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

February 28, 2006 – 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
4.0 Oral Communications From the Committee
5.0 Oral Communications From the Public
6.0 Investment Management Services of the Investment Committee Shall Review & Discuss
   6.1 Monthly Portfolio Performance Report
   6.2 Quarterly Investment Performance Analysis for Period Ended December 31, 2005
   6.3 Approval of the Investment Committee's Plan for Fiscal Year 2006/2007
7.0 Other Business
8.0 Investment & Finance Manager's Report
9.0 Adjournment

MINUTES OF SAMCERA'S Investment Committee

1.0 Call to Order: Mr. Bryan, vice chair, called the Public Session of the Investment Committee of the Board of Retirement to order at 9:00 a.m., February 28, 2006 in *SamCERA*'s Board Room, Suite 125, 100 Marine Parkway, Redwood Shores.

2.0 Roll Call: Mr. Bryan, Ms. Colson (excused), Mr. Hackleman and Ms. Tashman. *Other Board Members in Attendance:* None. *Staff*: Mr. Bailey, Mr. Clifton and Ms. Dames. *Consultants*: Strategic Investment Solutions – Ms. Jadallah and Mr. Thomas. *Retirees*: One, *County*: None.

3.0 Approval of the Minutes: Motion by Hackleman, second by Tashman, carried unanimously to approve the investment committee minutes of January 24, 2006, as submitted.

4.0 Oral Communications From the Committee: None.

5.0 Oral Communications From the Public: None.

6.1 Monthly Portfolio Performance Report: Mr. Clifton presented the monthly portfolio performance report for the period ending January 31, 2006. *SamCERA*'s 3.21% Total Fund Return for January 2006 outperformed the Total Plan Policy Benchmark return of 3.07%. The Fund's Fiscal Year to Date (FYTD) return, 9.43% is 484 basis points above the FYTD Actuarial Discount Rate, 4.59%, and 6 basis points above *SamCERA*'s Total Plan Policy benchmark of 9.37%.

In its last policy meeting with retiring Chairman Alan Greenspan, the Fed raised short-term interest rates by 25 basis points to 4.50%, while leaving room in its policy statement for new Fed Chairman Ben Bernanke to raise rates at least one more time. The global economy, despite a persistent headwind from higher oil prices, remains remarkably solid. The key positive is the success central bankers have had, to date, in sharply limiting the spillover from oil into the prices of non-energy consumer goods and services. The growth in world trade and the increased supply of low-cost products from around the world are playing a significant role in keeping inflation in check.

The table presented below shows the composite returns.

December 31, 2005	Market Value	One Month	Trailing Three Months	Trailing Six Months	Trailing Twelve Months
Equity Aggregate	$1,186,213,177	4.90%	10.31%	9.14%	17.03%
Equity Composite Benchmark		4.71%	9.98%	9.04%	16.65%
Variance		***0.19%***	***0.33%***	***0.10%***	***0.38%***
Fixed Income Aggregate	$496,257,172	0.09%	1.56%	1.08%	2.55%
Fixed Income Composite		0.01%	1.40%	0.84%	1.80%
Variance		***0.08%***	***0.16%***	***0.24%***	***0.75%***
Real Estate Aggregate	$105,291,355	0.00%	2.68%	10.14%	20.98%
NCREIF (one quarter lag)		0.00%	5.43%	10.11%	20.06%
Variance		***0.00%***	***-2.75%***	***0.03%***	***0.92%***
Cash Aggregate	$6,591,350	0.33%	0.84%	1.72%	3.62%
91 Day Treasury Bill		0.31%	0.97%	1.83%	3.22%
Variance		***0.02%***	***-0.13%***	***-0.11%***	***0.40%***
Total Fund Returns	$1,794,353,053	3.21%	7.32%	6.68%	12.57%
Total Plan Policy Benchmark		3.07%	7.20%	6.72%	12.48%
Variance		***0.14%***	***0.12%***	***-0.04%***	***0.09%***
Performance versus Actuarial Discount Rate					
Total Fund Returns		3.21%	7.32%	6.68%	12.57%
Actuarial Discount Rate		0.64%	1.94%	3.92%	8.00%
Variance		***2.57%***	***5.38%***	***2.76%***	***4.57%***

Ms. Tashman asked SIS if Goldman Sachs sent follow-up items regarding the issue of dispersion brought up at their annual review in January. No materials were received but staff and SIS will follow up with the matter. Ms. Jadallah also noted that SIS will monitor GSAM's capacity issue.

Action: No action is required. The Monthly Portfolio Performance Report is an informational report.

6.2 Quarterly Investment Performance Analysis for Period Ended December 31, 2005

Ms. Jadallah and Mr. Thomas presented SIS' quarterly performance report. Attention was focused on the underperformance by Brandes Investment Partners, ranking in the bottom fourth among small cap value managers. Ms. Jadallah noted that Brandes has suffered three bankruptcies this year (Winn Dixie, Delta and Delphi), which is significant even for a deep value manager. She reported that she had spoken with Brandes regarding their analysis on the auto-component sector. She noted the firm has deep value contrarian view. Mr. Bryan expressed that he did not feel comfortable with the amount of volatility that Brandes is illustrating. Mr. Thomas stated that the volatility is in line with Brandes' strategy. In response to a question by Mr. Hackleman, Ms. Jadallah discussed the few open alternatives in the small cap value arena. Ms. Tashman requested market cycle graphs for to better understand Brandes' performance. Mr. Thomas noted that the high risk associated with Brandes is part of *SamCERA*'s small cap structure. He also noted that he wants to ensure that Brandes is sticking to their fundamental investment thesis. It was the consensus of the Investment Committee that its fifteen months with Brandes is too early to carry out any action. However, the committee will discuss placing Brandes on the watch list should the board show the same concern one year from now.

Below is selected summary detail from Strategic Investment Solutions' Quarterly performance report.

INVESTMENT PERFORMANCE SUMMARY
December 31, 2005

- The composite fund returned 2.0% in the fourth quarter of 2005 and ranked 56th among other public fundsgreater than $100 million (median of 2.1%). The fund trailed its policy index (2.2%) during this time period. Longer term, the three and five-year returns of 13.9% (40th percentile) and 5.3% (48th percentile), respectively, were above median among large public plans (13.4% and 5.2%).

- Fourth quarter results were enhanced by the following factors:

  1. The BGI Russell 1000 Alpha Tilts Fund appreciated 3.3%, ranking 30th among large cap managers. Its benchmark was up 2.1%. Above par Info Tech (Western Digital, Apple Computer, Google) and Healthcare investments helped returns.
  2. The BGI Russell 1000 Index Fund ranked in the 56th percentile among large cap managers (median 2.3%), and matched its benchmark. The Russell 1000 Index had a return of 2.1%.
  3. Chartwell, was up 1.8%, while the Russell 2000 Index returned 1.1%. Chartwell ranked 46th among small cap growth managers (median of 1.6%). Positive attribution primarily came from its Financials sector (8.2% versus 2.1% benchmark return). Greenhill Properites and CB Richard Ellis Group appreciated at least 19.6%.
  4. Goldman Sachs ranked in the 59th percentile among its small cap core peers (median of 1.5%) and it matched its benchmark. The Russell 2000 Index returned 1.1%. Below par Materials (Quanex) and Consumer Staples (Nash Finch) investments were inhibitors of performance. Its intra-quarter trading helped.
  5. The BGI US Debt Index Fund was terminated on December 30th. Proceeds went to fund Fidelity. For the quarter, BGI returned 0.8% while the Lehman Aggregate Index was up 0.6%.
  6. Aberdeen Asset, formerly Deutsche Asset, (0.7%) beat the Lehman Aggregate Index (0.6%) and ranked in the 19th percentile among other core bond managers. Aberdeen's underweight strategy in autos, along with avoidance of other subsectors (particularly in the consumer areas), was positive for relative performance.

- Fourth quarter results were hindered by the following factor:

  1. Brandes returned -1.0% and ranked in the bottom fourth among small cap value managers. The Russell 2000 Index returned 1.1%. Negative performance attribution primarily came from stock selection in the Consumer Discretionary sector (Delphi Automotive, Visteon).
  2. Julius Baer's result of 3.5% was below the MSCI ACWI -ex US (4.4%), and ranked in the 72nd percentile among international equity managers. Relative performance was hurt by its underweight position to Japan, where the equity market rose 11.9% during the quarter. It also incurred negative stock selection in the UK.
  3. Mondrian, returned 2.5%, behind the MSCI AC World -ex US Index (4.4%) and ranked in the 88th percentile among its peers. Mondrian's negative performance alpha came from its Hong Kong and Dutch exposure and underweight position in the Japanese market.
  4. Western Asset Management's quarter was below par. It carried a return of 0.4% and ranked in the bottom decile among core bond managers. The Lehman Aggregate Index was up 0.6%. Credit, TIPS, nondollar bond, emerging market and high yield exposure detracted from relative performance of the portfolio. Its modestly overweight duration and MBS exposure added.
  5. The INVESCO Real Estate-USA Fund returned 2.7% for the quarter, lagged the NCREIF Index (5.4%), and ranked in the third quartile among real estate investments.

CAPITAL MARKET REVIEW: FOURTH QUARTER 2005

ECONOMIC REVIEW

• At the end of November, the trade deficit increased to $64.2 billion--an increase over the $59.0 billion September deficit, but slightly lower than the October deficit of $68.1B. This represents an 8.0% increase over the prior three months. In the fourth quarter, the U.S. dollar strengthened 1.8% against the euro. Similarly, the dollar strengthened against the Japanese yen, increasing 3.9% in the fourth quarter. Finally, the British pound fell 2.9%.

• Third quarter GDP growth increased at an annual rate of 4.1%. This compared with a 3.3% increase for the second quarter of 2005. At the end of December, the year-overyear change of the CPI was 3.4%. Although prices in December continued to rise, their acceleration was slower than November (3.5%) and October (4.3%). This disinflationary trend coincided with a decline in gas, food, and clothing prices, and an acceleration in productivity growth. Unemployment dropped to 4.9% in December, from 5.0% in November. With the exception of October and August 2005, the last time unemployment rate dropped to this level was August 2001.

EQUITY MARKETS REVIEW

• The major U.S. equity indices posted positive returns for the third consecutive quarter. The broader market represented by the S&P 500 increased by 2.1%. Seven of the ten S&P 500 economic sectors had positive fourth quarter returns. The highest returning sectors for the fourth quarter were Materials, gaining 11.0% and Financials, up 8.2%. This replaces last quarter's leaders, Energy and Utilities which posted the lowest quarterly returns, -7.3% and -5.5% respectively. However, Energy was up 31.4% for the year and Utilities at 16.8%, making them the year's leaders. The Communications sector posted the lowest annual return, at -6.2%.

• Among large capitalization stocks, growth outperformed value during the quarter, with the Russell 1000 Growth (R1000G) adding 3.0% versus the Russell 1000 Value (R1000V) up 1.3%. Among smaller capitalization stocks, growth outperformed value, with the R2000G adding 1.6% vs. the R2000V, which gained 0.7%. Large stocks have outperformed small stocks for the trailing 12-month period, with the Russell 1000 returning 6.3% and Russell 2000 returning 4.6%.

• The MSCI EAFE returned 4.1% and 14.0% for the quarter and year, respectively (U.S. $ terms).

FIXED INCOME MARKETS REVIEW

• The Federal Reserve increased the Fed Funds rate by a total of 50 basis points in the fourth quarter, bringing the rate to 4.25%. The new level was the highest since the May 2001 rate of 4.0%. The Fed remained committed to its policy of controlling inflation through a series of measured interest rate hikes, although its December 13 policy statement indicated that the cycle of rate increases might be coming to an end. The yield curve maintained its positive slope throughout all maturities, although it continued to flatten. In the fourth quarter, the spread between the 3-month bills and the benchmark 10- and 30-year bonds narrowed to 32 and 47 basis points, respectively. Comparing this to the third quarter, the spreads on the 10- and 30-ear bonds were 78 and 103 bps, respectively. The yield spread of AA-rated 10-year industrial bonds-to-treasuries was 63 basis points at the end of December and 8 basis points higher from December 31, 2004.

• During the fourth quarter, most of the major bond indices showed minimal returns. The Lehman Aggregate Bond Index (LAB) posted a 0.6% gain, while the Citigroup World Government Bond (CWGB) Index decreased 1.9%. The Lehman Mortgage Backed (LBMB) Index ended the quarter 0.6% higher. High yield corporates, as measured by the Citigroup High Yield (CHY) Index, gained 0.4%. For the trailing 12 months, the LAB was up 2.4%, the CWGB down 6.9%, LBMB up 2.6% and the CHY up 2.1%.

REAL ESTATE MARKETS REVIEW

• REITs continued to show impressive gains for 2005, with a one year annualized return of 12.1%, 26.5% for three years, and 19.0% for five years. The NCREIF Index reported a one year annualized return (ending 9/30/05) of 29.8%, 35.3% for three years, and 8.5% for five years.

• Commercial real estate, while still producing solid returns, may have started to level off, in part because interest rates and capitalization rates have been rising – ending the profits from "flipping" properties. One example is worthy of note as an indication as how much price appreciation has occurred: The office building located at 485 Fifth Avenue in New York City sold for $25 million in 1995 ($135 per square ft.), $37.5 million in 2000, $55.5 million in 2004, and, most recently, $88 million ($475 per square ft.).

The table below compares the Composite Fund Portfolio and Manager Portfolios to their Benchmarks. It also shows how the portfolios rank in their peer universe as of December 31, 2005.

	Last Quarter		Fiscal Year-To-Date		Last Year	
	Return	Rank	Return	Rank	Return	Rank
Composite Fund	1.98%	56	6.04%	51	7.56%	42
Policy Index	*2.15%*	*44*	*6.11%*	*51*	*7.50%*	*45*
BGI Russell 1000 Alpha Tilts	3.32%	30	7.73%	37	9.55%	31
BGI Russell 1000 Index Fund	2.12%	56	6.17%	59	6.31%	57
Large Cap Composite	*2.73%*	*42*	*6.95%*	*48*	*7.96%*	*44*
Russell 1000 Index	*2.12%*	*55*	*6.15%*	*59*	*6.27%*	*58*
Brandes Investment Partners	-0.99%	91	0.93%	96	-6.64%	100
Chartwell Investment Partners	1.76%	42	8.00%	35	7.21%	53
Goldman Sachs Asset Management	1.12%	57	5.28%	69	4.45%	79
Small Cap Composite	*0.77%*	*63*	*4.90%*	*71*	*2.26%*	*91*
Russell 2000 Index	*1.13%*	*56*	*5.88%*	*62*	*4.55%*	*78*
U.S. Equity Composite	*2.32%*	*44*	*6.56%*	*54*	*6.73%*	*56*
Julius Baer Asset Management	3.52%	72	17.66%	37	17.37%	40
Mondrian Investment Partners	2.54%	88	12.35%	79	14.76%	53
International Equity Composite	*3.04%*	*82*	*14.99%*	*59*	*16.04%*	*46*
MSCI ACWI-ex US Index	*4.39%*	*48*	*16.74%*	*43*	*17.11%*	*41*
Total Equity Composite	*2.50%*		*8.53%*		*8.89%*	
Aberdeen Asset Management	0.73%	19	0.22%	39	3.15%	25
Western Asset Management	0.41%	91	0.38%	18	4.07%	3
Lehman Aggregate Index	*0.59%*	*60*	*-0.08%*	*85*	*2.43%*	*73*
U.S. Fixed Income Composite	*0.68%*	*35*	*0.27%*	*47*	*3.32%*	*19*
INVESCO Core Fund	2.68%	59	10.15%	25	21.03%	29
Real Estate Composite	*2.68%*	*59*	*10.14%*	*25*	*20.98%*	*30*
NCREIF Index	*5.43%*	*15*	*10.11%*	*25*	*20.06%*	*33*
Cash Composite	*0.82%*	*76*	*1.65%*	*67*	*3.51%*	*15*
91 Day T-Bill Index	*0.92%*	*56*	*1.75%*	*51*	*3.07%*	*48*

Action: The quarterly investment performance report is informational. No action is required.

6.3 Approval of the Investment Committee's Plan for Fiscal Year 2006/2007

Mr. Cliton presented the Investment Committee its schedule for the coming year reflecting the committee's strategic objectives. He also proposed that annual investment manager reviews be conducted during the Investment Committee rather than the full board. The committee discussed the pros and cons— the educational value to the entire board and face to face contact versus the possible decrease in quality of the interview. Mr. Clifton also opined that agenda items following the interviews seem to be compressed. Ms. Tashman wished that the committee try to make interviews more efficient by reviewing manager presentations and raising more pertinent questions. The committee would like to see less marketing pitch presented by the manger and more product-specific information. The committee did not have a formal opinion regarding holding reviews at the investment committee level but wished to ask the full board for their input regarding the issue.

7.0 Other Business: None

8.0 Investment & Finance Manager's Report: Mr. Clifton reported that (1) *SamCERA*'s growth manager, Chartwell Investment Partners, announced that they are sub-advisors for the Vanguard group in the mid-cap product. (2) Western Asset Management selected two Russian securities from the emerging market LLC, created a Yankee LLC, reasoning that those securities are no longer emerging market securities but investment grade. (3) Aberdeen Asset Management had notified *SamCERA* that its Ford Motor credit has been downgraded in the portfolio. Mr. Clifton elected to keep it in the portfolio per Aberdeen's recommendation. (4) Mr. Clifton announced that he shall be attending client conferences this year. He will provide a schedule at the next board meeting should trustees also wish to attend.

9.0 Adjournment: There being no further business, Mr. Bryan adjourned the committee at 10:38 a.m.