TOWN OF PALM BEACH

Finance Department

MINUTES
OF THE INVESTMENT ADVISORY COMMITTEE MEETING
MONDAY, AUGUST 17, 2009
10:30 a.m.
Emergency Operations Center

I. CALL TO ORDER AND ROLL CALL.

The Investment Advisory Committee Meeting was called to order on Monday August 17, 2009 at 10:30 A.M.

ATTENDEES:

Chairman Michael F. Andrews
Committee Member Gundlach
Committee Member Bohannon
Sean Higman, Prime Buchholz
Jane Struder, Finance Director
Cheryl Somers, Assistant Finance Director
Melissa Morgan, Recording Secretary

ABSENT:
Committee Member Bernard R. Panfel
Committee Member William J. Mikus

II. PLEDGE OF ALLEGIANCE

Chairman Michael F. Andrews led the pledge of allegiance.

III. APPROVAL OF AGENDA

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

IV. COMMUNICATION FROM CITIZENS – 3 MINUTES LIMIT PLEASE

There were none.

V. APPROVAL OF MINUTES FROM APRIL 3, 2009 MEETING

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

VI. INTRODUCTION OF NEW COMMITTEE MEMBERS

Chairman Andrews informed the committee of the two new council members, Mr. Bohannon and Mr. Gundlach. Also, he asked them to give an little introduction of themselves today and again at the next meeting when the other members are present.

Mr. Bohannon: With respect to my qualifications I was in the fixed income industry working for Solomon Brothers for 18 years. I have also worked in the Hedge Fund industry working with fixed income for ten years which was all prior to me becoming a permanent resident in Palm Beach.

Mr. Gundlach: I am a resident of Palm Beach for thirty years. I worked on the Wall Street and with Morgan Stanley. I was the C.E.O of a property corporation. Prior to that I started out working for a steel company in Germany where I graduated from Law School.

VII. REQUEST TO DIVEST FROM COMPANIES THAT DO BUSINESS WITH SUDAN OR IRAN'S ENERGY SECTOR.

Chairman Andrews entertained a motion to ask the Town to:

1. Divest from doing any business with Sudan and Iran's Energy Sector.
2. Have no future involvement with them.
3. Send out all the information to the sub-manager in order for them to be in compliance.

Mr. Higman: Referenced Florida Statue 215.473.47 Section 3, which relates to co-mingled funds. According to the statues when you are dealing with co-mingled funds you need to send a letter to the co-mingled fund asking them to divest. The law calls them "scrutinized funds." They are quarterly reports that are put out by the Florida Board which list all of the scrutinized funds. If you are in a co-mingled fund, the burden is to ask them to divest and also to form a co-mingled fund that does not invest in those companies. Also the statute says if they do, you need to move your money into the other funds that are non Iran, Sudan funds. We recommend in the investment policy statement to comply with Referenced Florida Statue 215.473.47, Section 3 and all the requirements.

Chairman Andrews asked Mr. Higman: Do you think this is a big deal?

Mr. Higman replied to Chairman Andrews: No not at all. The Iran side is relatively new to this process and the industry, but the Sudan side has been going on for a long time.

Chairman Andrews: I appreciate what Prime Buchholz is doing and that they are ahead of the curve, but I would still like to entertain a motion to instruct the Town of Palm Beach Finance Department to:

1. Divest from doing any business with Sudan and Iran's Energy Sector.
2. Have no future involvement with them.
3. Send out all the information to the sub-manager that we deal with so they know what we want them to do to be in compliance.

Mr. Bohannon asked Mr. Higman: Under the suggestion that you just made, are you indicating that I am concerned about trying to conform to this particular statute in this particular way? We actually are flexible with respect to these funds. For example if we have to get out of something. Do you think we are going to harm them?

Mr. Higman replied to Mr. Bohannon: No, It is unlikely that any of these funds have these securities.

Ms. Struder asked Mr. Higman: Did you draft a letter for the other boards?

Mr. Higman replied to Ms. Struder: No, we request the attorneys do that.

Chairman Andrews entertained a motion to

1. Divest from doing any business with Sudan and Iran's Energy Sector.
2. Have no future involvement with them.
3. Send out all the information to the sub-manager that we deal with so they know what we want them to do to be in compliance.

The motion was seconded by Mr. Bohannon.
The motion was carried unanimously.

VIII.<u>UP DATE FROM PFM ASSET MANAGEMENT</u>

PFM: Discussed a handout of their investment Portfolio Structure. The handout gives details on what the Town is looking for in their portfolios which are maturities that are around the one year mark. The hand out also discusses the:

- Cash flow analysis which gives details on the short term and long term funds.
- Yield Curve Exceptionally Steep.
- Recent Two - Year Interest Rates.
- Two – Year Anticipated Future Fed Action.
- Two – Year Treasury Forecasts – July 2009.
- Current Market Yields.
- Current Investment Portfolio Structure.
- Detail portfolio of the Town of Palm Beach.

Chairman Andrews asked PFM: How long has the portfolio been in existence, the entire ten million?

PFM replied to Chairman Andrews: The original purchase date is back in August 3 and August 4. Also all the securities are being held at T.D. Bank.

Dr. Gundlach asked PFM: Where is this bank located?

PFM replied to Mr. Gundlach: Right here on the Island.

Dr. Gundlach asked PFM: Where are the headquarters located?

PFM replied to Mr. Gundlach: Their headquarters are located in Jacksonville, Florida.

PFM: In a recap of our presentation, we did a cash flow analysis, helped you select a custodian, put in the investment portfolio and we drafted the investment policy.

Ms. Struder replied to PFM: That is correct.

Chairman Andrews replied to PFM: I appreciated the drafted investment policy. I thought that was good.

Mr. Gundlach replied to PFM: I would like a more detailed cash flow analysis to be broken down into three or four categories, one being the on-going cash where you can do very little. The next category is a period where the money is due in two or three years. The next category is beyond five years and the self insurance fund where you can not touch the money unless a catastrophe occurs. Reason being, you can get a better return when you invest without taking any risk on your money. Today in America there are hardly any corporations with AAA treasuries. They have been all down graded to AA. I would stay away from BBB and BBB+. I agree with that. I think we should be allowed to in invest in A+. In fact, the AA is where a lot of first class names are. First, I think the Town Manager should amend the investment criteria and also foreign government securities. With the different categories it will allow us to use smaller percentages and to go into a higher rate. Basically I am saying that I would like to know how we can improve the return.

PFM replied to Mr. Gundlach: The cash flow analysis that we have presented to you has already been analyzed.

Dr. Gundlach asked PFM: Maybe you can present it differently so we are able to see it easier.

PFM replied to Mr. Gundlach: Sure no problem.

Chairman Andrews asked Mr. Gundlach: Did you see the updated cash flow analysis?

Dr. Gundlach replied to Chairman Andrews: Yes, but it is still very confusing.

Chairman Andrews replied to Dr. Gundlach: We basically have two funds the core and the operating. Dr. Gundlach is proposing that we open this to three or four.

Dr. Gundlach replied to Chairman Andrews: The more you see the more we can make a better detailed decision.

PFM replied to Chairman Andrews: Sure no problem.

Chairman Andrews asked PFM: Can this be done easily?

PFM replied to Chairman Andrews: Sure, no problem we can take the cash flow analysis and revise it into a draft.

Dr. Gundlach replied to PFM: Then we can see the draft and then if we have a comment we can comment on it. Does that make sense?

Chairman Andrews asked PFM: Yes that makes sense. Therefore, you would be giving us monthly reports?

PFM replied to Chairman Andrews: Sure no problem.

Chairman Andrews asked PFM: Maybe at the next meeting you can have a draft of what you can produce in a more detailed analysis?

PFM replied to Chairman Andrews: Ok.

Dr. Gundlach replied to PFM: Then we could make a decision. Also I think this group should meet by telephone and fax.

Chairman Andrews replied to Dr. Gundlach: We cannot communicate that way because of the Sunshine Laws. But you can communicate through Ms. Struder and she can send out your information to all of us.

Chairman Andrews asked PFM: In the handout under number three "Investment Objectives," Investments from time to time may be traded? The trading we are talking about is just for the Town? Is this correct?

PFM replied to Chairman Andrews: It is giving the Town authority to do trades, which is what we are hired to do for you. It is going to be PFM doing the trading and not your staff doing the trading, as we are your investment advisor. Therefore, it is the line of authority from the Town to PFM to allow us to do that.

Dr. Gundlach asked PFM: I suggest widening the range of what one can purchase, would that go in here?

PFM replied to Dr. Gundlach: Yes.

Chairman Andrews said to Dr. Gundlach: You have all ready done a lot of that all ready.

Mr. Bohannon asked PFM: Regarding number ten in the handout with regard to your requirements in liquidity, it is adhering to the current break down of funds of core and operating funds. For example, once we have reflected that on the cash flow analysis, which would effectively lead to the suggested four categories. Would we state that in the investment policy that way?

PFM replied to Mr. Bohannon: Yes you would.

Chairman Andrews asked PFM: We have to know the current and the operating and you mention obtaining a market rate of return. Are we talking about getting a market rate of return for the entire investment, is it different from the core? Are we getting a market rate for all four sectors?

PFM replied to Chairman Andrews: Yes on all four sectors.

Chairman Andrews asked PFM: We probably are going to get evaluated on how we do overall. This committee is going to get evaluated as a whole on the overall market rate of return.

PFM replied to Chairman Andrews: Keep in mind that this investment policy is to protect all investments not just what PFM is doing.

Chairman Andrews asked PFM: You suggest a six-month benchmark of treasuries?

PFM replied to Chairman Andrews: On page 14, there is a section called performance measurements. It mentions that the state requires a benchmark. Basically I am trying to establish a benchmark with each type of fund we have. Currently we have the short-term fund and we have the core fund. Therefore we have a benchmark for the short-term funds and a benchmark for the core funds.

Chairman Andrews asked PFM: If we have more funds, then we have more benchmarks, it this correct?

PFM replied to Chairman Andrews: You are correct. In paragraph “B” there is a variety of wording to provide several benchmarks but in paragraph “A” it establishes a benchmark.

Chairman Andrews asked Ms. Struder: Does the Town Council have to approve this benchmark?

Ms. Struder replied to Chairman Andrews: No, not if is written this way.

PFM: We are really serious about benchmarks for everything.

Chairman Andrews asked the Committee: Are there any more questions for PFM?

Mr. Bohannon replied: Yes, The forecast that are made for two year treasuries, are these extracted from the Bloomberg? Basically fed fund projections? To determine which fed funds it is going to be?

PFM replied to Mr. Bohannon: Correct.

Chairman Andrews asked the Committee: Are there any more questions for PFM at this time? Ok, hearing none. I would like to express the committee’s appreciation for your presentation and for your detail due diligence and your willingness to assist the Town as we go forward and to make a better financial document for the Town. Thank you for coming in today.

Chairman Andrews made a motion for a five minute break.
Dr. Gundlach seconded the motion and the motion was carried unanimously.

IX. QUARTERLY UPDATE FOR OPEB TRUST – PRIME BUCHHOLZ

Mr. Higman discussed a hand out. Generally speaking it is nice to see positive numbers. On page five, I want to express some caution so we do not get caught up in what so far has been a good market since March 9th. Looking at the equity returns you can see the monthly returns The S&P finished in July up 7.6% and the smaller cap stock finished a little better up 9.6% and international stock ended up marginally better as well. This year nine U.S. stocks have done better and all are mostly due to the currency which is due to the dollar depreciation a little bit and there is reason to believe that there are fundamentals that have driven the dollar down. This is due to the amount of stimulus that has been ejected into the economy on the other hand. This period of time has told us two things. First, we do not know much about how to predict this on a short-term basis. Second, we need a place universally across the world where people would go in case of a panic. Therefore, we want to continue to be globally diversified to be able to capture both global opportunities and the diversification effect that deals with the currency deals.

Mr. Higman: If you look at the one year numbers for domestic equity sectors the financials are up 5.15%. And also the financials are up about 50% since March 9th and just in the June quarter the numbers are up 29%. We do not have an economist on staff, but we can do a pretty good job on short term forecast. We only have two types: the long only which they look for small positive news and the hedge fund managers which looks for what has fundamentally changed in the market. They are not optimistic of what is going on today.

Chairman Andrews asked Mr. Higman: In the beginning we started out with a 8% bogie then it was immediately down and the worst thing you could do is from a time management standpoint is pick up the down part right in the beginning like what you said then you have to go up so far. Do you have any suggestions of a legitimate bogie that would be good for us to look at?

Mr. Higman replied to Chairman Andrews: We would continue to believe that we take our current assumptions are forward assumptions which has not changed considerably and look at your portfolio and continue to expect about an 8% rate of return.

Mr. Bohannon asked Mr. Higman: You mentioned something about if we do not change our forward assumptions. What are some of those forward assumptions?

Mr. Higman replied to Mr. Bohannon: There is some information in the handout on the asset allocation. Every year we have an asset allocation summit with our researchers, which consists of eighteen dedicated C.F.A's and the senior management that goes through line-by-line of the capital market assumptions.

Mr. Bohannon asked Mr. Higman: Are these your current asset allocations?

Mr. Higman replied to Mr. Bohannon: No, but I can send you the current tables.

Mr. Bohannon asked Mr. Higman: Given this point in time in the trust, what is the rate over ten years that we would need to use to get us back on the 8% track?

Mr. Higman replied to Mr. Bohannon: I would have to calculate, but it's about 10% - 12%. We are not suggesting that you change your risk profile because you have enough risk.

Chairman Andrews asked Mr. Diamond: Do you have a comment?

Mr. Diamond: The Town is looking into reformulating the Towns pension funds of Town employees. As you know we have the experts coming but we can't wait until there is a

12% rate of return as we slip more into the negative we will probably have a two step system and we will have to make other adjustments to the pension fund and it is not going to be a happy situation. On the other hand, if we don't do something we are going to be faced with a five or six million dollars in the negative going forward. Is this correct Jane?

Ms. Struder replied to Mr. Diamond: For the pension fund, it was estimated that the contribution would double in five years.

Chairman Andrews: Thanked Mr. Diamond for his comment.

Mr. Higman: If you look on page eight of the handout, there is good news on the one and three month fund on a calendar year basis. We are in line with our policy benchmark and we are ahead of our actual index. The target benchmark if you recall is the mid weight point times the benchmark. You need to be careful how you think about this because it does not have any fees in it. The total for the new members is a net of all fees number. So when you look at the actual index it is measuring the manager index over a period of time because it is the asset allocation times the benchmarks of each one of the managers. Therefore in the short run even months the managers had added about one hundred and ten basis points but we where still in the negative in the one year number to what transpired last fall. Some is real and some is a little bit artificial.

Mr. Bohannon asked Mr. Higman: I want to make sure I understand this, the "target index" is the mid- point of the asset allocation of what we have chosen times the benchmark? "Actual" is the actual allocation of what we have chosen times the benchmark?

Mr. Higman replied to Mr. Bohannon: Well, it is floating so it goes with whatever the different performances of the different markets are over time. Basically, it is how much was deployed in that asset class times the benchmark for that asset class.

Mr. Bohannon asked Mr. Higman: Is this like a report card of our asset allocation?

Mr. Higman replied to Mr. Bohannon: No, because we do not allocate. So we have set an asset allocation in a range and we deploy the money with the managers. But our policy is we do not want to flood the market. Re-rebalance when we violate the boundaries

Mr. Bohannon asked Mr. Higman: Has long as we are with the boundaries?

Mr. Higman replied to Mr. Bohannon: We allow the asset allocation to continue.

Chairman Andrews asked Mr. Higman: Has the Town contributed recently?

Mr. Higman and Ms. Struder replied to Chairman Andrews: No, you have not.

Ms. Struder: We do have around two million in that fund and we were talking about investing about one million of that into the fund.

Mr. Higman: Discussed handout, the international funds and Longleaf funds with the committee. Also he discussed on page nine the Western Asset managers to transition to Pimco over a period of nine months.

Mr. Bohannon asked Mr. Higman: Can you update me on Western being that I have not been here for the previous meeting? You just pointed out that they have rebounded strongly. Why are we moving out of Western?

Mr. Higman replied to Mr. Bohannon: The story with Western is that they were an under performer last year and we are very patient. They get done what they need to get done. Unfortunately, the market is trading away from them and now the market is trading to them kind of. In the course of that time more than half of their assets have been withdrawn and that continues today despite their strong performance. There are net withdrawals from Western but we continue to be with Western and we are the last shareholders?

Mr. Bohannon asked Mr. Higman: Are you saying if we look at Western today as a new proposed asset manager we would not even consider them?

Mr. Higman replied to Mr. Bohannon: No, we would not consider them, not the fund. We might consider them for a separate but their minimum is fifty million. Therefore, we would not consider them.

Mr. Higman: For a review, if you go to page eight where we stand today. The Domestic equities are 22% of assets and its target is 27.5 % of assets your international equities are at 15% and its target is 17.5%. It we look at our total alternative that is 23.7% and our target is 20%. Are fixed income in aggregate and are target is 20% and we are at 25%. And if you look at real assets are target is 15% and we are at 9%.

Chairman Andrews asked Mr. Higman: So you propose to take money out of fixed income and cash to get closer to our benchmark?

Mr. Higman replied to Chairman Andrews: Yes, getting closer to our benchmark on equities and real assets and the real asset bucket would get us closer to T.I.P.S.

Chairman Andrews said to Mr. Higman: One of the benefits of these two men is that they are full time Palm Beach residents. Therefore, we can have quarterly meetings that are more in line with other boards at the Town. When we have quarterly meeting we have the ability to address the rebalancing issue on a more consistent basis that is what everybody on the committee would like to do.

Mr. Higman suggested to the committee: You need to rebalance. We will rebalance from our over weight in fixed income and cash to increase our equities and our real asset categories to bring them closer to our targets. Also to reduce Western current exposure in half and we will revisit the other half at the next meeting

Mr. Bohannon replied: We want to be out of it, let's move half of it now and the rest of it will be done by the next meeting. We just do not want to look at it again.

Chairman Andrews replied: That is Ok.

Chairman Andrews made a motion to do the rebalancing of the funds.
Dr. Gundlach seconded the motion.
The motion carried unanimously.

Mr. Bohannon asked Mr. Higman: Give me your prospective on Guggenheim.

Mr. Higman replied to Mr. Bohannon: Guggenheim has a good management team and good risk management process. They were essential a private real-estate 70% some of it is their own direct investments and some of it is through the largest funds prudential funds. But the way they set up the vehicle was to attempt to set them up in a liquid asset giving them liquidity.

Chairman Andrews asked the committee: Are there any more questions for Mr. Higman?

X. <u>MONTHLY INVESTMENT REPORT</u>

Mrs. Somers: For the Town's excess operating fund for June, July will be e-mailed to you this week, we have a balance of $93 million in excess funds through the end of June. At the end of July, we transferred ten million dollars from Wachovia Evergreen to PFM. At the end of July, it will be down about ten million dollars. The current blended yield thru June is 1.98% rate return and our total interest earned for June is about one hundred and three thousand dollars. Also attached is a list to the holdings through Evergreen and the Florida League of Cities.

Chairman Andrews replied to Mrs. Somers: One thing we are looking at is trying to establish a benchmark it might work and I heard suggestions for the six month T bills, we would still look good against six month T bills down here.

Ms. Struder replied: Also through July we have the numbers for the Florida League of Cities earnings and it was two hundred and eight thousand.

Chairman Andrews asked Mrs. Somers: For the next meeting, can you add the six-month T-bills on here.

Mrs. Somers replied to Chairman Andrews: No problem.

Ms. Struder: At the next meeting I intend to invite The Florida League of Cities so the new members can meet them as well.

Chairman Andrews asked the committee: Are there any questions for Mrs. Somers?

Chairman Andrews: Thank you Finance Department.

XI. NEXT MEETING DATE

Chairman Andrews: All of the committee members are full time Palm Beach residents therefore we agreed on having quarterly meetings.

Mrs. Struder replied to Chairman Andrews: I will establish the meeting schedule for the year and e-mail the dates to you.

Chairman Andrews replied to Ms. Struder: That is a good idea that we know in advance.

XII. ANY OTHER MATTER

Ms. Struder: There is going to be a pension consultant meeting tomorrow at 2 p.m. Discussed in the meeting will be the pensions, general employee and the police retirement boards. This is a public meeting.

X ADJOURMMENT

Chairman Andrews made the motion for Adjournment.
Mr. Bohannon seconded the motion.

Investment Advisory Committee Meeting held on August 17, 2009