MINUTES
PENSION TRUST COMMISSION
SECOND FLOOR CONFERENCE ROOM
NEW CITY HALL
JULY 27, 2017 – 9:00 A.M.

Bart Hadley called the meeting to order at 9:00 a.m. in the New City Hall Second Floor Conference Room. Notice of meeting and agenda was posted on the City Hall notice board as required by law.

ROLL CALL

PRESENT: Bayones, Teri; Dentler, Carl; Ellwanger, Paul; Hadley, Bart; Hill, Andy; Livingston, Steve.

ABSENT: Kindt, Bill.

ALSO PRESENT: Denise Ezell, City Clerk's Office; J.I. Johnson, Finance Director; Perry Warren and Chad Rother, Morgan Stanley; Chase Massey, Human Resources Director.

II. Introduction of Visitors

Hadley stated we have no visitor today.

III. Approval of Minutes from April 13, 2017

Warren stated on the second page it should say 6.75 instead of 6.5.

Motion by Ellwanger, **Second** by Bayones, to approve the minutes of April 13, 2017 with stated corrections. **Aye**: Dentler; Ellwanger; Hadley; Hill; Livingston; Bayones. **Nay**: None. **Motion Passed**.

IV. New Business

A. Receive quarterly financial report from Morgan Stanley and take action if necessary – Perry Warren, Morgan Stanley.

Warren stated we would like to thank the Authority for the opportunity to be here each quarter. We have spent a good amount of time the last 3 years working on many things to include the asset allocations. With your permission we were able to adjust the asset allocation from 35% equities to a target of 50% with the ability to go as high as 70% or as low as 30%. In 2016 we created the benchmark that we named the Employees Retirement System of the City of Lawton Benchmark and the acronym is ERSOCOL. We made the changes based on the environment we have been in and with the understanding of the required return deeded by the plan. We look to continue to adjust the portfolio and to manage the account according to the plan goals and objectives.

Warren stated on page 4 you see the dollar weighted return. Year to date is 7.33, 2016 calendar year was 7.05 and 2015 -2.54. Each calendar years return is listed all the way back to inception.

Warren stated page 6 in the upper left quarter of the page you see the numbers under performance since inception. We started with $34,679,131; we have taken out $5,094,875 and investment earnings of $21,512,841. This leaves us with an account balance of $51,097,098. The return since November 13, 2007 has been 5.13%, 5 year return of 6.54% and 1 year return of 13.14. During the same period of time our benchmark has earned 9.33%. This is the first full year to compare versus our ERSOCOL benchmark. We outperformed the actuarial number during the last 12 months of 6.75%. Note that the Barclays Aggregate Bond return for the last year was -.31. To the right you see the 5 year return is 2.21 down from the 4.2 since inception. We anticipated this would occur.

Warren stated page 7 has been in most of our reports. I want to point out that since our change in allocation was the biggest internment in our results. Reducing bonds and increasing equities was the determent.

Warren stated on the next page you see the portfolio x-ray. This allows us to drill into the holdings of the account to see how the portfolio is positioned. The current asset allocation shows the account has 6.7% in cash and this includes the cash in the mutual funds we are holding. We have 69.94% in equities with 62.47 in domestic and 7.74% in international. Bonds and alternatives make up the remaining 23.29%. We have been selling domestic equities as the market is rising to maintain our target. We expect to continue to selling to maintain our asset allocation. The triangle to the rights show the portfolio position is neutral in reference to stock sectors. This means defense stocks, economically sensitive stocks and cyclical stocks. In the investment style selection look at the first 2 tic-tac-toe boxes. This shows that 45% of our bonds are in short term bonds and 32% in moderate term bonds. This reflects our stance on interest rates along with the duration of 3.91 years for our bond holdings. You see in the equity style box we are maintaining our balance between value and growth with a bias towards large companies. It shows 70% of our equities are in large companies.

Warren stated page 13 shows the asset allocation in dollars and percentage value. The cash in this account on the 24th was $647,947 and $300,000 was scheduled to be sent to the bank for distributions. We are not keeping much in cash at this time. Notice the 1.3% compared to the asset scan which is the actual cash we had to work with. The difference is the cash that the mutual funds own themselves.

Warren stated we have been over page 14 many times. It reflects the efficient frontiers for the last 20 years and the current 7 year forecast and the 20 year forecast. We have increased our equity exposure and volatility in an attempt to reach the actuarial 6.75% return. We are hopeful as rates rise that we will be able to reduce equity exposure and still reach our actuarial return. With bonds performing 2 or 2.2 and you have half of it there you are making one half of the portfolio. This means the other half has to make up 5.75 and you double that and that number is too big to expect from equities. This is why we are allocated the way we are.

Warren stated turn to page 15. With the higher allocation to equities we have reviewed this chart each meetings. I want to discuss and be aware that we have negative months, quarter and years. We believe the asset allocation is appropriate due to the long term nature of the account and combined with the performance goals of the account. We have to be mindful with the allocation we have in equities that the median declined entry year is 10%. With that much in equities it will fluctuate. We need to know that before it fluctuates. If we come in here next quarter and we have a big sell off we don't need to decide at that point to reduce our equity exposure.

Warren stated turn to page 16. At the last meeting Livingston pointed this out and I want to cover it. This shows investor psychology cycle. I want to point out that at this time we are not reducing our international equity exposure. We have been over weighted in domestic equities the last few years because internationals are separate. Recently international stocks have increased at a higher rate than domestics. They are still far behind on average. On page 6 in the performance since inception you can see that the world market since 2007 has made 1%. It has a ways to go to catch up. We have been over weighted in domestic equities and throughout the year we have sold off $2 to $3 million of equities and have bought bonds and made distributions. That is the reason we are keeping it right where we are. If you have one part of the portfolio that is going to make 2.25 and the other lose 10% but then make 10% this forces us over the longer period of time to be selling to buy bonds as they become cheaper. We have been over weighted in domestics the last few years and it has been beneficial. When we sell domestic equities we are knowingly increasing our allocations international equities. I think it is okay to increase it but we are not going to sell all our domestics and buy internationals. We are just letting that happen. Thank you for your time and I'll be glad to answer any questions.

Ellwanger stated we have about 70% of our portfolio in equities and that is why we are performing. You mentioned that we need to be prepared for when there is a downturn. Talk about that. Why do we want to be at 70% versus 50%?

Warren stated I would prefer to be at 50%. Mathematically at 50% right now and with the return on bonds you have to accept the fact that we were going to make 5.5%. I don't like being there. If there is an account that is appropriate to be at this level it would be this account because it is longer term in nature. If we could get 4% from our bonds that has us making 2%. To get to the 6.75% we need about 9 from our equities. That is doable. Over time 8 to 10 would be doable. With rates so low and likely to rise the performance of the bond is going to be about 1 or 1.25. That is the reason I made the comment if interest rates rise we can pull down on equities. As a board you could say we want to go to 60% equities. But within the guidelines we have we are there because the odds are greatly in our favor that over a period of time we will do it. If we are going to change the allocation it would be a good time to change it. If we change it we are aware that we are going to have to really out perform on the equities side to make the number.

Ellwanger asked so between now and the next time we meet if there is an adjustment in the market you are prepared to move right within the guidelines we have given you.

Warren stated yes.

Hadley asked and you have that ability with our guidelines.

Warren stated yes. We don't want to be market timers. That is not our deal. That is the reason we are having the discussion of where our allocations is. I don't know if you watch the 10 year treasury but 2 days ago is was up a bunch. The price of the 10 year treasury was 1.5% on something that yields 2%. Then yesterday it went back down. This morning it was back up because the feds announced there is $4.5 trillion they have built up in their balance sheet and they are going to unwind it. Nobody knows how that is going to happen and we have never had that happened. They quit buying more so they could be neutral. Now they are buying back what has matured. If they quit then the price will fall. That is the reason we have made several sets and we will do one again. The market is moving. It doesn't take long and its back over and I'll bring it back. Look at the red dots and you see every year you have some type of correction. One of the lowest is 2017. We need to be prepared if we have a 10% correction and we drop $3.5 million we need to accept that in order to have a median return of 12%. We are at 70% equities as opposed to 50%. In order to make the 12% over the long term you have to be willing to suffer a 10% decline in the short term. If we had 5% bonds our allocations would be different. When you count on 2.5% from bonds we would have to get 8.5% from equities. It makes sense to be allocated where we are. Domestic equities are high with all the overweight we have. So we have it in large domestic equities. They outperform overtime. I need to put another sheet in the report that shows the last 20 years of returns. A year ago the 20 year return difference between stocks and bonds was 1%. That is because over 20 years we had the last decade and the decline in 2007. That was a bad period for stocks. We don't know if it is going to be that way going forward. The forecast is you are not going to make a whole lot. Bonds have gone down from 5.25. You can look at the numbers on page 6. The Barclay Aggregate is the total bond market. It has dropped since 2007 from 4.2 to averaging 2.2. That is the driver of the change in allocation. That is the reason we are grateful the board let us change from where we were to where we are. It is not because we want to take more risk. It has to do with the function of where the environment is and what the anticipation from the account needs to be. That is the reason I said that as the environment changes we are going to change too. We want to be at the minimum amount of risk to meet the actuarial number over time. It would be great if we could go back to the 80's and be 80% bonds and 20% stocks to hedge off inflation. The last 12 months was good and that allowed the index that was 50/50/ to be 9.3 but we have had a market that was well above average. The 50% that was in bonds drug that down. We anticipated that would happen the last couple of years. Interest rates haven't moved. A year ago they were one of the lowest for the 10 year treasury. It rose from 1.4 to 2.4 by November. Since November interest rates fell. Not back to 1.4 but around 2.2 which leads to this overall bond market. Cash was better than bonds. We are going to be declining our amounts in equities over time if rate will cooperate.

Ellwanger stated thank you.

Hadley stated good discussion.

Motion by Hill, **Second** by Ellwanger, to accept the Morgan Stanley Report. **Aye**: Ellwanger; Hadley; Hill; Livingston; Bayones; Dentler. **Nay**: None. **Motion Passed**.

B. Receive Quarterly Employees Refunds Made From Retirement System and Receive Quarterly Statement of Receipts and Disbursement and take action if necessary – Finance.

Johnson stated the balance sheet shows that on June 30th we had total assets of $53,112,343. A little under a million of that is our cash in the bank or money market investment of the portfolio. Investments in bonds, stocks and judgments are $51,000,000, liabilities of $197,932 so the equity position was $42,914,410. On the next page you see the last quarter revenues exceeded the expenditures by $1,115,000. Ninety percent of this is due to the unrealized gains/losses we made on our investments. Those unrealized gains/losses were $1,102,583. You see a net increase income of $4,353,041. This increased our fund balance from $48,561,368 to $52,914,410. The last page is a listing of the refunds made from the retirement system totaling $151,381. You see this in the 4th quarter expenditure on the second page.

Hill asked is the $65,000 an employee that has left the city and taken his funds.

Hadley stated yes.

Hill asked wouldn't an employee with that type of refund have been able to retire.

Hadley stated sometimes the employee has been terminated. I don't know that was the case with these employees.

Hill asked is their alternative to leave it in the plan and then at retirement age draw a retirement.

Hadley stated if they are vested. I would say with that amount they would have been vested. Sometimes it is a life situation. People get in a bind and they view this as being their best option to get out of trouble.

Massey stated I believe both of those employees were vest. They were not eligible for retirement and chose to take a lump sum.

Hadley stated hopefully they reinvested it somewhere.

Ellwanger stated the balance sheet doesn't show a pension liability. Does it need to show our liability? Doesn't the city have to record that on their financials?

Johnson stated yes.

Livingston stated it would be the same every quarter. It is only updated after the actuarial report.

Hill asked based on the last actuarial report weren't we around $30 million short of being fully funded.

Hadley stated if I'm remembering right it was $34 million plus.

Johnson stated overall I would say that 2017 was a really good year.

Motion by Ellwanger, **Second** by Dentler, to accept the treasurer's report. **Aye**: Hadley; Hill; Livingston; Bayones; Dentler; Ellwanger. **Nay**: None. **Motion Passed**.

V. Old Business

None

VI. Consent Agenda

FOR THE BENEFIT OF THE AUDIENCE, ALL MATTERS LISTED UNDER THE CONSENT AGENDA ARE CONSIDERED TO BE ROUTINE BY THE PENSION COMMISSION AND WILL BE ENACTED BY ONE MOTION. THERE WILL BE NO SEPARATE DISCUSSION OF THESE ITEMS. IF DISCUSSION IS DESIRED, THAT ITEM WILL BE REMOVED FROM THE CONSENT AGENDA PRIOR TO ROLL CALL AND WILL BE CONSIDERED SEPARATELY.

A. Consider Memo of Information regarding the death of Bennie Marie MacDonald the beneficiary of retiree Marshall MacDonald.

B. Consider Memo of Information regarding the death Helen Pruitt the beneficiary of retiree Buford Pruitt.

C. Consider approval for the paid-in-full judgments to be released from the record.

Motion by Hill, **Second** by Livingston, to approve the consent agenda. **Aye**: Hill; Livingston; Bayones; Dentler; Ellwanger; Hadley. **Nay**: None. **Motion Passed**.

VII. Comments

Hill asked when will we receive our next actuarial report.

Johnson stated I have them working on it now. I hope it will be complete sometime in late fall.

Hadley stated as a reminder as of July 1 this pension system is closed to all new employees. New employees are on the defined contribution plan. The city is matching the new employees at 3.5% and the remaining 6.5% will continue to go into this plan.

Ellwanger asked if council makes a change to that number they cannot do so without board approval.

Hadley stated I wish that was the case. This council has committed to not touch the 6.5% until we have reached 100% funding. The actuary says we have to continue that amount for at

least 20 to 25 years to keep this plan a float. When we made the amendment to the trust we built in that Council cannot make any changes without first bringing it to the Trust and allowing them to investigate and make a recommendation. They still have the ability to go against the recommendation. They can't make a change without giving us the opportunity to address it.

VIII. Audience Participation

IX. Adjournment

There being no further business the meeting adjourned at 9:35 a.m.

Motion by Dentler, **Second** by Ellwanger, to adjourn. **Aye**: Livingston; Bayones; Dentler; Ellwanger; Hadley; Hill. **Nay**: None. **Motion Passed**.