

**GEOLOGICAL SOCIETY OF AMERICA
REPORT OF THE INVESTMENTS COMMITTEE CHAIR
Fiscal Year 2009 (July 1, 2008 – June 30, 2009)**

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 5.5%, at acceptable levels of risk.

Performance of the Investment Portfolio during FY 2009

As we are all too painfully aware, the 2009 fiscal year coincided with the most adverse global economic situation and resulting severe declines in investment returns in the past 75 years. As of June 30, 2009, the value of the portfolio, which includes funds of both GSA and the GSA Foundation, totaled \$24,939,876 as recorded by our financial advisor, *Innovest Portfolio Solutions*, and was down from \$32,291,139 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 negative 22.2% in fiscal year 2009.

This year-end result includes significant recovery during the final quarter of the fiscal year; at end of March, the loss had been almost 34%. Despite the broad diversify of the portfolio, declines were experienced in almost every market segment. The GSA portfolio did outperform its custom index benchmark in this difficult period, as it has consistently through time (see table), showing the benefits of active investment management. Although the 22% loss far exceeded the portfolio's modeled risk at 95% probability (2 s.d.), as earth scientists we should be familiar with the potentially severe impacts of infrequent catastrophic events relative to more steady-state processes. And performance of our diversified investments, though hardly desirable, was significantly better than that of some other highly regarded investment funds: e.g., Harvard's endowment is reported to have declined 27.3% in the same interval, and Yale was down 30% (*NY Times*, 9/11/09).

	<u>One year</u>	<u>Last 3 years</u>	<u>Last 5 years</u>	<u>Last 14 years*</u>
GSA Fund	(22.2%)	(3.4%)	2.0%	6.8%
Custom Index	(23.8%)	(6.0%)	0.0%	6.1 %
CPI + 5.5%	4.1%	7.6%	8.1%	8.0 %

* Since inception of guidance by *Innovest Portfolio Solutions*

Revised Investment-Asset Classes and Allocations

In the spring of 2009, in response to the challenging 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 Council also approved the Investment Committee's request to add *High-Yield Bonds* as an asset class. The purpose was to increase flexibility to conserve and grow investment assets during times of economic uncertainty. An initial outcome has been modestly to increase the overall fixed-income component of the portfolio to reduce risk in an unsettled investment environment.

Asset-Class Allocations and Limits, as of 6/30/09

<u>Macro Asset-Class Group</u> <u>Asset Class</u>	<u>Lower limit</u>	<u>Upper limit</u>	<u>Actual</u> <u>Year-end</u>
Equity Funds	40	65	61.0
Domestic large cap equity			39.8
Domestic mid-small cap equity			6.4
International equity			14.8
Fixed income & cash-equivalents	15	35	17.7 [#]
Core fixed income			8.9
High-yield bond funds			0 [#]
Bank-loan funds			8.7
Alternative investments	10	30	21.3
Absolute return (hedge fund-of-funds)			12.9
Commodity funds			4.8
Private-equity funds			3.6
Real-estate investment trust funds			0

Increased by 5%, in July 2009

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. As of 6/30/09, 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 returned 6.4%, which was almost 5% greater

than the goal of CPI plus 3 %. This result, far better than that of the GSA investment portfolio, reflects the appropriate fund focus on fixed-income securities that yield a reliable income flow for the donors.

Upcoming Issues and Potential Concerns

The GSA portfolio losses during FY 2009, coupled with mixed success in meeting the CPI+5.5% target for investment returns in recent years, raise some potentially challenging issues:

Potential for decreased investment returns in coming years: Many economists and financial advisors are concerned that recovery from the current “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 current investment-return goals (5.5% + CPI) at acceptable levels of risk. In coming months, the Investment Committee will be exploring, in collaboration with our advisors from *Innovest Portfolio Solutions*, whether the current goal remains appropriate. Any reduction in targeted investment returns could, of course, have impacts on spending draws by the Society.

Preserving inflation-adjusted investment values for the Society: A related concern is how to maintain the inflation-adjusted purchasing power of our investments in coming years, especially for the Society’s portion of the portfolio. To some degree, reporting for the combined investment portfolio of the Society and the Foundation may provide an incomplete understanding of the Society’s portion of these assets.

During the past decade, the Foundation’s portion of the portfolio has had healthy growth in dollars and in percentage of the total, despite weathering two recessions, from about \$4.6 M (~17% of total portfolio) at end of FY2001, to \$7.7M (30.8%) at end of FY2009, largely reflecting addition of several sizable bequests. In contrast, the Society’s portion of the portfolio has declined, both in numerical dollars (reflecting draws for strategic and operational spending, in conjunction with limited investment returns as noted above), and in percentage of the total portfolio (understandably, because new contributions are encouraged to go to GSAF).

As of the end of FY2009, as a consequence of the declines in investment value and concurrent sizable spending draws in recent years, the Society’s unrestricted portion of the portfolio was several million dollars below the minimum reserve amount mandated to be maintained by Council in the 2005 *Investment Portfolio White Paper* (an amount equal to the current-year operating budget) before draws can be made for strategic spending. Unless the national economy and investment environment recover robustly, as previously observed by the Investment Committee Chair John Costa in last year’s

report, "the Society may have to tighten its belt for a while and rely less on draws from the investment portfolio for continuing support and new initiatives."

Committee review of *Investment Portfolio White Paper* and *GSA Investment Policy*:
The current Strategic Plan of the Society charges 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 *White Paper*, prepared in 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 seems particularly timely and appropriate in the currently challenging times, and will be undertaken by the Investment Committee during FY2010, with intent to report to Council at its Spring 2010 meeting. Concurrently, the Committee will also review the *GSA Investment Policy*, which was last updated in 2003.

Activities of the Investment Committee during FY 2009

The Investments Committee meets four or more times a year (at least twice in person) 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. During FY 2009, the committee held four formal meetings and several additional telephone conference calls in connection with the difficult investment situation. The chair of the Investment Committee, John Costa, resigned in March 2009 for personal reasons, and in its May meeting, the committee appointed Peter Lipman as chair for the interval through 30 June 2010.

Investment Committee members (as of July 1, 2009): Peter Lipman (chair), Bruce Clark, Carl Fricke (GSAF representative), Jack Hess (GSA Executive Director), Murray Hitzman (new member, and current GSA Councilor), Heidi Natel, Jon Price (GSA Treasurer), Cindy Stewart (new member), Honey Tarrall, and Thayer Tutt Jr.

Respectfully submitted,
Peter Lipman, Committee Chair