THE BOARD OF PENSIONS AND RETIREMENT
INVESTMENT COMMITTEE MEETING
August 21, 2013

MEETING MINUTES

There being a quorum, Paula Weiss, Board Chair, called the Investment Committee Meeting to order at 9:37 a.m., in the Board Conference Room, 2 Penn Center Plaza, 16th Floor.

Present:

Rob Dubow, Finance Director
Paula Weiss, Esquire, Alternate, Deputy Director of Finance
Alan Butkovitz, Esquire, City Controller
Harvey Rice, Esquire, Alternate, First Deputy City Controller
James Leonard, Esquire, Alternate, Chief Deputy City Solicitor
Brian Albert, Alternate, Deputy Human Resources Director
Albert D'Attilio, Director of Human Resources
Celia O'Leary, Alternate, Deputy Director of Human Resources
Carol G. Stukes-Baylor, Employee Trustee
Ronald Stagliano, Employee Trustee
Andrew P. Thomas, Employee Trustee
Veronica M. Pankey, Employee Trustee

Francis X. Bielli, Esquire, Executive Director
Mark J. Murphy, Deputy Executive Director
Sumit Handa, Esquire, Chief Investment Officer
Brad Woolworth, Deputy Chief Investment Officer
Christopher DiFusco, Esquire, Director of Investments
Dominique A. Cherry, Investment Officer
Daniel Falkowski, Investment Officer

Also Attending:

Katherine Mastrobuoni, Esquire, Assistant City Solicitor
Ellen Berkowitz, Esquire, Deputy City Solicitor
Daina Stanford, Administrative Assistant
Carmen Heyward, Clerk Stenographer II
Donna Darby, Clerk Stenographer II
Robert O'Donnell, Esquire, O'Donnell Associates
Jacob Walthour, Cliffwater
Brad Atkins, Franklin Park
Raymond Jackson, Franklin Park
Tina Williams, FIS

THE BOARD OF PENSIONS AND RETIREMENT
INVESTMENT COMMITTEE MEETING
August 21, 2013

Shalonda Epps, FIS
McCullough Williams, FIS
John Spagnola, PFM
Kelly Arek, J.P. Morgan
Robert Smith, Vista Equity Partners, Foundation Fund II
Christine Pastore, Vista Equity Partners, Foundation Fund II

THE BOARD OF PENSIONS AND RETIREMENT
INVESTMENT COMMITTEE MEETING
August 21, 2013

Agenda Item #1 – Approval of Minutes of July 25, 2013

Ms. Weiss requested a motion to approve the minutes of July 25, 2013. Mr. Albert made the motion and Mr. Stagliano seconded it. All were in favor. There were no oppositions or abstentions. The motion passed.

Agenda Item #2 – Private Markets – Vista Foundation Fund II, L.P.

Mr. Dubow joined the meeting.

Mr. Handa stated staff and Franklin Park are recommending a $30 million investment in Vista Partners. The Fund is an investor in Vista Equity Fund III. The returns have been nothing less than extraordinary - 30% net since our investment. To put this into perspective, they are number one, in terms of performance, in their peer group.

Mr. Handa posed the rhetorical question: What does Vista do and why aren't others doing it? Vista is being recommended because Vista invests in enterprise software for businesses. They have certain ingredients in their "secret sauce". The first is they have very high customer retention, resulting in a very "sticky" business. The second is high barriers to entry. There are a limited number of people who can enter the stakes. The third is pricing power, the ability to raise prices on their customers. The businesses they buy are able to raise prices. The fourth is market dominance. The companies they buy are either number one or number two in their industry.

One of the criticisms of Vista is that they overpay for assets. Mr. Handa said that is wrong and is based on an EBITDA analysis. The right method is Return on Invested Capital. The return on invested capital is the penultimate test of the business. The return on invested capital for most of the Vista companies and their portfolio have been north of 50% to 70%, some higher. For those reasons, that is the formula they use to generate returns in the enterprise software area.

Mr. Handa explained the formulaic approach to enterprise software using as an example Reynolds and Reynolds. This is a company that Vista took private in 2007, What does Reynolds and Reynolds do? They are the backbone for every automobile dealership in the United States. Reynolds and Reynolds and ADP, the paycheck company, are the largest enterprise software and support services vendors in the United States, each with about 45% market share. The market is an oligopoly with only two players.

Ms. Weiss inquired about the size of the fund. Mr. Handa said they are looking to raise $500 million to $1 billion. The terms are "2 and 20", however if they earn 30% they are entitled to 30% of profits. Also, most management teams commit 2% in any sort of deal, Vista management will commit 4.6%, truly an alignment of interests with the other investors.

Ms. Weiss inquired about the concerns if they raise a billion dollars, will this stretch their staff, their resources and will there be enough deals.

Mr. Handa stated they have seventy-six employees and our research suggest that there are 27,000 companies out there, just in North America. There are plenty of deals that are available. Mr. Handa said they believe the opportunity set is quite large and the return potential is there as well. Mr. Woolworth added that it is an advantage that all of Vista's staff works exclusively on enterprise software.

Mr. Leonard asked if Vista was an African American owned firm. Mr. Handa stated it is. He stated 65% is owned by Mr. Smith and if the board was to approve this we would be making total aggregate this year $100 million in investments to women and minority funds. Of $250 million allocated to private markets this year, that's 40% to women and minority firms.

Mr. Rice asked Mr. Handa if we were restricted to $30 million and if they will accept more. Mr. Handa said he believes we could get more.

Mr. Bielli asked Mr. Handa if Brad [Atkins] could provide any further insight to Harvey's question. Mr. Atkins said this is probably one of the most value additive private equity firms in the industry. Their key strength is how they reengineer companies that they buy, bring in new management, restructuring the sales and marketing initiatives, restructuring operations, changing a czar. They have a successful track record, a deep proven team.

Ms. Stukes-Baylor asked Mr. Atkins if he had any concerns at all. She said one of the founding partners left and she wanted to know if that was going to be a mitigating factor on how they operate. Would that put an impact on the operation?

Mr. Woolworth said staff contacted Mr. Steven Davis. He was one of the co-founders of Vista back in the year 2000. He did not know if his departure had any meaningful impact. In contacting Mr. Davis about Vista, Mr. Davis had good things to say about the organization he had helped build and very good things about Robert Smith.

Mr. Bielli wanted to go back to Harvey's question of going larger than $30 million. Mr. Woolworth's advice was to ask.

Mr. Robert Smith, Chairman and CEO, and Ms. Christine Pastore, Senior VP and Head of Investor Relations, entered the Boardroom to make the Vista presentation.

Mr. Smith said enterprise software is the most productive tool introduced in our business economy in the last forty years. The tools that have been introduced have created massive amounts of productivity in our economy and as a result of that, enterprise software has become much more essential in the basic business fabric, globally. He gave examples from various industries.

Mr. Smith said Vista was founded in the year 2000 to take advantage of the software phenomenon which has really changed our businesses. Mr. Smith said as a result of the work we've done we now have been able to perform quite superbly in this marketplace. We do buyouts in enterprise software.

Mr. Smith said Vista is we created this system and a set of processes in a platform to identify those enterprise software businesses, make them run more efficiently and then capture the returns in that efficiency back to our shareholders, our stakeholders in terms of their partners and ourselves.

Mr. Smith said we have effected over 100 transactions, over $22 billion. We have made money on every buyout deal we have done since day one. I have just over $7.2 billion in assets under management. Our returns on realized deals is over four times cash on cash, just over 50% IRR on all of our realized deals and every single buyout company in our portfolio is held above cost.

Economic rent is a value that comes from productivity. What we do is identify the economic rent imbalance and figure out ways to capture that economic rent over long periods of time for our companies. The next thing we do is we become the low cost producer, not the low price provider. Enterprise software is a 95% gross margin product. We build a product once and sell it many times. We have no inventory to carry. We look for companies with high cash flow from recurring revenue, which can be used to invest in the business, re-lever the business, invest in a different business, or pay dividends. Eighty-two percent of our revenue is from recurring revenues under contract.

The other wonderful thing about enterprise software is we sell into verticals, where the markets operate as oligopolies. If we have competition, it will be from a small number of big players. Sometimes the market is a duopoly, or if we are really lucky, a monopoly. Enterprise software is a business where you can create a monopoly every day by making a product designed for the customer and on which the customer depends, and then entering into multi-year contracts.

Mr. Smith said the market is enormous. Vista has identified over 40,000 software, data and technology-enabled service companies worldwide, including 27,000 in North America. Of these, looking at the chart on page 5, only 75 have annual revenues exceeding $1 billion. We own two of them. There are only 2,000 companies between $75 million and $1 billion, but there are 25,000 companies below $75 million. That is where the Foundation Fund operates. In that market cap, there is over $800 billion of value. There is over $1 trillion of maintenance and support paid each year. In the Vista companies we maximize each dollar paid for maintenance and support by making it more efficient.

Mr. Smith reviewed the commitments, funding, investment and performance of the Vista funds.

Ms. Weiss wanted to know as far as size how staff will be able to handle that increase in business. Mr. Smith stated as you know our terms our typically ten years, five years in investment. On average we've been fully invested in all of our funds in about 3.3 years if you go to the same investment pace that takes you out to just under five years. We continue to build staff, build our organization. My expectation is the actual cycle time is about 4 to 4 ½ years to fully invest that capital with the team we have in place today.

Ms. Weiss wanted to know will Mr. Smith's team be stretched too thin. Mr. Smith said no, we continue to hire ahead of the curve because ultimately what we're going to do is have multiple funds.

Mr. Dubow asked Mr. Smith how big is your team now. Mr. Smith said we've got two co heads of the team, we have three vice presidents and we have a series of analysts and associates.

Mr. Dubow asked how many analysts and he inquired about the growth. Mr. Smith answered twenty-two analysts and associates and that it's a constant state of growing.

Vfsta is able to grow because it applies its best practices standard operating procedures to every Vista company, whatever the scale. Software companies are more alike than they are different, for example training the managers, writing the code, installing the code, service calls, managing and training the clients, marketing. The only thing that's really different is the customer base and how you price the product. If a person joins a Vista company as a manager, he or she joins all the Vista companies.
Mr. Smith said they have been fortunate and have done extremely well in the 2007 vintage Foundation Fund I. It's in the top three funds worldwide according to Thompson- Reuter's database. We just got an award from Preqin, saying we're the most consistent private equity performer in the world. There were four companies that were named in that same category; we're the only ones with over $2 billion in the assets under management.

Mr. Smith called the Board's attention to page 12 of his presentation, which shows the composition of the Investment Committee. We have a bottoms-up analysis of every single deal brought to the Committee. Before we write a check, we have a plan, generally multi-year, detailing every project to be completed.

Mr. Stagliano inquired about the possibility of the Board investing up to $50 million. Mr. Smith said because some partners would say it can't be over $1 billion and because they are big LPs and they've been supportive of us, the First Institutional Fund, Fund IV and Foundation Fund I, I have to make those commitments so I can't go over a billion dollars in this fund.

Mr. Smith said we have a co-invest fund and a credit fund which is different but basically the same dynamics occur. I cannot give you what you are asking for but we can give you what we can.

The presentation concluded.

Mr. Dubow requested a motion to invest $30 million in Vista Foundation Fund II, L.P. Ms. Stukes-Baylor made the motion and Mr. Albert seconded it. All were in favor. There were no oppositions or abstentions. The motion passed.

Mr. Handa added, to date, the Board has made $250 million of investments and in terms of commitments and investments to which $100 million is going to women and minorities, 40%.

Agenda Item #3 – Opportunity Fund Guidelines – Subcommittee Recommendation

Mr. Handa said the Board requested a review of the Opportunity Fund. Staff and Cliffwater conducted an independent due diligence' The Subcommittee met last Thursday. The conclusions were unanimous from the Subcommittee. The Subcommittee has made some recommendations.

Ms. Cherry reported as of June 30, which was the most recent information available, total assets in the Opportunity Fund were a little over $280 million. The tables in the Staff Report show the trailing performance of both managers. There were concerns about the Opportunity Fund and at the Board's request, Staff along with Cliffwater conducted a full analysis of the fund that was presented to the Subcommittee. Recommendations from that Subcommittee meeting will follow this report.

Mr. Dubow asked Ms. Cherry to talk about what our goals are for the Opportunity Fund.

Ms. Cherry reported overall what we're looking for in the Opportunity Fund; number one is to give opportunity to diversity and emerging managers. By taking advantage of direct relationships with the Opportunity Fund managers, it will ultimately be beneficial to the Board in terms of negotiating fees and having overall control of the process, selecting managers and decision making. All those things add to the bottom line which is what we're looking for, performance at the end of the day.

Ms. Cherry continued through research, Staff has come across several managers that would add diversity to our Fund. One of the recommendations is to add alternative asset classes to the Opportunity Fund. These include real estate, hedge funds and private equity. Staff has come across several managers who had to be passed over because they did not qualify for the main fund due to size, asset type or track record, and also did not fit into the Opportunity Fund guidelines. Therefore, the first recommendation is to add alternative strategies to the Opportunity Fund.

Number two is to expand the overall size of the Opportunity Fund, provide more opportunities to those managers, increasing the overall allocation and this will ultimately go up to the main fund as well.

Number three, transition out of the fund of funds model and move more into a direct program with Staff and Cliffwater overseeing the managers directly.

Number four; issue an RFP in several areas, such as Domestic Equity and U.S. Fixed Income to provide opportunities for those emerging and diversity managers.

Ms. Weiss added the way we talked about it at the Subcommittee is to expand, to include the newer minority, female and disabled managers by using the Opportunity Fund Guidelines to allow us to look at managers for the large fund that we definitely don't look at now. Ffor example, by allowing us to review managers who only have $100 million of assets under management, who may have a shorter track record than traditionally what we look at and in order to mitigate some of the risks of going with those newer managers and those smaller funds, maintaining no more than 10% of that investment against their assets under management. For a $100 million fund we wouldn't have more than a $10 million commitment, but that we would be able to grow our commitment as that fund grew and increase our actual dollar commitments as they maintain a larger fund.

Mr. Bielli said if these changes are adopted what effect do you anticipate that the change will have on the percentage of minority, disabled and women owned firms.

Mr. Handa stated it would be a substantial increase. We are currently at 6% in the Opportunity Fund. We believe you can get to almost 25% when you start allocating all the available dollars in the fund.

Mr. Dubow wanted to know if it was 6% to 25%. Mr. Handa answered it's 15% to 25%. Mr. Dubow wanted to know the strategy of going from 15% to 25%.

Mr. Handa answered the recommendation from the Subcommittee was to expand the Opportunity Fund and the Opportunity Fund Guidelines to include alternative asset classes, such as real estate, private equity and hedge funds, which we have in the plan.

Mr. Dubow inquired about the long only investments. He said one of the other recommendations is moving away from the fund of funds and asked why is that better. Mr. Handa said there is nothing wrong with having a fund of funds model; many plans have it to date.

Mr. Dubow asked about the workload. Mr. Handa stated Staff is more than capable of doing this. We certainly have the resources.

Ms. Pankey asked has the current manager been given the opportunity to look at the alternative strategy in which you wanted to turn to or you just want to eliminate them. You had a long term relationship with these individuals. I would like to hear from them and giving them the opportunity to turn to the strategy in which you want to go before one considers anything else. Has there been any recommendation from FIS or PFM in wanting to change their current strategy and has consideration been given them. I'm really concerned that the option to terminate our relationship with them is not a consideration. I really have a great concern with that.

Mr. Handa stated Staff and Cliffwater did review a proposal that was submitted by one of the parties.

Ms. Pankey asked which party is that. Mr. Handa answered FIS, the conclusions are in the analyses, respectively, by Staff and Cliffwater and the Subcommittee. As for the former, in terms of investment alternatives, I had a conversation with one of them last year and suggested they do consider investing into something the Board would like to do.

Ms. Pankey asked which one was that. Mr. Handa answered PFM. As for investing in alternatives in general, as of today, my understanding is that neither of them are doing it, investing in alternatives.

Ms. Pankey asked would they have to come back before the Board to be able to do that. Mr. Handa answered yes.

Ms. Pankey asked are you stating there was never any recommendation for either one of them to do that. Did either one of them send in a proposal to want to do this? Mr. Handa answered, no, not that I'm aware of.

Ms. Stukes-Baylor said that's because when the Opportunity Fund first started, alternatives were not part of our plan at all, we only had a small pool of assets.

Ms. Stukes-Baylor said as a trustee that sat on the Subcommittee when Mr. Handa first discussed this last year with me, it was never a consideration of transition out the manager of managers, we talked about expanding the Opportunity Fund, which I supported him on, because we need to include hedge fund, private equity and real estate managers.

Ms. Stukes-Baylor said at the Subcommittee meeting, she and another trustee had a concern which was could the Staff handle this operation. There were also several discussions on why do we have to transition from the managers of managers and not try to come to a median of finding some guideline with both Staff and the managers of managers. Ms. Stukes-Baylor said the concern with Staff is that we don't have the control to fire a submanager or hire a submanager if we chose to.

Ms. Stukes-Baylor said there was no back and forth communication between staff and FIS. Staff said that the fund of fund managers didn't have a database large enough for minority managers which took them aback. After some discussion with Mr. DiFusco and Ms. Cherry, they cleared it up. Both managers had a large enough database; it was the international part they were looking at.

Ms. Stukes-Baylor said to Mr. Dubow she did not know the Opportunity Fund was supposed to be the minority bucket. She thought it was supposed to be minority, women and emerging

Mr. Dubow said the Opportunity Fund is not all minorities.

Ms. Stukes-Baylor said they're not all. PFM tries hard to do a lot of minority. FIS is emerging. They have some minority and they have emerging. I don't know why the bucket of the minority people is in the Opportunity Fund and not in the larger fund.

Mr. Leonard asked Mr. Handa about the Board over the last few years, which has moved away from fund of fund arrangements. He asked Mr. Handa to put that into a larger context that Cliffwater talks about on page 4 of their report, with the change over essentially broader than just us. Mr. Handa referred Mr. Leonard to Mr. Walthour.

Mr. Walthour said if you go back in time to when the fund of fund business all started, those arrangements were structured differently than you might see a fund of fund relationship structured today, almost to the point where today a lot of fund of fund relationships very much look like consulting relationships. If you go back to the beginning of time those relationships were fully discretionary and the manager of managers would source the managers, perform diligence on the managers, negotiate with the managers, hire and fire the managers. Today you see those relationships being a lot more collaborative.

Ms. Stukes Baylor said we did eliminate the funds of funds in the hedge fund bucket but we didn't get rid of the consultant. We got rid of the consultant because the consultant wasn't doing a good job and I guess that's the relationship I thought PFM and FIS was acting more or less as a consultant . We did get rid of the fund to funds under private equity but we did not find a consultant. I guess that's where I'm a little confused, the transition of the manager to manager.

Mr. Dubow asked Ms. Stukes-Baylor if that answered her question

Ms. Pankey said I just want to reiterate and I strongly feel that the Subcommittee has established what the guidelines are going to be for the Opportunity Fund. They have not been imposed nor have they been discussed with PFM or FIS.

Mr. Handa said he thinks if changes to the guidelines were discussed or recommended, the Subcommittee and the Board would have to review it before it goes to any outside parties. They are outside parties. They're not parties to what the guidelines should be for the Fund. That's something the Board has to approve, until they approve them, we can't send them out to anyone.

Mr. Dubow requested a motion. Ms. Pankey made a motion to table the item and stated she would like to hear from PFM and FIS regarding their performance and their ability to turn to the strategy in which staff and the Subcommittee want the fund to go to, and if that's not something in which that they are willing to participate. Ms. Pankey said she heard Mr. Handa had a discussion with PFM and there was no response, and if that is not something they are going to perform, we bring it back for a decision. Three were in favor of the motion (Ms. Pankey, Ms. Stukes-Baylor, and Mr.Thomas). Five were opposed (Mr. Butkovitz, Mr. Albert, Ms. O'Leary, Mr. Stagliano and Mr. Leonard). The motion failed.

Mr. Dubow requested another motion. Mr. Albert made a motion to approve the recommendations of the Subcommittee. Five were in favor (Mr. Butkovitz, Mr. Albert, Ms. O'Leary, Mr. Stagliano and Mr. Leonard). One was opposed (Ms. Pankey) and there were two abstentions (Ms. Stukes-Baylor and Mr. Thomas). The motion passed.

<u>Agenda Item #4 – Quarterly Report for 2013 2Q and Flash Report for themonth ended July 31, 2013</u>

Mr. Walthour reported he had the quarterly report and the monthly flash report. He talked about the quarterly first. The performance numbers that you see are going to be impacted by lag specifically in some of the private asset performance. We had a conversation yesterday specifically because of the monthly flash for the month of July being a very large discrepancy because of index report that makes the numbers look a lot worse than they are so we are going to try to make some modifications to the performance presentation structure as well.

Flash report, the best performance came from the Real Assets managers, particularly the MLP managers. They made a very large contribution relative to the actuarial assumption rate. Emerald Advisers and O'Shaughnessy Asset Management made some pretty substantial contributions as well. This doesn't necessarily mean that everybody beat their index but they made relatively large contributions to the plan.

On the negative side, the Plan saw very weak performance from emerging markets and extremely weak performance from the emerging market sector. In the last quarter total emerging markets for the index performance was down somewhere around 8%.

For the quarter, the fund underperformed by about 34 basis points but for the fiscal year the fund eked out positive performance relative to the new bench mark. Looking at the fiscal year performance, we underperformed in U.S. equities, it being very difficult to pick active managers that consistently outperform their index particularly, when we start benchmarking things against the Russell 3000, the higher end of the market range

The U.S. Equity composite underperformed by 87 basis points YTD. while Non-U.S. Equity Developed underperformed by 218 basis points. With emerging markets there was a transition issue getting into the passive management that is not owed to any type of manager's performance issue. Investment Grade Fixed Income was a bright spot with 144 basis points of outperformance. Absolute Return was another bright spot with 273 basis points of outperformance.

The composite, the current lineup, of the17% that we have in the large cap space benchmarked to the Russell 1000, we now have indexed 14 out of those 17 percentage points. The most efficient part of it in the capital markets is now being indexed. We continue to have two active managers. Aronson + Johnson + Ortiz did 79 basis points in Alpha relative to their benchmark. O'Shaughnessy Asset Management, 233 basis points relative to that benchmark so the lineup for large cap equities appears to be in pretty good shape within the large U.S. between index and any active managers that you have.

In the midcap space Geneva Capital Management struggled for the fiscal year and this year, happy to say, they appear to be on the mend. Ceredex Value Advisors had been somewhat negative to the benchmark of which we are not that concerned about. Emerald Advisers generated 329 basis points of outperformance and continues to be one of the real consistent bright spots in the portfolio. Fisher Asset Management performance was 103 basis points of alpha as well. We added Snyder Capital Management for a manager off to a little of a slow start but there is no reason to be concerned at all about that relationship.

Mr. Walthour said, looking at the Opportunity Funds, the funds struggled a little bit during the second quarter. PFM was down 56 basis points relative to the index. FIS was down 40 basis points relative to the index. Together they did deliver a 16 percentage point return throughout the year ending June 30, which is certainly a positive contribution relative to, once again, an 8.1% actuarial return assumption.

Mr. Dubow corrected Mr. Walthour and said the return assumption is 7.95%.

The Non U.S. Equity performance is FYTD 200 basis points below the benchmark. That's attributed to a very costly year from Barings International Investment which was down by about 535 basis points relative to their index. You've had really strong performance from Causeway Capital Management who delivered just the opposite, which was a good idea to add additional capital to Causeway Capital Management throughout the fiscal year. They're up over 500 basis points relative to their index. Northern Trust Investments delivered 74 basis points relative to their index.

Turning to non-U.S. emerging, which has been a challenging asset class. Despite the market being down, the ESG Cross Border Equity Offshore Fund for calendar YTD generated real positive alpha relative to the benchmark. Putting alternative managers in traditional buckets has helped buffer the negative performance in the portfolio by delivering a positive result in that negative time period. Rhumbline is tracking the index fairly well but there is no way for an index to get out of the way of a negative performance.

The Investment Grade Fixed Income Portfolio, 144 basis points in alpha and fixed income portfolio over a year with very strong outperformance really being owed to Brandywine. They put in a very good year. Merganser Capital Management, 123 basis points of alpha over the year which we think is more realistic in terms of what we should expect.

Opportunistic Fixed Income, a newer asset class, and a negative quarter in the credit world. BeachPoint Capital Management, despite being in a negative credit environment, delivered a positive return of 344 basis points. This is another example of the point I was trying to make with ESG - putting alternative managers in traditional buckets has helped buffer the negative performance from long-only managers.

Mr. Walthour said this is going to be a recurring theme throughout the next fiscal year. Interest rates have been at historical lows whether you're looking at government securities, mortgage securities, asset backed securities, traditional investment grade, corporates, and high yield.

Looking at the Real Asset performance. If you look at the MLPs, it was a very good strategic decision by the Board to invest in MLPs and the Board also picked three really good managers that have consistently outperformed the Alerian benchmark. This has been a grand slam; the Board picked the right asset class in investment asset classes to add to your portfolio throughout the last fiscal year generating 34 percentage points in performance. Each of the managers delivered 600 basis points of alpha relative to benchmark. We also addred more liquid Real Assets, REITs. Axonic in the second quarter added 643 basis points of alpha.

The Absolute Return component of the portfolio, the portfolio delivered 270 basis points of outperformance relative to the index of Libor plus 400. We're trying to develop a portion of this portfolio that can act as a hedge to adversity and not necessarily being aggressive because we have enough long only exposure in the portfolio and so we added managers like the Kynikos Opportunity Fund. They're down in terms of their performance but once again we know why they're there, they're there to get a positive relative performance. Fiscal year to date while they're down almost 12%, relative to their benchmark they're up 5%, maybe not helping the overall portfolio but certainly doing their job, but within the space we've hired them.

Although the month of June was a difficult month for a lot of asset classes, you came back in the first month of our new fiscal year. The was really great performance in large cap equities. Europe, you've seen a pretty good performance there, also within the credit space and hedge fund space, we returned to positive performance.

For the total Fund, if we do a back of the envelope calculation in terms of what the negative cost of the lag in private equity performance benchmarks is, probably about 50 basis points of the 70 basis points so the index would probably beat us by about 20 basis points and not the 70 basis points and that would cascade all the way to the right.

Mr. Handa asked Mr. Walthour if he could possibly footnote in these documents stating all of this as well since this information becomes part of the public domain.

Mr. Walthour said when you think about what the fiscal year target is in terms of the actuarial assumption it's a very positive month, 2.3% in a given month is very strong performance on an absolute basis.

Select managers contributions, there were performers on the positive side as well on the negative side and we've also looked at a calendar year to date basis.

Taking a current look at our asset allocation and where we stand relative to the target. We've come a very long way in terms of moving portions of the portfolio around within the composites but also come a long way in terms of moving closer to our actual target asset allocation. So you can see even with assets underweight for Non- U.S. Equity and Hedge Funds, we're getting very close to our targets. With Private Assets even when you make commitments, it takes a while for those commitments to be drawn down by the managers, that's probably our biggest underweight at this time. We've also been talking with Staff about other ways of bringing that down and perhaps looking at strategies like activism as a way of chipping away at that relative underweight. Our overweight's, particularly the U.S. Equity market which has been the best performing stock market out of the existing large developed stock markets in the world, has been your biggest overweight and that has made a substantial contribution. Going slow, in terms of migrating to the new asset allocation was a great call on the part of the Board.

Mr. Leonard said the slide on page 25 typically shows the allocation snapshot and he asked Mr. Walthour if it is possible, next time, to show us the progress to the new allocation policy over the last several months since we put the policy in place.

Ms. Pankey asked Mr. Walthour if we can see where we are on the previous month, or the last month that we made an investment.

Mr. Walthour said Cliffwater could add a transaction summary. Mr. Bielli said there can be a change in valuation without a transaction. Mr. Walthour continued and stated we'll show month over month.

For July, each and every one of the composites underperformed its benchmark, but underperformed only by relatively marginal amounts. U.S. equities had positive performance for most of the active managers, Aronson + Johnson + Ortiz, O'Shaughnessy Asset Management, Geneva Capital Management, Ceredex Value Advisors, all produced a positive performance which is a good sign.

Non U.S. Equities, the only negative spot is Barings International Investment, down127 basis points relative to its benchmark. ESG Cross Border Equity Offshore Fund delivered within Non U.S. emerging, another powerful month with another 600 basis points of outperformance for the month in a very negative month for emerging markets performance, it is starting to add tremendous value if you followed them all since inception.

Mr. Bielli asked what the story with Baring International Investment was. Mr. Walthour responded, if look at International Equity one of the biggest contributors to outperformance and underperformance is very often how much of a weight they have to Japan. Japan had been a laggard in the market for a very long period of time and a lot of people were able to add value just by being underweight Japan. We've had a rise in the Japanese market particularly relative to the European markets and that has caused sort of extreme performance links.

Opportunistic Fixed Income, BeachPoint, a very positive month in a negative environment, others marginally underperformed they're various indices.

Within the Hedge Fund portfolio for the month, we lagged by about 67 basis points, that had a lot to do with Bridgewater's underperformance, they were down almost 4% for the month.

Ms. Weiss asked if they should be concerned about Bridgewater. Mr. Walthour said Bridgewater is the largest hedge fund in the world. We have been waiting for them to turn things around. We haven't seen the turnaround. We would be supportive of looking at other options that could deliver some positive performance and at the same time deliver in the event of a negative overall market scenario.

Mr. Stagliano asked how long it would take to get our money. Mr. Handa said it's a liquid fund; we can get out in 30 days.

Ms. Stukes-Baylor made a motion to terminate Bridgewater. Mr. Dubow requested a second. Ms. O'Leary seconded it. All were in favor. There were no oppositions or abstentions. The motion passed.

Mr. Dubow if there were other managers where you have similar concerns. Mr. Walthour said he thinks we should wait until we finish developing the framework for making these decisions as opposed to randomly picking managers and saying let's terminate. Mr. Dubow said if you have concerns and you think they're not performing and they are never going to perform, I don't think you should wait.

Mr. Handa said that calendar year to date Geneva Capital Management was down 400 basis points relative to the benchmark. The one year number was 900 basis points. Since inception they were down 400 basis points.

Mr. Dubow said for the last three months Geneva was beating their benchmark by roughly 70 basis points. He wanted to know if that was a sign that they're turning things around.

Mr. Walthour stated it's certainly a sign that they're turning things around if they are generating a positive alpha relative to the benchmark over a three month period. Mr. Walthour said I look at things in multiple ways. I look at things relative to the benchmark for the manager but also what's their contribution to the overall performance. The last three months they generated 8.53% absolute return, for the last month, 6.62%, I factor that in as well. That's why he was not saying you should fire them. He said there is clearly a method to what they were doing, generating those performance results.

Mr. Handa said be mindful the S&P was up 5% last month. The Russell midcap index was up 6.2% in a month. If the index is up 6 plus percent, they should generate that type of return in that month, and they did, however if you look at the one year number, the index was up 30.69%. Geneva Capital Management was up 23.5%. In the last three months, they turned the corner. Staff did meet with them in June and we highlighted some of the concerns.

Ms. Stukes said they had some other managers they were concerned about, the bottom performers. (Page 4 of Cliffwater report)

Mr. Handa said he had several conversations with the trustees, Board members and bottom-performing managers. Ms. Stukes-Baylor asked about Brandywine and Ms. Weiss asked about Stone Harbor

Mr. Handa said a lot of the underperformance has to do with the environment. The emerging market space has been obliterated. What has happened since April is that we have seen the Federal Reserve talk about language being used as tapering which has caused the interest rate of the Ten-Year note to move from 1.6% to 2.9%. This was a tremendous move. All of this has ramifications and it is playing out in the emerging markets. Mr. Handa gave examples and said this is all correlated to stimulus tapering language, which causes interest rates to move.

Mr. Handa said that rising interest rates particularly affect emerging markets. We are seeing that with the Indian rupee, which has declined 15% just since May, and the Indonesian rupiah, which is also collapsing. This is correlated to the tapering language. Mr. Dubow wanted to know what extent does that capture in the indexes. He said if the manager is doing worse in the index they are doing worse in the global reaction.

Mr. Handa replied that the indices are weighted by market cap. Mr. Handa said that with Stone Harbor being long-only their emerging markets debt portfolio had gotten obliterated. Investment Staff had taken steps, proactive steps, to lower our position in Stone Harbor. There are a lot of ramifications of a move in interest rates, it has to do a lot with allocating capital Sometimes even though the underlying manager has performed terribly, keep in mind what are they investing in for us, what is the objective of it, they are investing in emerging market debt as the strategy has collapsed .

Mr. Bielli said Mr. Butkovitz asked a question when we were discussing the Independence Fund, the hedge fund, and their ability to create a tactical instrument to respond to various things in the market. Emerging markets. If interest rates go up, it is in trouble. What are we supposed to do?

Mr. Handa said we've taken $15 million dollars off the table from Stone Harbor this year. That means that we've also taken other mitigating steps, for example putting ESG Cross Border Equity Offshore Fund in the Emerging Markets equity portfolio as an offsetting hedge to the long-only managers.

Mr. Handa stated there are other strategies in the portfolio that will have offset those losses, this includes BeachPoint , ESG, and there are other examples as well. As Mr. Walthour alluded to, we've had conversations about how to mitigate volatility. We continue to talk about we have almost $600 million in the pipeline we plan to take to the Board within the next six months to address all of these things.

Mr. Bielli said that he would rather take money from managers to pay benefits rather than watch it dwindle down. Mr. Handa said MLPs; we took 20 million dollars off the table to pay for benefits payments in the end of June. we realized because of a rising interest rate environment, these assets may not necessarily perform as well. We are trying to be proactive and vigorous in this approach.

In the Independence Fund there was a move by the Board to move $100 million dollars at the end of July. The Independence Fund is down 10 basis points, the S&P is down 2%, that's an example of being proactive, and you may not see that in the Flash Report, these are steps that you have taken collectively.

Mr. Walthour talked about U.S. equity manager underperformance. He said that getting back to Geneva, can we afford to have a manager underperform the index by 900 basis points. International managers historically have been able to dig themselves out of deeper holes quicker than U.S. equity managers where they are making a lot smaller decisions.

Mr. Handa said we have conversations every month regarding managers and strategic planning for portfolio allocation. He said that in April we took money from Stone Harbor to preempt the potential decline as a result of increasing interest rates. They still dropped as well, but the problem is where you continue to cut.

Mr. Bielli said, if the Board is concerned about interest rates, the Board is asking Cliffwater, with the likely inevitability of raising interest rates, what your suggestions are, in the firm's professional opinion, the moves that the Board should make.

Mr. Walthour said bring the duration down in the portfolio and lighten up on those sectors of fixed income that are likely to be the worse performing sectors of fixed income.

Mr. Handa reiterated, we have been doing all of that. We do this every month, we need to have fixed income exposure in this portfolio and we do have it. Some of the moves and investments we made this year were in anticipation of rising interest rates. We will be presenting something to the September or October Board that will decrease the amount of fixed income exposure. We expect that to be brought to the Board for recommendation approval.

Mr. Dubow asked if world events should cause us to revisit the asset allocation. Mr. Stagliano said the Board's asset allocation has always been fluid. We adjust it as we go along. Mr. Walthour said when we set the asset allocation there was no mention of the word tapering by the Fed, and tapering does require us to look at the fixed income portfolio. If we think that emerging markets are going to be the worst performing asset class in a rising interest rate environment, then it might not make sense to have the existing ETF in the portfolio. It might make sense to take that to cash, maybe not the whole thing, but maybe take a portion.

Mr. Handa said given the needs to grow the Fund, pay benefits and meet the actuarial assumption, Staff is trying to be as nimble as possible. Staff and Cliffwater are working on a revised asset allocation that will reduce fixed income, and will present at a future Board meeting.

Agenda Item #5 – Flash Reports for the Opportunity Fund Managers for the Period Ended July 2013

Mr. Dubow asked if there was anything else to add on agenda item #5, there was not.

THE BOARD OF PENSIONS AND RETIREMENT
INVESTMENT COMMITTEE MEETING
August 21, 2013

Agenda Item #6 Chief Investment Officer's Report

Securities Lending generated $1.5 million to date. Quality D has declined to under $570,000. Mr. Handa asked if there were any questions about the memos presented in the binders.

Mr. Handa talked briefly about three articles. One article was the Fannie Mae and Freddie Mac article. He said there is a lot of change going on in the mortgage area and that it is going to be a great opportunity set.

The second article was about an interview with David M. Rubenstein, co-CEO of The Carlyle Group. The article talks about what expectations are in terms of private equity investments and how individual investors are moving into the traditional private equity class.

The third article was about the MLPs. There was an interview with one of our underlined managers and two others about the MLP space.

At 12:00 p.m., Mr. Dubow requested a motion to adjourn the Investment Committee Meeting. Mr. Albert made the motion and Ms. O'Leary seconded it. All were in favor. There were no oppositions or abstentions. The motion passed.

At 12:01 p.m., Mr. Dubow convened the Board of Pensions and Retirement Meeting to affirm the actions taken at the Deferred Compensation Plan Committee Meeting and the Investment Committee. Mr. Albert made the motion and Mr. Stagliano seconded it. All were in favor. There were no oppositions or abstentions. The motion passed.

At 12:02 p.m., the full Board of Pensions and Retirement had a discussion on some "New Business."

New Business

The Controller initiated a discussion regarding PHDC and recent legislation which moves that agency to a MMO payment moving forward. The Controller asked Chairman Dubow if the Board was going to be asked to approve a move to an MMO payment retroactively, as there is a "gap" in the legislation that allows the Board to decide. Mr. Dubow indicated that he did not believe the Board would be asked to vote on the issue, and that the amount at issue, approximately $600,000, would be handled outside of the Board and through the City's General Fund.

Brief discussion amongst the Trustees ensued.

THE BOARD OF PENSIONS AND RETIREMENT
INVESTMENT COMMITTEE MEETING
August 21, 2013

At 12:10 p.m., Mr. Dubow requested a second motion to adjourn the Board of Pensions and Retirement Meeting. Mr. Stagliano made the motion and Ms O'Leary seconded it. All were in favor. There were no oppositions or abstentions. The motion passed.

The Investment Committee of the Board of Pensions and Retirement approved the Minutes on ____.

____
Rob Dubow, Finance Director
Board Chair