CALL TO ORDER   Acting Chair Richardson called the meeting to order at 9:06 A.M.

ROLL CALL   PRESENT: Bolger, Brenk, Given, Gladstern, Haim, McFarland, Richardson, Webb (retiree alternate)

ABSENT: Chair Phillips

A. OPEN TIME FOR PUBLIC EXPRESSION
Note: The public may also address the Committee regarding any agenda item when the Committee considers the item.

No public comment.

B. MANAGER ANNUAL REPORTS
1. Sector Overview – Private Equity – Callan Associates
Gary Robertson and Michael Bise of Callan Associates were introduced to the Board. Mr. Bise reported that the private equity portfolio is still developing, with 19% of the total commitment of $200 million paid in as of June 30, 2011. Across the portfolio’s forty-one partnerships, most investments are allocated relatively equally among Special Situations, Buyouts, and Venture Capital/Growth. By design, the two private equity managers complement one another in that the Pathway portfolio is concentrated toward Buyouts at 47%, while the Abbott portfolio is more weighted to Special Situations. The portfolios are well diversified across the United States and Western Europe, with some exposure to developing markets. Industry diversification is broad, with the largest exposure to basic industry.

The expectation for the private equity portfolio is long-term returns in excess of the public equity market and diversification, according to Mr. Callahan. He explained that in private equity, the return is received in distributions as the portfolio matures over time. Trustee Gladstern asked if fees are factored in, and he explained that in the early stages fees add to the J-curve effect, so that analyzing return is premature at this time.

Mr. Bise stated that the distributions from private equity are dependent on a strong public equity market, with value captured during favorable cycles.
2. **Abbott Capital – Private Equity**
Charles van Horne, Abbott Capital Management Managing Director, discussed the firm’s methodology for identifying suitable investment opportunities. For the Abbott Capital Private Equity Fund VI, the initial investment period was expected to be 3 to 5 years. The fund may be entirely committed by the end of June 2012, and it is expected to have a life of 12 years. Eventually the fund will be composed of 25 to 45% in venture capital equity with the balance in Special Situations, according to Mr. van Horne. Mr. van Horne explained that no foreign debt is in the fund.

Jonathan Roth, President and Managing Director, stated that 23 of a final 35 core managers have been selected. Buyouts and Special Situations involve mature companies that are being restructured or growing. Mr. Bise reviewed Special Situation funds and the nature of their investments. What is necessary to uncover inherent value, according to Mr. Bise, is the expertise to evaluate the potential of investments in small firms.

Mr. Van Horne announced that Abbott Capital would be launching Fund VII in 2012 and advised that non-binding intents to invest will be available. Rolling private equity fund investing captures diversification over time, he said.

The annual meeting will be in Menlo Park June 5 and 6 and trustees are invited to attend.

Acting Chair Richardson recessed the meeting for a break at 10:05 A.M., reconvening at 10:14 A.M.

3. **Pathway Capital – Private Equity**
Jim Reinhardt, Pathway Capital Senior Managing Director, introduced Senior Vice President Pete Veravanich to review the Pathway Private Equity Fund 2008. The business model for the fund is based on the concept of the scarcity of suitable investments, according to Mr. Veravanich. Efficiency prevents over-diversification, which can lead to average returns, he said. Mr. Reinhardt reviewed the decision-making process, which he said is deliberate and leads to a predictable track record. Investments, he added, are focused on firms with exceptional and stable management teams, sound business models, extraordinary resources, and long-term track records.

At maturity the fund will be comprised of over 500 companies and diversified as to geography and strategy, according to Mr. Veravanich. Significant capital contributions were made in the third quarter of 2011 based on strong investment activity across a number of partnerships. He expects the fund to be fully committed over the next 12 to 18 months. Mr. Veravanich reviewed targets and ranges of Buyouts, Venture Capital, and Special Situations.

Trustee Bolger was excused from the meeting at 10:43 A.M.
Responding to Trustee Haim’s inquiries, Mr. Reinhardt said that the oversight process includes frequent communication with general partners as well as close control over accounting for portfolio companies.

In closing, Mr. Reinhardt said that uncertainty and dislocation in the private equity market remains, though it is not as severe as in 2009 and 2010.

Mr. Reinhardt announced that Pathway will initiate a new fund in mid-2012.

4. Clifton – Futures Overlay
Jack Hansen, Chief Investment Officer and Principal for the Clifton Group, said that the firm’s asset and client growth continues and management is stable. The purpose of the Futures Overlay Program, he stated, is to eliminate excess fund cash exposures on a daily basis without using leverage. The program has returned on average 0.23% per year since inception, he reported.

Mr. Hansen stated that Clifton achieves higher expected returns by meaningfully increasing equity exposure of residual portfolio cash and liquidity needs. Also, transitions and reallocations are managed to push the portfolio toward target positions, he stated. Mr. Hansen observed that many clients take advantage of the program’s automatic rebalancing feature, and he recommended that MCERA consider that approach. The matter may be addressed at the March 2012 Strategic Workshop, said Mr. Wickman.

Examples of recent futures overlay program activities include efficient and risk controlled management of market exposure during incremental funding of the Eaton Vance Emerging Markets Portfolio. Also, Clifton assisted with the transition out of the market neutral program. Furthermore, the core liquidity overlay program was modified to direct new cash to underweight asset classes and liquidate exposure from overweight asset classes.

C. INVESTMENT CONSULTANT PERFORMANCE UPDATE

Investment Consultant Kevin Dunne, Callan Associates Vice President, reviewed recent modifications to the investment program such as the adjustment to the U.S. debt downgrade of setting relative measures for fixed income holdings. Other actions include moving the RCM portfolio from core to select growth, selection of two new core real estate managers, and eliminating foreign debt exposure in the cash account.

Mr. Dunne stated that the third quarter of 2011 saw equity market declines and the end of the Fed’s quantitative easing program, QE2. The Fed is following QE2 with credit-market activities to ease long-term interest rates to assist consumers with mortgage debt. There are concerns that the Greek debt crisis may spread, he said. Responding to Trustee Brenk’s inquiry, he said that low interest rates are expected to constrain fixed income returns. According to Callan Executive Vice President Jim Callahan, the fixed income managers will be able to add value relative to what the market offers. In the equity
markets, recent earnings results have led to relatively low price/earnings ratios, according to Mr. Dunne.

Mr. Dunne reviewed MCERA’s portfolio noting that there is approximately 60% allocated to equities. The fixed income portfolio showed slight underperformance to the benchmark but exceeded most peers. The Fund’s equity holdings declined in the third quarter and have shown recovery in October, with small caps and emerging markets taking the lead.

Trustee Bolger rejoined the meeting at 11:45 A.M.

Trustee Given inquired about the relative merits of active and passive management in the large cap equity space. Mr. Callahan replied that over 15 years Dodge & Cox shows value added of 2% per year and RCM is slightly underperforming the benchmark net of fees. Taken together the portfolios have added value to the Fund, and Mr. Callahan expects both to outperform net of fees over time. The large cap space is a natural area to add passive exposure, which MCERA has done by investing in the S&P 500 index.

When Trustee Haim suggested increasing the small cap and international equity allocation, Mr. Callahan said he could support increasing the international allocation, but recommended maintaining the strategy of matching the ratio of large cap to small cap to that of the equity markets. The reason for this is that a capitalization bias would cause performance to deviate from the market, he added. Trustee Richardson agreed, stating that neutrality is the safest strategy.

Ms. Gladstern inquired about potential additional private equity commitments, with Mr. Callahan advising that vintage-year diversification will be advisable once distributions allow the program to become self-sustaining. Planning for this stage of the private equity program may be discussed at the Spring 2012 Strategic Workshop.

Acting Chair Richardson recessed the meeting for lunch at 12:30 P.M., reconvening at 12:55 P.M.

D. OLD BUSINESS
1. S&P 500 High Yield Fund – State Street (Action)
Consider and take possible action to allocate funds to S&P 500 high yield fund

Mr. Dunne presented information on a variety of large cap indices for the Committee’s consideration. The most recognized index is the S&P 500 index, and others have been developed according to different metrics such as high dividend yield. One such index is the S&P 1500 High Yield Dividend Aristocrat index, which is designed to track the 60 highest dividend yielding S&P 1500 constituents that have consistent dividend policies. Mr. Dunne also reviewed the best-performing Russell 1000 Equal Weight index, which seeks to balance sectors. Mr. Dunne reviewed the relative performance and volatility of each index compared to the S&P 500.
Mr. Callahan noted that alternative indices have a market bias and the purpose of the bias should be well understood. An index with a bias to the market is an active strategy, he said, and may be better left to active managers who have flexibility to make portfolio decisions based on the attractiveness of stocks or sectors rather than rules based quantitatively oriented indices. An alternative to index investing is to have the current active managers mimic the bias of these indices.

Because the portfolio is over weighted to equities relative to peers, Mr. Callahan recommended other options to achieve diversification. He encouraged the Board to consider this approach, as many peers have done over the last 10 years, as a long-term strategy. Trustee Haim, supported by Trustee Brenk, recommended following the investment consultant’s guidance by considering these alternative investment approaches at the spring 2012 Strategic Workshop.

E. **NEW BUSINESS**
   1. **Exposure to Non-U.S. Investment Issues Presentation – Callan Associates**
      Consider and discuss MCERA’s current exposure to non-US investment-related banks, debt and overall investments

      The Board requested an analysis of the Fund’s non-U.S. exposure. Mr. Dunne explained that of the Fund’s 1.7% exposure, the largest positions are banks and insurance companies in the Morgan Stanley portfolio, and banks and sovereign debt in the Western Asset portfolio. Four managers reported no exposure, and the cash account exposure has been eliminated.

      Trustees Webb and Haim discussed potential methods of reducing risk. Mr. Callahan indicated that reducing overall equity exposure would be one alternative. Mr. Haim suggested discussing the foreign financial-related holdings with the portfolio managers

      2. **Consider and take possible action on Amendment to Investment Policy Statement re: RCM U.S. Large Cap Select Growth Statement of Objectives, Guidelines & Procedures (Action)**
      Mr. Wickman advised that the information for the RCM portfolio in the Investment Policy Statement is being updated in accordance with the change in strategy from core growth to select growth.

      It was M/S Given/Richardson to approve the amendment to the Investment Policy Statement regarding RCM U.S. Large Cap Select Growth Statement of Objectives, Guidelines & Procedures. The motion was approved by unanimous vote.

      Conduct three-year Policy review

      Mr. Wickman advised that the Governance Committee determined that the review of the Investment Code of Conduct and Insider Trading Policy should be conducted by the Investment Committee. Trustee Bolger indicated that the application of the
Policy is not directly related to the Board, and Trustee Given observed that Policy provisions are in accordance with its development. There was discussion about whether any scenarios that the Board may be presented with would be in violation of the Policy. Based on discussions, there was agreement that the Governance Committee should review the Policy to clarify its interpretation.

There being no further business, Acting Chair Richardson adjourned the meeting at 2:15 P.M.

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Gerald Richardson, Acting Chair  Attest: Jeff Wickman
                                          Retirement Administrator