CITY OF PHILADELPHIA

SINKING FUND COMMISSION

IN RE: November Meeting

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Wednesday, November 14, 2018

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This Meeting of the Sinking Fund Commission, held pursuant to notice in the above mentioned cause, before Angela M. King, RPR, Court Reporter - Notary Public there being present, held at Two Penn Center, 16th Floor Conference Room on the above date, commencing at approximately 10:05 a.m., pursuant to the State of Pennsylvania General Court Rules.

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STREHLOW & ASSOCIATES
FULL SERVICE COURT REPORTING AGENCY
54 FRIENDS LANE, SUITE 116
NEWTOWN, PENNSYLVANIA 18940
(215) 504-4622
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A P P E A R A N C E S

COMMISSION MEMBERS:
Donn Scott, Chairman
Rasheia Johnson, Treasurer
Kellan White, Controller's Office

ALSO PRESENT:
Christopher R. DiFusco, CIO, PGW
Alex Goldsmith, PFM Asset Management
Marc Ammaturo, PFM Asset Management
City Solicitor Representatives
PGW Representatives



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CHAIRMAN SCOTT: Good morning, everyone. It's my pleasure to call this meeting to order.

First order of business is approval of the Minutes dated September 12.

Is there a motion?

MR. WHITE: Motion to approve.

MS. JOHNSON: Second.

CHAIRMAN SCOTT: All those in favor say aye?

(Ayes.)

CHAIRMAN SCOTT: Ayes have it. Thank you very much.

The next item is the Review and Selection of Active Domestic Small Cap Core Managers. Turn it over to you.

MR. DiFUSCO: Sure. I will let Marc and Alex get into the detail of the two memos. It's essentially, a two-part proposal. Right now we have two active managers in the small cap space. We have Vaughan and Eagle. We discussed previously, and the Commission has approved the RFP. That is why we have three candidates coming in today for core manager.



What we would like to do is pair one core manager with a passive, with an index manager. So, that's the first memo. We would need a RFP authorizing us to search for a passive manager pegged to the S&P 600. We think this would do a couple things, not the least of which is lower fees which I think this Commission has done a good job on over the past few years. We have brought down fees fairly significantly.

I will let Marc and Alex go into the details of their two memos. That is the background of what we are proposing today.

MR. GOLDSMITH: Sure. Thanks, Chris.

You know, the genesis of this RFP goes back to -- similarly, to the other asset classes where this has been done. When we came on board in early 2016, the portfolio was largely set up on value growth dichotomy with style-bucket managers, value, you know, characteristics and then growth manager, growth characteristics.

It's a part of our philosophy that over time, the best of those sorts of dichotomies get you is a split or, at best, you can replicate



index performance. We prefer, you know, using a core manager approach where that manager has the discretion to select which factors may outperform at any given time in the market. There are periods when growth significantly outperforms core. We are in the midst of one of those periods right now. We think letting one manager make that decision rather than having manager with only one mandate focus on one side of the market yields better results long term.

Domestic equity space, if you recall, with the hiring of PineBridge, it's been most recently done with the international equity space with the hiring of Acadia and Earnest, two managers but both in the core space. Little bit different approach. There is quantitative elements to one and more fundamental elements to the other. But again, the theme is consistent.

That is what we are doing today. Interviewing three core managers, moving away from Vaughan Nelson and Eagle. You know, which if you look at their performance over time with the last five years, it essentially averages out to the broad Russell 2000. You are not getting





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advantage from having separate value growth over periods of time.

Chris mentioned the use of an index. We have obviously utilized an index approach in the other asset classes. It does lower fees fairly significantly. It removes the risk of missing a benchmark. However, typically again, you are not going to get any alpha above.

The Russell 2000 passive strategy has been approved for use in the Sinking Fund since early 2016, right before we came on board. It's sort of been sitting on the sidelines. Conventionally, the small cap space has been one where active managers have been able to, you know, utilize their informational advantage and outperform. And so you know, we -- while we have had that sort of an option to go to if we felt that market conditions warranted it using the Russell 2000 and a passive approach, we haven't utilized that just yet.

One of the reasons being that when it comes to indexing in the small cap space, PFM believes that there is, frankly, a better index to use. That's the S&P 600. That's the first

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memo you see in the book here. Essentially, the difference is, the S&P 600 includes -- is made up of all, you know, profitable, revenue-earning companies. Where the Russell 2000 includes some companies that are pre-revenue, pre-profit, essentially lower quantity. That's a vast much larger index. And you know, it's something we have done in our discretionary portfolios.

When we decided to add small caps, whether it's for tactical short term trade or diversification elsewhere, going with a passive S&P 600 is a way to access the asset class while keeping costs low. So that's, you know, the effect of pairing an active manager with an index, I think will be quite drastic on fees.

Right now the two funds are charging, you know, 1 percent for Vaughan Nelson and 80 basis points for Eagle. Across the asset class, you are paying all in 90. You know, the active manager that you will see in a proposed very attractive fees well below the current managers and/or total below, but then the effective pairing half the allocation with an index will be a reduced all-in fee of, I don't want to

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speculate, below 50 basis points. So, considerable fee savings.

And again, you know, you will have passive exposure. You are getting what the total asset class does. But remember, this S&P 600 has higher quality index. That should, I think, prevent some of the negative elements of investing in index. You ride the market up, but you also ride it down. One would expect higher quality companies to outperform in a down market.

I think maybe the first action -- I don't know do an action item right now. It would be to approve, you know, an RFP for the S&P 600, to switch the benchmark on the approved index from the Russell 2000 to the Russell 600. That would require an RFP.

CHAIRMAN SCOTT: That would require action?

MR. DiFUSCO: Correct.

CHAIRMAN SCOTT: The action again is to approve?

MR. DiFUSCO: Posting an RFP.

MS. JOHNSON: We would need an index

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manager for the S&P 600?

MR. DiFUSCO: Correct. We would need approval to put up the RFP. If the Commission is inclined, I would ask someone to make the motion to approve.

MS. JOHNSON: I will make a motion to approve unless questions.

A motion to put up the RFP for the S&P 600.

MR. WHITE: Second.

CHAIRMAN SCOTT: All those in favor?

(Ayes.)

CHAIRMAN SCOTT: Ayes have it.

MR. DiFUSCO: Thank you.

MR. GOLDSMITH: We will write that up.

The following page, the next memo is the summary of the three managers. I gave an overview of where we were coming from and what we'd ideally like to get to.

Like I mentioned, all three of these managers are core in that they are not dictated to a value or growth benchmark. All three of them are benchmarked to the Russell 2000. Now you might say, why don't we benchmark them to

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the S&P 600? It's -- the universe of active managers and small cap, majority of them are benchmarked to the Russell 2000.

Additionally, the plan benchmark or the -- the plan benchmark is the Russell 3000. We included small caps, including large caps, the equity component. But the way the IPS is stated, it's stated that active managers will look against -- will be benchmarked against broad market indexes such as the Russell 2000. It is explicitly mentioned in the IPS that given the total component of the plan, you know, of the small cap plan should be looked at against the Russell 2000.

It's sort of an active decision to add that S&P 600. We are trying to the use that 600 to basically beat the 2000. The active manager, their goal is to beat the 2000. As a whole, that is really our target in between whether it's PFM staff, management. When it comes to small cap space, the desired benchmark is that Russell 2000. That explains the difference there and why the benchmark these managers against the 2000.

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You know, broadly, two of the managers are fundamental managers running concentrated portfolios focused on bottom-up stock selection that. That is looking at each company based on the individual merits of, you know, their capital structure, you know, return on equity investment at the company, abilities of management, competitive position in their market, you know, relative to similar firms, competitors, you know, the traditional bottom-up approach.

Where the other funds, those funds are Copeland and Macquarie. There are some distinctions between them. I will get to them in a second. The other fund, Matarin. This is a quantitative model driven approach. I don't want to say it's formulaic in that these models are built. And so, that there is constant feedback given in the weighting of, you know, the factors that go into model output are constantly being updated or changed, adjusted or based on what industry a company is in or current market conditions.

There is, you know, portfolio manager

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element to it. There are macro decisions set. Human intervention is there at all areas -- at all stages of the process. But this portfolio is -- could be larger in terms of the number of stocks. It will be somewhat more benchmark like. You know, will have a higher turnover.

Between Copeland and Macquarie, I think other slight differences there. Both tend to skew towards the high quality spectrum of the small cap universe. So likely, they are going to hold off revenue profit companies anyway. Copeland, specifically, I think they looked quality in the dividend growth space. So you know, I think a lot of -- they will say to themselves, I think a lot of companies you think of large caps paying these kind of dividends.

There is a lot of small cap companies more greater number, actually, that are dividend players. It's an indication of the health of those companies how frequently and by what magnitude they are able to consistently grow their dividends. I think their philosophy is rooted in that.

Whereas, Macquarie, they basically take

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a pure bottom-up approach. There is not a lot of, almost no macro tilt to that portfolio. Their sector stock weightings are very similar to the benchmark. And they are looking for the best performer or best position, best -- you know, operating companies within each of those sectors.

You know, just some other asides, Matarin is a certified aluminum business based in New York. Macquarie, while they are owned by the large Australian conglomerate, they are the -- their investment management arm is actually headquartered here in Philadelphia via the acquisition of Delaware Investments. And you know, so they qualify as a local business. Copeland is based in Conshohocken which I think by definition excludes them from officially being considered a local business.

MR. DiFUSCO: I think it's also just worth mentioning, Copeland's fees are on page 39 of their proposal. They come in -- I am approximating here because of the tier breaks. Copeland was by far the lowest. They are at around 55 or so basis points. Matarin, they are





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on page 17 of their proposal. They are approximately 80, give or take. And Macquarie is on page 32 of their proposal. And they are roughly 85. And that, again, is because of the tier breaks. That is why I am approximating. Because it will depend on the exact dollar amount that is put in.

So you know, Copeland came in with the most competitive, you know, bid out of the three.

MR. AMMATURO: Relative to the universe of small cap managers, 55 basis points is very, very low. That's usually like a large cap fee.

MR. DiFUSCO: Yeah. That's very low.

And so, we had each manager scheduled to speak for approximately 20, 25 minutes, you know, and answer questions, et cetera. Happy to taken any preliminary questions before they begin if the Commissioners have any.

CHAIRMAN SCOTT: Do you normally see a disparity of that many basis points?

MR. DiFUSCO: For a fee? I think to Marc's point, it was a little surprising. I would have expected, you know, the lowest fee



to, let's say, maybe be 65 or 70. Fifty-five is very, very aggressive. I mean, you know, in a positive way, not in a negative way aggressive. You know as Alex mentioned, current managers who I think particularly Vaughan are a little on the high side. Vaughan is around 1 percent, Eagle is around 80. That is more typical in the small cap universe.

I don't think Matarin or Macquarie's fees are out of line compared to the universe. But Copeland is clearly, you know, aggressively pushing for the business. Discounting heavily relative to their peers. I would not say that that's normal. It's appreciated, but it's not normal.

MR. AMMATURO: Yeah. I echo those comments. Their pricing in the business, it's an outlier, 55 basis points, for small cap.

CHAIRMAN SCOTT: Does the City potentially claim any of these?

MR. DiFUSCO: We do not. We've interviewed Delaware for other -- Delaware/Macquarie. I have to go back and check my notes. It's been quite a while. We may have



distant pass used Matarin and/or interviewed them, but it was -- I am reaching there. It may have been before I started with investment staff. I feel like I have some familiarity with them, you know, from prior interviews. But we do not use any of these three.

MS. JOHNSON: Just so you know, we actually are in the midst of -- on the investment side for the City's dollars are contracting with Delaware Macquarie, so they can start to manage some of the City. It's very short-term.

MR. DiFUSCO: Okay.

CHAIRMAN SCOTT: When a firm gives us a fee, they are locked into that fee for what period of time?

MS. JOHNSON: Everything is negotiable.

MR. DiFUSCO: Everything is negotiable. There is no -- we can always press -- I mean, we always -- we get an initial fee. PFM and staff always go back and ask for best, last and final. That doesn't preclude us from pushing them again at the table or after the meeting. They are not locked into anything.



I think to Rasheia's point, I was unaware of that. I appreciate her bringing it up. That may give us a little more leverage with Macquarie because we can ask them, you know, to basically treat all the assets as City assets the same way we have done with PGW and municipal plan. We want to treat everything as one pile of City money for fee purposes. We may be able to exert additional pressure on that to lower the fees.

CHAIRMAN SCOTT: If a firm says 55, is that forever and ever?

MR. DiFUSCO: No.

MR. AMMATURO: It's not going to go higher.

MR. DiFUSCO: It's not going to go higher. Always able to -- I apologize. I didn't understand.

CHAIRMAN SCOTT: The bait and switch? That's what I --

MR. DiFUSCO: No. It's not going to go higher.

MR. WHITE: Like Comcast Cable.

MR. GOLDSMITH: These are five-year





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contracts still, correct?

MR. DiFUSCO: They are series of rolling one-year contracts. But it would never go higher. If a manager came back and said they wanted it to go higher, we would have to agree to that, which we obviously wouldn't do.

Will not go higher. We will always try to push it lower. Sorry about that.

CHAIRMAN SCOTT: No, no. No problems. Should we go on with the interview process?

MS. JOHNSON: Yes.

MR. GOLDSMITH: Okay.

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(Copeland Capital Management Reps brought in.)

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MR. DiFUSCO: Good morning.

Thank you gentleman for coming in. So your Commissioners are Donn Scott, Chairman; City Treasurer, Rasheia Johnson; and the First Deputy City Controller, Kellan White.

If you can take 20, 25 minutes, I will try to give you hand signals, five-minute warning sort of last question. Sure we will have questions along the way. Just go through



your strategy, your process and, you know, why you think you can add value to the PGW plan.

MR. BARRETT: Sure. Thank you for the opportunity to come in here this morning. I guess just brief introductions. My name is Chuck Barrett. I head up sales and relationship management for Copeland Capital Management.

MR. GIOVANNIELLO: Mark Giovanniello. I'm Chief Investment Officer and lead portfolio manager on small cap strategy.

MR. BARRETT: Great. In the interest of time, we handed out a presentation, maybe tell you a little bit about the form Copeland Capital.

We are a local firm. We are based just up the road here in Conshohocken. We are 100 percent employee owned, most members of the firm are equity owners. Every member of the investment team is an equity owner in the firm. We think that's an important part of our firm's organizational fabric and culture. I think it bleeds into how we manage the strategy as well as how we manage the organization.

We do one thing and one thing only, and



that's dividend growth investing. We do it across all capitalization ranges: Large, mid small. And even then separately, we do it with an international team as well that applies the same process to international focus.

As I said, we are based right up here in Conshohocken. We manage about 3 billion in assets. We've grown quite a bit over the last few years. We've added some key folks to the firm as you can see by the timeline. In 2012, we hired Erik Granade a formal global equity CIO at Invesco. More recently as the firm has grown, added Steve Adams from AMG. More recently Sofia Rosala from Aberdeen Funds and Anthony Godonis from Aberdeen, as well. As we have grown, we have developed a very significant operational and compliance infrastructure, as well, which we think is a very important part of the organization.

Page 3 tells you a little bit about some of the entities we manage money for. We have a very diverse client mix across different client types as well as across our different strategies, or small caps, mid, and all cap. I



can see some large corporate DB plans: Union Pacific and Caterpillar to name a few. Some large public funds: Pennsylvania Municipal Retirement, Chicago Transit Authority to name a few as well as some sizeable endowment foundation assets. And it's some large subsidized mandates with the likes of Russell and JP Morgan. So if there are no questions at the firm level, we can dive into the philosophy and the process and how that all comes together.

Does that make sense?

MR. GIOVANNIELLO: We do layout on Slide 4 the team, myself as I mentioned, CIO. Lead PM on the dividend growth strategy, also covering a couple of sectors, healthcare, energy and materials. We break up the world by sectors. This team is managing all -- each of the domestic strategies. And we have had stability. We have -- last man hired here was John Cummings back in 2014 right out of Haverford. We are proud of everyone being an owner in the firm on the team, even the young folks and having never lost anyone and having nice stability over time on the team.





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I think that points as well to the culture, the entrepreneurial attitude at the firm of a small emerging firm, but also one willing to share equity with everybody.

The real differentiator of Copeland is that we are solely focused on dividend growth investing, as Chuck mentioned. We believe that companies that consistently raise their dividend every year are most likely to outperform the market with a lot less risk, significant less risk. Typically, it's been a large cap phenomenon where you probably heard of many firms or strategies available in the large cap space, big blue chip companies such as Johnson and Johnson and IBM and so on, long term dividend growers. We are able to find companies in the small cap space, emerging companies that treat shareholders well, have a business model that's conducive to producing cash every single year so that they can pay and raise dividend every year. As a result, it puts us into a very attractive corner of the small cap market.

If you look on Slide 6, we show the typical Efficient Frontier, the brisk reward

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equation of where you invest in the market. Typically investors are very much expecting as you move down market cap, the further smaller you get, the more volatility to expect. What we have found is that honed in only on dividend growers, if you're looking at small cap, that diamond land, it actually has a risk profile really closer to large mid cap stocks in between. So, you are able to get access to high quality companies with greater growth opportunities given their size, but not take on the substantial risk, what it exists in the small cap benchmark.

If you look on Slide 7, you will see if you focus in on the Russell 2000, you will see 54 percent of the companies in that benchmark do not pay the dividend. And most of those companies are not earnings companies. Development stage, higher risk companies, some will succeed of course. There is a huge failure rate within small cap companies. If you look way over on the right, the S&P 500, one of the reasons we believe it's more stable and expected to be less volatile is because 73 percent of the

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company that actually have that ability to pay and raise their dividend every single year. And when they raise that dividend signal, the strength of their business look down into the small cap only 30 percent of the company.

So, we are able to find companies, if you look at the numbers, up in small cap, that there are 800 names that have raised their dividend at the current time by one year just in the last year. We actually hone in more on the three five-year plus div growers or average year of dividend growth. Happens to be about nine years in the strategy, but the availability is broad. You can see there is availability of 800-plus names, as many or more than you have when investing in large and mid cap only strategies.

So in the two points within one, we have plenty of names to pick from. But also that our benchmark that is more volatile, has a low percentage weight in these high quality successful companies, cash flow generative companies. And so, we are able to differentiate dramatically from that more volatile benchmark

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but still provide what we think are extremely attractive returns. If you look on Slide 8, this is going back to the 80s. We asked Ned Davis Research, which is research firm well known in the industry based up in Boston, produces a lot of studies related to dividend policy for the market. Most people have seen the large cap version of this study. We asked them back in 2009/2010 when we started launching these small mid cap strategies, to look at the studies they have done for large cap companies down market cap. They had never thought of it. No one had ever done it. Still today, we think we are the only managers out there doing investing in this way.

Ned Davis produces this for us. And you can see over time, this is back to the '80s, a very attractive premium return profile even though if you look at the bottom left, that risk profile well below other types of stocks, they break up the world by companies that pay a dividend, keep it flat or is really modest. Companies that, of course, we like that grow their dividend and then companies that don't have a dividend at all or cut their dividend. Of course, you know how you can expect companies to do that to be highly volatile and be poor performers.

The result in the bottom right, you can see upside/downside captures. There are a lot of numbers here. But one thing to hone in on is the ability to only have 63 percent downside capture. This is back to the '80s. It's not the performance of our strategy. But when you look at the actual numbers that we have had over the last close to nine years running, the small cap strategy, they are very similar. Upside capture in the '80s, that means when the market is up 10 percent, we would hope to be up 8 percent of that. When the market is down 10 percent, like it was in October, we would expect to hopefully be down only 60 percent of that, 6 percent. Actually, in October, we outperformed by 4, 500 basis points. The Russell 2000 was down 12 percent.

MR. GOLDSMITH: I was going to ask about the statistics, what they would have looked like in 2018. You say year-to-date through



September. Would it have been the same dividend growers outperforming, or has that not been the case until October.

MR. GIOVANNIELLO: So, we have a slide on that.

MR. BARRETT: On page 33, you will see that.

MR. GIOVANNIELLO: Through September and actually for all of 2017 and 2018, there was a very significant headwind against dividend growth. So if you look on Slide 33, 2017 small cap dividend grows in general were only up 9 percent while the bench was up 15. We, however, although we are only in that dividend universe, we turn 15 percent. You can see the non-dividend payers, the riskier stocks were actually up more. That was the year the market had a preference because of the low volatility requirement and the small returns of the market, people gravitate towards those higher risk stocks.

That's fine. We are fine to leave the lag a little bit on those big upside moves. Non-dividend payers are up 17 percent. Dividend



growers only up 9. We were able to do 15 percent. We will get into why we were able to do that. Has to do with our stock selection, our quantitative research we do that helps us do a better job picking within the dividend growth universe to add value. If you asked about 2018 through September, there was also a major headwind. Only 7 percent return for dividend growers, non-dividend payers up 15. Benchmark up a 11 and a half. We were a little bit ahead. Only modestly ahead. That was probably a little better than expected when most rapid rises in the market.

We have had years where we outperformed in big rallies. In most strong, aggressive rallies, we expect a lag a little bit. Now ten years into the longest running upturn in the market and the economy since 2008 and 2009, we think the risk of a rapid rise in the market from here to the next three or five years where you might be concerned or ten years is very low relative to the chance for more modest returns or more volatility like we are seeing emerge this year in the market in the environment where



dividend growth really shines.

You can see this year we actually -- we were only outperformed a little bit through September despite the headwind. But during October through this quarter, we are outperforming by 400 basis points. Up significantly as volatility spiked, the markets drew down. We delivered that downside protection. I think that's what our clients -- Chuck mentioned the client list upfront. That's what they appreciate more from us, most from us is our predictability. They know we might lag in an aggressive rally, but they know in over a cycle, we are very likely to outperform with less risk. In those tough times when they are trying to protect assets of their pension, say, they are more like, very likely given that downside protection.

MR. BARRETT: Maybe it makes sense to jump back to page 10 and talk about that a little bit in terms of how that plays out as results in blowups. And I think we will close this up and entitled more specifically about the process of how we manage money.





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Page 10, hopefully is eye opening to you. We talked about the universe of dividend growers and the small cap space. You can see the reason why the benchmarks characteristics are so volatiles is that this is going back to the early 1990. That 23 percent of all small cap, non-dividend payers will underperform the benchmark every calendar year by 40 percent or more. That's a big number when you contrast that to the five-year dividend growers, that drops to only 6. By simply avoiding that group of names, we can remove a lot of the volatility.

Then you flip over to the far right side, in terms of the -- that is the opposite by outperforming by 40 points or more. Shows you, we may miss a couple of home runs by being in this universe, but not as many as you might think. We will gladly take that trade off. We actually did an analysis even yesterday.

In calendar 2017, there were 137 small cap non-dividend -- 175, that underperformed by at least 40 points or more. Forty percentage points.

MR. GIOVANNIELLO: Because of what we



did, our history on Slide 11 shows you that year to year our presence of blowups in the portfolio, you can't miss everyone, is very small relative to the benchmark. And that is where we get a lot of our added value. There is a reason, though. It's not just that these companies raise their dividend, they avoid blowups. We think companies that have a rational recent allocation of their cash flow between investing in the business instead of -- and paying some back to shareholders are more cautious with shareholder capital.

So, a lot of companies, particularly at this point in the cycle, are being very aggressive with acquisitions, paying very high prices and premiums for acquisitions, leveraging up their balance sheet to do so, maybe building capacity right at the top of the macro cycle. Companies that are required by the board, by the shareholders to raise that dividend every year need to make decisions in the mindset of, hey, will this be cash flow, free cash flow per share creative to our business next year so I can deliver what is expected to be another dividend



hike. Or else frankly, they are out of their jobs. That's the mentality.

If you raise your dividend and then have to cut it after that, that's a tough year in future employment as manager. These companies are more careful; hence, they avoid the big mistakes a lot of companies make.

MR. DiFUSCO: You mentioned, you know, how you did last month when the market turned down. Maybe it was fortuitous that the products started, you know, when it did in September of '09 after. Have you done any back-testing to see how --

MR. GIOVANNIELLO: Yes.

MR. DiFUSCO: -- you would have performed in '07, '08, early '09? And what did that show?

MR. GIOVANNIELLO: Even to push back a little bit, like, when we lunched the strategy, that was probably the hardest time to launch the strategy from the availability of dividend growers and small cap and one side, which was still enough to launch and begin a strategy. It was also in the middle of big beta rally. Our



relative performance was a headwind, and has been a headwind since we launched. Still beaten by about 300 basis points a year. We are proud of that even though it's been a double digit return in market.

During the 2008 period, you would expect that the dividend growth universe as well as our model would have significant downside protection. So, we would see -- we actually have numbers on those studies. But pretty dramatic. We actually had outperformance. We had large cap strategy was live. And it did beat by 10 percentage points in a down 38 market. I will tell you that the small cap, because they are so far fewer dividend growers in that bench, the outperformance was even better down market cap.

MR. DiFUSCO: Thank you.

MR. GIOVANNIELLO: We even have an example in here of another period.

MR. BARRETT: We do. Page 31 shows the most substantial period of a down draft since the strategy's been launched. It's pretty significant, while it didn't feel like it was





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because it was spread over two different calendar years. You will see from July '14 to February 2016 period, the Russell 2000 was down 25 percent. We were down half as much. So, there have been instances while the market is essentially gone straight up since 2009, there have been brief windows of pull backs. This one that we talked about as well as October where the strategy has demonstrated significant downside protection characteristics.

MR. GIOVANNIELLO: We have talked a lot about defense. I'd like to make the point on Slide 12/13, where we are actually looking for growth companies. Actually, helps us keep up more than would expect in conservative defensive strategy in the up markets. Most people, investors believe that a company that is small that is paying dividend is waving the white flag. We don't have any good investment opportunities. We are paying out on dividend.

There are certainly some of those companies that are high yield, low growth, interest rate sensitive even companies. We are not that. We are not a dividend yield strategy.



We are looking for companies that pay a modest dividend, retain most of their cash flow and earnings to reinvest for growth. So, we are looking for the subset of our universe of dividend growers that have great growth opportunities in front of them. That they are not just, you know, low GDP type growers, but actual have the capacity to raise their dividend 10 to 20 percent or even more. Our average dividend growth is 15 percent today in accelerating as it's been a good year for earnings as well as with the tax cut.

Most of our companies are benefiting quite a bit. In a nice pace of dividend growth relative to a benchmark of 6, 7 percent dividend growth.

MR. BARRETT: Why don't we just get into how.

MR. GIOVANNIELLO: Sure. Slide 13 shows you the premium growth we have relative to the benchmark which results in a strategy that most dividend managers or small cap are either high yelled or deep value. That's not -- we are into growth companies with rational conservative



investment in the business to drive future dividend growth.

To Chuck's point, how we pick stocks, we talked a lot about the universe and place it puts us to win and beat the market. But we also have on top of that a great team, a lot of now over ten years since 2005, the firm running quantitative models and really significant research that's been done and invested to figure out which company's of the universe are most likely to raise their dividend to outperform and which ones are most likely to cut dividend.

Most important for us are criteria such as dividend coverage that cushion between cash flow and earnings relative to the dividend being paid. As the company raises its dividend ratio and the payout ratio is up too high, that signals less cushion for downturn in earnings or cash flow. So that in the next -- when that problem hits, we might have to cut. That is, of course, very tough for a stock.

We are focused in on profitability of the companies, the return on investment they generate. If you jump to Slide 18, it gives you



a little more of the nature of our quantitative process. We show seven different categories of what drives, we think, the best dividend growth in the future. It's companies that have high profitability. They have very healthy balance sheets, very little debt. Companies that convert earnings into cash, they have high quality earnings. You need to have that cash flow to produce growing dividend. I mentioned dividend health.

And we are also looking for companies that are consistent over time. Our modeling work goes back over a decade. Many of the factors that we'll look at how did earnings margins, return on investment trend in other tougher time periods so that we can tell our investors, our clients that every company in our strategy, we hope will raise that dividend regardless of the macro or competitive environment next year. That is where fundamental research is focused on ensuring.

When we start the blocking and tackling on Slide 21 is a good place to look. How do we pick now within a model that is telling us, hey,





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here are the top ranked names in healthcare, how do we select one which ones in the top rank names? We look for an understanding of how the company is producing their cash flow. What is their competitive mode on businesses? Is it likely to continue in the future? What is the growth potential of that industry? And is management appropriately attacking that growth opportunity by investing in the business?

A lot of our names might invest 80/90 percent of their cash back in the business for growth have a modest dividend in 1 to 2 percent and really drive that next three to five years of dividend growth when we hope the stock price would be a wise investment in new or higher return projects. A lot of industries aren't conducive to growth. You don't want them to invest that much. They should be paying out more cash as a dividend or buybacks, returning to shareholders. But those are less likely to be names we are interested in. We are looking for names with great growth opportunities.

Ultimately, as a team, the analysts team needs to forecast, what will dividend growth be



in the future. We think we have a 15 percent approximately growth forecast going forward over the next three to five years. That could lead to a doubling of the dividend, cash flow stream in the portfolio over above four to five years and, hopefully, a doubling of stock prices if we don't make valuation mistakes. We care about what we pay. We think we would like to pay reasonable price for the growth in the quality of the companies that we are investing in. And if we do our job right there, we will get that solution of high dividend growth. But also while we go, about a 2 percent dividend yield to augment our returns.

Maybe an example makes sense. U.S. Physical Therapy is the healthcare guide. It's a great story. The physical therapy industry is great demographic. I know I am a big customer. And it's a business that is -- demands consistent growth in volumes over the years. Very little macro sensitivity. It's a fragmented industry. It's a company that takes a 5 percent growing organic business that opens new stores with cash flow. Makes a modest size



acquisitions, not huge ones to drive double digit sales growth and even better, 15 or so percent dividend growth. It's a competitively advantage company, strong cash flows, very little macro risk. It's really in our sweet spot. So if we can have a portfolio of 50 or so companies with a bar chart like on twenty-three with dividends moving higher, we think the stock prices will follow ultimately.

Just quick on the sell discipline. We think selling as we are when we buy, a name that doesn't raise its dividend in any year is out, no questions asked. We need to raise that dividend. In fact, we track every dividend announcement. In fact, we think one of our advantages is to focus in on dividend information. Others can get it, but they don't pay attention.

The growth companies we own, others own it because they're high quality. And that's growth prospects. We own them when they raise that dividend. And when others don't pay attention to it, we have an edge in making our decisions. We also look for deterioration in



the model, pay out ratios that are stretched, cash flow that isn't covering the dividend and rate signals that have problems coming around the corner. And that focus makes us better in our sell decisions.

MR. BARRETT: I guess maybe just in wrapping things up here, I guess a couple points worth mentioning. On page 30, you can look at the year-by-year returns of the strategy. I think we did a pretty good job of pointing out how the strategy can certainly protect on the downside and provide some downside protection. You saw that play out in 2015 where the bench was down four, we were up five. Year like 2011 where the bench was down four, we were up one. But Marc spoke to it. I think it's important to highlight, it's not purely a defensive strategy. In year like 2013, when the benchmark was up 38 percent, we were able to outperform, as well.

We wouldn't expect to outperform in every 40 percent return environment, but we can deliver to the upside, as well. It's not purely a downside protection story. And I think it's the consistency of that return patterns that





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enable us to generate strong returns, be entrusted with the meaningful pulls of capital that we have. And we would think that that type of predictability would make your life easier. Another thing that we wanted to highlight also is up front on page 14, we didn't speak to it. But obviously, as rates have increased a little bit here as of late, who knows what they will do in the future, but it certainly is a topic of conversation. I am sure in rooms like this, as well as many others are having, what happens in a rising rate environment.

If you look historically, and that's all we can look at, historically, small cap dividend growth companies have actually been the best performing group of small cap stocks during periods of rising rates. So, these types of companies we spoke to, they are not high yielding dividend payers or they are not high yielding payers clipping that coupon. They are modest yields, high dividend growth throughout most of the return from that stock price depreciation, that rate of dividend growth pulling the stock price higher. These names



don't get traded out at rising rates. People don't pull them for the yield. They also tend to have a very healthy balance sheets. They are not constrained by higher borrowing costs during the period of higher rates. We wanted to point that out.

MR. GIOVANNIELLO: Just in summary, I think we would like to point out that in hiring an active manager, I know everybody is looking for a reason to believe they will drive some significant value over a passive benchmark. We think we found a solution to hone in on the highest quality companies, exclude those that are more volatile, more risky, have a lower rate of success and derive some consistent outflow over time.

Hope you guys can see that, as well. We'd love to work with you. Thanks.

Are there any questions that we can hit on?

MR. DiFUSCO: You answered mine.

MR. AMMATURO: You mentioned 3 billion assets. Can you comment on the trend of that? Is that due to firm size? Is that going to



peak? Where is that?

MR. BARRETT: We are at peak.

MR. GIOVANNIELLO: Good trajectory. Consistent strategies. Back in '09, we had a hundred million. Chuck and I really started growing the firm, 2012 we had a billion. I think we put it on the chart in 2012, we had pretty consistent growth since then.

MR. AMMATURO: How about the break in between? The institutional, how does that vary over the years?

MR. BARRETT: It's -- our business is almost exclusively institutional. We have high net worth. We have a mutual fund complex, our own. There is roughly 300 million in that. It's relative small percentage of our assets.

MR. AMMATURO: Thanks.

MR. DiFUSCO: Thank you.

(Copeland Capital Management presentation ends.)

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(Macquarie Firm Reps brought in.)

MR. CORKRAN: Thank you for having us here today. It's real pleasure to have this opportunity to present our capabilities with



small cap core. I am going to -- I will start off with some brief introductions. And then I'm going to hand the discussion over to our portfolio manager Frank Morris to really give you the sense for how we are doing in small core.

My name is Skip Corkran. I'm a senior member of the relationship management team at Macquarie. Been at the firm for six years. And I came to Delaware from BlackRock, where I spent ten years as a member of their global client group. I've been in the industry for about 26 years, and escaped most of the gray that goes along with that number until I grew a beard, and then it all came out. I'm probably going to shave this off soon.

On my far right is Shawn Lytle. Shawn is the Deputy Global head of Macquarie Investment Management. He is our leader. He's based here in Philadelphia as a member of Macquarie Group's Management Committee and also President of the Delaware Fund. Shawn came to us in 2015 as President of Delaware Investments, which we then branded in Macquarie. And prior





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to coming to us, he spent thirteen years at UBS where he ran all of UBS' investment management business in the Americas. He's a very accomplished investment management executive, and we are very pleased to have him here. He's also a member of the National Association of Securities Professionals, and is just coming off his year as chair of that organization. And also, member of the Sustainable Accounting Standards Board.

Shawn is here because this mandate is important to us and because we feel very strongly about the city in which we have our home headquarters. So, we wanted to make sure that you know that senior eyes are going to be on this mandate if we are, in fact, selected.

Next up is Frank Morris on my right. Frank is the Chief Investment Officer for Core Equity. He is the leader of the team that would manage your portfolio, and is also the portfolio manager who is ultimately responsible for the performance of this small-cap core product. So, the buck stops with Frank.

And he joined Macquarie in 1997, and has



35 years of experience in the industry. So, Frank has seen every type of market you can imagine including the Crash of '87, the tech bubble inflating and bursting in the '90s, and then also the financial crisis in '08. So, Frank is the guy you want to have around when things are getting dicey in the marketplace.

My hope is that you come away from this presentation with three key takeaways. One is that Frank and his team are highly experienced. The team averages over 29 years of investment experience in the industry. And that's meaningful value add.

Secondly, the disciplined approach that that team employs produces very consistent performance results. They are not just inclined to perform well in one type of market environment. They produced consistent results in all types of market environments, both good and bad.

And then finally, there is a culture of access in Macquarie that really sets us apart. If you become a client of ours and you manage a small-cap core portfolio for you, we encourage



you to take advantage of the entirety of the firm's capabilities. So, we have teams of experts and infrastructure and fixed income, real estate. And we encourage our clients, whoever -- whatever product they are actually using, to take advantage of us and help us help you in any way we can. And so, the culture of access is real important.

With that, Shawn, I am going to hand it over to you to give a few comments on the firm.

MR. LYTLE: Yeah. Have you go to Section One behind that pretty black tab. One, the firm overview and on page 6.

Just following on from Skip's last comment. I mean, this is an important mandate for us because this is our home city. And we take a lot of pride in the fact that we are based in Philadelphia and have always been based in Philadelphia.

We have been here since 1929. Delaware Funds, previously Delaware Investments, was named after the Delaware River. And we made a firm commitment after Macquarie Investment Management purchased the firm almost ten years



ago now that we were going to stay in Philadelphia.

So currently, what we did when I came in was to name this as our global headquarters for the overall organization here in Philadelphia, and we have continued to expand our staff. We have moved from a little under 500 staff up to 550 over the last three years, and continue to plan to invest in our home office and our home team here in Philadelphia.

A key part of that is the equity team and equity resources we have here. We trade all of our equities not only for the U.S. but globally out of Philadelphia. Have a large trading desk here as well as have a number of different equity boutiques. Frank, being the leader of one of our best boutiques that we have, equity boutiques we have based here in Philadelphia. But we have a number of other teams. And that point about delivering a high touch client service and customer portfolio is important.

Page 7 and 8, I'll just touch on these briefly. You know, page 7 is the commercial,





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what you see from every asset management, our commercial is this. We are a top 50 global asset manager. And we are top 50 global asset manager that's actually based in Philadelphia.

We also very proud of the fact we have the 43rd largest mutual fund family in the United States. Actually this year, we are actually ranked number 23 in term of flows in term of mutual funds. There aren't many winners in mutual fund industry. There aren't many winners in active management funds in the mutual fund industry. Frank's fund, actually, has been one of the number one flow funds in this category in the United States. And overall, our fund family is growing and off the back of very strong performance, particularly in our equity strategies.

So, we are very proud of that fact. And proud that, you know, we can say there is another big fund family here in town rather than Vanguard way out in Valley Forge. Other point is that we are the world's largest infrastructure manager. That gets the point, if you go to page number eight, we are running

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currently almost $140 billion in infrastructure. We are the experts in infrastructure. We basically created the asset class.

We just finished and reopened the Goethals Bridge in between here and New York. We actually oversaw the construction and development of that, and running that for the city. We own half of Teterboro Airport. We own a lot of other utility and other assets around the United States. And really trying to partner with communities and municipalities. And figure out how we can do things in a smarter way here in the US as well as overseas. That is a big emphasis in addition to the traditional equities and fixed income that's been our expertise for, you know, over 80 years.

On the equity side, we are running 95 million in assets under management. It means that we are a top manager, but we are not too big. This is something very important for us. We really do manager our capacity carefully and the number of client relationships we have, particular with Frank's strategy it's important. We are closing down the number of new money we

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are taking with mandate because we really do manage our capacity. We want to make sure we are managing our performance for our existing clients. It's very important to us. We have done that in a number of areas.

Key point there is, you will be important part of our client base. And particularly given you are here in Philadelphia, we are big enough to compete with the big players. We are not so big that we lose track of our clients and really focus on what's important which is performance.

And on the last page here on page 8, and I am very passionate about this, is our commitment to Philly. You know, I moved here from Boston -- sorry about that -- but moved here a couple of years ago after a long stint overseas. And I really made this my home. One of the key things we wanted to ensure is that we are making a big impact on the community. And from our standpoint, Delaware Investments was a firm that's been here since 1929 when we didn't really connect with the community and give back to the community in a way that I thought we

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needed to.

As you see, in terms of investing in our community, we really stepped it up in terms of our engagement with charities here. We are the number one sponsor for the Police Athletic League, PAL. Also number one sponsor for Girls Inc. Now we just raised $140,000 for them within an event we did last month. We now come in almost over ten yours, $2.1 million to charities around the city. Also, a big sponsor of Settlement Music School as well now with the Quakers and Girls Inc organizations.

As part of that, we also recently announced we are the prime sponsor on the Palestra, the basketball court over at UPenn, which gives us not only an opportunity to increase or visibility in the community, but also ties us into three charitable organizations that is part of Penn, especially girls' and women's charity there that will be connected and be able to do events with them.

In terms of being a prominent employer, we are one of the city's larger employers in terms of number of employees. Also important is faculty just announced we are moving our corporate headquarters, staying in the City of Philadelphia. We have been at 21st and Market since 1987. We are moving to 6th and Market. We are going to be right on Independence Plaza. We are taking over the Dow Building. We are making that our global headquarters. The Macquarie name will be on the top of the building. And we are going to continue to expand here in Philadelphia. We think it's a great place for talent, and particularly for young talent, that we are bringing into the organization.

And then finally, from a diversity inclusion perspective, we are doing a number of things in addition to the charitable work. We have been a prime sponsor now for the women's PA Conference. We have 60 employees attend that conference just a few weeks ago. We also got very involved in the Chamber of Commerce and also sponsoring diversity and inclusion events for the Chamber of Commerce. And John Fry, who is actually on our mutual fund board. He is on the Delaware mutual fund board, he and I been



partnering on a number of other initiatives to make sure we are fully engaging with the Chamber of Commerce and with the city.

Key point is, this is our home. We know this is your home. We want to make sure we do a great job for the City of Philadelphia, for Philadelphia Gas Works. And we will treat this mandate with a lot of the care if we are chosen.

MR. MORRIS: Thank you, Shawn. I will take over from there.

Pleasure to be here. Thank you for inviting us. I am going to talk a little bit about the small-cap core product philosophy, our process, our people and close a little bit about how our performance has been.

I'm on page 11 behind tab two. You know, our philosophy like that, the entire firm is that we believe in active management. And you know, we believe the markets are inherently inefficient. And that we find no greater inefficiency than those that exist in small-cap space. And I always say, if we are doing our job correctly, we are finding a 300/400/500 million-market cap company and growing with it



over time. We have gotten to it before. It was found out. We go to it before it was resurged. We invested in it at the beginning of its product cycle. And we grow with it over time until it becomes a large-cap company.

We are fortunate the small-cap space has a tremendous amount of inefficiencies in it. And then the question just becomes how one exploits the inefficiencies. For us, how we exploit the inefficiencies is through the combination of fundamental research conducted by the five-member team I will introduce you to in a moment along with quantitative techniques on the front end, which help us screen the universe down to an acceptable number of names to be able to analyze. And on the back end, to get a feel for and understand the risk that's inherent in the portfolio. So, we want to make sure that the there are no unintended consequences from the risk point of view within our portfolio.

You know, the benefits for those that are invested with us are listed in bottom of the page. We are very disciplined in how we manage our client's capital. That's enabled us to



generate good returns. Skip has pointed out, we go up and down markets. We have had a very stable team of applying consistent process over the number of years. We are very consistent in terms of our positioning within the small-cap core space. And finally, the hallmark of what we do is to generate a very high risk adjustment return.

Now, those are nice statements for me to put on the bottom of the page. Let me prove them up for you on the next several pages.

If you turn to page 12, this is a style consistency chart, you know. And it shows where we've been positioned slightly over 18 years. We've been managing this portfolio slightly over 18 years. What I always say about our portfolio is, you can draw a nice circle around us and the Russell 2000, and we will always be within that circle. Sometimes a little bit on the value side, sometimes on the growth side depending on where our research is taking us, but never far enough to be something not supposed to be. Never a small value fund when that is involved. Never a mid cap growth fund when that's

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involved. We recognize that when you hire us to be a small-cap cor manager, that's what you expect us to be. You can have a high comfort level, we will always be in that small-cap core space.

The team is on the bottom of the page. The page is on 13. First thing I always say, I apologize for using my high school picture in there. And I also then say right after that, that Mike Morris is not related to Frank Morris. So just FYI, there is no nepotism.

The three things I can say really about the team are, a lot of experience. Twenty-nine years in the business, seventeen with the firm. Why is that important? Well, we've all seen business cycles. We've all seen more than one business cycle. We've grown up following the sectors that are listed underneath our names. And in many cases, our very well known within those sectors and by those companies. And that gets to us see the right people, to ask the right questions, to ascertain whether a particular equity is a good investment for our portfolio.

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Second thing is, that we are structured. We are owners of the process. And so Macquarie is structured in a multi-group fashion. We run our business and manage our P&L. That's important to you from the standpoint of we control our resources. We travel where we need to go to generate output for this portfolio.

No offense to Shawn, but when we run a research trip, we don't have to run it up the flag pole and say, Shawn, can we go here. We merely justify it to ourselves. And what we say to ourselves is simply, go to the meeting, come back to our investment meetings and tell us what you learned, who you saw and why it was important to the portfolio, and are there any actions that we need to take as a result of that meeting. So, a good part of our alpha is generated but us controlling our own resources.

Finally, we are aligned with you. And so by design, we are all invested in the portfolio. So, we are invested in a variety of ways. Either through a direct investment in the mutual fund, the portfolio is also in the firms 401(k) lineup. And then a portion of our

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incentive compensation is deferred. And is deferred into our own portfolio. We are firm believers in eating our own cooking. I don't ask anybody on the team how they invested time and money. But it's safe to say they told me, we are all invested in all three trenches here. So, a significant portion of our net worth is invested in the success of this strategy. We want it to be most closely aligned with those that are invested with us.

So, experienced owners and aligned with our investors.

On page 14 and 15 shows you a little bit about our returns and the consistency of our returns. And so on page 14, you will see this is rolling one year quarterlies. And measured this way, we have outperformed 83 percent of the time. We are very consistent in how we generate our returns. That roles up to what you see on the bottom of the page, the classic chart that you see that we have nice upside capture, really good downside protection for what's been an 18-plus year close to 11 percent annualized return, 260 basis points better than that of the

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index. This is attribute to the research we conduct, the construction of the portfolio, and the adherence risk within the portfolio that has allowed us to generate these type of returns you see on this page.

And then finally, the hallmark of what we do is on page 16 and 17. Here we show you our risk adjustment returns. We show you since inception to drive home the point that no one period is driving these returns. This is what we come in every day to do. Pick good stocks, generate really good alpha for our clients. Do it while taking a lot lower risk than on our peers. For what is purely information ratio and one which approaches one over a longer period of time. This is the hallmark of what is behind everything that we are doing with respect to the small-cap core portfolio.

Now, a little bit about our process. Can I take you to page 21 right behind Tab 3. This is a 30,000 overview of our process. We start the morning, every morning, with a screen of the Russell 2000. And we are screening for three criterias: Valuation, expectation with





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Russell growth and quality. Statistical quality on how management has invested capital in the business. Think of this upfront screen as identifying good companies with good business models that are relatively inexpensive. This helps us take 2000 stock universe and get it down to 750 names for us then to do step two, fundamental research.

And on the fundamental research, what the five of us are doing is we are actively analyzing the company's balance sheet, cash flow, earning stream. We are actively seeing the company's to important part of what we do is to see the companies that we are invested in. And to that end, I always say by virtue of the firm's asset size, 250 billion we get a seat at the table. By virtue of our experience level, we have a seat at the table. By virtue of managing our business, we get a seat at the table.

And those meetings are important. They are important to the management because they get to tell their stories to us. We are asking them about, tell us your business stream. Let's talk

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about what you see for the future of your business and your sector. Let's talk about your corporate governance structure. And let's make sure that we are in alignment as to how you are managing your business, so that's the best possible investment for you and our portfolio. And then finally, we are all about asking ourselves what is the catalyst that we value shares of higher fundamentally. We are fortunate again. Small-cap investing, no short catalyst.

One and two for us are about research. Three is about portfolio construction. On the portfolio construction side, we are all about is allowing our stock selection to drop to the bottom line. What I always say is, we are not wild, crazy, sexy, overweight, underweight with respect to sectors. In fact, we are plus or minus 2 percent around sectors. What we have been able to demonstrate over time is that you can generate nice alpha for your clients by just picking good stocks. And what we do not want to have happen is a misplaced sector call deluding our good stock selection.

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Think of energy right now. The price of crude is corrected sharply, the equities are corrected sharply. If you have a massively overweight energy, you would have significantly underperformed and put your client in front of that. It's not to say we won't underperform in that sector, which is incumbent upon us to pick the best stocks in that area. But we are not so overweight that we lose total control of performance of the portfolio.

So, we are plus or minus 2 not wanting a huge stock collection. We do the exact same thing on factor analysis to make sure that you get a broad distribution of small-cap investment. This is end-to-end small-cap investment. Lowest market caps in Russell 2000, highest market caps. Lowest beta, highest beta. That's important from and the standpoint of, you know, market rapidly rotates. You will have positions within each one of those particular segments of the market. My worst client meeting is always to come in and say -- my worst client to come in and say, hey, we were naked one segment. That would have meant we didn't do our

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risk adherence right. And so, we benefit from being broadly diversified.

Finally, how do we sell stocks? We sell stocks like everybody else. We had success. We pat ourselves on the back. We do a little dance. We can't raise the price target, time to move on. I also give the team extremely high marks when we sell a name, when the thesis breaks down. You are never right a hundred percent of the time. If we are right a hundred percent of the time, we would own a island and we'd retire. You can save your clients a lot of underperformance by exiting when the thesis is different, when it's changed.

We are always fully invested. Cash is less than 5 percent at all times. It's a better opportunities portfolio. And finally, we are true small-cap portfolio. What I mean by that is, if a name grows up and graduates to become a large cap name, we will exit that name out of the portfolio and start the process all over again. What I always say is, you won't see Apple in our portfolio saying it still has value offset by give the other small-cap technology companies who maintain our small-cap stripes. This is true small-cap, true broad-based, small-cap investment.

That's a 30,000 foot overview. The proof is always in the pudding. If I can take you back to page 18 you'll see the performance numbers. And what you will see in the performance numbers, which I always say, blue bars are higher than the gray bars, and that's good for us and it's good for our clients. We've been very consistent in that regard in terms of generating alpha for our clients over a number of years.

As you can see here, a quick thought about what's transpired here in the most recent correction. True to what I told you earlier about preserving capital on the downside, we have widened this gap between us and the Russell 2000. And so the market as corrected, you know, at the time we were 135 basis points ahead of the index. We are now 165 basis points ahead of the index. We have widened the gap by preserving capital on the downside.

Those returns, as I said, come from



stock selection. And that should be everything we talk about, stock selection driving our return.

So, let me stop there and sum up by saying good philosophy, very strong philosophy, really strong people, very transparent process that's been able to generate really good returns while taking a lot lower risk. Okay. We are going to stop there and pass it over to Skip. But before Skip goes, I want to thank you for your time. And say that, we really -- would be an honor for us to manage this portion of your assets. And so, pleased that you brought us in to talk to you today.

Skip.

MR. CORKRAN: That's the bulk of our presentation. I just want to close by saying that the three things that make us feel really good about Frank's team are hear on page 19. And that is the experience that this team has under its hood, been consistent results they produce in both up and down markets. And the fact they are part of the Macquarie team and Macquarie is different in that we are highly



committed to the city. And we want to give you access to all of our resources and not just small-cap core. Thanks again.

MR. MORRIS: First and foremost, small-cap core.

MR. DiFUSCO: I have questions.

Rasheia had mentioned you guys are -- you folks are doing some business with her office in terms of managing some short-duration assets. Over time, there has been some limited discussion with the Muni plan and you mentioned infrastructure earlier. As it relates to your fee proposal, how open are you treating, you know, money whether it's from the Treasurer's Office, whether it's from the City Pension Fund, whether from this fund as not commingling it but in terms of fee rates or free proposal considering that's all City money? We have had other managers do that back at break points and things faster.

And so, I am wondering if you folks are open to those sorts of discussion?

MR. LYTLE: We are still under contract terms in the Treasurer's Office, and trying to



determine that. Happy to have an open discussion about how we can think about this as a broad kind of City-driven mandate.

MR. DiFUSCO: Yeah.

MR. LYTLE: And what that means.

MR. DiFUSCO: Yeah.

MR. LYTLE: Between the different strategies. From my standpoint, we see this as managing -- having a relationship with the City. We have to figure that out between fixed income side versus the equity side. We can do that.

MR. DiFUSCO: Thank you.

MR. LYTLE: Sure.

CHAIRMAN SCOTT: Thank you.

MS. JOHNSON: Thank you.

(Macquarie presentation ends.)

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(Matarin Capital Reps brought in.)

MR. DiFUSCO: Thank you for coming in. We appreciate it. You have met everyone. The three Commissioners are your primary audience today along with PFM and myself. If you can take about 20, 25 minutes, I will kind of give you the five-minute warning. Really talk about





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the process, the strategy, how you can add outlook to the portfolio. And we will definitely have questions for you along the way.

Thank you again for coming in.

MS. COTTON: I'm Marta Cotton. Good morning. Principal at Matarin. I'm Director of Client Development. And joining me Nili Gilbert, one of our partners who is Matarin cofounder. Nili is one of Matarin's cofounders and portfolio managers, as well. And nice to have a sunny day in Philadelphia. I always enjoy coming back here. My husband was born here. And in fact my mother-in-law, I don't know if I can point the right direction, she was born and raised 18th between Walnut and Chestnut. And she used to tell me stories about roller skating in Rittenhouse Square, I remember. So, it's nice to be here.

And about Matarin, we are an eight-year-old firm. We have an investment team that's also worked together for a number of years even before starting Matarin.

If you turn to page 2 in the book, looks like some of you got there already, you can see



a picture of our team. We are a hundred percent employee-owned firm, a through investment boutique, as well. Five of us are equity owners. So, ownership is already broad, and we intend to broaden it further over time. And as you can see today and in the photo, we are a diverse firm and we are a certified women-owned firm.

We also believe in diversity broadly. We believe in it in race and in gender, but also diversity in thought, diversity in opinion. And we actually think that all that diversity together is what helps make us good investors.

We all came from large firms. People often ask us, why would you leave such firms, you know, to start a firm like Matarin or join a firm like Matarin from scratch. In hindsight, it was probably a risky thing for so many of us to do. But the fact is that we all really wanted to work at a firm that we could really be proud of and get excited to wake up every day and represent and that truly put its clients interest first above the firm's own interest. And large firms, as you know, they can be a bit



siloed. There is no one group that is responsible for the entire client's investment experience. And we felt it important to be able to manage all those elements of a client's investment experience and make sure that we are not going to be a firm that's focused on its own pocketbook ahead of the interest of pensioners who put their trust in a firm. And we really wanted Matarin to be different in that fashion.

We have some core tenets or principles at Matarin. We will only offer strategies that can deliver a value for clients net of fees. We will close stratagems, this is really important, and add levels before transaction costs erode or turns our client. It's very important to us. We won't use soft dollars because that tends to lead clients to pay more.

These elements are driving principles for us. We are very proud at Matarin that we really believe we have got a firm that we built over those almost eight years now that have succeeded in putting its client's interest first.

If you flip over to page 3, see a little



bit in a picture about the kind of growth trajectory we have. We started Matarin with our own capital. And we seed its strategies with our own money. In fact, this small-cap strategy was started in January of 2011 with just one and a half million dollars from the IRA of Valerie Malter, our managing principal. And by the way, the first time we ever submitted an RFP to the City of Philadelphia, which was back in 2013, we had firm assets of 160 million. At Matarin, every year since inception, we've grown our assets and our clients each year over the year before, and we are proud of that. And in less than eight years, as of the end of this third quarter that just ended, we have firm assets of $1.6 billion from that standing start of $1.5 million just from Valerie almost eight years ago.

And the strategy we are talking about today, the small-cap strategy has most of those assets, 1.3 billion and 24 institutional investments from clients, client accounts. And our whole firm has about 32 institutional clients in total. Most of them are in the





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strategy. And if we think about the makeup of the client base that we have, we are very proud we have a number of public plans as clients. In fact, four of the five largest clients in our strategy are large state public plans. And we also have a number of city and county plans, as well. So, we know what it's like to work with clients similar to you. We know the kind of environment, the transparency under which you operate, the risk you take in hiring managers, it's something we are very familiar with.

Our primary goal is to deliver above benchmark risk adjusted returns. And we don't want to be the kind of manager you see with these high highs and these low lows that make the client experience really painful. So, we are quite focused on risk controls so we can deliver the highest possible level of returns while still managing the risk appropriately.

If you flip forward to page 14 and 15, share a little bit with you about the kind of performance we have had since inception. And also, the performance relative to the almost 600 strategies in the whole Evestment small-cap

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universe, which is on the following page. We are pleased we have done quite well for our clients in the time we have been managing the strategy. In the seven and three-quarter years since inception, we outperformed the Russell 2000 index by an annualized 2.1 percent. And that strong excess return performance ranks in the top 22 percent. You can see some of those rankings on the bar chart on the next page. That means, we beat 78 percent of other small-cap managers in delivering excess returns over that time period since inception. But really importantly, our risk adjusted returns are worth mention.

We rank in the top 14 percent for information ratio. That is important risk adjusted returns. Which means we outperformed 80 percent of those other managers. We are doing a good job in meeting investment objectives for our clients. But I mentioned risk controls and trying to keep those lows from reading too low. You can see in the measure of downside capture, that we outperformed in down markets. So there importantly, we rank in the

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top 17 percent of all those 600 small-cap strategies, beating 83 percent of them.

But I'd be remiss if I didn't mention our most recent performance. You can see it has not been as strong as the full since inception seven and three-quarter year's track record. And we all know that all managers have periods of outperformance and periods of underperformance. And we happen to have experienced the latter more recently since the first quarter of last year, but that follows a period of five years where we had really strong outperformance. So actually, we think it could be a really interesting and good time to potentially invest with Matarin. The environments that have given us the headwinds since last year, these our environments that do tend to revert.

And we happen to have some new clients that think so, too. Some investors have recently given us some new mandates, which is very exciting even following the period of underperformance. Giving us their vote of confidence. Three new clients just in the last

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few months. One of those is 125 million-dollar mandate from LACERA, which is the $56 billion Los Angeles County Employees Require Association. That was quite gratifying, as well.

I will turn it over to Nili to share with you a little bit more about our team's background, how we manage portfolios and to put that performance into context.

MS. GILBERT: Hi, everyone. As Marta said, I'm a cofounder and portfolio manager of Matarin. It's great to be here with you today. Actually, the last time I was in Philly, I was with our clients at the labor union in Norristown just outside of the city. The local union is a small-cap client of ours. And I had a chance to go out and volunteer with their union members for the day and their community. Marta mentioned how important our clients are to us. And for us, that means remembering the end beneficiaries of our work whether it's union members, city workers in addition to the trustees and investment team members that we have the chance to engage with.

In any case, the origins of our investment process at Matarin actually go all the way back to 1980 at a firm called Chancellor Capital Management, which was even before that Citi Bank Asset Management. It's fund out of Citibank. Part of why we believe in Matarin's investment philosophy so strongly is because it's actually been adding value for institutional clients like yourselves for over -- almost 40 years now.

My cofounder and fellow portfolio managers Stuart Kaye joined that group in 1994. And he was in the chief investment officer role when he recruited me out of Columbia business school in 2003 to join his team, and recruited our fellow portfolio manager Ralph in 1999. Sos, we have been working together managing strategies similar to these for a very long time. As a matter of fact, our group at Chancellor, was ultimately inquired by Investo, was managing over $25 billion in assets at the time that we all spun out to fund Matarin. It was in 2010 when Stuart, our cofounder Valerie and I started up the firm.



Our experience of working for very large firms as Marta mentioned over time just gave us the feeling that we could do better for our clients at the end of the day. We had all been portfolio managers. And we were proud of the alpha, the returns that we were able to generate for our clients. But we just felt like there is so much more that matters for your well being than just the returns. So, Marta mentioned the type of policies that we have put in place to be able to ensure and strengthen those outcomes.

So with that, let me just move into a discussion of our investment philosophy and process which, as I mentioned, does draw on several decades of work. I am turning to page 4 in the book which describes our philosophy at a high level.

Matarin's investment philosophy about why we believe we can beat the markets as active managers at all is essentially that we see the stock markets as being inefficient in the intermediate term. Actually, the thing that we believe creates most of these inefficiencies is investor's emotions. When you see things like



fear come into the market, for example, lately or greed, sometimes investors egos come into play or things happen that just cause them to forget to stick to their knitting. When those things start to happen, you can see stock prices move pretty far away from what we would call their long term fair value.

And so, what we do is we first start with ideas that we hope are insightful and creative about what will drive the stock's fair values over to long run. And then we find ways to quantity those insights so that we can implement them in the stock market systematically. And what being systematic means, is that we are able to get our own emotions and biases out of the way when we are making these investment decisions so that when the emotional dislocations happen, that we are able to take the other side of those trades.

In fact, oftentimes we will be making investment decisions that other investors might find uncomfortable. So, we say we tend to be contrarian in our style of investing at times. We actually believe that it's kind of hard to



get paid in the markets for making the most comfortable decisions. If it's something that is really obvious or, you know, really easy to do, it's probably already reflected in the price. Other investors have already made the comfortable decisions. It's hard to get paid for them.

What this has meant for our clients' portfolios over time is that we tend to offer a differentiated pattern of returns, especially at emotional turning points in the markets. I always like it when Marta says that our performance tends to zig when others zag. That is really by design.

If you move forward two slides to page 6, here you will see a description of the types of stocks we like to buy and hold in our portfolio. In a nutshell, we want to be buying good businesses that are trading at inexpensive valuations or prices with shareholder friendly leadership, that's our people concept. And then finally, we want to see evidence of some short-term catalyst for outperformance.

On the other hand, if a stock's business

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starts to deteriorate or if its price gets more and more expensive as we are holding it, or if the leadership starts making poor business decisions or the short-term catalyst breakdown, that is when we would make a decision to sell a stock out of the portfolio that we have been holding.

Since inception, all four of these concepts have added value for our clients' portfolios as we would hope. And another thing that's interesting about the way that we think about this design, is that all four of the concepts don't always do well at the same time. We are hoping if it's an environment that, say, very good for business, that maybe there is another concept that's less favor. But there is always something in the portfolio helping to support returns.

So for example, in the more recent period 2017 and 2018, until this recent market turn, one thing that we have seen is that very high momentum stocks, think of your high flying tech stocks or biotech stocks, have been very well rewarded. And so, our catalyst concept

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that focuses on the shorter term drivers of performance has been the strongest performer in the portfolio. But on the other hand, the market has not been focusing on whether stocks are trading at very high prices. So, expensive stocks have also been very well rewarded. And so, the price concept that focuses on valuation has underperformed. And it's actually that price concept that describes the negative performance that you have seen in the portfolio during those two years.

So, I also wanted to say about the process, that it's really not one size fits all. When it comes to individual names, we're really thinking about what makes different types of stocks trade differently. We wouldn't want to forecast the price of a biotech stock that's more speculative, thinking about its future product its future business the same way we want to forecast the price of a local utility.

For biotech stocks, it's actually the price momentum that matters more and the current business fundamentals that matter less. Whereas, for utilities, the current business

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fundamentals matter a lot.

MR. DiFUSCO: Can I ask a quick question on the valuations piece you mentioned?

MS. GILBERT: Yes.

MR. DiFUSCO: You talk about valuation, looking for inexpensive. Are you talking about compared to historical norms or compared to the environment you are in where, hypothetically say, everything in quotes is overvalued. And so, you are looking for something cheaper relative to what is going on at the moment. Are you looking more at something cheaper relative to historical norms?

MS. GILBERT: We are looking for stocks that are cheap relative to their peers currently. And when we think about valuation, we really want to get a robust picture of how stocks are being valued. So, we are looking at how it's valued relative to peers in its subindustry, relative to peers in its sector, and then relative to the entire investable universe for small-caps. This gives us a pretty clear picture of the current valuation.

When we think about valuation over time,

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we also do look at whether how value has been performing recently. Because if you are in an environment where currently, as I was saying, expensive stocks have just been getting more and more and more expensive, there comes a time when that is going to stop. And it's actually attractive to focus on valuation a lot more in your process. But when we do that, we want to adjust the amount of emphasis that we are putting on valuation for all of the stocks in the portfolio at once.

MR. DiFUSCO: Thank you.

MS. GILBERT: We'll just pause to see if there are any other questions before I move off of the discussion of how we pick stocks?

So in that case, I would like to talk about how we put it all together. Moving to slide nine, which is appropriately entitled "Putting It All Together."

Once we have got returns forecast for every stock in our investable universe and because of how we systemized our thinking, we are actually able to come up with fresh forecast for every stock, over 1800 small-caps stocks every single day. So once we have got these return forecasts, our portfolio construction process wants to combine information about the expected returns along with information about the risks of the stocks, along with information about how much it's going to cost to actually trade. As Marta mentioned, risk management is a very important part of our process.

Essentially, the way that we think about it is in terms of what we call risk budget. What we want to do when we are taking risk relative to our benchmark, is to spend our risk budget in the area where we think we have the most skill. And for us, that is picking stocks. So what that means is that we don't want to spend our risk budget on taking big bets in sectors as compared to the benchmark or big bets about macroeconomic risks, like, we wouldn't want to have a portfolio that has a lot of interest rate sensitivity as compared to your benchmark or oil price sensitivity. What we really want to do is create a process that allows us to focus just on our pure stock picking ability alone.



And then the third part, the transaction cost forecasts are really important especially in the small-cap space. Believe it or not, we have seen some situations where managers have spent 2 to 3 percent per year on trading costs alone, and that comes directly out of the returns that you are able to use to pay benefits. So, we forecast how much is going to cost to trade every stock, and won't make a trade if the expected cost of the trade is more than the expected return that we think we can pick up from doing the trade.

We put all of these elements together into what we call an optimizer, which is basically just you can think of it, I do, as a really big calculator that helps us to solve for all of these problems at once. Even though we love math at Matarin, it's more than we would be able to keep track of in our heads. And at the end of the day, what this results in is a portfolio that tends to have about 170 stocks on average, and is very diversified by sector.

This process, as we said, has led to returns for our investors since inception. And



hopefully, also going forward.

Any questions about the putting it all together piece or anything else that I said about the investment process?

If not, I will pass it on to Marta to conclude.

MS. COTTON: Hopefully, we have been able to share with you a little bit about how this process comes together. It's this blend of fundamental and quantitative. We think of it as the best of both worlds, actually. It's how do you take that best fundamental thinking that we have, and we just happen to use these rigorous and systematic tools to express the best and fundamental thinking. And our edge is the way in which we are able to put those together successfully.

You have heard about the common sense risk controls that we have that let's us focus on the area that is our greatest area of skill, which is that stock selection. The process is disciplined. It's repeatable. It's added significant value for clients. We believe in putting our clients interests first. We believe



in fair and client-friendly fees. And again, closing the strategy at an appropriate level that's in the best interest of our clients, something we feel extremely strongly about.

And we are actually not that far away, as it turns out in terms of small-cap at this point in time. So, our incentives are firmly aligned with yours, as well. We believe in, you know, eating our own cooking. And if you put your trust in us, we will work very hard for you. You will really get a true long-term partner. And we commit to coming back whenever you would like us to, to talk about the portfolio.

We commit to open clear transparent communication as well with PFM. And we would really be honored to work in service of PGW and the City if you would select us.

MR. DiFUSCO: I just had one additional question. Commissioners may, as well. Did -- you mentioned that the bulk of your assets are in this strategy. I least one of you or both said about 1.3 or 1.6.

MS. COTTON: Correct.

MR. DiFUSCO: Do you consider that firm risk or is there a concern about, you know, if there is an issue with this particular strategy, it causes stress on the entire firm? Are you looking to, you know, expand capital in other strategies?

If I'm not phrasing it right, hopefully you --

MS. COTTON: I know what you mean. Sure, Chris. So briefly, the other strategies just so you know what they are, we have a U.S. large-cap strategy. That is actually done exceptionally well versus a thousand strategies out there. It's in the fifth percentile for those risk adjusted returns that I mentioned. And so, obviously, large cap has had some headwinds. But we still are optimistic in growing assets in that strategy.

We also have a micro cap strategy which is very new, actually, which has seen new investments in it just in the last few months. We want to be prudent and thoughtful about the kind of strategies that we do offer. We have been approached, actually, to begin some very



strategies that we chose not to do because we didn't think we could deliver them in the best way for our clients. We talk all the time about other strategies. We are working on some other ideas potentially. It is something we will always approach in a really thoughtful way.

MR. DiFUSCO: Thank you.

MS. COTTON: Just to add to your question in terms of how we think about it in terms of business risk. It's something we do talk about. The way that we think about the business risk, is we want to be able to manage volatility whether in the markets or possibly, hopefully, not in clients while keeping the -- being able to always cover the firm's costs.

When it comes to business risks, one of the things that you see too often is that firms kind of scale up their costs as they grow and the markets are rising or when their strategy is in favor. And then when things go out of favor, it's hard to continue to cover those costs. And so, we have been so diligent in thinking about how we manage our financing ever since we founded the firm. I think it's also a byproduct



of being 100 percent management owned. We are not spending somebody else's money. And so, that -- from a business perspective, that's how we think about being able to stick it out for the long run.

You may also be interested to hear that when we founded the firm, we set a commitment to hopefully build an entity that can last even beyond its founder. We are thinking a great deal about longevity at Matarin.

MR. AMMATURO: How much of that 1.6 billion is with emerging manager programs as opposed to directly plan sponsored?

MS. COTTON: So, we feel very fortunate to have a number of accounts, especially early on, to come from those emerging manager programs. We always say we really wouldn't be here without them. They are very important. Who is going to give you money at the 18-month mark when you really don't have any. But in addition to having grown with the benefit of those programs, then as our track record got long enough and our assets grew, we started meeting the criteria for various RFPs and being



invited to finals and then winning some along the way.

Eight of our last ten clients, new clients, have been direct mandates such that the overall split from the firm has really moved, frankly, in a nice way for a firm like ours to have in its life cycle development. That split now is 70/30. Seventy percent is direct and 30 percent from those emerging manager programs.

MR. AMMATURO: Thanks.

CHAIRMAN SCOTT: Thank you.

MS. JOHNSON: Thank you.

(Matarin Firm presentation concludes.)

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MR. GOLDSMITH: Well, you know, looking at all that, I think there was some questions in between Macquarie and Matarin. There was some discussions about ownership I overhead a little bit. You know, in looking at the data, performance data we have in front of us, what we just heard from all three managers and the fee proposals they are in, I find it hard to make a case against Copeland, especially you know, if we are going down the road of, you know, one





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manager, one index.

You know, I think they -- we look at firm characteristics, employee owned. And more so than that, every member of the investment team is an owner even, you know, their quant analyst who is graduate from college in 2014. I assume that some element of his compensation is being awarded equity in the firm. The nature of their, I guess -- the philosophy is reflected in the nature of their performance in that they have exhibited not just in what they showed here, but in the book. If you flip ahead to this page -- I don't think it's a page number on it, but it's labeled Historical Statistics.

You know, it covers -- it features a number of metrics that are all over their books. Here is nice place where you can look at it all at once. There is number of applicable statistics on here.

MR. DiFUSCO: It's behind the PFM memo. The last page or two of the --

MR. GOLDSMITH: Right. Before the Copeland -- start of the Copeland book. This is all -- these are the composites of all the



managers over the same period. You know, all ending September 30. You know, some similarities. Think all managers probably noted this, the last year and a half or last seven quarters leading up to this point were not the best environment for the types of strategies they were running. You know that being said, you know, across all the periods here and flips on the ten years, well -- Copeland hasn't been around for ten years, neither has Matarin.

But you know, downmarket capture, the fourth column from the right. Copeland is very consistently far below the other managers. It tends to lag in the upmarket. All these things, again, pair very closely with what they said in their presentation. Alongside that, I think they got the lowest correlations with the benchmark. And the source of their -- if you look over the alpha, it's non-benchmark positions that are driving, you know, their return. Not non-benchmark, but excess, you know, alpha well above the other two managers.

At the same time, I think interesting to note that their standard deviation is if not



always frequently, the lowest across all periods. You know, these are things that point to, I want to say, defensively minded but also able to find that alpha in the small-cap universe. I think that flushes with our philosophy when it comes to total portfolio construction. At the same time, they run the most concentrated strategy within the lowest turnover. You know, 40 holdings or so. You know, 30 to 40 to 50 holdings at any various times. That type of strategy would pair well with an index. You have got your broad benchmark exposure, then a much more concentrated portfolio.

So again -- and then lastly, I will add in the fees were significantly lower. I mean, they are starting with the 20-plus basis point head start.

CHAIRMAN SCOTT: So, their dividend growth philosophy, is that unique?

MR. GOLDSMITH: Within these three managers, I would say it certainly is. I don't think it's unique to the overall universe of investment managers. I don't want to call it a



sub-bucket like value or growth. I would call it a philosophy that some managers have, you know, chosen to make their prevailing strategy. You know, we at PFM have utilized discretionary accounts, dividend growth managers in the large cap space. I think that's typically where it's most prevalent. It's not entirely unique in the small-cap space.

I think it requires, just like any management small-cap or large-cap, it requires more work to do. There are more names to cover. They alluded to that in their presentation with the numbers.

MR. AMMATURO: I think that's right. I think you see much more large-cap dividend paying managers out there. You would think a smaller size company needs to reinvest back in the business to make the business sustainable where it can grow and to be a mid-cap company, et cetera.

I wouldn't say it's 100 percent unique. But you want to see more dividend, high dividend stretch in the large-cap space than small-cap.

CHAIRMAN SCOTT: The concept, I think,





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Copeland was also employee owned; is that correct?

MR. GOLDSMITH: Yeah.

CHAIRMAN SCOTT: How do you evaluate the risk of that type of ownership versus that -- the larger firm we interview?

MR. GOLDSMITH: I think the risk to employee-owned firms, you know, broadly speaking, could be key man risk where one person owns the majority of the equity or the process is overly rely on that one person. We don't have those issues with either of these employee-owned firms.

You know, the bigger risk I think would be that of acquisition, which is not always a negative risk necessarily. But things can change. We heard, I think, Matarin talk about, you know, I think they all sort of moved away from those types of firms to specifically run the strategy and run the firm they way that they wanted to. I don't want to say the would go and sell to a large financial conglomerate. But you know, the performance is strong. Anything can happen in the investment management phase.



A change to culture could occur in that instance. Again, this is purely hypothetical. These are things that just my happen.

MR. AMMATURO: It's a net positive. We look for employee-owned firms. We look for portfolio managers, employee management ownership take in the firm. Interests are aligned with your interests. And that's one of the things we look for.

MR. GOLDSMITH: You know, on the flipside, Macquarie, they are certainly performance-based salary compensation schedule, you heard them. They also -- when -- we have our own P&L for just this strategy. That is a little interesting to hear. You don't always hear that with the large firms.

I think they take -- his success in Macquarie is relying on the profitability of that strategy. One that comes from performance but also, you know, keeping expenses I think. I thought it was interesting. But certainly, that's an Australian-owned large, large firm in the long run.

CHAIRMAN SCOTT: Understood what you



said --

MS. JOHNSON: I was just looking at for those small-cap space, had three firms here today at three varying sizes. And I guess from your -- I just want to hear from your perspective kind of the -- not saying which one of these firms you think, but kind of just upsides do you need a large Delaware Macquarie firm to be successful in this space? Or do, you know -- or a Copeland which is very different from Matarin firm.

So, just kind of want to get your perspective of that because these are three various sizes of firms.

CHAIRMAN SCOTT: Let me ask.

MR. AMMATURO: That's a good question.

CHAIRMAN SCOTT: One was 1.3 billion, another was 3 billion and another one was what, 150?

MR. GOLDSMITH: So 1.6, 3 and several hundreds.

MS. JOHNSON: When it comes to equities probably --

MR. GOLDSMITH: 90 billion maybe in



equities Macquarie.

MR. DiFUSCO: Yeah, that's right.

MR. AMMATURO: I think there's been proof statements out there that the emerging firms have been able to outperform the mainstream managers. That's not across the board, obviously. But there is proof statements out there that small boutiques have been able to add incremental return.

I don't think you're dealing with emerging firms here that are like 500 million, 600 million that are really business risk. I don't think PGW is entering down the roads of business risk by investing with one of these boutiques. I think especially Copeland is past that hurdle of $3 million.

So, you -- I don't think you can really go wrong. Because I think either shop in terms of the first two managers, to your point Rasheia, can't get much different. You are going from a boutique lean organization to a top hundred global manager. So at the end of the day, the performance is right on top of each other.





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MS. JOHNSON: Right. Their returns each year over year.

MR. AMMATURO: Is fairly consistent. It's more your appetite for that boutique lean organization or the multinational top 50 asset manager. Kind of what are you more comfortable with as a commission. We at PFM favor the boutique that is employee-owned that has skin in the game. But we presented all these firms because we are comfortable with all of them.

MS. JOHNSON: Fair enough.

MR. WHITE: Boutique sells 55 significantly cheaper fee.

MR. DiFUSCO: Right.

MR. GOLDSMITH: What's shown here, take away 20 basis points from the other two. These are growths.

MR. AMMATURO: That's a good point. If they are right on top of each other, that means Copeland outperformed by 25 basis points.

MR. GOLDSMITH: Like 57 I think.

MR. DiFUSCO: Yeah. I approximated because it depends on the exact break.

CHAIRMAN SCOTT: So, the firm that --

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the City of Philadelphia is looking at one of these firms or has a relationship with one of them?

MS. JOHNSON: We are contracting with Delaware Investments, Macquarie or whatever they are calling themselves.

CHAIRMAN SCOTT: The question that Christopher asked relative to the competitiveness of their fees, is it -- that's still in the discussion phase in terms of their fee structure? Or is that etched?

MS. JOHNSON: Our fee structure with them is etched. And either they're going to sign it or they are not. Everything is negotiable.

MR. DiFUSCO: I like how you negotiate. Sign it or leave.

MS. JOHNSON: We gave them best and final, and then I followed up. Because on our investment manager side, we had very small edge. We had about $3 billion in assets for the City that we have with managers. Again, very short term. But I think we had about five active managers. And we had no -- we wanted to do

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something differently. So, we went up for RFP. And we retained most if not all of our managers, but then added additional four or five. Everyone is not going to get money from the offset, but we negotiated with them.

They came up with their best and final offer. We'd like to contract with you, but can you move here, there. They agreed. Now it's with the Law Department and their compliance and kind of going back and forth. But the fees are solid.

CHAIRMAN SCOTT: Okay. Copeland relative to their diversity philosophy, how -- I can't recall.

MR. GOLDSMITH: Here are the numbers. I don't know if there was an explicit diversity philosophy. We talking diversity of employees or diversification --

CHAIRMAN SCOTT: Yeah, employees.

MS. JOHNSON: Employees.

MR. DiFUSCO: A quarter of investment professionals are minority, 18 percent of the executives in C-suite positions are female or minority. And employees as a whole, 22 percent

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each female minority, 11 percent ownership by female minority. Numbers, I would say, slightly higher depending on how you would break it down for Delaware. Although, I don't know if it's leaps and bounds of -- and then Matarin, obviously, is smaller. Shop only total employees. But over half women. And of the five women, two are Hispanic, one is African-American. The Hispanic women are both considered executive or C-Suite. Then African-American you know, is pretty much running strategy on the investment team.

CHAIRMAN SCOTT: PFM, you guys are recommending Copeland?

MR. GOLDSMITH: I think, like I we said, we came in today with -- standing behind all these managers. When you look at purely -- you heard the stories of philosophies. You know, regardless of whether you favor one or the other, assuming you stand behind all of those roughly equally, you look at historical performance in certain market periods.

I think Copeland stands out just based on purity to some extent. Even you can see that





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all managers performed generally well. I think when you apply the fees, it makes it a clear decisions -- well, a clearer decision I would say.
MR. AMMATURO: Macquarie, they would be willing to talk fees with you, did they not Chris at the end? You asked point blank. Said, we are willing to talk. Not sure how much wiggle room there is.
MR. DiFUSCO: Yeah. They would -- I guess my -- would they come down 30 basis points maybe, I think that's unlikely. We were talking 10 basis points maybe, I think they would talk. I don't know that I, based on my experience in past negotiations, not with them but with other firms, they don't come down.
MR. GOLDSMITH: I think Copeland had lower fees, I think from the start, as well, even what was proposed in RFP. Their business model or whatever they are willing to have, and their margins in general I think are lower.
MR. AMMATURO: That's the benefit of being a smaller employee-owned shop. There is more infrastructure, more red tape obviously at

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Macquarie relative to Copeland.
CHAIRMAN SCOTT: Yes. Is the committee -- I mean, Commissioners are you guys ready to vote?
Does anyone want to make a recommendation? I know I am prepared to make one.
MR. WHITE: Based on fees.
CHAIRMAN SCOTT: It look likes we are leaning in the direction of Copeland.
Is there a motion?
MR. WHITE: Motion to recommend or to the recommendation of Copeland.
MS. JOHNSON: Second.
CHAIRMAN SCOTT: Motion has been made and properly seconded that we go with Copeland.
All those in favor?
(Ayes.)
CHAIRMAN SCOTT: Ayes have it.
Now, one other thing that we need to do here.
MR. DiFUSCO: Well, Marc, will briefly cover the investment performance and then we have one other brief item.

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MR. AMMATURO: I'll be very brief. It's 2.1 of the page. It's labeled September 30, 2018 Total Fund Market Value, 550,636,304. Again, this is as of September 30. We all know, again, market sold off posts September 30. But through the first nine months in the calendar year, your portfolio was performing very well. On absolute basis, up 4.73 and on a relative basis. If you look at it verse the benchmark, benchmark is only 3.52.
What is driving that? Outperformance on a relative basis is two things. One, they are overweight to equity markets. And again, through the first nine months of the year, the equity markets are very strong. And you will see active managers have really done well in this portfolio. You have two things kind of adding to your incremental return over the benchmark.
Within large-cap, a lot of the assets are indexed, if you look at Rhumbline and Northern Trust, that is really 3 percent of your assets. So 33 out of 40 -- I'm sorry, 28 out of 40 is passively managed. And then you have

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PineBridge, a recent addition at the end of last year.
PineBridge just got started in November of last year. If you look all the way to the far right, and they are up 11 percent in this calendar year, slightly outperforming. That's 10 percent of your assets. Good start by PineBridge.
On the small-cap side, this is where we spent our morning discussing who is going to potentially replace Vaughan Nelson and Eagle. If you look at the compositive level, combined small-cap year to date column, 14.8 vs 11.5. Good outperformance for your active managers of small-cap this calendar year.
On the international side, again, I wouldn't focus on the year-to-date column and the combined equity. Negative 1.8 verse a negative 3. So international has not been the place to be this calendar year. But on a relative basis, your manager has minimized losses. That's what you want, right, from your active managers. Negative 1.8 versus benchmark that's negative 3 for the first nine months of

the year.

You have one index fund there. You see Rhumbline, which just got hired mid 2017. And you have three active managers, which are in the process of 16 getting replaced, as well: Mondraine, Harding and DFA. But again in the aggregate preservation of capital at the international equity level, which is good to see in this turbulent market.

On the fixed income side on the subsequent page, again, similar theme. It's been a tough year even with the bond market. Bond market is down negative 1.6 for the first nine months of the year. If you look at the Barclay's aggregate, your managers on a consolidated basis are negative. But again, not as far down as the benchmark. Negative 0.74, which again is good to see.

You have six active managers. And they all outperformed five of the six -- five of the top five outperformed. SKY Harbor, the bottom one, just got hired. If you look all the way to the far right, SKY Harbor just got hired in April. Let's put that one aside. But the other



five, all productive capital during this volatile time period for the bond market, which is good to see. The first two managers have the majority of the assets. That is almost half of your fixed income allocation. They both, you know, on a year-to-date basis, projected capital. Is good to see.

MR. GOLDSMITH: Just a note on SKY Harbor, you might remember, that's a high yield manager that was added. The benchmark for combined fixed income is the Barclay's aggregate. Even though SKY Harbor, you know, has lagged in its style specific benchmark, that decision to add high yield specifically into the fixed income portfolio has added a lot of value since inception. SKY Harbor is up 2.45 since early 2018, while the Barclay's aggregate is negative over that period. It's an allocation decision to high yield.

MR. DiFUSCO: Is this in the binder, as well?

MR. GOLDSMITH: Yes.

MR. AMMATURO: Is think it's worth to point out, reiterate 2.6 in the book, the large



book, I think it's an important point. Again, behind Tab 2. So, this is what I was saying earlier.

If you look at the blue bar for domestic equity, you have a nice size overweight. That's been a tailwind to your performance for the first nine months of the year. If you look at combined fixed income, you are underweight by about 5 percent. That is what's driving that relative outperformance for the first nine months of the year. Being overweight to equities and underweight at the bond market.

Your target is roughly 65 equity and you're close to 70 percent equity as of the end of September 30.

MR. GOLDSMITH: Speaking to maybe what happened in October a little bit, one thing we -- as this plan raises about 2.5 million in cash per month. It's been a theme throughout 2017, and really for most of 2018 that those selling assets to raise that cash has mostly come from U.S. equities. The strongest performing, most overvalued assets class.

So you know, by trimming sort of



consecutively throughout the year, it's a way of dollar-cost averaging those assets on the way out. So you know, being overweight in October to domestics didn't help. But letting it drift, it would have been much more overweight. I think that's, obviously, a little -- when we give our recommendations to Chris, relative valuations and our outlook for the future is always, you know, what goes into that decision.

We handed out the market value as of the end of the day yesterday. You know, I don't -- I think we are a little bit underweight to cash. That is by design throughout -- we like to keep a cushion to cash. So when there is volatility like you saw in October, we don't -- aren't forced to sell assets at, you know, in the middle of 10 percent market correction. And we did. I think you might have seen we rebalanced it this week. Taking assets from fixed income now as sort of the market conditions have flipped somewhat.

CHAIRMAN SCOTT: We went from September 30 we were at 550. And on November 13, 521?





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MR. AMMATURO: Yeah.

MR. DiFUSCO: About a 6.4 percent -- this morning, 6.4 percent decline.

MR. GOLDSMITH: We expect the October flash performance to be available, hopefully, later on today. If it is, Chris will distribute it to you all.

CHAIRMAN SCOTT: Thank you.

MR. AMMATURO: Thank you.

CHAIRMAN SCOTT: Chris, No. 5.

MR. DiFUSCO: Sure. We discussed this briefly. I mentioned over email. We set up Commission supported approval that diversity female veteran local brokerage program about a year ago. We started that at 30 percent target. We have seen a lot of managers close to it or exceed it. And a couple that are not or happy to be ones that, for various reasons, are on their way out.

And so, the large pension fund, the City pension fund recently increased the target to 35 percent. I think it makes sense. We have a lot of the managers in common. You know, a lot of these managers work with other public funds

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that have, you know, high targets, as well.

With the Commission's approval, I would like to increase the target here as well to 35 percent. Keep those consistent and, you know, push our managers on the diversity and gender front to deal with a little bit more. So if the Commission is so inclined, I would ask for a motion to support that.

MS. JOHNSON: I'll make a notion --

MR. WHITE: Second.

CHAIRMAN SCOTT: I think the motion was made and it was seconded.

MS. JOHNSON: All in the same breath.

CHAIRMAN SCOTT: All those in favor?

(Ayes.)

CHAIRMAN SCOTT: That is passed.

MR. DiFUSCO: Thank you. I will alert the managers. And just for reporting purposes, I will probably ask them to, you know -- you will see what it is at the end of the quarter. I will expect that they will start more fully given it's already mid November. You really kick that into gear the first of the year. That is my expectation given the target will increase

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immediately. But I am saying practically speaking, since we are halfway through the quarter, I suspect, you know, it's reasonable to ask them to start meeting that goal for the first quarter.

MS. JOHNSON: Make sense.

MR. DiFUSCO: Just being realistic.

CHAIRMAN SCOTT: At the January meeting, would we see actual performance?

MR. DiFUSCO: Sure. I send those out to you as I get them. You will have those -- in January on or before the first, you will have the numbers at the end of the quarter for third quarter. The fourth quarter numbers will probably be ready around the first of February. Have to add everything. Soon as I have them, I will send them out.

CHAIRMAN SCOTT: Thank you.

MR. DiFUSCO: Yup.

CHAIRMAN SCOTT: This has been a pretty long meeting.

MR. DiFUSCO: Try not to do that very often.

CHAIRMAN SCOTT: That's all right.

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Are you guys ready to adjourn?

Is there a motion to adjourn?

MR. WHITE: Motion to adjourn.

MS. JOHNSON: It's seconded.

CHAIRMAN SCOTT: Thank you, everybody.

(At this time, the Meeting adjourned at 12:19 p.m.)

C E R T I F I C A T I O N

I, hereby certify that the proceedings and evidence noted are contained fully and accurately in the stenographic notes taken by me in the foregoing matter, and that this is a correct transcript of the same.

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