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**Quarter Ended March 31, 2014 Performance Meetings
& Annual Investment Manager Reviews**

May 28, 2014

Retirement Fund Conference Room

Board of Trustees Present:

Joe T. San Agustin, Chairman, Board of Trustees
Wilfred P. Leon Guerrero, Ed.D, Chairman, Investment Committee
Gerard A. Cruz, Trustee
Antolina S. Leon Guerrero, Trustee
David O'Brien, Trustee

Staff Present:

Paula M. Blas, Director
Diana T. Bernardo, Controller
Rosalia L. Bordallo, General Accounting Supervisor

Other Present:

Maggie Ralbovsky, Wilshire Associates
Steve Weiss, Income Research & Management
Jeffrey Detwiler, Garcia Hamilton & Associates

**Economic & Capital Market Environment
& DB Plan Performance
Income Research Management
Garcia Hamilton**

**Pages 2-25
Pages 25-34
Pages 34-39**

Economic & Capital Market Environment & DB Plan Performance

Doris Flores-Brooks: I'm interested in your first comment, who were the ones that actually put their, oh no I was thinking the unfunded, I'm sorry this is just a reported actual bearer. Okay, I was thinking the GASB, sorry. Maggie Ralbovsky: Yeah so, good morning. Doris Flores-Brooks: Why this statement? Maggie Ralbovsky: What? Antolina Leon Guerrero: To get your attention. Doris Flores-Brooks: It did. Maggie Ralbovsky: So, good morning, there are a few things that I'd like to bring up. Antolina Leon Guerrero: I like Maggie. Maggie has an agenda she's like you all can say what you want but I'm going to get back to my

Agenda, are you done? Good morning. Maggie Ralbovsky: So a few updates. The first update item is the annual state funding study. So with regard to your question who are the 111 State retirement systems? These are just the retirement systems that reports. Doris Flores-Brooks: Whose funding is this? Maggie Ralbovsky: It's Wilshire's survey. Doris Flores-Brooks: Is that made available? I would like to get a copy. Can I get a copy of that? Maggie Ralbovsky: Yeah. Doris Flores-Brooks: Yeah alright, thank you. Maggie Ralbovsky: You have an access to their website. Antolina Leon Guerrero: It's a long flight. She can read it on the plane. Doris Flores-Brooks: Hey that's what happened last time when I left. There was no movie from Guam to Honolulu and I read the entire 135 pages that I had to read from the course. Antolina Leon Guerrero: You are well prepared. Doris Flores-Brooks: Really. Because I couldn't believe it and then my son had uploaded a movie for me you know but the problem was I had never got to it I did not know how to find it. How do I get the movie? I had to call him.

Maggie Ralbovsky: You should have asked a kid on the plane. Doris Flores-Brooks: I know I should have, I should have asked a kid on the plane you're right because that's what I always do, I ask my grandson, help grandma. David O'Brien: Or go through Narita. Gerard Cruz: Yeah. That's what I do. Just go through Narita. Doris Flores-Brooks: I am leaving this time through Narita. Gerard Cruz: It's much better. Maggie Ralbovsky: Okay, so since we all read the first page. Doris Flores-Brooks: Okay, so this is Wilshire study, this is an annual study? Maggie Ralbovsky: This is an annual study. Doris Flores-Brooks: Oh. All these years, I didn't know that. How come you never shared it? Maggie Ralbovsky: So you can see that the average funded ratio 75% and the average. Doris Flores-Brooks: So, Retirement Fund is below average? David O'Brien: Do you know what quintile we're in Maggie? Maggie Ralbovsky: That is correct. David O'Brien: Do you know what quintile we're in? Maggie Ralbovsky: What quintile you're in you can take a look at here. Doris Flores-Brooks: Okay, so we're in the 40 to 50, we're in that little bracket. Maggie Ralbovsky: You're in the tail. Doris Flores-Brooks: Yeah the tail. Not at the front of the tail we're at the back of the tail. David O'Brien: We're at the front of the tail. Maggie Ralbovsky: You can see the distribution. Doris Flores-Brooks: The front is the one when it's 140, who are those people? David O'Brien: No the 40 to 50, we're not at the tail 10 to 20. Maggie Ralbovsky: No you're not. Yeah those are the CNMI and Puerto Rico. David O'Brien: Right, there we are. So we are in the 5th percentile. Doris Flores-Brooks: Last one was 49%, right? David O'Brien: We're in the 5th percentile. Maggie Ralbovsky: It's not the 5th percentile. No that's actually not the way to read that I'm sorry if you want to read the percentile you should read down the top it's 25th percentile, not

below 25th percentile. Doris Flores-Brooks: Yeah because we're at. Maggie Ralbovsky: No wait, wait that's not how you read it either. Okay, so this is how you read this chart.

Doris Flores-Brooks: What does this graph mean? Maggie Ralbovsky: Okay, let me explain to David's comment. It's not 5th percentile. So this is the distribution which is the frequency. So, 5 out of 100. David O'Brien: So that's number of retirements. Maggie Ralbovsky: Well it's very close to 5th percentile, it's 5 out of 111. 5 people out of 111. Doris Flores-Brooks: And these are your clients? Maggie Ralbovsky: No this is not our clients. This is just 111 state systems that reported on or after June 30th. Doris Flores-Brooks: Okay. Maggie Ralbovsky: So you probably report after September, right. So these are the people who report in June. Doris Flores-Brooks: But are we included in this one? Is GovGuam. Maggie Ralbovsky: I don't think you are included in this one. Doris Flores-Brooks: Because see that's the way like the counsel state government always report as of June 30 because that's the most common year, but GovGuam is still included even though our year ends different. So that's my question is GovGuam still included in this 111? Maggie Ralbovsky: I don't believe you're included in here but it does not matter because the distribution you can see.

Wilfred Leon Guerrero: How come we have 111 system? Maggie Ralbovsky: How come? Because some states have police and fire and teachers. Doris Flores-Brooks: Yeah, fire is noted to have their own and teachers are noted to have their own and for example like in some states the counties have their own. Maggie Ralbovsky: But this is state system, we have another study for municipality. Paula Blas: But they have the state fire, they have state teachers. Doris Flores-Brooks: Oh okay only, this doesn't include municipalities they have their own. Maggie Ralbovsky: We have another study that is. Doris Flores-Brooks: Because that's a larger number. David O'Brien: So actually we are in the 5th percentile. Maggie Ralbovsky: Yeah it's close to 5th percentile it's a hundred eleven. Doris Flores-Brooks: Guam is usually classified as part of the state. We're not really classified as part of municipalities. Okay. Maggie Ralbovsky: Okay, now to your question for the 100% funded and more the state of New York is one example, they were over 110% funded. So, average fund ratios 75% we still have some work ahead of us obviously and then also. Doris Flores-Brooks: 92% were underfunded? Maggie Ralbovsky: 92% is because below 100 is underfunded, right.

Doris Flores-Brooks: Oh you used 100%, okay. Maggie Ralbovsky: Now another important data point is the fact it is to see what is the discount rate. GovGuam is actually more conservative in discount rate. So you are actually better funded than what 50% is showing because you're using 7% discount rate. The average discount rate is 7.75. So, if you use 7.75 you're actually going to be probably 10 points better. Probably in the sixty some percent funded ratio. Doris Flores-Brooks: Say that again. Gerard Cruz: But the 7.75% rate is based on a strategic allocation that doesn't look like ours though, right? I mean there's no based on our current strategic allocation because the 7% rate is same as our actuarial rate of return. Maggie Ralbovsky: Yes, so you're claim is correct but this is still unrealistic because we forecast based on the average asset allocation. So here's the average asset allocation we forecast to be 6.6%. Gerard Cruz: Oh on this average. Maggie Ralbovsky: Yeah this is average asset allocation. Gerard Cruz: So that's not even a real number then. The 7, 7, 5 it's not real. David O'Brien: 7, 7, 5 is a choice but remember we could go as high as 8 actually policy index is 8. Doris Flores-Brooks: But GASB is

going to change that. Maggie Ralbovsky: GASB whatever they change has nothing to do with the funding ratio calculation but. Gerard Cruz: They should start allocation. Maggie Ralbovsky: They just use that for. Doris Flores-Brooks: But you can't use an unrealistically high return. Yeah that's what I meant but GASB will change that. Maggie Ralbovsky: But GASB does not change this. This is Legislature kind of thing so actually some states have Legislature to set this rate, to determine this rate. Doris Flores-Brooks: Okay, let me rephrase what is median actuarial rate mean? How is that number derived? Maggie Ralbovsky: That's what the actuaries, just like we use 7%, this is what other states are using. Doris Flores-Brooks: So the median when you say median that means half are above this and half are below. Maggie Ralbovsky: So the funded ratio average is calculated based on an average of 7.75% so if you use a more realistic funded ratio, the funded ratio is going to go lower. So if GovGuam is using 7.75% you're probably over 60% funding and 7.75% based on their.

Doris Flores-Brooks: I thought it would just be the opposite because the 7.75 you were expecting to hit that versus over that 7% we will hit it. David O'Brien: No because the 7, 7, 5 is a discount rate. Maggie Ralbovsky: Higher discount rate gives you lower liability higher funded ratio. Doris Flores-Brooks: Yeah, but then comparing that to reality. Maggie Ralbovsky: Well reality doesn't enter in the picture. Doris Flores-Brooks: Alright I see what you're saying. Okay I got it. Maggie Ralbovsky: So based on the asset allocation we are projecting they will have like somewhere between 6 and 6.6%. David O'Brien: Because isn't it true that even though this may be the median for the states on the private side, ERISA side there are 5 or 6%. Maggie Ralbovsky: There are 4%. So here I have the number too if you want to look at that. The median long term discount rate is 4.8% that's on page 9. So the private sector based on 4.8% discount rate on average is 89% funded. So 89 is on page 6, 89.3% funded. So private sector has a higher funded ratio than the public sector. David O'Brien: By a lot. Maggie Ralbovsky: By a lot. David O'Brien: Because if everybody was forced to use 4.8. Maggie Ralbovsky: They are all like you know for every point dropped, you're counting 15% drop in funded this year. So, you're all like in 20, 30, but the 4.8% is also not realistic you know because public funds tend to have higher investment, longer investment horizon because public funds are perpetuities. Most of them are, GovGuam is not. Doris Flores-Brooks: We're not going in to modify. Maggie Ralbovsky: So, most public funds are perpetuities therefore they deserve a longer time horizon and a higher discount rate than a corporate fund because most corporate funds are frozen.

Maggie Ralbovsky: There are differences out there, there are supporting data points to say public funds should be using a higher discount rate by how much higher is the question that judgment. Okay, so that's a quick update. Now, I'm going to move to market environment. Market environment actually I'd like to start on page 12 and then we come back to page 11. Page 12, I actually copied this from New York Times. This is to make a joke to say hey you know is our interest rate correlated with how the Federal Reserve. So at you know with Janet Yellen. Doris Flores-Brooks: You mean Bernanke was actually shorter than what's his name the maestro? Wow, I didn't realize that. David O'Brien: Ex Maestro. Maggie Ralbovsky: So as we stand now the page 13 gives you historical perspective as to what is the cash yield versus 10 year breakeven. 10 year breakeven is the inflation so what's heist into the entire financial markets as the inflation expectation. And net of that what is the cash yield, so which is to say how much does cash compensate

you above inflation? And right now you can see cash is giving you negative 2.5% return. Not only those compensate you for inflation but also you're actually paying to hold cash. It is very unattractive asset class and in historical perspective, this is why we made the claim on page 11 this is at 100 year low. You have looked back 100 years to see this kind of phenomenon. With cash at 100 year lows in terms of real yield and bonds correspondingly also is at a 100 year low and stocks also projected for return is close to 100 year low. Because everything is priced off cash and we already went through the recovery rally which you know came out of the 2008 depressed levels but looking forward what has been given the earning power of these companies we're looking at a 100 year low projected return for stocks, bonds and cash. So this is the time where however you combine the traditional asset classes you come to an expected return that's at 100 year lows. So does that really mean we're going to have this kind of return in the future? We actually don't think so, we think most investors cannot live with this kind of return because they all have their goals. The insurance companies have goals to pay their bills and pension funds needs. So what is really going to happen is that leverage ratio is going to go up because to make this raw expected return higher the entire system will have to re-lever. So we went through 7 years of deleveraging, we talked a lot about deleveraging. Deleveraging has come to the point to where we are at a point of re-lever. That is conclusion we have. Doris Flores-Brooks: But who is going to re-lever? Yeah, because like the psychic of the consumer. Maggie Ralbovsky: Okay, listen to me. Leveraging comes in two different forms. I think we lost it right? So, leveraging comes in two forms. One is the intrinsic re-leveraging which happens at the company level. So every morning you open a newspaper and say hey this big company bought this other big company there was this merger. Now how does that happen? This big company has to borrow money to buy this other company, so that's increasing their leveraging ratio on intrinsic company level. So you are an investor you basically buy out stock, but the stock itself has levered. They have borrowed a lot of debt ahead of you because you are the residual holder, so even though you don't know that leveraging has happened that is happening, it is happening right now. The IP ratio as well as the merger ratio is at a huge spike right now. You have to go back to late 1990's to see the previous huge spike of the mergers and acquisitions. So re-leveraging is happening at the company level and the second thing that's happening is that in the investing community are creating levered vehicles to buy stuff and that's what we call the CLO 2.0. So it's a collateralized debt obligation the 2nd generation huge boom right now. And that's why I want to introduce not only the high yield but also the credit opportunities. I am actually going to introduce that asset class tomorrow because there is a huge support for that kind of a structure to have probably the next few years a secular rally for that structure and the reason is there is this very, very low expected return without leveraging. There is a desire for the entire community to create leverage and there's the desire on Central banks part to create leverage as well.

Wilfred Leon Guerrero: Maggie, you lost me. Maggie Ralbovsky: Okay. Doris Flores-Brooks: She's introducing to you a new product. Maggie Ralbovsky: Let him ask the question. Wilfred Leon Guerrero: Let's just start with this sentence that you have here, the world needs to accommodate the debtors, what does that mean? Maggie Ralbovsky: That means you see it let's start on this chart and I'll tell you what that means. Look at this chart. Wilfred Leon Guerrero: We're on page 11. Maggie Ralbovsky: Page 11, this chart is to say that normally the risk return pay off for cash, bonds and stock is at the normal level like that. Wilfred Leon Guerrero: Okay. Maggie Ralbovsky: Then what

happened was that because the central banks need to solve the debt problem, it needs to lower interest rate. What they can do is to print money. We printed so much money they pushed down the cash rate to zero. Joe San Agustin: Welcome to the world. Maggie Ralbovsky: Now when the cash rate pushed down to zero, everything else moved down to this level. Now the question now is does the central bank like that? Well the answer is yes, they actually like this kind of liquidity because there's still a lot of debt in the world even though in the U.S. we have come back to the leverage ratio before the previous cycle. In Europe you still have too much debt. In Japan you still have too much debt and in some emerging market you still have too much debt. So there is still this desire for Central banks not to have these debtors go bust because if they do go bust it's going to drag the entire world back into recession. So the entire world still has too much debt. So there is.

Doris Flores-Brooks: How is the U.S. though? Maggie Ralbovsky: The U.S. actually the leverage ratio has calmed down. U.S. actually is at a very good place. So it's tricky for the U.S. because we have to manage our conditions but because there's no inflation we don't have to be in a hurry to reduce the liquidity. But because the whole world has all these debtors that we have to take care of, really the Central banks bias is to help debtors not the creditors, not the investors. So if you're an investor you might as well make yourself in to debtor. How do you make yourself into debtor? You create leverage for yourself. You basically create these structures to lever and increase your return because you have a central bank put out there. The central bank put means that you can borrow money at a very low rate and the Central bank pretty much tells you yeah go ahead and do it I'm not going to raise interest rate on you. So that is what's happening. The levered investors actually are going to be having this favorable bias from the Central bank. That's not to say there's no risk, it's just that risk average is lower than the usual and because the desire to create more return, leverage ratio has to go up. Make sense? Wilfred Leon Guerrero: Nope. Maggie Ralbovsky: Okay. Which part doesn't? Wilfred Leon Guerrero: You are saying. There's a lot of them out there and what the banks are being encouraged to do is to give out more, loan more money. Joe San Agustin: Yeah, I print more money, I got more liquidity. Maggie Ralbovsky: Okay, banks are only a portion of the market, so what I'm actually trying to demonstrate here is that leverage only on the investment market is going up. Maybe I should go to the white board, can I? So, let's take a look at the company's balance sheet. A company with a balance sheet that starts from loans and debt then eventually just stops. And there are different classes of debt, there's secured debt, unsecured debt and subordinate debt now when you enter into a credit crisis what happens is that this portion gets wiped out. So companies will accumulate cash and start trying to pay off debt because they have too much debt that's called deleveraging. So at the bottom of deleveraging, stocks are the portion of the entire let's say the whole thing, capital structure is 100%. The lower leverage of the company will have a huge portion in stocks, let's say stocks become 70% and you only have 30% in debt because you don't dare to take on debt. So, what the Federal Reserve is doing is print money, print money to make debt so cheap. So what happens to this company is well you know debt is so cheap why don't we take more debt. We take on more debt, let's say you reduce this to 50% the stock becomes 50% for the entire capital structure. Your stock holders return actually gets levered up because you pay this debt holder now 2% and your company still makes 10% let's say.

Now if 2% is only paid to 30% of people this portion has a percentage of this annual lever basis is lower, so when you have more leverage these people get like a leverage debt when the return gets higher, this is what I call intrinsic re-leveraging because we went through the cycle of delever companies are now at this time with very low leverage ratio on their balance sheet, now they start to relevel up. This cycle probably will last for years because the entire credit cycle is about 15 years. We had 7 year down and probably 7 year up. So it's a good time for companies to start leveraging and the things we are already seeing is companies are issuing huge pieces of debt to go buy other companies. So that's one part that's happening, it has nothing to do with if you borrow from the bank for mortgage, you could do that. Another thing that's happening is that on Wall Street all these bankers are saying you know what, we could create a structure to go buy these debts so these debt are only paying 2%, but if we know these debt are really, really safe. Joe San Agustin: Treasury now is 2.25. Maggie Ralbovsky: Okay, like when Facebook, not Facebook, Google, not Google. Who went down? No, Google issued debt, no, Apple issued debt 2%, 2% debt. Joe San Agustin: They have to depreciate the stocks.

Maggie Ralbovsky: It had so much cash on the balance sheet. So they issued debt and they borrow at 2% lower than U.S. Treasury. Joe San Agustin: That's a good investment. Maggie Ralbovsky: People are starving to buy this 2% debt but then how can you make money with 2% debt? Well the only way you make money is you borrow at zero you buy 10 times of this, so it's called the CLO's, collateral and loan obligations. CDO's Collateral Debt Obligations. These 2 structures are coming back. This is coming back. This has been huge boom last year. So much of these structures are created and they basically borrow at 0% then go buy these 2% debt 10 times levered up. So that's what's creating the systems leveraging. Not that we are sitting here trying to borrow, not that. But the system is starving for leveraging and the reason it starves for leveraging is because returns are so low and at the same time risk is also low. Federal Reserve tells you I'm not going to raise interest rates for the next 3 years, so let's create some CLO's for 3 years and these since I have this thought. Joe San Agustin: Federal Reserve is going to be picking up the pace again.

Maggie Ralbovsky: So now these structures are called CDO 2.0 because the structure has been improved. We know that in 2008 there were a lot of issues with these things quite unwind because underlying these structures they were buying mortgage and securities that were bad. Yes, so once the underlined debt gets bad you have to unwind this thing which is what hits the credit market because when you lever up 10 times you have to unwind it. So this 2.0 they have to set aside a reserve very regulated reserve ratios. Doris Flores-Brooks: Who's regulating them? The market is unregulated. Joe San Agustin: Federal reserve banks they regulate those with reserve. Doris Flores-Brooks: Not those CLO's and CDO's. Are those being regulated? David O'Brien: That's the question when we start talking about the credit opportunities that you want to do. I mean what's changed because this is what got us as Maggie says in trouble in 2008. Doris Flores-Brooks: Right. David O'Brien: So, now she wants us to go there. Maggie Ralbovsky: What has changed is these underlined securities are no longer mortgage securities that are corporate securities and so there's definitely vintage issue. So, right now you can make an assessment to say all these corporate issues are actually pre-high quality because corporations are very, very, very high levels of cash. So that's one. Another thing is these structures are now

being regulated, I think it's the Congress who had some part of that probably has something to do with this.

Joe San Agustin: The cause of the market slump in 2008 and all that 2009. That's what causes that. Maggie Ralbovsky: The issue is that if you find very illiquid securities here and if you lever them up and the securities are illiquid and low quality try to unwind that it's going to drag down the whole system. It's a systematic risk. Joe San Agustin: Is security mortgages value the property is going down. Maggie Ralbovsky: If these things are liquid and higher quality and you put enough reserve on the side so that's the hope here obviously. So bottom line, these things are happening and there's a huge, huge desire, so even the most recently Fannie Mae, Freddie Mac, Fannie Mae debt the new mortgage debt which has the investors take the risk. So in the past Fannie Mae, Freddie Mac mortgage back securities were basically supported by the government. So that's why all the tax payers had to bail out then when they went into trouble. Now the new debt they are issuing has very, very light support from the government. The investor has to actually pitch in if all these mortgages go bad. At first they set the interest rates pretty high because they thought you know probably nobody wants it because of the change in this kind of dynamic but it actually was 15 times over subscribe. So, just because all these structure everybody's desire had some frostiness then.

David O'Brien: But you understand though why this is kind of our first foray in derivatives, right? Maggie Ralbovsky: This is not, I wouldn't call that derivatives. David O'Brien: These are not derivatives? Gerard Cruz: They're actually. They're asset back, right? Maggie Ralbovsky: Yeah, they're asset back. Okay, that's tomorrow's discussion. David O'Brien: Yeah that's what I said. Gerard Cruz: We couldn't do derivatives. David O'Brien: Yeah I know that's kind of what I was asking. Maggie Ralbovsky: So does that answer your question about leveraging? How it's happening? Wilfred Leon Guerrero: When is the interest rate going to go up? Maggie Ralbovsky: When is interest rate going to go up? Well, according to Janet Yellen, well the market pricing. David O'Brien: Second quarter 2015. Maggie Ralbovsky: That's what the markets pricing in, so you know that's what the markets guess is, I have no guess. Wilfred Leon Guerrero: What is it? Maggie Ralbovsky: In the middle of 2015 the interest rate is going to go up. But it's already some of it. Wilfred Leon Guerrero: That's what Mercer is saying, but Wilshire doesn't have a position. Maggie Ralbovsky: Well you can make all projections you want but it's always going to be wrong. So it was funny that you know you can ask a question to economist, why do you still have your job every time you make a forecast its wrong? And I got this good answer from JP Morgan's economist, he's says well I have always been wrong, not even once I was right but the demand is so high I still have to keep turning it up. There's always demand for my forecast even if it's always wrong. So the market is expecting mid. Wilfred Leon Guerrero: Next year. Maggie Ralbovsky: Yeah, we think it's probably going to be a little later than that.

Wilfred Leon Guerrero: Okay, that's what I wanted to hear. Maggie Ralbovsky: We think, yeah. Wilfred Leon Guerrero: And what you described here, it looks like we're leading up to something again like. Doris Flores-Brooks: Another change in law. Maggie Ralbovsky: Well market goes through cycles there's no way you can stop it. It's like a train, okay this train is going around the track it still has to go its course. Well at some point market will crash but I don't think it's going to happen in the next few years. Joe San Agustin: No

wait, we don't want to hope for that. Maggie Ralbovsky: Well cycles, we cannot stop the cycles. Doris Flores-Brooks: It has to happen: Maggie Ralbovsky: So the capital boom and bust cycle always happens. Wilfred Leon Guerrero: Like what Doris is saying I think we're going to get into the situation again. Maggie Ralbovsky: We will, we will. Wilfred Leon Guerrero: And the product is available and its good but we can't do it because the law needs to change. Doris Flores-Brooks: Right. Joe San Agustin: Nobody wants to buy. Maggie Ralbovsky: We will what? Doris Flores-Brooks: A law change in order to do this. Maggie Ralbovsky: We already changed the law. Doris Flores-Brooks: The law brought enough to include it? Oh, okay. Maggie Ralbovsky: Yes. Joe San Agustin: What law? Gerard Cruz: Our investment law. Maggie Ralbovsky: The statute. Doris Flores-Brooks: I remember the last discussion was what was the kind of bonds? Maggie Ralbovsky: High yield. Doris Flores-Brooks: High yield bonds, are you able to do that now? Maggie Ralbovsky: Yes. Doris Flores-Brooks: Okay. So is it under like that, a high yield bond? Sort of the same. Maggie Ralbovsky: You know the thing is fixed income is actually very, very broad category there are so many different instruments. Doris Flores-Brooks: So I guess the question is what did you do in the law that allows you to do this about going back? What was changed in the law? Gerard Cruz: The ratings, right. Maggie Ralbovsky: Yes. So the law changed, so let's talk about the cycle. My goal is the three cycles. The only way we know how to deal with the cycle is diversification because there's no way you can stop the cycle. You can't say hey you know cycle is bad this is irrational. Yeah you can say all you want, things still going to happen you know this. So the only way we can try to insure or try to shoot for a smoother ride is diversification. And that's what I'm trying to achieve here is to say here's the opportunities available to us let's assess how to put the portfolio together so we can utilize all these available opportunities to diversify.

Maggie Ralbovsky: So shall we move on? Yeah, so bottom line we think that the market environment is very supportive to risk assets at this particular point in time and we also think the leveraging ratio in the entire system is going to go up and as an investor in the market place I think it's important to understand this dynamic and try to see how we can take advantage of it. Joe San Agustin: But you still have some tolerance level. We have tolerance level in risky asset. Maggie Ralbovsky: Yeah we already have a very, very high risk. Doris Flores-Brooks: Extend your risk tolerance. Extend your risk tolerance to reach your goal. Right? That's what you're saying. Little bit in other words put your toe into the water. Joe San Agustin: Yeah and when it's hot enough take it out and go some place else. David O'Brien: What she's saying is two things I think is what I'm hearing, one is that riskier assets are going to get the higher returns right now and second thing is you protect yourself by diversification and you have to do both of those things together not just one or the other. Maggie Ralbovsky: That's right. Okay, so let's move on. Let's take a look at these are backward looking data now. Economic review shows us that inflation levels are still low, so we're talking about page 14, first bubble in orange. Inflation levels are relatively low and the industrial activity is relatively high. Employment picture seems to be steady even though the market has been debating on this particular ratio of labor force participation rate. You can see that the labor force participation rate has been dropping and there is the calculation some people call it the U6 employment rate which is to account for all the people who supposedly are discouraged workers or under employed people and the unemployment rate still is very high if you count those people. But now on the other side of the debate people are saying you know what these people probably never going to come back today because a lot of the people didn't retire in the past because they

wanted to wait until 65 so they can have Medicare, now you don't have to wait you can have Obamacare whatever, whenever you retire. So, maybe that made the change for people to retire early and there are also the demographics that the baby boomers are reaching that age with the affordable care act.

So there's this kind of debate which I think has a lot of truth to it. I don't think the labor force participation rate we should expect it to go back to the old levels. I do think the demographic supports the fact that these people are never coming back which is an important assessment because if these people are indeed coming back we probably will be looking at average wage being depressed because if you have more people trying to come back you have a deflationary force. But because these people are probably not going to come back we're probably going to see the average wage go up and which is the biggest input to inflation. So that's another factor we need to consider is if inflation really is going to be driven by the wage growth, what does that mean to the asset classes? We know that it's not going to be good for bonds for sure, you know some asset classes are not very good when inflation goes up. Joe San Agustin: Are you saying that we got to start shifting to stocks? Maggie Ralbovsky: That's not what I said, no. Joe San Agustin: Well bonds are attractive. Maggie Ralbovsky: Well there are many asset classes besides stocks and bonds. I really wanted us to expand our horizon and take a look at all the available opportunities out there. Gerard Cruz: We are though. Maggie Ralbovsky: I know we are not just shifting stocks it's not just bonds and stock, two asset classes. Joe San Agustin: Well that's the traditional way. Maggie Ralbovsky: Yeah that's the traditional way. Joe San Agustin: You try to put some more sophisticated in between. Maggie Ralbovsky: Yes. Joe San Agustin: What such a slot now? Maggie Ralbovsky: I have a discussion for tomorrow but we already started talking about changes. Joe San Agustin: Okay, I'll hold that. Maggie Ralbovsky: Okay hold that.

Maggie Ralbovsky: Okay so we are going to move on to take a look at the equity market. Stock market was up 2% U.S. stock was up 2% and this is as of March. And interestingly after March things actually changed dramatically in terms of leadership of sectors. As of March we still have a growth you can see large cap already started to shift leadership. Large value actually outperformed large growth. Small cap seemed still to be very, very strong especially small growth wasn't too bad for this quarter but after the first quarter leadership entirely changed. Large value was the sole place that we're doing really well after March. Large growth really, really tanked and small cap really, really underperformed afterwards. So there was a huge change in leadership which may be showing the market is getting wary about the past rally being very frosty. Past rally has been driven by the speculated sectors. This explains some of our manager's underperformance. Our fundamental driven managers we have some underperformance there because they were not chasing these deals, this frosty kind of deals. And then after the end of this quarter the market started to consolidate that and you can see the biggest gainer this year was REITs, was up 10% from the quarter. But we know that's a rebound from last year because you see the 1 year number for REITs is 4.4%. REITs underperformed about 30 percentage points last year with general markets so it had a little rebound.

Joe San Agustin: How long is this going to last? Maggie Ralbovsky: The REITs? Joe San Agustin: Yeah. Maggie Ralbovsky: I do believe REITs are going to have a pretty difficult

time going forward. Gerard Cruz: I think so, too. Maggie Ralbovsky: Yeah, because. Joe San Agustin: So they maximize it. Maggie Ralbovsky: Well this quarter the reason it went up was because interest rate actually went down. At the beginning of the year there was this huge storm on the East Coast. The storm actually made a huge change to GDP. GDP was negative for the first couple months of the year because of the bad weather in the East. So construction projects couldn't start, roads, like housing start was terrible, consumer spending was bad because nobody goes to the mall when the snow storms. So, interest rate actually went down because of that and REITs was the beneficiary for that because REITs we know are very highly levered. REITs actually has huge leverage in the structure. Joe San Agustin: There's a Hong Kong market Maggie, REITs now is going up. Maggie Ralbovsky: Okay, Hong Kong market isn't global REITs right, this is U.S. REITs only and we are going to try to expand. Joe San Agustin: Just talking about that's the effect in emerging market is on China now. Maggie Ralbovsky: That's right emerging market they have a huge rally because of the same effect that the interest rate went down. The more levered you are the better. Joe San Agustin: REITs now are becoming the fallback.

Maggie Ralbovsky: Yeah, so after the 1st quarter though the same issues the market starts to consolidate actually gravitating towards higher quality sectors. Joe San Agustin: What I'm getting at Maggie is I'm visualizing what's going on in Asia is that what you're saying this is going to happen in the states when you start concentrating more on REITs. Maggie Ralbovsky: The REIT law has been passed in more and more countries and the global real estate managers also have been buying real estate operating companies so even though a country doesn't have a REIT law is to also have a real estate security. Joe San Agustin: REITs has a very bad history in the states you know the early days where it's just no good. Maggie Ralbovsky: Because REITs in the U.S. if you just focus on U.S. REITs it's a quite small sector. It has 110 securities total, so does it deserve 10% of our assets which in my view, it does not deserve 10% of our assets for 100 securities that's why. Joe San Agustin: So whatever happened in United States if REITs is not going to have an impact over all? Maggie Ralbovsky: REIT is a segment of the U.S. stock market. It is a very small sector. Its 100 securities, 110. Joe San Agustin: Yeah but you still got a lot of market complex and all that stuff. Maggie Ralbovsky: It's a 110 Mid to Small Cap security. Yeah. Small value. REIT is considered small value. Wilfred Leon Guerrero: Wait before you turn. Maggie Ralbovsky: So you want me to explain this page? James Duenas: Can you explain page 16 first. Maggie Ralbovsky: Yes. James Duenas: The graphs, how come the dates aren't consistent? Maggie Ralbovsky: Dates with what, is not consistent? James Duenas: You know you go June 2004 and then March 2005, December 2005 then you jump to September 2006, June '07. Maggie Ralbovsky: Why is it not consistent? James Duenas: It's not consecutive. Maggie Ralbovsky: Oh, because this is just a scale of the chart. So, if I put every month here it will be too busy. James Duenas: No but usually it's if you going to do June 04, then you do June 05, June 06, it's a more consistent looking graph. Maggie Ralbovsky: Okay, so these are every 9 months. David O'Brien: There's 9 months in between. Maggie Ralbovsky: Yeah these are all 9 months. David O'Brien: Yeah it's not quarterly. Maggie Ralbovsky: It's just a scale, the computer automatically, it's a scale from 9 months. James Duenas: I was just wondering why the months jump to. Maggie Ralbovsky: Oh I see its 9 months in between. That's just the scale. Doris Flores-Brooks: All of them are 9 months in between. Maggie Ralbovsky: Yeah.

Maggie Ralbovsky: Okay, so this chart is showing where the corporate earnings came from. Wilfred Leon Guerrero: You're going to have to explain these words but the first one is that earnings have been quite strong since the recession, are we out of the recession? Maggie Ralbovsky: Since 2000, so if you look at 2008, this is the recession right so you see everything was down. 2008 so that's 2007 in between 2007 and 2009 that's the recession. Since then you see that corporate earnings have been very strong those bars are all above. Wilfred Leon Guerrero: So when did it officially go out of the recession? Maggie Ralbovsky: Well, you know officially I don't care where officially start or end but if you look at since 2008, the corporate earnings have been very strong. Doris Flores-Brooks: And it's due more to margin because of cost cutting. It's hard to margin. Maggie Ralbovsky: So this whole chart is trying to demonstrate the fact that the past corporate earnings you see the gray portion on the top is very, very large but that has started to become smaller actually for a couple of quarters was negative. Which is to say that the corporation's first reaction to the recession is to cut cost so they lay off people. Wilfred Leon Guerrero: What does margin mean? Maggie Ralbovsky: Margin. Doris Flores-Brooks: Revenue minus cost. Maggie Ralbovsky: That's right. So if you made \$100 you pay the \$10 to the supplier to the employee, your margin is \$90. So margin means what is the revenue minus cost, yes. So you see that the margin contributed to 21% majority of the earnings was from margin. Wilfred Leon Guerrero: And what's share count? Maggie Ralbovsky: What's share count is market share. So a company gained market share meaning they expanded their market share. Doris Flores-Brooks: Issued more stock? Maggie Ralbovsky: No, so you sold to other markets. So let's say I sell gadgets in the past. Doris Flores-Brooks: When you say share count does it mean share. Not count as in the number of shares but market share. Maggie Ralbovsky: Market share. Doris Flores-Brooks: Share count means market share? Maggie Ralbovsky: Market share. Doris Flores-Brooks: So overall market share only counted for a very small portion.

Maggie Ralbovsky: Yes. Doris Flores-Brooks: Okay. Maggie Ralbovsky: The revenue growth is not very large. Doris Flores-Brooks: Mostly due to cost cutting. Maggie Ralbovsky: The major corporate earnings came from cost cutting. There is a limit to that. So you cannot cost cut forever because you'll still have. Wilfred Leon Guerrero: Okay, it's telling me that the growth is due to improving margins and I don't understand that. Maggie Ralbovsky: You don't understand that. Basically means that companies have been laying off people to save cost. Wilfred Leon Guerrero: Why didn't you just say that, on cost? Maggie Ralbovsky: Okay, I will say that in the future. Wilfred Leon Guerrero: That tells me that the unemployment is going to continue to be high, right? Maggie Ralbovsky: No this basically is saying that there's a limit to this you can't increase your profit by forever at cutting people. Somebody has to do the work right so this is to say at this point where the corporate earnings is going to come from becomes uncertain because we know that the contributing factor is going away. So that's basically what this chart is trying to say. David O'Brien: But it also says there's room for revenue growth because look historically what's driven earnings per share growth it's the blue line right and now you're saying the waiting in the blue line so the question becomes as employment comes back are you able to increase sales i.e. increase revenues and does that become your driver? Maggie Ralbovsky: That's right. Leadership has to change somehow.

Maggie Ralbovsky: So this chart if you think about what we talked about corporations are trying to buy other corporations and if you look at this top graph that says Wilshire 5000 Index and if you focus on the blue line for now, the blue line shows you how many number of companies in the Wilshire 5000 and the white axis on the left hand side shows that information. So, when Wilshire 5000 was started in 1972 there's a reason it's called Wilshire 5000 because there were 5000 stocks in the index. Wilfred Leon Guerrero: We don't have 5000 stocks anymore. Maggie Ralbovsky: We have 3800 today so today you can call Wilshire 3800 and at one point it was 7500 that was in the late 90's so there were lots of consolidation and you could also count for failure, little companies go bankrupt being gobbled up by bigger companies. So bottom line there's 3800. Doris Flores-Brooks: But there was 3800 back in the 80's right just around that same. Maggie Ralbovsky: That's right. Doris Flores-Brooks: So we're back where we were back in the 1980's. Maggie Ralbovsky: A little below that. So it was boom and bust it's just the cycle but on the other hand. Wilfred Leon Guerrero: Why should I be interested in this?

Maggie Ralbovsky: Why should we be interested in this? Wilfred Leon Guerrero: Why should I be interested? Maggie Ralbovsky: But if you look at market cap of these companies, in 1980 even though. Doris Flores-Brooks: Fewer companies have more value. Maggie Ralbovsky: So going back to 1980 even though there were same amount of companies but look at how little. Doris Flores-Brooks: The value. Maggie Ralbovsky: How little these companies were worth compared to today. So in the 1980's it's a trillion dollars for those 3800 companies. Today the 3800 companies compose 19 trillion dollars. So there's a tremendous amount of the wealth concentration in the large companies these days. So why do you care about this? You think about what we're talking about the cycle the de-leveraging and re-leveraging we're at a point of re-leveraging because these companies are consolidating but at the same time. Doris Flores-Brooks: And they can afford to lever because of their value. Maggie Ralbovsky: Yeah but at the same time you can also expect number of companies to grow because look at this, this is the IPO. We also have IPO growth there was IPO drought for a little bit during this period, now it's going to start to come back.

Doris Flores-Brooks: So, 2009 at the recession there was very little. Maggie Ralbovsky: Very few, very few. And a lot of these companies were bought out by private equity firms they are just waiting for an opportunity to sell the shares in public. So, shall we move on? A little bit, what time is it? Doris Flores-Brooks: It says merge extends losses, what is that? Emerging extends losses on your next page. Maggie Ralbovsky: Yeah, so emerging market was difficult. Okay so let's take a look at the emerging market. You see emerging market has negative return for this quarter, you see that here. And it was having terrible return last year either as well. So emerging market is going through this consolidation but after the 1st quarter ended emerging market actually had a rebound because people came to realization emerging market is not just one class there's actually 5 groups of emerging market countries out there. So I think I'm trying to remember there's people who labeled who give them each a name so there was the structural strugglers which include China, India because they have structural issues. Then you have the forever mismanaged which include Ukraine, Venezuela, Argentina then you have those almost emerged so those are the Korea, Taiwan and then you also have those people who are struggling with the past debt which are like Hungary, Turkey. Then you have the forever over spender like spending out of your means so you have those countries like Kuwait. You have some

group of those countries. So there are 5 groups of countries emerging market and now there's a lot of interest that goes back into the more solid ones. Instead of across the board selling of emerging market, now they are just trying to differentiate the different groups in emerging market. But emerging market is still having a lot of issues. So that's what it's trying to say.

Wilfred Leon Guerrero: The frontier market is the Middle East countries, right? Maggie Ralbovsky: What? Wilfred Leon Guerrero: The frontier market is the Middle East country? Maggie Ralbovsky: Oh the frontier market is an interesting, interesting place. Wilfred Leon Guerrero: That's in Middle East, right? Maggie Ralbovsky: Africa, mostly Africa. I think Africa really is the next big opportunity but not necessarily for all Africa. So, Africa is a huge place and East Africa now has a generation of leaders that are really, really determined to. Doris Flores-Brooks: When you say, who are the countries in East? Maggie Ralbovsky: Kenya, Kenzania the people who are in that East African region not so much South of Africa. South Africa is actually right now in the good part of emerging markets. So it's the other East African countries that have leaders that who are actually educated in the West and really went back and cleaned up their books. So I think that we're facing a window for good opportunity in Africa so I think if you want to look at the next boom don't go to China, go to Africa that's my view. So, what were we talking about? Oh frontier market. Antolina Leon Guerrero: What about the Eastern block countries? Maggie Ralbovsky: The eastern block countries have the forever mismanaged and the past debt people who still consolidate the past debt so I think it's a mixed bag although they are much smaller than Africa. So I hope Africa can put their act together it would represent the next opportunity for the entire world.

Okay, high yield. High yield bonds you see the spread is getting lower and lower which means it's getting more and more expensive. It is at the point to be too expensive and we don't think it's too expensive but we think it's fairly value at this point. Which is to say you probably would just get your coupon don't expect huge up appreciation but the coupons in the 6, 7% range but the quality is very strong. There's very, very little default and there's a lot of companies have re-borrowed at much lower interest rate and pushed to their maturity way, way in the future. So the quality is very strong but the spread has compressed to historical average levels. So what you're saying is that we're probably going to expect to get the high single digit return not like in the past few years the huge, huge spread compression. Gerard Cruz: Good segway. Maggie Ralbovsky: This segway to say we're going to issue RFP and we're going to probably wait and the process will take a little time probably will be at a time where it might be better. The opportunity may get better, right.

Doris Flores-Brooks: Let's go back to 23. Maggie Ralbovsky: 23 is a message of diversification. Every asset class has a different color and the observation is to try to make it simple to say look there is not a single color that consistently stays on the top or the bottom, they change leadership. I guess that was my. Doris Flores-Brooks: 2014 is where the Fund is now and then the annualized is over the five? Maggie Ralbovsky: Yes. So year to date the best performing asset class was REITs. Doris Flores-Brooks: You said that earlier. Maggie Ralbovsky: And commodities. Gerard Cruz: These REITs are global REITs though right not just REITs, this is REITs as a complete mandate. Maggie Ralbovsky: This is actually the U.S. REITs. Gerard Cruz: No kidding. Maggie Ralbovsky:

Was up 10% and the commodities was up 7% and then guess what's the best performing commodity? It was coffee it was up 70%. Paula Blas: And it's continuing to go up. Maggie Ralbovsky: Yeah because of the fungus or whatever is eating all the coffee. So, coffee crisis. Antolina Leon Guerrero: Thank God I don't drink coffee. Rosalia Bordallo: South America is also going to have a problem there's another fungus that's killing the bananas, South America produces the bulk of the bananas. They're having that problem. Maggie Ralbovsky: So agriculture and water I think these are the two things the world is. Doris Flores-Brooks: What is developed? Maggie Ralbovsky: It's developed foreign countries. Doris Flores-Brooks: Oh, okay. Maggie Ralbovsky: Yeah, so there was this report that was mind boggling the whole world is one bad harvest away from mass starvation. That's just the reality. Doris Flores-Brooks: What? Maggie Ralbovsky: The whole world is one bad harvest season away from mass starvation. Doris Flores-Brooks: You're kidding. Maggie Ralbovsky: Yeah. Gerard Cruz: It's life. I mean that's just the way, that's how it's always been. Maggie Ralbovsky: Yeah, so then in my view it's also one bad harvest away from the 3rd world war because when there is mass starvation people are going to try to fight for resources and they're going to have a war. Then after that you are going to kill a bunch of people and then you have enough resources. Joe San Agustin: Be optimistic, Maggie. Maggie Ralbovsky: I'm just saying.

David O'Brien: You might as well be Mercer. We're on the verge of total collapse in China. Maggie Ralbovsky: Really? That's their forecast. David O'Brien: That's the thing is China is the worry spot. Maggie Ralbovsky: I think Chinese leadership has never been so educated as today's leadership. They know what they want. They wanted stability, they wanted the mass employment. They really don't care about what the West cares about, the West cares about profitability, GDP growth, they don't really care. I think that if we use the Western standard trying to measure China, you're measuring the wrong thing and China is just going to be fine. Although I do not think China is the opportunity of the future but I don't think it's going to collapse. David O'Brien: They are already in Africa. Maggie Ralbovsky: Yes, Africa. Wilfred Leon Guerrero: Yeah but you know the Chinese built those cities without people in it. Maggie Ralbovsky: Yes that is true. They're just going to have to. Wilfred Leon Guerrero: But you still have confidence in them? Maggie Ralbovsky: Yeah those cities were built without borrowing, it wasn't from debt. Some people just used their equity to buy those houses. Okay, you're not going to trigger the kind of a debt bubble like the U.S. has. James Duenas: It's not from borrowing from the banks some of them are borrowing from the other forms of. Maggie Ralbovsky: Yeah but the country could overnight maximize all their banks which is the means U.S. never had. So it does have its own problems I don't think China is the future but I don't think it will collapse. Doris Flores-Brooks: But the contingent is self contained. Maggie Ralbovsky: I don't know. I actually don't know that is the case anymore if China blows up it's going to be a huge event. It's the 2nd biggest economy in the world but I don't think it's going to blow up. Wilfred Leon Guerrero: You don't think China is the future either. Maggie Ralbovsky: I do not. I do not. I think U.S. is the future and Africa. I think U.S. will be the future because of the Shell gas the fracking exploration. U.S. is going to be energy sufficient, energy self. U.S. is going to be energy exporter by the year 2025 and U.S. right now has the lowest electricity rate, has the lowest energy cost.

Doris Flores-Brooks: Not on Guam. Joe San Agustin: That's for sure. Rosalia Bordallo: We'll all live in the mainland. Maggie Ralbovsky: Yeah, so that is a huge advantage for

the U.S. Manufacturing is going to go back to the U.S. So I think U.S. is the future of this and if you talk about. Doris Flores-Brooks: Despite our debt. Maggie Ralbovsky: We will not have a debt problem if GDP grows. Debt you cannot review in isolation. Debt is a ratio of the GDP. If GDP grows your debt can grow and right now GDP is growing faster than the debt. Doris Flores-Brooks: Right now we're at about 80%, debt is 70% of GDP? Maggie Ralbovsky: Depends on how you count it. We're at 100 right now but if you have a high growth you don't care about high growth of debt, right. Debt is good if you have a growing economy. So debt cannot be viewed in isolation and U.S. is definitely having a lot of competitive advantage to be the brightest spot for this century. But the next bright spot I think is going to be Africa, I really do. Joe San Agustin: Africa is a developing country, how do you... Maggie Ralbovsky: Africa is a big country. Doris Flores-Brooks: There's so much corruption in Africa. Maggie Ralbovsky: It is but you cannot just blanketly say Africa. It's like saying Asia entire Asia there's so many countries there's 30 different countries, more than that maybe. Joe San Agustin: How many? 38 countries in Africa? Doris Flores-Brooks: But a lot of them. Maggie Ralbovsky: You know I had to there's a change. Antolina Leon Guerrero: Give them a minute.

Doris Flores-Brooks: But corruption as long as. Maggie Ralbovsky: It's not every country. Doris Flores-Brooks: But like Nigeria and countries like that. Maggie Ralbovsky: Nigeria is only one country out of Africa. Doris Flores-Brooks: It's 180 million people. Maggie Ralbovsky: Nigeria is actually very good spot for development because that is the energy. Doris Flores-Brooks: 180 million. Wilfred Leon Guerrero: Okay, what about Japan? Doris Flores-Brooks: We're losing our tourist from Japan. Maggie Ralbovsky: Japan is actually in a very bad situation because they tried to do the Abenomics, they tried to do the printing money thing and try to buy time for themselves to change the structural problems but they never did anything. Wilfred Leon Guerrero: They still have structural problem? Maggie Ralbovsky: Oh yeah their structural problem the inflexibility of the labor force. They have quite low unemployment rate because they cannot fire people. So, if you fire somebody you have to pay them for life why do you fire them. Gerard Cruz: You still have to pay them for life? They still have that program. Maggie Ralbovsky: They still pay them. Gerard Cruz: Lifetime employment? Maggie Ralbovsky: Well close to life like for long. Gerard Cruz: No, this one they used to have where you can't touch them. Even if you do, you have to pay them so they're not. Rosalia Bordallo: That's just like GovGuam. Doris Flores-Brooks: Right, I mean that's GovGuam. Hello. Rosalia Bordallo: And we even paid for 2 year vacations. Gerard Cruz: This is even the private sector. Maggie Ralbovsky: Yeah, the private sector. You can't really fire anybody so then you have this inflexibility issue that's the structure issue for Japan. They also have aging population and they never were able to change that. It's a hard decision to make, so I think Japan is really in a tough spot right now. And they raised the sales tax which is really bad in this particular time. Gerard Cruz: What was the rationale for that just because they needed tax revenues? Maggie Ralbovsky: Because they are going to default in their debt, Goldman is actually projecting Japan is going to default in their debt before the year 2020. Japan's debt is over 200% GDP. Doris Flores-Brooks: Yes, I know that. Maggie Ralbovsky: The reason Japan is still okay right now is because they have no outside debt. Doris Flores-Brooks: It's self contained. Maggie Ralbovsky: That's right. So but with all this aging population, these people are going to cash out their cash at some point somebody has to buy their debt. So there's no way to support this. Who is going to buy JGP at 1% when you have 200% debt, right? So they're going to default in their debt

at some point if they do not make this transition and that's part of the reason. Gerard Cruz: Wow. Okay.

Maggie Ralbovsky: Okay, shall we move on? Gerard Cruz: Sure. Let's take a look at our performance. Maggie Ralbovsky: Let's take a look at performance. Gerard Cruz: We didn't do so hot. Maggie Ralbovsky: We have a few underperforming but it's not in a huge way and international equity is the part that we had a large under performance and that was because two of our managers actually severely underperformed partly due to the fact that we rallied international were quite low quality. I'm going to show you some of the data for these two managers but just on a total fund level you can see the underperformance is actually relatively small. And with this performance we're actually ranked 23rd percentile the universe so it's actually a relatively good quarter even though we underperformed. Doris Flores-Brooks: 23rd percentile out of how many? Maggie Ralbovsky: So, 23rd is the top 23rd percent. Doris Flores-Brooks: And how many in the. Gerard Cruz: This is all public funds? Maggie Ralbovsky: Yeah. Wilfred Leon Guerrero: Seventy something and below, right? Maggie Ralbovsky: Right, yes all public funds are reported to tax universe. Gerard Cruz: So it's pretty big. Maggie Ralbovsky: Yeah. Okay, so let's talk about Northern Trust. Northern Trust had a subpoena. Doris Flores-Brooks: Oh my gosh. Why? Maggie Ralbovsky: It may just turn out to be something. Wilfred Leon Guerrero: I told you guys about this, I wouldn't trust those bankers. Gerard Cruz: But these guys have been in litigation in Chicago for a long time. Maggie Ralbovsky: Yes. Rosalia Bordallo: This is ongoing Dr. L.G. Maggie Ralbovsky: This is new. But this is a new subpoena from SEC. Gerard Cruz: But it's actually related to. Maggie Ralbovsky: To past. Gerard Cruz: Okay. Maggie Ralbovsky: So this was not something new. Joe San Agustin: Actually, Fred you curtail securities lendings and all that based on that school in the Northern. Doris Flores-Brooks: Not directly only indirectly, right. Maggie Ralbovsky: That's right. Yeah we actually don't have an exposure to this issue but it is something just as an update that they received the subpoena. Joe San Agustin: Pennsylvania school house or something. David O'Brien: Sorry, excuse me I have a lunch I have to go to.

Maggie Ralbovsky: Okay, so that's a quick update and let's move on and let's take a look at our asset allocation page 33. Page 33 is the asset allocation. Wilfred Leon Guerrero: Wait on Northern Trust. Antolina Leon Guerrero: Your focus list are the better ones. Maggie Ralbovsky: We have no direct exposure because our securities lending program does not allow them for re-investment it's a treasury only, this issue. Joe San Agustin: So, we're not involved in this. Maggie Ralbovsky: No. This issue. Joe San Agustin: We got out of it really. Maggie Ralbovsky: We never really participated. Remember they asked us to do it we never did it. So this issue has something to do with re-investment pool of their collateral and we do not participate in that re-investment program. Joe San Agustin: They wanted us remember. Maggie Ralbovsky: That's right. Joe San Agustin: Even when they came to Guam for that. They made a personal appeal. Wilfred Leon Guerrero: So if your security lending is under investigation. James Duenas: Even though it does not directly impact us, how big of an indirect impact? Maggie Ralbovsky: I think if SEC found any deficiencies they may ask Northern Trust to pay a fine or make their shareholders. Gerard Cruz: Shareholders? Clients? Maggie Ralbovsky: Clients whole because during the time when people wanted to redeem their money, Northern Trust put restrictions on them so those people actually couldn't take their money out because Northern Trust lending pool froze up. Their lending pool had no liquidity anymore so they

couldn't actually return people's money. So, the SEC may ask them to go back and calculate the damage. Gerard Cruz: I thought they did that though.

Maggie Ralbovsky: They had a gate so they actually had said this entire pool can only redeem 2% every month, so if you are the person who send in your redemption request after the first 2%, sorry you have to wait until next month and I'm going to put you on top of the list. So they kept this waiting list going until most recently. This most recent quarter they actually distributed the remaining money. It took how many years? 7 years for them to unwind this whole thing. Antolina Leon Guerrero: Lola COLA. Maggie Ralbovsky: So SEC is going back to check on this whole practice. Paula Blas: No, it's still ongoing. Antolina Leon Guerrero: I know that's what I mean, it's still not unwind. Paula Blas: The Lola COLA. Maggie Ralbovsky: Okay. Shall we take a look at asset allocation on page 33? Wilfred Leon Guerrero: 33? Maggie Ralbovsky: 33. So, page 33 asset allocation we did last time have a decision to wait until we do the asset allocation change so even though the actual risk policy is above the range and the differential we waived that range for now. I just want to make sure we know that, right now it is above range differential. Okay. Now let's take a look at the U.S. equity composite which is page 42. James Duenas: When were we going to correct this? Wilfred Leon Guerrero: When are we what? James Duenas: Correct it? Wilfred Leon Guerrero: Correct it. Antolina Leon Guerrero: We had to wait for the law to be passed. Maggie Ralbovsky: No, we had to wait until the RFP. Antolina Leon Guerrero: Right, it's just part of the process. Rosalia Bordallo: The law had to be changed. Wilfred Leon Guerrero: What law? What law needs to be changed? Antolina Leon Guerrero: The investment. Maggie Ralbovsky: Did we say what? Diana Bernardo: Did we say we're waiting 6 months. Maggie Ralbovsky: Yeah we did. Diana Bernardo: Was that the time frame? Maggie Ralbovsky: We did. Wilfred Leon Guerrero: Yeah, we held back on the rebalancing. Rosalia Bordallo: So the law has been changed and then you walk to the next step of issuing out RFP. Doris Flores-Brooks: You haven't issued the RFP yet though, right? Maggie Ralbovsky: We did say 6 months. Paula Blas: For the transition it's going to close July 10th for transition managers. Antolina Leon Guerrero: Because we have to set up transition managers first before we, remember we needed a place to put the money when we. Gerard Cruz: That's coming along though, right? Paula Blas: Yes. July 10th it closes. Wilfred Leon Guerrero: And that RFP has already been issued? Paula Blas: It's going to be issued in the P & I on June 6th. It has to go into their magazine. Antolina Leon Guerrero: And it's like 3 at one time right we're doing. Paula Blas: No there's more than one transition manager that we're. Antolina Leon Guerrero: To take advantage of. Paula Blas: Yeah so there's one for fixed income, one for. Maggie Ralbovsky: We just have a bench that every time we have this pre-bid for it. Paula Blas: That's kind of how we. Maggie Ralbovsky: Framed it. Wilfred Leon Guerrero: You know she needed to convince us. Paula Blas: It took longer to convince them. Okay, move on.

Maggie Ralbovsky: Okay, so our managers, we have one manager on watch and I'm keeping them on. Wilfred Leon Guerrero: What page are you on? Maggie Ralbovsky: I'm on page 42. Gerard Cruz: 42? Maggie Ralbovsky: All these others just data. Page 42, Eaton Vance is on watch and I'm actually happy to report that April they out performed which would be if they didn't it would be anti the theory right because April was the consolidation month where all the high flyers underperformed and their whole underperformance was due to the fact they avoid these high buyers. Gerard Cruz: Stick

with quality. Maggie Ralbovsky: That's right. So that actually proved out to be true in April but as of March they are still under performing. I want to show you their historical performance and why we are not recommending changing the manager because on page 45 you can see that the underperformance was very concentrating to the near term. Okay, so this is page 45, this is a chart that's the Universe Comparison chart and you want to be on the top of the chart. The higher you are the better off you are and you can see the blue dots are Eaton Vance. And Eaton Vance underperformance is near term but near term they have been struggling. So that's that. That's the reason I'm not. Wilfred Leon Guerrero: It's the same team. Maggie Ralbovsky: Yeah it is the same team. Wilfred Leon Guerrero: Now, zero in 2007. Maggie Ralbovsky: It is the same thing. That is correct, that is correct. Wilfred Leon Guerrero: Do you think they're. Maggie Ralbovsky: No, it's the market environment. Antolina Leon Guerrero: So you're saying April it's going to go up? James Duenas: This is a negative correlation. Maggie Ralbovsky: No, this is the investment style issue so this portfolio manager has been focusing on higher quality sectors and they simply avoided things like REITs and stuff. And those are the sectors the lower quality sectors have been rallying until this past month. Antolina Leon Guerrero: So we'll see this change in the next for April. Oh cause this is quarterly right. Maggie Ralbovsky: This is a 3 year return so they'll have to continue to do better. So I do want to put them on watch to see if that happens but at this time I am not recommending any changes to this manager just put on watch. I want to address.

Wilfred Leon Guerrero: I thought we have them on watch? Maggie Ralbovsky: They have been on watch. Wilfred Leon Guerrero: For how long? Maggie Ralbovsky: We have had them on watch. Doris Flores-Brooks: Since 2011. Maggie Ralbovsky: No, we have had them probably for a year or so already. Let's talk about Numeric. Numeric had this thing they hold a security called Altisource. Antolina Leon Guerrero: I remember that. Maggie Ralbovsky: They still hold the security. Antolina Leon Guerrero: Litigation. Gerard Cruz: They still hold it, right. Maggie Ralbovsky: They still hold it. They sold a few shares. But, the total when they initiated the position was 700 thousand, I think right now it's 500 thousand. Gerard Cruz: But the issue that we were being asked to consider has to do with not the performance of this stock it was the relationship between this and the affiliate. And they're saying that there's a lack of arms length dealing. Maggie Ralbovsky: Yeah, they're saying that they are overpaying this company. Gerard Cruz: The management company. Maggie Ralbovsky: Yeah the management company and the reason they say that is because there's a total of 3 companies do what they do. So there's total of 3. So compared to this company with the other two peers. The peers this company is paying more to the management company than the other two. But that's. Gerard Cruz: There's a related party involved and that's why their rationale is that they're paying more. Maggie Ralbovsky: Because the chairman actually is the biggest share holder of the related company which is not rare in REITs. Now, the reason they paid this company more was because their contract is actually on a performance base so it's like a revenue sharing kind. So if the underlined company does better they get paid better. So just because the other 2 companies were actually on fixed fee this company is on performance fee turned out to be higher on that. Gerard Cruz: The dollar amount turned out to be higher. Maggie Ralbovsky: That's right. So for the same service turns out to be higher. Which is a very gray argument to say they're overpaying it. No, I personally think this is a going to be a very hard case to.

Paula Blas: They did say it was novel. They were just chasing to see. Gerard Cruz: They said they didn't think it would go anywhere. Maggie Ralbovsky: They said that? Gerard Cruz: Well I don't know did they say they were looking. Actually I don't know, they may have not said that, I'm sorry. Maggie Ralbovsky: Yeah so you know. Antolina Leon Guerrero: Right if the deal is you say you'll take a fixed fee and then you get mad because somebody's underperformance fee gets paid more, but that was the deal you agreed to a fixed fee, and that's the performance that was bad and paid less I'm sure you wouldn't have given the difference. Maggie Ralbovsky: Right. So their own performance it's like you hired money manager you pay one money manager on performance with one money manager on fixed fee, you really can't make a case to say who is the overpay. Antolina Leon Guerrero: Right, how come he gets more? Maggie Ralbovsky: That's right. Gerard Cruz: I think the issue was not so much that, I think the issue was the related party. Maggie Ralbovsky: Well all these are related parties. Gerard Cruz: I am not making the argument, I'm just repeating it. Maggie Ralbovsky: Right, I know the reason they think its related party be paid more they think they paid more was because it's related party, but that's a new point because that's how REIT managers do it. You know REITs is basically a financing structure and they can set up all these different parties by themselves basically out source it. Gerard Cruz: But here's our concern or at least my concern with this whole thing is that we look to you for investment advice and then we look to these attorneys for legal advice, right. Maggie Ralbovsky: Yeah I'm not giving legal advice. Gerard Cruz: No I understand that but yes. Maggie Ralbovsky: This is not advice let me hedge it, I'm not a lawyer and I really do not want to upwind on this matter I'm just offering what the observation is from my vantage point. So these are basic is factual. Gerard Cruz: No I think our decision wasn't based on what you said it was more based on what Joanne advised us right, it was our Board. Maggie Ralbovsky: Yes, so for the record this is just a factual information here there is no opinion here. Paula Blas: So just based on the type of service that this Altisource, this company does, how many of them? Maggie Ralbovsky: There's only 3 companies that are public traded. Paula Blas: It's only the 3 that actually do it? Maggie Ralbovsky: Because it's kind of a new thing after 2008, this company's business is basically going out to the people who couldn't pay their mortgages. So they basically say okay I'm going to take over your property and you pay me a rent. So, basically it's like from you're the owner but I am not going to evict you just because you didn't pay your mortgage. I'm going to let you stay in your house but you have to pay me rent. So it's like a modified arrangement so these people can stay in the house. Gerard Cruz: They lose the house they just rent it, right? They don't own the home anymore. Maggie Ralbovsky: Unless they make it up. So there's some sort of deal you could have buy back in the future. Doris Flores-Brooks: It says either foreclose or rent or sale. Maggie Ralbovsky: Yeah unless this person is really, really not impossible then they are going to sell the property for you. So that's the business motto which really started this whole industry after 2008. There was no such industry so that's why there's so few people.

Doris Flores-Brooks: This takes a lot of time, too. Joe San Agustin: Banks do that. Maggie Ralbovsky: The banks do that, not REITS. Of course there's people that's doing that but it's not REITs. So these are REITs. So, then it has to hire service providers somebody has to service the loans. So it's basically outsourced to these other companies which have common shareholder. Not all common shareholder just one person. So that's that business motto and they're paying these people based on performance. So that's the

issue there. Wilfred Leon Guerrero: You know getting back to what Gerry is talking about, the facts that you're giving us does not contain information about this conflict of interest. Maggie Ralbovsky: I do not know if I should say this as a conflict of interest or not because I am not giving you any advice, I'm just saying this is the fact. Wilfred Leon Guerrero: I understand that but that's the point that Gerry made is that the allegation here is a conflict of interest and the fact that you're giving us there's no conflict of interest here.

Maggie Ralbovsky: Well the lawyers alleging this pre-arrangements was because the related company has a common shareholder. Wilfred Leon Guerrero: Right, a conflict, yeah. Maggie Ralbovsky: That's what they are saying. They would have to prove this case and the thing is I don't know if they can prove this case. So, the reality is also that the security has outperformed the other two. Wilfred Leon Guerrero: See the thing about it is that I think Joanne is basing her opinion on the information they're getting from you. Maggie Ralbovsky: Well the information I'm giving her is just a factual information so then she. Wilfred Leon Guerrero: But it's not addressing the conflict of interest that is being alleged. What is the conflict of interest you know I think that's what needs to be addressed? Maggie Ralbovsky: Okay. So what are you suggesting? Joe San Agustin: Is there a conflict of interest? Paula Blas: I think that's what is being alleged. Maggie Ralbovsky: Right. Paula Blas: Is that there is a conflict of interest. It's being alleged by the securities. Maggie Ralbovsky: By those people who were soliciting. Wilfred Leon Guerrero: Whatever. Maggie Ralbovsky: So what are you suggesting? Are you suggesting these facts are not answering the question? Wilfred Leon Guerrero: Right. Maggie Ralbovsky: But these are the facts. Joe San Agustin: The fact there's an alleged conflict of interest but what is the conflict of interest? Paula Blas: It hasn't been determined whether there is or isn't. Joe San Agustin: Have you determined where's the conflict of interest? What is the conflict? What was the conflict of interest? Doris Flores-Brooks: I guess the question is did Wilshire do its own due diligence to satisfy itself about the alleged conflict of interest?

Maggie Ralbovsky: Wait, wait so the alleged conflict is that this company Altisource is paying the service provider higher than the industry fixed fee. Wilfred Leon Guerrero: That is the alleged? Maggie Ralbovsky: That is the alleged conflict of interest. Paula Blas: There are only 3 companies that exist and 2 of them are on a fixed fee and this company is on a performance fee but because they get a higher fee versus the 2 fixed fees, there's an alleged conflict because they are saying that Altisource's Chairman of the Board is the same person that owns the company. Doris Flores-Brooks: How come the others weren't offered performance as opposed to fixed? Paula Blas: They probably didn't ask for it. See and that's what we were saying is if they underperformed and they got a reduced fee below the fixed fee, would they have made up the difference? I mean it works both ways. James Duenas: So it would only be a conflict if they underperformed but then they got more back. Maggie Ralbovsky: Yeah so if they underperformed they still get paid more than you can make a case. But the fact of the matter is that they have been over performing so they get paid more and is that a conflict of interest or not? It's a case you have to prove and that you don't know how to prove that. Doris Flores-Brooks: But the issue here is how come the two were not offered performance and instead. Maggie Ralbovsky: But it's a private company there's no. Gerard Cruz: There's 3 different companies, so they structured. Doris Flores-Brooks: So I can see where the conflict might arise because hey

you two we're only going to give you a fix, but hey because I'm related to you I'm going to give you performance. Maggie Ralbovsky: Oh no that wasn't the case. The other two are two different companies. Doris Flores-Brooks: That's my point because the other company is where he is an interest he got a better deal because he's related, that's what I'm saying. Verse the other two they weren't wrong we got to pay fixed regardless. James Duenas: Could it also been that the two came in early. Maggie Ralbovsky: The other two are not affiliated with them are not entered in this contract. James Duenas: When they made their contracts they made their contracts first without thinking about that and now they are saying sorry.

Rosalia Bordallo: No, this company doesn't deal with these other companies they are only dealing with this. These other companies this is the normal practice of how they charge they are just using them as examples and so they are saying, look at these other companies this is how they charge. James Duenas: Oh they all don't. Rosalia Bordallo: But they're not working with this company at all. Maggie Ralbovsky: That's right. Rosalia Bordallo: This company is like sister or brother or whatever you want to call it. James Duenas: What is the industry intake? Maggie Ralbovsky: The industry. James Duenas: Fixed or performance fees. Maggie Ralbovsky: This industry started in 2008. James Duenas: Not the company. Maggie Ralbovsky: Yeah this industry these three companies are in this industry and this industry has started after 2008 and those other two companies were also sort of affiliated with their parent company because that's their motto, people cannot build up their entire thing they outsource portions to companies that sort of affiliate with them. James Duenas: What I'm really trying to say is like they're governed by certain party right, what is the certain party that governs them if they allow both fixed and performance then it's fine. Maggie Ralbovsky: What I'm saying is that there's no structure governing party, this is a private company they arrange into a contract with another private company. So that's just the way it is. James Duenas: Yeah but then there's always the law governing.

Wilfred Leon Guerrero: Chairman, you know one thing that I am concerned about is that whenever you ask a legal opinion from, what the heck is her name? Joe San Agustin: Joanne. Wilfred Leon Guerrero: Yeah Joanne, she consults with Maggie and so we're not getting an independent. Maggie Ralbovsky: I didn't give her any advice I just provided her. Doris Flores-Brooks: I think Joanne has to get the lay of the land and then from that information make a determination. She has to consult with. Maggie Ralbovsky: She just asked me for the background information which was just the facts, I just provide what the data points are and then she made her assessment. Wilfred Leon Guerrero: But okay, I wonder whether if Joanne consults with the people in San Diego? Joe San Agustin: Who in San Diego? Wilfred Leon Guerrero: You know. Antolina Leon Guerrero: BLBG? Joe San Agustin: Oh Bernstein? Wilfred Leon Guerrero: Yeah. Antolina Leon Guerrero: No, you see that's the whole thing he didn't want to take an action without getting somebody else. Wilfred Leon Guerrero: Right, but at least talk to them. Paula Blas: Well she had. Joe San Agustin: She opted not to talk to them. That's up to her. She opted to talk to them. Paula Blas: She went by what he wrote regarding what the case was and applying based on that information that Bernstein already provided. Joe San Agustin: If she opted not to talk to Bernstein, that's her problem not mine. Antolina Leon Guerrero: Her prerogative not her problem. Wilfred Leon Guerrero: Well I'm concerned about something. Joe San Agustin: Really. That's her legal opinion. Her bases on the opinion got to be

what she has, she felt she doesn't want to talk to Bernstein rather talk to Maggie, that's her position. I don't want to go beyond that before you know it we start questioning every legal opinion that comes in. What's your rationale?

Wilfred Leon Guerrero: No, no, no I just sometime. Joe San Agustin: You would think she would do it, but she didn't do it apparently. I don't know if she did or not. For all I know she might have talked to Bernstein. Because we never got a reaction back, when we told Bernstein no more all we got is a flat email response. Paula Blas: Just a thank you. Joe San Agustin: Just a thank you and that's it. Didn't present any argument one way or the other. I would expect Bernstein to say how about this way or this way didn't get anything we just told them the decision and that's it and he drops it. I expect Bernstein to ask back and say what's the rationale, why you cancelled? Antolina Leon Guerrero: We told them why. Joe San Agustin: I know but he didn't challenge it. Antolina Leon Guerrero: Right because we gave him a good reason for why we didn't do it. Joe San Agustin: If I'm a lawyer and I'm told then I should pursue this case. Antolina Leon Guerrero: There wasn't even any action. There was no demonstration of harm I mean that's. Joe San Agustin: Bernstein agreed otherwise we would question why they just disagreed. That's why I was asking Paula what was their reply, she said nothing just a flat email. Wilfred Leon Guerrero: Okay. Paula Blas: Just a thank you, not a flat. Joe San Agustin: I know but see that even raises the question why Bernstein act the first time and didn't even argue back why it was rejected. For me that's a yellow flag.

Maggie Ralbovsky: Okay, let's look at international. International Equity. Page 50 is the International the summary of the international managers. For this quarter we have 3 managers underperforming and also all underperformance was above 100 basis points for this quarter. Dimensional was the only one that actually outperformed so we had a pretty large underperformance and I wanted to not make any recommendation for change or on watch because I want to show you page 53, to show you that the underperformance for Earnest and Fisher are both short term in nature. You can see this is the same universe comparison chart. Earnest pretty much dropped off in the very recent quarters and Fisher was more sporadic. Fisher has never been very consistent performer on the beginning of time anyway so but. Wilfred Leon Guerrero: Focus list is your best performer, right? Maggie Ralbovsky: Focus list is our assessment of their stability and their experience of the organization, it is independent of the performance. Antolina Leon Guerrero: But it is the highest rating? Maggie Ralbovsky: It's the highest rating yes it is. So we do think Earnest is a very strong organization and it's very similar to Eaton Vance. They are underperformed recently and that is because. Wilfred Leon Guerrero: They're strong organization but they are not making. Maggie Ralbovsky: Not in the recent quarter and that's what I want to show you on 53, historically it's been a very strong performer you can see that right. The recent underperformance is very much related to their style. Very similar to Eaton Vance's style just focus portfolio it's very concentrated portfolio follow focus on bottom up high quality stock picker kind of a style and that really hasn't helped them for this most recent period. On the other hand Fisher is supposed to be the other kind of style. Fisher is a more top down manager making macro calls and you can see their performance has not been very consistent starting from the beginning anyway. So bottom line I have no recommendation any change but we're going to monitor these managers performance.

Maggie Ralbovsky: Okay, let's move on to U.S. Fixed Income. Now we have one manager on watch there and then we continue to suggest keep this manager on watch. Recommend this manager on watch. So let's take a look at page 58. 58 is the summary of the fixed income portion and you see that we had a good quarter all managers out performed. But Franklin continues to underperform since inception and I want to show you the universe comparison on page 60 and 61. And you can see Franklin has become consistently been ranking below 75 percentile and this is a very different picture than the other managers I showed you earlier. So this is why we continue to recommend putting them on watch and exactly the short term and long term. Joe San Agustin: You said they're consistent at 70%? Maggie Ralbovsky: Yeah, look at the blue dot the blue dot on page 60. Rosalia Bordallo: And what's the cross thing? Is that the. Maggie Ralbovsky: The cross thing is the benchmark. Rosalia Bordallo: Okay, so for the last 2 quarters they 1 2 3 4 they're above the benchmark? Maggie Ralbovsky: They're above the benchmark for 3 year, this is a 3 year number so every dot is a 3 year number but they're below 70 percentile. And now the other two bond managers on page 61 and you can see both of them are more often than not above median. So that's a completely different picture for Franklin. Doris Flores-Brooks: And this has been going on since 2007, so this is already 7 years they've been on watch 7 years? Joe San Agustin: Wow. Maggie Ralbovsky: I can't speak for 7 years, I've only have been here for 4.

Rosalia Bordallo: I thought all the bond managers have the same benchmark? Maggie Ralbovsky: Yeah, they do. Rosalia Bordallo: So I would think that, okay this is Garcia Hamilton, right? It's the same benchmark where in the picture wouldn't the benchmark list the same as this? Maggie Ralbovsky: Well the benchmark in this chart has a different color, it's the green one see that? Rosalia Bordallo: So you have 2 managers on the bottom. Maggie Ralbovsky: Yes, so I have both managers. Rosalia Bordallo: So you changed the benchmark? Maggie Ralbovsky: I changed the color. Probably should have kept it. James Duenas: What is GHA? Maggie Ralbovsky: It's Garcia Hamilton. Rosalia Bordallo: See that's why that little cross, benchmark on the top. Maggie Ralbovsky: It's the green thing. Antolina Leon Guerrero: The template it's the automatic field. Maggie Ralbovsky: Yes basically the computer did it. Doris Flores-Brooks: The reason it is different is because the one above only has 2, this one has 3. Rosalia Bordallo: See she changed this is the benchmark here, right here. It should have stayed like the cross. The benchmark should have stayed the same. Maggie Ralbovsky: I should have done that, yes.

Maggie Ralbovsky: Okay, so last but not least is the REIT in the portfolio, page 66. We actually have one manager outperforming one underperforming for this quarter. I think we're going to hear from them tomorrow for the 3 managers. REITs as you know this is a sector we're going to make a change for so we're going to select a new manager so I do want just to show you the results so there's nothing. Gerard Cruz: We're selecting a global manager. Maggie Ralbovsky: Global manager. Gerard Cruz: And splitting the money the funding is going to come from these two guys? No. Maggie Ralbovsky: Basically both of them are going to be gone. Gerard Cruz: Both of these managers are going to be gone. Maggie Ralbovsky: Yeah. Well you may pick one of them to make them a global manager. That's yet to be determined. Antolina Leon Guerrero: Oh they can compete. They can submit a proposal, I see. Maggie Ralbovsky: That's right. Doris Flores-Brooks: So you're only going to have one manager in this section as opposed to

two? Antolina Leon Guerrero: And it's going to be global. Paula Blas: Right now it's just U.S. Maggie Ralbovsky: Okay. Doris Flores-Brook: How much is the share they're going to get? Maggie Ralbovsky: We're going to reduce allocation of 5% as well. Global. Paula Blas: Is that it Maggie. Maggie Ralbovsky: That's it. Gerard Cruz: What time do we have? Paula Blas: 12:05.

Income Research & Management

Wilfred Leon Guerrero: Okay we'll begin and we'll let you lead us in discussion about the portfolio and the same thing any organization changes and any regulatory agencies issues with you and litigation. Steve Weiss: Okay. Maybe I'll hit the litigation thing first is because you all are aware that one of our employees who left us a few years ago and he sued us for wrongful termination and age discrimination and he's fifty something. Wilfred Leon Guerrero: Age discrimination? Steve Weiss: But you can sue over forty. Yeah he can sue for age discrimination. And that's been sort of ongoing and you know ultimately the way it comes out it's not going to affect us as a firm from a settlement point of view but want to update you that the trial is actually happening right now as we speak. When we tried to settle and it went to trial and you know when you go to jury anything can happen but we're prepared for either way we think we have a good case we'll be fine even if we lose we have plenty of cash and insurance and all those kind of stuff. So it won't affect the organization but we want to keep you abreast the situation so I'll be able to send you an email probably in a week and a half after the decision to let you know which way it came out but again it will not have any impact on the way we are as a firm but wanted to give you that and get that out of the way. Other than that no regulatory issues, no real organizational changes, couple of new hires here there on the analyst side but we promoted some folks to portfolio manager and we added since last time we were here a few employee share holders and now there are 35 employee share holders total who own the firm out of about 140 total employees. So the plan continues to do that majority owners own this is John Sommers, Jack Sommers and so some of his family own 53% from an economic ownership point of view. But we also introduced voting shares so they own the voting shares and ultimately they will take direct economic ownership below 50% and continue to take it below after they transfer the ownership to the rest of us over time. So we're committed to remaining an independent firm and will not be selling ever to some sort of bigger organization.

Steve Weiss: So let me jump in, everyone has a book, I'll start with performance first everyone probably wants to talk about that and then we'll go into market charts and a little bit of the portfolio and take questions and when do you want me to stop talking? Wilfred Leon Guerrero: You just keep talking, we'll interrupt. Steve Weiss: Okay, excellent. So on page 2, you could see a performance there we have all different time periods that you asked for. On the far right is the since inception numbers that's an annualized number since you hired us back in the end of '08 the beginning of '09 and we've been outperforming obviously very well since inception. We actually been outperforming in every time period here, so I think one of the time periods I'd like to point out more than anything is that where you asked for September 2012 through September 2013, and I think that's an important time frame because that's when the market had a rising rate environment that's when rates were really starting to take off. Last June is

when rates really started to rise that's when the Fed talked about tapering and you can see that in that market when rates rise we really outperformed a lot. And that's one thing we pride ourselves is really trying but we try not to outperform all the time but we think in a rising rate environment the way we approach our portfolio we'll typically have an advantage over the index and we'll go into some of that a little bit more. We really try to focus on the downside protection. So we're on the...you need another book?

Steve Weiss: We're on page 2. Joe San Agustin: Oh I'm looking at other companies. Paula Blas: He's in tomorrow. Steve Weiss: And you can see we outperformed for the first quarter of this year as well 232 basis points well 2.32% versus 1.84. And I can tell you that over this time period the main sources of our performance have been really underweight to treasuries and are overweight to corporate bonds and are overweight to securitized paper. So corporate bonds continue to perform very well and have been really outperforming treasuries for quite a while now and we've been remaining overweight in that position we'll talk about how we're set up in a second. But basically corporates are doing well because the economy is okay, corporate fundamentals are decent but there's a real strong tactical demand for corporate bonds. So everyone wants something that yield more than treasuries and there's a lot of people just buying anything they can that yield more than treasuries and corporate bonds have benefit that. Little cash on the sideline looking for places to put it and corporate bonds have been the biggest beneficiary of that. So our strategy has worked. If you remember we don't make interest rates bets either so our duration of our total portfolio remain similar to that of the benchmark. We're really going to try and add our value by bottom up bond picking we're going to try to buy better bonds with lower ended index. Any questions on the performance?

Steve Weiss: So there's a bunch of charts here that talk about the market, I won't bore you to tears with everyone but I'll just certain touch on some highlights. When you go to page 4, what you're looking at there, the dark blue line is the yield on the 10 year treasury and the light blue line is the spread of U.S. Corporate bonds over treasuries and you can see really that time period I talked about where we outperformed from 9/30/12 through 9/30/13 is really that area where the rates rose, you can sort of see the rates continuously sort of rise during that time period and that's where I think we really earn our keep in outperform there. And that rise in the rates was mainly attributed to the economy doing a little bit better and the Fed talking about tapering better quantitative easing program and basically going to stop buying as many treasuries and mortgage back securities. And then since then the market's kind of gone a little sideways, rising a little bit more towards the end of the year and then rates coming right back down as we turn the corner so we're back kind in to that environment where everyone is worried about rates and we can talk about what we think about rates. But, generally you know the direction of rates the market is telling you that rates are going to rise we can sort of see there the way the markets projecting it, not a ton of rising rates are being predicted by the market but who knows.

When you go to page 5 couple of highlights here this is sort of the US economic environment and I would characterize it by saying its okay, not great. So there are some positive things happening on the upper left hand side. You know GDP growth has been okay, Industrial production is up, on the lower left hand side you've got payrolls continue to add jobs to the overall economy but the number I think that counter acts that is that

blue line has been going down lower and lower and that's the labor force participation so that's the real issue I think that the Fed is watching on basically people who are not working who now have stopped looking for work. So the unemployment rate can be sometimes artificially high because they keep decreasing the denominator so people just aren't looking for work anymore. So that's something really that has the Fed worried. On the lower right hand side Cap Ex and Consumer Spending is basically consumer spending and corporate spending was kind of on a downward trajectory there and has kind of leveled off recently so that could be a positive sign to the economy. So again overall when you think about the US economy we're not overly constructive we think it's in okay shape. We don't think it's certainly going to blow up but it's also not chugging along the way I think we would like it to this far into recovery.

Steve Weiss: On page 6, this sort of talking more about rates and this gets into what rates are going to do, the upper left hand side, the light blue line is the current shape of the yield curve as of 4/30 this is treasury yield positively sloped and then 4/30/2015 is where the market is saying it thinks rates are going to go. So it thinks rates are going to go higher but not dramatically so and flatten out a little bit so the long end might not rise as much as the front end of the curve. The really interesting chart is the one on the lower left hand side. What this is, is basically going back over the past 30 years, taking the yield on the 10 year treasury and subtracting out the yield on the 2 year treasury and creating a spread. So what it's telling you is that over the past 30 years, the spread has never gotten beyond roughly 3%. And why that's important is that means that the 10 year and we're pretty much at the widest right now what that means is that the 10 year treasury probably can't move higher until short rates start to come higher, until this 2 year starts to rise. And the 2 years really not going to start to go up in yield until the Fed really officially tries to attack and raise short term rates. So everyone is worried about the rates, where they going to go who knows, but in terms of the longer term rates they're really not going to move until the Fed moves the front end of the curve, according to this chart.

On page 7, in this where overweight corporate bonds this is sort of a couple of different pictures about the corporate market this is the fundamentals, the corporate fundamentals are decent. So when you look at all the companies in the United States and look at their earnings and their balance sheets and how they are using their cash, it generally paints a pretty strong picture. So you look on the upper left hand side, you look at the last 3 bars sort of doing a stair step down, that's leverage. So leverage is coming down and as a bond holder you want leverage to come down because that means the company is in decent shape. One thing to watch though is this interest coverage. Interest coverage is the measure of how well the company can cover its steps they basically add up all their payments they have to make to the bond holders look at their cash and say how much do they cover it? And that's in pretty good shape the interest coverage is good. What we're worried about a little bit there is that corporations have been borrowing a decent amount but with relatively short terms they've been borrowing at the 3 year and 5 year sort of maturities and those rates are very low. So if we get a rise in rates they haven't really locked in those costs so if rates start to rise they're going to have to refinance those 3 year and 5 year bonds as they mature into higher rates which could hurt their coverage. So some of them we look very closely to see if companies are over leveraging with really low rates setting themselves up for some higher cost debt in the future. That's one of the things our analysts are focusing on.

Corporate earnings on the lower left hand side, the light blue lines. You know revenues are up, earnings are slightly positive you sort of see the last 3 quarters sort of stair stepping up there a little bit. So earnings are improving but they're not gang busters they're not where they were pre-crisis. And then on the lower right hand side is really look for every bond that we own, we really like to look and understand how management is using all this cash. So you hear a lot about tons of cash on corporate balance sheets and for us the analysts says what are they doing with that cash? Are they re-investing back in their business which would be great for the economy in general or are they using the cash to basically pay off shareholders and either increase their dividends or just buy shares back? And basically they've been using their funds really more to help shareholder returns and grow cap backs over the past year. So that's not a trend we'd like to see we'd rather see them investing in the business. That's something we're watching out for and screen very heavily on the companies that we own making sure that they are not going to do any kind of M & A activity or something like that.

Page 8 is more a picture of the technical side of the bond market. So fundamentals like I said before on the previous page are pretty good shape. And you can sort of see on the lower left hand side the spreads have really been grinding tighter and tighter over this time period. And when you look at the upper left hand side you can really see the net issuance is pretty low the dark blue lines talk about gross issuance, but there's a lot of maturities coming so when you look at actually how much net issuance is out there sort of new to market bonds are out there it's not as much as the gross issuance. You might read a lot about sort of record numbers of corporate bonds being issued but the net issuance is still relatively low. So you create a supply in demand imbalance more money chasing fewer bonds and you've got a nice technical environment where bonds spreads continue to tighten and grow tighter and tighter.

Page 9, switching gears a little bit now, is talking about commercial mortgage back securities. It's been one of our favorite sectors really since the crisis and we own in the portfolio 13.7%. And you can see that when you look at upper left hand side the price index of all properties and the major markets, there's been a steady improvement since the crisis. So commercial real estate really is doing well in the U.S. In the lower left hand side looks at within the pools of properties that we own, we track delinquencies and are the people current on their payments and overall delinquencies have sort of peaked a little bit and starting to come down, loans are being cured, newly delinquent loans have been decreasing so really the overall health of the commercial mortgage back market has been great. We haven't changed the types of deals that we buy as we've talked about these before we like to buy the bonds that are highest of the capital structure so when you look at CMBS you can buy bonds that are subordinate to somebody's claims and we don't like to buy those at all. We really focus on the higher part of the capital structures the very high quality bonds.

Page 10, talks a little bit about residential mortgage backed securities and this is probably one of our biggest under weights in the index. So the index as you know is chalk full of fixed rate pass through so your standard mortgage agency backed passed through roughly 30% of the index is in these. And this is what the Fed has been buying pretty much over the past 2 years which is part of the quantitative easing. So the upper left hand side is

basically saying who's been buying these bonds. 2013 the Fed was the major buyer but now with quantitative easing in 2014 they are not going to be as big a buyer so who's picking up the slack and that slack is being picked up by money managers like us. Potentially like us, we don't actually like the fixed rate pastures of that bar really isn't much of us but it's something to watch. So, right now issuance and the residential mortgage backed side are fairly low. So the mortgage been able to handle the Fed's stepping away and spreads haven't really done anything but it's something to watch. So if for some reason the housing market picks up and there's a lot more refinancing and more mortgage issuance coming, who's going to buy all that origination? And that's what we're going to watch another reason we're under weight on those particular bonds. Not going to spend too much time talking about municipals. We do own some taxable municipal bonds. We actually decreased our overall exposure to those they've done well and our focus is more on the revenue bonds so not the general obligation bonds. So we don't own California, we don't own Illinois we didn't own Detroit and we're sure everyone heard about Detroit. We don't own Puerto Rico. Puerto Rico bonds obviously Puerto Rico's been having some difficulties they issue their debt at 8 or 9%. Even though it may be attractive it's not in their risk spectrum that we like to play in. So we like to buy actually universities they have issued a lot of debt so we like to buy those because they are very stable and some other revenue bonds but no general obligation bonds in your portfolio right now.

So, what are we doing as a result of all this? What's that? Joe San Agustin: You don't have any Guam bonds? Steve Weiss: We do not have any Guam bonds, no. I meant to look it up. Joe San Agustin: You can't find them here. Steve Weiss: They're not out, I don't think from a ratings point of view. Joe San Agustin: No, because they're all picked up. Steve Weiss: Yes they trade and you don't issue taxable bonds do you? I think most of them are tax exempt. Yeah so for us that would benefit. Maggie Ralbovsky: Pension obligation bonds. Steve Weiss: Yeah do you have judicial pension? Maggie Ralbovsky: We have some pension obligation bonds. Steve Weiss: Okay, so they're taxable. Maggie Ralbovsky: It's probably very small. Joe San Agustin: Revenue bonds yeah. Steve Weiss: We also look at size of issuers because you want to have a certain float out there to make sure that there's a liquid market and well Guam probably trades fine, it's probably not a big enough market for us to go ahead. Joe San Agustin: Well they're not open in trading. Steve Weiss: Right. Joe San Agustin: People hang on to it. Steve Weiss: We're yield a lot so. Joe San Agustin: Yield is good. Steve Weiss: Right. So when you think about everything that I just talked about, what are we doing in the portfolio as a result of this? We're talking about an okay economy, corporate fundamentals are decent but then when you look at globally there's a lot of stuff going on and we basically been taking this opportunity over the past year to trim some of the risk out of the portfolio because we think there's going to be some potential volatility ahead both in rates and potentially in some of the fundamentals as the world tries to figure out what's going on. You've got quantitative easing happening in Europe, you've got Japan committed to lower rates, so the world doesn't feel that great right now so we want this to get a little closer to home and take out some risk. The way we've been doing that actually when you look at the nominal weightings in the portfolio there hasn't been much change, let's actually turn the page down. So if you look at page 14 on the upper right hand side, that's one of the ways to think about what we're doing in terms of risk, the obvious thing you would see would be if we were basically increasing our treasury allocations. That would tell you that we are

trimming risk. We can see here that we are not doing that actually because treasury yield is so low we actually decreased our treasury holdings. So how are we trimming risk? You look at the credit line that's the same right, 29.7 versus 29.8 that doesn't look like we're trimming risk, Securitized the same, Municipals are actually up a little bit they're down from where they were a couple of years ago, but up from last year.

So it's hard to show you what we're doing but to tell you what we're doing is you've heard us talk about we like bond structure right we like to go out and find bonds that have unique things about them, maybe it's a hundred year bond, maybe it's an off the run security, maybe we'll buy a 25 year bond instead of a 30 year bond because it's a little less liquid it trades with little bit of premium little bit of extra yield to own that bond because it's not quite as liquid. We've been trimming those positions, the less liquid bonds to get a more liquid portfolio. So while we maintain our same over weights, we believe to be a more liquid portfolio which we think will help handle some of the volatility and give us some drive power to take advantage of that volatility and we buy some of those less liquid bonds you know when it happens. Remember liquidity is a relative term so when I say liquid I don't mean non agency bonds, I don't mean the stuff that you suffered with through '08. I mean instead of being able to go to a dealer and say hey, what's your market on IBM 20 year bonds? And they'll make you a bid spread of 5 basis points, we're talking about maybe a bid spread of 10-15 basis points which is very small. You know back in the day that would translate into a quarter or a 3/8 of a point where you think about those non agency bonds they were trading with 2, 3, 4 point type markets. So that's what I mean I don't want you to get scared when I say less liquid.

So, just to review real quick on the upper left hand side of the portfolio, I actually looked at where we were 2012 to give you some relative figures and it's actually somewhat astonishing 4/30/2012 which isn't here on your book, the yield on your portfolio was 2.62% it's exactly where it is today. Which is unbelievably coincidental I mean very random that happens. But you can see we went from 2012 to 2013 rates came down a lot, the yield went from 262 down to 185 and then with the rise in rates last year, the yield went from 185 back up to 262. So we're in a lot better position frankly than you were last year. So you know you suffered with that sort of negative performance over that 1 year period but from a going forward perspective you're much happier with a 2.62% yield than you are at 1.85% yield and yield is a very strong part of a bond return and reinvesting in higher yield is actually good thing. So the other thing to point out is that spread grind a little bit tighter. The duration actually extended so when you look at the duration that's a measure of volatility in the portfolio, it went from 5.13 out to 5.51 the index is actually a 5.63 that's because there's mortgage backed securities that the index has extended out a lot and got longer maturity. So anyway, long story short we made kind of nice yield advantage value benchmark by 30 basis points that's because of our underweight to treasuries and over weight to the different spread sectors, maintaining a very high quality portfolio right on top of the benchmark. When you look down below, a healthy amount in AAA securities only some just from 14% in Triple B. So again a very high quality portfolio when you look on the right hand side you can sort of see looking at the middle column compared the far right column that's the current snapshot of the portfolio. We're about 28% in governments relative to the index which is 39 so we're under weight governments. Mostly that under weight is in treasuries, we don't like treasuries they just don't yield a lot they are going to be the most volatile part of the market when rates hopefully go higher.

What we do like is that government guarantee line to about 12% roughly now, those are the SBA's we've talked about before the small business administration certificates and those are backed explicitly by the Federal government of the United States. The trade almost 50 basis points to 1% cheaper in treasuries. So it's a nice pick up yield for a market that's been growing in size, by 28 billion they're obviously little less liquid in treasuries but from a get your money back point of view they're just as strong. We'd rather earn that 1% extra yield right now especially since we're in the low interest rate environment. So when you get in that low interest rate environment, you can chase yield many different ways. You can go lower quality, you can go pick up riskier securities. Our approach is to go ahead and buy again maybe a slightly less liquid bond but from a quality point of view, exact same thing as United States treasury with SPS probably our best idea right now.

When you look at credit we've reduced that we're basically right on pretty much on top of the benchmark now. We're still over weight in finance. One thing to say about that is right now what we like in finance is we've actually reduced the banks positions we're underweight the big banks for a while because from a credit point of view they were great. They continue to trade tighter and tighter and tighter and we worried a little bit about some issuance. We thought they were going to have to come to market with a lot of bonds to really fix some sort of some regulations that have been put on them. So we didn't like those, we did like some REITs so debt from REITs from large insurance companies and from asset managers. So the asset managers that we like in particular are KKR, Carlyle and BlackRock. So when you look at the debt of those companies, they're A rated, they're rated higher than most of the banks, much stronger fundamentals and trade a lot cheaper. So we've been a very big fan of those and that's where we can also take advantage of our size. So those three companies came to market with a total of about 3.8 billion since '09. Corporate market is 3 trillion in size roughly 3.8 billion is not a lot of bonds. A very large manager like Pimco or BlackRock really wouldn't even be able to play in that market because they couldn't buy enough of it but because of our size even though we're big at 40 billion that's still relatively small in the grand scheme of things. We can go ahead and still get some of these we think really nice ideas in the portfolio in a meaningful way.

So we're over weight industrials, we're over weight utilities, we're underweight the non corporate sectors, so sovereign and those types of names that's been a really chronic under weight for us, it's just for us when you look at the sovereign world you can buy the supra national type really high quality type stuff that trades really tight to treasuries we'd rather own some corporate bonds that yield more then you can buy the real sort of scary stuff. Turkey that yields a ton that's too risky for us. We're going to sort of hunt them back to the stuff in the middle and if we like it we'll find the bond and buy that otherwise we're probably going to remain under weight that sector. Now on the securitized so we're over weight in securitized under the 40% limit that you guys have but over weight and the interesting thing is when you look at the RNBS line and I won't bore you too much more with details but in the index that 29% is all of those fixed rate passed throughs that I talked about. We're 22% but when you look at the fixed rate passed through component of that it's only 7%. It's actually very underweight the index in terms of fixed rate passes. We like our hyper on structures that we talked about before some multi-family structures which don't have nearly the interest rate volatility as the residential single family

mortgages and then some CMO structures in very short duration very understandable cash flow CMO. So we think it's a better way to get exposure to the residential mortgage back all agency backed none of this stuff is non agency. All agency backed little bit yieldier but a lot less volatile. It's not going to lengthen or shorten with changes in interest rates the way the fixed rates pass throughs are and then that over weight communities that we've talked about. So that's generally how the portfolio is positioned, are there any questions on that? I covered a lot in a very short time frame manner.

Maggie Ralbovsky: So for the RNBS the agency mortgage backed securities the recent issues by Fannie was a different structure, has the risk sharing kind of thing. Steve Weiss: Yes. Maggie Ralbovsky: So do you see in the future more of these deals are going to be in that format? Steve Weiss: I think so, I think the GSC's are trying to figure themselves out and they have Melwat who sort of in charge there and I think he's a big fan of risk sharing component of issuance so yeah I think we can continue to see that. Maggie Ralbovsky: Are you participating in that too? Steve Weiss: I don't think we have done much of that I think our focus really on the residential side is still some of the older issue higher coupon structure that we think have really gone through. The way we approach these bonds is to really look and understand the potential for pre-payments. The residential mortgage back side you know you can get your money back because you trust the United States government but the question is when do you get your money back? And that's the analysis. So if prepayments were to pick up faster than you were expecting, you get your money back sooner. And right now a lot of bonds are trading at a premium at dollar priced you don't want to get your money back too soon. So we spent a lot of time trying to understand the prepayments and the underlined cash flows of these things and for us a lot of the older issued bonds when you look at what's still left in these pools they got higher coupons the people whose mortgages in the pools have had 3, 4, 5 years of the opportunity to refinance those mortgages and haven't so the question is why haven't they? A lot of them are under water a lot of them actually at this point the loan is older they don't want to extend back out again, they're happy having a shorter mortgage. And there's the heart program and hand programs some things that the government is trying to do to help people but a lot of these pools the loans are harpable to use that word so there's some burn out in those pools. We like going by those because we think basically we understand the cash flows, we're not going to get surprises on the prepayment side the bonds make it a little bit longer which is great because their premium structure will earn more yield on it.

So our focus really have been on some of those older issues and not as much on the current issuance because the current issuance had really low coupons and those are the ones that really got hurt when rates rose and we don't want to do that. The other thing we don't do is we don't buy TBA's so I don't know if you're familiar with this but there's a. Maggie Ralbovsky: Remember we talked about TBA's to be announced mortgage last time. Steve Weiss: To be announced basically one of the common structures in the mortgage market has issued basically TBA's. What happens is the GSC Fannie and Freddie will issue they'll say alright we're going to have 2 billion of this traunch TBA, and that means you don't know what the coupon is, you don't know the underlined pools are. Joe San Agustin: You don't know when it'll be issued. Steve Weiss: You don't know when they'll be issued. We know when they'll be issued but they're forward settling. It's settled a long time in the future and it's a way for the larger managers to get exposure. They can't go

buy. Maggie Ralbovsky: Remember we talked about whether it's a future, whether it's a derivative. Gerard Cruz: We concluded it was, right? Maggie Ralbovsky: We concluded we don't allow it, right. Because we don't allow the treasury futures. Paula Blas: It hasn't been defined. Maggie Ralbovsky: Yeah because nobody really. We sort of know what you're buying just like treasury futures.

Steve Weiss: It's kind of like, it's solid. The bottom line is we've never bought them and because of our size, we don't have to buy them to get exposure. We'd rather go look at the bonds if we want that bond and we're going to pay the price for that bond. We're going to get that bond today as opposed to having to get exposure to the mortgage market in that sort of big way it's also implied leverage. So that treasury market practice group TMPG recently came out and recommended that anybody who is going to trade TBA's along with some other regular old mortgage backed securities are going to have to negotiate agreements with the primary dealers out there to post collateral which complicates everything and we don't do TBA's which is what it's aimed at but it also focuses on longer than T plus 3 settlements for regular mortgage bonds. So we may go ahead and negotiate some of these agreements on behalf of our clients in case we want to buy something that settles longer than T plus 3. Gerard Cruz: And what instance would you have of a settlement beyond 3 days? Steve Weiss: So what happens is because the mortgage market is so complicated and basically every month all this math goes on and says how many prepayments happens in this loan and they do these factor adjustments. There's a convention in the market right now to do good settlement basically means we know you're buying this one pool but let's settle all these bonds on the same day every month because that way the factor adjustments are all done together, it's easier, everyone gets it so in that case you may buy a bond that could definitely trade Tplus3, but I want to say let's do a good settle and settle it in 2 weeks. So that might be a reason where you want to do it. The practice is really aimed at TBA's which can be abused and levered and have really long debt settlement where you might have some movement. And a specified pool trade like this where you know what bond you're buying and it happens to settle in 2 weeks, it's really not that risky. So everyone in the markets annoyed by this.

Gerard Cruz: So the agreements that the clients are being asked to sign just lump that entire practice into one. Steve Weiss: Yeah, but what's happening is FINRA, I don't want to bore you with all this stuff, but FINRA who regulates brokers, sort of saw what the TMPG did and say oh yeah we think that should happen too and that threw everyone to a tizzy. So, now there's letters being written that they shouldn't get involved so basically the long end short of it is this has been talked about now for a year, we are not negotiators with MFSTA with anybody I don't think anyone has implemented anything yet it's just a lot of talk. But, ultimately it could all go away I think what likely would happen is that the market would say forget about this good settlement stuff so if it passes, everyone is going to say let's just trade everything Tplus1 or Tplus3 and the only thing that will be affected would be TBS ultimately I think. So we think that for clients who will not let us do this, for whatever reasons for statute reasons or they just don't like the sound of it, we'll be able to do what we want to do and it's really not going to affect our portfolio. So sort of long story short, it's not a big deal for us but it's something that's out there a lot right now. Gerard Cruz: Right. It is. Steve Weiss: I don't think you want to go line by line in the portfolio.

Gerard Cruz: You no longer trade a transition portfolio, right? Steve Weiss: Yeah, that's gone. Gerard Cruz: It's been a while. Steve Weiss: It's been a while. Yeah, 2 years. We're almost out of everything. We had a meeting last week actually they're still a few portfolios that have some legacy. Gerard Cruz: Assets. Steve Weiss: Yeah and that's normal course of business we get portfolios all the time when we get hired but they don't have the scary stuff in them anymore. So. Paula Blas: Only Guam gives you the scary stuff. Steve Weiss: Oh no, no we got a lot of scary stuff from a lot of people, you were just the first. Gerard Cruz: Oh we were the first? Steve Weiss: Yeah for us. I mean you guys came in the door. Gerard Cruz: Right around '08. Steve Weiss: Yeah the end of '08 is when you guys came in and. Gerard Cruz: Like 75% of our portfolio with you is transition. Steve Weiss: Yeah and then everyone was trying to figure it out and then you guys actually helped us figure it out and then we had a nice process in place and I think other clients were benefited from the work we did for you guys actually because we got a pretty good head in.

So, anyway on page 22, just a sort of round out the firm update. Like I said 35 employee shareholders now our assets are up to 41 billion. I think you guys came to us in '08, '09 we're probably closer to 15 billion so you see some decent growth but it's very balanced. So it's been some core, it's been some long, it's been some short duration, tips and treasuries. And really the one thing that we've done I think is really decided to focus on our business which is U.S. Fixed Income investment grade bonds. So, now for the past couple of years I would go around seek consultants like Maggie and other firms and I'd walk in and the consultants would say do you do bank loans? No. Do you do high yields? No. Do you do EM? No. Do you do unconstrained? No. All these no's because all we do is this and I think that probably we could have drawn more if we did all those other stuff but it would have taken us out of our comfort zone. So for us we'll just stick with what we do, we think there's a lot of opportunity in corporate pension plan, corporate pension space with liability driven investing, in the front end of the curve there's opportunity. We're about to launch some daily priced funds so not mutual funds but collective investment trust for the DC business. Right now we don't have a way to really participate in the DC business in a broad way so now we'll have some funds or if you wanted to hire us at priced every day, we can do so in a much more efficient fashion than some of the mutual funds and by efficient I also mean cheaper. So, collective investments trust because they don't have all the overhead mutual funds can price very cheaply and without all that revenue sharing stuff. So in general the firm is in great shape. I'll let you know what happens with that litigation outcome and I think that's it. Any questions?

Wilfred Leon Guerrero: Questions? Gerard Cruz: No sir. Steve Weiss: Good. Gerard Cruz: Thanks, Steve. Steve Weiss: Thank you. I sure appreciate.

Garcia Hamilton & Associates

Jeffrey Detwiler: Does everyone have a book? Paula Blas: Did you need one? Jeffrey Detwiler: Yeah if you have one. Gerard Cruz: Yeah you can have, here. Jeffrey Detwiler: Oh perfect. Maggie Ralbovsky: Talk from memory. Jeffrey Detwiler: I can talk from memory too. So I want to be respectful to everyone's time, how long did you want me to go for? Wilfred Leon Guerrero: 45 minutes but you need to answer the question first about

any regulatory agency that is after you? Jeffrey Detwiler: No issues. Wilfred Leon Guerrero: Okay, are there any changes in the organization? Jeffrey Detwiler: There are some changes. So on page 2, we have a picture of key professionals couple of the things I want to highlight, Ruby Dang who has been with the firm for since 1995, 20 years of investment experience was promoted to Director of marketing and client services and Karen Tass, who has been a fantastic addition to our team has been promoted to Portfolio Manager from analyst and she focuses on the mortgage backed security sector. Joe San Agustin: Who's the other one? David O'Brien: Tass and Dang, Dang Tass. Joe San Agustin: Two ladies. Jeffrey Detwiler: That's correct two ladies. And are there any other questions I can answer? No litigation. Wilfred Leon Guerrero: You're not getting any lawsuit from the men?

Jeffrey Detwiler: So with that lets go back to tab 1, organization. So just a little background update on the firm, again founded in 1988 so we recently celebrated our 25th anniversary. We're 100% employee owned of that 75% ownership is among women and minority partners. Deep in experienced team with a lot of experience working with each other. As of 3/31 the firm manages 3½ billion in assets, that number is probably closer to 4 billion with some recent new accounts. We manage high quality fixed income and equity strategies by client type down at the bottom pie chart, our largest is fixed income aggregate, which we manage for you by clients 71% in public funds so public space is very important to us. So going to page 2, I mentioned the recent promotions, just some pictures of who the partners are. Gilbert Garcia is the managing partner and head of fixed income. Janna Hamilton is our head of client service. Beth McWilliams our compliance officer and Kevin Lunday our chief operating officer really handle the firm day to day management. There's not been a change in the firm ownership structure since we bought ourselves back from the AMG back in 2010. From professionals myself, Nancy and Karen are PM's we're supported by deep and experienced team of investment professionals.

On page 3, recent accounts, approximately 424 million added over the past 12 months so the firm is healthy and growing. There continues to be interest in the aggregate product intermediate as well as short duration products as well. Estimates for new accounts approximately 321 million as of 3/31. Gerard Cruz: Wow. Okay. Jeffrey Detwiler: On page 4, a representative client list. 2 things I wanted to highlight here. One, the clients that are bolded in green are clients that have been with the firm for 10 plus years, so that's a sign that our firm has done a good job navigating volatile markets. Something we're extremely proud of and something we look forward to more and more of this page turning green over time. Also, the clients that have a star next to them in blue are clients that are located in the pacific region. And really I want to say a thank you very much number 1 because this has been a very long relationship with our firm and yours and the fact that we had this relationship really has been a stepping stone to additional accounts in the region, whether that be here or Saipan or Marshall Islands or the FSM so again thank you very much. Gerard Cruz: You're still in Saipan? Jeffrey Detwiler: We manage money for MPLT and Century Insurance in Saipan. Gerard Cruz: MPLT is 10 million? Jeffrey Detwiler: What we manage for them? Gerard Cruz: Yeah. Jeffrey Detwiler: We manage closer to 15. Gerard Cruz: What is Micronesia Development Bank? Jeffrey Detwiler: It's not the bank of the FSM, its Micronesia Development Bank. Gerard Cruz: Was that the former FSM Development bank? Jeffrey Detwiler: It might be. Joe San Agustin: It's an FSM bank. Jeffrey Detwiler: It's an FSM bank. Gerard Cruz: So it's a

development bank, like GEDA. It's a government sponsored bank. It's not PIDB, Pacific Island Development Bank, right. Jeffrey Detwiler: Not that I'm aware of. The name that's on the contract is FSM Development Bank. Gerard Cruz: That's like GEDA. Joe San Agustin: Not necessarily. They do guarantees. Gerard Cruz: They guarantee loans, okay. So who are your favorites? The brown or the green. Jeffrey Detwiler: Who are my favorite clients? Gerard Cruz: Yeah. Jeffrey Detwiler: Well number 1, you guys and number 2 everyone else. Gerard Cruz: This includes the time we were with you guys with the equity mandate. Jeffrey Detwiler: Correct.

On page 5, Goal and Philosophy. Joe San Agustin: I said with you guys you've lasted so long we expect you to do better. Jeffrey Detwiler: We're trying our best sir. So on page 5, Goal and Philosophy hasn't changed since day 1 of the firm. Outperform our benchmarks, net of fees, over a full market cycle using a high quality strategy with less risk and low turnover. We want to preserve principal, maintain liquidity and provide high current income.

Page 6, what we do and what we don't do? When we say high quality the only thing we purchase are Treasuries, Agency Debts, Agency Guaranteed Mortgage Back Securities and Corporate Securities Rated A or better, we concentrate on Spread Product in our portfolios to the short to intermediate part of the curve. So the aggregate index has securities from 1 to 30 years the long end of the curve beyond 10 years we will not buy spread product which means we won't buy long corporate, long agencies, we'll only buy Treasuries on the long end of the curve that's a way to contain credit risk in your portfolio. No big surprises so we won't do any foreign bonds because we don't want the currency risk, we don't do any triple B's, we don't do high yield even though triple B's are still investment grade we want to maintain a higher quality bonds in the portfolio, no derivatives or leverage of any kind. The reasons why we are different and reasons why we can outperform is we're flexible nimble firm we actively rotate sectors, we move along the yield curve, we will manage our duration to take advantage of opportunities as we see them, we have risk controls in place, we have risk controls that help us make decisions, we have risk controls that help us monitor decisions, the category of helping us make decisions we have a quantitative strategist who runs technical models which we use as a cross check to our fundamental work. So we don't blindly follow the technical models but if we see a disagreement between fundamental and technical it makes us do some extra homework to make sure we get it right. We have a software that allows us to look at our interest rate sensitivity by sectors as well it's not enough to know that you have X percent in a sector because what if those securities are short securities or 30 year securities so you need to know where your interest rate is coming from. So that concludes sort of the background on the firm.

So let's take a look at how your money has done on page 7, I have the performance numbers in the requested format you can see we began managing money for you back in September '08 average annual return for the account has been 8.1% versus the index at 5.3%, the fiscal 1 year as of September '13 obviously a very challenging environment for fixed income investors as the index was down 1.7% over that time period your account outperformed by approximately 109 basis points over that time frame, the quarter ended December 2013 again the index was negative your account was up 98 basis points, the quarter ended 3/31 we've seen a rebound in fixed income in the index up 1.8 versus your

account of 2.5 and for the month of April largely ahead of the benchmark 89 versus 84, for the month of May through yesterday's close your account is up 77 basis point which is roughly even with the index for the month of May. Joe San Agustin: Excuse me, this annualized inception to date 9-30-08 that 8.12 is as of what date? Jeffrey Detwiler: All these performance numbers are as of April 30. Wilfred Leon Guerrero: We have over a million dollars in cash, is that unusual? Jeffrey Detwiler: It's not necessarily unusual, number 1 keep in mind that at a 126 million, 1 million in cash is less than 1% and also number 2 there are monthly cash sweeps where you request money from us on a monthly basis. Wilfred Leon Guerrero: Okay. Jeffrey Detwiler: So as soon as that money comes out that percentage comes way down. On page 8, performance numbers more of a standard format so we have the 5 years, 3 years, 2 years, 1 year since inception again outperforming the benchmark over all time periods. Over the next few pages I want to talk about the market environment how we've been able to achieve this outperformance, but again I think the key take away here is that we've been achieving this using the high quality strategy with no derivatives or leverage, no high yield, no international exposure.

So on page 9, I graph the yield of the 10-year treasury because I wanted to visually show everyone basically what we've seen in interest rates over the past couple of years the Fed has been very active in the market in an attempt to keep rates low to help stimulate the economy so in late 2011 they announced open-ended asset purchases where they would purchase treasury securities and mortgage back securities. Early last year Ben Bernanke hinted about tapering that program cutting back on the bond purchases as a way to play a little defense in your portfolio going into last year the duration of our portfolio was positioned to be approximately 10% shorter than that of the benchmark duration is measured interest rate sensitivity. So, we anticipated rates rising and so we shorten the duration so we'll be less sensitive to rates rising and that's exactly what we saw. We can see from roughly May of last year to September of last year interest rates on the 10-year rose from approximately 1.7 to 3% that was really the driving force behind the negative return in bond market we saw on the previous performance page. We saw some volatility in the 4th quarter the Fed eventually announced the taper at the beginning of this year, what we saw in the bond market was extreme pessimism and when we see the herd mentality everybody moving in one direction that's usually a signal for us to move the opposite direction. So we went from a short duration in anticipation of rising rates to a neutral duration once rates had moved in our favor and now we positioned portfolio with a longer duration. As you can see from this chart from the point the Fed announced the taper toward the end of last year to now interest rates have come down we're at roughly 2.5% on the 10-year today. So again, our duration management has been a big factor on why we outperformed not only last year in a negative period but this year on a positive period.

Another reason for our outperformance has been our sector strategy and on page 10, I would like to discuss the corporate bond market so when we started managing money for you in late 2008 that was a very low liquid environment, high crisis environment a lot of concern about what's going to happen next we saw that as an opportunity. So, on this chart here we're looking at the historical spreads or additional yield you received from buying corporate bonds the red line is the corporate sector and blue line is the financial sector within the corporate bonds and during various crisis points spreads widened inverse relationship with bonds when rates go up, prices go down and so spreads are

widening that means corporate bonds are underperforming treasuries. So in 2008, we had Bear Stearns and Lehman Brothers, people who were running away from corporate bonds and towards agencies securities we started buying corporate bonds and moving into corporate bonds in a meaningful way in your portfolio.

There's been some volatility around Greece and the US treasury downgrade but generally speaking the trend has been lowered and so if we focus on the period over the past year you can see spreads have declined so we've been overweight a sector that has outperformed and that's another main reason why we have been outperforming the benchmark.

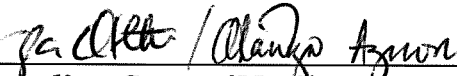
So on page 11, this is a graph of one of our technical models, this is the liquidity model versus the ISM manufacturing index. The goal of this model is not to target a particular statistics such as GDP will get to 3% or yield on a 10-year will get to 5% or anything like that. The goal of this model is just to get a sense of direction, expansion or contraction and over the year it's done a good job of helping us make decisions and helping us monitor decisions. Focusing on the period around 2006, 2007 you can see the blue line was in the contractionary period before the red line basically fell off the cliff. Our fundamental work was telling us that the opportunity in spread product was tremendous the technical work here you see the blue line pointing straight up, while the red line was pointing straight down is also telling us that the liquidity going into the system would help us recover out of this recession. So we basically had the recovery trade on in your portfolio and continue to do so you can see as the blue line has remained in the expansionary territory. So again, there is subjective as well as objective component to the work that we do for your portfolio and as the economy has recovered you see the red line has moved back to expansionary territory it has been a terrific environment for investors and corporate bonds.

So where are we positioned today on page 12, on the left hand side you have the index, on the right hand side you have your portfolio, at the bottom are some important statistics. So you see the overweight to non-treasury securities particularly 44% in corporate bonds and 41% in agencies guaranteed mortgage backed securities. In the corporate sector all of your corporates are A or better, where as with the index approximately a third of those are triple B's. The index also has approximately 2% in the asset backed sector which are lower liquidity type securities, lower quality type securities, we would not hold those securities in your portfolio. So even though we're maintaining the higher quality bias we have a higher average yield which is another reason for the outperformance again going back to our philosophy on fixed income getting that extra income will help you outperform the average yield 3% versus the index of 2.3, the average coupon 4.7 versus 3.3, average maturity largely longer, the duration as I mentioned we positioned your portfolio to be longer than the benchmark going into this year in adjacent of a declining rate which has worked out well. So before I lose my voice let me just open up for any questions. I will also add that looking forward in the next train we are starting to trim some of the credit risk in your portfolio as we've been in this recovery for an extended period of time, we're probably in the later stages of the economic recovery. Gerard Cruz: Alright.

Maggie Ralbovsky: So with the interest rate gone up are you still comfortable with longer duration, I mean went down. Jeffrey Detwiler: Interest rates have already moved in our favor this year by 50 basis points, we believe that rates will remain range bound and

probably sideways to a little bit lower. Could they go from 2½ about to 2 and quarter I think that's very possible if interest rates on the 10-year got below 2% that will probably be a signal for us to start shortening our duration again. When you have a longer duration and it's an upward sloping yield curve you're getting extra income for being longer, so if rates move sideways after getting extra income it's a good thing, if rates continue to go lower the fact that you're longer duration it's a good thing. Even if rates marginally go up the fact that you're getting that extra income there's a break even before rates rise and hurt you. So, really in 2½ out of 3 scenarios having a longer duration does benefit the portfolio. Gerard Cruz: Good. Wilfred Leon Guerrero: Good. If Gerry is satisfied then we're okay. Jeffrey Detwiler: Well perfect, thank you. Wilfred Leon Guerrero: If Gerry says it's good, it's good. Jeffrey Detwiler: Just for your reference if you need it my card is in the back as well as an announcement that we were named the Investment Grade Manager of the Year by Institutional Investor. Gerard Cruz: Congratulations. Jeffrey Detwiler: Thank you so much.

Respectfully submitted,


Angelina Castro/Marilyn Aguon
Recording Secretary

Affirmed:


WILFRED P. LEON GUERRERO, Ed.D.
Investment Committee Chairman