TOWN OF PALM BEACH

MINUTES OF THE INVESTMENT ADVISORY COMMITTEE MEETING
HELD ON WEDNESDAY, OCTOBER 27, 2009 AT 2:30 P.M.
AT THE EMERGENCY OPERATIONS CENTER (EOC), THIRD FLOOR,
CENTRAL FIRE-RESCUE STATION, 355 SOUTH COUNTY ROAD

I. CALL TO ORDER AND ROLL CALL

The Investment Advisory Committee Meeting was called to order on Wednesday, October 27, 2009 at 2:30 p.m.

ATTENDEES:
Chairman Michael F. Andrews
William John Mikus
Dr. Heinz L. Gundlach
Benton P. Bohannon
Steven Alexander CTP, CGFO, Managing Director, PFM
David Jang, Senior Managing Consultant, PFM
Jane Struder, Finance Director
Cheryl Somers, Assistant Finance Director
Melissa Morgan, Recording Secretary

ABSENT:

Bernard R. Panfel

II. PLEDGE OF ALLEGIANCE

Chairman Michael F. Andrews led the pledge of allegiance.

III. APPROVAL OF THE AGENDA

Motion by Chairman Andrews for approval of the agenda.
Motion seconded by Mr. Bohannon
Motion carried unanimously

IV. COMMUNICATION FROM CITIZENS – 3 MINUTES PLEASE.

There was none

V. APPROVAL OF MINUTES FROM AUGUST 17, 2009.

Motion by Mr. Mikus for approval of the agenda.
Motion seconded by Mr. Bohannon
Motion carried unanimously

VI. PFM ASSET MANAGEMENT

1. Investment Performance Review

PFM: Discussed performance report as of September 30, 2009, with the committee. On page A2 they discussed the treasury yield curve which shows an increase in interest rates. They informed the committee that Washington is changing a lot of factors that affect the interest rates.

PFM: Discussed strategies they are going to propose on page A-3 which reflects the downward sloping yield curve affecting the term of maturity.

Mr. Bohannon asked PFM: Where is the optimal place on the curve if you had no restrictions on what you are doing?

PFM replied to Mr. Bohannon: Probably the three to five year range would be a good range considering the market value situation and the capital gain position between point A and point B. Also right now we are at that one year area and we will do as much as we can with that. Even though the initial yield on the investment looks low we are hoping to add more basis points of total return gain to those numbers so we can do the best we can with those dollars for you. This position will be beneficial to the Town next year when the interest rates rise again because it will be less likely to lose a tremendous amount of market value. The problem with rising interest rates as you know as rates go up we lose market value. Also another problem we are facing is the coupon rates are very small. Small coupons give small cushion price devaluation so we need to be careful with that. That is our strategy going forward.

PFM: Discussed the spread analysis chart on page A-4. This chart shows the spread between two years of Corporate and Federal Agency Investments during the time period of September 2008 and September 2009.

PFM: The “AA” bond has really come down from last year when the spreads were about 200 basis points. Therefore, the market does not perceive much risk between agencies at this point. The other areas where the spreads have come down are the “AA” corporate bonds. There is a good spread as it improves but we will be a little conservative on corporate bonds because there are still more shoes to drop but it is improving.

Dr. Gundlach asked PFM: When you say corporate do you mean financial or non-financial?

PFM replied to Dr. Gundlach: Both

Dr. Gundlach asked PFM: Are there more shoes to be dropped in non-financial, do you think? Or do you think in financial because of commercial real estate.

PFM replied to Dr. Gundlach: Yes, financial because of commercial real estate.

Dr. Gundlach asked PFM: Do you also see that in non-financial?

PFM replied to Dr. Gundlach: Yes we are, in certain limited areas and we are seeing non-financial access the market in a more efficient market this year. Also Dr. Gundlach you asked about non-financial, some of them are homebuilders and auto suppliers. Those are markets that have been stressed.

Dr. Gundlach replied to PFM: These two I consider a great risk and if you stay away from those, the rest of the corporate world in my opinion, is out of the worst.

PFM replied to Dr. Gundlach: The spread shows that on page A-4.

Chairman Andrews asked PFM: As you roll down the yield curve and you make different investments can you show me the sizes of the investment we are going to have? Or are we going to have big chunks? Do we wait until the next part comes in? Or are you constantly rolling these over?

PFM replied to Chairman Andrews: Let’s turn to the monthly report to answer that question specially. It is a one million dollar block.

Chairman Andrews replied: OK that is fine. I would be concerned if they where larger sizes?

PFM replied: There is not nine million in one block. There are several pieces.

Mr. Bohannon asked PFM: In reference to your mandate, is the mandate one year? Is that a specific mandate or is that a duration mandate?

PFM replied to Mr. Bohannon: That is a duration mandate that we received at the beginning of this engagement.

Mr. Bohannon replied to PFM: So you could have longer maturities if you wished?

PFM replied to Mr. Bohannon: Yes, the overall duration has to be around one.

Chairman Andrews asked PFM: On page B-2. The benchmark is a three month U.S Treasury bill. Did we agree on that to be our benchmark? That is kind of short if you are out there for one year.

PFM replied to Chairman Andrews: Yes it is short so we are going to make it one year. This page was just a temporary page until we got set up and we bought the securities. Now we are set up and they are fully funded and now we will go to a total return report then we will go to the same treasury index as the portfolio. The duration currently is about .99.

Mr. Bohannon asked PFM: In reference to page B-1 bullet four. There might be value in extending the maturities based on liquidity preferences? What are you saying there?

PFM replied to Mr. Bohannon: We are saying that we are putting aside the liquidity needs and the Towns needs and we would like to extend further than the one year.

Mr. Bohannon asked PFM: So we are going to change the benchmark to a one year. Is that correct?

PFM replied to Mr. Bohannon: Yes we are.

Chairman Andrews asked Ms. Struder: Do we need a policy on that?

Ms. Struder replied to Chairman Andrews: That is a part of the investment policy and we will go over that later.

Chairman Andrews replied to Ms. Struder: That I fine and that will be a better place for it anyway.

Chairman Andrews asked PFM: What is your comfort level in investing for us for the past two quarters? Also what do you anticipate for the next quarter we are in? Do you anticipate any problems from an operational standpoint?

PFM replied to Chairman Andrews: I am not aware of any operational problems. We try and get the trade tickets from every trade and everything is on line. We have been working with Cheryl on some of the accounting and she has been to our training classes in Orlando. We just want to make sure everything is running smoothly.

2. Proposal For Investment

PFM: Discussed the handout, Market Update and Investment Outlook. On page 16 it shows our recommended portfolio structure for about the next 5 to 6 months with the maturities and their yields.

PFM: We have been looking at the short term assets given to the Town and we are at the low end because cash receipts have not come in yet. We are just offering some suggestions at to what could be done on page 16.

Mr. Bohannon asked PFM: In terms of short term are you going to be breaking the total fund into two chunks? Core and short term, which short term is about 22 million?

PFM replied to Mr. Bohannon: Yes that is correct.

Dr. Gundlach asked PFM: You handle just the ten million?

PFM replied Dr. Gundlach: Yes, that is correct.

Chairman Andrews asked PFM: Just to review a few things. You were hired to invest the first ten million. We had Wachovia doing our pure money market. You came in to take the slot between the money market account and we have another doing the one to three year. So you can take that slot. What area of money are you talking about here?

PFM replied to Chairman Andrews: This would fall into the Evergreen bucket, which is really short term, earning one basis point. We have some other money market accounts that are earning about twenty basis points. We just wanted give you some options to improve those short term assets.

Chairman Andrews asked PFM: Tell us how this chunk of money is going to fit in with the current chunk of money you are in managing. Tell me how close they would be. Or would they not be close at all? Your current proposal is completely different from what you gave us before. There might be some overlap but you did not really go into the short term.

PFM replied to Chairman Andrews: There is a few different ways to approach this because the money market funds are in general pretty much at zero. We will improve this investment tremendously by laddering it out. There will be plenty of maturities occurring so there will be plenty liquidity. We also are money managers that have a money market account. The account is a 227 account that is designed only for local investors which makes it safer for you so you are not involved with other corporate investors. Those are earning about 15 to 20 basis points depending on which one you choose. Those are two good additional options to the overnight Evergreen rate at this point.

Chairman Andrews asked PFM: Are you going to be firm with the ten million or are you willing to take slightly less?

Ms. Struder asked Chairman Andrews: Are you referring to the additional ten million? Well if you wanted to completely liquidate the entire Evergreen fund it would not necessary hurt our feelings especially if we have the overnight liquidity that we need.

Chairman Andrews replied to Ms. Struder: I think that would be fair. This is an administrative decision and between the finance department of the Town of Palm Beach and PFM. I would like a board indication if we support the Town for pursing this change or do we want to hold things currently until we have another meeting?

Dr. Gundlach replied to Chairman Andrews: My view is it is a very hard time for the short term and we earn nothing. I would prefer all the money to be managed by one firm except what the Florida League has to manage. I feel comfortable with what these gentlemen have been doing so far, I have been observing all of this. I would not object, in fact I would recommend PFM.

Mr. Bohannon replied to Dr. Gundlach: I mentioned earlier why I like PFM so much. They have their own separately managed accounts. We know where they are and we know they are in good hands. I am not are sure If I would go with putting it all with one manager.

Chairman Andrews gave an overview: The original reason why PFM got the first ten million is because we wanted some diversification. We are going from three firms to two firms.

Mr. Mikus asked PFM: What are you charging us on the ten million right know?

PFM replied to Mr. Mikus: 6.5 basis points

Mr. Bohannon asked PFM: What is in your prime series money market funds?

PFM replied to Mr. Bohannon: We have a government fund which consists of treasuries FDIC papers. So everything in the fund is some type of governmental investments.

Chairman Andrews asked the committee: Are there any more questions for PFM regarding the investments?

Ms. Struder asked PFM: Would your fees schedule still be the same as your original quote for the first ten million?

PFM replied to Ms. Struder: Yes it would, whatever was in the original contract for the original securities. Yes good point there is no fee for the money market account. Whatever is in the money market account it has its own fees.

Ms. Struder asked Chairman Andrews for a motion:

Move the funds to from Evergreen to PFM up to the full balance based on the PFM recommended portfolio structure.
The motion was seconded by Mr. Mikus
The motion was carried unanimously.

3. Investment Policy

Mr. Bohannon asked PFM: We are not at normal times when it comes to commercial paper. In the past what role did commercial papers have in money market accounts in the investment process?

PFM replied to Mr. Bohannon: For the individual portfolio the max would not be higher than 30%, in a short term portfolio.

The Committee and PFM discussed several changes in the Investment Policy Draft-Handout.

Ms. Struder informed PFM: The Investment board Chairman reports to the Town Council once a year in January and we also send monthly reports to the Town Council.

PFM informed the committee: That a maximum of 25% of available funds may be invested in intergovernmental investment pool.

Mr. Mikus asked PFM: We might have to increase this? Increasing it does not make nervous.

Mr. Bohannon commented: We should go to 50% then? Is this running against best practices? Or what is the thinking behind 25%?

PFM replied to Mr. Bohannon: 25% is good from this standpoint because these funds are very well placed but you can you can run into a negative position and from a liquidity standpoint.

Ms. Struder informed the Committee: These numbers are a little distorted because this time of year the cash is flow is down in the Evergreen account. Between November and December the eighty five million will go to about one hundred million. The Florida League of Cities will stay the same.

Chairman Andrews asked the Committee: Are we willing to make a change on that 25%?

Mr. Bohannon replied to Chairman Andrews: Are you willing to be in violation for a period of time?

Mr. Mikus replied to Chairman Andrews: You can say you can’t go over a certain percentage amount for a certain period of time, one year.

Mr. Bohannon replied to Mr. Mikus: You would still be in violation

Mr. Mikus replied it would only be seasonally. Therefore, we would only be in violation seasonally.

PFM replied to Committee: You should put in language at the time of purchase or the time of initial investment that meets that guideline. At the time Ms. Struder and Mrs. Somers purchase them they might have over 125 million.

Chairman Andrews replied to PFM: Good point, I like the language and that solves the seasonal issues.

Chairman Asked Ms. Struder: Are we at a point where we can give this to the Town Attorney for review?

Ms. Struder replied to Chairman Andrews: Yes that would be the next step. Give a copy to the Town Attorney for review then to the Town Council for adoption, in December or January.

Chairman Andrews asked Ms. Struder: Is there anything else you need from us at this point in time?

Ms. Struder replied: No

Chairman Andrews replied to PFM: Thanks for coming and we appreciate your knowledge and depth regarding funds. Thank you for keeping us in best practices so we don't do anything crazy.

Mr. Andrews asked the committee for a break.

VII. MONTHLY INVESTMENT REPORT

Mrs. Somers: The $85.5 million dollars has a fiscal year blended rate of return of 2.7% which compares to 3.37% for the end of FY 08. Total earning are 2.864 million for the fiscal year.

The third page of the handout shows an interest analysis that we have prepared and includes the interest earnings including FMIVT in the mix of the investments versus if we would have been invested with Evergreen funds only.

Chairman Andrews asked Mrs. Somers: In the past we only had FMIVT but now because we have PFM we need to mention them in the mix. Therefore, I think we can go against our benchmark. For example, our benchmark is six month T bills we did better than Evergreen. I do not have any problems with doing that. At the last meeting we agreed about using six month. I think we need to thank the Finance Department for doing such a wonderful job this year. At the end of 2008 there was a loss that FMIVT took on the securities lending fund, as they mature, which is relatively short term the losses would show up in this year numbers.

Chairman Andrews asked Ms. Struder: Regarding the citizen's report I noticed for the 2009 budget the interest earnings was going to be about one million where did that number come from?

Ms. Struder replied to Chairman Andrews: We usually take what we think the interest rates are going to be and multiply it by what we think the reserves are going to be. We underestimated these numbers to our benefit for that year.

Dr. Gundlach replied to Ms. Struder: You under estimated?

Ms. Struder replied to Dr. Gundlach: For this current year. We underestimated the budget.

Dr. Gundlach asked Ms. Struder: Is it actually higher?

Ms. Struder replied to Dr. Gundlach: It is much higher.

Mrs. Somers asked Ms. Struder: Is that the general fund Chairman Andrews is referring to?

Ms. Struder replied to Mrs. Somers: Yes

Chairman Andrews: We did much better than we have proposed. We had a good year.

Chairman Andrews asked the Committee: Are there any more questions for Mrs. Somers at this point? Ok hearing none let's move on to the next item.

VII. UPDATE ON REBLANCING OF OPEB TRUST FUND

Ms. Struder discussed the handouts. The first one was done on August 20th. I received instructions yesterday and forwarded them onto the money managers and the custodians and I did the final part yesterday.

Mr. Bohannon asked Ms. Struder: I am a little confused you received instructions from whom?

Ms. Struder replied to Mr. Bohannon: Prime Buchholz. They tell me which funds need to be rebalanced and they tell me the amounts to transfer. They prepare a letter of instruction and I send it the investment company and to the custodian.

Mr. Bohannon asked Ms. Struder: The only thing I remember from the last meeting is that we should be rebalancing with no discussion on how to rebalance. That is all I recall. I remember a discussion about getting rid of Western Asset Core Asset and the minutes indicate that we are going to get rid of half and then the balance by the next meeting.

Chairman Andrews told Mr. Bohannon: Mr. Higman wanted us to keep the basic allocation like what we had a year ago. Therefore, we would not have to do any changes to the allocation.

Mr. Bohannon asked the Committee: Why did we not rebalance in March being that we were way under equities and there was nothing done about it?

Mr. Mikus replied to Mr. Bohannon: We were not fully allocated in March we were still allocating money in March?

Chairman Andrews replied to Mr. Bohannon: We started out with 16 million in the fund this year. It has improved considerably being that it was down by 30% last March.

Mr. Bohannon asked the Committee: Did Prime Buchholz send out instructional booklets? Why were there no instructions forth coming in March when the same situation existed? The impression I got was that nobody wanted anything to go into equities.

Chairman Andrews replied to Mr. Bohannon: We would have been in equities if he would have stayed with his original allocation.

Mr. Bohannon asked the Committee: How does the rebalancing occur? Is it discussed, is it debated, do you say let's do that let's do this? Do we receive an instructional list from Prime Buchholz?

Ms. Struder replied to Mr. Bohannon: Mainly he comes before the Committee and presents the quarterly report and the committee would decide to rebalance or not to rebalance at that time.

Mr. Bohannon said to the Committee: The entire six month period Prime Buchholz has done nothing.

Chairman Andrews replied to Mr. Bohannon: I do not want to micro manage them. If we do not like them we can change companies. They have been doing it for only two years and they started at the worst time in the market and they have done OK. Could they have done better? Possibly.

Mr. Bohannon asked the Committee: Why has Prime Buchholz allocated no money to the Sound Shore and Brandywine funds. I am sure he has a good reason I just wanted to know why? Then he puts five hundred thousand into some stocks.

Mikus replied to Mr. Bohannon: Just to give you some history perception Prime Buchholz came in and he gave us their recommended managers. They gave a good presentation. They argued why these were their manager selections and went back and forth. I believe they were more pro Western Asset than Pimco. We ended up pushing them to put more money with Pimco. It was kind of like a give and take. The allocation is a two- way conversation.

Dr. Gundlach commented: The problem I have is I do not know what I own. Some of these money managers are good some are bad and some of the good ones are sometimes bad. At least I would like to know what I own, ten million, twelve million. I think we should have three direct managers so we know what we have.

Mr. Mikus commented: We have sixteen million and the most efficient effective way is to hire using a mutual fund format. The reason why we have Prime Buchholz is that we do not want to take the responsibility of selecting different managers. They have done all the research and they have a good track record.

Mr. Mikus replied to Mr. Gundlach: You were not on the board then, but they were very clear and they proved why they add value.   You can call him direct and he will send you a binder of all the managers how and why and what their portfolios looks like.

Chairman Andrews asked the Committee: I think we should wait until the next meeting to discuss these inquires. Are there any specific issues regarding the rebalancing of the OPEB fund? We had a lot of discussion but does anybody have a motion, or does anybody want to do anything? Hearing none we can move on.

IX. NEXT MEETING DATE

Ms. Struder asked the Committee: Can we agree on some dates for the meetings for the year. They are in the back up? There are three dates in December, three in February and three in May and August. I picked these dates because they are around the pension board meetings.

Ms. Struder: OK so we will have Prime Buchholz and Florida League of Cities at the next meeting. There is no need to bring back PFM so quickly.

X. ANY OTHER MATTERS

Chairman Andrews asked the Committee: Are there any other matters to be discussed today? There were none.

XI. ADJOURMENT

Chairman Andrews made a motion to adjourn at 4:30 p.m.
Mr. Mikus seconded the motion
The motion was carried unanimously.