**CITY OF PONTIAC, MICHIGAN**
**GENERAL EMPLOYEES RETIREMENT SYSTEM**
**BOARD OF TRUSTEES**
**JUNE 17, 2013**

A special meeting of the Board of Trustees was held on Monday, June 17, 2013 at the Retirement Office Conference Room, 2201 Auburn Road, Suite B, Auburn Hills, MI 48326. The meeting was called to order at 10:31 a.m. and immediately adjourned due to lack of a quorum.

**TRUSTEES PRESENT**
Kone Bowman, Vice Chair
Jan Gaffney
Charlie Harrison, Chairman
Walter Moore

**TRUSTEES ABSENT**
Shirley Barnett *(excused)*
Bob Giddings *(excused)*
Leon Jukowski *(absent)*
John Naglick *(excused)*
Sheryl Stubblefield *(excused)*
Patrice Waterman *(excused)*
Kevin Williams *(excused)*

**OTHERS PRESENT**
Larry Gray, Gray & Co.
Chris Kuhn, Gray & Co.
Deborah Munson, Retirement Accountant
Ellen Zimmermann, Retirement Administrator
Kristina Kalebich, Calamos Investments
Barry Livingston, Calamos Investments
William Orke, WCM Investments
Kurt Winrich, WCM Investments
Dave Schwarzenberger, WHV Investments

**International Equity Finalist Presentations**

Mr. Gray reviewed that international equity will represent about 15% of the portfolio. The current manager Artio has been underperforming for some time and the Board indicated they wished to replace them with a firm that would be a good compliment to the other international manager, First Eagle. All the firms presenting today fit that requirement.

First Eagle is a deep value-oriented manager so those presenting today are all growth style to balance out the existing manager. This mandate is approximately $34.4 million.

Calamos Investments
Mr. Livingston works in the Institutional Group within the firm and Ms. Kalebich is a portfolio manager for this product. Mr. Jeff Scuderi could not attend due to a bicycle accident and the surgery that he is undergoing.

The firm has 353 employees, of which 63 are investment professionals. The firm is owned 80% by the Calamos family and there are 80 employees who also have shares. He reviewed the organizational structure and noted that they utilize a team approach. The firm has $29.3 billion in assets under management. The international growth product has been in place since 2005. He introduced Ms. Kalebich who is a Senior Portfolio Specialist.

Ms. Kalebich reviewed the listing of representational clients noting that their clients include public plans as well as Taft-Hartley and Not-for-profits and corporate clients.

She reviewed the Growth/Convertible Investment Team noting the experience of the team members and explaining the interaction of the various groups within the firm. The firm utilizes a team approach and features a capital structure research process. The approach asks the team to think like a private buyer of the entire company and analyze the entire structure. In this way they are able to assess risks and identify opportunities. The firm began as a convertibles manager.

The team investigates both the credit and equity sides of the equation. They look for opportunities by sector using a top-down and bottom-up approach. Top down factors include global macro analysis, industry and sector, themes, regions and countries and risk. The bottom-up considerations include the credit analysis, fundamental analysis, quantitative analysis and the risk/reward of candidates.

As the portfolio is constructed, they consider diversification by theme, sector, country, number of holdings and position size. Each candidate is also vetted within the context of the portfolio. Once established, they monitor the scenario, the risk/reward balance, attribution analysis, liquidity, characteristics and portfolio guidelines.

They identify themes, both secular and cyclical. Cyclical themes are tied to the general business cycle. Secular themes are long-term trends that drive growth for decades in a particular sector or industry. Examples of these are globalization and demographic shifts such as the evolution of middle class globally. She briefly discussed current portfolio positioning.

Ms. Kalebich explained the analysis involved in the bottom-up process that determines for them the source and sustainability of a company’s growth. These include quantitative screening of growth metrics, timeliness factors, valuation bands and credit metrics. The resulting candidates are subjected to further fundamental analysis. Finally, she described the sell discipline where they are very disciplined and use upside and downside capture as part of the review.

They have no more than 5% in any single name and normally hold between 50 and 75 names in the portfolio. Currently they are holding 78 names. They monitor country exposure and exposure to emerging markets which is currently about one third of the portfolio.

The top ten names comprise one third of the portfolio and the top 20 names comprise half the portfolio. They take a lot of positions away from the benchmark. They pay attention to revenue sourcing. Apple, for example, is a U.S. firm that has 60% of its revenue from non-U.S. sources. They look for companies that can grow without taking on debt and fund growth from their own balance sheet. They do not invest in Russia because there is no transparency and they have low economic freedom scores.

Performance shows that they beat the index six of eight years. In 2008, the selloff was led by high quality stocks.

The fee schedule is being discounted for the Board to 73 basis points.

<u>WCM Investments</u>

Mr. Orke, Managing Director of Client Service, said the firm was established in 1974; they are currently the second generation owners. They have 25 employees of which 19 are shareholders in the firm. The firm is based in Laguna Beach, California.

Mr. Winrich is the Co-CEO and Portfolio Manager on the global team. Their focus is the international growth product which has $1.6 billion under management. He reviewed the global equity team members and their years of experience. He noted which people are also members of the investment strategy group that determines which names go into the portfolio.

What differentiates them from others is that they manage a high conviction portfolio of about 30 companies. They use a buy-and-manage approach with a low turnover. They are bottom-up stock pickers using a team approach and a diversified portfolio of companies.

They believe that you must control risk to be successful in the long-term (control downside); that you have to be different than the benchmark to beat the benchmark; and great businesses make great investments. He reviewed annualized returns compared to the MSCI EAFE index showing they beat the benchmark in all periods shown. Downside capture, inception through March 31, 2013, showed a 68% downside capture rate and a 100% upside capture rate.

Their investment philosophy helps them identify great companies by looking for companies with “tailwinds”, “moats” and “culture”. Tailwinds means a company is benefiting from long-lasting global trends. Moats are businesses that have growing and durable competitive advantages. Culture is a business with great people who are empowered and engaged. They search for firms that have high cash flow and low debt and so are self-financing.

Mr. Winrich said they are invested in consumer, healthcare and technology sectors. For non-U.S. firms, 40-50% of growth is in the consumer sector. The biggest source of their effort is in scuttlebutt – an expert network comprised of vendors, employees, former employees and competitors. They diversify by country, sector, currency and theme.

The maximum industry exposure is 15% and maximum sector size is 45%. The emerging market maximum is 35%. Focus is on the best ideas and great growth companies at a fair price.

They begin with a universe of 1,500 names that go through an initial screening to arrive at 250 names that are subject to growth analysis. The resulting 75 names are subject to fundamental analysis and from those the team selects 30 names to be in the portfolio.

Their fees are 100 basis points.

WHV Investments

Mr. Schwartzenberger, Senior Vice President of Client Service, provided an overview of the firm saying it was founded in 1937 and opened to institutional investors in 1945. There are 60 employees and of those 18 are investment professionals. The firm is wholly owned by Laird Norton since 1994. Investment professionals have an average of 20 years industry experience and 10 years with the firm.

Assets under management as of March 31, 2013 totaled $14.3 billion. The firm manages several investment strategies from micro-cap to large cap and from emerging markets to global equity. The majority of assets under management, 78.33%, are in the international equity strategy. Public funds comprise almost 18% of their clients. Mr. Schwartzenberger reviewed the representative client list noting which are invested in the international strategy.

At WHV, the portfolio management is a star system and Dick Hirayama is the lead portfolio manager. He has the ability to identify trends and creates a portfolio in a top-down method that focuses on the most attractive sectors globally. This is in recognition of globalization. At the current time, the focus is on energy and materials sectors. Mr. Hirayama is assisted in this effort by two Portfolio Manager/ Security Analysts, Allison Goodson and Laura Stankard.

The investment process begins with analysis of the 10 economic sectors. This is followed by analysis of the 67 industries and the 51 countries. Stock selection begins with 1,500 foreign equity securities (primarily ADR's) from which a portfolio of 30 to 60 stocks is created.

Risk controls prevent investing more than 40% in any one economic sector; no more than 33% at cost can be invested in any specific country and not more than 10% can be invested in emerging markets. The maximum allowable investment in any single issuer is 7.5% at cost or 10% at market value of the portfolio. Securities must have a minimum capitalization of $1.0 billion at the time of purchase.

Mr. Schwartzenberger reviewed the portfolio characteristics, the sector weights and top ten holdings. It was explained that country weightings are based on where the company is tax domiciled. They have no investment in technology, telecom or consumer discretionary sectors. They have exposure to Canada, but none to Japan. He discussed a chart of total returns for the years 2000-2012 by sector that showed the three highest returning sectors were materials, consumer staples and energy.

The international equity strategy considers the dominant global economic forces to determine where to invest. Capitalism is becoming a global phenomenon and this reallocates wealth to the lower cost countries. Emerging markets are the world's growth engine because of lower cost land, labor and capital: they comprise 85% of the world population. There is an industrial revolution occurring in emerging markets with the resultant urbanization and infrastructure building. Global growth is energy and natural resource intensive; emerging markets are not self-sufficient in energy and natural resources, importing large amounts of oil, iron, copper, etc. There are finite supplies of energy and natural resources with long lead times for production.

Therefore, energy, materials and industrials sectors are favored due to high demand growth prospects and long term supply constraints.

China and India are prime examples of emerging markets where industrialization and urbanization are increasing substantially. As they grow, their demand for energy and resources will likewise increase as they urbanize and build infrastructure.

Performance for the strategy was reviewed. This strategy also has a low correlation to the MSCI EAFE (net) Index of 0.89. Past performance shows the product has added value in bull, flat and bear markets. Construction of the portfolio differs from the benchmark adding about 9.72% return. While they have underperformed recently, they have outperformed over time. They invest in supplier to the emerging markets. Industrialization will continue to drive demand.

Their fees are 84 basis points.

<u>Wrap up</u>

Discussion followed by the trustees. The consensus was for WCM Investments. Mr. Kuhn will prepare a recap of the recommendation.

## <u>**Fixed Income Review**</u>

Mr. Kuhn began by discussing how to evaluate fixed income in a low interest rate environment. The aspects to be covered include the risks of fixed income in a rising rate environment; the performance of varying fixed income/equity allocations in different capital market scenarios; the diversification benefits of different fixed income sub-classes; and the potential benefits of active versus passive investment management. He indicated this is an educational session so feel free to ask questions as they arise.

There was brief discussion of the yield curves for February 2013. This was followed by an explanation of duration which is the measure of weighted average cash flows of a fixed income vehicle measured in years. Mr. Kuhn then discussed the various returns that would be needed from the remainder of the portfolio in order to make up for fixed income losses of 2%, 4% and 6% with varying amounts of fixed income in the portfolio (between 10% and 50%), to illustrate the impact to the total portfolio.

Mr. Kuhn discussed the yields for the 10-year treasury and the Barclay's U.S. Aggregate index over 19 quarters. The projected fixed income performance was shown for the absolute, relative and average scenarios and in all cases, the treasuries underperformed the Barclay's Aggregate. Again using a 19-period rolling returns, he gave the equity performance for the same period.

Finally, he gave multiple examples of fixed income/equity mixes and the performance under pessimistic, base and optimistic cases to illustrate the range of returns. This was also done with two periods when equity performed poorly.

Fixed income indexes were discussed and the characteristics of these as of January 2013 were shown. Discussion followed about indexing versus active management. Traditional core fixed income is comprised of investment grade debt securities issued by the U.S. Government, agencies, U.S. domiciled companies and foreign issuers. It can also include mortgage-backed securities, asset-backed securities and commercial mortgage-backed securities.

Core Plus strategies include the above and introduce lower-rated securities, non-dollar denominated securities and emerging market debt. Strategies focusing on only below investment grade debt are called high yield.

International fixed income covers a vast spectrum of investment options, from international developed markets to emerging market debt to international opportunistic fixed income to global fixed income.

Expected returns from traditional core fixed income in coming years are projected to be dismal. If interest rates rise as is expected, the expectation is for losses for this asset class although it provides protection for the portfolio in times of stress in the equity markets. Fixed income can be diversified across various types of fixed income strategies that may improve results. Other asset classes, such as real estate, hedge funds, private equity and timberlands can also prove diversification.

Mr. Gray noted that with a fund such as this, a laddering of maturities can be an effective strategy.

Mr. Kuhn noted that the total portfolio is currently out of compliance with PA 314 based on the changes that became effective in March, however, the portfolio is due for rebalancing shortly.