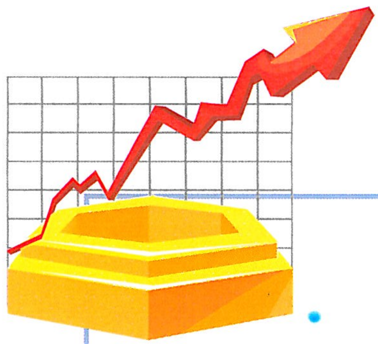
2012 - 13 ET #6.3
2012 - 13 Council #16.0
2012 - 13 EBD #13.2
(2012 – 13 Midwinter Meeting)



Endowment Trustees
Report to Council/Executive Board

- Membership Information Session -

John Vitali – Senior Trustee

Saturday – January 26, 2013

ALA Endowment Trustees
Report to Council
Saturday - June 26, 2013
Seattle, WA

This report provides information regarding the performance of the ALA Long Term Investment Fund (LTI) aka the Endowment. It is provided as a supplement to the oral report given by the Senior Trustee of the ALA Endowment Trustees. Specific items will include information on the general condition of the financial markets, the performance of the fund, its individual portfolio managers and other issues that impact the Endowment fund that are viewed as important to the membership. This report will be placed on the Treasurer's web page after this Midwinter Meeting.

Attachments

Attached for your review are charts (Exhibits 1- 8) detailing issues impacting the general market, the value of the portfolio, world market performance, manager performance & allocation and other pertinent information related to the management of the Endowment Fund.

Endowment Fund Performance

The Investing Environment in 2012 – as noted in previous reports the first quarter of 2012 was very similar to the first quarter of 2011 – where the results were good and things looked promising for the remainder of the year. This is evidenced by the fact that the endowment realized a return of 7% and gain of $2.1 million.

Since the first quarter the portfolio was once again impacted by a number of factors that came into focus in the minds of investors:

- Continued European Sovereign/Bank Debt Issues
- Recessionary Induced Austerity in Europe
- Year-End U.S. Fiscal/Debt Issues
- Slowing Growth in the Pacific Rim

As these issues and others – see exhibit #2 - came into focus after the first quarter, investors reacted quite negatively as is their tendency to do to any bad news i.e. over reaction.

As uncertainty and any bad news continued to take hold throughout the year, the markets reacted with extreme volatility. Investors in turn reacted as they typically do by abandoning equities and plowing funds into fixed income. This was done with the mind-set that the U.S. is still a safe haven – where the money flows - in times of trouble and uncertainty. As such, the dollar strengthened against most of the world's currencies and U.S. treasuries saw their rates falter. Seeking higher yields investors began to look at riskier asset classes and move up the risk curve.

Performance - The Trustees can report that the value of the endowment for the calendar year ending 12-31-12 was $32.6 million. This represents an increase in value of $2.3 million and a return of 10.5%, which compares to its benchmark of 12.1%. As we can see from exhibits 5-6, the results from the individual managers were positive. Although the results were positive, half of the managers underperformed their respective benchmarks. This of course is not the ideal situation as all the managers strive to meet or exceed their benchmarks. We do take solace in the fact this is one moment in time and that on a 3 and 5 years basis the results are much more favorable.

Currently there are two managers that are on our watch list – NFJ/Alliance and the Endowment Fund. NFJ/Alliance is our small cap manager who has served the portfolio for a number of years. However, performance over the last year has significantly underperformed its benchmark. The Trustees will be conducting a thorough review of NFJ/Alliance at its February meeting. Although the Trustees have made quick decisions on making manager changes due to poor performance, the general practice is allow for a full market cycle (3 years) to adequately judge a manager's performance. In many cases a good manager will have a down period but make up the loss in future performances. On the other hand the Endowment Fund (alternatives) has seen its performance negatively impacted by large redemptions by investors. To address this problem the Endowment Fund management has restricted the size of future redemptions for the foreseeable future – four quarters. It was management's belief that this action was necessary to protect the investors who remained in the fund. It should also be noted that hedge funds as an asset class has underperformed other asset classes for each of the last four years. This is the longest period of underperformance since 1998.

While the equity managers realized mixed results in their performance against their benchmarks, the fixed income managers held up much better. All the fixed income managers outperformed their benchmarks, particularly the Global Bond manager. Despite this stellar performance in 2012, efforts to keep interest rates low will likely minimize big fixed income returns ion 2013.

Outlook 2013

The 2012 Presidential election is over, the US economy is recovering more slowly than most would like and both the US and Euro zone still need to address their debt/spending issues. The expectation is for economic GDP growth in the US of only 2.0%. The world's central banks are on course to continue their efforts to provide liquidity by providing large amounts of money into the financial markets. This is all designed to keep interest rates at near record low levels, stimulate consumer demand and spending and move investors into equities.

Growth (returns) in the endowment is dependent on investor expectations for increasing equity valuations coupled with the health of the economy (growing). Current expectations are that the economy with be negatively impacted by the ongoing discussions and expected outcomes on deficit reduction spending cuts being negotiated in Congress.

Asset Allocation Changes

The Trustees are still strong advocates of the idea that asset allocation is the key to generating excess returns in the portfolio, while at the same time provide opportunities to protect the corpus. After a critical review of the markets in the spring, it was clear to the Trustees and their investment advisor that certain realities have not yet been fully priced into the market and would eventually drive returns lower. As a result the Trustees made an asset allocation change designed to help address the concerns regarding the impending year-end fiscal issues. The Trustees took the action of reducing[1] the portfolio's exposure to real assets (4.4%), which contains commodities and other hard assets and allocated those dollars to the corporate fixed income manager. This changed was defensive in nature as it offered a slightly higher return offered by corporate bonds and protection against an unsuccessful resolution to the "Fiscal Cliff" issue. Although the issues

[1] Closed out

received a good deal of attention from Congress, partisan brinksmanship took things to the very limit. As a result only a portion of the issues were addressed – expiring taxes. The more difficult deficit reducing spending cuts have received another reprieve till the end of March. The Trustees will continue to monitor the situation and the strength of the economy before further adjustments to the asset allocation in the portfolio are made.

The Trustees still remain confident that the portfolio is still well positioned to thrive in the current financial environment, which should to protect the corpus and still add value to the portfolio. Changes to the portfolio will be made as circumstances dictate.

Payout Recommendation

Each year the Trustees review the conditions for establishing the spending/payout rate from the endowment. This past Spring the Trustees recommended to the Executive Board a payout rate for FY13 of 4%, the same as in FY12. As we constantly monitoring market conditions and working with management the Trustees are now recommending and increase in the payout rate for FY13 to 5%. The change in the rate will increase the amount available for scholarships, awards, program support and general operations from $1.3 million to $1.6 million or an additional $277,414.

The rational for the change follows the “Best” practice of utilizing a higher payout rate during lean times in the market in order to maintain a certain level of support and a lower rate during good times to replenish/build up assets. Additionally, it is within the operating guidelines of the Trustees to recommend such a change if conditions are warranted.

Acknowledgements

On behalf of the Trustees I would like to thank the ALA Finance staff who assists the Endowment Trustees in carrying out our duties. We continue to be especially well served by Greg Calloway, Keith Brown and Elaine Klimek of the ALA financial staff. They have been very dependable, reliable and thorough in assisting the Trustees in our financial oversight responsibilities.

Respectfully submitted,

Exhibit #1

Issues That Affected the Market in 2012

- The slow resolution of the European sovereign debt crisis
  - Nine Euro nations saw their debt rating downgraded
- Volatility was extreme throughout the year.
- Bad derivative trades at JP Morgan causes a $2 billion loss.
- Legislative gridlock in Washington was problematic throughout the year.
- Federal Reserve a third round of quantitative easing.
- Events leading up to the November Presidential election.
- Hurricane Sandy devastates parts of the Northeast.
- "Fiscal Cliff" brinksmanship.

Market Value @ 12-31-12

Exhibit #2

$32,633,463

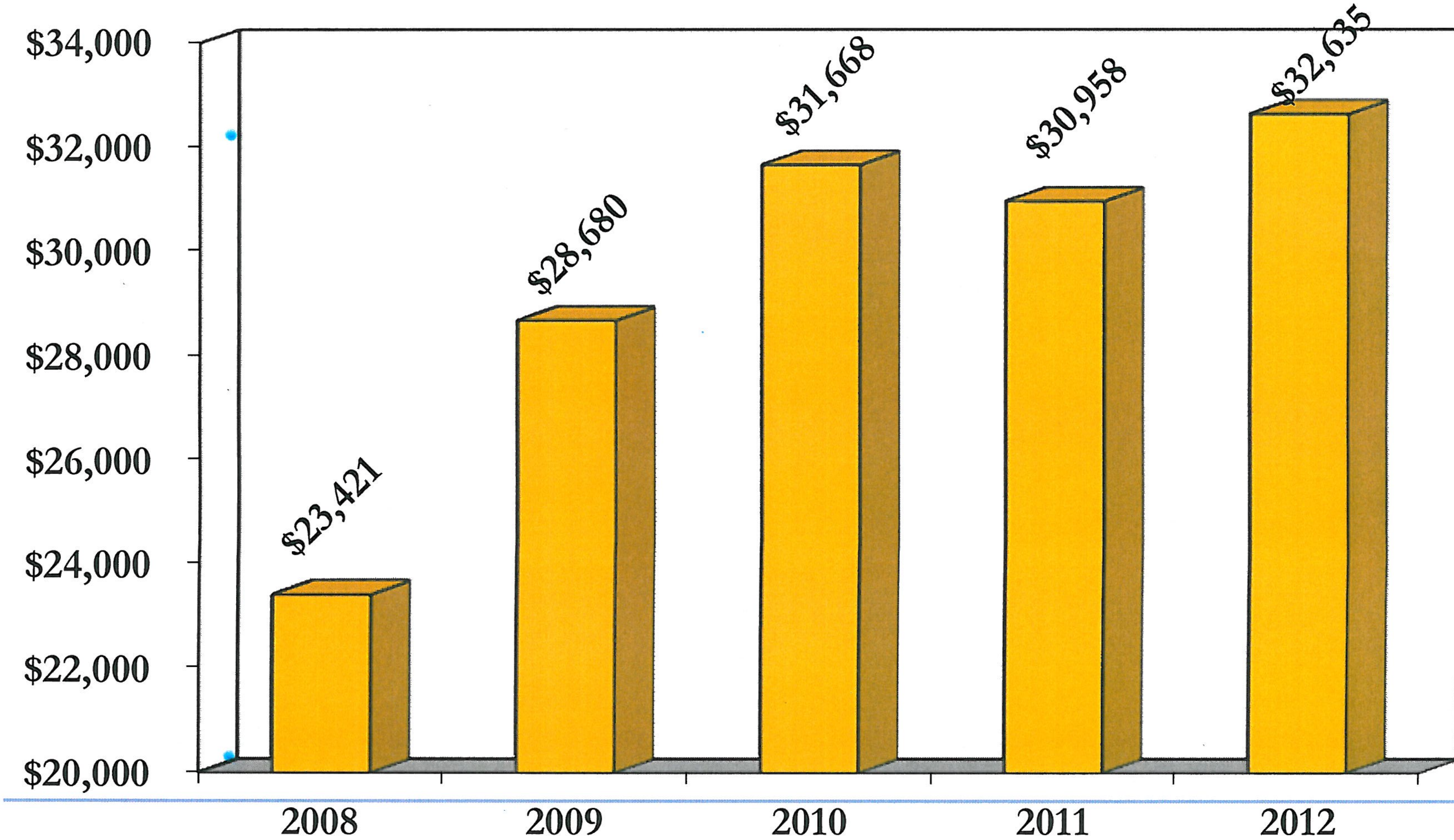


Exhibit #3

Endowment Fund Manager

Allocation & Style @ 12-31-12

$32,633,463

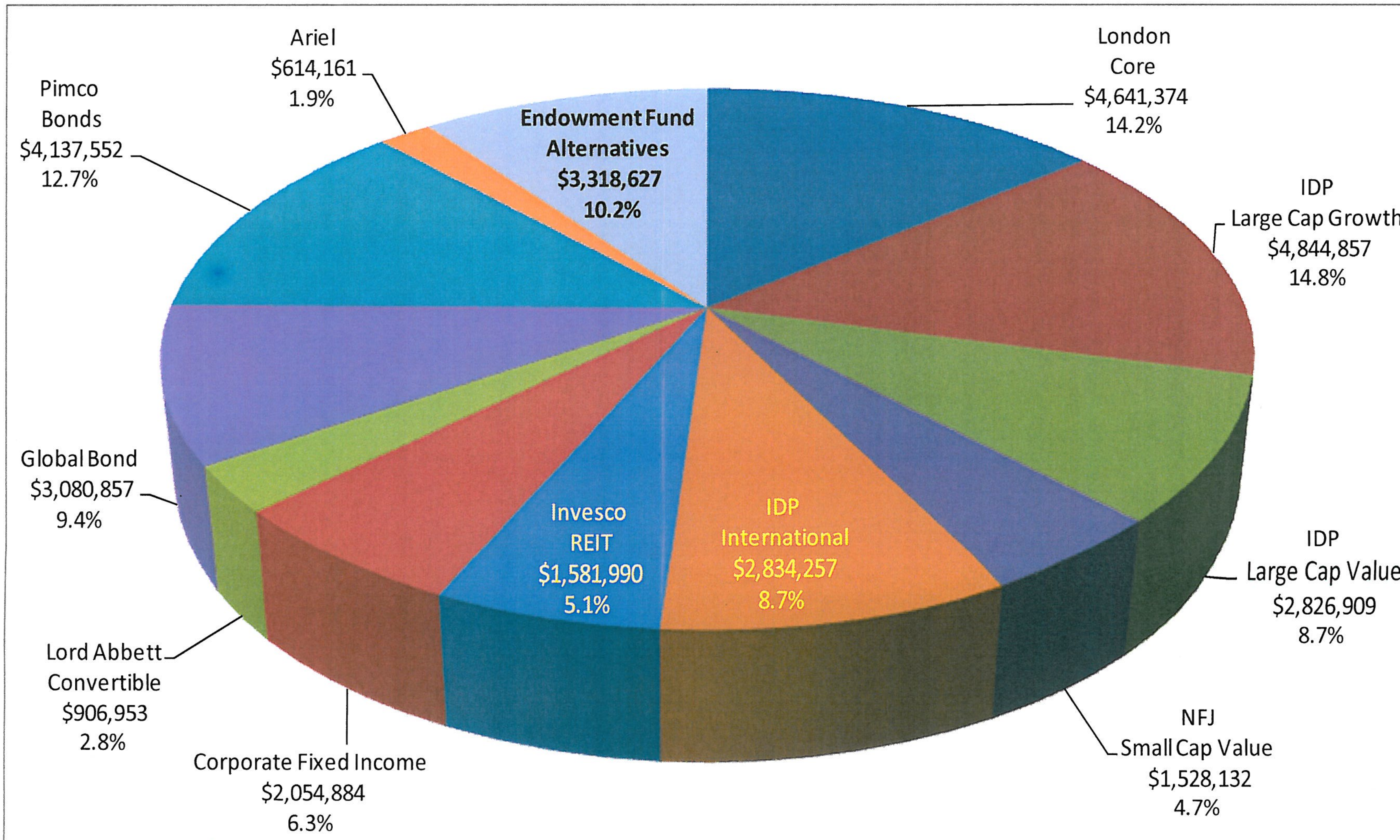


Exhibit #4

World Market Performance

- Market Returns Twelve Months 12-31-12

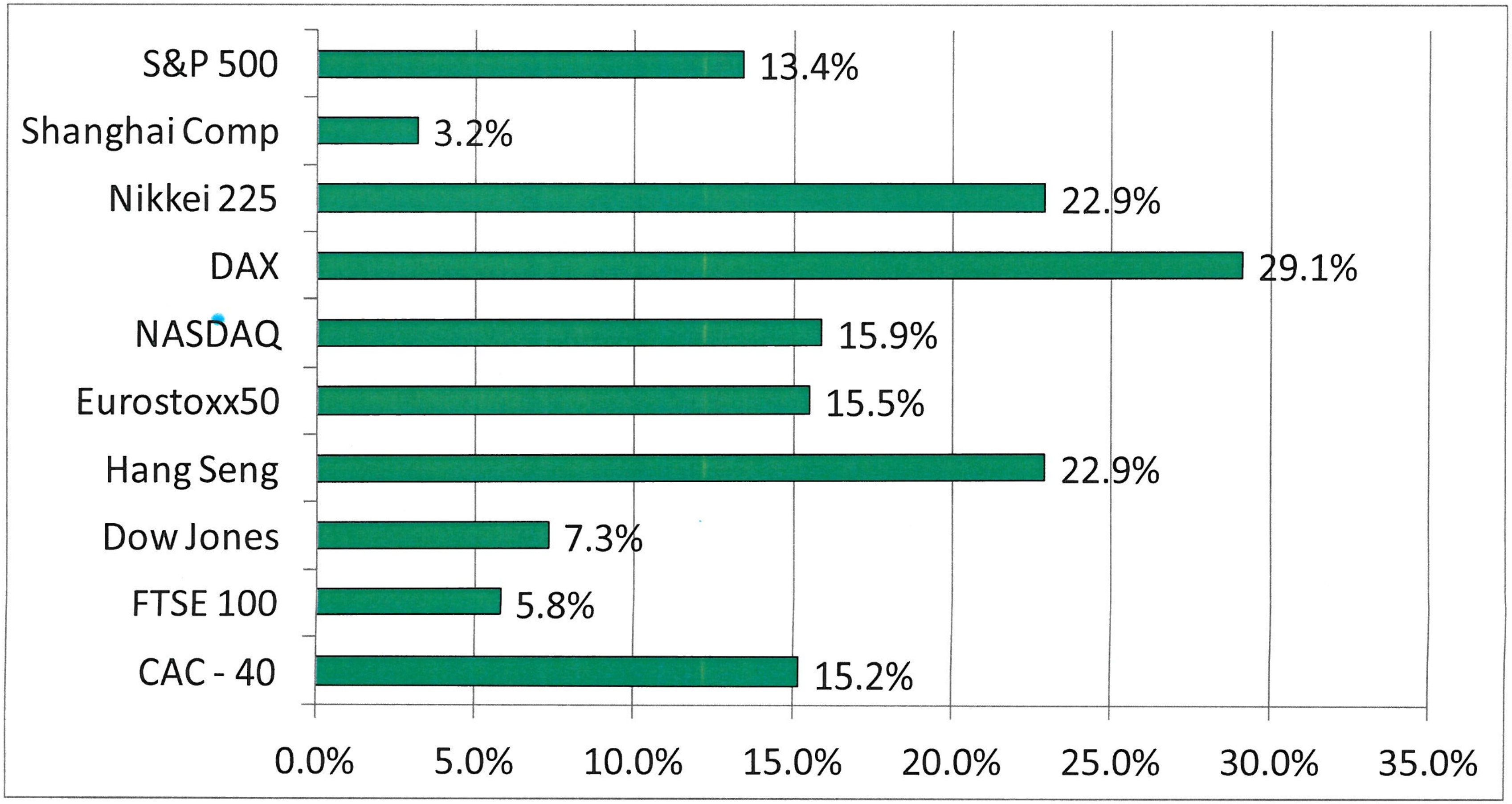


Exhibit #5

Performance Gains
Calendar Year Ending-12/31/12

Managers	Market Value	% of Portfolio	Returns	Index
London – Core	$ 4,641,374	14.2%	12.6%	17.5%
IDP – Large Cap Growth	$ 4,844,857	14.8%	12.4%	15.2%
IDP – Large Cap Value	$ 2,826,909	8.7%	14.0%	17.5%
NFJ – Small Cap Value	$ 1,528,132	4.7%	3.4%	18.0%
Ariel Capital - SRI	$ 614,161	1.8%	18.8%	18.5%
IDP - International	$ 2,834,257	8.7%	17.9%	17.9%
Endowment Fund*	$ 3,318,627	10.2%	-0.6%	3.4%
Invesco - REIT	$ 1,844,900	5.7%	16.6%	19.7%
Total Equity	$22,453,217	68.8%		

*Performance reported on a one month lag.

Exhibit #6

Performance Gains
Calendar Year Ending-12/31/12 (Con't)

Managers	Market Value	% of Portfolio	Returns	Index
Corporate Fixed Income	$ 2,054,884	6.3%	6.8%	2.9%
Lord Abbett – Convt. Bonds	$ 906,953	2.8%	12.1%	10.0%
Global Bonds	$ 3,080,857	9.4%	17.1%	4.1%
Pimco - Bonds	$ 4,137,552	12.7%	7.7%	4.5%
Total Fixed Income	$10,180,246	31.2%		
Total Portfolio	$32,633,463	100.00%	10.5%	12.1%

Exhibit #7

Manager Composite Performance

@ 9/30/12

Managers	1 Year	Benchmark	3 Year	Benchmark	5 Year	Benchmark
London Company - Core	25.6%	29.2%	NA	NA	NA	NA
IDP - Large Cap Growth	26.1%	30.9%	17.9%	11.8%	8.0%	(0.9%)
IDP - Large Cap Value	26.0%	30.9%	10.2%	11.8%	NA	NA
NFJ - Small Cap Value	15.1%	32.6%	7.8%	11.7%	1.2%	1.4%
Ariel Capital - SRI	31.6%	29.3%	12.6%	13.9%	3.3%	1.7%
IDP - International	16.7%	14.3%	3.8%	2.6%	NA	NA
Invesco - REIT	31.6%	33.8%	12.6%	20.7%	3.3%	2.3%
Corporate Fixed Income	NA	NA	NA	NA	NA	NA
Lord Abbett - Conv Bonds	13.2%	14.0%	6.1%	6.7%	2.6%	(0.4%)
Global Bond & Real Assets	NA	NA	NA	NA	NA	NA
PIMCO - Bonds	8.8%	5.4%	7.0%	6.3%	7.9%	6.5%
Endowment Fund - Alternatives	1.1%	2.8%	2.6%	1.7%	(1.2%)	(1.4%)
ALA Endowment						

Exhibit #8

Asset Allocation Strategy

ASSET ALLOCATION STRATEGY	POLICY GUIDELINES @ 9-30-12			
	Min	Target	Actual	Max
Domestic Large/Medium Cap Stocks	30%	40%	39.5%	50%
London Company - Core			14.2%	
IDP - Large Cap Value			8.7%	
IDP - Large Cap Growth			14.8%	
Ariel - SRI			1.8%	
Domestic Small/Medium Cap Stocks	0%	5%	4.7%	10%
NFJ - Small Cap Value			4.7%	
Alternative Investments	0%	10%	10.2%	15%
Endowment Fund			10.2%	
International Equity	5%	10%	8.7%	15%
IDP - International			8.7%	
Real Estate Investment Trust (REIT)	5%	5%	5.7%	15%
Invesco			5.7%	
Investment Grade Fixed Income	20%	30%	31.2%	50%
Corporate Fixed Income			6.3%	
Global Fixed			9.4%	
Lord Abbett			2.8%	
PIMCO - Bonds			12.7%	
Cash and Cash Equivalents	0%	0%	0%	5%
			100%	