CALL TO ORDER  Acting Chair Bolger called the meeting to order at 9:00 A.M.

ROLL CALL  PRESENT:  Bolger, Brenk, Cooper, Given, Gladstern, McFarland, Piombo (alternate safety), Shaw (ex officio alternate), Smith, Stevens, Webb (alternate retiree)

ABSENT:  Richardson

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.  OLD BUSINESS  
None.

C.  INVESTMENT CONSULTANT QUARTERLY REPORT AND PERFORMANCE UPDATE  
For quarter ending December 31, 2012

Anne Heaphy, Vice President for Callan Associates, reviewed economic and capital market conditions through the fourth quarter of 2012. Factors improving the economy included better-than-expected performance in China which she said impacts the global economy. Also, European policy makers signaled their intent to keep the Eurozone intact. For the calendar year 2012, there were favorable returns for fixed income, real estate, and equity assets, according to Ms. Heaphy.

Trustee Stevens observed that domestic fixed income managers significantly outperformed benchmarks and inquired about the risk level in the portfolios. In response, Ms. Heaphy explained that the underweight to U.S. Treasurys led to relatively favorable performance as corporates outperformed. Jim Callahan, Executive Vice President of Callan Associates, expressed confidence in the risk level of the fixed income portfolios.

Trustee Given joined the meeting at 9:11 A.M.
Ms. Heaphy reported that MCERA’s Total Fund return for the calendar year 2012 was 14.9% net of fees, outperforming the benchmark return of 12.9%. Ms. Heaphy noted that the rally in equities helped total fund performance. The equity rally continued through February 28, 2013, with notable outperformance by the Fund’s international equity portfolio.

Mr. Callahan observed that the overall equity allocation is on target and domestic equity asset levels will normalize as the private equity program is funded. Changes in the equity mix during the quarter included moving assets from two actively managed large cap equity portfolios in portions to the S&P 500 index and to small cap managers.

A detailed review of historical asset allocations, long-term returns, and performance attribution by Ms. Heaphy followed. For the calendar year the manager effect was strong. Mr. Callahan reviewed the nature of returns from the private equity program as it emerges from the J-curve effect.

A discussion of the investment return assumption followed. There was general agreement to consider the matter prior to beginning the June 30, 2013 actuarial valuation in the Fall of 2013. Trustee Stevens indicated that she would favor lowering the assumed rate of return in view of the difficulty in achieving that return over the past 17 years. Trustee Smith observed that from a historical perspective the market downturn in 2008 has given pause to employers with regard to benefits.

Due to recent outperformance of the Woodmont portfolio, removal from the watch list will be considered by the Governance Committee at its next meeting. The Committee will also discuss establishing processes for how managers can be removed from the watch list. There was a general discussion about Woodmont as an asset manager and MCERA’s contractual relationship with Woodmont. Mr. Callahan indicated that it is unusual for the Board to have the sole fiduciary authority over buy/sell decisions for real estate.

Further historical analysis of the portfolio was provided by Uvan Tseng, Vice President for Callan Associates, who compared performance of asset classes to benchmarks and reviewed risk-adjusted rankings and relative market-cap weightings. The positive manager effect in the small cap equity portfolio was noted. According to Mr. Callahan the quarterly analysis can flag style drift in a portfolio manager’s strategy. The portfolio has been riskier than peers historically, he said, but is less so now due to recent changes that have been made.

Acting Chair Bolger recessed the meeting for a break at 10:45 A.M., reconvening at 11:02 A.M. and directing deliberations to Agenda Item D.2.

D. NEW BUSINESS

2. System Risk Review – SF Sentry
   Presentation and discussion of system risk analysis

   David Hansen of SF Sentry presented the risk analysis of the Fund for the quarter ending November 30, 2012. Mr. Hansen noted that the volatility index spiked to
22.72 during the quarter but remains at relatively low levels, ending the quarter at
18. Macro headlines reviewed by Mr. Hansen included the linking of asset
purchases by the Federal Reserve Board to unemployment and inflation rates.

Mr. Wickman discussed a recent meeting that he, Trustees Bolger and Gladstern had
with GMI Ratings. GMI utilizes different sources of publicly available data to rank
companies in areas like accounting and governance. Mr. Wickman asked SF Sentry
if they could look at the tool and provide an analysis to the Investment Committee on
how it could be incorporated in their current risk analysis. Mr. Hansen explained
that GMI Ratings are used by some investment managers to screen potential
investments. Risk factors considered in the tool include corporate governance,
litigation, dual role of CEO and Chairman, share repurchases, and revenue and
expense recognition. Mr. Hansen ran MCERA’s portfolio through the tool looking
for risk areas in accounting and governance. Some MCERA holdings showed with
aggressive ratings, particularly in the small cap portfolio. It was noted that the
overall percentage of aggressive GMI Ratings was less than 10%.

Mr. Holmes reported on several risk-based metrics. The cash level in the Wellington
portfolio has come down from previous levels as the duration lengthens. The
equity stress test shows the Total Fund is less risky as a result of the increased
allocation to the S&P 500 Index. Interest rate risk is slightly higher. Equities
continue to drive risk in the portfolio and the private equity allocation is increasing.
Consumer staples and consumer discretionary are overweight in the equity class. In
response to Ms. Bolger’s inquiry, Mr. Callahan explained that staples are more
defensive positions, while the consumer discretionary sector is tied to market cycles.
The value of top ten holdings has fallen as a percentage of the portfolio indicating
increased diversification of the Fund.

Ms. Bolger pointed to the move in the fixed income portfolio to U.S Treasurys from
riskier holdings. This is a defensive strategy, according to Mr. Hansen, and shows
the managers’ skills in actively managing the portfolios.

Acting Chair Bolger directed deliberations to NEW BUSINESS, Agenda Item D.1.

1. **Real Asset Strategies (Action)**
   Consider and take possible action to invest in alternative real assets

   Mr. Wickman stated that the presentation on real asset strategies is a follow-up to
previous discussions. Mr. Callahan presented the following overview of real assets
strategies.

   Real assets can serve as diversifiers and for hedging potential inflation in the years
ahead. Since the financial crisis of 2008 there has been concern about the potential
for rising inflation. Real assets include liquid financial assets that can be backed by
physical assets such as TIPs, REITs, and natural resources equities, or illiquid
physical assets where investors have direct ownership of tangible assets such as real
estate, timber, or oil properties. Mr. Callahan reviewed correlations of various real
assets with the CPI, noting the relatively high correlation of commodities as
compared with other real asset classes in recent history. He added that TIPs are currently not favorably priced and are subject to price volatility.

Mr. Callahan stated that the question for the Committee is whether to add to inflation-hedging strategies in anticipation of a rise in inflation. Current portfolio inflation hedges include real estate, domestic and international equity exposure to the energy sector, and the ability of fixed income managers to purchase TIPs. For the long term, these allocations are appropriately balanced to long-term liabilities, according to Mr. Callahan.

Trustee Cooper was excused from the meeting at 12:18 P.M.

In summary, Mr. Callahan discussed the advantages of a diversified approach to public real assets that would limit the number of managers and allow for a flexible asset mix. For private real assets, liquidity is lower and fees are higher, he stated. A fund-of-fund manager could be considered that would involve implementation risk. Since diversification is needed, however, alternative real asset strategies may be more suited to larger funds, he advised.

Acting Chair Bolger recessed the meeting for a break at 12:38 P.M., reconvening at 1:00 P.M. for a working lunch.

Trustee Piombo was excused from the meeting at 12:50 P.M.

After discussions among the trustees on real asset strategies, there was no consensus on the appropriate approach. Ms. Bolger and Trustees Given and Gladstern favored using diversified liquid public assets, and Ms. Bolger also expressed interest in a liquid total return fund that is valued daily. In response to Trustee Gladstern’s suggestion, Mr. Callahan offered to conduct a search to look into more options. Trustee Stevens spoke to the value of dedicating a small portion of the portfolio to a defensive posture and favors infrastructure for diversification. Mr. Callahan cautioned that Master Limited Partnerships may be too highly priced. Trustee Smith suggested having an academic expert present an analysis of portfolio allocation.

Acting Chair Bolger’s request for a straw vote resulted in a 6-1 vote in favor of pursuing a new real asset investment. More discussion followed, with Trustee Given recommending further diversification for the Fund with an actively managed real return strategy. Mr. Wickman noted that the Committee was not expressing a clear consensus on whether to develop a real asset allocation within MCERA’s portfolio. There was general agreement with his recommendation to delay the decision on real assets until the asset allocation discussion at the Strategic Workshop.
Acting Chair Bolger redirected deliberations to Agenda Item C, INVESTMENT CONSULTANT QUARTERLY REPORT AND PERFORMANCE UPDATE.

Mr. Tseng reported the Initial Public Offering (IPO) of Artisan shares to pay down debt and return capital to original investors. He noted the IPO is not expected to affect management of the firm. Mr. Callahan pointed out that the employees still own a majority of the firm.

NEW BUSINESS, continued.

3. Due Diligence Report – Dimensional Fund Advisors
Report on on-site visit to Dimensional Fund Advisors

On February 6, 2013, a due diligence site visit to Dimensional Fund Advisors was conducted by Investment Committee Chair Jerry Richardson, Trustees Brenk and Smith, and Ms. Heaphy. Meetings included Portfolio Manager Lukas Smart and representatives of trading, research, compliance and client service teams.

Mr. Brenk reported that the investment strategy is intact and academically based. Trading practices minimize expenses and investment returns have been favorable. There were no negative findings as a result of the visit, he stated. Trustee Smith concurred, observing that the visits to investment managers are important to assess how managers go about their business. In summary, Ms. Heaphy stated that the strategy provides good diversification for the small cap space and she is comfortable with the firm and its operations. In response to Acting Chair Bolger’s inquiry, Ms. Heaphy expressed confidence in the planned transition from co-CEO’s to a single CEO.

Mr. Wickman announced that Deputy County Counsel Tom Lyons will no longer serve as counsel for the Investment Committee. Mr. Lyons has been offered a new role within the County Counsel office. Mr. Wickman will consult with the Marin County Counsel’s office to determine his replacement.

There being no further business, Acting Chair Bolger adjourned the meeting at 2:08 P.M.

__________________________________   _____________________________________
Bernadette Bolger, Acting Chair        Attest:  Jeff Wickman
Retirement Administrator