# Investment Committee Minutes
## May 20, 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

1. **Minutes from meeting of February 2nd, 2010**
   **Motion:** Moved McMullen, seconded Saunders, approved. Minutes adopted without amendment.

2. **UUCEF Performance Review –** Moseley, Kondry – NEPC
   - 2011 Capital Market Observations
     - 1st quarter resilient; strong returns from all asset classes; market shrugged off disruptions
     - Market thinking short-term and responding to Fed's liquidity stimulus
     - McMullen: underlying global economies better than many think, even US
     - Moseley: after withdrawal of QE2 will have 1 – 2% GDP growth; globally more of a positive story
     - Bradburd: need to position the portfolio for multiple scenarios

   - 2011 General Actions for Clients:
     - Consider adding emerging market debt – put on agenda for Fall meeting
     - Short presentation on Seix unconstrained high yield fund later.

   - 1st Quarter Total Fund Performance:
     - Up to $138 mm from $130 mm in quarter
     - Committee asked to have EM equity broken out from all international managers on report so EM exposure is clear
     - McMullen: need to be careful not to double up on these bets.
     - NEPC will include the names of the funds and the ticker on the Flash report in the future
     - For quarter, up 3.6% gross return vs. allocation index of 3.3%; trailing three quarters up 22.3% in top 25% of similar sized endowments. Both the structure of the fund and the managers added value. NEPC will include the data points for the comparable endowment universe on future reports.

– McMullen: we should review our investment policy and mission at least annually. Add to agenda for summer retreat and include some UUA board members.

3. **GAA manager presentation – Bridgewater All Weather Fund** (by phone) Joel Whidden
    - Kondry: Bridgewater is very different from other GAA managers that are based on a 65/35 portfolio. BW levers up the debt to create a risk balanced portfolio with an underweight to equities: a risk parity portfolio.
    - Founded 36 years ago; deep experience; have never lost a manager; employee owned and controlled.
    - Only two strategies: Pure Alpha (closed), All Weather. All Weather is the best long-term allocation for equity returns.
    - Invest passively with goal of generating returns in all market conditions. Risk adjust the assets. Hold many different assets. Want to be as diversified as possible. Goal 6.5% over cash with 10% volatility.
    - Drivers of asset class values are growth and inflation; each can happen in rising or falling markets, thus four possibilities. Assume each of four is equally likely. Don't make any active bets.
    - Invest across five asset classes and global liquid markets. Where they can, they use futures. No counterparty risk because securities are exchange traded.
    - Use 2 to 2 ½ times leverage.
    - Strategy does well in all environments except when cash is the best asset. In 2008 moved into safe portfolio, not just cash because that can be subject to inflation and revaluation. Test is efficacy of monetary policy and responsiveness of markets to central bank action; when not effective "depression" gauge is tripped. Safe portfolio removes leverage. Exited safe portfolio after 16 months in 2010.
    - Expects economy to slow after expiration of QE2. Then the question is: will private debt step in. Long term rates will likely grow by 180 bpts.

4. **GAA income manager presentation – GMO,** Edmund Bellord; Adam Dicker
    - For last 12 months have underperformed by 175 bpts. This is a period when low quality has outperformed. This is shifting over the last several months. Over last quarter, quality is up 460 bpts. While S&P is up just a bit.
    - 7-year forecasts are down since last version. US large cap and small cap are projected to go down in real terms. Continue to favor high quality on a relative basis – low leverage, consistent profitability. Includes 200 companies from Russell 1000. Overweight health care, high tech, consumer staples. Believe this is the cheapest part of the market. Less interest rate sensitive; therefore, less benefit from low rate environment.
    - Purpose of QE2 was to prop up asset prices to get wealth effect and thus drive spending. This also drives down future returns. We are in a very

low return environment. Reaching for yield is the worst thing to do in this situation.

- Modest overweight to emerging because growth is from commodity based stocks.
- Jeremy Grantham's quarterly letter addresses commodities. Timber, which has the highest projected return is not in our portfolio because it is a private equity fund with a very long lock-up.
- Commodities are now highly correlated to equities and over invested. 200 year period of declining real commodity prices may be coming to an end. We are at an inflection point. Expect rolling shortages in the future. GMO prefers to get exposure through underlying producers.
- Expected absolute return for portfolio is 4.0% with 9.6% volatility. This pessimistic view is driven by underlying valuations. Profits are mean reverting; we are at the highest level of profitability ever, yet markets are assigning high P/Es. GMO believes that profitability will mean revert and P/Es will decline.
- Now is not a time to reach for risk because you are not being rewarded.
- Sherblom: this suggests we should reconsider reducing small cap and add emerging market debt.

5. **GAA manager presentation - Wellington,** Bill Samuels; Brian Burke
   - Brian Burke is our new client relationship manager. Update on the firm: one of the partners has decided to resign – the person in charge of compliance. Will stay on through the end of the year.
   - Consider the firm a collection of boutiques; no CIO overlooking the managers and directing overall strategy.
   - Not a benchmark relative strategy. Use benchmarks only as a reference point. Unconstrained basket of securities; all market traded. Use derivatives. Choices based on fundamental analysis for the most part. Thematic, top-down, best ideas portfolio; concentrated in limited investments.
   - Looking for niche exposures with strong structural tailwinds, cyclical/distressed opportunities; alpha opportunities. Make currency bets.
   - Invests in Wellington funds and tactical positions through derivatives.
   - Major themes include equities in emerging markets, natural resources, and precious metals; fixed income securities in emerging markets debt and credit opportunities. Like emerging market inflation linked bonds.
   - By investing in Wellington funds, get bottom up analysis.
   - Believe govt. policy will provide significant tailwind. Globally believe we are early in an increasingly normalized cycle. Believe supply and demand are tight. Outlook continues to be bullish.
   - Expect US economy to muddle through and improve, but not enough to bring down unemployment. Therefore Fed will stay loose. Concerned about potential for stagflation because we don't control our inflation.

6. Asset allocation

- No change from current allocations to Global Asset Allocation. We have four managers in alternative investments with 30% of the portfolio.
- We are currently at 45% equity, 25% fixed.
- Defer to a subsequent meeting adding an emerging market debt allocation.
- Keep Relational allocation within equities after that account is closed.
- Sherblom: Now may be a good time to move away from small cap value. Sherblom suggests moving to Rhumbline bringing it to 10%. Remove Hotchkiss & Wiley and leave Pier. Keep developed international managers at current levels.
- Consider having Rhumbline use the Russell 2000.
- Could put 5% into small and mid-cap

  Motion: Close Hotchkiss & Wiley account.

  i. Domestic equity 20%
     - Rhumbline 9.5%
     - Sands 7.5%
     - Pier 3.0%

  ii. International 25%
     - DFA 5%
     - Templeton 7%
     - Artio 6.5%
     - BCAM 6.5%

  Moved: Saunders, Second Skye. Voted.

**7. Governance issues**

- If the UUCEF is to be structured as a separate entity, legal counsel now recommends using a 501c3 structure. The application process will likely take the better part of a year.
- Standards are changing on liability and D&O insurance.
- McMullen: Recommends Wolf & Co.; CPA firm and law firm for tax advice.
- **Action**: Brennan to investigate costs of incorporation, audit, tax filing, D&O insurance.
- **Aug 10 meeting**: will begin with discussion of mission. What are the qualifications and selection process for members of the committee?

**8. Upcoming meetings and agendas**

- Next search: emerging market debt deferred to a later meeting.
- Next meetings: Aug 10, 9 to 5; Nov 9, 9 to 2
- August: 9 to 11, portfolio review; 11 to 5 what's our mission? Implications for managing the portfolio. Invite others for perspectives such as: Lucia Santini Field, Geeta Aiyer, Craig Scholl, a UUA board member, perhaps Jeanne Pupke, someone from Shelter Rock, Charles Samnel. Also discuss what it means to be a fiduciary in the 21st century. Will Saunders will write a paper for discussion.