

MINUTES

INVESTMENT COMMITTEE MEETING MARIN COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

One McInnis Parkway, 1st Floor
Retirement Board Chambers
San Rafael, CA

September 12, 2013 – 9 A.M.

CALL TO ORDER Chair Brenk called the meeting to order at 9:04 A.M.

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

ABSENT: Cooper

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 period ending June 30, 2013

Anne Heaphy, Vice President for Callan Associates, presented the quarterly investment report as of June 30, 2013. Ms. Heaphy reported that in the U.S. equities rallied in April and mid-May and were modestly positive for the quarter. Fixed income was affected by higher treasury yields as a result of news of the potential end to the Federal Reserve's economic stimulus program. Emerging markets trailed developed markets due to weakness in the materials and energy sectors as China moves toward a consumer-driven economy. In response to questions from Chair Brenk and Trustee Bolger Brett Cornwell, fixed income specialist with Callan Associates, indicated that rising interest rates are a result of the markets anticipating the end to quantitative easing.

For the fiscal year ending June 30, 2013, MCERA assets were valued at approximately \$1.7 billion, having gained 14.77% net of fees, outperforming the benchmark return of 12.74%, and ranking in the 6th percentile of the Callan Public Fund Universe. For the quarter ending June 30, 2013, the Fund gained \$7.3 million, or 0.64% net of fees (versus

0.07% for the benchmark). Ms. Heaphy reported that the total Fund performance outpaces the index in all time periods.

Ms. Heaphy reviewed Fund performance by sector and attribution, reporting that asset allocations and managers had a positive effect on performance, with the exception of private equity and real estate. As examples Ms. Heaphy noted that Eaton Vance's underweight to Brazil, Russia, India and China, and Morgan Stanley's underweight to Australia led to outperformance. Strength in micro-caps benefited the Dimensional Fund Advisors portfolio which balanced the out-of-favor small cap growth sector.

Trustee Smith posed a general question on the overall positioning of the Fund. In response Ms. Heaphy stated that asset allocation drives returns and manager attribution is adding value on top of that. Recent adjustments to asset allocation targets were reviewed. The move to hire a global fixed income manager, she explained, is an incremental move to help meet the investment return assumption target. In response to Trustee Shore's inquiry about tail risk, Ms. Heaphy referred to the risk parity presentation by AQR. Responding to trustee inquiries, Uvan Tseng of Callan Associates explained the advantage of a commingled structure for international investments as opposed to a separate account that involves a costly, complex and elongated process.

Ms. Heaphy reported on the two private equity partnerships that are approximately one-third funded. As they mature the diversified investments are expected to generate positive cash flow. In response to Chair Brenk's inquiry on slower-than-expected funding for these vehicles, Mr. Wickman explained that the deal flow and therefore capital calls have been slow since MCERA's initial commitments were made in 2008. Annual reviews for the two private equity portfolios will be presented during the morning session of the October 16 Strategic Workshop.

Chair Brenk recessed the meeting for a break at 10:15 A.M., reconvening at 10:20 A.M.

Ms. Heaphy reported on several personnel changes at Western Asset, including the retirement of Steve Fulton, head of the agency mortgage-backed securities sector team, at the end of September. Anup Agarwal, who in August replaced Paul Jablansky, Head of Structured Products, will assume Mr. Fulton's duties. In addition, Chief Investment Officer Steve Walsh will retire in 2014, succeeded by former CIO Kenneth Leech, according to Mr. Cornwell. In the coming months Callan Associates will visit the firm to meet new personnel and assess the situation. Also Callan Associates will be monitoring Morgan Stanley's Dirk Hoffman-Becking who replaced John Goodacre who covered the energy sector with Peter Wright.

D. NEW BUSINESS

1. Manager Search – Global Fixed Income (Action) – Brett Cornwell, Anne Heaphy of Callan Associates
Consider and take possible action to select global fixed income manager for interviews

Brett Cornwell, fixed income specialist with Callan Associates, presented the companies that met the search criteria for global fixed income consideration. Mr.

Cornwell provided an overview of fixed income market opportunities outside the United States (U.S.), reviewing risk and return characteristics, hedging and currency attribution, and credit quality. According to Mr. Cornwell, global fixed income is an attractive opportunity that would provide diversification through exposure to different economic cycles and varying interest rate, duration and inflation environments.

Comparing the two major global fixed income indices, Citigroup World Government Bond Index and the Barclays Global Aggregate, Mr. Cornwell explained that with more issues and sector diversification, the Barclays index is a better indicator of the fixed income landscape. The relative performances of hedged versus unhedged currency strategies in weak and strong dollar environments were reviewed by Mr. Cornwell. In response to Trustee Bolger and Trustee Shore's observation that the hedged strategy is less volatile, Mr. Cornwell indicated that most managers use active (i.e., unhedged) currency management as a source of alpha. Discussions included the relative merits of more or less volatile strategies and correlations of major stock and bond indices. Trustee Smith expressed his support for an unhedged strategy.

Mr. Cornwell compared and contrasted the characteristics of each global fixed income manager. Factors considered included the degree to which the manager varied from a benchmark regarding interest rates, geographic location, duration exposure, and the risk/return profile. Discussions included consideration of performance attribution factors such as security selection and sector allocation. Based on recent changes to their personnel, Mr. Cornwell recommended removing ING Investment Management from the list of potential candidates to interview.

In summary, Mr. Cornwell stated that the managers presented for consideration as interview candidates represent a variety of risk/return profiles with some more aggressive than others. He responded to the trustees' inquiries on the availability of commingled investment vehicles, how long strategies were in place, and the effect of where the corporate headquarters were geographically located.

Chair Brenk asked each trustee to provide their top candidates for consideration. Based on the initial polling Manulife, Colchester and Brandywine received the largest percentage of interest. The Board also discussed whether to consider Loomis and Mondrian as potential interview candidates

Mr. Cornwell reviewed the characteristics of Manulife, Colchester and Brandywine. At Trustee Shore's suggestion, the performances of each manager during the 2008 and 2009 market crisis were reviewed and compared. According to Trustee Given, expected returns would make up for the relatively higher fees for MCERA that would be charged for global fixed income as was noted by Trustee Bolger.

It was M/S McFarland/Given to select Colchester Global Investors, Ltd., Manulife Asset Management, and Brandywine Global Investment Management LLC as interview candidates for global fixed income manager at the November Investment Committee meeting.

AYES: Bartfeld, Bolger, Brenk, Given, Gladstern, McFarland, Piombo, Shore,
Smith

NOES: None

ABSTAIN: None

ABSENT: Cooper

2. Review of Scope of Services Provided by Investment Consultant
Review and discuss investment consultant services

Mr. Wickman reported that Callan Associates will provide a comparison of investment manager fees with the industry and institutional investors. As background Mr. Wickman presented a memo outlining services provided by Callan Associates through the Investment Policy Statement and the contract with MCERA that include assisting in fee negotiations and considering whether fees are competitive when considering new managers. Discussion included the potential for negotiating lower fees, measuring fee levels among similar managers, and considering net-of-fee performance. The fee analysis will be considered at the January 2014 Investment Committee meeting.

There being no further business, Chair Brenk adjourned the meeting at 12:39 P.M.

Greg Brenk, Chair

Attest: Jeff Wickman
Retirement Administrator