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FEDERATED CITY EMPLOYEES' RETIREMENT SYSTEM

Committee for Investments Summary

THURSDAY

SAN JOSÉ, CALIFORNIA

MARCH 12, 2009

Present:

Jeffrey Perkins
Matt Loesch
David Busse

ALSO PRESENT:

Russell Crosby	-Secretary/Director		
Carmen Racy-Choy	-Staff	Patrick Thomas	-SIS
Ali Amiry	-Staff	John Meier	-SIS
Ron Kumar	-Staff	John Cashwell	-Seix
Ceara O'Fallon	-Staff	George Goudelias	-Seix
Cristin James	-Staff	Kirk Kashevaroff	-MacKay Shields
Patrick Skillsky		Michael Kimble	-MacKay Shields
Pete Constant			

RECOMMENDATIONS

1. Approval for staff to initiate a Request for Proposals for an investment consultant.
2. Approval to invest in two separate accounts composed of Bank Loans and High Yield securities.
 - a. Approval to invest \$50 million each with Seix Investment Advisors and MacKay Shields.
 - b. Authorization for the Secretary to negotiate and execute agreements with Seix Investment Advisors and MacKay Shields.

MEETING SUMMARY

1. Discussion and action regarding Strategic Investment Solutions, Inc.

Ms. Racy-Choy stated that staff feels that Strategic Investment Solutions, Inc. ("SIS"), as a firm, lacks the depth of resources needed from an investment consultant to manage the assets of the Federated City Employees' Retirement System ("System"). Their strategy is 10 to 15 years out-of-date compared to the strategies in place in other plans in today's market. SIS lacks real estate expertise, hedge fund expertise, security lending experience, and commodities experience. In addition, there is no backup for Patrick Thomas if he is out of the office.

Ms. Racy-Choy added that an Asset-Liability Study (“ALM”) is usually completed by actuaries, who project the assets and liabilities of a plan in thousands of different scenarios, in order to analyze potential risks. They also analyze added risk and added return for each asset class in these scenarios. SIS has been utilizing staff with investment background to work on the ALM study as SIS does not have actuaries on staff.

Dr. Amiry stated that it is dangerous to have an investment consultant who is not in charge. If staff questions numbers on a report, SIS will change the report instead of providing their opinion and backup for original numbers. Staff has also found errors in reports produced by SIS and these reports are being provided to staff at the last minute, which causes staff to rush to get correct information to the Board. More importantly, it has been an issue with SIS not following up on managers regularly so that staff has to initiate due diligence visits with managers that are not meeting their benchmark.

The Secretary stated that if we compare the System’s portfolio with other public plans we would find that plans that had better access to alternative investments did much better over the last year.

The Secretary explained that SIS has been adding staff and consultants to cover the workload, but that does not help us in getting work completed currently. Staff would like to do an RFP for an investment consultant to see who else is in the market. The System has a vendor review policy where consultants are reviewed every six years.

Chair Perkins stated that the Board never expected SIS to have an actuary on staff back when they were working for the System on a project basis. Not staying on top of the managers, however, is a problem.

The committee approved giving staff the authority to initiate an RFP for an investment consultant.

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

- 2. Discussion and approval to invest in two separate accounts composed of Bank Loans and High Yield securities.**
 - a. Approval to invest \$50 million each with Seix Investment Advisors and MacKay Shields.**
 - b. Authorization for the Secretary to negotiate and execute agreements with Seix Investment Advisors and MacKay Shields.**

Dr. Amiry explained that staff recommends investing \$100 million in high yield bonds and bank debt with \$50 million to Seix Investment Advisors (“Seix”) and \$50 million to MacKay Shields. Staff determined guidelines for the managers to follow when selecting assets for the System’s portfolio. The current market conditions have provided a unique short-term opportunity for enhanced returns on investments.

Ms. Racy-Choy stated that the managers will not reinvest cash proceeds from this portfolio into other bank loans or high yield bonds unless directed by the Board. As the bonds mature, the proceeds will be used to invest in appropriate asset classes. Staff has been working on capital market assumptions in order to show the difference in projected returns with the addition of credit assets. The goal is to capture higher returns without adding risk to the portfolio.

Dr. Amiry stated that 90% of the risk in the System's portfolio is from the equity market; thus, to reduce the risk, direct exposure to the equity market needs to be reduced.

The Secretary stated that SIS had recommended a move to high yield bonds in the fall of 2008.

Mr. Thomas explained that SIS recommends an investment into this asset class and that Seix and MacKay Shields are good choices for managers.

Presentation by Mr. Kimble and Mr. Kashevaroff (MacKay Shields):

Mr. Kimble of Mackay Shields stated that the firm seeks to achieve attractive risk-adjusted returns by eliminating uncompensated risk. Their senior team has worked together for 20 years and has excellent, consistent outperformance over numerous market cycles.

Mr. Kimble explained during a bond's cycle, there are events that can cause both gains and losses to the price, such as in the current market where bonds are being sold at a discount. MacKay Shields is conservative, avoiding big risks and using client guidelines for the initial screening of bonds for the portfolio. The average price of a bond in the current market is sixty cents on the dollar so, when the market rallies, there will be gains.

Presentation by Mr. Cashwell and Mr. Goudelias (Seix Investment Advisors):

Mr. Cashwell of Seix stated that the firm has produced top-quartile performance since inception in the high yield portfolio. They have a buy and hold approach and look for short-to-medium maturity on the bonds they review. Their focus is on high-quality bonds that are income focused, stressing principal preservation.

Chair Perkins asked what it was that allowed Seix to outperform its peers.

Mr. Cashwell explained that Seix has had the discipline to stick to their investment process. In tough times, the process keeps the strategy on the defensive.

Chair Perkins asked if the Board was making these investments too late in the market cycle.

Mr. Goudelias of Seix explained that some opportunities are no longer available, but there are still many good assets in the market.

Ms. Racy-Choy stated that both SIS and staff are recommending that the Board invest in this asset class. It will be funded from BlackRock's domestic fixed income mandate.

The committee approved investment of \$50 million each with Seix Investment Advisors and MacKay Shields and authorized the Secretary to negotiate and execute agreements with Seix Investment Advisors and MacKay Shields.

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

Approved:



RUSSELL U. CROSBY, RETIREMENT DIRECTOR
BOARD OF ADMINISTRATION