

CONTRA COSTA COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

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May 30, 2007

The Board of Retirement met in regular session at 9:00 a.m. on Wednesday, May 30, 2007 in the Conference Room of the Contra Costa County Employees' Retirement Association, 1355 Willow Way, Suite 221, Concord, CA.

Present: Dave Gaynor, Brian Hast, Paul Katz, Sharon Naramore, William J. Pollacek, Jim Remick, Bob Rey, Jerry Telles, and Clifton Wedington.

Staff: Marilyn Leedom, Retirement Chief Executive Officer; Cary Hally, Retirement Chief Investment Officer; Rick Koehler, Retirement Accounting Manager; Toni Warren, Retirement Administration Manager.

Outside Professional Support: Representing:
Ashley Dunning Steefel, Levitt & Weiss
Bob Helliesen Milliman, USA
Tim Price Milliman, USA

Other Attendees:

Margie Breen Contra Costa County Employees' Retirement Association (CCCERA) Staff
James Lee Patrick Hubert Partners
Bob Campbell Auditor-Controller
Tina Kaufmann Auditor-Controller
Robert Leete San Ramon Valley Fire
Ranjit Sufi Nicholas Applegate
Brit Stickney Nicholas Applegate

1. Public Comment

No members of the public offered comment.

2. Approval of Minutes

After removing "EAFE" from a "130/30 product" and changing the second sentence to: "Wedington is now Vice President of SACRS" on Page 7, Item 13 (c) Rey's comments, it was M/S/C to approve the minutes of the May 16, 2007 meeting as amended. (Yes: Gaynor, Hast, Katz, Pollacek, Remick, Rey, Telles, and Wedington)

After an appeal to move Item 9 before the Board moved into closed session, it was the consensus of the Board to grant the request.

9. Ratify Contribution Rates for Consolidated Fire District

Koehler reviewed the rationale for his recommendation to the Board. It was M/S/C to accept staff's recommendation to ratify contribution rates for the Contra Costa Fire Protection District (Con Fire) effective July 1, 2007 through June 30, 2008. (Yes: Gaynor, Hast, Katz, Pollacek, Remick, Rey, Telles, and Wedington)

The Board moved into closed session pursuant to Govt. Code Section 54956.9(b).

The Board moved into open session.

3. Potential Litigation

No reportable action taken.

4. Review of Total Portfolio Performance

Milliman USA - Bob Helliesen

Helliesen began by noting the benchmarks adopted by the Board in April will be included in the 2nd Quarter 2007 report. After discussion on Nicholas Applegate, the liquidation of FFCA and the appraisal for Willows Office Park, Helliesen reviewed his report.

He noted that domestic equity markets registered modest gains in the first quarter of 2007, along with a significant amount of intra-quarter volatility. The S&P 500 returned 0.7% in the first quarter. Small capitalization stocks out-performed larger capitalization issues, with the Russell 2000® returning 2.0%. The median equity manager returned 1.7% and the broad market, represented by the Russell 3000® Index, returned 1.3%. International equity markets had strong results in the first quarter, with the MSCI EAFE Index returning 4.2%. The U.S. bond market was also positive in the first quarter of 2007, with the Lehman Aggregate Index returning 1.5% and the median fixed income manager returning 1.6%. Hedged international bonds were also slightly positive, with the Citigroup Hedged Index returning 0.9%. The domestic real estate market continued to post positive results in the first quarter of 2007, with the NCREIF Property Index returning 3.6% and the Dow Jones Wilshire REIT Index returning 3.7%.

CCCERA's first quarter return of 3.0% was better than both the median total fund and the median public fund. CCCERA has out-performed both medians over all trailing time periods, ranking in the upper quintile of both universes over the past one through five-year periods.

CCCERA total domestic equities returned 1.8% for the quarter, above the 1.3% return of the Russell 3000®, the 0.7% return of the S&P 500 and the 1.7% return of the median manager. Of CCCERA's domestic equity managers, Rothschild had the strongest performance with a return of 4.6%, better than the 3.1% return of the Russell 2500® Value Index. Emerald returned 3.9%, exceeding the 2.5% return of the Russell 2000® Growth Index. Progress returned 3.8%, well above the 2.0% return of the Russell 2000® Index. Intech Large Cap Core returned 2.9%, above the S&P 500. Wentworth returned 2.6%, well above the 0.7% return of the S&P 500. Intech Enhanced Plus returned 1.9%, above the S&P 500. PIMCO returned 0.9%, better than the S&P 500. Delaware returned 0.7%, below the Russell 1000® Growth return of 1.2%. ING returned

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0.6%, slightly trailing the S&P 500 (but matching the S&P 500 ex-Tobacco Index). Finally, Boston Partners returned 0.4%, trailing 1.3% for the Russell 1000® Value.

CCCERA international equities returned 6.0%, well above the 4.2% return of the MSCI EAFE Index and the 3.6% return of the median international manager. The GMO Intrinsic Value portfolio returned 4.8%, above the MSCI EAFE and S&P Citi PMI EPAC Value indexes, as well as the median international equity manager. McKinley Capital returned 7.1%, well above both the MSCI EAFE and MSCI ACWI ex-US Growth indexes, as well as the median international equity manager.

CCCERA total domestic fixed income returned 1.7% for the first quarter, above 1.5% for the Lehman Aggregate and 1.6% for the median fixed income manager. AFL-CIO's return of 1.7% was better than the Lehman Aggregate and the median fixed income manager. PIMCO returned 1.7%, above the Lehman Aggregate and the median. Western Asset returned 1.5%, matching the Lehman Aggregate but slightly trailing the median. ING Clarion returned 9.9%, well above the high yield fixed income median and the 2.7% return of the Merrill Lynch High Yield Master II Index. ING Clarion II returned 3.0% in the first quarter, above both the 2.7% return of the ML High Yield II Index and the high yield fixed income median manager. Nicholas Applegate returned 2.8% versus 2.7% for the ML High Yield II Index, but slightly trailed the 2.9% return of the median high yield fixed income manager.

The Fischer Francis Trees & Watts international fixed income portfolio returned 1.0% for the first quarter, slightly exceeding the 0.9% return of the Citigroup Non-US Government Hedged Index.

CCCERA total alternative investments returned 12.3% in the first quarter. The Bay Area Equity Fund reported a return of 25.4%, Nogales had a return of 22.5%, Pathway returned 17.8%, Energy Investor Fund reported a return of 15.4%, Adams Street Partners reported a return of 12.1%, Energy Investor Fund II reported a return of 2.3%, and the Hancock PT Timber Fund returned 1.5% for the quarter. (Due to timing constraints, all alternative portfolio returns except Hancock PT Timber Fund are for the quarter ending December 31.)

The median real estate manager returned 3.5% for the quarter while CCCERA's total real estate returned 5.3%. DLJ's RECP II returned 20.3%; DLJ's RECP III returned 15.9%; BlackRock Realty returned 6.1%; Adelante returned 4.0%; Prudential SPF-II returned 4.0%; Invesco returned 3.8%; DLJ's RECP I returned 3.7%; FFCA returned 2.7%; Fidelity returned 2.4%; and the Willows Office property returned 1.2%.

The Board expressed their pleasure with CCCERA situated in the top 3% of public funds.

There was discussion on the trend of public funds moving towards alternative investments, and CCCERA's target allocation to commodities. Hally noted discussion on the commodity allocation is scheduled to be on a future agenda.

Managers Under Review

After discussion, it was the consensus of the Board to not remove any investment manager currently Under Review from the Watch List.

5. **Nicholas Applegate, Collateralized Loan Obligation Fund II** - Ranjit S. Sufi, William L. Stickney

Sufi thanked CCCERA for the long-term relationship with their firm. He began by noting the number of discussions with CCCERA's Chief Investment Officer (CIO) and the investment consultant preceding this presentation.

Stickney provided a definition of Collateralized Loan Obligations (CLOs) and Collateralized Debt Obligations (CDOs). He then explained the attractive characteristics of bank loans, noting they were the least risky part of a capital structure. He then compared the primary benefits to the primary risks involved with investing in CLOs. He also reviewed the strengths of Nicholas Applegate in CLO management and the income and growth strategies of the team.

When asked if Nicholas Applegate would waive the confidentiality of their presentation material, Stickney agreed to waive the confidentiality.

Naramore was present for subsequent discussion and voting.

Stickney then provided a hypothetical capital structure, loan obligation return profile, and collateralized loan obligation timeline. He noted Collateralized Loan Obligation Fund II is a custom structure for CCCERA.

The presentation concluded by discussing the longevity of Stickney with Nicholas Applegate and the base fee for this product.

6. **Nicholas Applegate, Collateralized Loan Obligation Fund II**

It was *M/S/C* to accept staff's recommendation, to invest \$50 million with Nicholas Applegate, Collateralized Loan Obligation Fund II, subject to contract negotiation, a successful on-site visit and to authorize the CEO to sign all necessary documents. (Yes: Gaynor, Hast, Katz, Pollacek, Remick, Rey, Telles, and Wedington)

7. **Pathway Capital's International Exposure**

After Hally reviewed his recommendation to the Board, it was *M/S/C* to accept staff's recommendation to increase the percentage of non-U.S. commitments allowed in the private equity fund-of-funds portfolio managed by Pathway Capital Management to 30%. (Yes: Gaynor, Hast, Katz, Pollacek, Remick, Rey, Telles, and Wedington)

8. Capital Commitments

a. **INVESCO Real Estate Fund II**

Because approximately \$10 million of CCCERA's total \$50 million commitment for IREF I will not be called and invested, it was *M/S/C* to accept staff's recommendation to increase CCCERA's capital commitment of \$75 million to INVESCO Real Estate Fund II (IREF II) by \$10 million to a total commitment of \$85 million. (Yes: Gaynor, Hast, Katz, Pollacek, Remick, Rey, Telles, and Wedington)

b. **U.S. Power Fund III**

To help maintain an allocation of capital to an investment organization which has proven successful for CCCERA, to keep the total allocation to energy within alternative investments to a reasonable level for diversification reasons and to help move CCCERA towards its long-term target of 5% in alternative investments, it was *M/S/C* to accept staff's recommendation to increase CCCERA's capital commitment of \$50 million to United States Power Fund III, L.P. (USPF III) by \$15 million to a total commitment of \$65 million. (Yes: Gaynor, Hast, Katz, Pollacek, Remick, Rey, Telles, and Wedington)

Wedington noted the decisions were made easier because of the detailed information provided in the memos by the CIO.

10. Miscellaneous

- (a) Staff Report - Leedom noted an on-site visit with Ice Miller will be performed while staff and Board members are in Chicago for the Adams Street conference.

Normal Retirement Age will be on the agenda for a follow up review because of the latest information issued by the IRS.

The old closed session room will be remodeled to be used as a short term solution for the new General Counsel position.

Leedom noted the three-year Experience Study will be on the June 13, 2007 agenda and urged all Board members to attend the meeting.

- (b) Outside Professionals' Report - Nothing further

- (c) Trustees' Comments - Katz noted Hast's report on the ING Clarion Conference in the Board packet and requested a report from those that attended the recent NCPERS conference.

Rey noted as an addition to Hast's ING Clarion report, an eye needs to be kept on REITs with international real estate. Laws are changing to allow the same platform as U.S. REITs. He also reported on other aspects of the Global Real Estate Conference he attended.

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Pollacek - discussed the opportunities of Global REITs. Hally noted Global REITs will be on the agenda in June. Pollacek reported on the appointment of Tom Branan, originally with the Public Retirement Journal, to the position of Policy Director for the Public Employee Post-Employment Benefits Commission.

Telles - discussed the trustee orientation at the recent NCPERS conference, noting a session that gave trustees the role of an investor. He felt the training was valuable and entertaining. He also reported on other speakers during the conference.

It was *M/S/C* to adjourn. (Yes: Gaynor, Hast, Katz, Pollacek, Remick, Rey, Telles, and Wedington)



Clifton Wedington, Chairman



William J. Pollacek, Secretary