

FEDERATED CITY EMPLOYEES' RETIREMENT SYSTEM

Committee for Investments Summary

THURSDAY

SAN JOSÉ, CALIFORNIA

FEBRUARY 26, 2009

Present:

Jeffrey Perkins

Matt Loesch

David Busse

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

RECOMMENDATIONS

1. Approval of Minutes:

a) Committee of the Whole Meeting, December 11, 2008.

b) Investment Committee Meeting, January 29, 2009.

MEETING SUMMARY

1. Approval of Minutes:

a. Committee of the Whole Meeting, December 11, 2008.

b. Investment Committee Meeting, January 29, 2009.

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

2. Discussion and approval to invest in Bank Loan, High Yield, and Convertible Bonds.

Dr. Amiry explained that bonds are loans made to an entity that are paid back periodically with interest. Issuers may vary from a small local firm to municipalities and state governments to the U.S. government. The factors that determine the price of a bond are maturity, credit worthiness of the borrower, and the inflation rate. In the last year, many individuals have assumed that businesses would go bankrupt so they rushed to invest their money in U.S. Treasury bonds, which are backed by the U.S. government.

Dr. Amiry stated that convertible bonds can be converted into a common stock at the option of investors usually at some pre-determined ratio. It is a hybrid security that pays interest like a bond, but can benefit from the upside price movement of the equity market. Due to current market conditions, the yield on these securities is between 9 and 10%. Convertibles are a good alternative investment in this market.

Dr. Amiry explained that a bond is considered high yield if it is rated BBB- or lower by the credit rating agencies. Generally, they are bonds that are judged by the rating agencies to be less likely to meet payment obligations (i.e. higher default rate). Given the current yield on these bonds, the risk reward balance is very attractive.

Chair Perkins asked how the portfolio would be balanced if the System was to invest in these alternative asset classes.

Dr. Amiry explained if the System does make an allocation to bonds then the funds would be taken out of the equity and fixed income allocations, which would reduce the risk to the portfolio. When the bonds mature, the proceeds will be received in cash. As cash is available, the Trustees can decide what new investments to make depending on the market situation at that time.

Ms. Racy-Choy stated that this is an asset class where active management will make a difference. The goal is to find a long-term active manager who has a proven track record in many market cycles. When the System makes a new investment, money would be taken from the asset classes that exceed the target allocation, which would reduce the risk in the overall portfolio.

Member Loesch asked how much money staff feels is appropriate to invest in this alternative asset class.

Dr. Amiry explained that staff is considering investing \$100 million in this asset class split evenly between Seix Investment Advisors and MacKay Shields. The allocation will be discussed in detail at the next meeting.

3. Discussion regarding Strategic Investment Solutions Inc.'s Capital Market Assumptions.

Mr. Thomas reviewed SIS's 2008 strategy for the System, which was to increase the private equity allocation to 5%, increase the international equity allocation, and to decrease the U.S. equity allocation.

Mr. Thomas stated that SIS develops their investment strategy using a process that looks at long-term portfolio growth. The portfolio needs to make sense in both up and down markets. The capital market expectations are determined using quantitative factors such as economic growth forecasts, return history, risk reward, and correlations. Each asset class is expected to perform based on past cycles.

Ms. Racy-Choy stated that the analysis conducted by staff shows higher numbers for "expected volatility" than those presented by SIS. Staff used historical relationships, but assumed that the future market will have a higher risk. The Asset-Liability Study that is currently being revised by SIS will run many market scenarios and analyze possible outcomes.

Dr. Amiry stated that 10 years ago no one would have projected that the equity market would show long-term, negative returns. In the last 20 years there had been high return with low volatility. However, the current market has very high volatility and negative returns. Staff feels that volatility will be higher in the future with continued lower returns.

4. Discussion and action regarding Fisher Investments.

Ms. Racy-Choy stated that this discussion will be deferred to a future meeting.

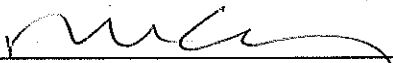
5. Approval to purchase access to investment databases.

Ms. Racy-Choy stated that this discussion will be deferred to a future meeting.

6. Informational Item: Commodity Futures Research Paper.

Ms. Racy Choy explained that there is concern that commodities are risky investments. Commodity futures are negatively correlated with stock and they are positively correlated with inflation. Commodities would add a high level of diversification to the portfolio. It is very important for a plan with a cost-of-living adjustment to have sufficient exposures that are tied to inflation, the most common being TIPS and commodities.

Approved:



**RUSSELL U. CROSBY, RETIREMENT DIRECTOR
BOARD OF ADMINISTRATION**