

FEDERATED CITY EMPLOYEES' RETIREMENT SYSTEM

Committee for Investments Summary

THURSDAY

SAN JOSÉ, CALIFORNIA

JANUARY 29, 2009

Present:

Jeffrey Perkins

Matt Loesch

David Busse

ALSO PRESENT:

Russell Crosby -Secretary/Director

Carmen Racy-Choy -Staff

Ron Kumar -Staff

Ceara O'Fallon -Staff

Cristin James -Staff

Patrick Thomas -SIS

RECOMMENDATIONS

NONE

MEETING SUMMARY

1. Discussion regarding the current Capital Markets.

Mr. Thomas reviewed the performance of the Federated City Employees' Retirement System ("System") and the asset classes in which the System invests for the last ten years. Large Cap US Equity benchmarks for the ten year period were negative. Bonds showed positive performance with a 5.00% gain. The total fund performance for the quarter of -11.77% slightly outperformed the benchmark of -11.86%. The one year performance for the System was -23.79%.

Mr. Thomas stated that the 42.0% loss in the Dodge & Cox domestic equity portfolio hurt the overall performance of the System. The Boston Company international equity portfolio's performance improved dramatically. The Fisher Investments international equity portfolio has consistently underperformed. BlackRock, domestic fixed income, and Loomis, global fixed income, both had a disappointing quarter.

Ms. Racy-Choy explained that Ali Amiry and Patrick Thomas met with Fisher and completed an in-depth due diligence visit. Both feel that Fisher is no longer an appropriate investment for the System. Staff is working with SIS on a recommendation to move the funds at Fisher to distressed opportunistic funds and small cap international funds. Searches for distressed opportunistic fund managers and small cap international fund managers should be completed and presented to the Committee in February or March.

Mr. Thomas stated that the whole western financial system received a capital call and, in the last 3 months, over-leveraged entities have panicked and raced toward liquidity. The Federal Reserve, U.S. Treasury, and Congress moved to address the risk to the financial system. The government stepped in to save some institutions while others like Lehman Brothers were allowed to file for bankruptcy. The U.S. economy is currently in a severe recession,

which will most likely continue through 2009. On the positive side, the price of oil has come down along with mortgage rates.

Member Perkins asked why, since this is a worldwide financial crisis, the System does not allocate more to cash at this time.

Mr. Thomas explained that there are a lot of distressed opportunities in the market because of the financial crisis. Distressed Mortgages and Super Senior Bonds have never traded below \$95 and are now trading in the \$60's. Those bonds should fundamentally be no less than \$80, which creates a great opportunity for the System to make money.

Ms. Racy-Choy stated that the Investment Policy allows up to 7.00% of the assets to be held in cash. Staff has been looking at moving more money to cash and possibly implementing some hedging within the Equity portfolio to help protect the System from further market declines.

Ms. Racy-Choy added that SIS is working on an Asset-Liability Study, which will look at market expectations and worst case scenarios. Hedging is very expensive in this market but can be used as a tool to manage risk.

2. Discussion and action on SIS's Distressed Private Equity recommendation.

Ms. Racy-Choy stated that this discussion will be deferred to a future meeting. She noted that distressed securities offer more opportunity and respond to what is happening in the current market.

3. Discussion and action on The Boston Company's fee revision.

Mr. Thomas stated that he visited The Boston Company for a due diligence review at the end of 2008. SIS believes The Boston Company is a top quality firm. They have maintained their investment process, which is finally paying off. As requested by the Investment Committee, SIS negotiated a 15% reduction to The Boston Company's sliding fee schedule with the new fee to remain in force until The Boston Company's three year trailing return exceeds the return of the MSCI ACWI Ex U.S. benchmark. SIS recommends that the System accept the negotiated fee arrangement with The Boston Company until the manager's returns improve.

Member Perkins suggested that a time certain constraint be added to the revised fee structure where The Boston Company's improved performance would be evaluated in one year and, if it still exceeds the benchmark, then the fee structure will revert back to the original schedule.

Ms. Racy-Choy suggested that staff should go back and calculate the point when The Boston Company began underperforming and calculate performance from that point going forward. When their performance exceeds the benchmark for one year, the fee should be returned to normal.

Mr. Thomas stated that he will speak with The Boston Company and add the time certain stipulation to the fee structure.

The committee recommended accepting the revised fee schedule for The Boston Company and allowing staff to negotiate any additional terms with The Boston Company.

(M.S.C.) Motion carried 3-0-0

4. Informational Item: Notification of Contracts due to expire on June 30, 2009.

Member Loesch asked if it would be reasonable to ask the managers to present to the Board before we negotiate a new contract.

Ms. Racy-Choy explained that when the Asset-Liability Study is completed the staff and SIS will re-evaluate all the managers. Staff and SIS will perform due diligence reviews to make sure that the System has the best possible managers.

5. Informational Item: Soft Dollar Transaction Report.

The Secretary stated his opposition to soft dollar transactions and would like to end the use of soft dollar by managers over time.

Mr. Thomas agreed that ending soft dollar over time is a good idea as the benefits the System receives are questionable and there is transparency with hard dollar transactions.

6. Informational Item: Update on Investment Managers on Probation & Watchlist – October and November 2008.

Ms. Racy-Choy explained that at future meetings the Committee will see a modified probation report. Staff currently uses commentaries from managers but would prefer to include information from an independent source. Staff has been reviewing a few research databases that could be used to provide independent, objective market information that would be useful to staff in evaluating managers.

Approved:



RUSSELL U. CROSBY, RETIREMENT DIRECTOR
BOARD OF ADMINISTRATION