

Minutes of the Special Meeting of the Region 9 Pension Committee
October 24, 2011

Filed subject to approval

Attendees: Leon Karvelis, Chair, Thomas Logie, David Boczar, Jeanne Wendschuh, Peggy Sullivan, Michael Welz (Investment Advisor with USI Consulting Group). No members of the public attended.

1. Call to order at 5:32 pm in the Career Center at Joel Barlow High School.
2. Motion to approve the minutes of the September 28, 2011 meeting was made by Mr. Logie, seconded by Mr. Boczar, and approved (Mr. Karvelis abstained).
3. There was no public comment.
4. Mr. Welz thoroughly discussed the information detailed in USI Advisors, Inc.'s Investment Review for Easton-Redding Regional School District #9 Retirement Plan based on Plan Assets as of September 30, 2011, which were emailed to the committee in advance of the meeting. He reviewed the market highlights (page 4) and noted that only two investments remain on "Watch" at this time, Davis NY Venture and American Funds Growth Fund of America.

USI continues to be concerned with Davis NY Venture's strategy and performance (discussed at length in the September 28, 2011 meeting) and reported that the fund had failed to capitalize on the recent energy rally since its holdings are more heavily weighted in natural gas than in oil. Mr. Logie pointed out that natural gas has recently decoupled from oil. Mr. Welz offered to forward the September 30, 2011 attribution analysis for Davis NY Venture when he receives it.

Mr. Welz noted that American Funds Growth Fund of America has struggled in the up markets of 2009 and 2010, largely due to the mega cap bias its portfolio tends to have since larger growth stocks have lagged those of smaller capitalization during this period. Investors have withdrawn substantial amounts from this fund since January 2010, it is a very large fund with low turnover, and its underperformance has raised sufficient questions that the fund issued a formal comment titled "An update on The Growth Fund of America" in October 2011 to address some of those questions, including concerns that the fund's total assets may be too large to be manageable. Mr. Welz distributed copies of the update to the committee (and a copy is attached to these minutes). He commented on the fund's unique portfolio management structure with counselors' compensation based on 3, 5 and 7-year (long term) performance. Mr. Welz reported that all twelve of USI's managers at a recent USI meeting expect the American Funds Growth Fund of America to return to its normal levels of performance.

5. Mr. Welz then discussed the Economic Review – Summary of the third quarter (page 5), saying that this is input to help us determine where we see the economy moving in the future. He noted that growth was much less than expected at this stage of a recovery. He referred to a recent ECRI (Economic Cycle Research Institute) outlook that "the US economy is indeed tipping into a new recession. And there's nothing that policy makers can do to head it off." Consumer sentiment and spending are about where they were when Lehman Brothers collapsed and throughout 2009. There have been no improvements in jobs. The housing market continues to struggle and it is hard to imagine an exogenous event that might turn it around. The one bright

spot in the economy is increasing corporate profits in the 2011 second quarter over the 2010 second quarter, but they may begin to face headwinds if they haven't already. The Consumer Price Index is rising steadily.

The Federal Reserve announced that interest rates will remain extremely low into mid-2013 and has begun "Operation Twist" to extend lower interest rates to long-term bonds in an attempt to stimulate consumer and business spending. Mr. Logie commented that Operation Twist is distorting interest rates and markets. The Plan's fixed income investments expose it to interest rate risks and Mr. Welz advised the committee to devise our investment strategy to prepare for the time when interest rates begin to rise.

Internationally, the markets continue to be challenged by Europe's debt issues, basically another "toxic assets" situation (i.e., loans that cannot be fully repaid), and it is uncertainty how or when the European Union may resolve Greece's sovereign debt problems. Unlike the Lehman Brothers situation, Mr. Welz commented that Europe's debt risks are relatively known, but characterized these Eurozone issues as primarily political and structural, suggesting that the EU is not really united but it is more a group of separate nations called on to bail out other countries. Mr. Logie elaborated saying that the Eurozone issue stems from past lending to countries that could not and cannot afford those obligations and the need of the stronger core EU nations to maintain the Euro to support their exports.

Pages 6 through 12 graphically show some of the highlights of the economy. In reviewing them briefly, Mr. Welz noted that there has been no meaningful recovery in employment, wondered how long corporate profits could continue to rise without revenues increasing, and wondered when elevated oil prices would begin to impact the transportation sector.

6. Mr. Welz continued with a review of capital markets. The data on page 13 highlight that investors have continued to move money out of equities and low-yielding money market funds and have maintained a rather steady flow into taxable bonds. The data on page 15 report negative returns for domestic and international equities in all 2011 periods with small cap and mid cap stocks underperforming large cap stocks. During the recent downturn, riskier equities yielded worse "returns" than those with less risk. Pages 16 and 18 graph domestic equity returns by size and style and page 17 reports their returns by sector.

The data on page 23 report fixed income returns. Mr. Welz noted that except for corporate high yield, fixed income returns were solid in the third quarter and 2011 year to date. He repeated his concern that the committee urgently address the question of how to position the Plan's fixed income portfolio going forward, to determine a fixed income strategy that will contribute to achieving reasonable, expected portfolio returns. He noted the impact of a 1% rise or fall in interest rates, shown on page 25, highlighting the 8.8% price decline in 10-year Treasuries expected to result from a 1% rise in interest rates.

7. Then Mr. Welz reviewed the status of the Plan's assets (particularly pages 30 – 33). He pointed out that the committee had previously decided to hold recently contributed money in cash until now (nearly \$399,000 in money market funds at September 30, 2011). Referring to page 32, he highlighted the three categories that were outside the Plan's strategic allocation limits – domestic equity, DFA all equity portfolio and cash. Referring to page 33, he highlighted the Plan's \$357,000 in contributions, \$45,000 in benefit payments and \$336,000 in investment losses

during the third quarter of 2011.

8. Moving on to the investment analysis, reviewing the time-weighted portfolio analysis on page 41, Mr. Welz pointed out that the Plan's portfolio during the third quarter of 2011 was more heavily weighted to fixed income and less heavily weighted to equity than the 60% S&P500/40% Barclays Aggregate blended index to which it's return is compared. (See page 32 of the Investment Review for the September 30, 2011 47% equity/53% fixed income weighting and page 36 of the Investment Review for the June 30, 2011 58% equity/42% fixed income weighting.)

In reviewing the consolidated analysis on pages 42 through 45, Mr. Welz commented on each fund's performance as reported there, highlighting individual performance that varied from its peer group or benchmark. He noted that the 1-year return is also included in the 3-, 5- and 10-year returns, so one must also look at performance in each discrete year. He also pointed out that with international bonds, in addition to collecting interest at the coupon rate, an investor is exposed to currency risk.

9. Mr. Welz then directed the discussion to rebalancing the Plan's portfolio. In response to the committee's request, Mr. Welz had provided information (pages 86 through 89) on Pioneer Equity Income A and T. Rowe Price Equity Income R, two investment alternatives to Davis NY Venture A, which he reviewed briefly, pointing out differences in their up capture and down capture ratios and noting that dividend become more important when investing in such large cap equity funds.

The committee estimated that the Plan would need to keep approximately \$140,000 in cash to provide for benefit payments until the next Plan contribution (approximately \$15,000 per month), leaving approximately \$240,000 available for investment (of \$383,000 held at October 24, 2011) and recognized that the Plan's assets were valued at \$3,076,000 on October 21, 2011.

Referring to the portfolio changes Mr. Logie had suggested at the committee's September 28, 2011 meeting, Mr. Boczar proposed the following actions to rebalance the Plan's portfolio:

a.

- **Selling the entire position in Davis NY Venture**
- **Reinvesting \$50,000 in JPMorgan High Yield A (currently held in the portfolio)**
- **Reinvesting the remainder in Pioneer Equity Income A (new to the portfolio)**

b. From the \$240,000 cash available for investment

- **Investing \$180,000 in the DFA All Equity Portfolio**
- **Investing \$20,000 in Ivy Asset Strategy A**
- **Investing \$20,000 in Invesco Developing Markets A**
- **Investing \$20,000 in Columbia Acorn International A**

All members of the committee concurred with the actions proposed by Mr. Boczar.

10. **At the January 30, 2012 meeting the committee will decide how to reallocate its fixed income investments to seek reasonable total returns without incurring unreasonable risk during the continuing low interest rate period and looking forward to rising interest rates**

in the future. Mr. Boczar suggested paring down investments in more volatile bond funds (including Oppenheimer International Bond N and Oppenheimer Senior Floating Rate A) and moving those amounts into investments in Pimco Real Return A as a possibility.

11. Mr. Logie noted that this was his last meeting as a member of this committee but said that he plans to attend the January 30, 2012 meeting. Mr. Karvelis acknowledged Mr. Logie's considerable contributions to the committee and thanked him for his service. All attendees expressed their appreciation for his contributions and service.
12. The meeting adjourned by mutual consent at 6:46 pm.

Respectfully submitted,

Jeanne Wendschuh, Secretary