CITY EMPLOYEES RETIREMENT FUND BOARD

MINUTES

DRAFT

SEPTEMBER 17, 2009

PLACE: City Hall
200 Orange Street
Dept. of Finance Conference Room
New Haven, Connecticut 06510

PRESENT: Jerry Sagnella, Chairman
Thomas Cama
John Varrone, Members' Representative
Mark Pietrosimone, Secretary

ABSENT: Mayor John DeStefano, Jr.

ALSO PRESENT: Joann Giri, Benefits Auditor
Tim Ryor, Hooker and Holcombe
Patricia Solomon
Derek Ciampini, Ameriprise
Chris Coppola, Ameriprise
Wendy Coppola, Ameriprise
Leslie Williams, Ameriprise

Mr. Sagnella convened the meeting at 10:05 a.m.

1. APPROVAL OF MINUTES

Mr. Varrone moved the approval of the minutes from the meeting of August 25, 2009; Mr. Cama seconded, and the vote was unanimous.

2. DEATH AFTER RETIREMENT – INFORMATION ONLY

a) Hughes, Loretta

3. WITHDRAWALS – INFORMATION ONLY

The Board reviewed the information under Item 3.

4. AGE ANNUITY RETIREMENT – INFORMATION ONLY

The Board reviewed the information under Item 4.

5. AGE ANNUITY RETIREMENT/PER STIPULATED AGREEMENT INFORMATION ONLY

The Board reviewed the information under Item 5.

6. PAYMENT OF BILLS

Mr. Cama made a motion to approve payment of the bills in Item 6; Mr. Varrone seconded and the vote was unanimous.

7. ADMINISTRATIVE MATTERS

Mr. Sagnella stated he would be soliciting competitive premium bids for trustee liability insurance coverage as well as coverage for legal fees. By the next meeting he will have three competitive bids. Mr. Ciampini noted that the Board only had a 30-Day extension and the coverage will lapse; he suggested extending the coverage for an additional quarter. Mr. Sagnella stated he would look into that possibility. Mr. Coppola stated if the policy lapses they may bump up the premium. Mr. Cama stated the new policy should go retroactive so there is no window in which there is no coverage.

Attorney Carolyn Kone was present at the meeting to provide an update on Northern Trust.

Mr. Pietrosimone made a motion to add an item to the agenda, "Review of teleconference with Northern Trust regarding securities lending"; Mr. Varrone seconded, and the vote was unanimous.

8. REVIEW OF TELECONFERENCE WITH NORTHERN TRUST REGARDING SECURITIES LENDING

Mr. Ciampini stated Northern Trust communicated a few important updates regarding Northern Trust securities lending. There were two big issues that caused the securities lending to have some realized losses, the Lehmann Brothers and the CIT group. The Fund held those bonds in the collateral pool which caused a realized loss. The money managers of the pool found it imperative to sell these bonds prior to bankruptcy; that caused a total realized loss of $51,666.

Up until recently Northern Trust has taken the stance that they are not going to require payment on the realized loss or the unrealized loss (the collateral deficiency); they have since changed this stance and by December 15 all of their clients have to pay their realized loss. Therefore, CERF has to pay $51,666 by December 15.

Mr. Ciampini stated Northern Trust is offering a staged liquidation of the collateral pool. Assuming the assets in the pool get healthier over time they will continue with the staged withdrawal process.

Attorney Kone stated CERF currently CERF has $318,000 in collateral deficiency; Northern Trust will reduce that collateral deficiency over time but they did not say when or how; they were clear that they are not allowing additional staged withdrawals.

Attorney Kone agreed that the fund is responsible to pay the $51,666 in realized loss. Mr. Sagnella stated Northern Trust is claiming if the market improves significantly those toxic assets become healthier and we could get to the point where we do not owe anything for collateral deficiency. Mr. Ciampini agreed but noted the fund still owes a realized loss of $51,666.

Attorney Kone stated you are still in the program, just reducing the collateral deficiency. Mr. Ciampini does not necessarily agree with Northern Trust's optimism regarding the collateral pool. The split used to be 60/40 where CERF received 60% of earnings and Northern Trust received 40%; Northern Trust changed the split to 70/30 to try to help CERF build back the loss.

Mr. Varrone made a motion to go into executive session to discuss strategy and negotiation regarding pending litigation; Mr. Pietrosimone seconded, and the vote was unanimous. The trustees and Attorney Carolyn Kone will remain in the room.

Mr. Pietrosimone made a motion to come out of executive session; Mr. Varrone seconded, and the vote was unanimous.

9. EXECUTIVE SESSION FOR POTENTIAL LITIGATION

There was no discussion under this item.

10. ALTERNATIVE INVESTMENTS – HEDGE FUND REPLICATION PRESENTATIONS

a) Natixis Alpha Simplex

Patrick Fitzsimons and Jeremiah Chafkin entered the meeting at 11:26 a.m. Mr. Fitzsimons is the managing regional director for the northeast Natixis. They are one of the fifteenth largest asset management firms in the world and their structure is that of a holding company; they own 18 money management firms one of which is Alpha Simplex based out of Cambridge, Massachusetts. Jeremiah Chafkin, the president and CEO of Alpha Simplex, is participating by telephone. Mr. Chafkin thanked the Board for the opportunity to present. His partner, Dr. Andrew Lo, is one of the pioneers in this area and continues to pioneer the technology and theory around hedge fund data replication; they think that their product is unusually robust and highly competitive. They are about 10 years old and specialize in absolute return strategy and specifically bridging the gap between alternative investing and traditional investing.

Andrew Lo is a professor at MIT in addition to publishing one of the earliest papers on the subject called" Can Hedge Fund Returns Be Replicated?" In late 2007 Alpha Simplex was acquired by Natixis Global Asset Management; that provided Alpha Simplex with the resources in regards to business management and marketing to allow Dr. Lo and his research scientists to focus on ongoing research and the investment process itself.

They have 22 employees and about $400 billion in assets; their investment philosophy is built on the idea that the world changes, markets change and your strategy needs to be adaptive to change with market conditions in order to continue to deliver the objective.

They think there is an argument for the asset class of alternatives not as some high risk satellite investment but rather a prudent and conservative asset allocation strategy; it stabilizes the overall return of a portfolio and enhances its risk return relationship. The chief benefit of hedge funds is the fact that they have historically not been correlated with traditional investments. They have only been available to wealthy investors and even among those only to those who were willing to sacrifice transparency and liquidity. They saw the opportunity to bring to the marketplace the advantages hedge funds but to do so with the transparency, liquidity and lower fees and minimums that are required by pension, public funds and retail investors.

Alpha Simplex has a bottom up replication process and a database with more than 1500 hedge funds in it. They have equal weight in each category. They scale the volatility of the overall portfolio to 8%. Since this product was launched October 2008 it allowed them to be battle tested early on. They told their investors that at any given time they were going to have an annualized volatility of 8%. In the 4th quarter 2008 their volatility was 7.92. The negative impact to the portfolio was minimal.

Mr. Sagnella would like to look at their performance record. Mr. Ciampini stated as of 9/30/08 when the S&P 500 index was down 20% the Alpha Simplex was up .19%.

Mr. Chafkin stated they made a conscious decision to forego some return to make sure they have a highly liquid, transparent portfolio.

They distinguish themselves by having a greater emphasis on liquidity. They also make a conscious decision not to be in junk bonds or emerging markets because they can become highly illiquid. They have exposure to more asset classes to produce more stable and reliable performance.

Return is only half of the equation; the other half is risk. While some of their competitors may appear to have higher returns on an absolute basis, when you look at return as a unit of risk, it is actually lower.

Mr. Ciampini asked what the minimum investment is. Mr. Fitzsimons stated the minimum investment for the mutual fund account is $1 million.

Mr. Fitzsimons stated the other thing that differentiates Alpha Simplex is Dr. Andrew Lo who is the brain trust behind this hedge fund replication concept; the other is risk control. They employ a 12% stop loss; if a strategy is not working they will scale their exposure at that 12% stop loss threshold. The third difference is their use of up to 30 different asset classes which means more diversification. Mr. Chapkin stated they rescale the risk daily.

Mr. Sagnella asked how many public clients they have. Mr. Chapkin responded they currently have no public funds. Mr. Ciampini asked about fees. Mr. Fitzsimons stated their fees are 1.4% per annum. Mr. Ciampini stated that is extremely inexpensive in this asset space.

Mr. Pietrosimone asked if Mr. Ciampini is recommending a mutual fund or a separate account. Mr. Ciampini stated the minimum for a separate account is $30 million which is too high for our fund. The investment would have to be a mutual fund.

Mr. Coppola asked what kind of contract they have with Dr. Andrew Lo. Mr. Fitzsimons stated he is locked in for 5 years starting last year, which is standard.

Mr. Fitzsimons left the meeting at 12:05 p.m.

b) Index IQ

Anthony Davidow, Adam Patti and Salvatore Bruno of Index IQ entered the meeting at 12:15.

Mr. Patti stated Index IQ focuses on building index based alternative investments. They differentiate themselves by being a small high touch firm. They are one of the pioneers of hedge fund replication, launching their first product in March 2007. Their product is fully transparent, fully liquid, and low cost.

Mr. Davidow stated they offer something that provides all the positives and removes all the negatives and makes the product available to everyone. They use ETF's which is unique. Sal Bruno is their Chief Investment Officer. Robert Whitelaw is their Chief Investment Strategist one of the pioneers in hedge fund replication.

Mr. Ciampini asked if there is any flexibility on the minimum investment for the separate accounts. Mr. Davidow stated there is some flexibility. Mr. Davidow noted that they do not invest in hedge funds; they invest in ETF's. They think that the size of the current hedge fund market makes it very difficult for hedge funds to perform.

Hedge funds have fee structures that are sometimes difficult to understand. Most have a 2/20 fee structure; 2% management fee and 20% of performance fee. Fees are something they are very sensitive to.

Mr. Bruno stated one of the key differences between their product and some of the others is they are trying to do hedge fund replication at the strategy level and have chosen six distinct hedge fund strategies that they want to replicate. They update their weights and exposures on a monthly basis. The final step is to put the six strategies together into the final portfolio. They see how each strategy has been performing over the last twelve months and put them together in a way to get high return, low volatility and high correlation to a broad hedge fund index. Each month they reallocate some portion of the portfolio across different strategies. They try to stay diversified by starting off with 1/6 of each strategy; they then allow the model to overweight or underweight (within limits) certain strategies depending on how that strategy has been performing over the past twelve months.

Mr. Ciampini asked if they limit their exposure to different sectors; Mr. Bruno stated each one is limited to be no more than one third of the portfolio. Mr. Davidow stated from a performance perspective they very well last year; their mutual fund was down 2.6% versus the market down 26% and the hedge fund market was down 18%.

Mr. Sagnella asked how long they have been in business. Mr. Davidow responded since June 2006. Mr. Ciampini asked if they have any municipal clients. Mr. Patti stated they do not.

Mr. Ciampini stated they are used to seeing long track records. Because this is a fairly new strategy a short track record is not a bad thing. Mr. Davidow stated although they do not have a lengthy track record the real litmus test would be their performance in the second half of 2008.

Mr. Ciampini asked what are the fees on the separate accounts of between $5-10 million under management. Mr. Davidow stated 70 basis points up to 10 and 50 basis points on the next 10.

Mr. Sagnella asked if they have a plan to deal with issues that affect the market such as healthcare, increased taxes, etc. Mr. Davidow stated they are not making forward projections and that their strategy is rule based. That helped them in the second half of last year. They feel we are likely going into an inflationary environment and have developed some other strategies which were designed to help with hedging the impact of inflation. Mr. Ciampini asked how many holdings are in the account? Mr. Bruno stated about 20. Mr. Ciampini asked what is the structure of the company as far as ownership. Mr. Patti responded that employees own about 50% of the company.

Mr. Coppola asked if they think hedge funds will ever be regulated. Mr. Davidow stated they will regulate the large companies but those are probably not the ones they need to be concerned about, but rather the smaller, fly by night firms.

They left the meeting at 1:10 p.m.

9. INVESTMENT REVIEW

Mr. Ciampini stated the trustees had discussed adding money to international fixed income. He would like to narrow it down to three candidates; Evergreen, Strategic and Mondrian. Mr. Ciampini would like the Board to set up a subcommittee meeting for the presentations. He would also like to push the next meeting to October 22, 2009.

For the month of August the fund was up 1.5% or $2.3 million versus 2.1% for the index. Year to date the fund was up 12.4% versus 12% for the index. The total Fund as of August 31, 2009 was $159,527,618. Mr. Ciampini reminded the Board that the City put in $9.5 million in July 2009. Munder continues to underperform; they will keep an eye on their performance. They were only hired 1.5 years ago.

The trustees preferred the second presenters, Index IQ. Mr. Ciampini stated there is a merit to hiring both. Index IQ is more concentrated and they go into emerging markets whereas Alpha Simplex does not. There is a basis for having Alpha Simplex, they are more diversified and more risk averse; it makes sense to have both of them to some capacity.

Mr. Coppola stated Alpha Simplex tries to replicate individual actual hedge funds. Index IQ is mimicking different strategies.

Mr. Ciampini stated they want to have an ultimate alternative weighting of 15% of the fund and save of that 15% a portion for commodities and real estate. They think 7-8% total allocation to a strategy like this looking at $13-14 million total. They would like to set aside an extra 6% available for real estate and commodities. Mr. Ciampini stated they also prefer Index IQ but feels the 2 firms compliment each other. He suggested allocating $8 million to Index IQ and $4 million to Alpha Simplex.

Mr. Cama made a motion to accept Index IQ to be funded at $8 million and Alpha Simplex to be funded at $4 million to; Mr. Varrone seconded, and the vote was unanimous.

The meeting adjourned at 1:30 p.m. on a motion by Mr. Pietrosimone and seconded by Mr. Cama and the vote was unanimous.

The next meeting was rescheduled to Thursday, October 22, 2009 at 10:00 a.m.

ATTEST:

____
Secretary