

GENERAL RETIREMENT SYSTEM
and
POLICE and FIRE RETIREMENT SYSTEM
BOARD OF TRUSTEES
CITY OF GRAND RAPIDS
MICHIGAN

MINUTES
JOINT MEETING
MAY 21, 2014 – 8:05 a.m.
233 East Fulton

The meeting was called to order by Vice Chairman Craig VanderWall. Other members present: Mr. David Tryc, Mr. Martin Timkovich, Mr. Thomas VanderPloeg, Mr. Michael Hawkins, Mr. Philip Balkema, Mr. William Butts, and Ms. Jane Hofmeyer. Absent: Chairman J. Patrick Scripps and Mr. Walter Gutowski.

Also present: Ms. Peggy Korzen, Executive Director of the Retirement Systems, Ms. Elizabeth White, Deputy City Attorney and Legal Advisor to the Boards, Mr. William Bensus and Mr. Nicholas Sefchok of Wilshire Associates, Inc., Mr. Larry Fumarolo of The Northern Trust Company, and Mr. Gregory Sundstrom, City Manager for the City of Grand Rapids.

Mr. Balkema made the motion to excuse the absences of Chairman Scripps and Mr. Gutowski. The motion was seconded by Mr. Butts and carried.

There were no public comments regarding agenda items.

Mr. Tryc made the motion to approve the minutes of the Joint meeting of March 19, 2014 and the minutes of the Special Joint meeting of April 16, 2014. The motion was seconded by Mr. Hawkins and carried.

Mr. Bensus presented the quarterly performance report to Trustees. In a Capital Market update through May 16, 2014, Mr. Bensus noted that the Federal Reserve continued its tapering program in May, scaling down large-asset purchases to \$45 billion per month. The April unemployment rate decreased to 6.3% and 288,000 non-farm payroll jobs were added; real GDP increased at an annual rate of 0.1% in the first quarter of 2014. Retail sales rose by 0.1% in April, up 4.0% over the past year; housing starts rose 13.2% in April and were up 26.4% from last year; and crude oil was trading near \$100 per barrel. In the U.S. Equity market, YTD, utilities lead U.S. large cap sectors (up 12.0%), while consumer discretionary was the largest laggard (down 4.3%). YTD large cap stocks were outperforming small cap stocks and value stocks were leading growth stocks. In the non-U.S. equity markets, the European Union was still struggling with lackluster economic expansion and lower than expected inflations; and the recent Russia/Ukraine tensions and fallout risk have added to the overall concern across the EU region. In the fixed income market the Fed Funds target rate is 0.0% to 0.25% and the Federal discount rate is 0.75%. As of May 16, 2014, YTD, the S&P 500 was up 2.4%, the Russell 2000 was down 4.8%, the Wilshire 5000 was up 1.9%, the ACWI was up 2.8%, the Barclays Aggregate Bond Index was up 3.5% and the Wilshire RESI Index was up 16.5%. Mr. Bensus commented that he and Vice Chairman VanderWall recently conducted a due diligence visit with PIMCO (Western Asset Management was visited by Vice Chairman VanderWall and Mr. Sefchok) and they continue to be impressed with their operations and how they are addressing some of the recent concerns that involved their firms. Mr. Bensus recommended no changes at this time, but to keep a watchful eye on them. Following a review of market returns, the Quarterly Funds Evaluation of the investment managers of the General and Police & Fire Retirement Systems was conducted.

**SUMMARY OF INDEX RETURNS
PERIODS ENDED 03/31/14**

<u>Index</u>	<u>QTR.</u>	<u>1 YEAR</u>	<u>3 YEARS</u>	<u>5 YEARS</u>	<u>10 YEARS</u>
S&P 500	1.80	21.86	14.65	21.15	7.41
RUSSELL 2000	1.12	24.90	13.19	24.31	8.53
NAREIT GLOBAL RE INDEX	4.01	2.18	8.48	N/A	N/A
MSCI ACWI X-US	0.51	12.31	4.15	15.52	7.12
BARCLAYS AGGREGATE	1.84	-0.10	3.75	4.80	4.46
DJ UBS COMMODITY INDEX	6.99	-2.09	N/A	N/A	N/A
91 DAY T-BILLS	0.01	0.07	0.08	0.11	1.65

General Retirement System

Asset Commitments as of 03/31/14:

Domestic Equity	46.9%
Fixed Income	27.6%
Cash Equivalents	0.1%
Real Estate	4.8%
Private Equity	0.9%
International Equity	15.8%
Commodities	3.9%

Asset Allocation to Managers:

NTAM	14.1%
PIMCO	6.4%
Wellington Management Company	12.2%
Ziegler Capital Management	14.2%
Baird Advisors	14.0%
Western Asset Management	13.6%
Cash Account	0.1%
Neuberger Berman	15.8%
CBRE Clarion	4.8%
Adams Street Partners	0.6%
FLAG Capital	0.2%
Wellington Commodities	3.9%

Quarterly Summary of the General Retirement System

	<u>Market Value</u> <u>03/31/14</u>	<u>Market Value</u> <u>12/31/13</u>	<u>Market</u> <u>Difference</u>	<u>Rate of</u> <u>Return</u>	<u>Universe</u> <u>Ranking</u>
Retirement System	\$417.2 million	\$411.6 million	\$5.6 million	2.50%	13 th percentile
Total U.S. Equity	\$195.6 million	\$201.5 million	(\$5.9 million)	2.69%	6 th percentile
Total Non-U.S. Equity	\$65.8 million	\$65.0 million	\$800 thousand	1.16%	25 th percentile
Total Fixed Income	\$115.1 million	\$106.3 million	\$8.8 million	2.67%	20 th percentile
Total Real Estate	\$20.2 million	\$19.6 million	\$600 thousand	3.05%	46 th percentile
Total Private Equity	\$3.9 million	\$3.4 million	\$500 thousand	5.42%	N/A
Total Commodities	\$16.2 million	\$15.6 million	\$600 thousand	3.36%	N/A
NTAM	\$58.7 million	\$62.7 million	(\$4.0 million)	1.77%	70 th percentile
PIMCO	\$26.6 million	\$25.9 million	\$700 thousand	2.84%	16 th percentile
Wellington Mgmt. Co.	\$50.9 million	\$51.2 million	(\$300 thousand)	3.50%	8 th percentile
Ziegler Cap. Mgmt.	\$59.4 million	\$61.7 million	(\$2.3 million)	2.90%	14 th percentile
Neuberger Berman	\$65.8 million	\$65.0 million	\$800 thousand	1.16%	40 th percentile
Baird Advisors	\$58.4 million	\$51.3 million	\$7.1 million	2.20%	28 th percentile
Western Asset Mgmt.	\$56.7 million	\$55.0 million	\$1.7 million	3.13%	10 th percentile
CBRE Clarion	\$20.2 million	\$19.6 million	\$600 thousand	3.24%	46 th percentile
Adams Street Partners	\$3.0 million	\$2.5 million	\$500 thousand	29.03%	N/A
FLAG Capital	\$903 thousand	\$835 thousand	\$68 thousand	-7.40%	N/A
Wellington Commodities	\$16.1 million	\$15.6 million	\$500 thousand	3.36%	N/A

Police and Fire Retirement System

Asset Commitments as of 03/31/14:

Domestic Equity	47.1%
International Equity	15.0%
Fixed Income	27.8%
Cash Equivalents	0.3%
Real Estate	5.1%
Private Equity	1.0%
Commodities	3.8%

Asset Allocation to Managers:

NTAM	13.9%
PIMCO	6.3%
Wellington Management Company	12.8%
Ziegler Capital Management	14.0%
Baird Advisors	14.5%
Western Asset Management	13.3%
Cash Account	0.3%
Neuberger Berman	15.0%
CBRE Clarion	5.1%
Adams Street Partners	0.7%
FLAG Capital	0.2%
Wellington Commodities	3.8%

Quarterly Summary of the Police & Fire Retirement System

	<u>Market Value</u> <u>03/31/14</u>	<u>Market Value</u> <u>12/31/13</u>	<u>Market</u> <u>Difference</u>	<u>Rate of</u> <u>Return</u>	<u>Universe</u> <u>Ranking</u>
Retirement System	\$394.5 million	\$387.7 million	\$6.8 million	2.50%	13 th percentile
Total U.S. Equity	\$185.7 million	\$194.2 million	(\$8.5 million)	2.68%	6 th percentile
Total Non-U.S. Equity	\$59.3 million	\$58.6 million	\$700 thousand	1.16%	25 th percentile
Total Fixed Income	\$109.7 million	\$97.1 million	\$12.6 million	2.68%	20 th percentile
Total Real Estate	\$19.9 million	\$19.3 million	\$600 thousand	3.24%	46 th percentile
Total Private Equity	\$3.9 million	\$3.4 million	\$500 thousand	5.42%	N/A
Total Commodities	\$15.0 million	\$14.5 million	\$500 thousand	3.36%	N/A
NTAM	\$55.0 million	\$60.2 million	(\$5.2 million)	1.80%	63 rd percentile
PIMCO	\$25.0 million	\$24.3 million	\$700 thousand	2.84%	16 th percentile
Wellington Mgmt. Co.	\$50.3 million	\$50.3 million	\$0	3.49%	8 th percentile
Ziegler Cap. Mgmt.	\$55.3 million	\$59.2 million	(\$3.9 million)	2.91%	14 th percentile
Neuberger Berman	\$59.3 million	\$58.6 million	\$700 thousand	1.16%	40 th percentile
Baird Advisors	\$57.2 million	\$46.2 million	\$11 million	2.20%	28 th percentile
Western Asset Mgmt.	\$52.5 million	\$50.9 million	\$1.6 million	3.13%	10 th percentile
CBRE Clarion	\$19.9 million	\$19.3 million	\$600 thousand	3.24%	46 th percentile
Adams Street Partners	\$3.0 million	\$2.5 million	\$500 thousand	29.04%	N/A
FLAG Capital	\$903 thousand	\$835 thousand	\$68 thousand	-7.40%	N/A
Wellington Commodities	\$15.0 million	\$14.5 million	\$500 thousand	3.36%	N/A

The report was received and filed by the Chairman.

Mr. Bensur next addressed the Asset Allocation analysis that was presented to Trustees last month. Mr. Sefchok reiterated that Wilshire's recommendation is Alternative A: 22.5% Equity; 22.5% Non-U.S. Equity; 5.0% Private Equity; 25.0% U.S. Core Fixed Income; 5.0% REITS; 5.0% Commodities; 10.0% TIPS and 5.0% MLPs. Mr. Bensur stated that if Trustees take no action with their current asset allocation, the advantages the plans have will deteriorate over time. While this alternative does not significantly increase the return, it lowers risk by about 1.25%; this will help the portfolios if the marketplace enters an inflationary period. The biggest change from the current policy is in the equity portion; currently it is 60% and Alternative A proposes a 50% allocation to equity (split equally between U.S. and Non-U.S.). Wilshire recommended this change to eliminate the home country bias. If the Trustees decide to implement Alternative A, Mr. Bensur stated they would try to find a suitable manager for ADRs (American Depository Receipts) which would represent 7.5% of the 22.5% allocation to non-U.S. equity. Mr. Balkema commented that the U.S. economy is doing well right now, so why should Trustees eliminate the home country bias. Mr. Bensur stated that although the economy is doing well now, the plans are designed for the long-term and there is no compelling reason to

believe that the U.S. economy will continue to fare better than other countries over long periods of time. Mr. Sefchok reviewed the educational report on Master Limited Partnerships (MLPs) and Treasury Inflation Protected Securities (TIPS). He noted that an MLP is a publicly traded partnership that receives special treatment under the U.S. tax code. The majority of MLPs today are energy and natural resources related businesses. An MLP is publicly traded on a stock exchange and combines tax benefits of partnerships with the liquidity of equities. The ownership of a share makes the purchaser a limited partner. The legal structure makes ownership interests more marketable and the general partner operates the business. Mr. Bensus reviewed the structure of energy and natural resources MLPs and the investable market. The two major independent MLP index providers are Alerian and S&P. He noted that the tax advantages of MLPs are that a significant portion of initial cash distributions are considered a return of capital and are tax deferred and the structure avoids taxation at the corporate level. The disadvantage of MLPs is that some tax-exempt institutional investors face a complication as MLPs may produce unrelated business taxable income (UBTI) and according to the IRS, "if an exempt organization regularly carries on a trade or business not substantially related to its exempt purpose...the organization is subject to tax on its income from the unrelated trade or business." However, Mr. Sefchok noted that this type of risk is mitigated for public fund investors. MLP managers can take steps to limit or manage the UBTI by establishing different investment vehicles for holding the assets. Each individual partnership has risks which generally include declines in throughput volumes, commodity price risk, execution risk associated with natural disasters/acquisition/regulatory approvals and interest rate risk. Some of the general risks to the asset class include: 1) possible changes in tax law; 2) commodity price sensitivity; 3) fund flows; and 4) UBTI for tax-exempt investors. Mr. Bensus reviewed the implementation options currently available, which include: diversified, open-end funds; separate accounts; closed-end funds; private partnership (direct MLP); private partnership (total return swaps); and exchange-traded notes. He stated that MLP yields in general have been declining for the last 15 years from approximately 9% to 6%; however, the MLP yield spreads over the Barclays U.S. Treasury Index remains above the historical average. Correlation statistics show a potential diversification benefit from investing in MLPs. From a return/risk perspective, MLPs are very attractive and can help provide diversification benefits with some inflation hedging properties and low commodity price exposure. MLPs are however a relatively new asset class in the institutional marketplace and warrant a cautious approach. Mr. Tryc commented that there have been articles written recently about the risks involved with MLPs. Mr. Sefchok agreed that there are risks involved with MLPs; however, there are ways to mitigate the risks. Mr. Bensus stated a good way to help mitigate these risks is to do the due diligence on the prospective MLP manager to ensure their operations area is knowledgeable. Mr. Sefchok then explained that TIPS are inflation indexed bonds issued by the U.S. Treasury; principal and interest on the bonds increase with inflation and decrease with deflation. TIPS provide protection relative to anticipated inflation and they may also provide protection in down equity or "flight to quality" markets. The size of the TIPS market has increased from \$48 billion at the end of 1997 to nearly \$844 billion as of December 31, 2013. He reviewed the mechanics of TIPS and noted that TIPS are attractive due to their lower correlation with other asset classes. TIPS provide several benefits when included in investment portfolios: 1) inflation hedge; 2) partial deflation hedge; and 3) diversification. TIPS are considered a low return asset class. Mr. Sefchok reviewed Wilshire's top-rated TIPS investment managers. Mr. Balkema asked how the new asset allocation would be implemented if Trustees chose to make a change from the current allocation; Mr. Bensus stated that there is no reason to rush in implementing any changes. He suggested that Trustees make any changes thoughtfully, as they have done in the past. He stated that Trustees will need to decide today whether or not they wish to continue the relationship with Ziegler Capital Management (ZCM) as it ties into any potential asset allocation changes. Once a decision is made regarding ZCM, he does not feel there is any reason to wait on implementing a TIPS allocation as they are fairly liquid. MLPs however should be entered into more carefully; he stated it would be nice to have any asset allocation changes in place by the beginning of 2015. Following Trustee discussion, Mr. VanderPloeg made the motion on behalf of the Police & Fire Retirement System to implement Alternative A as outlined in the Asset Allocation Analysis provided by Wilshire Associates at the April 16, 2014 Special Joint meeting. The motion was seconded by Mr. Hawkins and carried. Mr. Hawkins made the motion on behalf of the General Retirement System to implement Alternative A as outlined in the Asset Allocation Analysis provided by Wilshire Associates at the April 16, 2014 Special Joint meeting. The motion was seconded by Ms. Hofmeyer and carried. Trustees asked if there would be an increase in fees due to the new asset allocation structure; Mr. Bensus stated there should not be a significant change in fees to investment managers based on the new asset allocation. Mr. Timkovich commented that he is concerned that the portfolios will be sacrificing returns to mitigate more risk. Mr. Bensus stated that Alternative A, while keeping roughly

the same expected return as the current portfolio, does so with dramatically lower risk; this is a benefit, not a cost of implementation. Mr. Bensur stated that Trustees' options with ZCM are: 1) keep them; 2) terminate them and roll the funds into the existing structure; and 3) terminate them and hire a new equity manager. Vice Chairman VanderWall stated that ZCM has clearly changed from when Trustees initially hired them. Mr. VanderPloeg stated he was glad that their most recent quarter went well; however, their overall performance has suffered and the original staff that ran the portfolios are being phased out. Mr. Hawkins asked Mr. Bensur what his thoughts are regarding ZCM. Mr. Bensur stated he is frustrated with ZCM due to their organizational and performance issues. Mr. Tryc suggested perhaps hiring a mid-cap equity manager; Mr. Bensur stated Trustees could do that however he felt that the portfolios are not lacking because they don't have an allocation to a mid-cap manager. Trustees could revisit that issue at a later date if they wish. Mr. Fumarolo stated that the Retirement Systems have ongoing agreements with The Northern Trust Company for transitioning portfolios. The process would be fairly easy and cross-trades can be used to keep costs down. Following Trustee discussion, Mr. VanderPloeg made the motion on behalf of the Police & Fire Retirement System to terminate the relationship with Ziegler Capital Management and utilize The Northern Trust Company as transition manager to divide the funds in the portfolio proportionately between existing accounts. The motion was seconded by Ms. Hofmeyer and carried. Mr. Hawkins made the motion on behalf of the General Retirement System to terminate the relationship with Ziegler Capital Management and utilize The Northern Trust Company as transition manager to divide the funds in the portfolio proportionately between existing accounts. The motion was seconded by Mr. Butts and carried. Mr. Bensur stated that ZCM should be notified to stop trading immediately and then terminate the relationship with them as early as the contract permits. Mr. Balkema stated that when the funds are appropriated to the other managers, they should be made aware that these additional funds may not be permanent. Ms. Korzen noted that Trustees previously suggested having an MLP and TIPS manager come to a future Board meeting to make an educational presentation to Trustees. Mr. Bensur asked if that should be scheduled for the June meeting; Ms. Korzen stated it might be prudent to have the MLP and TIPS managers come and present at the August 2014 Joint Board meeting as Mr. Bensur will be at that meeting and the June meeting is already quite full. Mr. Bensur stated that he would coordinate having Harvest Fund Advisors (MLP manager) and Brown Brothers (TIPS manager) come to the August 2014 Joint Board meeting and present an educational session to Trustees.

Ms. Korzen noted that Mr. Craig VanderWall attended the 2014 Spring MAPERS Conference. Board approval was requested for attendance at the upcoming BLB&G securities monitoring seminar to be held June 17. Mr. Butts, Mr. Tryc and Mr. VanderPloeg will be attending this seminar. Mr. Balkema made the motion to approve Mr. VanderWall's attendance of the aforementioned conference, and attendance of the BLB&G seminar by Mr. Butts, Mr. Tryc and Mr. VanderPloeg, per the Trustee Training, Educational Development and Due Diligence policy. The motion was seconded by Mr. Hawkins and carried.

There were no comments on items not on the agenda.

The meeting adjourned at 9:53 a.m.

The next Joint Meeting of the General and Police & Fire Retirement System Boards will be held Wednesday, June 18, 2014, at 8:05 a.m., 233 East Fulton, Grand Rapids, Michigan.

Peggy Korzen
Executive Director
General and Police & Fire Retirement Systems

05/21/14