VENTURA COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

BOARD OF RETIREMENT

BUSINESS MEETING

SEPTEMBER 19, 2011

MINUTES

DIRECTORS PRESENT:	Tracy Towner, Chair, Safety Employee Member William W. Wilson, Vice Chair, Public Member Steven Hintz, Treasurer-Tax Collector Steve Bennett, Public Member Albert G. Harris, Public Member Tom Johnston, General Employee Member Arthur E. Goulet, Retiree Member Chris Johnston, Alternate Employee Member Will Hoag, Alternate Retiree Member
DIRECTORS ABSENT:	Joseph Henderson, Public Member Robert Hansen, General Employee Member
STAFF PRESENT:	Henry Solis, Interim Retirement Administrator Lori Nemiroff, Assistant County Counsel Brenda Cummings, Retirement Operations Manager
PLACE:	Ventura County Employees' Retirement Association Second Floor Boardroom 1190 South Victoria Avenue Ventura, CA 93003
TIME:	9:00 a.m.

ITEM:

I. INTRODUCTION OF MEETING

Chairman Towner called the Business Meeting of September 19, 2011, to order at 9:03 a.m.

II. APPROVAL OF AGENDA

Mr. Harris moved, seconded by Mr. Goulet, to approve the Agenda.

Motion passed.

III. CONSENT AGENDA

A. Regular and Deferred Retirements and Survivors Continuances for the Months of July and August 2011.

B. Report of Checks Disbursed in July and August 2011.

C. Asset Allocation as of July 31, 2011 and August 31, 2011.

D. Statement of Plan Net Assets, Statement of Changes in Plan Net Assets, Summary of Investments and Cash Equivalents, and Schedule of Investment Management Fees for the Month Ended June 30, 2011.

E. Statement of Reserves as of June 30, 2011.

F. Statement of Plan Net Assets, Statement of Changes in Plan Net Assets, and Summary of Investments and Cash Equivalents for the Month Ended July 31, 2011.

G. Budget Summary – Year to Date as of June 2011, Fiscal-Year 2010-11.

H. Budget Summary – Year to Date as of July 2011, Fiscal-Year 2011-12.

I. BlackRock Asset Management Report for the U.S. Equity Index Fund, Extended Equity Market Fund, U.S. Debt Index Fund, ACWI EX-US Fund for the Months Ended July 31, 2011 and August 31, 2011.

Staff stated there was a correction to the Regular and Deferred Retirements and Survivors Continuances for the Month of August 2011. The Total Service for John Quick was omitted and it should read 30.69 years of service.

Mr. Harris moved, seconded by Mr. Hintz, to receive and file the items on the Consent Agenda, as amended.

Motion passed.

IV. INVESTMENT INFORMATION

A. Loomis Sayles Investment Presentation, Stephanie S. Lord, CFA, CIC.

Stephanie S. Lord, CFA, CIC, Vice President, Client Portfolio Manager, was present on behalf of Loomis Sayles to review the firm's organization, investment results for VCERA's accounts, investment process, and outlook.

Organizationally there have been no substantive changes to the firm, according to Ms. Lord. Loomis Sayles currently has $162 billion under management, of which $146 billion is in fixed income.

Ms. Lord stated that since inception the return of the VCERA fund has been 7.79% annualized; for 2010 the fund returned 14.04%; and for the period July 1 through August 31, 2011 the portfolio returned 5.48%.

Ms. Lord stated that there have been sector allocation changes made in the last twelve months in response to market volatility. She stated that they have moved money out of Treasuries and into cash and equivalents, and have built up reserves weighted to the Canadian dollar.

Ms. Lord commented, in response to Mr. Wilson's query, that she would place 20-23% of the portfolio in Non-US dollars, if it weren't for the 20% constraint, and that there is a five percent limit on cash, much of it invested in equivalents.

The Non-US Dollar has provided an excess return of 73 basis points, while high yield has added an excess return of 111 basis points, according to Ms. Lord. She opined that high yield bonds will be a good opportunity in the next couple of weeks.

Ms. Lord opined that the decline in rates is over, and rates will be low for a long time. With this outlook, along with the predicted volatility in the next three to four weeks and the deteriorating conditions in Europe, will mean that Europe will be the number one risk and biggest opportunity going forward. She stated the current volatility is a consequence of the crisis in Europe having a shorter duration than the long term scenarios that are being considered.

Ms. Lord noted that most companies are in better financial condition than when the 2008 downturn occurred, so while the US high grade corporate spreads are at about their fifteen year average, they still like credit going forward. She stated they also have a large position in convertibles and they will increase their position, when they feel more comfortable that there won't be a double dip in the economy. However, she did note that over the last month while they do think the odds of a double dip have increased from the

IV. <u>INVESTMENT INFORMATION</u> (continued)

A. Loomis Sayles Investment Presentation, Stephanie S. Lord, CFA, CIC. (continued)

low twenties to about forty percent, they do not think there will be a double dip because the issues in the auto supply chain have been worked out. She opined that this will help keep the US in positive territory for the next six months.

So while Loomis continues to focus on Europe, they are aware that China has done a wonderful job managing their situation, keeping global growth up; however, they are concerned about the shadow banking issue, according to Ms. Lord.

In response to inquiry by Mr. Vandolder, Ms. Lord stated that the "street" is different now than it was in 2008, but due to lack of liquidity, some of the same challenges are present. Ms. Lord stated that while there are some indicators that a scenario like 2008 may occur, they are not predicting that it will occur.

B. Reams Asset Management Investment Presentation, Mark M. Egan, CFA, CPA.

Mark M. Egan, CFA, CPA, Managing Director, was present of behalf of Reams Asset Management (Reams) to review the firm's organization, investment process and investment results for VCERA's account.

As of November 2010 Reams became a division of Scout Investments, but this has not resulted in any material changes with regard to how they manage portfolios, according to Mr. Egan.

Reams has approximately $10 billion under management, exclusively focused on U.S. fixed income portfolios, and Scout Investments has approximately $20.5 billion in assets under management, according to Mr. Egan. He stated that they have lost two small accounts and had two rather large accounts contract them, but there have been no net addition of assets. As of June 30, 2011 they have 97 fixed income accounts, and 13 fixed income investment professionals. Mr. Egan stated that the professional staff has been very stable, with the addition of a new staff member last year, Trey Harrison, CFA, ASA, an actuary.

Mr. Egan reviewed the client list, and the products list, noting that each of the fixed income products was the result of a current client asking Reams to fulfill a specific mandate. Currently, in this low interest rate world, their clients are asking if there is a way to squeeze extra return out of the

IV. INVESTMENT INFORMATION (continued)

B. Reams Asset Management Investment Presentation, Mark M. Egan, CFA, CPA. (continued)

allocation, according to Mr. Egan.

Mr. Wilson received clarification of what assets are included in the "Real Return" portfolio which is down to $5 million because clients are moving away from a Treasury Inflation-Protected Securities (TIPS) type of portfolio.

Mr. Egan stated that the Investment Objective and Guidelines from the VCERA Board is to be credited with the great performance of the fund. The Core Fixed Income mandate was funded approximately 10 years ago and has gone from $225.7 million to $306.8 million. The portfolio is returning about 3.3 percent after fees compared to the market at 2.7 percent, and for the month of August 31 the market is up 5.9% and the portfolio is up approximately 5.8%, according to Mr. Egan. He noted that the approximately 70 basis points of excess return were derived from rates, sectors, and securities.

Mr. Egan stated that the volatility they expected has occurred and that it is time to be a bit more aggressive in the portfolio, and to buy high quality corporate bonds, which when adjusted for defaults are giving equity- like returns. He posited that the government wants people to invest in these sectors, so the current policies are likely to be in place for a long time. The U.S. treasury return is guaranteed to be less than inflation for five years, opined Mr. Egan.

Mr. Goulet received clarification regarding the status of the U.S. market relative to the European market. Mr. Egan stated that the interrelatedness of Greece to the other European countries creates complications that the U.S., because of its sovereignty, does not have.

Mr. Hintz requested a list of the ten corporations that comprise the largest percentage of VCERA's corporate holdings with Reams.

Mr. Egan stated that with the low growth, and absent inflation in the market, they began restructuring the portfolio in August and September to take advantage of high yield corporate credit, adding a little more risk to the portfolio. He stated they agree with Loomis, markets today are driven by a number of variables, and they do not believe that VCERA should be invested in Treasuries given the fund's time horizon. Mr. Egan noted that they learned from the 2008 markets, and if that scenario reoccurred there would be opportunities available in terms of incremental returns for the portfolio.

IV. INVESTMENT INFORMATION (continued)

B. Reams Asset Management Investment Presentation, Mark M. Egan, CFA, CPA. (continued)

Mr. Egan stated, in response to Mr. Goulet's query, that Quantitative Easing 2 (QE2) was considered a failure because wages did not go up, prices for food and energy went up, and disposable income went down. It is a global economy now and the U.S. federal government cannot get the results they are seeking directly; however, because of the rollover of debt some form of quantitative easing will be necessary going forward, Mr. Egan opined. The International Monetary Fund (IMF) stated they would like the developed economies to have an inflation rate of 3 to 5 percent rather than 0 to 2 percent to create this increase.

Mr. Goulet received clarification that Reams decreased Mortgage Backed Securities (MBS's) and they never have been extensive users of home loan or non-agency mortgage backed securities.

C. K 2 Advisors Investment Presentation.

Matthew Annenberg, Managing Director, and Robert Rodman, Managing Director, were present on behalf of K2 Advisors to review the firm's organization, investment process, and investment results for VCERA's account.

Mr. Annenberg acknowledged that the investment results have been poor.

Mr. Rodman commented that a lot has happened since K2 last came to the Board in 2010. He stated that the amount under management has grown from \$9.4 billion to \$10.5 billion, and the currency side has grown from \$150 million to \$200 million. Many of their clients are looking for a strategy that manages the spiky volatility and benefits from the deep liquidity and lack of correlation to other strategies, according to Mr. Rodman.

Mr. Annenberg reviewed the condition of the foreign exchange (FX) market since April. He noted that it had been a difficult period, similar to 2008, but the market has just broken out of that flat-line range. The flatness of the market has masked some extreme cases of valuation, primarily the issue of the Swiss Franc, Mr. Annenberg opined. He noted that because of the managers' patience with the Swiss France and the SNB's actions, K2 has begun to see results. Mr. Annenberg distinguished the European situation from that in the U.S.

The outlook is good because FX and other macro type asset classes have the potential to do very well when other markets are having difficulty,

IV. INVESTMENT INFORMATION (continued)

C. K 2 Advisors Investment Presentation. (continued)

according to Mr. Annenberg. He stated that K2 reached their performance low in the middle of August, down about 2%, they made about 1% back by the end of August, and are up about 3% so far in September. He opined that the volatility in the market in the first half of 2012 will result in this product recovering some of its prior losses.

Mr. Annenberg stated that over the course of this difficult period of "whipping markets" they have made some changes to the portfolio. One of those changes was in June when they decided to overweight their discretionary managers. At that point K2 realized they will make money where they can. At the end of August they moved part of that overweight back to managers with the expectation that the market was moving into a more trending market. He stated that, so far, that has worked and they have mitigated the loss in the portfolio by about 110 basis points. He stated they are also working with Mr. Vandolder to better align their interests with VCERA's by instituting a lower management fee and a performance fee, which will effectively reduce fees by more than one-half.

Mr. Rodman reiterated the challenges in the market, and stated that they are staying away from a carry strategy because it looks, acts, and behaves like everything else in the VCERA portfolio.

Mr. Vandolder reminded the VCERA Board that one of the intentions of the current K2 strategy was additional volatility containment while experiencing a new component of the investment market. Mr. Annenberg stated that this strategy needs volatility to be successful and two positive things occurred in the last four weeks that has resulted in positive returns. First the Swiss National Bank took corrective action as they realized that the extreme misevaluation of the Swiss Franc could potentially be negative to its export sector. Second, they started to see the dollar finally show some sustained upwards momentum against various country currency dollars.

Mr. Towner received clarification of the fund's poor performance at the beginning of 2011 given the volatility experienced during that period, as evidenced by the VIX (Chicago Board Options Exchange Market Volatility Index) and DB CVIX (Deutsche Bank Currency Volatility Index).

Mr. Wilson received clarification that in currency, as with many asset classes, there is a reversion to the mean and K2 tries to be nimble and take advantage of that; so if one strategy has done well for a period of time they will assume there is some reversion. For example, the overweight to the discretionary manager in June did extremely well for three months, but they

IV. INVESTMENT INFORMATION (continued)

C. K 2 Advisors Investment Presentation. (continued)

have cut back those managers.

In response to Mr. Bennett's query, Mr. Annenberg compared and contrasted the current FX environment and what unfolded in 2008 and is hopeful that the markets have digested in 2011 the similarities that occurred in 2008 and that we are now entering the action phase now that the expectation for weaker
euro has set in.

D. Hewitt EnnisKnupp, Kevin Vandolder.

1. Second Quarter 2011 Performance Report.

Mr. Vandolder stated that VCERA, compared to other systems he works with, has one of the best total returns for the year. He noted that the fund's ranking, relative to peers, is 9, which is in the top one-third, the goal of the Board.

Mr. Goulet commented that the returns exceed those of both PERS and SDCERS, both of which utilize more investment resources than VCERA. Mr. Vandolder stated VCERA has one of the lowest costs because of the heavy replication of passive investment funds and that it is VCERA's focus on risk control, cost control, and patience that has made the fund so successful.

In addition to highlighting the positive overall returns of the portfolio, Mr. Vandolder discussed Acadian, Artio, the real estate strategy, and K2

Mr. Wilson stated that the performance for the twelve months was spectacular because they are not taking any undue risk and are "cherry picking" for active returns. Mr. Wilson received clarification regarding VCERA's year to date total fund portfolio ranking of 35, relative to the policy portfolio's ranking of 59.

Mr. Vandolder discussed his fear of stagflation, inflation without growth in the economy, and politics rather than the fundamentals driving the market. He stated that the fed is buying long term debt back, hoping the economy can gain some traction and rebound on its own merits, as opposed to planners being the catalyst for economic growth, in the face of more quantitative easing type strategies.

Mr. Towner stated that he would expect more return from Reams based

IV. INVESTMENT INFORMATION (continued)

D. Hewitt EnnisKnupp, Kevin Vandolder. (continued)

1. Second Quarter 2011 Performance Report.

upon their risk. Mr. Vandolder stated that the portfolio is trying to achieve an overall rate of return of 8% minimizing risk, as a whole, using mean variance optimization.

Mr. Goulet requested that Mr. Vandolder provide a Table of Contents with page and tab numbers in the quarterly report.

Mr. Vandolder stated he is available to the Board Members between meetings, or to meet with Staff. They will be spending more time together in October at the retreat.

2. Monthly Manager Updates/Summary, July 2011.

   a. Sprucegrove
   b. Artio
   c. Hexavest
   d. Walter Scott
   e. GMO
   f. Acadian
   g. Western
   h. Reams
   i. Loomis Sayles
   j. K2

3. Monthly Manager Updates/Summary, August 2011.

   a. Sprucegrove
   b. Artio
   c. Hexavest
   d. Walter Scott
   e. GMO
   f. Acadian
   g. Western
   h. Reams
   i. Loomis Sayles
   j. K2

Mr. Vandolder stated that with the last pull back of the market, the fund did not go below $3 billion, but the markets continue to be a challenge for the participants.

IV. <u>INVESTMENT INFORMATION</u> (continued)

D. Hewitt EnnisKnupp, Kevin Vandolder. (continued)

3. Monthly Manager Updates/Summary, August 2011. (continued)

He stated the decline in Western was expected with the downturn, but Hexavest and Sprucegrove provided sizable downside protection, as did WalterScott and GMO. He stated that the passive debt fund, Black Rock U.S. Debt Index Fund, will be reflecting an increase in government holdings as governments release more debt. Mr. Vandolder noted the increases in fixed income, and that he will continue to challenge the Board to see less and less risk control in VCERA's fixed income program, largely because of the inefficiencies of the benchmark.

Mr. Hintz received clarification that Mr. Vandolder is not suggesting that the Board terminate K2, but rather to have patience for the next six to twelve months because the investment is small, he can relate to the difficulties their currency managers are having, and it is a complex asset class. Mr. Vandolder stated that it does cause concern that it is difficult for the Board to communicate to others what they are trying to do on VCERA's behalf. He concluded by noting that this type of investment may not be the most efficient use of VCERA's funds with regard to risk versus reward.

Mr. Hintz moved, seconded by Mr. Harris, to receive and file items 1. through 3.

Motion passed.

4. Highlights and Research, September 2011.

   a. Board of Retirement Retreat Agenda
   b. Capital Market Assumptions
   c. Second Quarter 2011 Hedge Fund Update
   d. Opportunistic Credit Basket (Revisited) Overview
   e. Investing in a Volatile Environment
   f. Monthly Summary of Medium Term Views – U.S.
   g. HEK University Agenda: *Navigating Your Investment Program*
   h. Update from CEO
   i. Proposed Change in Consulting Manager

Mr. Towner requested that HEK provide a webpage where the Board Members may access the status of the portfolio, especially during the months that the Board is dark. Mr. Vandolder stated that they can

IV. INVESTMENT INFORMATION (continued)

D. Hewitt EnnisKnupp, Kevin Vandolder. (continued)

4. Highlights and Research, September 2011. (continued)

create a web portal where the Board Members can see all the reports they deliver for them.

Mr. Vandolder reviewed the Retreat Agenda, and explained that the change to a one-day meeting on October 6 was due to Mr. Angelo's unavailability on October 7.

Mr. Wilson received clarification that HEK's expectation of CPI inflation for ten years at 2.2% was derived directly from the Blue Chip survey and the leading economists believe that meaningful inflation is low, with some calling for deflation. Mr. Vandolder reiterated his concern regarding stagflation, but noted it was more of a personal observation rather than a view held by HEK, which is reflected in the reports. He noted that HEK refers to global inflation, while Mr. Angelo uses wage inflation.

Mr. Vandolder reviewed the three building blocks of capital market assumptions; inflation, income and global growth. He stated that the assumptions going forward will be a 2.2% inflation rate, a 2% income rate, and a 3% or greater global growth rate, for a total of approximately 7% returns on stocks. At least a 2% growth rate will be required to accommodate the amount of debt that developed countries have created over the last several years, according to Mr. Vandolder.

Under the medium term view, any hint of developed countries continuing to slow will have a significant impact on the emerging markets growth which is already embedded in current prices, according to Mr. Vandolder.

Mr. Hintz received clarification that the HEK University program is available to the Board Members. Mr. Vandolder stated he will provide the Board with more advance notice of the dates for 2012.

Mr. Vandolder reported that Mr. Eric Kuhl is no longer with HEK, and Mr. Kevin Chen will be assisting him in the future.

Mr. Goulet moved, seconded by Mr. Harris, to receive and file item 4.

Motion passed.

V. OLD BUSINESS

A. Letter from County CEO and CEO-HR Regarding Retirement Administrator Recruitment Update; Approval of, and Authorization by VCERA to Pay Costs Associated with Candidate Travel in Compliance with the Administrative Policy Pertaining to County of Ventura Travel Reimbursement for Position Applicants, Candidates.

Mr. Goulet moved, seconded by Mr. Wilson, to approve and authorize VCERA to pay the travel costs (including air, lodging, auto, and meals) associated with those candidates interviewing with VCERA for the Retirement Administrator position.

Motion passed.

B. Pension Administration System Project Update.

Staff stated that because of the large number of agenda items on the September 19, 2011 Agenda, and to provide adequate time for the presentation and questions, the Pension Administration System Project update has been rescheduled to the October 3, 2011 Disability Meeting.

VI. NEW BUSINESS

A. Request to Attend CALAPRS Trustees' Roundtable, San Jose, CA – October 14, 2011

Mr. Wilson moved, seconded by Mr. Harris, to approve Mr. Goulet's request to attend the California Association of Public Retirement Associations (CALAPRS) Trustees' Roundtable in San Jose, California on October 14, 2011.

Motion passed.

B. Conference Report – Trustee Chris Johnston

Mr. Harris moved, seconded by Mr. Wilson, to receive and file Mr. Chris Johnston's Conference Report.

Motion passed.

VII. INFORMATIONAL

A. Letters Regarding Termination of STAR COLA Benefit from: Margaret R. Pierce, Dallas Mallernee and Frances M. DeJohn.

B. Publications (Available in Retirement Office)

1. Institutional Investor
2. Pensions and Investments

VIII. PUBLIC COMMENT

None.

IX. BOARD MEMBER COMMENT

None.

X. ADJOURNMENT

There being no further items of business before the Board, Chairman Towner adjourned the meeting at 11:30 a.m., upon motion of Mr. Hintz, seconded by Mr. Goulet.

Respectfully submitted,

HENRY C. SOLIS, Interim Retirement Administrator

Approved,

WILLIAM W. WILSON, Vice Chairman