

BOARD OF INVESTMENTS AGENDA 5-9-11

LACERA

300 N. Lake Ave., Suite 810
Pasadena, CA 91101

9:00 AM

I. APPROVAL OF THE MINUTES

- A. APPROVAL OF THE MINUTES OF THE MEETING OF THE BOARD OF INVESTMENTS OF APRIL 13, 2011.

II. PUBLIC COMMENT

III. REPORT ON CLOSED SESSION ITEMS

IV. ACTION ITEMS

- A. Recommendation as submitted by James Rice, CFA, Investment Officer, Vache Mahseredjian, CFA, Principal Investment Officer and Gerry Flintoft, Investment Officer: Direct Staff to advance manager candidates to your Board for implementing a customized hedge fund of funds Program. (Memo dated April 29, 2011.)
- B. Recommendation as submitted by James Rice, CFA, Investment Officer, Vache Mahseredjian, CFA, Principal Investment Officer and Gerry Flintoft, Investment Officer: Invite the following firms to interview with your Board for a Hedge Fund of Funds mandate: Grosvenor, Blackstone, and Goldman Sachs. (Memo dated April 29, 2011.)
- C. Recommendation as submitted by Vache Mahseredjian, CFA, CAIA, ASA, Principal Investment Officer: Renew the Emergency Line of Credit (ELOC) with BNY Mellon. (Memo dated April 29, 2011.)
- D. Recommendation as submitted by Richard Bendall, Chief Audit Executive: Invite the following firms for interviews with your Board for the actuarial consulting services and actuarial auditing services projects: (Memo dated May 2, 2011.)
- Milliman, Inc.
 - The Segal Company
 - Gabriel Roeder Smith & Company
 - Cheiron, Inc.
- E. Recommendation as submitted by the Travel Policy Committee: Adopt the changes shown on the attached draft Education and Travel Policy. (Memo dated April 28, 2011.)
- F. Recommendation as submitted by Cynthia Lau, Legislative Affairs Officer: Recommend that the Board of Investments endorse a proposal which would require retirement systems operating under CERL to adopt a policy relating to education for board members.

V. REPORTS

- A. Real Estate Performance Measurement Report 4th Quarter 2010
Trina Sanders, Investment Officer, Real Estate (Memo dated April 25, 2011.)
The Townsend Group
Micolyn Magee, Principal
- B. Performance Review as of March 31, 2011
John McClelland, Interim Chief Investment Officer
- C. Chief Executive Officer's Report Gregg Rademacher, Chief Executive Officer (Memo dated April 28, 2011.) (For information only.)

VI. EXECUTIVE SESSION

- A. CONFERENCE WITH LEGAL COUNSEL — ANTICIPATED LITIGATION (Subdivision (c) of California Government Code Section 54956.9)
1. Initiation of litigation pursuant to subdivision (c) of California Government Code Section 54956.9: One potential case.

VII. GOOD OF THE ORDER

(For discussion purposes only.)

VIII. ADJOURNMENT

BOARD OF INVESTMENTS MINUTES 5-9-11

PRESENT

John M. Barger, Chair
Simon S. Russin, Vice Chair
Herman B. Santos, Secretary
Mark J. Saladino
Michael Schneider
Leonard Unger
Estevan Valenzuela

ABSENT

William Pryor
Diane Sandoval

STAFF, ADVISORS, PARTICIPANTS

Gregg Rademacher, Chief Executive Officer
Robert Hill, Assistant Executive Officer
Janice Golden, Assistant Executive Officer
John D. McClelland, Interim Chief Investment Officer
Vache Mahseredjian, CFA, Principal Investment Officer
Christopher J. Wagner, Senior Investment Officer, Private Equity
June H. Kim, Senior Investment Officer, Equities
James Rice, Investment Officer
Robert Z. Santos, Investment Officer, Fixed Income
Gerald P. Flintoft, CAIA, Investment Officer, Private Equity
Juan Almaguer, Senior Investment Analyst
Shelly P. Tilaye, CAIA, Senior Investment Analyst, 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
Johanna Fontenot, Senior Staff Counsel
Michael D. Herrera, Senior Staff Counsel
Christine Roseland, Staff Counsel

I. APPROVAL OF THE MINUTES

A. APPROVAL OF THE MINUTES OF THE MEETING OF THE BOARD OF INVESTMENTS OF APRIL 13, 2011.

A motion was made by Mr. Russin, seconded by Mr. Saladino, to approve the Minutes of the Meeting of the Board of Investments of April 13, 2011. The motion carried by unanimous vote.

II. PUBLIC COMMENT

None.

III. REPORT ON CLOSED SESSION ITEMS

None.

IV. ACTION ITEMS

- A. Recommendation as submitted by James Rice, CFA, Investment Officer, Vache Mahseredjian, CFA, Principal Investment Officer and Gerry Flintoft, Investment Officer: Direct Staff to advance manager candidates to your Board for implementing a customized hedge fund of funds Program. (Memo dated April 29, 2011.)

Staff provided the Board with an update on the hedge fund of funds (HFoF) Request for Information (RFI) and the proposed recommendation, directing staff to advance manager candidates to the Board for implementing a customized HFoF Program. Staff concluded that the goal of reducing total fund volatility while maintaining expected returns is achievable. Top HFoF managers could follow LACERA defined guidelines and generate expected returns of 6-8%, while limiting the Program to moderate levels of volatility between that of fixed income and public equities. The Program could further reduce total fund volatility because it is expected to have low to moderate correlation with LACERA's existing asset classes during most time periods and that such a Program could be implemented with satisfactory levels of liquidity, transparency and leverage. A brief discussion followed on strategy concerns. A motion to approve the recommendation was made by Mr. Valenzuela, and seconded by Mr. Unger. The motion carried with

Messrs. Saladino and Russin voting no.

- B.** Recommendation as submitted by James Rice, CFA, Investment Officer, Vache Mahseredjian, CFA, Principal Investment Officer and Gerry Flintoft, Investment Officer: Invite the following firms to interview with your Board for a Hedge Fund of Funds mandate: Grosvenor, Blackstone, and Goldman Sachs. (Memo dated April 29, 2011.)

A brief summary was presented on the finalists on the search for the Hedge Fund of Funds (HFoF) mandate. The proposed recommendation is that the Board invite Grosvenor, Blackstone, and Goldman Sachs. The Board authorized a request for information (RFI) for a hedge fund of funds manager, to identify candidates that could create a customized portfolio of hedge funds to reduce the total fund's volatility, without materially reducing expected returns.

Based on the evaluation process and all information gathered, the final scores determined the three finalists as follows:

Grosvenor's final score was 92. Grosvenor has specialized in hedge fund investing since 1971, and is one of the largest independent HFoF managers with over \$25 billion in assets under management (AUM), \$22 billion of which is managed on behalf of institutional investors. Their entire business is the HFoF, which differentiates them from the other finalists. The entire organization has been very stable, as the senior management team has been in place since the early 1990's. Grosvenor has a team of knowledgeable, experienced investment and due diligence professionals with a process that is thorough and disciplined.

Blackstone's final score was 90. Blackstone is a global alternative asset manager and financial advisory firm, founded in 1985. Blackstone's HFoF assets are managed by the Blackstone Alternative Asset Management (BAAM) division. BAAM was founded in 1990, to manage assets of the firm's partners and has developed into a leading HFoF manager, with \$33 billion in AUM. Approximately 90% of HFoF AUM is for institutional investors. They have one of the largest institutional client bases and have had a long-standing stable team structure. BAAM's key competitive strengths are in three areas: (1) developing a global macro view which is incorporated in their strategic allocation; (2) conduct impressive manager due diligence by investment and operational teams; and (3) identifying special opportunities for investment and creating unique funds by working proactively with hedge funds to capitalize on them.

Goldman Sachs' final score was 88. They manage client hedge fund portfolios through its Hedge Fund Strategies (HFS) team. They have approximately \$22 billion in AUM, half of which is managed on behalf of institutions. HFS, through a predecessor firm, acquired in 1997, has been investing in hedge funds since 1969. The senior people within HFS are knowledgeable and experienced, and are supported by a very capable staff that is empowered to participate in the decision-making process. One of the key advantages of HFS is their ability to leverage resources from Goldman Sachs' other global businesses.

The three finalists are leaders in the HFoF industry. Their strengths include managing in excess of \$20 billion in HFoF assets, employing over 100 professionals with specialized expertise in investment, operational due diligence, legal compliance, research and analytics. All three have demonstrated a strong fiduciary culture and are proactive in recommending and instituting best practices in the industry, protecting their clients' interest. A brief discussion following.

A motion to approve the recommendation was made by Mr. Valenzuela, seconded by Mr. Unger. The motion carried with Messrs. Russin and Saladino voting no.

- C.** Recommendation as submitted by Vache Mahseredjian, CFA, CAIA, ASA, Principal Investment Officer: Renew the Emergency Line of Credit (ELOC) with BNY Mellon. (Memo dated April 29, 2011.)

Mr. Mahseredjian provided a brief background on the proposed renewal of the emergency line of credit (ELOC) with BNY Mellon. He reported that staff had invited BNY Mellon (LACERA's custodian and current ELOC provider) to submit a proposal, along with five of the largest U.S. banks. Only three firms submitted proposals, and BNY Mellon's proposal was the most competitive. BNY Mellon has proposed an alternative product called Earnings Credit Plus (ECP). LACERA would deposit \$209 million into a BNY Mellon account (the account has 100% FDIC insurance through 12/31/12) that earns interest at a rate equal to the 90 day Treasury Bill yield plus 15 basis points, currently equal to a total of 20 basis points. LACERA would have daily liquidity through the Federal Reserve Fedwire settlement system. With the ECP, LACERA would save 15 basis points in explicit costs, but would have an opportunity cost of 90 basis points in potential return, for a net loss of 75 basis points. The ELOC is a preferred solution over the ECP, given the current level of interest rates. Staff has determined that the ELOC was the better choice. A brief discussion followed.

A motion was made by Mr. Santos, seconded by Mr. Saladino to continue this item to the next regularly scheduled meeting of June 8, 2011. The motion carried by unanimous vote.

- D.** Recommendation as submitted by Richard Bendall, Chief Audit Executive: Invite the following firms for interviews with the Board for the actuarial consulting services and actuarial auditing services projects: (Memo dated May 2, 2011.)
- Milliman, Inc.
 - The Segal Company

Gabriel Roeder Smith & Company

- Cheiron, Inc.

Mr. Granger provided an executive summary of the proposed recommendation, reporting that a Request for Information (RFI) was being conducted as part of the normal course of business and staff's continued effort to balance risks and controls. The current relationship with actuarial service providers have been in place since 1999 and staff feels it was time to test the market-place and determine the current competitors and fees. A brief discussion followed. A motion to approve the recommendation was made by Mr. Russin, seconded by Mr. Schneider. The motion carried by unanimous vote.

- E. Recommendation as submitted by the Travel Policy Committee: Adopt the changes shown on the attached draft Education and Travel Policy. (Memo dated April 28, 2011.)

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

- F. Recommendation as submitted by Cynthia Lau, Legislative Affairs Officer: Recommend that the Board of Investments endorse a proposal which would require retirement systems operating under CERL to adopt a policy relating to education for board members.

Ms. Lau provided a brief summary on the proposed endorsement of a proposal which would require retirement systems operating under CERL to adopt a policy relating to education for board members. A motion to approve the recommendation was made by Mr. Santos, seconded by Mr. Saladino. The motion carried by unanimous vote.

V. REPORTS

- A. Real Estate Performance Measurement Report 4th

Quarter 2010

Trina Sanders, Investment Officer, Real Estate

(Memo dated April 25, 2011.)

Micolyn Magee, Principal

The Townsend Group

Ms. Magee of The Townsend Group, LACERA's Real Estate consultant, gave a presentation on the Performance Measurement Report for the Fourth Quarter 2010 on LACERA's Real Estate Investment Program and conveyed that notwithstanding having experienced the worst real estate downturn in 25 years, LACERA's properties continue to signal a favorable turning point. In the fourth quarter 2010, LACERA's properties recorded net appreciation of 1.1%, its third increase since the third Quarter 2007.

Ms. Magee also reported that LACERA's core properties dominate the portfolio (since they represent 73% of the portfolio) and have performed well compared to the benchmark. Core assets are benchmarked to the NCREIF Property Index minus 50 (NPI-50) basis points. LACERA's core holdings have delivered a 4.3% net return over a five-year period, 130 basis points higher than the NPI-50). The core investment has served the Fund well, having met the goals of diversifying the total portfolio and generating good cash flow. The non-core investment has not fared as well during the downturn. The current slow pace of job growth, suggest that non-core investment will continue to suffer for some time. Non-core investments are expected to out-perform core in an improving market environment. The value-added component underperformed the five-year benchmark. Leverage is a major factor contributing to the under-performance. Future performance will hopefully be positively impacted as several commingled fund vehicles make new investments at the bottom of the market cycle. Commingled funds with significant uncalled capital should help future performance. LACERA's portfolio generated a one-year income return of 6.4%. A brief discussion followed and the Report was received and filed.

- B. Performance Review as of March 31, 2011

John McClelland, Interim Chief Investment Officer

The Performance Review as of March 31, 2011 is for information only and was received and filed.

- C. Chief Executive Officer's Report

Gregg Rademacher, Chief Executive Officer

(Memo dated April 28, 2011.) (For information only.)

The Chief Executive Officer's Report is for information only and was received and filed.

VI. EXECUTIVE SESSION

- A. CONFERENCE WITH LEGAL COUNSEL—ANTICIPATED LITIGATION (Subdivision (c) of California Government Code Section 54956.9)

1. Initiation of litigation pursuant to subdivision (c) of California Government Code Section 54956.9: One potential case.

The Board met in executive session to discuss an item of possible litigation and gave direction to Legal Staff. There is nothing further to report at this time.

VII. GOOD OF THE ORDER

(For discussion purposes only.)

The Board commended staff on their reports and presentations.

Messrs. Unger, Russin and Barger reported that Milken Institute's Global Conference was excellent and very informative. Mr. Rademacher reminded the Board that the Legal Office and Human Resources have arranged to provide Parliamentary Training for Board members and staff following the June 8, 2011 meeting.

Green Folder Items

- A. 1. Memo dated May 5, 2011, from Robert Z. Santos, Investment Officer, Fixed Income regarding Clearlend Securities.
- 2. Memo dated May 5, 2011, from Robert Z. Santos, Investment Officer, Fixed Income regarding Post Advisory Group.

VIII. ADJOURNMENT