Investment Committee Minutes
February 7, 2011

Rice Room, Eliot and Picket House
Boston, MA 02108

Members Present: Jim Sherblom *Chair*, Julie Skye, Arnold Bradburd, Dan Brody, Carol McMullen, Will Saunders, Tim Brennan

NEPC: Kevin Kondry, Scott Driscoll, Doug Moseley

Others Present: Rachel Daugherty (UUA)

1. **Minutes from meeting of December 8th, 2010**
   Motion: Moved Skye, seconded Bradburd, approved. Minutes adopted without amendment.

2. **UUCEF Performance Review –** Moseley, Kondry – NEPC
   - 2011 Capital Market Observations
     i. Investors are facing a lower expected market return environment.
     ii. Funds employing traditional allocations will struggle to meet return targets
     iii. Quantitative easing by Fed Reserve dominates markets creating steep yield curve and increasing uncertainty
   - 2011 General Actions for Clients:
     i. Maintain asset allocation discipline
     ii. Continue to build illiquid strategies
     iii. Continue to diversify into emerging markets including EM debt
     iv. Recommend 5% to 10% in private equity
   - 4th Quarter Total Fund Performance:
     i. Total assets in endowment of $130 mm at 12/31/10, up about $15 million in previous year
     ii. The Endowment's 4th quarter return (+6%) ranks in the 45th percentile of the custom endowment universe
     iii. Trailing one- and three-year returns ranked in the top quartile of peer group
   - At summer meeting have a discussion of the justice implications of various investments, e.g. currency and commodities

3. **NEPC Long-term Outlook – NEPC**
   - Under NEPC's asset class return assumptions, the current UUA asset allocation targets would yield 6.5% annual return over seven years. This is down from the 2010 projection of 7.4%. This does not include any assumption for alpha.

4. **Fixed income manager presentation – PIMCO** (by phone) Robert Morena
   - In a volatile year, fixed income delivered consistently positive returns

- Key to keeping volatility low is to mitigate downside risk in portfolios
- A diversified allocation to fixed income played an important role through the crisis
- Sector rotation and security selection helped drive performance in 2010
- 2011 outlook upgraded on tax stimulus, although "new normal" headwinds remain.
- Believe yield curve will continue to steepen. Pimco taking high quality approach.

5. **Fixed income manager presentation – Seix,** Mark Ahern
    - Portfolio focused on high quality, high yield bonds, i.e. the highest credit quality in the high yield space
    - Goal is to protect and defend downside
    - Fixed income broadly:
        1. Anchor to the portfolio (Seix had no defaults during crisis)
        2. There's a natural question to ask: are we in a bond bubble? High yield has had strong performance over recent years; Seix doesn't think so, they look at the markets as rational.
    - Discussion:
        1. Should we consider a different strategy? Seix offers an unconstrained product that gives the manager more leeway. The fee for the unconstrained portfolio is 74 basis points, whereas the current strategy is 50 basis points. The volatility might be a little higher in the unconstrained, but would be picking up an extra 1% return.
        2. This is not presented as an ESG portfolio, but Seix is the underlying manager for the Domini Bond Fund. There's no tobacco in their portfolio.
    - Their view in 2011 is that 7 or 8% is competitive
    - The committee has been very happy with what they've been doing for us. 2008 was their first negative period and they've recovered from that.

6. **Fixed income manager presentation - GMO Global Bond,** Adam Dicker and Tina Vandersteel
    - Only do sovereign debt. Do not offer ESG products, but avoid rogue regimes such as the Sudan. Strategy is to minimize defaults while tracking the benchmark.
    - The Global Bond product focuses on developed economies, AA sovereign bonds with a yield of 3½%. Local debt has yield of 7%, but with default risk.
    - Emerging market bonds have much less liquidity.
    - Cost is 45 basis points for the current product, they will send the cost of the emerging market strategy. Would be more volatile because this international foreign debt, a much less efficient asset class.

- If we are ESG minded, will going into emerging market debt increase the "pain and misery" index?

7. **Fixed income manager presentation - Loomis Sayles,** Chris Lazarro
    - Fed is encouraging movement to riskier assets so 2011 comes back to credit picking. This plays to Loomis' strength – fundamental research.
    - Credit quality is at its highest levels in several years.
    - Loomis was hired initially to pursue fixed income opportunities. While spreads have narrowed and many of those opportunities have been captured, Loomis believes there will always be opportunities, and it's their job to find them.
    - Do not rely on bond rating agencies; have their own internal rating system. Their analysts anticipate rating agency moves.
    - They don't manage to any SRI mandate; no specific guidelines restricting them in that area. Cannot customize to a client because it is structured as a co-mingled trust.

8. **Discussion of Fixed Income allocation and strategy**
    - May be time to tweak the mix to less interest-rate sensitive, more total return. Concern about doubling up.
    - Committee will request that Seix consider creating an ESG high yield fund. Moseley said he would discuss with other NEPC clients to see if there might be interest.
    - For now, leave allocations to Seix, GMO and Loomis at 5% each with Pimco holding the balance. Discuss the allocation to fixed income in May.

9. **CFO update** – possible new structure for the UUCEF
    - Brennan discussed the possibility of restructuring the fund as a separate entity. This would provide liability protection to our investing congregations. Both legal counsel and our auditors have recommended investigating this.
        - i. Would have to re-file with all the states.
        - ii. Legal counsel's recommendation is that this new entity should be structured as a limited liability company. The LLC would have to file a tax return and issue K-1s. There was concern that this could be confusing to congregations. Brennan will discuss other alternatives with counsel.
        - iii. Sense of the committee was that this is best practice and we should move forward if costs are not excessive.
        - iv. Brennan will consult with the auditors about additional audit fees and tax filing costs.

10. **Next meeting May 20**

- Look at Global Asset Allocation funds – bring in managers to present to committee for 45 minutes each: GMO, Wellington, Bridgewater.
- Discuss allocation to fixed income.