

San Mateo County Employees' Retirement Association
Minutes of the Investment Committee

April 22, 2003 – Investment Committee Agenda

PUBLIC SESSION – The Committee met in Public Session at 10:15 A.M.

- 1.0 Call to Order
- 2.0 Roll Call
- 3.0 Approval of the Minutes for the Investment Committee Meeting
- 4.0 Oral Communications From the Committee
- 5.0 Oral Communications From the Public
- 6.0 Investment Management Services of the Investment Committee
 - 6.1 Acceptance of Monthly Portfolio Performance Report
 - * 6.2 Review & Selection of Optimal Portfolios for the Asset / Liability Modeling Study
 - 6.3 Acceptance of Barclay Global Investors Compliance Certification Statement
 - 6.4 Annual Global Custodian Review – State Street Bank & Trust Company
 - 6.5 Investment Manager Interim Review – Bank of Ireland Asset Management
- 7.0 Other Business
- 8.0 Adjournment

**The Committee will briefly discuss this topic. The Agenda Item in its entirety will be heard at the Board.*

MINUTES OF SAMCERA'S Investment Committee

- 1.0 Call to Order:** Mr. Bryan called the Public Session of the Investment Committee of the Board of Retirement to order at 10:15 A.M., April 22, 2003 in *SamCERA's* Board Room, Suite 125, 100 Marine Parkway, Redwood Shores, California.
- 2.0 Roll Call:** Mr. Buffington, Mr. Bryan, Ms. Colson and Mr. Cottle (11:00)
Board Members in Attendance: None *Alternate Board Member:* Ms. Arnott (10:30) *Staff:* Mr. Clifton.
Consultant: Ms. Jadallah *Public:* none *Retirees:* One
- 3.0 Approval of the Minutes:** The March 25, 2003 Investment Committee Minutes were unanimously approved.

Action: Motion by Mr. Buffington, seconded by Ms. Colson, carried unanimously to accept the Investment Committee Minutes.
- 4.0 Oral Communications From the Committee** None
- 5.0 Oral Communications From the Public** None
- 6.1 Acceptance of Monthly Portfolio Performance.** Staff provided the following review of the portfolio performance.

Nine months into the fiscal year *SamCERA's* year-to-date return is -7.32%. With continued uncertainties about the health of the economy and the political risks to future global harmony weighing on investors, it appears the Association is headed for its third consecutive year with negative returns (FYE2002 -5.92%, FYE2001 -4.25%). Last month's performance report saw negative numbers extend to the trailing five-year period for the first time (-0.35% as of 3/31/03).

San Mateo County Employees' Retirement Association
Minutes of the Investment Committee

For period ending 03/31/2003, total returns slightly underperform the policy benchmark for the trailing three and six months (refer to page six). However, the one-month "trend" shows positive portfolio returns vis-à-vis the policy benchmark. The one-month outperformance is attributed to security selection, which was positive in all asset classes with real estate contributing 12 of the 16 basis points of outperformance. The portfolio weights slightly hindered performance (-0.01) in the same period. international equity, domestic equity, and domestic fixed income portfolios.

Mr. Buffington wished to have the minutes reflect that the Plan has lost money the past couple of years. By this he means that *SamCERA's* expenses have been greater than the contributions plus portfolio income.

Below is a table with the composite returns followed by portfolio market values and target versus actual allocations.

March 31, 2003		One Month	Trailing Three Months	Trailing Six Months	Trailing Twelve Months
Equity Aggregate	\$687,322,566	0.44%	-5.02%	2.06%	-25.35%
Equity Composite Benchmark		0.39%	-4.19%	3.07%	-24.23%
Variance		0.05%	-0.83%	-1.01%	-1.12%
Fixed Income Aggregate	\$357,812,435	0.00%	1.43%	2.62%	11.58%
Fixed Income Composite Benchmark		-0.08%	1.40%	2.99%	11.70%
Variance		0.08%	0.03%	-0.37%	-0.12%
Real Estate Aggregate (1)	\$64,836,536	3.74%	5.01%	8.99%	14.45%
NCREIF (one quarter lag)		1.67%	1.67%	3.49%	6.74%
Variance		2.07%	3.34%	5.50%	7.71%
Cash Aggregate	\$6,339,876	0.15%	0.41%	0.92%	2.61%
91 Day Treasury Bill		0.12%	0.31%	0.74%	1.66%
Variance		0.03%	0.10%	0.18%	0.95%
Total Fund Returns	\$1,116,311,413	0.48%	-2.43%	2.51%	-12.07%
Total Plan Policy Benchmark		0.33%	-2.23%	3.25%	-12.94%
Variance		0.15%	-0.20%	-0.74%	0.87%

Asset Allocation As of 3/31/2003	Market Value	Allocation		Percentage Off Target	Rebalance Range
		Current	Target		
BGI Russell 1000	\$435,831,961	39.04%	40.00%	-0.96%	±5%
BGI Russell 2000	\$100,978,608	9.05%	10.00%	-0.95%	±5%
BIAM	\$150,511,997	13.48%	15.00%	-1.52%	±5%
Total Equity	\$687,322,566	61.57%	65.00%	-3.43%	
BGI US Debt	\$190,046,711	17.02%	16.00%	1.02%	±3%
DAMI	\$167,765,724	15.03%	13.00%	2.03%	±3%
Total Fixed Income	\$357,812,435	32.05%	29.00%	3.05%	
Real Estate	\$64,836,536	5.81%	6.00%	-0.19%	±2%
Cash	\$6,339,876	0.57%	0.00%	0.57%	
Total	\$1,116,311,413	100.00%	100.00%		

San Mateo County Employees' Retirement Association
Minutes of the Investment Committee

Action: The Committee unanimously accepted the Monthly Performance Report. The Committee will recommend to the Board of Retirement that it accept the report.

6.2 Review & Selection of Optimal Portfolios for the Asset / Liability Modeling Study

Mr. Bryan, acting Chair put this item over pending the arrival of Mr. Cottle. Mr. Cottle resumed the chair for this item.

Marc Gesell and Margaret Jadallah of Strategic Investment Solutions (SIS) presented the Asset / Liability Projections Part I: Asset Mixes. This presentation flows from the Board's decisions on March 25th regarding the suitable asset classes, constraints, and weighting schemes for integration of sub-classes that would be used in the study

SIS provided the following five mixes.

	SAMCERA TARGET	MIX 1	MIX 2	MIX 3	MIX 4	MIX 5
US LARGE CAP EQUITY	40.0%	29.5%	31.3%	34.4%	37.3%	40.0%
US SMALL CAP EQUITY	10.0%	7.4%	7.8%	8.6%	9.3%	10.0%
INTERNATIONAL EQUITY	15.0%	18.9%	20.0%	20.0%	20.0%	20.0%
US FIXED INCOME	29.0%	36.6%	32.8%	28.6%	24.3%	20.0%
REAL ESTATE	6.0%	7.6%	8.1%	8.4%	9.1%	10.0%
% EQUITIES	71%	63%	67%	72%	76%	80%
TOTAL RETURN	8.23%	7.94%	8.09%	8.25%	8.39%	8.55%
TOTAL RISK	11.74%	10.68%	11.18%	11.73%	12.27%	12.85%

Mr. Buffington suggested that it would be difficult to achieve the “historic averages” used to arrive at the above mixes. The Committee noted that the Board will reconsider the actuarial interest rate next year and it is very likely that the rate will be lowered to 8.0% or below. The consensus is that it would be useful for the Investment Committee to view more of the lower risk spectrum. • Mr. Bryan reminded the Board that although the actuarial rate may be lowered, the Board should not choose a mix that is too conservative. The Asset Liability study is about being prudent and selecting a portfolio of well-diversified assets.

The Committee discussed adding a high yield fixed income component to the asset mix. The consensus is that a high yield component should be added to the additional mixes the Committee will review.

Action: The Committee unanimously asked SIS to return next month with ten portfolios on the efficient frontier. The Committee will recommend that the Board adopt those constraints.

San Mateo County Employees' Retirement Association
Minutes of the Investment Committee

6.3 Acceptance of Barclay Global Investors Compliance Certification Statement.

Staff reported that in the past six months there have been no significant changes in the *SamCERA*/BGI relationship. Barclays Global Investors reported two personnel changes. In January 2003, Mr. Robert Slotpole joined BGI as Chief Investment Officer for active equity products managed in the US. Also in early 2003, Rich Ricci joined BGI to take on the role of Chief Operating Officer

On March 31st, BGI managed 65.0% of *SamCERA*'s portfolio at market in the following passive asset classes:

ASSET CLASS	PERCENT OF PORTFOLIO	BOOK VALUE	MARKET VALUE	TRAILING TWELVE MONTH RETURN	ANNUALIZED RISK
Domestic Large Cap, Russell 1000	39.0%	\$449.6	\$435.8	-24.49%	16.81%
Domestic Small Cap, Russell 2000	9.0%	\$131.5	\$101.0	-26.81%	22.53%
Domestic Bonds, US Debt Index	17.0%	\$130.1	\$190.0	11.85%	3.36%
TOTAL (in millions)	65.0%	\$711.2	\$726.8		

Action: By consensus the Committee accepts the Investment Committee's fiscal year 2002-2003 Strategic Plan (work plan).

6.4 Annual Global Custodian Review – State Street Bank & Trust Company.

This item will be heard in its entirety before the full Board. **Karen Jacobs**, Director and Senior Vice President, **Bernie McCrossan**, Vice President, and **Asim Azfar**, Client Service Officer will be available to discuss all aspects of the custodial relationship at the meeting of the Board later in the day. **Lisa Massena**, State Street Analytics will be available to discuss performance reporting and related subjects.

Staff reported that State Street acquired the Custodial Business of Deutsche bank in the past year. State Street reports that the assimilation of the business is going well. Staff also reported that *SamCERA* and State Street have begun discussions on developing an interface with *SamCERA*'s accounting software. This project should be completed in the next fiscal year. SSB will also provide *SamCERA*'s staff with updated training for In-Sight, SSB's on-line system. Another significant project is foreign tax reclaims. State Street is working with foreign governments to improve the tax reclaim process. Recently SSB assisted the Association in establishing electronic filing for tax reclaims with Germany.

Ms. Jadallah noted that Mr. Cottle raised a question regarding SSB's change in pricing services. The Custodian should have at least two distinct pricing services. When Lehman merged with SSB's other pricing service, it required SSB to acquire a new service.

Mr. Buffington suggests that *SamCERA* should revisit its policy on security lending. If the Plan is

San Mateo County Employees' Retirement Association
Minutes of the Investment Committee

able to get a good split (75/25 with no transaction fees), the incremental income is worth pursuing. • Ms. Jadallah reminded the board that BGI only provides *SamCERA* a 50/50 split on the Indexed Portfolios. BGI only negotiates a better split with their very largest clients. • Mr. Clifton noted that the Treasurer administers a large fixed income portfolio, which is very attractive to a security lender. Even with a change in manager structure, *SamCERA*'s lendable securities will not warrant a split similar to that of the Treasurer's Portfolio. • Mr. Buffington reiterated that *SamCERA* should pursue security lending after it reviews manager structure. At that time it will be clearer what portfolios are lendable and how attractive they are to a security lender.

Action: By consensus the Committee approved a recommendation to the Board that would authorize the Board Chair to execute an amendment to the BIAM Agreement, which amends the maturity date from 6/30/2003 until 10/31/2003.

6.5 Investment Manager Interim Review – Bank of Ireland Asset Management.

Staff recapped why the Committee invited BIAM to appear before it today. In early 2002 attribution analysis indicated that BIAM's stock selection had deteriorated. In May of 2002 the Board asked BIAM to make a special appearance before it to discuss portfolio performance. At the meeting Mr. Cottle expressed concern that BIAM does not appear to have an explicit sell discipline that requires the managers to cut their losses when individual stocks fall out of favor. Mr. Connolly reported that BIAM will sell a stock under four conditions: (1) when a stock has performed above expectations and BIAM feels fundamentals do not support the price; (2) when relative value makes a new stock more attractive than the current holding; (3) when a company's management changes its strategy and BIAM concludes that the management is not up to the task; and (4) when a company has completely failed to meet BIAM's targets. Mr. Connolly reported that BIAM did not have a fixed point sell discipline, such as automatically selling when a stock is down 50%.

Padraig Connolly, Vice President Client Services, and Michael McCarthy, Portfolio Specialist, appeared before the Board in November 2002 at BIAM's regularly scheduled annual review. The Board again expressed concern over BIAM's performance relative to stock selection.

In February 2003 Mr. Clifton informed the Board that Bank of Ireland Asset Management's performance qualifies it to be on *SamCERA's "Watch List"*. The Investment Plan provides three definitions of underperformance on page seven of Section Nine. BIAM's trailing twelve month performance meets the first definition, which is, *"Four cumulative quarters in which the manager's performance (gross of fees) falls below the style based benchmark return times 0.8 (for example, if the benchmark return is 10%, the manager's return would be less than 8.0%)." Ms. Jadallah offered that the Strategic Investment Solutions 12/31/2002 quarterly report would show that BIAM also meets the second definition, which is, "Performance (gross of fees) below the 50th percentile for equity managers and 60th percentile for fixed income managers in a universe of the managers' peers over any consecutive 8-quarter period. Below median performance on a risk adjusted basis is also a guiding tool in the evaluation of the investment manager."*

Padraig Connolly, Vice President, Client Services and **John Forde**, Senior Equity Manager were present to discuss BIAM's performance, processes and why the portfolio is positioned as it is.

Mr. Connolly updated the Board on the announcement that Brian Goggin replaced BIAM's Chief Executive Officer, Willie Cotter upon his retirement. The asset managers have been organized within a team structure. Three deputy CIO's have been named. They are Jane Neill, John Nolan and Des Sullivan.

San Mateo County Employees' Retirement Association
Minutes of the Investment Committee

Mr. Forde wanted the Board to know that BIAM has not changed its policies, procedures or strategies. He has been with the bank since 1995 and of the senior managers, who are members of the investment strategy group; he is the most recent addition. The people *SamCERA* hired in 1996 are the same people today. • Although there are a number of factors leading to recent underperformance, the ultimate explanation is poor stock selection. What has gone wrong for BIAM is a combination of dollar sensitivity and underweighting of Japan. BIAM points to a large cap effect over the past year, due primarily to liquidity. BIAM's portfolio is a fairly concentrated portfolio on the large cap end of the market, approximately 70 issues. It suffered because of the large cap effect.

Ms. Colson noted that the BIAM portfolio has a low P/E relative to the market and appears to be positioned well for a recovery. The stocks may be financially superior to the market and have a better chance to deliver than the overall market going forward. • In a response to Ms. Colson's question, Mr. Connolly noted that BIAM has gained more clients than it lost in the past year. He believes that BIAM has not lost clients due to performance issues.

Below is BIAM's performance as of 03/31/2003.

Performance & Values As Of 03/31/2003	Book Value	Market Value	Trailing Three Months	Trailing Six Months	Trailing Twelve Months	Since Inception
	(Unit Million)					
Bank of Ireland Asset Management	\$181.0	\$150.5	-10.93%	-5.16%	-25.99%	0.31%
MSCI ACWI Free ex-US			-7.30%	-0.94%	-22.19%	-1.97%
<i>Return Variance</i>			<i>-3.63%</i>	<i>-4.22%</i>	<i>-3.80%</i>	<i>2.28%</i>

Action: By consensus the Committee approved a recommendation to the Board that would authorize the Board Chair to execute the Written Consent of Sole Shareholders in Lieu of Annual Meeting for each of SamCERA's Properties.

7.0 Other Business: None

8.0 Adjournment: There being no further business Mr. Cottle adjourned the Committee at 11:58 A.M.