Doylestown Township Pension Advisory Committee
Minutes for July 13, 2020

In attendance: Ed Denton, Chairman; Sinclair Salisbury, Vice Chairman; Members: Robert Salanik, Joe Delikat, Colleen Mullin, Tom Burke and Detective Bill Mokriski.

Board of Supervisors Liaison – Jen Herring

Staff Liaisons – Ken Wallace, Finance Director and Stephanie J. Mason, Township Manager

Absent: Robert Salanik

Minutes Approval June 8, 2020:

On motion of Mr. Delikat, seconded by Ms. Mullin, the minutes of the June 8, 2020 PAC were unanimously approved, with the following changes:

Page, 2nd paragraph; after "Merck" insert "suggested that due to the size of the Township's portfolio going to Van Guard makes sense."

Last page, 1st paragraph; after "80% funding" add, "assuming 7.75% discount rate"

OLD BUSINESS:

Investment Policy Statement, Benchmarks, etc.

Mr. Burke provided the Committee with the attached handouts. The first was the review of the Equity and Fixed Income Portfolio that he believes will enable the Committee to create its own benchmark for the advisor to follow. He indicated that the US markets lead in returns and if the Township follows suit this would help. Also needs reference IPS.

Mr. Denton thanked Mr. Burke for putting all the details together for the Committee and believes this will be a good guide going forward.

Mr. Burke discussed the equity market performance and the reference policy benchmark performance and showed actuals vs. benchmark in the graphs as well.

Mr. Burke believes changing the language in the investment policy statement so that the advisor can add value is a strategy to be pursued.

Ms. Mullin indicated that the advisor does provide performance data now.

It was agreed that there was no reason to contest the information until PAC meets with Ms. Brede and that PAC can share with the Board of Supervisors going forward.

Mr. Burke indicated that there seems to be a disconnect between the advisor and providing no attribution information.

Mr. Delikat indicated that all equity funds are in index funds. All bond funds are actively managed.

Mr. Burke suggested that the advisor have a fixed income benchmark strategy. He indicated that there were three areas, geography, style and size to consider. He explained the differences between the midcaps, small caps, equities, large caps and that things are not clear in the information provided by the advisor. He further explained that you can be underweight in the large cap and overweight in mid cap. Large cap in the US maybe doing well. Quarter to quarter you need to know the performance of the subcategories as well. Equity benchmark of the US core value or growth, mid cap value or growth. Those are important things to know and where the funds are being placed.

Mr. Delikat indicated that hindsight is 20/20, but in the policy going forward it should address in a general basis and be simple to understand. Also, that the advisor gives attribution with the benchmark, that way the advisor is accountable for the overs and unders in performance of the plan. He also indicated looking back is fine but how do we improve going forward.

Mr. Burke indicated that the advisor constructs benchmarks to that MSCI and if it exceeds its value added, if it under performs there's no value and that allows the Township to judge the performance of the advisor.

On the last page of the information provided, Mr. Burke has a summary and recommendations.

Mr. Denton asked how we can communicate with Ms. Brede on the topic. It was consensus to share the report with Ms. Brede so that she is able to address it when she comes to present in August.

Mr. Delikat questioned why the Township didn't shop the service previously. He believes they should be shopped.

Mr. Denton indicated that the Committee is doing a lot to improve reports and further evaluate the reports. Next year's RFPs should be the big task, along with rewriting the IPS this year. It's going to be the roadmap for a new RFP.

Ms. Mullin indicated that Mr. Burke did great work and she indicated that Ms. Brede provided a blended benchmark. The blended benchmark can be found on page 22 of the report.

There was a question on seeing if the advisor should be tactical with long term view on growth and that should be clear in the IPS.

Mr. Delikat indicated that his opinion is that the bonds make up only 30% of the portfolio and that it is small enough to go to an index and not worry about fees anymore.

Mr. Denton asked what the next steps are.

Mr. Burke suggested sharing this information with Ms. Brede, so that she has an understanding of the ongoing dialog of the Committee and write up the ISP. It was suggested that Mr. Burke, Mr. Delikat and Mr. Denton work on that. Also, to ask Ms. Brede for a soft copy of the IPS so they can make editing easier. Consider doing an RFP in 2021.

NEW BUSINESS:

Discuss possible adjustments to Investment Performance Report prepared by Brede

It was indicated that Mr. Delikat and Ms. Mullin worked on this with Ms. Brede and provided the blended index that was missing. However, a lot of what the Committee wanted is provided.

Ms. Mullin indicated that page 22 provides the blended benchmark.

Mr. Delikat indicated that there was a lot of disclosure required.

It is anticipated to have the report by the end of July 2020 from Ms. Brede for review. The Committee will develop questions that Ms. Brede can address when she comes in August.

Mr. Delikat indicated that we need to take the data from Ms. Brede and dilute it for the Board of Supervisors to understand. So that it can be shown to them.

Discuss PAC objectives for balance of 2020

Mr. Denton asked what the objectives are. One is to focus on the discount rate and two, recommend Township contributions over the five years.

Mr. Delikat mentioned the place holder in the budget for the Committee, should not be negotiable and should be put in the budget and then discussed by the Board of Supervisors.

Ms. Herring indicated that it was good to have all the worst case scenarios in the budget for the Board's consideration.

OTHER ITEMS FOR DISCUSSIONI/FUTURE BUSINESS:

Review and refine report prepared by Brede going forward.

Finalize IPS.

Also, an education plan for the Board of Supervisors and the Committee. PAC has done some on the discount rate and the opportunity to present education in an executive summary on the IPS. To Educate the Board is important.

Mr. Delikat indicated that meetings should be held off-site, one on one, the Committee with the Board of Supervisors.

Ms. Mason reminded the Committee about the Sunshine Law, quorums.

Mr. Denton said it was a good idea to get everyone up to speed.

Ms. Mullin shared a conversation that she and Mr. Denton had with Mr. Kennedy on decoupling the plans. Contributions might be helpful to add more money to the Non-Uniformed Plan, but in terms of the discount rate to stay on the same path over the next 10 years for both plans.
It is anticipated that everyone in the non-uniformed plan will have retired or be near retirement in 10 years. Also the potential of a pension transferring risk to an insurance company was also discussed but not something typically done in the municipal sector.

Mr. Wallace indicated it did not appear Mr. Kennedy was in favor of decoupling the plans, but adding funds to the non-uniformed vs. uniformed plan could have consequences and needs further discussion.

Mr. Delikat indicated that there is a legal compliance on the MMO for the Township and that additional funds provide flexibility and Mr. Kennedy provides a frame of reference. Also, every 2 years Act 205 recalculates the gains and losses and are reflected in the MMOs.

Mr. Wallace indicated that the ten year MMO projection for the budget was sent to the Committee.

Ms. Mullin indicated that a middle ground is needed.

ADOURNMENT:

Being no further business the meeting adjourned at 5:57 p.m. on motion of Mr. Delikat and seconded by Ms. Mullin.

Respectfully submitted,

Stephanie J. Mason

Doylestown PAC
July 13, 2020

1) Equity Market Performance

For perspective, equity investment performance has improved/rebounded dramatically from the 1Q and the US market leads all regions:

	1Q	2Q	YTD (June)	One Year (June)
MSCI US	-20.0	+21.2	-3.1	+6.3
MSCI EAFE	-23.4	+14.2	-12.6	-7.4
MSCI EM	-23.9	+17.3	-10.7	-5.7
MSCI ACWI	-21.7	+18.7	-7.1	+0.3
MSCI ACWI (x US)	-23.9	+15.4	-12.2	-7.1
US/ACWI (xUS)	+390	+580	+910	+1340

2) Reference/Policy Benchmark Performance

Global Equity

ACWI ETF	-21.4	+19.3	-6.2	+2.2

Fixed Income

AGG ETF	+3.1	+2.9	+6.1	+8.6
65/35	-12.8	+13.5	+1.9	+4.4

Review of Equity/Fixed Income Portfolios

In an effort to get us (PAC) closer to a an agreement of establishing a Reference/ Policy Benchmark, I reviewed the Equity/Fixed Income investment profile in detail utilizing the data provided by the Advisor (as of 1Q 2020).

In addition, for reference purposes the current IPS states the following Asset Weightings:

	Range	Target	
Domestic Equities	40-55%	43%	
Int'l. Equities	10-25%	20%	
Real Estate*	0-5%	2%	65%
Fixed Income	30-45%	24%	
Cash	0-10%	1%	35%
Alternative Investments	0-5%	0%	

* Considered equities.

Observation: The goal of a Reference/Policy Benchmark should be to establish a "high level" simple to monitor base for broad asset allocation (65/35 Equity/Fixed Income, in our case). Thus, a two variable measure based upon standard ETF's becomes the "default" low cost proxy to asset allocation.

With a clear desire to have international equity diversification, the MSCI ACWI (iShares: ACWI; 33bps cost) aligns well to the objective and should be considered the Equity Investments Reference/Policy benchmark. Real Estate, as a separate asset class, is redundant as real estate (REIT) equities are already established as a portion (sector) of the ACWI.

While the fixed income universe is more complex and diverse, the IPS as currently constructed, does not distinguish among fixed income strategies/investments. The most commonly accepted depiction of "fixed income" in an asset allocation context is the Barclay's Aggregate (iShares: AGG; 6bps cost).

The below "weightings" for equity and fixed income strategies were clearly determined at the the discretion and advice of the Advisor and, no doubt, approved by the Plan(s) at some point in the past. This is where the Advisor "proves the ability" to add value to the overall portfolio performance. I believe it is the obligation of the PAC to critically monitor such "positioning" for efficacy. The Reference/Policy Benchmark is but one tool to facilitate this exercise.

Equity/Fixed Income Investment Profile

Equities

- All passive, ETF's
- 12 investments; 11 benchmarks
- Equity allocations are indicated by the Advisor as follows (as of 1Q 2020):

	S&P500 Blend (Core)	10%		
	S&P500 Growth	10%		
	S&P500 Value	10%		
	S&P Midcap 400 Growth	4%		
	S&P Midcap 400 Value	4%		
	S&P Small Cap 600 Growth	2.75%		
	S&P Small Cap 600 Value	2.75%		
	DJ Global US Real Estate	1%		
Total US Equities			44.5%	68% of total
	MSCI EAFE	15%		
	MSCI Emerging Markets	4.5%		
	DJ xUS Select RE	1%		
Non-US			20.5%	32% of total
Total Equities			**65%**	**100%**

- Performance v benchmarks: Not indicative of overall portfolio contribution or efficacy (+ or -) as the ETF's always closely track the benchmark (tracking error) to which they are indexed. That is, the "US Fund Large Blend" investment tracks the benchmark (S&P500 Total Return Index) within a few basis points reflecting the ETF fee netted against any income derived from stock lending activity by the sponsor. Therefore, performance relative to benchmarks is expected to be consistently within a few basis points of benchmark for all investments.

- Performance v Reference/Policy Benchmark: Assuming the MSCI ACWI as the equity asset class proxy, the 65% equity allocation can be compared. The ACWI consists of 57% US equity exposure, approximately 33% EAFE and 10% Emerging Market exposure. Thus, the equity portfolio has a "structural" overweight to the US market (68% v 57%) and an underweight to non-US international markets (32% v 43%).

The below represents two looks at the equity performance: 1) individual investments that outperformed the ACWI over the 2015-2019 period, and 2) individual investments that outperformed the ACWI by calendar year:

Investment *outperformance* of equity investments v. MSCI ACWI, five year period (ending 2019):

5 out of 5 years	None
4 out of 5 years	3
3 out of 5 years	2
2 out of 5 years	4
1 out of 5 years	3

Investment *outperformance* of equity investments v. MSCI ACWI, by calendar year (ending 2019):

2019	4 of 12 investments
2018	6 of 12 investments
2017	3 of 12 investments
2016	8 of 12 investments
2015	7 of 12 investments

Observation: The composition of the US equity portfolio is diversified by style and size. The S&P 500 Blend (Core), Growth and Value are approximately 85% large cap, 15% midcap. The portfolio has additional exposure to mid-caps (S&P Midcap 400 Growth and Value) and small caps (S&P Small Cap 600 Growth and Value). The ACWI is 80-85% large cap, 15-20% midcap; no small cap exposure. Thus the

- Performance v benchmarks: Relevant to the efficacy of the specific fund manager to "add value" relative to a given benchmark/strategy.

- Performance v Reference/Policy Benchmark: Assuming the iShares AGG as the fixed income asset class proxy, comparisons are more tenuous than that of the equity portfolio due to the diversity/complexity of the fixed income investment universe.

The below represents two looks at the fixed income performance: 1) individual investments that outperformed the relevant strategy benchmark over the 2015-2019 period, and 2) individual investments that outperformed the AGG by calendar year:

Investment *outperformance* v related BM, five year period (ending 2019)

5 out of 5 years	None
4 out of 5 years	4
3 out of 5 years	4
2 out of 5 years	None
1 out of 5 years	2
0 out of 5 years	1

Investment *outperformance* v iShares AGG, by calendar year (ending 2019)

2019	2 of 11 investments
2018	7 of 11 investments
2017	10 of 11 investments
2016	10 of 11 investments
2015	5 of 11 investments

Observation: Given the active fund manager aspect of the fixed income portfolio and the discretion of the Advisor in selecting investment strategies, the AGG is, admittedly, not as easily comparable as that with equities. That said, I do believe that selecting the AGG as the "baseline" fixed income benchmark is appropriate, for its simplicity in representing the broad asset class. Additionally, the AGG has a "core" exposure to US Treasuries (38%), which I believe are under represented in the fixed income portfolio.

portfolio is underweight large cap, overweight midcap and small caps are "off benchmark" to the ACWI.

I question the use of "equal weight" exposures to the S&P 500 Growth and Value (10% each) as the effect is neutralized due to the fact that the Growth + Value = Blend (Core). Thus, it is pointless to have two separate investments that offset each other with equal weights when the Blend (Core) satisfies overall exposure. Furthermore, the cost of the Growth and Value ETF's at 18bps are well in excess of the Blend (Core) at 4bps. Similarly, the same reasoning applies to the Midcap Growth/Value (4% each) and Small Cap Growth/Value (2.75% each) exposures which are high cost (24-25bps) alternatives to a composite midcap/small cap index (6-7bps).

While the portfolio holding in the USMV (iShares MSCI US Min Vol ETF) is not explicitly specified in the above weightings (measured against the S&P 500), this is a viable investment option for the portfolio, in my view. It is an instrument (MSCI US market index based) that provides downside protection in its portfolio construction, focusing on a low volatility factor investing discipline. Disclosure: The UN Pension Fund was a "seed" investor in this ETF at inception in 2011.

Fixed Income

- All active, fund managers
- 11 investments; 8 benchmarks/strategies
- Fixed income allocations are indicated by the Advisor as follows (as of 1Q 2020):

BofA ML US High Yield	3%
BofA Libor 3 M Constant Mat	9.75%
BB Barc US Aggregate	3%
S&P/LSTA Lvg Loan Ix	3.25%
BB Barc USGov 1-5 yr	6.5%
BB Barc US Univ Bond	5.5%
JPMorgan EM Bond	1%
FTSE Non-USD WGBI	3%
Total Fixed Income	**35%**

In the current allocations, the underlying AGG index accounts for 8.5% (3% of 35% total) of the fixed income benchmark. In my view, the fixed income portfolio strategies are diverse, complex and many are related to high risk market segments such as emerging market debt, leveraged loans, mortgages and high yield debt.

Such risks in these asset class must be balanced against the strategic purpose of the 35% allocation. That is, the overwhelming majority of the long-term expected investment returns for the Plan(s) will be derived from equity investments, with fixed income acting as a "ballast" in equity drawdown periods (such as 1Q 2020). For this reason, I believe we (PAC) need to be particularly aware and diligent in our review (implicit approval) of the utilization of such strategies.

Summary/Recommendations:

1) Adoption of a "high level" 65/35 asset allocation proxy will provide the PAC with insight into the general performance of markets, in a given period. This is easily calculated and provides a "real time" look at market performance.
2) The PAC needs to request that the Advisor construct a composite benchmark for BOTH equity AND fixed income strategies, weighted to the disclosed allocations.
3) The PAC needs to request that the Advisor construct a composite investment performance measure for BOTH equity AND fixed income investments, weighted to the actual exposures.
4) This will provide the PAC with the ability to compare (3) with (2) utilizing (1) as a broad baseline for a 65/35 portfolio. This will highlight specific investments that contributed/detracted from performance in a reporting period.
5) Currently, the PAC only sees a total portfolio performance figure for the two Plans based upon either IRR or TWR and a "hypothetical" calculation of returns v 65/35 benchmark. We should be able to see a performance and attribution of the investment portfolios BEFORE Plan cash contributions and withdrawals.

TEB
6/12/20