MINUTES

INVESTMENT COMMITTEE MEETING
MARIN COUNTY EMPLOYEES' RETIREMENT ASSOCIATION (MCERA)

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

December 10, 2015 – 9:00 a.m.

CALL TO ORDER Chair Brenk called the meeting to order at 9:01a.m.

ROLL CALL

PRESENT: Bolger, Brenk, Given, Gladstern, Haim (alternate retired), Murphy, Piombo, Stevens, Thomas

ABSENT: Cooper (alternate safety), Shaw (ex officio alternate), Shore

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. Manager Overview – *Jim Callahan, Callan Associates*

Jim Callahan stated that managers presenting annual portfolio reviews today are Columbus Circle Investors on the small cap growth portfolio, State Street on the Securities Lending Program, and Pathway Capital Managements on their private equity funds. Later in the agenda a new commitment to the Abbott Capital Management Private Equity Fund AP 2016 will be considered.

2. Columbus Circle Investors – *Erik Osberg, Cliff Fox – 9:05 a.m.*

Erik Osberg, Vice President and Client Servicing/Marketing Officer for Columbus Circle Investors, reported that the firm replaced one analyst who moved and hired a Chief Compliance Officer. Mr. Osberg noted that the Small Cap Growth fund has been closed for several years. As of September 30, 2015 the Columbus Circle Small Cap Growth portfolio returned negative 13.85% (versus negative 13.06% for the Russell 2000 Growth Index) and negative 2.34% for the prior 12 months (versus 4.04% for the Russell 2000 Growth Index).

Cliff Fox, Senior Managing Director and Portfolio Manager for Columbus Circle Investors, stated that the objective is to identify strong, growing businesses in an environment that is unexpected. Mr. Fox explained that the strategy is to identify industry changes and invest in secondary trends that are accelerating in the small cap space. Mr. Fox characterized the current economic environment as relatively weak with the United States (U.S.) in a moderate economic posture and the rest of the world in worse position. Trustee Brenk observed that the small cap growth portfolio is on the Watchlist and inquired about underperformance to the benchmark. In response Mr. Fox stated that as a result of multiple years of quantitative easing by the Federal Reserve there is a distortion in the marketplace which inflates the value of weaker companies, thereby making benchmark comparison less favorable for the small cap growth portfolio. Mr. Fox believes the abnormal monetary policy is coming to an end which should benefit their investment strategy. Stronger job reports support a period of rising interest rates leading to the end of the misallocation of resources, he said. Trustee Piombo observed the portfolio outperforms and then underperforms across business cycles. Mr. Fox explained that in some scenarios the portfolio outperforms because holdings have a relatively stronger growth component as compared with other companies investors might sell in a downturn.

Responding to Trustee Gladstern's inquiry on how sector weightings affect performance, Mr. Fox explained that the portfolio will be overweight in sectors with better fundamentals and underweight sectors with weaker fundamentals. As an example Mr. Fox pointed to the underweight to the energy sector due to the relatively low price of oil. The portfolio manager explained that one reason for underperformance in the last several years is the underweight to the biotech (13% of the benchmark) sector, which has been in a bull market. As to Trustee Haim's inquiry on the sell discipline, Mr. Fox explained that when the driver of positive surprise begins to weaken and there is valuation compression then he will reduce and/or exit the position. Moving forward a normal economic cycle and monetary policy with rising interest rates should favor performance, Mr. Fox believes.

Mr. Fox said the unusually high 5% cash level at the end of the quarter noted by Trustee Piombo is an anomaly. Mr. Fox discussed the turnover rate of 150% in response to Trustee Stevens' inquiry and indicated the Russell 2000 Growth Index is not an unreasonable benchmark. As noted above, the biggest factor in underperformance has been the underweight to the biotech sector, according to Mr. Fox. The portfolio manager repeated that he anticipates performance to normalize as monetary policy becomes normalized. The reverse would be expected if quantitative easing were to continue, Mr. Fox stated in response to Chair Brenk's inquiry.

3. State Street, Securities Lending Progra*m – Henry Disano – 9:30 a.m.*

Henry Disano of State Street Bank's securities finance division reviewed the securities lending program. Mr. Disano reported that centralizing relationship management teams resulted in layoffs, including MCERA relationship manager Jeffrey Trencher whose replacement is senior team member John Powell. Since 2007 the securities lending program has generated $3.5 million of revenue for MCERA.

Mr. Disano stated that MCERA's cash collateral (102% of the value of securities on loan) is invested in the Quality D portfolio, a conservative commingled fund with standard approved borrowers. Mr. Disano noted that liquidity guidelines have become more conservative since 2011. In response to Chair Brenk's inquiry Mr. Disano stated that State Street provides indemnification against borrower default and, for example, covered MCERA's position when Lehman Brothers defaulted. Responding to Trustee Haim's query Mr. Disano explained a new program called enhanced custody whereby entities like CalPERS borrow the securities from themselves at less cost than with a prime broker. State Street is a party to this transaction that is controlled by strict procedures and compliance oversight. Trustee Bolger noted 17% of lending is to State Street and Mr. Disano assured her the securities lending division is subject to daily compliance to make sure State Street does not get a better deal. The question of whether lending to State Street was advisable was discussed.

Mr. Disano reviewed borrowing exposure statistics, noting that Goldman Sachs is the largest borrower. He explained that investors receive the yield on the cash in the Quality D pool and a fee from borrowers. Rates for different securities may vary according to demand. Mr. Callahan indicated that the allocation process for a security in high demand is important. According to Mr. Disano the methodology embedded in State Street's securities lending system makes traders blind as to the lender that is chosen on a first come, first served basis. Noting there is an incentive for State Street to borrow a security for itself, Mr. Callahan inquired as to whether any clients restrict borrowing by State Street and Mr. Disano responded affirmatively.

4. Pathway Capital Management – *Valerie Ruddick, Jim Reinhardt – 9:55 a.m.*

Valerie Ruddick, a director of Pathway Capital Management reported that in 2008 MCERA made its first commitment to the Pathway Private Equity Fund (PPEF) 2008, followed by commitments to PPEF I-7 and PPEF I-8. PPEF 2008 is fully committed, nearing full contribution status, and providing meaningful distributions resulting in a net compounded annualized 5 year return of 8.27% as of September 30, 2015, with upside to come.

Ms. Ruddick reviewed allocations by investment strategy and region for PPEF 2008. The predominant strategy is buyouts followed by special situations and venture capital, 75% of which are in North America. Responding to a question by Trustee Brenk, Ms. Ruddick indicated returns for the matured private equity portfolios are expected to be 3 to 5 percent over the public benchmark. A meaningful comparison to the public benchmark would occur at the 10 year mark. Fees lessen with the size of the commitment and step down through the end of the life of the fund, Ms. Ruddick said in response to Trustee Gladstern's inquiry.

PPEF 2008 is well diversified across managers, partnerships and vintage years. Buyouts and venture capital strategies are the strongest performers. In the special situations category Ms. Ruddick stated Pathway continues to have confidence in the managers of energy focused funds. In summary Ms. Ruddick noted the particularly strong performance of the venture capital segment where more profitable exits are expected.

In 2013 MCERA committed funds to the PPEF I-7 portfolio which was committed at a more normal pace of 2 and ½ years due to a better fund raising environment than when PPEF 2008 was launched. In 2016 PPEF I-7 is expected to be 52% funded. Ms. Ruddick reviewed diversification characteristics of the portfolio that are similar to PPEF 2008, with buyouts the predominant strategy and more relatively more weight to special situations.

PPEF I-8 was launched in 2015 with capital being deployed at a good pace, according to Ms. Ruddick. Two secondary investments have resulted in early distributions.

Chair Brenk recessed the meeting at 10:45 a.m., reconvening at 10:55 a.m.

C. NEW BUSINESS

1. Abbott Capital Management Private Equity Fund AP 2016 (**Action**)
   Consider and take possible action on private equity program commitment to AP 2016 based on reduced fee schedule.

   Mona Marquardt who manages client relationships for Abbott Capital Management (Abbott) discussed the Annual Program (AP) 2016 private equity fund which offers greater flexibility and better fees for investors. Meredith Rerisi, Managing Director, reported that Abbott has hired a dedicated compliance manager. AP 2016 will be led by the same management team and use the same strategies as the ACE fund series. With the annual program clients have the opportunity for more frequent investments with the same diversification characteristics as the ACE series. In addition portfolios may be customized across strategies.

   Ms. Marquardt reviewed the due diligence process in which alignment of interests and governance are carefully analyzed. Less than 5% of investment opportunities considered are selected for investment. Ms. Marquardt reviewed characteristics for AP 2016 that are consistent with prior funds and provide vintage year diversification over three years. A modified fee schedule for AP 2016 features a lower base management fee than ACE VII, a volume discount, and a repeat investor discount that drops the average annual fee from 55 basis points to 38 basis points. In addition there is an early closer discount waiving the 2016 management fee.

   Regarding Trustee Haim's inquiry Ms. Marquardt explained that a newspaper reference to high private equity fees in a CalPERS portfolio was referring mainly to fees associated with the underlying portfolio companies. Abbott makes sure such fees are as contracted, and its management fee is a simple percentage of the amount of the investment. In answering Trustee Stevens' question on past performance, Ms. Marquardt explained the metrics were not directly comparable to Abbotts' fund of fund returns which include different vintage years. Ms. Rerisi explained that internal rates of return are calculated net of fees and expenses, and the multiple measures how many dollars MCERA receives in return for each dollar invested.

   Mr. Wickman reminded the trustees that at the September 2015 Investment Committee meeting the Committee approved the Annual funding method for the private equity portfolio. During that meeting Mr. Callahan presented a pacing analysis showing annual commitment levels that would fund the private equity program to its target. This year the amount would be $50 million to each private equity manager. Mr. Callahan noted that the early investor discount will apply if the commitment to AP 2016 is made by December 31, 2015.

It was M/S Bolger/Piombo to commit $50 million to the Abbott Capital Management Private Equity Fund AP 2016 in accordance with the fee schedule presented.

AYES:	Bolger, Brenk, Given, Gladstern, Murphy, Piombo, Stevens, Thomas
NOES:	None
ABSTAIN:	None
ABSENT:	Shore

Callan Associates private equity specialist Gary Robertson gave the example of the average annual interest earned on a bank account to explain the meaning of the dollar-weighted internal rate of return. Mr. Robertson said the Pathway and Abbott private equity portfolios have similar performance metrics that are directly comparable because the timing of the investments is the same. When the two private equity mangers were originally selected it was noted that Pathway is a little more expensive, he said. Both managers are conservative and are complimentary with respect to the use of debt, Mr. Robertson explained in response to a question by Chair Brenk.

2. UBS Trumbull Property Fund Capital Call (**Action**)
   Consider and take possible action regarding January 2016 capital call.

   Mr. Wickman stated that in September MCERA received a capital call from UBS for its $50 million commitment to the Trumbull Property Fund. At that time the Investment Committee deferred $42 million which is now being called. Mr. Callahan explained in response to Chair Brenk's inquiry that MCERA's two core real estate funds are pools of seasoned income-producing existing properties. Mr. Callahan further stated that real estate is a natural inflation hedge in that rents can be increased.

   Mr. Callahan advised reducing the $42 million capital call to $20 million and relinquishing the remainder of $22 million for the following reasons. The reasoning is that this is a current investment opportunity that would keep real estate within its range at 9.2%, provide a cushion for real estate as the Fund grows, and maintain total real assets slightly below target. In addition the investment consultant pointed out that the fixed income portfolio has been restructured and real estate has a yield premium in current market conditions. As a source of funds he recommended the S&P 500 which is overweight.

   Trustee Piombo expressed support for Mr. Callahan's analysis. In response to queries by Chair Brenk and Trustee Stevens, Mr. Callahan acknowledged there would likely be a redemption queue if the real estate market weakens but he indicated the Fund has sufficient liquidity and is more liquid than most public pension systems.

It was M/S Piombo/Gladstern to accept the investment consultant's recommendation to reduce the UBS Trumbull Property Fund $42 million capital call to $20 million.

AYES:	Bolger, Brenk, Given, Gladstern, Murphy, Piombo, Stevens, Thomas
NOES:	None
ABSTAIN:	None
ABSENT:	Shore

It was M/S Piombo/Stevens to accept the investment consultant's recommendation to relinquish the UBS Trumbull Property Fund capital call balance of $22 million.

AYES:	Bolger, Brenk, Given, Gladstern, Murphy, Piombo, Stevens, Thomas
NOES:	None
ABSTAIN:	None
ABSENT:	Shore

Chair Brenk recessed the meeting at 12:08 p.m., reconvening at 12:31 p.m.

3. Investment Policy Statement (**Action**)
   Consider and take possible action on Governance Committee's recommended updates to policy regarding Watchlist and Proxy voting provisions.

   Mr. Wickman presented and reviewed the Governance Committee's recommended updates to the Watchlist provisions in the Investment Policy Statement. The updates were developed in response to rebalancing discussions at September's Investment Committee meeting. Previously managers on the Watchlist could not receive additional funds in a rebalancing scenario. With the proposed updates a manager on the Watchlist could receive additional funds if the Investment Committee so chose. In addition, Mr. Wickman said, the updates include new provisions for tracking managers on the Watchlist over time.

Based on the action of the Governance Committee, Governance Committee Chair Bolger moved that the Board adopt updates to the Investment Policy Statement as presented.

   Using Columbus Circle as an example, Mr. Callahan addressed the importance of patience in considering managers on the Watchlist in response to Trustee Stevens' inquiry. During periods of time when a manager is out of favor, considerations would be what if anything has changed as far as expectations and strategy. So long as the manager remains disciplined, he stated, they are expected to recover. It is crucial, Mr. Callahan said, not to terminate managers if they have a bad period because the cycle is costly and you end up selling low and buying high.

   Trustees Bolger and Piombo indicated an interest in considering a passive investment vehicle as an alternative to the actively managed small cap growth portfolio. Chair Brenk called for the vote.

AYES:	Bolger, Brenk, Given, Gladstern, Murphy, Piombo, Stevens, Thomas
NOES:	None
ABSTAIN:	None
ABSENT:	Shore

D. INVESTMENT CONSULTANT QUARTERLY REPORT

1. Quarterly Report and Performance Update
   For period ending September 30, 2015

   Mr. Callahan presented the Quarterly Report as of September 30, 2015. The investment consultant reported that a major theme in the capital markets is the divergence of domestic from international markets. The U.S. has improving economic metrics and is relatively stable compared to the rest of the world that remains in a stimulus monetary policy mode. It was a risk off quarter in the capital markets, he said, with weakness particularly in the energy sector as commodity prices decline, and the health care sector. Real estate continues to perform well, he said. In the fixed income portfolio interest rates came down in the quarter, a surprise to active managers, and Treasurys and government securities outperformed. European and emerging market debt were particularly bad performers, in part because the rise of the dollar against foreign currencies reduces emerging markets returns. As to monetary policy Mr.

Callahan said it is difficult to know when and for how long the Federal Reserve will raise rates.

Within the equity portfolio the balance is 60% domestic and 40% non-U.S. which Mr. Callahan stated is reasonable in response to Trustee Haim's inquiry. Moreover, there is integration in that the emerging market countries are dependent on developed markets to buy their products. Mr. Callahan expressed confidence in the current asset allocation and diversification of the Fund for the long term.

The Fund returned negative 4.2% for the quarter, outperforming the custom benchmark by 1.5%. For the past 12 months the Fund outperformed its benchmark by 2.2%, with similar outperformance over the previous 3 and 5-year periods. The returns resulting from the sale of Woodmont properties were very favorable to the Fund.

The returns for each asset class were reviewed by Mr. Callahan. In domestic equities the small cap overweight was a detractor. The small cap value Dimensional Fund Advisors portfolio is in line with its benchmark for the quarter and outperformed for the past year. The Columbus Circle Investors small cap growth portfolio is slightly behind the benchmark for the quarter and trailing otherwise. The international portfolio has performed well in relative terms, outperforming the index by protecting in a down market, which is one of the benefits of active management, Mr. Callahan observed. Both the Morgan Stanley and Artisan international portfolios have done very well over time and continue to complement one another well. Mr. Callahan noted that Pyramis was the best performing international manager for the quarter and long term performance looks good. Pyramis, which has been the institutional division of Fidelity, is returning to its "Fidelity" name, he reported. The Parametric emerging markets portfolio outperformed its index by about 3% for the quarter and the long term returns look good relative to the index in what has been a difficult market over the past five years, Mr. Callahan said. Collectively the international portfolio has added significant value by outperforming its index by 4.5% over five years, he reported.

In the fixed income portfolio Mr. Callahan recalled that active managers were repositioned by moving Western Asset Management from a core plus strategy to an intermediate duration credit strategy and bringing Colchester on board to be the global bond manager. Mr. Callahan reported that over the past three years our fixed income benchmark has underperformed the Barclays Aggregate Index. The investment consultant expects the fixed income portfolio performance to improve if the Federal Reserve moves on raising rates, noting that individually the managers have done well in their spaces.

The real assets composite returns are driven by the favorable Woodmont portfolio asset sales. Core real estate managers trailed the ODCE benchmark and public real assets suffered sharp selloffs due to deflationary pressures in the market. Callan Associates has conducted searches for active managers in natural resource equities and commodities for consideration by the Investment Committee. REIT returns are decent.

Mr. Callahan reviewed the structure of the private equity portfolio which he said is beginning to have meaningful returns. As of June 30, 2015 private equity returns are slightly above the Cambridge Universe median. Private equity managers Abbott Capital Management and Pathway Capital Management are solid managers with comparable returns that are beginning to pay benefits to the Fund. Mr. Wickman noted that the Fund's fiscal year return as of June 30, 2015 improved to 5.01% net of fees once private equity values were included.

2. Wellington Management Company Team Update

   Mr. Callahan reported that L. T. Hill is retiring in June 2016 and his responsibilities will be absorbed by other team members. Mr. Hill has been a leader for core strategies and duration posturing on interest rates. Callan Associates will monitor the situation and Mr. Callahan is not concerned because of the depth of the Wellington team.

There being no further business, Chair Brenk adjourned the meeting at 2:01 p.m.

Greg Brenk, Chair

Attest: Jeff Wickman
Retirement Administrator