VENTURA COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

BOARD OF RETIREMENT

BOARD RETREAT

JUNE 3, 2009

MINUTES

DIRECTORS PRESENT:	Tracy Towner, Chair, Safety Employee Member William W. Wilson, Vice Chair, Public Member Lawrence L. Matheney, Treasurer, Ex-officio Member Albert G. Harris, Public Member Joseph Henderson, Public Member Karen Becker, General Employee Member Arthur E. Goulet, Retiree Member Chris Johnston, Alternate Employee Member Will Hoag, Alternate Retiree Member
DIRECTORS ABSENT:	Peter C. Foy, Public Member Robert Hansen, General Employee Member
STAFF PRESENT:	Tim Thonis, Retirement Administrator Lori Nemiroff, Assistant County Counsel Henry Solis, Fiscal Manager
PLACE:	Ventura County Employees' Retirement Association Second Floor Boardroom 1190 South Victoria Avenue Ventura, CA 93003

ITEM: **TOPIC:**

I. **Introductions, Administrative Matters and Review of Agenda**

Chairman Towner called the Board Retreat to order at 9:00a.m.

Mr. Matheney moved, seconded by Mr. Harris, to approve the June 3, 2009 retreat agenda.

Motion passed.

II. Asset Allocation and Peer Practices

Kevin Vandolder and Sherri Young were present from EnnisKnupp & Associates.

Mr. Vandolder addressed the goals of the retreat including the answering of several key questions regarding private equity and the potential hiring of one or more currency overlay managers. Mr. Vandolder also noted the presentation of PIMCO (Pacific Investment Management Company) on the TALF and PPIP programs and characterized these federal programs as the "ultimate dislocation" strategy. Mr. Vandolder further noted the late morning presentations of STW and Loomis Sayles regarding the current state of the fixed income markets.

Mr. Vandolder commented briefly on the state of the current financial markets noting the improved equity markets and the 20% return year-to-date of Reams Asset Management.

Mr. Vandolder offered comparisons of VCERA's current asset allocation relative to peers and offered commentary regarding VCERA's current conservative orientation relative to peers in the alternative investment category. Specifically, Mr. Vandolder illustrated that peers maintained an 8% allocation to alternatives and 29% to domestic equity, while VCERA maintained a 40% allocation to domestic equity with no alternatives other than real estate. In terms of international equity allocations, Mr. Vandolder noted VCERA's higher allocation relative to peers.

Mr. Vandolder commented on the future roles of continued increased levels of global equity in VCERA's portfolio as well as private equity noting the increased return opportunities globally, the potential for risk reduction and the high arithmetic return projection of private equity.

According to Mr. Vandolder, VCERA's real estate program maintains an important place in the overall allocation due to its ability to offer diversification benefits, current income and a hedge against inflation.

Ms. Young reviewed the benefits of private equity investments and noted the historical evidence that supports private equity investments during difficult economic periods.

Mr. Matheney questioned the liquidity and management risks of private equity investing.

II. Asset Allocation and Peer Practices (continued)

Mr. Vandolder noted both the benefits and risks of private equity investing and described the benefits to include superior return potential, diversification and the long-term investment horizon. Risks described included illiquidity, lack of a performance benchmark and complex contractual arrangements.

Mr. Goulet requested and received clarification regarding the time periods cited in the chart on page 2.32 of the material.

Mr. Vandolder provided a brief overview of the dislocation strategies in the current market.

Mr. Towner requested and received clarification regarding VCERA's expected future returns given VCERA's current asset allocation.

III. Non-Agency Mortgages and Impacts on Government Intervention

Kim Stafford and Deepa Salastekar were present from PIMCO to discuss the investment opportunities associated with the TALF and PPIP federal government programs for distressed securities.

Ms. Stafford provided an overview of the TALF (Term Asset-Backed Securities Loan Facility) program and why PIMCO established an investment vehicle to participate given the attractive investment opportunities in AAA fixed income assets.

Ms. Salastekar described the program as a $200 billion government program designed to finance purchases of AAA asset-backed securities (ABS) by private investors. Asset-backed securities include auto loans, credit cards and student loans. The overall objective of TALF was to restart the flow of credit to consumers by reviving ABS issuance and investment.

The TALF program features non-recourse financing, typically 3-5 years, with no re-margining requirements. Leverage exists in the program but there are no margin calls if the asset price falls. Additionally, there is no cross-collateralization and the loans may be pre-paid. The program is scheduled to end December 31, 2009.

According to Ms. Salastekar, the AAA rating of the TALF securities is provided through rating enhancements such as over-collateralization, excess spread, subordination and the establishment of reserves.

Mr. Goulet questioned why investors should trust the credit agencies and what exactly these credit enhancements were.

III. Non-Agency Mortgages and Impacts on Government Intervention (continued)

Ms. Salastekar responded that it wasn't a question of trust, but rather a detailed examination of the bond issuance and the onus was on the manager to accomplish appropriate due diligence on the credit securities rather than blindly relying on the credit rating. Ms. Salastekar further described the possible credit enhancements.

Ms. Salastekar summarized the TALF program investment process including the margin requirements and the associated Federal Reserve (Fed) loan financing the security purchase with the earnings from the program based upon the principal and interest received less the financing charges paid to the Fed.

An investor could expect to earn, based upon the leverage in the program, a 1,500 basis point spread based over LIBOR.

Mr. Vandolder noted the attractiveness of the "non-recourse" financing.

Mr. Matheney questioned the life of the PIMCO TALF fund and learned that PIMCO expected their fund's life to be approximately 3.5 years.

Mr. Wilson requested clarification on the ownership of the TALF program's securities.

Ms. Salastekar noted that the securities were newly originated and securitized by the dealer community.

Ms. Salastekar reviewed several case studies for various security types.

In summary, Ms. Salastekar noted there were six more TALF auctions this year with \$90–\$120 billion more in bonds entering the market. The PIMCO fund is expected to close on June 30, 2009 with capital drawn down through March 31, 2010. The minimum investment size is \$10 million with leverage dictated by the terms of the TALF. The fees are the lesser of 5 basis points of notional invested commitments or 75 basis points of investment commitments with an associated performance fee of 15%.

Mr. Vandolder questioned who was investing PIMCO's fund. Mr. Wilson questioned the level of committed capital.

Ms. Stafford responded that there was \$700 million in committed capital, but could not provide a list of clients.

Mr. Vandolder questioned the political risks of the TALF program.

III. Non-Agency Mortgages and Impacts on Government Intervention (continued)

Ms. Salastekar and Ms. Stafford noted that the government could change the margin requirements, but only for new issuances.

Mr. Matheney questioned the impact of the TALF program on the economy especially at the expiration of the program.

Ms. Salastekar noted there may be selling pressure at the time the program ceases, but PIMCO was building protections by limiting maturities.

Ms. Salastekar summarized the PPIP (Public Private Investment Partnership) federal program noting it was sponsored by the Treasury and FDIC with the government investing dollar for dollar with investors in legacy loans and legacy securities in the RMBS (residential mortgage backed security) and CMBS (commercial mortgage backed security) markets.

The securities in this program are much different than those in the TALF program because they are both legacy and distressed. The leverage profile is also much different in the PPIP program, according to Ms. Salastekar, due to the lower credit quality.

In response to a question from Mr. Vandolder, Ms. Salastekar noted the expected returns for the program being in the low 20% versus the mid-teens for TALF.

Mr. Wilson questioned whether the program was currently operating and Ms. Salastekar responded that it was expected to begin in the near future and PIMCO was awaiting additional details on the PPIP from the Treasury and FDIC.

Mr. Matheney questioned whether these securities would be issued with recourse and PIMCO responded that all the details on this subject were not available just yet.

Mr. Vandolder questioned whether PIMCO was considering TALF in core plus investments and learned PIMCO had not been investing due to the leverage component.

Mr. Vandolder requested PIMCO's future outlook on inflation and how funds may protect assets in an inflationary environment.

III. Non-Agency Mortgages and Impacts on Government Intervention (continued)

Ms. Stafford noted a low risk for inflation in the short-term due to unemployment, but noted PIMCO's outlook for inflation on a secular (3–5 year outlook) basis. Ms. Stafford noted the protections provided by an allocation to TIPS (Treasury Inflation Protection Securities) and investments in real assets including the "All Asset" strategy offered in conjunction with Rob Arnott.

Mr. Wilson questioned whether PIMCO was increasing allocations to global TIPS.

Ms. Stafford noted that PIMCO could allocate to global TIPS tactically and PIMCO was currently neutral on the dollar. Ms. Stafford also commented on the "New Normal" and noted that there would probably be a reversion to the mean, but that the mean may be different than what one may expect.

IV. Credit Opportunities Across the Capital Structure

Billy Williams and Richard Rezek were present from STW along with Matthew Eagen and Rich Bruder from Loomis Sayles to discuss opportunities within the current credit markets.

Mr. Williams provided background on the current markets and described how credit spreads widened relative to Treasuries in 2008. Mr. Williams described 2008 as a once in a 13 billion year event. In Mr. Williams opinion, spreads widened due to forced sellers in the market place. Since late November, Mr. Williams noted that liquidity was returning to the market place and the similarities of 2008 to previous financial market panics.

Mr. Eagen described his experience with the "panic" including the impact on money market funds and the need for mutual funds to meet redemptions. Mr. Eagen also noted how thinly traded many securities were during this period and described the fall of 2008 as a nine standard deviation event.

Mr. Eagen provided the Board with an analysis of default rates over various historical periods.

Going forward, Loomis Sayles saw continuing opportunities in the investment grade credit markets and the high yield markets, although the high yield market was quickly becoming fairly valued.

IV. **Credit Opportunities Across the Capital Structure (continued)**

STW noted that spreads were currently being driven by supply/demand and fear/greed while credit fundamentals would not be driving spreads for at least another 12 months. STW also opined that it would be prudent to be taking more cyclical credit risk and they would be comfortable further down the capital structure in longer dated securities.

Mr. Vandolder questioned the managers on their inflationary views.

Mr. Eagen noted that Loomis Sayles wasn't too worried near term, but was concerned long term due to the Fed stimulus package. Mr. Eagen noted that the bigger problem was the size of the U.S. debt.

Mr. Rezek noted the continued issuance of government debt as being a concern. Mr. Williams noted the potential to limit interest rate risk if the bond portfolio's duration matched the plan's liabilities. Mr. Williams further emphasized his preference for corporate bonds.

Mr. Wilson requested Loomis Sayles and STW comment on the government's expected debt level and the future role of fixed income in a pension fund's portfolio.

Mr. Eagen identified the risks in a declining growth environment due to reinvestment rate risk. Mr. Eagen noted that Loomis Sayles did not hold Treasuries and Agencies, but did hold corporate bonds, CMBS and high yield. Mr. Eagen noted the problem for equities in an inflationary environment.

Mr. Williams commented on the difficulty in shortening the duration of a bond portfolio using futures and future government debt levels.

Mr. Vandolder asked why neither STW nor Loomis Sayles participated in the government programs.

Mr. Rezek commented that STW does not use leverage in their portfolios as directed by clients and was concerned with the quality of the securities within the programs. In addition, STW did not have the resources available to participate.

Mr. Eagen commented that Loomis Sayles chose not to participate due a scarcity of firm resources, but noted that Loomis Sayles was buying some of these government offered securities on an unleveraged basis.

Mr. Vandolder requested how Loomis Sayles and STW viewed the dollar.

IV. Credit Opportunities Across the Capital Structure (continued)

Mr. Eagen noted that Loomis Sayles was not a "dollar bear", but acknowledged that most of the future growth in the world would be outside the U.S. and currently invested approximately 4% of the portfolio in foreign markets. According to Mr. Eagen, the non-dollar exposure was concentrated in New Zealand, Canada and Australia.

Mr. Williams opined that the home currency was the low risk currency because plan liabilities are denominated in U.S. dollars.

Mr. Wilson commented on how good economies can be destroyed by poor government policies.

Mr. Williams and Mr. Eagan opined on U.S. debt levels and attempting to invest for doomsday scenarios.

Mr. Towner requested how Loomis Sayles and STW viewed Mr. Bernanke's performance as Chairman of the Federal Reserve.

Both STW and Loomis Sayles expressed confidence in Mr. Bernanke.

Mr. Goulet requested clarification on the level of consumer debt in the economy.

V. Private Equity Redux

Mr. Vandolder reintroduced Shane Shurter who arrived to assist the Board in its currency overlay decision

Ms. Young discussed the current market environment, opportunities that existed and how private equity programs may be implemented.

Ms. Young noted the variety of investment strategies within the asset class across all areas of the capital structure. Ms. Young recommended investors hold a long term view of the asset class and diversify the investment program through the use of different strategies, utilizing different geographical areas and varied vintage years. Also, Ms. Young discussed how private equity investors can move tactically within different sectors due to market conditions.

Ms. Young opined that this was a great time to be considering private equity investments due to access to top quartile funds in the primary and secondary markets.

Mr. Matheney questioned how the industry prices private equity investments.

V. **Private Equity Redux (continued)**

Ms. Young noted the difficulty of the appraisal process, but noted how FASB recommended comparable company analysis and discounted cash flow analysis.

Ms. Young reviewed the risk/return profiles of various private equity strategies and the strategies currently favored by EnnisKnupp including overweighting corporate finance (small/middle market), infrastructure and late stage venture capital.

Mr. Vandolder discussed the merits of investing in fund to fund strategies including the immediate diversification benefits.

Mr. Wilson questioned how managers raise capital in fund to fund strategies and the frequency of capital raises.

Ms. Young referred the Board to page 15 of the presentation illustrating the time horizon of a typical private equity investment and noted how investments were made early in the program with distributions/returns being generated in later years. Mr. Vandolder noted the challenges of reaching target allocations given the capital flows within a private equity program.

Mr. Vandolder noted three potential outcomes for the Board to consider including to choose not to fund a private equity allocation, direct EnnisKnupp provide a private equity fund to fund manager search for consideration in the fall and consider the private equity search in the fall with the addition of a satellite approach for tactical opportunities.

Mr. Matheney requested clarification on how private equity capital flows occur.

Mr. Wilson moved, seconded by Mr. Matheney, to have EnnisKnupp provide a search report for three private equity fund to fund managers in October.

Mr. Towner requested clarification on the impact of private equity on the fund's risk profile. In response, Mr. Vandolder stated it would move the risk profile slightly lower.

Mr. Harris requested whether there would be further study of VCERA's asset allocation with additional consideration given to "alternatives".

Mr. Goulet questioned why VCERA was not considering the other options discussed in EnnisKnupp's material and expressed concern regarding the fee levels for fund to fund strategies and objected to using option #4 due to the potential for conflicts.

V. Private Equity Redux (continued)

Mr. Towner reemphasized his concern with reaching the 8% earnings assumption rate and the amount of risk being added to the reach the targeted return.

Motion passed.

VI. Finalizing Currency Overlay Decision

Mr. Shurter discussed the benefits of active currency management including the uncorrelated return patterns for currency, the ability of active managers to add value and varying return patterns.

Mr. Goulet requested clarification on the correlations of the presenting managers relative to VCERA's total returns.

Mr. Shurter also discussed the volatility levels of the presenting managers and how each manager may contribute to the portfolio's risk level.

Mr. Wilson questioned whether VCERA should pursue multiple managers and noted the significant variance in recent performance numbers amongst the managers.

Lee Wanie, CFA, and Thomas Dobler, PHD, were present from Barclays Global Investors (BGI).

Mr. Wanie discussed BGI's competitive advantages in the active currency markets. In summary, Mr. Wanie discussed BGI's global presence, quality risk controls and research capabilities. Mr. Wanie stated that BGI has the ability to monitor currency markets 24 hours per day with a dedicated group of risk and credit market analysts. Mr. Wanie noted that BGI did not have any exposure to the counterparty defaults that occurred in 2008 and had a deep level of researchers dedicated to the currency markets.

Mr. Wanie discussed BGI's returns through April 2009, at the 2% risk level, of 1.26% with an active risk level of 1.96% that provided an information ratio of .64.

Mr. Dobler identified the sources of inefficiencies in the currency market and how active currency managers assumed the risks within the currency markets. Mr. Dobler also discussed how BGI identified the fundamental factors that drive the currency prices. Examples of fundamental factors include central bank decisions, balance of payments between countries and pricing differences. BGI then questions the predictive nature of the factors and whether the factors are additive to the existing model.

VI. **Finalizing Currency Overlay Decision (continued)**

Mr. Dobler described BGI's forecasting techniques that focus on fundamental values, the economic environment and overall market sentiment that attempts to asses investor behavior.

Mr. Dobler provided an example on the demand for New Zealand dollars based upon the price of wool given New Zealand's reliance on exporting wool.

In terms of risk management, BGI focuses on how closely currencies are matched and cross-hedges within regions to provide protections against regional liquidity crises. BGI also focuses on minimizing transaction costs in implementing trades as the reduction of trading costs impacts net returns materially.

Mr. Wilson questioned what makes BGI different.

Mr. Dobler responded that the transparency in the investment process was a differentiator and Mr. Wanie responded regarding the depth of the currency team was an advantage as well.

Steven Greenblatt and Dori Levanoni were present from First Quadrant to discuss their firm's currency capabilities.

Mr. Greenblatt outlined First Quadrant's organization and the drivers of VCERA's active currency manager search. Mr. Greenblatt summarized that VCERA was looking to generate alpha and also looking to improve diversification. Mr. Greenblatt analyzed VCERA's current asset allocation and the correlations towards various asset classes and which currency styles provide the best diversification benefits relative to VCERA's asset allocation. Additionally, Mr. Greenblatt analyzed the correlation benefits of First Quadrant's strategy relative to the Wilshire 5000 and MSCIWorld indices.

Mr. Greenblatt cited the distinguishing features of First Quadrant including the stability of the organization, diversified backgrounds of the investment professionals and the focus on fundamentals within the organization. In terms of currency management, First Quadrant focuses on a diversified approach rather than a certain style such as the carry trade.

Mr. Levanoni discussed First Quadrant's investment style and philosophy that focuses upon a quantitative approach with a corresponding diligent approach to risk management.

VI. **Finalizing Currency Overlay Decision (continued)**

Mr. Levanoni noted First Quadrant's use of the Purchasing Power parity valuation model and other models including supply and demand models based upon changes in capital flows, trade flows and economic imbalances. Mr. Levanoni also discussed the strategies First Quadrant does not employ including carry trade strategies and momentum strategies.

Mr. Levanoni reviewed the risk management processes within the firm and how the risk office at First Quadrant functions.

To summarize, Mr. Greenblatt described the distinguishing characteristics of First Quadrant's currency strategy including the diversification benefits for VCERA, the experience of the firm's currency team and the firm's risk controls.

Mr. Vandolder inquired regarding the availability of a commingled fund strategy to which Mr. Greenblatt responded that First Quadrant was willing to launch a commingled fund.

Mr. Goulet requested clarification on the fund's liability.

Karen Fernandes, Jordan Alexiev and Scott Carleton were present from State Street/Windham Capital.

Ms. Fernandes described the partnership between Windham Capital and State Street and discussed Mark Kritzman's role in the organization.

Mr. Alexiev described the strategy and distinguishing features of State Street Associates. Mr. Alexiev discussed the fund's return objective is to outperform 3-month LIBOR by 12–14% net of fees over three year periods with an expected volatility of 12–14%.

Mr. Alexiev identified and discussed State Street Associates' sources of alpha including the carry trade, trend analysis and their customized turbulence index. Mr. Alexiev also discussed how correlations among currencies can impact returns.

The most important piece of the investment process, according to Mr. Alexiev, was the turbulence index that determines when to shift between the carry trade component of the strategy and the trend component in order to provide a better risk adjusted return.

VI. Finalizing Currency Overlay Decision (continued)

Mr. Alexiev further defined State Street Associates' risk management process and the performance of the fund since 1997. Mr. Alexiev commented further on the correlations between the carry trade and the trend/momentum strategy.

Mr. Vandolder questioned the status of the commingled fund vehicle with State Street being the largest investor with $15 million.

VII. Board Member Comment and Reaction

Mr. Vandolder summarized the four key discussion points of the day being dislocation strategies, private equity, commodities and currency strategies.

Ms. Becker moved, seconded by Mr. Harris, to authorize a legal and competitive review of the federal government's dislocation strategies, including TALF, based upon a notional commitment of $10 million.

Motion passed.

Mr. Vandolder offered to deliver a research piece on the merits of commodity investing in July and discussed bringing closure to the currency manager search in July as well.

Mr. Matheney moved, seconded by Mr. Goulet, to review the overall asset allocation and decide what percentage to allocate to alternative investments including private equity by October.

Motion passed.

VIII. Adjournment

There being no further items of business before the Board, Chairman Towner adjourned the retreat at 4:50 p.m.

Respectfully submitted,

TIM THONIS, Administrator

Approved,

TRACY TOWNER, Chair