Old Saybrook Pension and Benefits Board Meeting
Thursday, February 22, 2024
8:30 a.m.
First-floor Conference Room, Town Hall – Hybrid Meeting
To access the audio from this meeting, please use the following link:
https://youtu.be/4Pmx3QuwCEo

Meeting Minutes

Attendees

Members Present:	**Others Present:**
Carl Fortuna, First Selectman	Lee Ann Palladino, Finance Director & Pension Plan Administrator
Susan Quish	Janet Vinciguerra, Pension Board Liaison
Rowena Moffett	Kevin Nichols, Morgan Stanley Investment Advisor
Paul Tracey	Andrea Brundrett, Administrator
Loraine Cortese-Costa	Barbara Labriola, Town Treasurer
Leland Mckenna	

Absent:

Darrell Pataska

Welcome and Public Comment

The meeting was called to order at 8:30 a.m. by Mr. Fortuna. No members of the public were present. Mr. Fortuna welcomed Mr. Mckenna to the board. Mr. Mckenna is the Vice President of Planning and External Affairs at Middlesex Health and was also involved with the Chamber of Commerce Board of Directors and is a volunteer coach through the Park and Recreation Commission.

Approval of the Minutes

The minutes of the January 25th, 2024, meeting of the board were reviewed. A motion was made by Mr. Fortuna and seconded by Ms. Moffett to approve the minutes. The motion passed unanimously.

Pension Liaison Report

Ms. Vinciguerra reported that for the February pension gross payroll the town had 98 retirees with a gross monthly payroll of $155,724.21, with one less retiree due to Mr. Peterson's passing on 1/11/24. There is a total of 99 participants with one QDRO spouse. The Fire Department has 37 retirees for a gross monthly payroll of $14,107.62, with one less retiree due to Mr. Peterson's passing. There is a total of 38 participants with one QDRO spouse.

Pending retirements include Julie Pendleton, Director of Operations, Facilities & Finance at the BOE, who retired on February 1, 2024. She will be added to the March 1st pension payroll and will receive two monthly benefits. There are no other pending retirements at this time.

As of February 16th, 2024 the defined benefit plan has 46 contributing town employees and 21 contributing BOE employees. The defined contribution plan has 43 town employees and 21 BOE employees. 83% of DC participants elected the optional town match. Mr. Tracey noticed the percentage of DC participants electing the additional match has gone from 90% to 83%. He asked if it would be necessary for Mr. Nichols to reach out to those participants who are not electing the additional match, as Mr. Nichols has done in the past. Mr. Nichols said he can reach out to those participants not electing the additional match to request meetings and discuss the importance of the additional match. Ms. Vinciguerra said she would be able to provide Mr. Nichols with a list of the people not electing the additional match.

Investment Advisor Report – Morgan Stanley

Mr. Nichols started by reviewing the Wealth Management Perspectives. Referring to the Executive Summary he wanted to point out the Major Investment Controversies. Under terminal policy rates, Morgan Stanley believes that higher for longer means lower valuation multiples. He explained that while the general investing public feels the Federal Reserve is going to start cutting rates because they've done a good job with inflation, Mr. Nichols said the Feds incentive to cut rates is very low right now. This is because if they start cutting rates, that would be inflationary. When referencing the "Magnificent Seven", Mr. Nichols said that earnings have increased over 20 times since 2016 and stocks have increased over 70 times their value. He continued that Wall Street sees this growth trajectory continuing when historically, they tend to level off. They may continue growing but not at the rate we've been seeing. Mr. Nichols then referenced the Yielding Extreme Concentration and Risks for the Index graph, which he said is greater than it's been at 33%. This is referring to the S&P Index, top 10 shares of the total market cap. He continued, the Fed Funds Futures implied rate for 2025 is 3.6% which implies about 6 or 7 rate cuts. Morgan Stanley believes it will be 2 rate cuts, with unemployment being very low even with layoffs at tech companies and financial companies. Mr. Fortuna asked, with the commercial real estate market refinancing and everything coming due within the next 3 to 4 years, what would the Fed Funds interest rate have to be for it not to be considered a crisis. Mr. Nichols said he couldn't speak on behalf of commercial real estate but in terms of community banks, any rate cut would make a difference based on the amount of interest they pay in deposits and the margin they are getting on their loan books right now. He continued, with interest rates where they are, the volume of residential and commercial loan transactions is very low. In terms of commercial real estate, the valuation and the transaction value that's happening is much lower than residential real estate. The biggest issue for commercial real estate is gaining tenants. If they are unable to occupy a building at the capacity needed to cover their loan, which is around 5%, they may be forced to sell at a lower value than they bought at. Ms. Cortese-Costa asked how much exposure is in the Town of Old Saybrook's portfolio. Mr. Nichols said minimal exposure with the small-cap and mid-cap managers not having a lot of financial exposure.

Mr. Nichols then went over earning multiples, saying that the bullish consensus sees the S&P 500 Index earnings ratio being at $5,250 over the next 12 months. Morgan Stanley believes it will be around $4,500 because bonds are offering a higher yield right now than stocks in terms of equity risk premium. They are expecting earnings growth in the next few years but it is below consensus right now with higher interest costs not having effected the S&P 500 companies yet, since they haven't had to refinance. With the maturity walls coming due in 2025 it depends on what the Federal Reserve does with interest rates.

Mr. Nichols then reviewed the report for the town pension which for the fiscal year quarter's end is up 5.44% for return. As of February 21st, 2024 return is up 6.71%. The portfolio is up 1.21% for February versus the 6.40 which is up 1%. When referring to the Time Weighted Performance Summary, Mr. Nichols showed that the portfolio is underweight in cash and US Large Cap. The portfolio was overweight in US Mid Cap and US Small Cap but those were reduced to get under the maximum value. Mr. Nichols said the portfolio is a little overweight in short-term bonds relative to intermediate bonds which is a shift that was discussed being made at a previous meeting. He said the portfolio would want to remain in short-term bonds until interest rates on the 10-year bonds starts to rise, possibly to 4.75%. Mr. Tracey mentioned that at the last meeting they discussed the asset allocation to value and asked if any adjustments were made after that discussion. Mr. Nichols said yes, they did move funds from the S&P 500 to Aristotle because they are seeing the most risk in the S&P 500. This move creates less risk in the portfolio. Mr. Tracey added that funds could be moved to the equal weight S&P 500 which Mr. Nichols agreed with.

Mr. Nichols went over the Time Weighted Performance Detail, saying for the fiscal year, the equity managers are doing well. The top advisor is up 11.87% vs the 10.74% benchmark; and being in the short-term corporate bond ladder which is up 2.94%, has been more beneficial than the intermediate maturity bonds which is at 1.79%. He continued that US Small Cap has been a top performer as well as the S&P 500. US Mid Cap did not do as well and although Emerging Markets beat the benchmark, they were still down. For February, Emerging Markets is up 4.6% and is the best performing manager in the month of February and inflows into Emerging Market equities were the highest they've ever been on record. In regards to the projected income for the portfolio for the next 12 months, the summary shows a total of $706,910. Ms. Labriola said she reported on this to the Board of Finance and the Chairman of the Board asked if they could have a reference to what the projected income was for the last 12 months. Mr. Nichols said he would be able to get that to her. Mr. Tracey added that US Mid Cap seems to lag quite often and asked if we have the right manager. Mr. Nichols said the manager is very conservative and value oriented which has not been beneficial to them. They did very well in 2022 but beyond that they have been lagging in the upward market. This is something they will be reviewing and seeing if there is a better core manager.

Mr. Nichols then went over Morgan Stanley's investment philosophy for Mr. Mckenna with this having been his first meeting. Their goal is diversification and lower volatility as well as cash flow to provide income, so regardless of what's going on in the market the pensioner's benefit payments can continue to be made. Mr. Mckenna asked how frequently the allocations are changed in an average year. Mr. Nichols explained that there is a very specific investment policy so sometimes adjustments are made to adhere to the ranges in the policy, it depends on changes in the market. He added for example, funds were moved into fixed income from equities based on the market during the pandemic. Mr. Fortuna added that the Town's IPS minimum and maximum are on page 7 and page 10 shows the managers for various sectors. Ms. Palladino added that the allocation is reviewed every 5 years with Morgan Stanley having full discretion to stay within those ranges.

Plan Administrator's Report

Ms. Palladino reported that at the Board of Finance meeting our auditors, Mahoney Sabol, presented the financial reports for fiscal year 2023. They discussed long-term liabilities and pension for the Fire Department and the Town as well as OPEB obligations. The liabilities did decline due to full funding of both plans, higher interest rate, and demographic changes. Becky Sielmann will be attending our March meeting and will go over those details. The auditors added that overall, we are on a strong path in regards to our long-term liabilities. Ms. Palladino also reported that we are in the midst of our budget process and so far, the ADC has been fully budgeted. The Board of Finance will be reviewing the budget next. Lastly, for the April meeting the Cash Flow Review by Morgan Stanley will take place. Milliman will then give their actuary report and go over the variables that will influence the amount set aside for employer contributions. Ms. Palladino added the Annual Policy Review is typically done after the Cash Flow Review so if there are any questions the board members have that they would like looked into in terms of policy, to let Ms. Palladino and Mr. Nichols know. At this time there are no suggestions for change.

Mr. Fortuna said that two years ago the Actuarily Defined Contribution was not being fully funded but it is now. With the amount of money required to fund the ADC trending down, there is a surplus. Instead of moving those savings, Mr. Fortuna advises leaving those funds in the ADC fund. With larger retirements coming up and the market doing well Mr. Fortuna doesn't see a need to move these savings out of the ADC at this time. Mr. Mckenna asked when the market is doing well, does that change any policy spending in a budget cycle and also because of the market doing well is that why there hasn't been a need to make the full contribution or are there other variables. Mr. Fortuna answered that the contribution amount had been increasing for years until the amount that the actuary recommended the ADC being at was reached. He added ultimately it wasn't because the market was doing well, the ADC was being fully funded regardless. In regards to Mr. Mckenna's first question, Mr. Fortuna said the Town's rainy-day fund is at 17%, which is a Board of Finance policy versus the State's policy of 15%. The ADC is being made, even though the pension is 85% funded. In addition, the discount rate has been lowered from 7.75% to 6.75% and the actuary is not recommending any changes. Ms. Palladino added that the difference between the State and the Town is that the Town fully funds their obligations without having to rely on surplus. Mr. Fortuna added that in 2006 the Town's pension was funded at 115% which decreased to 65% in 2008. With there being a lot of catching up needed since that time, the actuary is recommending the amount that needs to be budgeted to be fully funded. Ms. Palladino added that there is a $315,000 pension reserve if needed. Mr. Fortuna continued that some of our OPEB benefits are larger and "pay as you go" including health insurance for retirees. That obligations costs about $300,000 per year. Ms. Palladino added that other post-employment benefits will be declining because they have closed down the ability to have health insurance if an employee was hired after a certain point. Life insurance is still offered to employees. Mr. Mckenna said Middlesex Hospital was the same in regards to transitioning everyone off a Defined Benefit plan. He added that he looks forward to having discussion about the health insurance aspect since he is uniquely positioned to speak on the matter and what they see happening with trends.

Old Business

No old business

New Business

The March meeting will be held in the second-floor conference room and held virtually due to early voting.

Mr. Fortuna made a **motion** to adjourn seconded by Mr. Tracey, all were in favor and the meeting adjourned at 9:19 a.m.

Respectfully submitted,

Andrea Brundrett, Recording Secretary

The next meeting will be Thursday, March 28, 2024, at 8:30 a.m. by hybrid meeting format in the Town Hall, second-floor conference room.