

NORWALK MUNICIPAL EMPLOYEES' PENSION BOARD MINUTES

Minutes from Meeting

PENSION BOARD

MARCH 9, 2005

ATTENDANCE: Jim Murphy, Chairman; Charles Pirro, Michael Sweeney, Michael Salvator, Patricia McCormick

STAFF: Sara LeTourneau, Director of Personnel & Labor Relations; Frederic Gilden, Comptroller

OTHER: Ellen Petrino, EAI

CALL TO ORDER

The Chairman called the meeting to order at 6:15 p.m.

MARKET OUTLOOK – AL ZESIGER

Mr. Zesiger stated they were looking at a long business cycle. And instead of a normal three to four year cycle, it would probably be a four to five year one. He said that U.S. Equities were reasonably priced and as long as the business cycle begins, they will continue moving upward, although interest rates will go down. He spoke to the fixed income, where they have high yield bonds that respond more to the economic situation than to trends. He explained that in the pension fund, there is up to 34% in the international market and it's currently at 61% in the domestic market. The limit for international stocks has been at 30%, but he expressed he would love to see it turn to 40%. He reviewed how historically the international returns have compounded as compared to the domestic rates that are up 1 to 2%, noting that the international market has performed well. He further noted that in the U.S., the top tier will be big institutional stocks and this applied to overseas entities as well. So they were looking to extend that philosophy overseas and perhaps look at India in the future. Mr. Murphy commented that India has been a hot spot for awhile now.

Mr. Murphy asked how the domestic equity portfolio has performed. Mr. Zesiger said for the domestic standards&P 500, it has been compounding at 10% annually since inception of the account (10/1/95) and emerging markets have compounded at 3% annually. He thought this would probably change, though due to the development of the consumer class in places like India and China, where they are beginning to consume their own manufacturing. He thought this would continue for at least four to five years.

Ms. Petrino asked if there was still foreign money propelling the markets upward. The response was that as per capita income rises, a domestic class develops as is apparent in Korea today. But there has been cyclical in the market that moves the business cycle here. However, they are betting that this is changing and there will be less of a cyclical element to it. As domestic investors grow, this will create a domestic investor class, thus, it will smooth out cyclical. However, it will be a slow process.

Mr. Zesiger commented that the GDP might come in at 4% this year, noting that most emerging markets were up 10%. Ms. Petrino asked if he thought the US P/E ratios had to come down. Mr. Zesiger said not for a long cycle.

Mr. Salvator questioned with increased spending and buying power, does this create an opportunity to import more goods and create a bigger market. Mr. Zesiger said yes in theory. It was added that there is a global opportunity, but they were not getting evaluation by investing in emerging market security.

Mr. Zesiger said the yield on the international portfolio tends to be higher than the domestic portfolio. Mr. Sweeney asked if this meant a dividend or earning yield. Mr. Zesiger said it was dividend.

Ms. Petrino asked if there were other things they should be thinking about. Mr. Zesiger commented that in the domestic market, they were looking at Biotech and in the international market they have invested in South East Asian entities.

It was stated that within the overall universe of emerging markets; they have looked at areas that will do well in the long run. But they have looked selectively at domestic markets. And just recently, they are looking to do so in more Asian markets, such as in China and Hong Kong.

Mr. Murphy asked about private placements and where they stand today. Mr. Zesiger said in relation to private placements, they were not seeing the values they used to. They have some opportunities in private equity, but they are moving slowly on these.

Mr. Murphy said he would like to see the back up information on the international markets. The response was that they would research information that may be more salient. Mr. Zesiger noted the key thing to watch for is foreign GDP.

Mr. Sweeney asked about incentives for people to invest in equities. Mr. Zesiger said they were finding that people are beginning to invest in their own market. For instance, China has done this. He noted that local investors are increasingly putting large portions into equities, but they are realizing they are not getting the yield they should out of domestic markets.

WELLINGTON – OPPORTUNITIES GROWTH

Ms. Petrino introduced this firm. She stated that they ran a fairly concentrated portfolio.

The representatives from Wellington approached. Ms. Welling thanked the committee for having them attend. She introduced herself as the Business Fund Developer. She also introduced Steve Clark, Business Development Consultant and Bob Hrabchak, Equity Product Manager.

Ms. Welling gave an overview of Wellington Management. She pointed out they took a growth approach that was focused on all segments of the market. And importantly, they are very focused on research where they are a fundamental research house.

Ms. Welling referred to page #1 in the handout and commented on the following as outlined:

- Ownership – this is a key to delivering results. They are able to track, retain and motivate the best professional across the globe.
- Business model – this serves their clients well, the firm well and the individual employees.
- Investment platform – this is very broad and it could be thought of as a series of investment boutiques where opportunistic growth is a boutique within the firm to cover all public traded securities. Thus they know their supplier and investors well.
- Culture – their motto is “ clients are first”

She referred to representative clients listed on page #2. She expressed they were very familiar with the concerns and challenges public funds were facing. She urged all to ask about their reputation and she said they would be very impressed.

She referred to page #3 showing the number of professionals. They have (46) people on their global research team that cover a narrow defined industry. This is important to assure that people are dedicated to the industry. She noted that many have been around for years and have generated positive returns. She further emphasized that research was paramount to achieving objectives.

She referred to page #4. She explained they need to have faith in folks who do the research, highlighting that commitment to research was key.

Mr. Hrabchak referred to page #6. He discussed the team and philosophy process. He reviewed key items outlining that an opportunistic portfolio is a pure investment. He said their approach and focus is on sustainable growth over the next three to five years. He said they employ an integrated team that is comprised of five members who meet together daily to brainstorm. He noted they have four dedicated analysts. He referred to page #7 and explained the life cycle of an industry that focuses on small, mid and large caps. He said it was important because a lot of research that is done on small cap companies may identify issues that can disrupt what's in the large cap space. He further talked about where Wellington's being involved in researching large cap stocks has led them to ideas for mid and small cap investments.

Mr. Sweeney asked what was meant by opportunistic growth. Mr. Hrabchak said they invest in stocks opportunistically across the size spectrum.

Ms. Petrino asked what benchmark was used. Mr. Hrabchak said it was the Russell 1000 Growth.

Mr. Sweeney asked why the large cap growth had lapsed through the years. Mr. Hrabchak said it has lagged over the course of four to five years; but they were able to find good ideas in large caps. However, many just got overextended in the past, but currently; they are finding some large caps for their portfolio.

Mr. Hrabchak reviewed page #8. He said they focused on four criteria:

- Sustainable growth
- Superior business models
- Proprietary fundamental research
- Early identification of change

He commented that they spend a lot of time focused on what makes sustainable growth. He spoke to generating cash flow internally that is key for investors, because these companies are able to buy back their own stock. As for early identification, this speaks to the team looking at the growth sector and it gives them the ability to identify opportunities.

Mr. Hrabchak reviewed page #9 outlining Opportunistic Growth Investment Process Summary. Mr. Murphy asked about the number of stocks in the portfolio where it was denoted they had 80 – 110 stocks. Mr. Hrabchak said they want to know the stocks and the risks associated. This is why they spend time on research, because it is important to have a broadly diversified portfolio. However, he pointed out that page 9 was a summary of the process. He said the result of the first three steps was to ensure they are investing in pure growth companies. He emphasized the importance of focusing on growth companies alone, rather than on all types of companies.

Mr. Hrabchak reviewed page #10 outlining Opportunistic Growth Sustainable Growth Focus. He said this was an important step in the process. He noted that companies such as Yahoo must have a cost advantage to allow them to deliver the product cheaper than others. There is also a customer advantage and a competitive advantage. He reviewed page #11 Growth Price Disciplined. He said when you buy and sell, there is a disciplined approach conducted by three factors: Revenue Growth – this includes unit growth and pricing power. Profitability - this is inclusive of normal operating margins and for Capital Requirements – they need to consider how much cash they need to run the business.

Ms. Welling distributed and reviewed a spread sheet sorted by sector that indicated companies where fair values and upside percentages were outlined. She said they effectively established target prices and ranked them accordingly. She noted the key criteria on was revenue growth.

Mr. Sweeney asked if they back tested at all. Mr. Hrabchak said no, they focus on the relative merits of an investment.

Mr. Sweeney asked how they ultimately come to a decision on what to invest in. Mr. Hrabchak said it basically came down to a conviction level in management and analysis. He noted they do have risk controls in place.

Mr. Hrabchak reviewed page #12 as outlined. He reviewed page #13 outlining Top Ten Holdings as of December 31, 2004. He explained this was a diversified list with a significant number of non-benchmark companies that they have close interaction with. He noted the top companies had very high amounts in cash. He reviewed page #14 Sector Weights as December 31, 2004. He commented that where they don't find growth, they don't force it. He reviewed page #15 Opportunistic Growth Portfolio Characteristics as of December 31, 2004. He said they employ a bottom up approach opportunistically buying stocks throughout the spectrum. He noted that for price to cash flow, they could see they are priced less than market.

Mr. Steve Clark provided an update on the Securities Exchange Commission (SEC) focus on the money management arena. He pointed out that Wellington has worked with SEC and cooperated fully by providing information etc. He explained that the issues focused on trading and trade allocation practices, but he believed their policies were fair to clients, so again, they are working with the regulators.

Mr. Clark reviewed page #16 Opportunistic Growth Investment Returns US\$. He said this process was in place and disciplined and sustainable. He expected them to deliver results as outlined over time. He reviewed page #17 Opportunistic Growth Risk Comparison – Five Years Ended December 31, 2004. He said when it came to risk taken by the team; the amount of tracking error over benchmark was minimal. He reviewed page #18 The Wellington Management Relationship. Overall, he thought they had good characteristics to partner with the City of Norwalk. He further expressed that while investing was fun, at the end of the day, it was key to make sure the pension fund was invested in appropriately.

Mr. Murphy asked what the minimum investment was. Ms. Welling said it was \$5million in the co-mingled fund.

Mr. Sweeney asked if they used any relative value measures of when growth or value is in favor. Mr. Hrabchak said they do growth investing, so it was not their focus to track other styles.

TRANSAMERICA GROWTH

Mr. Dave Kania introduced himself as the Regional Sales Director. He initiated a

conference call to Chris Ericksen, Portfolio Manager at the San Francisco office. He stated they were present tonight to discuss large cap growth.

Mr. Kania reviewed Section 1 of the handout booklet. He stated that TIM, LLC was a newer phase to a well established organization where they have managed money for over 25 years. He noted that anyone who is not an owner in the firm does participate in the profit sharing plan. He went on to review page #3 pointing out the client list. He commented that the list has grown over time and the State of New York and the City of San Francisco have recently been added. He reviewed Section 2 TIM Equity Philosophy & Process. He said they were a long term investment manager that focuses on a five to ten year horizon; they are investors, not traders.

Mr. Ericksen reviewed the team's background. He made the point that there were 12 people, 9 of whom work day to day on growth products. He further noted that a key element of the process was communication. He also pointed out that Jeff Van Harte was the leader of the team and had plenty of investment background. He said the team ran three products, small, mid and all-cap.

Ms. Petrino asked if all-cap had a shorter time frame. Mr. Ericksen said yes. They're allowed to hold more cash in this portfolio.

Mr. Kania said there were no distinctions in how the Portfolio Manager and Analysts operate. They work in conjunction to assure the best investment strategy.

Mr. Ericksen reviewed page #7 Investment Philosophy. He commented that they were long term investors of five to ten years. They track where the business will be over a long period of time. He further noted that the hedge fund community was key and he spoke to specific industries that have become long term investors. He referred to the modern portfolio statistics. He said in terms of adding more stocks to portfolios, they have found the cost was crucial, so they concentrate on 25-30 high return funds. This assures more of win rather than a loss. He said they also look to businesses that can generate free cash flow. He reviewed page #8 highlighting the Investment Process: Idea Generation. He spoke about universe coverage that has a flat structure, i.e., each Portfolio Manager is also an Analyst. They have a general list approach to sector coverage and each member of the team can look up or down the capitalization structure. The minimal capitalization for large growth strategy is \$3 billion. He further mentioned that for Idea Generation, they don't screen at all. He emphasized that change was instrumental in this type of investing and they focus more on progressive tracking of what's happening in the industry.

Mr. Ericksen further reviewed page #9 Investment Process: Company Evaluation. He reviewed the three steps. He explained that going through the steps allows them to get individual stock investments right over time. He spoke to Groundswell of Change. He said he believed they can purchase great business models, but ultimately, they are interested in growth. He further reviewed varied companies that have benefited from groundswell of change, thus resulting in high returns on capital. He referred to Valuation

and said the focus was on cash flow to be generated in five to seven years; the analyst concentrates on where a business may be within this time. He reviewed Validation noting this related to teams evaluation of investment ideas and how the market is impacting their securities. They meet once a month brainstorming companies they are researching where each offers their opinion.

Mr. Ericksen spoke to the fact that ultimate accountability lies with the Lead Portfolio Manager. It is important to avoid closing off a crucial investment opportunity.

Mr. Kania commented that all large cap opportunities are looked at and managed the same.

Mr. Sweeney asked about the E-Bay investment. He also asked how they handled stocks that are down. Mr. Ericksen said they try to evaluate the investment thesis. And if they find the company is not intact, the general approach would be to get it out of the portfolio as soon as possible. As for E-Bay, they thought it was an overall good investment.

Mr. Ericksen reviewed page #10 Investment Process: Portfolio Construction. He commented they hold stocks for five years on the average and if they see a decline they allow a year to get out of it. He further noted they were benchmark aware, but not benchmark driven.

Mr. Kania skipped to page #13 outlining the Holdings. He said the percentages were indicative of their portfolio at year end.

Mr. Murphy asked why they sold Northern Trust. Mr. Ericksen said when they had the opportunity to buy E-Bay, Northern Trust was the most obvious stock to sell.

Mr. Sweeney asked why they bought Gillette. Mr. Ericksen said they purchased it 2 ½ years ago. They got great free cash growth out of it, but they thought that P&G over paid a bit for Gillette. However, they are evaluating P&G now and he thought they have been very smart in managing the company, which is solid .

Mr. Sweeney asked about Microsoft. Mr. Ericksen said that Microsoft had limited growth opportunities and it didn't show the same growth potential that it had a few years ago. But growth will still be in the mid to high single digits.

Mr. Kania said they would find in the portfolio structure there were two different types of companies, i.e., there is what he termed the "steady eddy" such as a company like Microsoft and also the higher beta and higher alpha companies.

Mr. Kania reviewed page #14 Large Growth Characteristics. He said their Up Capture and Down Capture statistics reflect the understanding of the downside and upside. They view risk as the likelihood of losing the principal. Mr. Ericksen added in a down market they would expect they would have negative absolute returns.

Mr. Kania said they have always run 25-30 stock portfolios and they were committed to maintaining that number. They are not interested in increasing stocks for diversification sake because concentration really adds value.

Mr. Ericksen reviewed page #16 Calendar Year Returns. He pointed out this page highlighted year by year performance. He reviewed page #17 Peer-Relative Returns noting that what was contained on this page was evidence of consistency. He said he expected the process was geared to tilt the odds in the investor's favor.

Mr. Kania referred to Section 4 where the fees schedule and disclosure were highlighted.

Mr. Murphy asked about Wellpoint. Mr. Ericksen said that Well point was a good competitor in terms of use of IT. They also liked them from a segmentation perspective, because they were looking to target the younger market. They are also shareholder friendly.

Ms. Petrino asked the process for decision making. Mr. Kania said that Jeff Van Harte was the final decision make. He decides what stocks get in and at what weights.

Mr. Kania thanked the committee for their consideration.

Mr. Murphy commented that both firms showed outstanding performance. He said there was a question if they should keep the portfolio concentrated or split it. The consensus among the committee members was that they should keep it concentrated.

Mr. Sweeney commented that he liked Wellington's portfolio.

Ms. Petrino commented that they want a large cap growth. She said they are looking to replace TCW due to their management change.

Mr. Pirro expressed that his preference would be to go with a concentrated portfolio. And that he liked Wellington.

Ms. McCormick said she also liked Wellington.

Mr. Gilden said he was inclined to go with TransAmerica.

Ms. Petrino said she would line up statistics for the next meeting to allow them some to review some more information before taking a vote on this matter.

Ms. McCormick left the meeting at 8:45 p.m.

**** MR. SWEENEY MADE A MOTIION TO TAKE \$ 8 MILLION FROM TCW AND
AUTHORZIE THE COMPTROLLER TO MAKE THE TRANSACTION**

** MR. PIRRO SECONDED
** MOTION PASSED UNANIMOUSLY

MINUTES APPROVAL

-TABLED – UNTIL THE NEXT SCHEDULED MEETING.

APPROVAL OF PENSION APPLICATIONS

§ Fahey, Jr., James P.
Public Works
Commencement Date: April 1, 2005

Type of Pension Annual Monthly Benefit
Early \$1,624.00

§ Papowitz, R. Louise
Board of Education-Nurse
Commencement Date: March 15, 2005

Type of Pension Annual Monthly Benefit
Regular \$1,571.00

§ Chin, Anna H.
Board of Education – Secretary
Commencement Date: March 15, 2005

Type of Pension Annual Monthly Benefit
Regular \$1,673.00

** MR. PIRRO MADE A MOTION TO APPROVE
** MR. SWEENEY SECONDED
** MOTION PASSED UNANIMOUSLY

OTHER BUSINESS

Ms. Petrino of EAI briefly reviewed the Large Cap Value Search. She said they talked about replacing Boston Company. She referred to page 6 outlining Relative Value Large Capitalization Equity. She pointed out there were three managers that have similar relative value processes. But they are also advocating a full value style also, but avoiding deep value because deep value has done so well over the last five years. She further referred to page #14 that detailed more full value oriented companies.

ADJOURNMENT

** MR. MURPHY MADE A MOTION TO ADJOURN

** MR. PIRRO SECONDED

** MOTION PASSED UNANIMOUSLY

The meeting was adjourned at 9:05 p.m.

Respectfully submitted,

Diane Graham

Telesco Secretarial Services

