

NORWALK MUNICIPAL EMPLOYEES' PENSION BOARD MINUTES

NOVEMBER 8, 2006

ATTENDANCE: James Murphy, Chairman; Charles Pirro, Gerry Moran, Patricia McCormick, Michael Sweeney

STAFF: Frederic Gilden, Comptroller; Victor S. George, Personnel; John Schlosser, Personnel

OTHERS: Ellen Petrino, Evaluation Association; Mr. Howard Potter, Capstone; Jeffrey Shaw, Armstrong Shaw Associates; Terry Newman, Armstrong Shaw Associates

CALL TO ORDER

Mr. Murphy called the meeting to order at 6:00 p.m.

There was a brief discussion about what constituted a quorum for the Pension Board. Mr. Murphy explained that this Board considers the presence of a majority of appointed members to be a quorum.

1. ARTISAN, LEANNE CONTRERAS, PORTFOLIO REVIEW VIA CONFERENCE CALL.

Ms. Contreras thanked the board for taking the time to review this with her. Ms. Contreras directed the Board members to a hand out titled "International Fund Management Team". Ms. Contreras then reviewed the quarterly investment returns with the Board. She indicated that due to some market fluctuations, while the market started out strongly in the first quarter, during the second quarter, strong performing investments reversed themselves and underperformed after the market correction. In the third quarter, lower energy prices and other factors made for a much more optimistic feeling, so the market performance moved back into the positive grid.

Ms. Contreras explained that concerns about sources of future growth may have contributed to the market's renewed preference for value stocks. Growth stock valuations have fallen fiercely since 2000, which results in investors paying more per unit for future growth for value stocks than they are for growth stocks.

She also commented that Large Cap Stocks outperformed Small Caps. This may be the result of a moderating growth environment and that this may continue to pave the way. Ms. Contreras then explained Artisan's philosophy for their country allocation selection. The advertising area and the communications area did not perform as expected. Increases occurred in the energy field.

Ms. Contreras reported that Artisan historically would invest 20% in any given developed

market (except 25% in the UK and Japan). This year, Artisan made the decision to change that percentage, and now the investment maximum is 30%. A change was also made in the Emerging Markets maximum exposure, from 15% to 20%.

Ms. Contreras said that overall, the past year has been a very good one for Artisan's type of investments.

Mr. Murphy had some questions about the percentage assigned to the Emerging Markets. Ms. Contreras reviewed the philosophy and the details of the issue. She said that there continues to be a great deal of growth opportunities in the Emerging Market. Mr. Murphy suggested the benchmark be changed to MSCI ACWI ex-US, which has a permanent weight of about 12% in emerging markets, consistent with Artisan's thinking going forward.

The Board thanked Ms. Contreras for her presentation and concluded the call.

2. CAPSTONE, HOWARD POTTER, PORTFOLIO REVIEW

Mr. Potter gave a presentation regarding the bond investments to the Board. He directed the Board's attention to a Portfolio Review booklet, which the Board had. The bond market has been stable and Mr. Potter stated that the market had earned even more basis points in the time period since the close of the third quarter and his presentation to the Board.

Regarding the future, Mr. Potter explained that the portfolio has duration of something just slightly less than the benchmark. He stated that the Federal Reserve has been very transparent and usually gives indications as to what direction it will be moving in. However, at this point in time, the indications are that the Federal Reserve does not know what direction it will be moving in. Mr. Potter also explained that the yield curve is flat, so it doesn't pay to lengthen duration. The economy shows many indicators of slowing down. For the first time, the core inflationary number is starting to increase. A component of that is increasing labor costs. Inflation is the Fed's first priority.

Mr. Moran asked if Capstone could purchase TIPS. Mr. Potter replied he has a similar product in the portfolio called SIPS, which are tied to changes in the CPI index. These actually have a monthly coupon. The TIPS program has the month earnings automatically reinvested. Ms. Petrino asked if Capstone would use TIPS as a hedge. Mr. Potter said that TIPS would always be available for immediate purchase, unlike the SIPS, which are opportunity driven.

There were also some questions about how the indexes were measured. Mr. Potter reviewed the process and the numbers with the Board members. Ms. Petrino asked about the Yield and the Portfolio for the next year. Mr. Potter said that the current yield of the portfolio was 5.64%, which is about 50 basis points ahead of the market. Ms. Petrino said that the Board generally talks about duration, which is 4.49 years, verses the index core of 4.61, which is why Mr. Potter said that the duration was essentially neutral.

The discussion then moved on to mortgage backed securities, which have a variety of risks. Mr. Potter reviewed some of the risks involved with this type of investment. Ms. Petrino asked if Capstone was investing in a particular type of mortgage bond. Mr. Potter reviewed the triple A credit companies, along with the adjustable rates bonds.

There was a discussion about 10.01 product, which has almost all of the principal paid off in the first ten years, which means it is really a ten year bond rather than a thirty year bond. Those who are transferring or purchasing the house on speculation utilize these.

The Board thanked Mr. Potter for his presentation.

3. ARMSTRONG SHAW - TERRY NEWMAN, PORTFOLIO REVIEW

Ms. Newman gave a quick overview of the company and assured the Board that everything had been stable with the investment firm. It was noted that the firm had come up significantly short of the benchmark since the City had hired the firm. While Armstrong Shaw has historically outperformed, this past year has been a particularly difficult year. During September, the tide started to turn and the City's portfolio was up 2.9%.

Mr. Shaw commented that his firm has been in business over twenty-two years and the company has been able to outperform both the Russell 1000 Value and S&P index. During the last seventeen years, the firm had never underperformed both of those indexes during the same calendar year, which had resulted in very consistent returns. Mr. Shaw reminded the Board that the account had been opened in the middle of last year and experienced five challenging months in the markets. During the last two months, the market had changed and the performance has moved in a positive direction. Ms. Newman also stated that no trend goes on forever, and that the Russell 1000 Value may reverse in the future. When the S&P starts to overtake the Russell, then Armstrong Shaw will most likely also overtake the Russell index.

Mr. Shaw reviewed the company's held and their standing with the Board. He also reviewed the key factors that should benefit the portfolio. Mr. Murphy asked about the future of G.E. stock. Mr. Shaw explained the firm's philosophy regarding a return pattern like G.E.'s. There was also some discussion regarding Pitney Bowes investment. When asked about the Cemex stock, Mr. Shaw reviewed the reasoning for the firm holding the stock in that company. He also gave a brief overview of the cement market and why this particular company was a solid investment. In reply to a question as to Armstrong Shaw's market focus, Mr. Shaw stated that his firm is focusing on the U.S. marketplace, but stated that it was important to realize that the market was becoming more global.

There was some interest in the history of the Boston Scientific holding. Mr. Shaw gave a brief overview of the company's history and why Armstrong Shaw holds stock in the company.

Another question was directed at the recent sale of Wellpoint stock. Mr. Shaw explained that with a changing political climate and concerns about spiraling health care costs, Armstrong Shaw felt it was time to reduce its holdings in the health care field.

Mr. Shaw also reported on the firm's views regarding the mega cap stock holdings. He stated that the firm was comfortable with the mega cap stocks that it was holding, despite the fact that some of them had not had good returns recently. Mr. Shaw said that those stocks would rebound in time. Ms. Newman also commented that the firm would continue with the companies that offer fundamental value, some of which have produced good returns and others of which the firm feels confident will provide good returns in the future. When a firm holds a concentrated portfolio that runs close to the benchmark, if the index changes, things can swiftly shift. Mr. Shaw said that if a firm chooses to chase the benchmark, then eventually, the portfolio will look like the benchmark and that is not what makes Armstrong Shaw different from the others. He said that for the last twenty-two years, Armstrong Shaw has been able to beat the benchmark and they were not going to change their philosophy at this point in time. Ms. Newman explained that they are looking for very strong absolute returns that will over time out perform the benchmarks. She concluded with the statement that Armstrong Shaw recognizes that they have fallen short of the benchmark during the time period and hoped that the Pension Board will be patient.

The Board thanked Mr. Shaw and Ms. Newman for their presentation.

4. EVALUATION ASSOCIATES

a. Discussion regarding Armstrong Shaw

Mr. Murphy reported that the Pension fund had once invested in a company called Nicholas Applegate. During the first year of performance, the investment decreased by 20%, but Mr. Murphy and Pirro decided to stick with the firm. Subsequently, the firm yielded a very good return for the investors over the long term. He stated that he did not like to fire a manager that one had hired in a relatively short period of time.

Ms. Petrino reported that this portfolio was more staid than most. Ms. Petrino said she would recommend that the Pension Board keep Armstrong Shaw because they are poised to do better. They have done well over the long term and have a concentrated portfolio. The City does not need the diversification, because it had it across the portfolio.

Mr. Gilden expressed some concerns about Armstrong Shaw. Ms. Petrino pointed out that there had been seven years of value outperforming growth, so she recommended sticking with the active value managers and index growth. She noted that the benchmark was very complicated and very volatile. A brief discussion on Armstrong Shaw's performance followed. Mr. Murphy commented that he did not feel the Board should terminate Armstrong Shaw without at least another year's performance to judge by, if not through July 2007. With such a short time frame, it was difficult to judge. Mr. Murphy said that he would like to continue with the firm for the time being. Mr. Moran said that

he felt the need to have an index fund, but it doesn't have to be now. He concluded with the statement that he did not disagree with Mr. Murphy. Mr. Murphy then suggested that the Board consider tabling the matter until June, and asked Ms. Petrino to put the firm on the schedule for May or June.

b. Discussion regarding infrastructure

Mr. Murphy stated that he had spoken with Frank Nash and Mike Salvatore. He then suggested that the Board not vote on anything at this time and wait until next month when everyone was present. Ms. Petrino then reviewed the information booklet titled "Pro Forma Fund Structure as of 11/7/06" with the Board. The sources of funds would be from fixed income, some from cash and some could be taken from equity, if the Board so desires. There was some question about the private equity commitments that had been voted on last month but were not reflected on this sheet. Ms. Petrino said those commitments had not been noted in a footnote and suggested a column with commitments in the future. Mr. Murphy asked for a flow chart that shows committed funds, taken down and equity returns. Mr. Gilden commented that the pensions that are approved of each month brings the numbers up.

Ms. Petrino gave a brief overview of two proposed investments, Alinda, a new investment group that will have investments in the U.S. and Europe and Macquarie, an established group that will only invest in the U.S. and Canada. Alinda will be primarily industrial, energy and public structures. Macquarie will be involved in larger projects.

One of the Board members wished to know where the leveraging was indicated on the chart. Ms. Petrino said that it was approximately the same because infrastructure across the board was about the same at 80%. This was very common, she assured the Board. There was a discussion about the details of leverage and how it was working. There was some concern about the City's position in terms of payment in the event of disaster. Ms. Petrino pointed out that the projects were rated "investment quality" and stated that the projects were insured. This discussion was followed by a discussion on privatization and unions. There were also some questions about the details of the returns and percentages.

Mr. Murphy requested that Ms. Petrino create a report in terms of absolute proposal. Ms. Petrino said that she would. The closings for these are scheduled for January. There was also a request that the Alinda representative and the union representatives be present at the next meeting.

c. Further Modeling of Private Equity

Ms. Petrino reviewed the charts for Projected Cash Flow and the Projected Private Equity Allocation with the Board.

d. September 30 Performance and Asset Allocation

Ms. Petrino stated that the value as of November 7, 2006 was \$356.5 million. She then directed the Board Members' attention to pages 4 & 5 of the Quarter Ended September 30, 2006 report. Ms. Petrino stated that Bear Stearns has not been doing any direct brokerage trading, so Ms. Petrino put in a call to them about this.

e. U.S. Equity Index Funds

Ms. Petrino said that the information had been sent but she had not been able to analyze the information. She said that her recommendation was for SSGA because they have a broad range of funds and are the cheapest. This will be continued on the December agenda.

5. APPROVAL OF THE MINUTES FOR OCTOBER 11, 2006

A question was raised as to whether or not there was a quorum present. Mr. Murphy explained that over a long period of time, often there was only one union member that came to the meetings. He reviewed the history of the meetings. Over the period of time, it was accepted that there would be a quorum with a majority of the six members who were appointed by the Mayor and approved by the Council, along with the appointed designee from the Finance Department in order to conduct business. This is reflected in the minutes as far back as fifteen years ago. There was a question about where the operating rules would be found. Mr. Murphy stated that Personnel would probably have a copy and that it was approximately four pages long. No business has been conducted by the Board unless four votes were present. Ms. Petrino asked how the union votes are handled. Mr. Murphy replied that if the union representatives are present, they vote.

**** MR. SWEENEY MOVED TO APPROVE OF THE MINUTES FOR OCTOBER 11, 2006 AS SUBMITTED.**

**** MR. GILDEN SECONDED.**

**** THE MOTION PASSED UNANIMOUSLY.**

6. APPROVAL OF PENSION APPLICATIONS

**** MR. MORAN MOVED TO ENTER INTO EXECUTIVE SESSION TO DISCUSS THE PENSION APPLICATION OF HADAR MONSALVE.**

**** MR. SWEENEY SECONDED.**

**** THE MOTION PASSED UNANIMOUSLY.**

The Board entered into executive session to discuss the pension application of Hadar Monsalve and reconvened into public session at 8:40 p.m.

**** MR. PIRRO MOVED TO APPROVE THE PENSION APPLICATION OF HADAR MONSALVE AS OF OCTOBER 1, 2006 AT THE RATE SET FORTH ON THE APPLICATION OF \$1,365.50.**

**** MR. SWEENEY SECONDED.**

**** THE MOTION PASSED WITH ONE VOTE IN OPPOSITION (MS. MCCORMICK).**

Mr. Murphy then read the list of retirees into the record:

Barbara D'Urso, 10 yrs. 10 mos. Service, age 59, had a deferred early retirement with a final average salary of \$18, 168 with a standard form of benefit with \$308.50 per month.

Louis W. Barndani, Jr, 31 yrs. 5 mos. Service, age 63, has a regular pension with a final average salary of \$71,315. Mr. Murphy noted that the annual monthly benefit should read "\$36,570.00" rather than "\$63,570.00". His monthly benefit will be \$3,047.50 with a commencement date of November 15, 2006.

Carlos Hernandez, 19 yrs, 11 mos., age 55, early retirement, has an early retirement with a final average salary of \$62,665, and the standard form with the commencement date of April 1, 2006, with a three month benefit payment of \$1,727 and a five month benefit payment of \$1,752.91.

There was question regarding Mr. Monsalve's application, where both regular and vested benefits checked. Mr. George explained the reasons for this. Mr. Murphy stated that the commencement date of October 1, 2006 should be noted for Mr. Monsalve's pension application.

**** MR. PIRRO MOVED TO APPROVE THE PENSION APPLICATIONS FOR BARBARA D'URSO, LOUIS BARDANI, JR., CARLOS HERNANDEZ.**

****MR. MORAN SECONDED.**

**** THE MOTION PASSED UNANIMOUSLY.**

7. OTHER BUSINESS

Ms. McCormick commented that it had been impossible to get a response from the unions. She suggested that the Board schedule one or two dates, announce them and let the people attend. If questions are submitted in advance, the meeting will run smoother. Mr. Murphy asked where the preferred location would be. Ms. McCormick replied that City Hall would work. Mr. Murphy said that he would work that out with Jim.

Ms. McCormick asked if the agenda could be arranged so that the briefer administration matters are disposed of in the early portion of the meeting. Mr. Murphy replied that as a courtesy to those who come with presentations and have to travel, the managers have been scheduled first. Ms. McCormick asked if the first fifteen minutes could be scheduled for administration before the presentations. Ms. McCormick said that there might be more union participation if it was scheduled this way. She commented that she had spent three hours where as the bulk of her work was focused on administrative issues. Mr. Murphy replied that he was disappointed in that because part of the responsibility of the Board Members was to be cognizant of the managers and evaluating managers. Ms. McCormick suggested alternating the agendas. Mr. Murphy said that he prefers to have

the managers first because he believes it a courtesy to the managers who often have to travel.

8. ADJOURNMENT

** MR. PIRRO MOVED TO ADJOURN.

** MR. MORAN SECONDED.

** THE MOTION PASSED UNANIMOUSLY.

The meeting adjourned at 8:50 p.m.

Respectfully submitted,

Sharon L. Soltes
Telesco Secretarial Services

