

**EMPLOYEES' RETIREMENT SYSTEM OF THE CITY OF MILWAUKEE
ANNUITY AND PENSION BOARD**

Minutes of the Investment Committee Meeting
held December 12, 2008

The meeting was called to order at 9:10 a.m.

Committee Members Present: John Barmore
 Larry Holland
 W. Martin Morics
 Michael J. Murphy, Chair

Committee Members Not Present: William C. Carey
 Thomas Fischer (excused)
 Ron Walter

Retirement Staff Present: Bernard J. Allen, Executive Director
 Martin Matson, Deputy Director
 Tom Rick, Chief Investment Officer
 David Silber, Pension Investment Analyst
 Bruce Thomas, Pension Investment Analyst
 Ben Rode, Pension Investment Intern
 Suzanne Fortier, Board Stenographer

Others Present: Doug Kryscio and Patricia Hafner, Mercer Investment Consulting; Pam Newton, Walter Weisenburger; Richard Clark and Don Anderson, Northern Trust; Mark Egan and Thomas Fink, Reams Asset Management; and Beth Cleary, City Attorney's Office.

Fixed Income Structure Review and Recommendations. As a matter of information, Committee members received a copy of the presentation booklet, dated December 12, 2008. Ms. Hafner briefly recapped what has occurred with respect to the asset liability study. She said that today Mercer and the Committee will talk about the fixed income review, with some of the discussion about the number of managers, as well as the active versus passive decisions. Ms. Hafner indicated that Mercer did confirm that the benchmarks of ERS' managers are appropriate. She stated Mercer does not feel it is warranted to look at TIPS as a separate asset allocation. Ms. Hafner briefly talked about ERS' current fixed income managers and the fees paid to each manager.

Mr. Kryscio talked about what Mercer calls firm risk exposure, noting that the Board agreed to proceed with a cut to BGI when it comes to alpha tilts. He said Mercer is actually putting on the table a recommendation to also take money away from Loomis and Reams, which has nothing to do with a loss of confidence of any of these firms. Mr. Kryscio also stated these recommendations are also time dependent, possibly 6 months. The overall theme is Mercer recommends a fourth fixed income manager at a 5 percent allocation, which is anywhere from \$150 to \$200 million. He said the funding would come from taking 2 percent from Loomis, 1 percent from Reams and 2 percent from BGI. Mr. Kryscio asked the Board to think about considering whether you are comfortable with the 5 percent recommendation. He said that where Mercer splits up the 1 and 2 percents will be somewhat dependent when ERS is ready to look for another manager. Brief discussion ensued.

Mr. Kryscio said there will be times where there is an opportunity to make short-term and tactical moves, and from a governance perspective, ERS is not set up to do that. He said one thing Mercer would want the Board to consider at some point in the future is are you comfortable and willing to allow staff, with oversight from outside consultants, to have a percentage of assets to do short-term tactical moves, assuming they complete their due diligence and update the Board. Mr. Kryscio gave some examples and brief discussion ensued.

Northern Trust Custody and Investment Management Presentation. Mr. Thomas handed out an updated performance chart for the S&P 500 Index Fund and provided some background information. Ms. Newton thanked the Committee for the continued business between Northern and ERS, and stated that she has personally been doing business with ERS for 16 years. Mr. Weisenburger briefly addressed the Committee. Mr. Anderson talked about how securities lending works and how revenue is generated using cash collateral loans. He also talked about recent factors and events affecting the market and governmental support.

Mr. Anderson spoke about the committee at Northern that provides an overview of the collateral pool deficiency determination, and the impact of the collateral pool deficiency determination. Discussion ensued. He indicated that in order to ensure that all clients share equally in these liquidity risks, Northern Trust determined on September 19, 2008, that a collateral deficiency existed. Mr. Anderson said the declaration of deficiency left ERS with two payables to Northern Trust, and he talked about those payables. Mr. Anderson said that the \$3.8 million, which is the remainder of the deficiency, is related to the open cash pool in the core fund and is an unrealized liability based upon the prices of those securities having deteriorated. He commented on the Lehman security, stating ERS' pro-rata share valued at par is about \$393,000; the difference between the \$393,000 and the \$51,000, leaves ERS about \$342,000 that can be looked at as a realized loss, because the value of Lehman is not going to come back.

Mr. Anderson stated that since then, Northern has made a contribution to ERS' Fund to the tune of \$460,000 that was posted in October 2008. This was a direct contribution to ERS' Fund and can be used in any manner ERS sees fit. He indicated that ERS could use that to reduce the payable. He stated that the second step taken by Northern was to adjust the fee split effective October 1, 2008 to 76/24, which was done across the board to all clients in that pool. Discussion ensued. Mr. Anderson reported on earnings stating year-to-date through October, 2008, ERS earned approximately \$1.9 million, and in November 2008 ERS earned an additional \$262,000, putting ERS at \$2.2 million net through November.

Mr. Clark briefly talked about the portfolio performance as of September 30, 2008. Discussion ensued.

Mr. Murphy called for a break at 10:50 a.m. The Committee reconvened at 11:02 a.m.

Reams Asset Management Presentation. As a matter of information, Committee members received a presentation booklet, dated December 12, 2008. Mr. Rick handed out an Overview slide. Mr. Silber provided some background and performance information. Mr. Fink briefly talked about the firm stating as of September 30, 2008,

Reams has 81 fixed income accounts with \$10.2 billion under management. Mr. Kryscio asked if Reams has seen any client losses. Mr. Fink stated Reams has not seen any client losses, but numerous clients have made asset allocation changes looking to increase their equity allocations because equities are down so much. He talked about Reams' objectives and guidelines and their relationship with the ERS. Mr. Fink also provided a market review. On performance, Mr. Fink stated that year-to-date through November 30, 2008, ERS' portfolio is down about 13.5 percent, with the index marginally positive with a return of 1.5 percent. Discussion ensued.

Mr. Egan talked in length about the market environment, recession, and the stimulus package. He talked about the sector spreads in basis points and the reasons why Reams is optimistic. He said the portfolio is in quite good shape to do very well going forward. Lengthy discussion ensued throughout the presentation. Mr. Egan talked about the fixed income outlook and strategy summary. He also talked about the portfolio summary as of November 30, 2008. Discussion ensued.

Mr. Barmore called for a break at 11:42 a.m. The Committee reconvened at 11:47 a.m.

Real Estate Strategic Plan Update. As a matter of information, Committee members received a copy of the Real Estate Strategic Plan, January 2009. Mr. Rick stated last month the Committee met with Mercer and Townsend with respect to our target ranges for traditional asset classes, and also real estate. He indicated that after the Investment Committee and Board approved the changes to the target ranges for real estate, Townsend modified ERS' strategic plan to reflect the two items that were changed. Mr. Rick went over those changes reflected in the updated document.

There being no further business, Mr. Murphy adjourned the meeting at 11:50 a.m.

Bernard J. Allen
Secretary and Executive Director

(NOTE: All proceedings of the Annuity and Pension Board Meetings and related Committee Meetings are recorded. All recordings and material mentioned herein are on file in the office of the Employees' Retirement System, 789 N. Water Street, Suite 300.)