

# **BOARD OF INVESTMENTS MINUTES 6-9-10**

## **PRESENT**

- Herman Santos, Chair
- John M. Barger, Vice Chair
- Diane Sandoval, Secretary
- Simon S. Russin
- Mark J. Saladino
- Michael Schneider
- Estevan Valenzuela

## **ABSENT**

- Leonard Unger
- William Pryor

## **STAFF, ADVISORS, PARTICIPANTS**

- Gregg Rademacher, Chief Executive Officer
- Robert Hill, Assistant Executive Officer
- Lisa Mazzocco, Chief Investment Officer
- John McClelland, CRE, Principal Investment Officer, Real Estate
- Vache Mahseredjian, CFA, Principal Investment Officer
- Christopher J. Wagner, Senior Investment Officer, Private Equity
- June H. Kim, Senior Investment Officer, Equities
- Robert Z. Santos, Investment Officer, Fixed Income
- Gerald P. Flintoft, CAIA, Investment Officer, Private Equity
- Esmeralda Vita del Bosque, Senior Investment Analyst, Equities
- Dale Johnson, Senior Investment Analyst
- Robb Van Der Volgen, Chief Counsel
- Earl W. Buehner, Senior Staff Counsel
- Michael D. Herrera, Senior Staff Counsel
- Christine Roseland, Staff Counsel
- Cynthia Lau, Legislative Analyst

### **1. PUBLIC COMMENT**

None.

### **2. REPORT ON CLOSED SESSION ITEMS**

None to report at this time.

### **3. ACTION ITEMS**

1. Recommendation as submitted by Gregg Rademacher, Chief Executive Officer: Adopt the LACERA Fiscal Year 2010-2011 Administrative and Retiree Health Care Benefits Budgets. (Memo dated June 2, 2010.)

Mr. Rademacher provided an executive summary of the presentations made during the budget hearings which were held on April 29 and May 19, 2010. He also thanked the Board for attending. Mr. Rademacher reported that there were no changes made to the spending plan as a result of the

budget hearings. He thanked Shamila Freeman and Kaelyn Ung, LACERA's Budget Team, for their hard work and dedication in putting together the Budgets and he commended LACERA's Communications and Management Team for their help and input. A Brief discussion followed.

A motion was made by Mr. Russin, seconded by Ms. Sandoval to adopt the LACERA Fiscal Year 2010-2011 Administrative and Retiree Health Care Benefits Budgets. The motion carried by unanimous vote.

2. Recommendation as submitted by James Rice, CFA, Investment Officer: That your Board authorize staff to issue a Request for Proposal (RFP) with the minimum qualifications in this memo to search for one additional commodities investment manager. (Memo dated June 2, 2010.)

Mr. Rice provided a brief overview on the Commodities Structure and Implementation Plan and reported that on June 13, 2009, LACERA's Board had approved a new Asset Allocation Policy, which increased the target allocation for commodities from 2% to 3%.

LACERA invests in the commodity asset class to dampen Total Fund Volatility and to provide a hedge against inflation. LACERA currently uses two commodities managers, PIMCO and Neuberger Berman/Gresham. Staff is recommending a search for another commodities manager to implement the Board's new Asset Allocation Policy. A brief discussion followed.

A motion to approve the recommendation was made by Mr. Santos, seconded by Mr. Valenzuela. The motion carried by unanimous vote.

3. Recommendation as submitted by Cynthia Lau, Legislative Affairs Officer: That your Board continue its "watch" position on Senate Bill 414 relating to the process of filling Board member vacancies. (Memo dated June 2, 2010.)

Senate Bill 414 is sponsored by California Retired County Employees Association (CRCEA) and addresses the process of filling vacancies on boards of retirement and boards of investments in counties operating retirement systems under CERL. The bill was subsequently amended on May 19, 2010 to:

1. Specify that the alternate retired member may participate in the deliberations of any of its committees to which the alternate retired member has been appointed.
2. Specify that the alternate seventh member may participate in the deliberations of any of its committees to which the alternate seventh member has been appointed.
3. Require the Board of Retirement or Board of Investments (in the case of an elected-member vacancy) to cause an election to be held at the earliest possible date.

In summary, with respect to the alternate retired member and alternate seventh member having the ability to only participate in deliberations of committees to which they have been appointed, this does not impact LACERA's board members since its Committee meetings are considered a joint meeting of the Committee and the Board of Retirement.

A staff member in the Board of Supervisors Executive Office raised concerns with the phrase "cause an election" under Sections 7 and 8 of the bill. He believes that this language could be interpreted to shift responsibility for holding elections from the Board of Supervisors to the Board of Retirement/Board of Investments. CRCEA reports that this is not the intent and that the phrase "cause an election" does not mean "call an election". However, new language may be forthcoming. A brief discussion followed.

A motion was made by Ms. Sandoval, seconded by Mr. Barger to take a "Watch" position on SB 414. The motion carried by unanimous vote.

#### 4. REPORTS

1. PENN Capital Management — Manager Review  
Robert Z. Santos, Investment Officer, Fixed Income

(Memo dated June 1, 2010.)

## **PENN Capital Management**

- Peter R. Duffy, CFA, Senior Portfolio Manager & Partner
- Christine E. Formoso, Regional Director

Robert Santos provided a brief overview of PENN Capital Management's ("PENN") review. He reported that PENN personnel would make a formal presentation to the Board as required by LACERA's Manager Monitoring and Review Policy. He introduced the principals of PENN and they followed with a review of the portfolio.

PENN manages a high yield fixed income portfolio in LACERA's Emerging Manager Program. Their investment process incorporates a top down analysis of the macroeconomic cycle, including industry and sector reviews, quantitative screens of issuers, liquidity analysis, and qualitative research. Portfolios are well diversified with holdings representing, on average, between 1% and 3% positions (maximum issuer weighting is 3%).

PENN's performance as of April 30, 2010 outpaced the Barclays Capital High Yield Ba/B Index by 1.5%, but trailed the index by 1.2% for the one-year period, net-of-fees. Since the account's inception, the portfolio has underperformed by 14bps annualized, net-of-fees. PENN underperformed the benchmark by 509 bps in the second quarter of 2009, which caused the firm to experience its first observation below the lower performance band. The underperformance was the direct result of the firm's decision to avoid investing in financial sector bonds. Financials were the best performing sector within the High Yield Index for the quarter, returning nearly 93%, versus Industrial and Utility sectors which returned 57% and 33% respectively. PENN's underweight to auto-related securities, their cash exposure, and higher quality holdings detracted from the strategy's performance. Since the beginning of 2010, PENN's performance has begun to rebound. Calendar year-to-date, the portfolio has outpaced its benchmark by 166 bps and 151 bps, on a gross- and net-of-fees basis, respectively. A brief discussion followed on the emerging manager program and performance concerns. The report was received and filed.

2. Private Equity Portfolio Annual Report  
Christopher J. Wagner, Senior Investment Officer, Private Equity (Memo dated June 1, 2010.) (For information only.)

The Private Equity Portfolio Annual Report is information only and was received and filed.

3. For Information only as submitted by Cynthia Lau, Legislative Affairs Officer, regarding Assembly Bill 1913 — Diversity in State Pension Funds. (Memo dated June 2, 2010.) The memoranda relating to Assembly Bill 1913 is for information only and was received and filed.

## 5. GOOD OF THE ORDER

(For discussion purposes only.)

Mr. Rademacher reminded the Board of the Off-Site meeting which is scheduled to be held on July 14, 2010. The planned discussions will cover educational sessions on hedge funds, a review of the triennial Actuarial return assumption, capital market return assumptions and risk focused diversification. He encouraged the Board to attend. The Board commended Mr. Rademacher on the LACERA Budget Report and on LACERA receiving the GFOA Award, its 20th consecutive award.

## 6. EXECUTIVE SESSION

### 1. CONFERENCE WITH LEGAL COUNSEL — ANTICIPATED LITIGATION.

1. Initiation of litigation pursuant to subdivision (c) of California Government Code Section 54956.9.: One Potential Case The Board met in executive session pursuant to subdivision (c) of California Government Code Section 54956.9 to discuss anticipated litigation and there is nothing to report at this time.

## **Green Folder Items**

1. Chief Executive Officer's Report
2. Memo dated June 4, 2010, from Lisa Mazzocco, Chief Investment Officer regarding the July Board of Investments Meeting Schedule.

### 7. ADJOURNMENT

 PROTECT | We continue to employ solid investment and business strategies designed to serve the best interests of our members and their beneficiaries.

4/28/11