal, because we're taking a little more risk to get more income.

MR. MILLER: In my opinion, it's possible, but I think it's becoming incumbent upon this committee to put the fund in more – position to than it's – you know, with the risks and all that being part of it. We would, I think, I don't think we want to be overly aggressive and so we're not going to fix the problem, but I think anything that we can do to contribute to the improved performance will go a long way.

MR. MOCARSKI: I mean that's what I was thinking that, you know, as part of the goal.

MR. MILLER: Yeah, we're not here to sit on our hands, but we're not here to lose all the money either.

MR. MOCARSKI: Because, looking at the data you put together it really doesn't seem like we're picking up a ton of incremental data or risk by making that adjustment.

MR. BERTONAZZI: It's not, but it would be for example in 2008 maybe three or four hundred basis points better or less losses, let me put it that way or more losses, so if you make a move like that, this is, there's some harm in this, but I will tell you the move I'm – the move from thirty four to twenty nine in a really bad year, if we increased our risk making that move from thirty four to twenty nine, I would project that it would be three to five hundred basis points worse in the bad year. So instead of losing twenty, we lose twenty three or twenty five in that really awful year. Instead of losing five or six in a merely a bad year, we lose seven or eight. That type of thing. In a good year, in an average year instead of making eight or nine, we make ten or eleven. In a really good year, if we make the – make the decision to get a little more risk or making twenty – we make twenty three or twenty four, or twenty five. That's the type of thing that I'm talking about. In the extreme years, very good or very bad, this type of a change would be something like three to five hundred basis points is my guess. Now, in calm times. which are kind of like right now, not – not – when we're all thinking long term and dispassionately, we might say that's okay, that's interesting and thanks a lot, but in 2008 when reasonable folks were really worried about what was going to happen, how bad things could have been, what I have observed in my career is that folks tend to act out of fear naturally and when times are really scary and it's hard for them to think dispassionately and long term. And there are some of your competitors, some of your peers, who are in that peer group that made some changes in 2008 that they're regretting right now, because they have not participated in the rebound. And vice versa, there were some peers that you would know that made some changes in the late '90s that they are regretting, and they got more aggressive then perhaps was warranted that they are regretting the year 2001 and two. So folks can react in a self defeating way, reacting to the recent very good times and then recent very bad times. This board has been very disciplined, and I'm very happy to say that and that's one of the reasons you're doing so well compared to your peers, but you know, I don't have the constituency that you do. I don't have to answer to these folks.

MR. NAPOLITANO: I have unless there's a compelling reason to change, I don't think I get that from, you know, but based upon what the gentlemen just told us in terms of the market and who's doing what and where everybody is paranoid every morning. It's going to go up, it's going to go down. That said, the time you chose is not good. The other factor I think we have to consider here is that in terms of funding by which has been good for at least – we're not sure, and also the benefits here – regardless of the fact, I mean, it's just outrageous, but we've got to live with them, we cant change, like you said, there's nothing you can do. So my statement right now, unless there's a compelling reason I think any move that we do, and particularly in the portfolio unless we have a situation where one of the managers are totally our whack, I would sit tight and revisit this issue the first of the year. That's my option at this point and time. Not that we don't want to – but it's my theory, I just wanted to say that. Not that we don't want to – but I'm saying with the swings, they are small, it is a lot of money, but we're really cognitive of the fact of what we actually push out and what the city is able to contribute money into meeting the demands so we can meet our 8.5%. Right now we're doing that and I'm not saying we shouldn't, but for right now I don't think – I just get that feeling. There's an uncertainty of the market that it would weather the storm without portfolios being set up, but right now, I don't feel as though we should do anything until the first of the year. We'll have the elections out of the way, people will have cooler heads, it's cooler, the summer is not hot, people are not crazy and you know it's the first of the year and maybe you can, you know, it's the first of the year and maybe you know – but I think in this point of time I would be very reluctant to change anything right now.

MR. SIMON: When you set this up it looks like you put about – taking 5% out of fixed income and you put about 3% more on the equity side, and then like 2% more towards the hedge fund and private equity side.

MR. BERTONAZZI: Yes.

MR. SIMON: Have you – I like the idea of decreasing fixed income right now because I actually think it's fixing the market, historically very over valued. I see that planning itself out over the next ten years, but I don't like the thought because of what –what's that – I don't like the though of adding more to equities, because of the uncertainty that's out there, because of what we just talked about. Is there – have you done – have you taken a look at what, you know, what our – what types of returns, what the standard deviation would look like, if we said – if we started taking that 5% out of fixed income, but concentrated it more towards, you know, Forest and Renaissance, and the total return strategy that is not as market depending as equity. I mean, equities are 100% market value, yes, but taking that 5%, you know, I don't know what that, what you –

MR. BERTONAZZI: We could do absolutely, done it millions of times. I didn't do it in this particular one, but the answer is yes, we can do that. You would have more market neutral type of exposure, managers who might be able to make money in bad times, and still over the long run get returns better than bonds and maybe equity life. So, the answer is yes you can go in that direction if you did that, too, go over the numbers and show it, but that would be, this was just a first run in saying, here's what we might do. We would have had to –

MR. MOCARSKI: Can we do something like that at the next meeting? Because this is allocated on a prorated basis across all the classes that we're in. That's what you get for a proxy right now, when you put this sheet together. You did it overweight more into the incremental five you're taking up overweighting in the hedge or ending –

MR. BERTONAZZI: Right, no, I just – no, we just put about three into alternative and two into equities, but could we put all five in alternative and none in equity.

MR. SIMON: You mean three equity and two alternatives.

MR. BERTONAZZI: We had – we had on, one, two – I guess that's what we had was – it's two and three. I'm sorry, I misspoke. So could we go all five, sure or none to that, absolutely and I can certainly go over with you those changes in those deltas – are they liquidity when you go that way or less liquid, but maybe you don't care and that's fine, we can talk about it. There's a lot of things to talk about absolutely that would be one very reasonable way to go.

MR. MILLER: Maybe we were taking about – I would I still would like to see some type of emerging markets, merging managers still on the table. And I don't know what everybody else is thinking but real estate, something in the long term.

MR. BERTONAZZI: I have no problem with the real estate exposure. Most, if not all of them are other portfolios have real estate exposure. This board has made a couple of decisions some years ago to avoid real estate. I had made a recommendation a couple of times that – I've been in this for about sixteen years now. So, back in the mid 90s and the late 90s, and even around 2000 or so, I made that recommendation and the city had a bad experience with some local real estate players and they just did not want it. They made that clear to me, quite clear. So, yes, that could be something else we could think about. We could do public, we could do – we wouldn't have to do local real estate, so yes, would that be a thing to consider, sure.

MR. MOCARSKI: Is there a decent real estate exposure on the private equity managers that we have.

MR. BERTONAZZI: There is a little bit in there, yes, and there would always be. We could use more of it by direct exposure in one form or another.

MR. MOCARSKI: Just the way this worked over here, because I understand, you know, the 34% is the target, and you explained about how the money comes out, although when you look at private equity it's not as fluid or as liquid as a market, as some of the other markets. And we're sitting at 1.8% today. So, when I look at your fund of funds and private equity allocation, and we you aggregate those you're going to 7.25%. You're actually taking everything and putting into private equity by this change.

MR. BERTONAZZI: By the target change.

MR. MOCARSKI: By the target change because we're not at the 6% target right now, we're only at 2%.

MR. BERTONAZZI: That's correct, so our portfolio is not at the target right now. And it's that reason for many, mostly because of the burn down on fixed income. That changes your ways.

MR. MOCARSKI: And I also wanted to point that out, too, because I do hear your point. You know, what is the present need to do this today given the uncertainty. I think the net are making these changes, if we can't do it over night because you can’t just snap your finger and increase your exposure to private equity on the manager and so forth. It’s not like giving more money to Renaissance where you just stroke another $2 million dollar check –

MR. BERTONAZZI: That’s correct.

MR. MOCARSKI: -- and you’re at Renaissance, so this won’t happen over night making the changes.

MR. BERTONAZZI: Well, what would happen is if we did – so, that’s absolutely true – but what would happen is if we wouldn’t replenish Loomis Sales up to 34% in September or October. We would replenish it up to twenty nine, so that money would at least not go – all of it would not go to Loomis, it’d go it something in the meantime.

MR. MOCARSKI: It’s going to be a short term instrument.

MR. BERTONAZZI: Well it could be, we could put it in cash away, or we could put it temporary in Loomis, or we can put it in fixed income, or other parts of the portfolio, but you are correct. It will take a while to build up private equity exposure without them.

MS. YORK: -- we were in 25% and then when do you change to 34%.

MR. BERTONAZZI: Early ’09. That type of – after the crisis, yeah.

MS. YORK: And it seems to me that what we’re really – does that mean that what we’re really – to get back to, we were it’s fine, the service will do well. By going back to – will be opposing where we have been over a long period of time and that over a long period of time has serviced funds as well as we were hoping. So, I can see this where in a sense tinkered in ’09 and if this is approved to – in excess I think the timing is not to wait until – I personally think that in tinkering, and in terms of doesn’t work so well, it doesn’t work well. In terms of the allocation at least it’s hard to follow the target, whatever the allocation was and that is, I have not seen the another fund hat has done so well, and the only explanation for that is sticking to the formula.

MR. BERTONAZZI: I think it's helped – it's served you very well. I've been doing this for a long time and worked with a lot of boards and this board has been the most consistent with its asset allocation and the most willing to stick to the risk of the profile and when times were good, when times were bad and when were average. I think it is one of the very big reasons that your rankings have been so high and you've performed relatively speaking so well. So, whatever target we choose, you choose I'm confident you'll stick to it, it's just a question of which target are you going to be comfortable with going forward.

MR. MILLER: Well, I think to summarize it. The summary is that if you go versus more numbers based on the – you come back and then move forward.

MR. BERTONAZZI: That's fine with us.

MS. YORK: And we're still looking at the twenty going back through and working our way back to twenty five, so when we would go back to twenty nine this.

MR. BERTONAZZI: Correct. Yeah, that was – I was splitting the difference. I was going about half way back to wear we were before, but it hasn't –

MR. MOCARSKI: The twenty nine feels right with the back testing. I think understanding the strategies in this and how they were implemented, because you know, I was looking – you're looking at finding $17 million dollars to place in private equity and you know, that's three new managers, four new managers that we're going to have to find.

MR. BERTONAZZI: Yeah, we're talking, if we moved 5%, well that's about $15 million dollars or so. Yeah, it's a lot of money then we move it on up.

MR. MOCARSKI: Yeah, so we're going to have to start doing that work and think about the kind of manager and strategy in the targeted returns and , you know, which we probably won't get us to January, February, somewhere like that –

MR. BERTONAZZI: Well, you know that said, if Michael Boyd is right, we're going to wish we didn't tinker with this portfolio over the next six months or a year. Now does – I can get you a whole bunch of other managers in the cage that tell you the exact opposite, which is what I like because it tends to work to our benefit.

MS. YORK: And ultimately because – or what this is going to look like in five or ten years –

MR. BERTONAZZI: Correct.

MS. YORK: And that's, I mean, that's particularly and – I've seen it in the past, the board represents an automatic single investment and over time you have noticed and over time this has produced.

MR. BERTONAZZI: So it's not an easy decision for you to make. And I'll try to help however I can. So we'll do some more work if you like. We'll bring it back next meeting and go over it again and have your discussion and we will help however we can.

MR. YORK: The question for the next meeting is really what would you do with that five or ten percent, or how would you allocate it.

MR. BERTONAZZI: We'll give you a couple of things to think about.

MR. NAPOLITANO: How – would you say that 5% is too much, Eric. That's what I want to –

MR. BERTONAZZI: What we could do is do maybe go back from thirty four to thirty one, that type of thing, you won't see it a lot in the numbers, but it wouldn't be of some difference in the extreme years.

MR. NAPOLITANO: We can do it half year. The other we have to remember also, not only is the board been steady for the past several years, the contributions have been timely as well.

MR. BERTONAZZI: I'm sorry, I couldn't hear you.

MR. NAPOLITANO: Another factor is the last several years, the contributions have been coming in and at the appropriate time.

MR. BERTONAZZI: Yes, much better funding per year than in the past.

MR. MILLER: Let's move on, Motley Rice, a motion.

MR. NAPOLITANO: I'll make a motion that we continue the matter of Motley Rice, number III to the next meeting.

MR. YORK: Second.

On motion of Mr. Napolitano, seconded by Ms. York, it is voted to continue the Discussion Relative to the Motley Rice Portfolio Monitoring matter.

MR. MILLER: All those in favor?

COMMITTEE: Ayes.

MR. MILLER: The "Ayes" have it.

ADJOURNMENT: On motion of Mr. Napolitano, seconded by Mr. Mocarski, it is voted to adjourn the meeting at 3:50 o'clock P.M.

Lori L. Hagen

Second Deputy City Clerk

Kimberly Discullio

Assistant Clerk