CITY OF PONTIAC MICHIGAN
GENERAL EMPLOYEES RETIREMENT SYSTEM
BOARD OF TRUSTEES SPECIAL MEETING –July 25, 2006

A Special Meeting of the Board of Trustees was held on Tuesday, July 25, 2006 at the Municipal and Health Services Credit Union, 144 East Pike, Pontiac, Michigan 48342, Lower Level Conference Room. The meeting was called to order at 1:11 p.m.

ROLL CALL:

TRUSTEES PRESENT

Shirley Barnett
Kone Bowman (arrived at
Ray Cochran, Secretary
Robert Giddings
Charlie Harrison
Javier Sauceda, Vice Chairman
Devin Scott (arrived at 1:24 p.m.)
Kevin Williams
Debra Woods
Andrea Wright (arrived at 1:19 p.m.)

TRUSTEES ABSENT

Mayor, Clarence Phillips (absent)

OTHERS PRESENT

Laurence Gray, Gray & Company
Andrea Coffey-Stewart, Gray & Company
Tom Michaud, VanOverbeke, Michaud & Timmony
Ellen Zimmermann, Retirement Administrator
Jane Arndt, Retirement M-Admin Assistant

Gray & Company -Trustee Development Session

Larry Gray explained that the training would be broken down into three segments; the Investment Policy Statement, The Basics of Asset Allocation and Evaluating Managers and Selecting the Appropriate Benchmark. He encouraged questions and feedback during the session.

Andrea Stewart began with the Investment Policy Statement. She informed the Board that they would be voting to accept the revised Investment Policy Statement at the July 26, 2006 Board Meeting.

She outlined the statement saying that it contains the basic information of the plan displaying contact information, who pays into the plan, beneficiaries of the plan, what benefits are paid out and when. She reviewed the role of the Board, the Retirement Administrator, Investment Consultant, Custodian, Actuary and the Investment Managers.

Trustee Wright arrived at 1:19 p.m.

Trustee Barnett questioned whether the Board is adhering to the requirement for due diligence. It was explained that Gray and Company is handling the due diligence process on behalf of the Board. Ms. Zimmermann commented that it makes more sense for the consultant to handle that process because they are the experts and that they've been trained to make the assessments.

Ms. Stewart stressed the importance of meeting the funding obligations, the diversification of investments, the establishment sound investment policies, the definition of permissible investments and their relationship to doing what is in the best interest of an institutional investment.

The target asset mix and the rebalancing process were discussed using an example of why it is important to shift assets in order to keep the asset allocation in line. Ms. Stewart stated that it is important to comply with the policy. Mr. Gray commented that it requires discipline to rebalance to meet asset allocations. He emphasized that the greatest part of a fund's return is generated by the asset mix, not the managers selected. Chairman Harrison questioned how it is determined which manager to take the distribution from. He was told that you usually take from the winner. Mr. Gray said to think of it as a risk-management tool.

Trustee Bowman arrived at 1:35 p.m.

Manager selection criteria were summarized stating the importance of style, discipline, past performance, staffing and level of experience and assessment of future investments. Ms. Stewart commented that during the assessment process past experience is not any guarantee of future success.

Ms. Stewart detailed the prohibited investments and derivative policy sections of the Investment Manager Guidelines. She reviewed the domestic equity section noting that managers are to be fully invested and are to manage for the long-term. She also explained the revisions in the domestic fixed income managers and international equity manager sections which need to be adopted at the meeting on July 26, 2006. The changes were made to accommodate the criteria of the high yield investments.

Manager probation and termination was discussed at length. It was stressed that the Board needed to be 100% sure the termination of a manager is in the best interest of the fund. Criteria for probation or termination include turnover of key personnel, especially if the Board is not notified. Another cause is if a manager's performance is in the 75^{th} percentile or below for two consecutive quarters. These reasons are identified in the policy as an objective way to determine whether action is warranted.

Trustee Wright left at 1:48 p.m.

Commission recapture programs were reviewed. Chairman Harrison asked if there is a list of local companies. Ms. Zimmermann said that the list was compiled by the committee but that it had not been update recently. Mr. Gray suggested revising the policy to include commission recapture. Ms. Zimmermann commented that securities lending makes significant contributions to the fund and that monies recovered by commission recapture are very small in relation.

Ms. Stewart asked if there were any questions. Ms. Zimmermann commented that if the trustees don't have time to review the entire policy, that the Board should read the sections on their roles and responsibilities and manager termination.

Chairman Harrison stated that the current consultant has added a level of consistency that they did not have with the past two consultants. He spoke about manager termination and how it was difficult to put a manager on probation or terminate because the consultant never started the clock to monitor a manager. Ms. Zimmermann stated that there was no policy when she started. *Trustee Scott left at 1:58 p.m.*

Meeting Break at 2:00 p.m.

Meeting Resumed at 2:10 p.m.

Trustee Wright returned at 2:10 p.m.

Mr. Gray presented the basics of asset allocation. He began by stating that asset allocation is the holy grail of the investment business. He said that it is the most important element of a fund's policy. It is important because it balances risk versus return and determines long-term returns.

Asset allocation and rebalancing are important because they minimize negative returns, minimize frequency of negative returns and minimize the duration of negative returns. He showed how difficult it is to recover from negative returns. He showed an example of return attribution comparing asset allocation to manager performance and their relationship to returns.

He told the Board that asset allocation is not picking or predicting individual stocks or timing the market. Asset allocation is set to clearly identify plan's goals and objectives along with evaluating the plan's time horizon and risk tolerance of trustees. The asset allocation comprises over 90% of the returns of a fund.

Targets are clearly detailed and defined by the Investment Policy Statement. Once the asset allocation has been set the manager structure will be defined.

A risk return chart was displayed showing the 79-year growth of $1 million dollars ending December 31, 2004. It showed the various investment opportunities with viable calculated numbers and the standard deviation of each investment.

A wealth indices of investments chart was show which compared the values of risk versus returns and the importance of diverse allocation. Asset class returns for 1926 – 2004 were shown displaying annualized returns.

Mr. Gray explained risk as losses, uncertainty and volatility. In order to achieve repeatable results you cannot avoid risk. He said you have to look at risk as an opportunity and that it is the currency used to "buy" returns. He referred to a chart that showed total annual returns in percentages by investment showing annualized returns and risk; it illustratedto the lowest to the highest returns.

Trustee Bowman left at 2:27 p.m.

Trustee Wright left at 2:29 p.m.

Trustee Bowman returned at 2:30 p.m.

Trustee Wright returned at 2:31 p.m.

He told the Board that the key to asset allocation is controlling risk, not about predicting returns. A good investment policy is a statement about risk more than a forecast of returns. In order to control risk you have to diversify your investments by asset classes, managers and securities. A chart showing diversification by subcategories was reviewed.

He discussed correlation of asset classes and how it affects risk-return characteristics. Historically, when some assets are up, others are down. Steady returns compound faster then a portfolio with more ups and downs.

He showed annual returns and risks by asset classes based on historical and contemporary (more of a global economy) investments. Examples of asset mix comparisons were shown and how the appropriate mix of buckets can reduce risk and increase rates of return.

A number of investment return assumptions by allocation of stocks and bonds were shown and how it affects the rate of return. This showed the how important it is to rebalance to your target within an asset class.

Mr. Gray concluded by stating that rebalancing can be achieved by transferring assets among asset classes and by utilizing cash flows. He said that it is sometimes compared to "whipping your best child" when money is taken from a high performing manager. He stressed that historically there is regression toward the mean in regard and favored asset classes tend to move through cycles. This increases the importance of rebalancing. He reiterated that you diversify in order to control risk, not to boost returns. He added that it is important to stay with those assets that you understand. Mr. Gray ceded his remaining time to Mr. Michaud.

Tom Michaud told the Board that education is an ongoing process that will require a time commitment from the trustees. He also mentioned that if the trustees have any specific topics they would like to cover to contact him or Larry Gray. He added that diversity is the mantra of investment and that liability is the mantra of fiduciary responsibility.

Chairman Harrison thanked Larry Gray, Andrea Stewart and Tom Michaud for taking the time to educate the Board. He added that he thought it was a good overview and a great start.

The meeting was adjourned at 2:55 p.m.

I certify that the foregoing is the
True Minutes of the Special Meeting of
the General Employees Retirement
System held on July 25, 2006

Raymond Cochran, Secretary

As recorded by Jane Arndt