CITY OF PHILADELPHIA
BOARD OF PENSIONS AND RETIREMENT
SPECIAL INVESTMENT MEETING
August 11, 2011

MINUTES

On August 11, 2011 Rob Dubow called the Special Investment Meeting of the Board of Pensions and Retirement to order at 10:05 a.m. in the Board's Conference Room.

Present:	Rob Dubow Paula Weiss Alan Butkovitz Brian Albert Celia O'Leary Carol Stukes Anne Kelly King Ronald Stagliano John Reilly Veronica Pankey Hilary Cornell
Also Attending:	Francis Bielli, Mark Murphy, – Board of Pensions Harvey Rice – Controller's Office Sumit Handa, Rhonda McNavish – Investment Unit John Foulkes, Brad Woolworth - Investment Unit Daniel Falkowski, Dominique Cherry – Investment Unit Maximillian Marine – Intern, Investment Unit Christopher DiFusco, Joshua Stein, Benjamin Hinerfeld – Law Dept. Robert O'Donnell – O'Donnell Associates Andrew Thomas – Fire Department Catherine Lucey – Philadelphia Daily News Bob Warner – Philadelphia Inquirer Jim Osman, Andi Korff – CBS 3 M. Dunn – KYW Radio

Mr. Dubow stated that this is a special meeting where they want to talk about what's going on in the market and how the Board wants to react to it.

Sumit Handa stated that uncertainty is one of the most difficult factors for professional as well as individual investors to deal with and it is currently dominating the markets. Uncertain markets are characterized by increased volatility in correlation to all asset classes, as well as increased shorter timeframes for investment decisions; none of this will improve the probabilities of earning satisfactory returns over a reasonable period of time. Rather, in most instances, these will improve the odds of an opposite outcome. One relatively new factor contributing to the volatility is the impact of algorithm trading which in the US markets is over 60% of the volume.

Another significant change which has occurred over the last 20 years is the domination of hedge funds which now control approximately 2 trillion dollars in equity. With three times leverage this would equate to approximately 6 trillion dollars of the S & P which has a market capitalization of 12 trillion dollars. Well over half of the daily trading activities reported to be from hedge funds. Many of these are mathematically driven and momentum driven. This means they follow the market trends rather than working with economic fundamentals. The market often falls in response to negative headlines often ignoring positive underlying fundamentals. Hedge funds also exaggerate this trend. Once the markets are responding to economic fundamentals hedge funds again follow the trend and exaggerate on the upside. At this moment, hedge funds are exaggerating the negative headlines and markets have fallen in response. It is largely driven by this algorhymic volatility and holding period measures are judged in minutes, if not seconds. Couple this with day trading and you end up with completely irrational trade movements. The ability to predict and explain this sort of swing movement is virtually impossible. In order to function and make objective decisions one has to make other parameters for decision making.

Mr. Handa stated his view is that profits and cash flows will remain the fundamental long term drivers of equity valuations. The probabilities of objectively valuing the economics and sustainability of a business are far better than the alternative of predicting the movements of the market over any given period of time and critical evidence supports this view. He does not ignore global questions and considers how larger trends will impact businesses. He believes it is important to focus on finding a good business to buy at an attractive price. That’s what the Board should be doing as well as the underlying managers. At this time, staff does believe it is necessary to have some tools in place to have a strategic and tactical fund within the equity book. As the plan is currently structured we have significantly outperformed the markets because of our conservative nature and large fixed income exposure. While many of the managers have reduced risk and volatility in the portfolio, under the current structure there’s no way for the fund to mitigate the entire volatility in the equity book. Staff believes that a strategic fund will help mitigate this risk in the equity portfolio in order to protect the fund during market declines. Staff has determined that a minimum of $50,000,000 will be needed to meet this objective. Staff also believes the proceeds should come from two of our managers; Turner Investment Partners and Penn Capital Management to start this strategic fund.

The Board has already determined not to move forward with Turner Investment Partners and Penn Capital Management. Both of these managers have lost approximately 20% growth this month and the aggregate of the managers equate to a little over $45,000,000. Staff cannot say as of today where the money will be deployed as the markets are changing rapidly and staff will need to determine that upon receipt of the funds. Staff might determine not to do anything with the proceeds. Staff will need to have the ability to trade with one of our brokers. Staff believes that the diversity brokers are more than capable of handling these transactions. Legal assistance will handle these affairs and all trades will be signed and authorized by the Chief Investment Officer. Additionally, staff believes the Board should select an Executive Committee. All trades will be reported immediately to the Board and the Board can terminate any and all transactions. Staff also encourages the Board to meet more frequently during this uncertain time so appropriate decisions can be made and staff can keep the Board apprised of global events, our managers and performance of the fund. Staff believes it is imperative that the Board remain proactive in these challenging times. At the last special board meeting staff recommended the

Board redeem from Paulson. Since that decision, Paulson has lost an additional 4.6% in July and according to the Wall Street Journal, Paulson is down 31%. Staff will continue to monitor the markets and provide the Board with daily updates.

Mr. Dubow said there is clearly a disruption that is going on now that can have an enormous impact on us and over a longer period of time it may straighten itself out in some way, but we just can't wait about it and should do something.

Mr. Butkovitz stated that the distinction between this proposal and the status quo is that our long managers are locked into certain strategies and there will be greater freedom to hedge investments or to hang on to cash.

Mr. Bielli asked Mr. Handa how the use of $50,000,000 would have mitigated the losses the fund has currently experienced, and if it was estimated how much would be saved in fees if trading is done in-house.

Mr. Handa said they could have gone out in the end of July or early August when there was no volatility in the options markets and it was a good time to buy protection. He didn't have an exact number but believed savings can be significant. The volatility index has risen over 44% in the last three weeks. The $50,000,000 would have offset most of the losses experienced in the equity portfolio. Even if staff did nothing with the $50,000,000 and left it in cash these assets would have been protected.

Ms. Stukes asked who is going to manage the strategic fund and if Mr. Handa had talked to the Law Department. She was concerned if the Board has the staff to do this. She stated she wasn't comfortable with it and needs to be educated a little more about the process. She asked why they didn't have a regular meeting to discuss this when the consultants were here and if the consultants have they been informed about the decision.

Mr. Handa replied that staff will manage the fund with the approval of the Executive Committee. They will have complete transparency with every trade and transaction as well as approval or disproval at any time. In terms of skill set, Mr. Handa stated he has 10 years of hedge fund experience and believes his background is the reason the Board asked him to come here. As for staff, he believes that anyone that can do private equity, real estate and credit work can also do public equity as the underlying basis of all of these things is the same. Certain members of staff have several years of credit experience as well as finance experience to handle matters like this.

Mr. Butkovitz stated that the Board has been balancing this question with the emergency that exists in the market, and there has been a consensus that the prudent thing to do to protect pensioner's funds is to have some quick acting mechanism at a diversified level. He believed $50,000,000 is not a lot in this fund. It's being taken from managers who have lost 20% in the short term. This will shelter a percentage of the fund from this rollercoaster ride which is being computer driven, and then staff will have the capacity to hedge those investments. The Board will also get a data string on a daily basis in which this block can be judged, versus the managers. It is modest and prudent and will add to the wealth of the information that is available in making these decisions going forward.

Ms. Stukes was concerned why this was an emergency when at the last meeting the Board was told to wait and do nothing. She asked if this is going to be done with just the equity portfolio or are they looking at the whole spectrum.

Mr. Handa explained that his opinion has changed since then as the facts have changed and believes that action is now required. The proposal on the table today only deals with public equities.

Mr. Stagliano asked if $50 million was enough and how long would it take to measure that.

Mr. Dubow said it is enough to give the Board a chance to see how well it works and if it does, it can be expanded later.

Mr. Bielli added that going forward, the public equity managers can be measured as their performance warrants and can be addressed at the upcoming meetings

Mr. Albert asked if the hedge would be based on their positions or will it just be looking for opportunities in the market.

Mr. Handa said it will be a combination of the two.

Ms. Pankey stated that this seems like a continuation of the last meeting in which the Board talked about eliminating managers; looking at their performances and potentially pulling equity from them and investing in other places. She agreed with Ms. Stukes that the Board needs to meet with these managers that they are looking at, with statistics of a particular timeframe. Right now, the market is volatile. She questioned if they are going to look at their performances over a year or six months to make a determination, or just a day to day basis. She stated she has a problem with that and asked what parameters the Board is going to put in place for terminating someone who, in the past, they have been doing business with.

Mr. Stagliano said that no one has suggested they go outside the normal process they have for evaluating managers.

Ms. Stukes stated that isn't true and she still hasn't received an answer to the question she asked before.

Mr. Dubow stated that they shouldn't go outside the normal process for evaluating managers.

Mr. Butkovitz stated there is another factor in that there is an emergency and their principal responsibility is to protect the pensioners and the taxpayers. The managers are a very subordinate consideration and he isn't concerned about due process to money managers. He cares about protecting the capital in the Fund.

Ms. Stukes agreed and said she isn't worried about money managers making money but doesn't want to risk the portfolio based on basis fees and performances. She questioned if they are sacrificing themselves. She also stated that since she is a pensioner sitting at this Board they are not supposed to play Russian roulette with their money and her life. Since it is her responsibility she isn't putting the pension fund on the crap table. They should follow the process they have in place. She hasn't been given answers to questions she has asked. These managers have been doing this job all of their life while the Board has a two staff team. Ms. Pankey asked a question and she wants it addressed going forward. She stated that the Board is not a private fund but a public fund and in it for the long run. They can't operate this on a day to day basis. They all have fiduciary responsibility and liability. That is her concern.

Ms. Pankey agreed and said she understands the crisis. She stated the other issue is when the Board looks at the other managers and decides what they want to pull from them, what is the Board's liability as it relates to their contract with them, if a manager is terminated based on poor performance in a short period of time.

Mr. Stein stated that every one of their contracts is structured to terminate without cause at any time for any reason.

Mr. Dubow stated there are two issues. One is the short term proposal to use the money from the managers the Board agreed to terminate and the longer term issue of how manager termination works and the question of what time period the Board will be looking at. There is a process in place to make sure the funds are protected.

Ms. Pankey stated she wanted to clarify if that process is going to be altered going forward. There are two issues on the table but they are looped together because it was stated this is going to be done on a trial basis and then the Board will look to their other managers.

Mr. Butkovitz said they don't know what the market is going to do next week so he can't answer that question. He believed she was asking for a commitment.

Ms. Pankey said she is asking for a commitment to a process that the Board will follow.

Mr. Stagliano said the Board has a process and always reserves the right to change that process going forward as they see fit.

Mr. Dubow said they aren't talking today about how to do terminations. He asked for any other questions or comments.

Alan Butkovitz made a motion to establish a strategic and tactical fund in public equity in the amount of $50,000,000 and for the Board to appoint a supervisory Executive Committee. Ronald Stagliano seconded the motion.

The motion to establish a strategic and tactical fund in public equity in the amount of $50,000,000 and for the Board to appoint a supervisory Executive Committee carried 6-2.

Mr. Dubow moved on to the issue of the Executive Committee and said he would like to be on the committee. Ms. Stukes, Mr. Stagliano and Mr. Butkovitz also volunteered for the committee. Mr. Dubow asked for a motion.

Mr. Stagliano made a motion that the following Board Members be part of the Executive Committee: Rob Dubow, Carol Stukes, Alan Butkovitz and Ronald Stagliano. Brian Albert seconded the motion.

The motion carried unanimously 8-0.

Alan Butkovitz made a motion to recess the meeting until Wednesday, August 17, 2011, at 1:00 p.m. when the money is available and the Board can decide what to do with it. Ronald Stagliano seconded the motion.

The motion to recess until Wednesday, August 17, 2011 carried unanimously 8-0.
The meeting ended at 10:45 a.m.

The meeting reconvened August 17, 2001 at the Board of Pensions and Retirement in the Board's Conference room at 1:00 p.m. In attendance were:

Board Members: Rob Dubow
Paula Weiss, Designee
Alan Butkovitz
Brian Albert
Celia O'Leary
Carol Stukes
Ronald Stagliano
John Reilly
Veronica Pankey
James Leonard

Also attending: Sumit Handa
Rhonda McNavish
Dominique Cherry
Francis Bielli (via phone)
Joshua Stein
Benjamin Hinerfeld
Andrew Thomas
Catherine Lucey – Daily News
M. Dunn – KYW Radio

The Board briefly summarized the proposal that was approved at the meeting of August 11, 2011, and discussed the amounts of the funds received from Penn Capital Management and Turner Investment Partners.

Ronald Stagliano made a motion to adjourn. Carol Stukes seconded the motion.

The motion to adjourn carried unanimously 8-0. The meeting ended at 1:15 p.m.