

**GEOLOGICAL SOCIETY OF AMERICA**  
**REPORT OF THE INVESTMENTS COMMITTEE CHAIR**  
**Fiscal Year 2010 (1 July 2009 – 30 June 2010)**

The GSA Investments Committee is charged with investing and monitoring the performance of a diversified portfolio of stocks, bonds, and alternative investments that nurture the strategic goals of the Society and the Foundation. All of GSA’s equities are in mutual funds, selected on the basis of long-term records of reward versus risk, in consultation with our financial advisor, *Innovest Portfolio Solutions* in Denver. The GSA portfolio is currently modeled to provide a long-term rate of return equal to the consumer price index (basically inflation) plus 5.0%, at acceptable levels of risk.

**Performance of the Investment Portfolio during FY 2010**

After the adverse global economic situation and resulting severe declines in investment returns during the 2009 fiscal year, FY 2010 saw substantial partial recovery, especially during the initial three quarters. As of 30 June 2010, the value of the portfolio, which includes funds of both GSA and the GSA Foundation, totaled \$28,816,080 as recorded by our financial advisor, *Innovest Portfolio Solutions*, up from \$24,983,862 at end of the prior year. With adjustments, for capital increases (mainly bequests to GSAF) and draws for Society activities, the overall investment portfolio return was a positive 13.9% in fiscal year 2010 (in comparison, Harvard University gained 11% in FY2010 on its large endowment).

This year-end result for GSA includes significant losses during the difficult final quarter of the fiscal year; at end of March, the FY2010 investment gain had been about 21%. The broad diversity of the GSA portfolio was beneficial, and the portfolio continued to outperform its custom index benchmark in these challenging times (see Table 1), showing the benefits of active investment management.

**Table 1: GSA Investment returns**

	<u>One year</u>	<u>Last 3 years</u>	<u>Last 5 years</u>	<u>Last 15 years*</u>
GSA Fund	13.9%	(4.6%)	2.8%	7.3%
Custom Index	13.5%	(6.8%)	1.0%	6.5 %
CPI + 5.0%	6.0%	6.5%	7.3%	7.4 %

\* Since inception of guidance by *Innovest Portfolio Solutions*

**Current Investment-Asset Classes and Allocations**

In the spring of 2009, in response to the difficult investment environment encountered during the year, the Investments Committee requested, and GSA Council approved, revised guidelines to provide the Investment Committee with authority more expeditiously to adjust strategic allocations of individual asset classes within limits specified for macro asset-class groups (see table below), in collaboration with the recommendations of our investment consultant. The purpose was to increase flexibility to conserve and grow investment assets during times of economic uncertainty.

An initial outcome was modestly to increase the overall fixed-income component of the portfolio to reduce risk in an unsettled investment environment. During FY2010, positions in

large-cap equity were modestly reduced, while mid-small cap equities were enlarged. Late during the fiscal year, acting on advice from *Innovest*, the Investment Committee recommended to that a modest position be added in “Direct Real-estate Investments;” this recommendation was approved by Council in April 2010, but the investment change was not made until early July, and thus is not listed below.

**Table 2. Asset-Class Allocations and Limits, as of 30 June 2010**

Macro Asset-Class Group <u>Asset Class</u>	Lower limit	Upper limit	Actual Year-end
Equity Funds	40	65	53.9
Domestic large cap equity			28.4
Domestic mid-small cap equity			11.7
International equity			13.8
Fixed income & cash-equivalents	15	35	24.6
Core fixed income			13.3
High-yield bond funds			5.2
Bank-loan funds			6.1
Alternative investments	10	30	21.5
Absolute return (hedge fund-of-funds)			12.2
Commodity funds			4.9
Private-equity funds			4.4
Real-estate investments			0

### **Pooled Income Fund**

The Investments Committee also oversees a Pooled Income Fund, which is part of the GSA Foundation. Donors make a cash contribution to the Foundation and receive quarterly cash payments of the interest income (currently goal is CPI plus 3%) until death, at which time the original donation becomes part of the regular investment portfolio of the Foundation. Accordingly, the primary investment goal aims to optimize direct income (interest, dividends) relative to capital gains, which are not distributed to the donors. As of 6/30/10, the Pooled Income Fund consisted of a broadly invested bond fund (90.8%), a real- estate investment trust index fund (7.7%), and cash (1.5%).

Last year the Pooled Income Fund had a total income of 13.7%, which was 9.6% greater than the goal of CPI plus 3 %. A substantial part of the income was in capital gains, and thus greater than the dividend and interest income that is returned to donors. This result, almost the same as that of the more broadly diversified GSA investment portfolio, reflects the strong bond market during the year and the appropriate fund focus on fixed-income securities that yield a reliable income flow for the donors.

### **Revision of the *Investment Portfolio White Paper*:**

A major committee effort this past year was preparing a revised draft of the Society’s *Investment Portfolio White Paper* on the size, performance, and draw policy of the portfolio. The current Strategic Plan of the Society charged the Investment Committee to provide “periodical (annually or biennially) review of the *Investment White Paper* to conform to GSA’s vision, mission and goals.” The original *White Paper*, prepared in February 2005, was intended

to provide guidance for future Society draws for strategic spending in relation to the size of the Society's portion of the investment portfolio. Such review seemed particularly timely and appropriate in the currently challenging times, was undertaken by the Investment Committee during FY2010, and approved by Council at its April 2010 meeting.

The revised *White Paper* addresses: 1) the purpose of having a GSA investment portfolio, 2) minimum optimal investment balances, and 3) how the Pardee bequest received in 1993 should be valued in relation to Council resolutions. It additionally summarizes interpretations of Council mandates concerning strategic spending draws from the GSA investments, briefly reviews GSA activities and other events affecting the investment portfolio during the past five years, proposes revisions in response to changed accounting and audit requirements, and suggests a few additions to the recommendations that were in the 2005 *White Paper*. In particular, the revised *White Paper* recommends that future draws for strategic initiatives from unrestricted investment funds be reduced to a maximum of 4% (from 5% previously), in response to the continuing difficult investment environment and resulting decline in constant-dollar value of the investment portfolio since approval of the initial *White Paper* on these topics in 2005 (see Table 3).

### **Changes to the “Investment Policy for the Investment Portfolio**

The Investment Committee also recommended two specific changes to the Investment Policy, both approved by Council at its spring meeting:

a. **Modify Investment Performance Objectives** to state that “*The investment objective is a long-term rate of return on assets that is at least 5.0% greater than the rate of inflation as measured by the CPI.*” This represents a reduction from 5.5% (0.5%) that is recommended by the Committee and our investment advisor (Innovest), in light of projected slow economic recovery and difficult investment environment during at least the next several years.

b. **Slightly modify an existing allowable asset class**, changing the present “*Real-estate investment trust funds*” to “*Real-estate investment funds.*” This small change permits better diversification of the investment portfolio, taking advantage of broader opportunities than the existing asset listing permits, in accord with recommendations from our investment advisors.

Concurrently, the Committee agreed to undertake more comprehensive review during the coming year of the *GSA Investment Policy*, which was last fully updated in 2003.

### **Continuing Issues and Potential Concerns**

The difficulties encountered for the GSA portfolio in attempting to meet the CPI+5.0% target for investment returns in the most recent three- and five-year time periods (Table 1) underline significant current and future challenges, addressed in part by recommendations in the revised *Investment Portfolio White Paper*.

**Potential for decreased investment returns in coming years:** Many economists and financial advisors are concerned that recovery from the recent “great recession” may be more prolonged in timing and less robust than previous recessions in recent decades because of the exceptional levels of accumulated debt in the financial sector, heavy government borrowing, high unemployment, continuing distressed real-estate markets, and increased global competition—especially from the so-called “developing economies.” Such outlooks further underline the challenges and uncertainties in achieving our long-term investment-return goals at acceptable levels of risk, even though reduced by Council this past year from 5.5%+CPI to 5.0+CPI. Any sustained continued failure to achieve targeted investment returns could, of course, have significant impacts on spending draws by the Society.

**Preserving inflation-adjusted investment values for the Society:** A related concern has been how to maintain the inflation-adjusted purchasing power of the Society’s investments in coming years. As of the end of FY2010, as a consequence of the declines in investment value and concurrent spending draws during the past ten years, the inflation-adjusted (“constant-dollar”) investment value of the Society’s portion was substantially below that at the time of the 2005 *Investment Portfolio White Paper* (see Table 3). In addition, the Society’s unrestricted assets in the portfolio continued to remain below the minimum reserve amount mandated to be maintained by Council in the *Investment White Paper* (an amount equal to the current-year operating budget) before draws can be made for strategic spending. In contrast, the GSAF portion has grown steadily, reflecting both more limited draws, added funds from bequests, and investment gains.

**Table 3. GSA Investment Portfolio Balances, 2000-2010**

Period ending:	GSA portion	GSAF portion	Grand Total	Percentages		CPI	Yr CPI%	Society only
				GSA	GSAF			CPI-adjust (constant \$)
6/30/10	19,446,288	9,369,792	28,816,080	67.48%	32.52%	218.0	0.9%	15,121,143
12/31/09	20,115,082	9,416,949	29,532,031	68.11%	31.89%	216.0	0.1%	15,929,947
6/30/09	17,296,931	7,686,931	24,983,862	69.23%	30.77%	215.7	2.6%	13,133,952
12/31/08	16,762,247	6,649,188	23,411,435	71.60%	28.40%	210.2	0.1%	12,942,925
12/31/07	26,173,958	7,373,390	33,547,348	78.02%	21.98%	210.0	4.1%	22,366,963
12/31/06	24,381,362	6,595,579	30,976,941	78.71%	21.29%	201.8	2.5%	21,483,232
12/31/05	22,139,506	5,784,057	27,923,563	79.29%	20.71%	196.8	3.4%	19,787,190
<b>12/31/2004*</b>	<b>21,344,918</b>	<b>4,863,221</b>	<b>26,208,139</b>	<b>81.44%</b>	<b>18.56%</b>	<b>190.3</b>	<b>3.3%</b>	<b>19,668,465</b>
12/31/03	19,320,372	4,382,063	23,702,435	81.51%	18.49%	184.3	1.9%	18,284,238
12/31/02	16,666,802	3,550,051	20,216,853	82.44%	17.56%	180.9	2.4%	15,974,319
12/31/01	20,470,228	4,037,352	24,507,580	83.53%	16.47%	176.7	1.6%	20,157,440
12/31/00	25,880,125	4,547,493	30,427,618	85.05%	14.95%	174.0	--	25,880,125

\* Reference time frame, initial (2005) White Paper

### Activities of the Investment Committee during FY 2009

The Investments Committee meets four or more times a year to review the financial and operational performance of the portfolio, consider the recommendations from our investment consultants, and consider updates and changes to the investment portfolio. In prior years the committee met at least two times in person, but during FY 2010, the committee began holding its formal meetings by web-based (GoToMeeting) conference calls in order to reduce costs (some out-of-state committee members attended a February meeting in Boulder, at personal expense). Lipman completed his term as chair of the Investment Committee, and in its May meeting, the committee appointed Carl Fricke as incoming chair for FY2011.

Investment Committee members (during FY2010): Peter Lipman (chair), Bruce Clark, Carl Fricke (GSAF representative), Jack Hess (GSA Executive Director, *ex officio, non-voting*), Murray Hitzman (current GSA Councilor), Heidi Natel, Jon Price (GSA Treasurer), Cindy Stewart, Honey Tarrall, and Thayer Tutt Jr.

Respectfully submitted,  
Peter Lipman, Committee Chair