

**REGULAR MEETING OF THE RETIREMENT BOARD OF ADMINISTRATION
WATER AND POWER EMPLOYEES' RETIREMENT PLAN**

MINUTES

MAY 9, 2012

Board Members Present:

Javier Romero, President
Cindy Coffin, Vice President
Mario Ignacio, Chief Accounting Employee
Ronald O. Nichols, General Manager
Barry Poole, Regular Member
Robert Rozanski, Retiree Member

Board Members Absent:

DWP Commissioner - Vacant

Staff Present:

Sangeeta Bhatia, Retirement Plan Manager
Monette Carranceja, Assistant Retirement Plan Manager
Mary Higgins, Assistant Retirement Plan Manager
Jeremy Wolfson, Chief Investment Officer
Julie Escudero, Utility Executive Secretary

Others Present:

Marie McTeague, Deputy City Attorney

President Romero called the meeting to order at 9:05 a.m.

Ms. Bhatia indicated a quorum of the Board was present.

Public Comments

Ms. Escudero stated no public comments were requested at this time.

1. Request for Approval of Minutes

- a) **March 14, 2012, Regular Meeting**
- b) **March 28, 2012, Regular Meeting**
- c) **April 4, 2012, Special Meeting**
- d) **April 11, 2012, Regular Meeting**

2. Termination from Rolls

- a) **Termination of Monthly Allowance from the April 2012 Retirement Roll**
- b) **Termination of Jeannine Y. Massie from April 2012 Permanent Total Disability Roll**

Mr. Rozanski moved that the Board approve Items 1 and 2; seconded by Ms. Coffin.

Ayes: Romero, Coffin, Ignacio, Nichols, Poole, Rozanski

Nays: None

THE MOTION CARRIED.

3. Report of Payment Authorizations for March 2012

4. Notice of Deaths for March 2012

5. **Investment Reports for March 2012**
 - a.i) **Summary of Investment Returns as of March 31, 2012 (new format)**
 - a.ii) **Summary of Investment Returns as of March 31, 2012 (old format)**
 - b) **Market Value of Investments by Fund and Month as of March 31, 2012**
 - c) **Market Value of the Retirement, Death, and Disability Funds and Retiree Health Care Fund as of March 31, 2012**
 - d) **Summary of Contract Expirations**
6. **Report on Status of Insurance as of April 10, 2012**
7. **Request from Board Member to Attend Training**
8. **Report on Organizational Changes at Oaktree Principal Fund V. LP**
9. **Report from Pension Consulting Alliance on Site Visit to Pyramis Global Advisors Trust Company**

Mr. Rozanski moved that the Board approve Items 3 through 9; seconded by Mr. Nichols.

*Ayes: Romero, Coffin, Ignacio, Nichols, Poole, Rozanski
Nays: None*

THE MOTION CARRIED.

10. Discussion of Pyramis Global Advisors Trust Company

Mr. Wolfson provided the background on this item which recommended the Board remove Pyramis Global Advisors Trust Company from organizational watch.

Mr. Rozanski moved that the Board approve Resolution No. 12-76 to remove Pyramis Global Advisors Trust Company from organizational watch; seconded by Mr. Nichols.

*Ayes: Romero, Coffin, Ignacio, Nichols, Poole, Rozanski
Nays: None*

THE MOTION CARRIED.

11. Presentation by Pension Consulting Alliance on New Private Equity Investment Opportunity

The Board acknowledged Tad Fergusson from Pension Consulting Alliance (PCA). Mr. Fergusson presented information on the Ares Corporate Opportunities Fund IV. He described it as a special situations partnership that targets middle market companies that have attractive growth opportunities but have experienced issues that prevent them from taking advantage of the growth opportunities. He noted Ares has consistently implemented a flexible investment strategy and has generated consistent attractive risk adjusted returns, and he stated PCA is recommending the Board commit \$25 million from the Retirement Fund and \$5 million from the Health Fund to Ares Fund IV.

In response to Mr. Nichols' concern with the lack of information on the process PCA uses to evaluate which firms they recommend as investments, Mr. Fergusson explained PCA receives approximately 300 to 350 opportunities each year, and they employ an ongoing detailed process to evaluate and prioritize each opportunity and match them with client needs given the market window. He described

that process and added that he provided additional information in the presentation material on how they evaluated Ares Fund IV. He indicated he will provide further information on the evaluation process for future recommendations.

In response to Ms. Coffin's statement that she continues to be concerned that PCA provides only one opportunity at a time, Mr. Fergusson explained the nature of the various investment opportunities makes it difficult to present multiple firms with the same strategies at the same time.

Mr. Rozanski asked about Ares' previous use of a placement agent in addition to reduced fees for CalPERS. Mr. Fergusson stated Ares had agreed not to use a placement agent in the future, and the fee reduction for CalPERS was related to the size of the relationship. He added the Ares representatives would address this in their presentation.

The Board then acknowledged David Kaplan and Merrit Hooper from Ares Management. Mr. Kaplan provided an overview of Ares Management and reviewed Ares' management platform, investment process, types of investments, and how they perform in different market environments. He reported their three previous funds performed in the top quartile with a compounded return of 24.5% on a gross basis and 17.8% on a net basis. He explained the Ares Fund IV is a \$4 billion private equity fund with a 2012 vintage.

Mr. Nichols asked about the length of a typical holding period. Mr. Kaplan explained they generally underwrite an investment to earn two and one-half to three times their money, which can typically take five to seven years.

In response to a question from Mr. Rozanski regarding leverage, Mr. Kaplan stated because they use less leverage in their buy-outs, they generally underperform those with more leverage and more risk. He described a typical transaction and stated one in four times the debt will convert to equity and three out of four times they will sell the debt and move on.

Ms. Bhatia asked Mr. Kaplan to speak to their past use of a placement agent. Mr. Kaplan explained they used a placement agent in 2010 to introduce them to The New York Common Retirement Fund and, as a result of using that placement agent, they successfully raised the fund; however, they signed a code of conduct with the New York Attorney General who investigated the situation. He stated they were not found of any wrong doing nor were they issued any fine. He added Ares Management is now a large enough firm with sufficient internal resources to market their products. With respect to the CalPERS fee reduction, he stated it was a commingled product and every investor paid the same fee with the same terms, and it did include a fee reduction in a separate, non-commingled account and in other products but not in private equity. He clarified they do not reduce fees for any private equity funds clients.

Also at the request of Ms. Bhatia, Mr. Kaplan described an example of an unsuccessful investment.

Mr. Rozanski moved that the Board adopt Resolution 12-77 to invest \$25 million from the Retirement Fund and \$5 million from the Health Fund in Ares Corporate Fund IV; seconded by Mr. Ignacio.

*Ayes: Romero, Coffin, Ignacio, Nichols, Poole, Rozanski
Nays: None*

THE MOTION CARRIED.

12. Discussion of International Equity Passive Guidelines

Ms. Bhatia explained the background of this item and stated the Investment Policy currently does not include investment guidelines for a Passive International Equity mandate. She stated Staff and representatives from Pension Consulting Alliance developed asset specific guidelines for this mandate which have been provided for the Board's approval.

Mr. Rozanski moved that the Board approve Resolution No. 12-78 to adopt the passive developed international equity investment guidelines; seconded by Mr. Ignacio.

*Ayes: Romero, Coffin, Ignacio, Nichols, Poole, Rozanski
Nays: None*

THE MOTION CARRIED.

13. Discussion of Active Value International Equity Manager Specific Investment Guidelines

Ms. Bhatia explained the Investment Policy currently includes only general investment guidelines for the Active Value International Equity mandate. She reported that as a result of the Board selecting MFS Investment Management as the new Active Value International Equity manager, Staff and representatives from Pension Consulting Alliance developed investment guidelines specific to the manager. She indicated the proposed manager specific guidelines have been provided for the Board's approval.

Discussion ensued regarding hedging with respect to currency.

Mr. Rozanski moved that the Board approve Resolution No. 12-79 to adopt the manager-specific active value international equity investment guidelines; seconded by Mr. Ignacio.

*Ayes: Romero, Coffin, Ignacio, Poole, Rozanski
Nays: None
Abstained: Nichols*

THE MOTION CARRIED.

14. Discussion of Investment Policy Benchmark

Neil Rue from Pension Consulting Alliance (PCA) explained this item was requested by Mr. Rozanski for a better understanding of why the Plan does not roll up and combine all of the benchmarks and allocations for the individual investment managers to create a customized benchmark for the Plan. Mr. Rue explained the Plan uses broad strategic class benchmarks for the major asset classes to have a comprehensive reference from which to compare the performance and adjust the allocations for each class. He explained if all of the underlying classes and managers, with their individual specific allocations, were rolled-up into a customized benchmark, it would be too specialized and would not allow for comparisons against other options.

He pointed out as an example, the performance results using the rolled-up concept and the comprehensive reference concept for the domestic equity class was basically the same, and the results for the international equity and fixed income classes varied slightly due to structural differences.

(The meeting recessed at 10:25 a.m. and reconvened at 10:36 a.m.)

15. Discussion of Performance of Fred Alger Management, Inc.

Mr. Wolfson provided a brief background for this recommendation to place Fred Alger Manager, Inc. on performance watch.

Mr. Rozanski moved that the Board approve Resolution No. 12-80 to place Fred Alger Management, Inc., Large Cap Growth Manager, on watch status; seconded by Mr. Nichols.

Ayes: Romero, Coffin, Ignacio, Nichols, Poole, Rozanski

Nays: None

THE MOTION CARRIED.

16. Annual Presentation by Fred Alger Management, Inc. – Large Cap Growth Manager

The Board acknowledged Peter Latara, Senior Vice President and Head of Client Relations; and Daniel Chung, Chief Executive Officer, Chief Investment Officer, and Portfolio Manager for Fred Alger Management.

Mr. Chung provided an overview of the firm and its philosophy. Mr. Chung explained the reasons for the firm's underperformance in 2011, reviewed the improved performance for the first quarter of 2012, and the current portfolio structure and outlook.

He reported the firm maintained strong performance in the first part of 2011 but by the end of the year had underperformed the benchmark by approximately 900 basis points. He reported the decline in performance which began in the third and fourth quarters was chiefly due to their stock selection and investment strategy. He indicated the portfolio lagged the benchmark in the third quarter by 560 basis points, chiefly due to investments in the energy and technology sectors and, although the energy weighting was in line with the benchmark, the firm's return was lower due to specific weightings within that sector. He noted the sell-off in technology was a defensive move atypical of their strategy but caused by concerns about the European crisis and reaction to the debt ceiling in the United States. He added performance improved in the fourth quarter and was up 8.4% but still trailed the benchmark which was up 10.6%. He again attributed this to their philosophy and stock selection.

He reported the portfolio had recovered 151 basis points in the first quarter of 2012 and outperformed the benchmark on a stock selection basis in the technology, industrials, and consumer sectors.

He stated they continue to employ their philosophy that fundamentals will win out over short term sentiment or volatility.

Following the performance review, Mr. Chung addressed the European market situation at length, as well as the expiration of the tax cuts implemented by the Bush administration.

17. Annual Presentation by T. Rowe Price – Large Cap Growth Manager

The Board acknowledged John Plowright, Client Services; and Rob Sharps, Portfolio Manager; and Ron Taylor, Portfolio Specialist from T. Rowe Price.

Mr. Plowright reported nothing new regarding the organization transpired since their last presentation; and the firm's investment process, philosophy, and staff remain unchanged since the Board hired T. Rowe Price two years ago.

Mr. Sharps provided a market overview and remarked on how and where they are considering investing.

He briefly reviewed the firm's performance and commented that 2011 was a difficult year for active large growth managers. He added in the first quarter of 2012 they recaptured more than what they underperformed in 2011. He attributed some of the underperformance to stock selection and the timing of when the portfolio was established. He noted the long history of this strategy has generated annualized excess returns of approximately 200 basis points and, given the opportunity and duration, the Plan's results would be similar.

18. Presentation by Courtland Partners—Fourth Quarter 2011 Real Estate Portfolio Performance

The Board acknowledged Bill Foster from Courtland Partners. Mr. Foster reported the portfolio's market value at the end of 2011 was approximately \$181 million (2.2% of the total plan), with another \$129 million of uninvested commitments. He reminded the Board that during the first quarter of 2012, the Plan committed \$20 million from the Retirement Fund and \$5 million from the Health Fund to BlackStone.

He reported portfolio's income return was 6.7% for the one-year period and 6.8% for the two-year period. He reported the total one-year return was approximately 19.5% gross/17.2% net, the two year return was 20% gross/17.5% net, and the longer time periods were slightly negative as a result of the sell-off that occurred in 2009 following the market collapse in 2008.

He reviewed the returns per categories with calendar year-to-date for Core at 16.9%, Value-Add at 19%, and Opportunistic at 9%. As for Opportunistic, he noted the LoneStar investments that are in the early stages are currently on track with an expected 20% net return.

He noted Value-Add still has the most opportunity with healthy income yields. He noted the goal is to continue with Core allocations which currently comprise most of the portfolio, although an increase in interest rates and inflation could adversely impact the value of those assets.

He compared the portfolio to the National Council of Real Estate Investment Fiduciaries (NCREIF) property index returns, which is an unlevered Core index. He reported the portfolio grossed 19.5% for the one-year period versus NCREIF at 14.3% and, compared to the Courtland Partners' index, the Plan's portfolio also performed very well.

He reviewed the Risk/Return. He noted the target allocation is 70% in Core, 20% in Value-Add, and 10% in Opportunistic, and they are aiming for 65% in Core, 25% in Value-Add, and 10% in Opportunistic. He noted the current Request for Proposal for \$50 million in REIT securities is a good proxy for Core real estate and would help reach the target Core exposure.

He also noted leverage is trending down and managers have done a good job of paying down debt. He stated the aim is for an 8% to 8.5% portfolio return with minimal volatility, and leverage is a key issue.

19. Retirement Plan Manager's Comments

Ms. Bhatia reported the results for the Active Member elections were received and approved by the DWP Board of Commissioners on May 1, and she congratulated Mr. Romero, Ms. Coffin, and Mr.

Poole on their reelection to the Board. In response to a question from Ms. Coffin, she stated generally the results of the election are announced only at the Retirement Board meetings. Ms. Coffin suggested a Department-wide announcement be made.

Ms. Bhatia noted earlier that morning management acknowledged the work and efforts of everyone involved in the implementation of the Integrated Pension System. She stated that even though the system's three modules have been implemented, a number of lingering items, for which there are manual processes, still need to be worked on with the vendor. She stated she will be meeting with the vendor tomorrow. She said work on the separate web-based module where members can access their information has not yet begun.

She reported Staff plans to update the Board at the next meeting on the Vontobel contract and new options on how to proceed.

She stated Staff also will bring a report regarding the recent selection of L.A. Capital.

20. Future Agenda Items

Mr. Poole requested an educational item on Emerging Manager programs.

With no further business, the meeting adjourned at 11:49 a.m.




Javier Romero
Board President

6/13/12
Date



Sangeeta Bhatia
Retirement Plan Manager

6/13/12
Date



Julie Escudero
Utility Executive Secretary

6.13.12
Date