

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

January 27, 2004 – Investment Committee Agenda

PUBLIC SESSION – The Committee met in Public Session at 9:00 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 Adoption of SamCERA's Investment Manager Structure – International Equity
 - * 6.3 Selection of finalist for SamCERA's Domestic Equity Manager Structure
 - 6.4 Adoption of Strategic Objectives Schedule for Fiscal Year 2004/2005
 - 6.5 Approval of Change of Committee Meeting Date from February 24 to February 18
- 7.0 Other Business
- 8.0 Adjournment

** The Investment Committee will review all semi-finalists in detail and make a recommendation to the Board. Selection of the finalists will be 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 9:00 A.M on January 27, 2004, at SamCERA's Board Room, Suite 125, 100 Marine Parkway, Redwood Shores, California.
- 2.0 Roll Call:** Mr. Bryan, Ms. Arnott for Mr. Buffington, and Ms. Colson. Mr. Lewis is excused. Board *Members in Attendance:* Mr. McMahon (9:10), Ms. Salas, Ms. Stuart (9:55), and Ms. Tashman *Staff:* Mr. Clifton and Mr. McCausland. *Consultant:* Mr. Brody, Ms. Jadallah, and Mr. Thomas *Public:* none *Retirees:* Two (one at 10:12)
- 3.0 Approval of the Minutes:** The November 25, 2003 Investment Committee Minutes were considered and unanimously approved. There was no Investment Committee meeting in December 2003.

Action: Motion by Ms. Colson, seconded by Ms. Arnott, 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.** Mr. Clifton reported that in December 2003, investors continued to receive a string of evidence that the world economic activity is improving. Investors' overall confidence continues to be high. Weak employment data has all but eliminated any chance that the Federal Reserve will raise its target of 1.0% in the near future. Fixed Income rates remain low in spite of all the talk of a bear fixed income market. Equity markets in Asia were mixed last month, while Europe and the U.S. experienced modest gains of between 0.9% and 2.5%. Amid concern regarding the US trade and budget deficits, the euro & the pound sterling gained strength against the US dollar.

For the period ended 12/31/2003, SamCERA's trailing twelve-month return is a respectable 22.68%. The returns for the one (3.62%), three (9.17%) and six (12.21%) month periods are also good absolute returns. Those returns exceed the actuarial interest rate in each of the periods. However, during those periods poor security selection primarily in international equity resulted in total portfolio returns that underperformed relative to the plan policy benchmark. • Ms. Colson noted that one very good year could not negate the negative impact of the previous three years.

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The table presented below shows the composite returns

December 31, 2003		One Month	Trailing Three Months	Trailing Six Months	Trailing Twelve Months
Equity Aggregate	\$975,167,399	4.17%	12.74%	17.46%	33.12%
Equity Composite Benchmark		4.24%	12.73%	17.47%	33.26%
Variance		-0.07%	0.01%	-0.01%	-0.14%
Fixed Income Aggregate	\$379,512,874	1.01%	0.46%	0.31%	4.52%
Fixed Income Composite Benchmark		1.02%	0.32%	0.17%	4.11%
Variance		-0.01%	0.14%	0.14%	0.41%
Real Estate Aggregate (1)	\$58,073,782	1.45%	2.04%	3.23%	11.68%
NCREIF (one quarter lag)		1.97%	1.97%	3.98%	8.15%
Variance		-0.52%	0.07%	-0.75%	3.53%
Cash Aggregate	\$7,092,167	0.19%	0.47%	1.12%	2.14%
91 Day Treasury Bill		0.10%	0.26%	0.50%	1.15%
Variance		0.09%	0.21%	0.62%	0.99%
Total Fund Returns	\$1,419,846,222	3.62%	9.17%	12.21%	22.68%
Total Plan Policy Benchmark		3.68%	9.03%	12.85%	23.94%
Variance		-0.06%	0.14%	-0.64%	-1.26%

Performance versus *SamCERA's* Actuarial Discount Rate

Total Fund Returns	\$1,419,846,222	3.62%	9.17%	12.21%	22.68%
Actuarial Discount Rate		0.64%	1.94%	3.92%	8.12%
Variance		2.98%	7.23%	8.29%	14.56%

The table below shows portfolio market values and target weightings versus actual allocations.

Asset Allocation As of 12/31/2003	Market Value	Allocation Current	Target	Percentage Off Target	Rebalance Range
BGI Russell 1000	\$587,714,201	41.39%	40.00%	1.39%	±5%
BGI Russell 2000	\$166,996,382	11.76%	10.00%	1.76%	±5%
BIAM	\$220,456,815	15.53%	15.00%	0.53%	±5%
Total Equity	\$975,167,399	68.68%	65.00%	3.68%	
BGI US Debt	\$210,240,398	14.81%	16.00%	-1.19%	±3%
DAMI	\$169,272,476	11.92%	13.00%	-1.08%	±3%
Total Fixed Income	\$379,512,874	26.73%	29.00%	-2.27%	
Real Estate	\$58,073,782	4.09%	6.00%	-1.91%	±2%
Cash	\$7,092,167	0.50%	0.00%	0.50%	
Total	\$1,419,846,222	100.00%	100.00%		

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

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6.2 Adoption of SamCERA's Investment Manager Structure – International Equity

Strategic Investment Solutions' (SIS) representatives, Margaret Jadallah, & Patrick Thomas, provided an overview of three proposed structures for International Equity Investment Management. This presentation flows from Strategic Investment Solutions' first International Investment Manager presentation on 11/25/2003. After discussing the manager structure alternatives presented that day, the Committee opined that it wished to view three additional alternatives. Those alternatives were to include data from actual managers so that the Board may better view the portfolio relationships. The alternatives are outlined below:

- 1) One Core Manager (Growth Bias). (Active Risk 4.00%, Information Ratio 0.29, Alpha 1.20%)
- 2) Two Core Managers. (Active Risk 3.76%, Information Ratio 0.31, Alpha 1.20%)
- 3) One Core Value and One Core Growth Manager. (Active Risk 3.02%, Information Ratio 0.45, Alpha 1.35%)

After an active discussion the Committee eliminated the one and two core manager structures. • Ms. Colson asked why Bank of Ireland Asset Management (BIAM) did not fit into any of the alternatives. Mr. Thomas explained that *SamCERA's* International Equity Benchmark requires emerging market exposure. Since BIAM historically has very little emerging market exposure it does not fit into an optimum manager structure. The Committee discussed alternatives that would offset BIAM's under exposure to emerging markets and found none acceptable. • Mr. Bryan noted that the third alternative with a Core Value Manager and Core Growth Manager provides manager and style diversification, which reduces risk. Those managers also provide the emerging market exposure that *SamCERA's* benchmark requires. The Committee agreed with Mr. Bryan.

Action: Motion by Ms. Arnott, second by Ms. Colson, for the Investment Committee to recommend to the Board of Retirement that it adopt a Core Value and Core Growth Manager Structure for its International Equity Portfolio. The exact weights of the value and growth portfolios will be determined at a later date.

6.3 Selection of finalist for SamCERA's Domestic Equity Manager Structure. Strategic Investment Solutions' representatives, Jonathan Brody, Margaret Jadallah, & Patrick Thomas, present the semi-finalists for *SamCERA's* domestic equity manager searches.

Ms. Jadallah briefly explained Strategic Investment Solutions' process of quantitative and qualitative screening, which has a goal of finding the strongest organization with the best people demonstrating a sound investment process. That firm would have quality performance with effective risk control efforts. The risk control efforts are especially important in the enhanced products. SIS produces a client book to assist in selecting the best firm. The client book includes firm and product data, a description of the product, a summary section, which outlines strengths and weaknesses and performance and risk measures. It also includes comparison performance over a variety of time periods, peer rankings, style graphs, and upside and downside return patterns. A statistical section appears at the end of each book, which provides a comparison of the managers presented in that book.

The Investment Committee has not conducted a manager search for several years. It noted SIS' heavy reliance on statistical information in their client book and is uncomfortable with that approach. The Committee then spent considerable time reviewing the presentation format. • Ms. Arnott noted that the

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Committee directed Strategic Investment Solutions to conduct the manager searches using its database and not to issue Requests for Proposal (RFP). However, she recalled *SamCERA's* previous manager search where the staff issued a Request for Proposal. The RFP process and presentation of materials allowed for more text in the evaluation of the investment firms. Text provided trustees with insight into the capabilities of the managers that responded. In Ms. Arnott's opinion a statistical analysis of the firms denies the trustee qualitative information that would allow him or her to be more comfortable in selecting an investment manager. • Mr. Bryan echoed Ms. Arnott's sentiment regarding the small cap presentations, but found the approach acceptable with the large cap enhanced presentation. • Ms. Colson noted that SIS provides some analysis in text form. She suggested that SIS augment that analysis with responses from the questionnaire it sends to all semifinalists.

The Investment Committee directed SIS to amend the client books and reschedule the domestic equity manager search presentations. The client books should be amended to include the following:

(1) Additional text should be provided to assist the trustees in understanding the quantitative and qualitative data. (2) The primary source of this text will be the responses to the questionnaire SIS distributes to each semifinalist. (3) The criteria employed in the manager search screening process. The trustees find value in seeing where and why firms fell out of the search process. It is easier to compare and contrast managers when they are presented in sections separated by tabs. The Committee directed SIS to present six or fewer semifinalists in each category. The semifinalists in small cap value and growth are to be rescheduled for February. Also in February, SIS will present a proposed calendar for the other manager searches. Mr. Thomas concurred with the requested presentation format. He noted it is important for trustees to be comfortable with the selection process. It is better to take time to explore all concerns than to hasten the process and thus lose confidence in it.

The Committee also discussed Strategic Investment Solutions' role and responsibilities in the manager search process. Mr. Bryan reminded the Investment Committee that the Board charged SIS with performing the manager searches and granted full discretion for SIS to present the best-qualified firms in each search category. Should a trustee or staff wish to suggest names to be included or excluded from the search process, those suggestions must be made in an open forum at the Board or Committee. No direction is to be taken by SIS without Board approval. • The committee members believe certain unsuccessful candidates will wish to discuss why they were eliminated from the search. SIS was directed to receive those calls on behalf of the Association. However, those calls should be received only at the conclusion of the search process. SIS may use its discretion regarding the information to be provided to investment managers.

Since the search process is to be rescheduled, Strategic Investment Solutions briefly discussed the following semifinalists. SIS also provided an overview of the screening process used in each manager mandate. The mandates and semifinalists are provided below:

Large Cap Enhanced Index

- 1) Barclays Global Investors
- 2) Batterymarch Financial Management
- 3) Franklin Portfolio Associates (No relationship to Franklin/Templeton)

Ms. Jadallah stated that there are only fourteen managers that run a large cap enhanced product versus the Russell 1000 Benchmark. • Ms. Colson suggested that since the skills required to manage an Enhanced

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S&P 500 product are transferable to the Russell 1000 product, perhaps the Committee should look at additional managers who may have demonstrated skill in managing an Enhanced S&P 500 product. • Mr. Brody offered that if a manager does not currently offer a Russell 1000 product or has a short track record, it might be problematic to provide meaningful performance data. • Ms. Colson noted that for fee leverage it might be beneficial to consider managers that have products in more than one domestic equity category. SIS concurred and will take that into consideration in screening managers

Small Cap Enhanced Index

- 1) Barclays Global Investors
- 2) Citigroup Asset Management
- 3) Goldman Sachs Asset Management
- 4) JPMorgan Fleming Asset Management
- 5) Panagora Asset Management

The Committee express regrets that Barclays Global Investors small cap enhanced product is closed. The remaining managers are strong candidates and will allow the committee to make a good selection.

Small Cap Active Value

- 1) Boston Partners
- 2) Brandes
- 3) RS Investments

SIS reminded the Committee that active small cap managers reach capacity quickly and close their doors. The Committee wishes to see additional names in the small cap value.

Small Cap Active Growth Strategic Investment Solutions briefly described the following candidates:

- 1) Chartwell Investment Partners
- 2) Mazama Capital Management
- 3) Next Century Growth Investors
- 4) Wellington Management Company
- 5) Westcap Investors

After reviewing the semifinalists the Committee opined that Mazama Capital Management did not have a product that meets the Committees criteria. SIS was instructed to come back in February with six or fewer candidates in each of the domestic small cap value and small cap growth mandates.

Members of the public, Mr. John Murphy & Mr. Bob Friday asked for clarification on the Committee's policy regarding questions or interaction from members of the audience. • Mr. Bryan reiterated County Counsel's opinion that Trustees not on the Investment Committee may not interact with the Committee. Members of the public, after being recognized by the chair are given one or two minutes to address the Committee under the agenda item *Oral Communications from the Public*. The individual will identify himself or herself and provide their comment. That comment may be that they wish to address the Committee when a specific agenda item is being discussed. If a member of the public wishes to address the Committee under a specific agenda item, the Chair will recognize that individual at the appropriate time, which is generally after the Committee has concluded its deliberation, but before a vote is called.

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Action: Motion by Mr. Bryan, second by Ms. Arnott to recommend to the Board of Retirement that Strategic Investment Solutions reschedule the manager search calendar and amend the format of the client books to include additional text on the quantitative and qualitative attributes of the investment managers.

- 6.4 Adoption of Strategic Objectives Schedule for Fiscal Year 2004/2005.** Mr. Clifton presented a draft schedule for the Investment Committee's fiscal year 2004/2005 calendar. The draft schedule introduces educational presentations by SIS, semi-annual Capital Market and Inflation assumption reviews, and review and revision, as required, of *SamCERA's Investment Plan*. The Committee proposes to hire six additional investment managers. Their annual reviews have been scheduled along with *SamCERA's* other investment professionals as follows:

Investment Services Provider	Annual Review	Compliance Certification Statement
Strategic Investment Solutions	July 2004	January 2005
Deutsche Asset Management	August 2004	February 2005
INVESCO Realty Advisors	September 2004	March 2005
Barclays Global Investors	October 2004	April 2005
Bank of Ireland Asset Management	November 2004	May 2005
* Large Cap Enhanced	February 2005	August 2005
* International Equity Manager II	February 2005	August 2005
* Small Cap Enhanced	March 2005	September 2005
* Fixed Income Core-Plus	March 2005	September 2005
* Small Cap Value	April 2005	October 2005
Global Custodian	April 2005	October 2005
* Small Cap Growth	May 2005	November 2005

Action: Motion by Ms. Colson second by Ms. Arnott to adopt the proposed Investment Committee Calendar as presented by Mr. Clifton. No action is required at the Board.

- 6.5 Approval of Change of Committee Meeting Date from February 24 to February 18.** Ms. Colson explained that she wishes to change the date of the next Investment Committee since she will be traveling February 24th. The committee members, staff and Strategic Investment Solutions indicated that they are available to meet at 1:00 P.M. on February 18, 2004.

Action: Motion by Ms. Colson, second by Ms. Arnott, to change the next Investment Committee date from February 24, 2004 to February 18, 2004 AT 1:00 P. M.

- 7.0 Other Business: None**

- 8.0 Adjournment:** There being no further business Mr. Bryan adjourned the Committee at 11:30 A.M.