

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

May 27, 2008 – Investment Committee Agenda

PUBLIC SESSION

- 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 - The Investment Committee Shall Review & Discuss
 - 6.1 Monthly Portfolio Performance Report
 - 6.2 Quarterly Investment Performance Analysis for Period Ended March 31, 2008
 - 6.3 Annual Review of *SamCERA's* Fixed Income Asset Class and Investment Managers Roundtable Discussion
 - 6.3 a Annual Investment Manager Review – Aberdeen Asset Management
(Interviewed by the Investment Committee)
 - 6.3 b Annual Investment Manager Review – Pyramis Global Advisors
(Interviewed by the Investment Committee)
 - 6.3 c Annual Investment Manager Review – Western Asset Management
(Interviewed by the Board)
 - 6.4 Approval of Large Cap Manager Structure
 - 6.5 Approval of Topics for Manager Review – Julius Baer Investment Management
 - 6.6 Approval of Topics for Manager Review –Mondrian Investment Partners
 - 6.7 Approval of Topics for Manager Review –
 - 6.7 a INVESCO Realty Advisors
 - 6.7 b Brandes Investment Partners
 - 6.7 c Chartwell Investment Partners
 - 6.8 Approval of Topics for Investment Consultant Review – Strategic Investment Solutions
- 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:** Ms. Jadallah called the Public Session of the Investment Committee of the Board of Retirement to order at 8:30 a.m. May 27, 2008, in Franklin Templeton Investments, Building 920, Room A, One Franklin Parkway, San Mateo, California.
- 2.0 **Roll Call:** Ms. Arnott for Mr. Buffington, Ms. Jadallah and Ms. Tashman. *Excused:* Ms. Salas *Other Board Members in Attendance:* Mr. Murphy. *Staff:* Mr. Bailey, Mr. Clifton and Mr. Hood. *Consultants:* Mr. Meier and Mr. Thomas, Strategic Investment Solutions. *Public:* None. *Retirees:* None.

Mr. Clifton reported that Ms. Tashman, Board Chair, has appointed Ms. Jadallah to serve as chair of the Investment Committee. With her election to Board Chair at the April meeting, Ms. Tashman decided to relinquish her chairmanship of the Investment Committee and focus on her role as Board Chair.

3.0 **Approval of the Minutes: Motion** by Tashman, second by Arnott, carried unanimously to approve the minutes of the April 21, 2008, Investment Committee meeting, as submitted.

4.0 **Oral Communications From the Committee:** None.

5.0 **Oral Communications From the Public:** None.

Ms. Jadallah then took up agenda item 6.3, *SamCERA's* Fixed Income Investment Manager Roundtable Discussion.

6.1 **Monthly Portfolio Performance Report:** Mr. Clifton reported that *SamCERA's* 2.85% Total Fund Return for April 2008 underperformed the Total Plan Policy Benchmark return of 3.49%. The fund's return for the trailing twelve months is -3.24%, which is 1,099 basis points below the Actuarial Discount Rate, 7.75%, and 417 basis points below *SamCERA's* Total Plan Policy Benchmark of 0.93%. The realized return continues to trail both the policy return and the actuarial assumption rate for the trailing-twelve-month period.

Investors built on the optimism that took hold following the rescue of Bear Stearns in mid-March. Subsequent improvements in the financial markets were apparently substantial enough to convince many investors that the worst is behind us. Oil prices have continued to rise, despite the US economic slowdown. They went through the \$120 mark and are being driven up by supply concerns, sustained demand growth and the weakness of the US dollar.

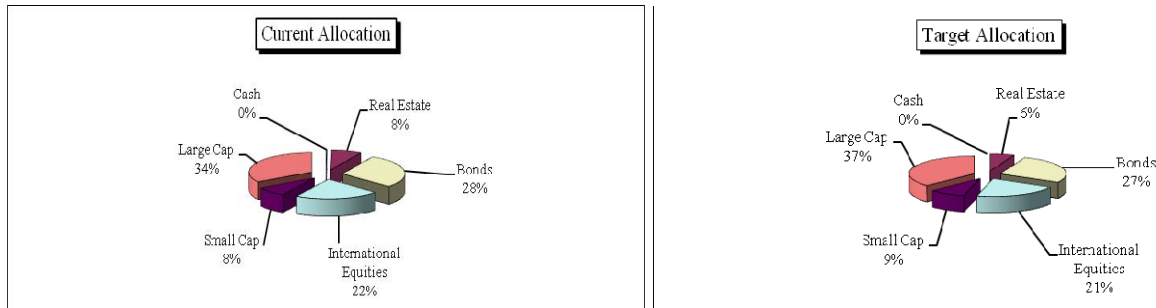
The table presented below shows the composite returns:

April 30, 2008	Market Value	One Month	Trailing Three Months	Trailing Six Months	Trailing Twelve Months
Equity Aggregate	\$1,323,132,106	4.53%	2.02%	-10.30%	-6.76%
Equity Composite		5.18%	2.43%	-9.92%	3.59%
Variance		-0.65%	-0.41%	-0.38%	-10.35%
Fixed Income Aggregate	\$594,195,840	0.14%	-1.88%	0.42%	1.76%
Fixed Income Composite		-0.21%	0.27%	4.08%	6.87%
Variance		0.35%	-2.15%	-3.66%	-5.11%
Real Estate Aggregate	\$166,888,025	0.00%	1.32%	3.49%	10.74%
NCREIF (one quarter lag)		0.00%	1.60%	4.86%	13.58%
Variance		0.00%	-0.28%	-1.37%	-2.84%
Cash Aggregate	\$5,282,683	0.25%	0.79%	1.96%	4.10%
91 Day Treasury Bill		0.11%	0.49%	1.75%	4.28%
Variance		0.14%	0.30%	0.21%	-0.18%
Total Fund Returns	\$2,089,498,654	2.85%	0.81%	-6.50%	-3.24%
Total Plan Policy		3.49%	2.15%	-5.24%	0.93%
Variance		-0.64%	-1.34%	-1.26%	-4.17%

Performance versus Actuarial Discount Rate

Total Fund Returns		2.85%	0.81%	-6.50%	-3.24%
Actuarial Discount Rate		0.62%	1.88%	3.80%	7.75%
Variance		2.23%	-1.07%	-10.30%	-10.99%

SamCERA's current asset allocation is summarized as follows:



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

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Quarterly Investment Performance Analysis for Period Ended March 31, 2008: Mr. Thomas from Strategic Investment Solutions was present to review the quarterly investment performance report for the period ended March 31, 2008. The composite fund returned -6.1% in the first quarter of 2008 and ranked 80th among other public funds greater than \$100 million (median of -5.4%). The fund trailed its policy index (-5.6%) during this time period. Longer term, the three and five-year returns of 7.1% (73rd percentile) and 11.4% (54th percentile), respectively, were below and at median among large public plans (8.0% and 11.4%).

Summary details from Strategic Investment Solutions' quarterly performance report for the period ended March 31, 2008, is as follows:

	Last Quarter		One Year		Last 3 Years	
	Return	Rank	Return	Rank	Return	Rank
Composite Fund	-6.07%	80	-3.27%	97	7.11%	73
<i>Policy Index</i>	-5.65%	66	0.17%	53	8.26%	41
BGI Russell 1000 Alpha Tilts	-9.33%	30	-9.74%	79	5.06%	80
BGI Russell 1000 Index Fund	-9.48%	42	-5.34%	59	6.25%	44
<i>Large Cap Composite</i>	-9.31%	29	-9.02%	77	5.10%	77
<i>Russell 1000 Index</i>	-9.48%	43	-5.40%	60	6.19%	45
Brandes Investment Partners	-2.93%	5	-26.38%	100	-3.99%	100
Chartwell Investment Partners	-12.84%	77	-2.24%	9	7.50%	34
<i>Small Cap Composite</i>	-9.39%	48	-18.29%	86	0.76%	94
<i>Russell 2000 Index</i>	-9.90%	53	-13.00%	64	5.06%	63
<i>U.S. Equity Composite</i>	-9.32%	36	-10.82%	75	4.28%	84
Julius Baer Asset Management	-9.57%	69	2.03%	31	18.16%	21
Mondrian Investment Partners	-8.33%	40	0.56%	38	15.58%	39
<i>International Equity Composite</i>	-8.95%	56	1.30%	35	16.89%	30
<i>MSCI ACWI-ex US Index Free</i>	-9.06%	59	2.58%	27	16.49%	31
<i>Total Equity Composite</i>	-9.19%	N/A	-7.16%	N/A	7.58%	N/A
Aberdeen Asset Management	-1.47%	93	2.13%	91	3.99%	92
Pyramis Global Advisors	0.78%	75	3.11%	85	N/A	N/A
Western Asset Management	-1.49%	94	1.27%	95	4.09%	89
<i>U.S. Fixed Income Composite</i>	-0.73%	79	2.17%	81	4.06%	87
<i>Lehman Aggregate Index</i>	2.17%	38	7.67%	40	5.48%	49
INVESCO Core Fund	1.32%	38	10.74%	58	16.40%	38
<i>Real Estate Composite</i>	1.32%	38	10.74%	58	16.40%	38
<i>NCREIF Index</i>	1.60%	31	13.58%	35	16.75%	36
<i>Cash Composite</i>	0.90%	43	4.27%	75	4.04%	82
<i>91 Day T-Bill Index</i>	0.88%	49	4.62%	57	4.41%	59

Ms. Jadallah then took up agenda item 9.0.

6.3 **Annual Review of SamCERA's Fixed Income Asset Class and Investment Managers**

Roundtable Discussion: Mr. Clifton presented the investment managers present for SamCERA's fixed income roundtable discussion. Mr. Clifton hoped that the roundtable would help aid the committee in a better understanding of the amount of risk involved in the Association's current fixed income portfolio. Mr. Thomas added that the committee would like to learn more about the individual securities within the portfolios and sought information to explain why SamCERA's overall fixed income portfolio, which was intended to be low-risk, has severely underperformed relative to the Lehman Aggregate benchmark.

During the roundtable, the investment managers discussed current economic issues, the impact on fixed income markets with the market dislocations of 2007, portfolio management, risk management and the general outlook for the economy and the market.

6.3a **Annual Investment Manager Review – Aberdeen Asset Management:** Christopher Gagnier, Senior Portfolio Manager, and Boris Karol, Portfolio Manager, were present for Aberdeen Asset Management's annual review.

Mr. Karol provided a brief organizational overview. He reported that the product was closed to new business in September 2007. He attributed this to the fact that the product had reached its growth target of 15-20% annual growth and also due to the volatility in the market.

Mr. Gagnier then performed a brief overview of the fixed income team. He discussed the additions of two senior portfolio managers and various sector managers and analysts. He also mentioned that Steve Illott left the firm in March 2008 as Head of Fixed Income in order to start his own alternatives business. Gary Bartlett is now US CEO and Head of Fixed Income.

Mr. Gagnier then discussed the portfolio's performance. The fund significantly underperformed the benchmark in the second half of 2007 and first quarter of 2008. As of March 31, 2008, the portfolio underperformed the Lehman Aggregate by 559 basis points. He then thoroughly reviewed the three main drivers of performance — (1) residential mortgage backed securities: prime hybrid ARM super seniors, (2) commercial mortgaged back securities: AAA, BBB and (3) financial hybrid capital securities. Mr. Gagnier then responded to trustees' questions.

6.3b **Annual Investment Manager Review – Pyramis Global Advisors:** Art Greenwood, Senior Vice-President, Relationship Manager, Chris Pariseault, Fixed Income Investment Director, and Daniel Tremblay, Institutional Portfolio Manager were present for Pyramis Global Advisors' annual review.

Mr. Pariseault performed an overview of the portfolio's performance. The one-year performance as of March 31, 2008, trailed the benchmark by 456 basis points. An overweight to the spread sectors detracted as Treasuries continued to rally. He also added that sub-prime and CMBS exposure detracted during the first quarter of 2008. Out of index exposure to TIPs was a significant contributor and bulleted yield curve exposure was also additive as the curve steepened further. Credit was neutral as the fund's positioning was selective.

Mr. Tremblay then discussed and explained the characteristics of the portfolio: rating, sector, credit and sub-prime allocations. He then answered trustee questions.

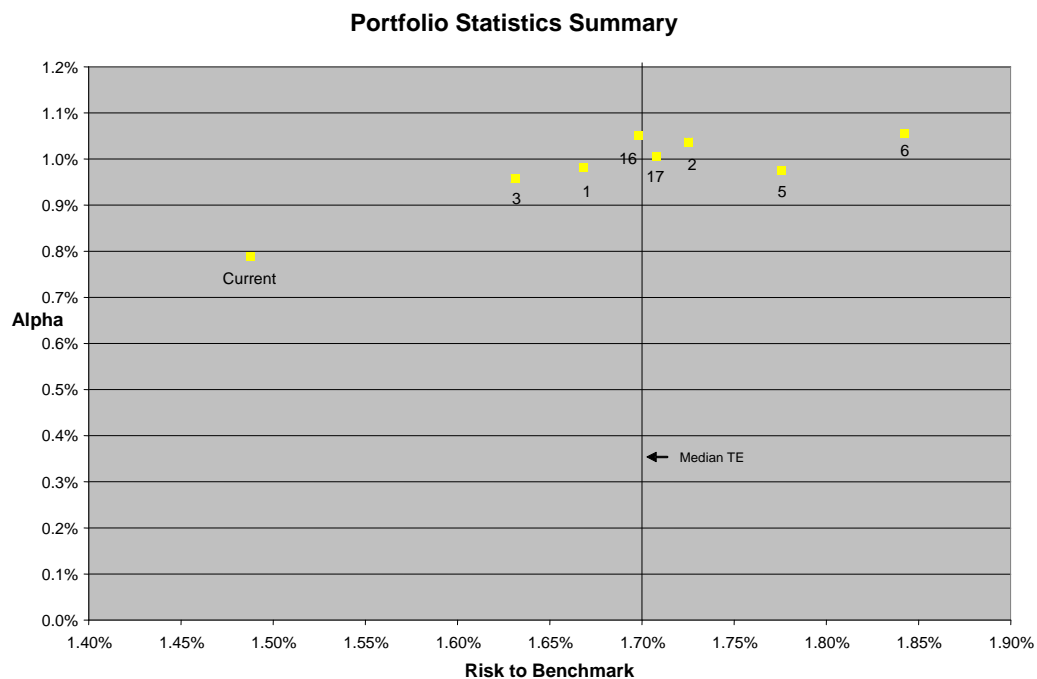
6.3c **Annual Investment Manager Review – Western Asset Management:** Western Asset Management’s annual review was conducted at the Board of Retirement meeting later that day.

6.4 **Approval of Large Cap Manager Structure:** Mr. Meier and Mr. Thomas reviewed *SamCERA*’s US equity large cap manager structure. They discussed the following large cap alternatives, which are expressed as a percentage of *SamCERA*’s large cap allocation:

- 1) 35% BGI R1000 Index, 25% BGI Alpha Tilts, 20% LC Growth, 20% LC Value
- 2) 35% BGI R1000 Index, 20% BGI Alpha Tilts, 20% LC Growth, 20% LC Value, 5% 130/30
- 3) 40% BGI R1000 Index, 20% BGI Alpha Tilts, 20% LC Growth, 20% LC Value
- 5) 50% BGI R1000 Index, 25% LC Growth, 25% LC Value
- 6) 45% BGI R1000 Index, 25% LC Growth, 25% LC Value, 5% 130/30
- 16) 30% BGI R1000 Index, 30% BGI Alpha Tilts, 15% LC Growth, 15% LC Value, 10% 130/30
- 17) 30% BGI R1000 Index, 30% BGI Alpha Tilts, 20% LC Growth, 20% LC Value

The current large cap structure is 80% BGI Alpha Tilts, 20% BGI R1000 Index

Below is where these alternatives appear in risk/return space:



Ms. Jadallah inquired about the significantly higher Manager Event Risk in alternative 16 and 17 relative to the other alternative structures. Mr. Meier explained that the Manager Event Risk in the two structures is not due to the enhanced allocation but more due to the decreased allocation to passive and increased allocation to active managers. Ms. Jadallah then asked the committee for their comments regarding the various alternatives. The committee discussed 130/30. Ms. Jadallah stated that she was neutral on 130/30. Ms. Jadallah eliminated alternative 5 and 6 due to their higher than median tracking error and its zero allocation to an enhanced index. She indicated preferences towards alternatives 3, 16 and 17 for a sound long-term large cap allocation. In reference to alternative 16 (30% BGI R1000 Index, 30% BGI Alpha Tilts, 15% LC Growth, 15% LC Value, 10%

130/30), Ms. Tashman said that she would not be opposed to interviewing 130/30 managers. If the committee does not find a suitable 130/30 manager, she suggested that the committee then possibly select alternative 17 (30% BGI R1000 Index, 30% BGI Alpha Tilts, 20% LC Growth, 20% LC Value) or alternative 3 (40% BGI R1000 Index, 20% BGI Alpha Tilts, 20% LC Growth, 20% LC Value) as the fund's large cap structure. Ms. Arnott and Ms. Tashman both expressed their preference to alternative 3 for its larger allocation to the index. Despite her opposition to a 130/30 product, Ms. Arnott also was willing to invest time interviewing 130/30 candidates during the large cap manager search process. Ms. Tashman then stated she would consider the possibility of a larger allocation to the large cap passive index in order to look at other instruments in the portfolio, for example, international equity or real estate, to incorporate more risk into the entire portfolio.

Following extensive discussion, **motion** by Tashman, second by Arnott, carried unanimously to recommend to the board to allocate 60% of the large cap assets to an index and enhanced index while the other 40% of large cap assets will be allocated to active managers in the form of large cap value, large cap growth and possibly 130/30.

- 6.5 **Approval of Topics for Manager Review – Julius Baer Investment Management:** Mr. Clifton presented the list of questions for Julius Baer Investment Management's annual review, which will occur in July. The committee did not recommend any changes to the list of topics.

Without objection, Ms. Jadallah approved the topics for Julius Baer Investment Management to be held at the July Investment Committee.

- 6.6 **Approval of Topics for Manager Review –Mondrian Investment Partners:** Mr. Clifton presented the topics for Mondrian Investment Partner's annual review which will occur in July. The committee did not recommend any changes to the list of topics.

Without objection, Ms. Jadallah approved the topics for Mondrian's annual review to be held at the July Investment Committee.

- 6.7 **Approval of Topics for Manager Review:**

- 6.7a **INVESCO Realty Advisors:** Mr. Clifton presented the Compliance Certification Statement (CCS) and a series of questions designed for INVESCO Realty Advisors' annual review. Pursuant to board direction, the CCS had been modified from the one in Appendix D of *SamCERA's* Investment Policy. The modified version strives to include only questions that may apply to INVESCO's asset mandate.

Without objection, Ms. Jadallah approved the topics for INVESCO's annual review.

- 6.7b **Brandes Investment Partners:** Mr. Clifton presented the list of questions for Brandes Investment Partner's annual review. He also presented the Compliance Certification Statement which had been modified to inquire about Brandes' portfolio. Ms. Jadallah then recommended two additions to the list of topics.

Without objection, Ms. Jadallah approved the topics for Brandes' annual review.

- 6.7c **Chartwell Investment Partners:** Mr. Clifton presented the list of questions for Chartwell Investment Partner's annual review. He also presented the Compliance Certification Statement which had been modified to inquire about Chartwell's portfolio. Ms. Jadallah also recommended that the list include questions about Chartwell's outlook regarding the small cap growth market.

Without objection, Ms. Jadallah approved the topics for Chartwell's annual review.

- 6.8 **Approval of Topics for Investment Consultant Review – Strategic Investment Solutions:** Mr. Clifton presented a suggested list of questions for Strategic Investment Solutions' annual review. Ms. Jadallah added two questions to the list of topics regarding: (1) SIS' plans to help *SamCERA* with its real estate portfolio and (2) SIS' plans to add a second consultant to the *SamCERA* team. Ms. Tashman also wanted to add a question regarding SIS performing an alternatives search.

Without objection, Ms. Jadallah approved the topics for Strategic Investment Solution's annual review.

- 7.0 **Other Business:** None.

- 8.0 **Investment & Finance Manager's Report:** Mr. Clifton reported that Julius Baer will now be called Artio Global Investors effective June 15th.

Ms. Jadallah then took up agenda item 6.1.

- 9.0 **Adjournment:** There being no further business, Ms. Jadallah adjourned the committee at 12:20 p.m.

MARGARET JADALLAH, CHAIR