

# FEDERATED CITY EMPLOYEES' RETIREMENT SYSTEM

## Summary of Quarterly Investments Committee of the Whole

**THURSDAY**

**SAN JOSÉ, CALIFORNIA**

**February 26, 2009**

### Present:

**DAVID BUSSE, CHAIR**

Matt Loesch

Patrick Skillsky

Jeffrey Perkins

Pete Constant

Ed Overton

### Also Present:

**Russell Crosby** -Secretary/Director

Carmen Racy-Choy -Staff

Ali Amiry -Staff

Ron Kumar -Staff

Ceara O'Fallon -Staff

Cristin James -Staff

Patrick Thomas -SIS

Marc Gesell -SIS

Sheila Borer -McKinley Capital

Brandon Rinner -McKinley Capital

## MEETING SUMMARY

### PRESENTATIONS

The following presentations were given to the Board:

- ☐ **Strategic Investment Solutions (SIS) – Patrick Thomas**  
Performance Monitoring Report for quarter ending December 31, 2008.

Mr. Thomas explained that active managers had a difficult time exceeding their benchmark in 2008. Financials were the worst performing sector in the fourth quarter of 2008. Consumer staples and healthcare outperformed other sectors in the down market. The energy and materials sectors endured significant losses in the second half of the year. Commercial mortgage-backed securities and asset-backed securities were always considered AAA with low risk but now are trading like high yield bonds. During the fourth quarter of 2008, the portfolio experienced an 11.8% loss, which was slightly better than the policy index and ranked in the 24<sup>th</sup> percentile.

Ms. Racy-Choy stated that the goal of the System for investment returns is to meet or exceed the 9.15% (gross) actuarial assumption, which includes management fees. The portfolio did not meet the actuarially assumed rate for the System, which is currently underfunded. It is better to analyze the portfolio by the actuarial expectations instead of by comparison to its peers.

Member Perkins explained that the goal of the Trustees has always been to meet the actuarially assumed rates of the System, not to beat its peers. While the ten-year return of 4.2% is above other public plans, it is not good enough to fund the System.

Mr. Thomas stated that Wellington and The Boston Company performed well in the fourth quarter. Fisher, McKinley, and Dodge & Cox underperformed. SIS is in close contact with Dodge & Cox regarding the Large Cap Value strategy. Dodge & Cox has made poor stock selections in the financial sector and, thus, were hurt when the market declined so drastically. They are an example of a good manager who had a bad year.

Mr. Thomas added that The Boston Company stuck to their conviction through the down market and their belief in underpriced stocks finally paid off. SIS recommends removing The Boston Company from the Watchlist now that they are outperforming their benchmark.

Mr. Amiry explained that he and Mr. Thomas made a due diligence visit to Fisher recently. They observed that the organization is run by a small group of people with one person in charge of stock selection. They are not using a process that they can be held accountable for and not reacting to the market. Staff will present a recommendation regarding Fisher at a future meeting.

Mr. Amiry reported that he attended a meeting in February with Mr. Kumar and Ms. O'Fallon regarding our investment in PRISA. The company has cash flow issues and are having trouble selling off holdings to provide the cash needed, which may lead to some forced selling. There is a 2-3 year queue to withdraw out of this fund.

☐ **McKinley Capital Management** – Sheila Borer and Brandon Rinner  
Quarterly Report for period ending December 31, 2008.

Ms. Borer stated that there has been a change of ownership at McKinley Capital and now the company is 19% employee owned. Personnel has been stable with only a few support staff that left and were not replaced. McKinley hired a new compliance director in 2008. Assets under management dropped from \$16 billion to \$10 billion and McKinley Capital reopened the product for additional investments. Most of the drop in the portfolio value was due to market losses. There was a minor change to the process, which allows up to 75 names to be held in the portfolio.

Mr. Rinner explained that McKinley Capital has a bottom-up strategy, constructing their portfolio one stock at a time. There is liquidity in all stock purchases. The increase in the number of securities held in the portfolio should lower risk and allow for greater diversification in the portfolio. The portfolio is fully invested with only 2.5% in cash.

Mr. Rinner stated that McKinley Capital underperformed in 2008 largely due to energy and material holdings.

Member Overton stated that smaller, low quality stocks did better in 2008 and it appears that McKinley Capital does not invest in this sector.

Mr. Rinner stated that McKinley Capital's goal is to invest in higher quality stocks with more growth potential.

Mr. Amiry asked what was being done about the downside risk of buying higher priced stocks with a growth strategy, because, if the market does not go up, then the portfolio is at risk.

Mr. Rinner explained that McKinley Capital has a quantitative discipline. When a stock begins to show negative risk-adjusted performance it is sold.

**PERFORMANCE SUMMARY WITH BENCHMARKS – PERIOD ENDING DECEMBER 31, 2008**

Total Returns Net of Fees – (*Annualized)	Quarter	YTD	1 YR	3 YRS*	5 YRS*
<b>TOTAL FUND</b>	<b>-11.8</b>	<b>-24.0</b>	<b>-24.0</b>	<b>-2.4</b>	<b>1.9</b>
Custom blended benchmark	-12.3	-22.7	-22.7	-1.7	2.4
<b>DOMESTIC EQUITY PORTFOLIOS</b>					
<b>Large Cap Manager</b>					
<i>Atlanta Capital</i>	<b>-24.0</b>	<b>-36.4</b>	<b>-36.4</b>	<b>-7.6</b>	<b>-2.7</b>
Russell 1000 Growth	-22.8	-38.4	-38.4	-9.1	-3.4
<i>Dodge &amp; Cox Large Cap</i>	<b>-23.0</b>	<b>-42.2</b>	<b>-42.2</b>	<b>-11.9</b>	<b>N/A</b>
Russell 1000 Value	-22.2	-36.9	-36.9	-8.3	N/A
<b>Index Manager</b>					
<i>Northern Trust</i>	<b>-22.7</b>	<b>-37.3</b>	<b>-37.3</b>	<b>-8.6</b>	<b>-1.9</b>
Russell 3000	-22.8	-37.3	-37.3	-8.6	-1.9
<b>Small Cap Equity Manager</b>					
<i>Eagle Asset MGT</i>	<b>-26.3</b>	<b>-36.1</b>	<b>-36.1</b>	<b>-4.8</b>	<b>1.4</b>
Russell 2000 Growth	-27.4	-38.5	-38.5	-9.3	-2.4
<i>Brandywine</i>	<b>-25.2</b>	<b>-30.2</b>	<b>-30.2</b>	<b>-10.4</b>	<b>-1.8</b>
Russell 2000 Value	-24.9	-28.9	-28.9	-7.5	0.3
<b>All Cap Equity Manager</b>					
<i>Wellington</i>	<b>-22.1</b>	<b>-39.2</b>	<b>-39.2</b>	<b>-9.5</b>	<b>N/A</b>
Russell 3000 Growth	-23.2	-38.4	-38.4	-9.1	N/A
<b>INTERNATIONAL EQUITY PORTFOLIOS</b>					
<i>Boston Company</i>	<b>-15.6</b>	<b>-38.6</b>	<b>-38.6</b>	<b>-6.9</b>	<b>2.1</b>
<i>Fisher Investments</i>	<b>-25.2</b>	<b>-47.0</b>	<b>-47.0</b>	<b>-10.6</b>	<b>N/A</b>
<i>McKinley Capital</i>	<b>-22.2</b>	<b>-50.0</b>	<b>-50.0</b>	<b>-8.7</b>	<b>N/A</b>
MSCI ACWI (EX-US)	-22.3	-45.2	-45.2	-6.6	3.0
<b>FIXED INCOME PORTFOLIOS</b>					
<b>Domestic</b>					
<i>Dodge &amp; Cox</i>	<b>2.1</b>	<b>-1.1</b>	<b>-1.1</b>	<b>3.1</b>	<b>3.1</b>
<i>BlackRock</i>	<b>0.9</b>	<b>-1.9</b>	<b>-1.9</b>	<b>2.9</b>	<b>3.2</b>
Lehman Aggregate	4.6	5.2	5.2	5.5	4.7
<b>Global</b>					
<i>Loomis, Sayles</i>	<b>2.5</b>	<b>-1.7</b>	<b>-1.7</b>	<b>5.3</b>	<b>N/A</b>
Citigroup World Govt Non US	8.8	10.9	10.9	9.3	N/A
<b>REAL ESTATE PORTFOLIO</b>					
<i>MIG</i>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>16.1</b>	<b>7.5</b>
<i>Fidelity LP</i>	<b>-24.8</b>	<b>-34.8</b>	<b>-34.8</b>	<b>5.8</b>	<b>18.9</b>
<i>Fidelity Growth Fund III</i>	<b>-9.2</b>	<b>-24.1</b>	<b>-24.1</b>	<b>N/A</b>	<b>N/A</b>
<i>PRISA</i>	<b>-14.7</b>	<b>-13.7</b>	<b>-13.7</b>	<b>4.9</b>	<b>N/A</b>
NCREIF Property Index	-8.3	-6.5	-6.5	8.1	11.7
<i>GEAM Asset LP</i>	<b>-21.3</b>	<b>-21.6</b>	<b>-21.6</b>	<b>N/A</b>	<b>N/A</b>
<i>American Realty</i>	<b>-0.6</b>	<b>3.6</b>	<b>3.6</b>	<b>N/A</b>	<b>N/A</b>
<i>DRA Growth &amp; Income II</i>	<b>0.0</b>	<b>10.8</b>	<b>10.8</b>	<b>78.3</b>	<b>49.9</b>
<i>DRA Growth &amp; Income V</i>	<b>-1.2</b>	<b>3.8</b>	<b>3.8</b>	<b>8.8</b>	<b>N/A</b>
<i>DRA Growth &amp; Income VI</i>	<b>4.6</b>	<b>11.7</b>	<b>11.7</b>	<b>N/A</b>	<b>N/A</b>
NCREIF Property Index (Quarter lag)	-0.2	5.3	5.3	13.2	14.2
<b>PRIVATE EQUITY</b>					
<i>Private Equity</i>	<b>-5.6</b>	<b>-4.0</b>	<b>-4.0</b>	<b>2.3</b>	<b>N/A</b>
S&P 500 + 3% (Quarter lag)	-20.8	-34.0	-34.0	-5.2	N/A

**INFORMATION AND COMMUNICATION**

- ▣ Quarterly Proxy Voting Report.
- ▣ Report on Rebalancing Transfers.
- ▣ Commission Recapture Report.
- ▣ Investment Managers' Performance Reports for the quarter.

Approved:



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**RUSSELL U. CROSBY, SECRETARY / DIRECTOR**  
**BOARD OF ADMINISTRATION**