EMPLOYES' RETIREMENT SYSTEM OF THE CITY OF MILWAUKEE
ANNUITY AND PENSION BOARD

Minutes of the Investment Committee Meeting
held September 4, 2008

The meeting was called to order at 9:15 a.m.

Committee Members Present:	John Barmore William C. Carey W. Martin Morics Michael J. Murphy, Chair
Committee Members Not Present:	Thomas Fischer (excused) Larry Holland (excused) Sebastian Raclaw Ron Walter (excused)
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 Kathleen Conway, Board Stenographer

Others Present: Doug Kryscio, Mercer Investment Consulting; Jessie Magee and Katie Driver Ealy, Earnest Partners; Lawrence Spieth, Dimensional Fund Advisors; and Bob Peterman, Smith Barney.

2nd Quarter Performance Report. As a matter of information, Committee members received a Second Quarter 2008 Board Report submitted by Mercer Investment Consulting, ERS' 2nd Quarter Performance Report, dated September 4, 2008, and a report on Additional Manager Performance for the Second Quarter 2008. Mr. Kryscio talked about the economic environment, interest rates, inflation and unemployment rates. Discussion ensued. Using the 2nd Quarter Performance Report from ERS, Mr. Rick talked about the asset allocation as of June 30, 2008 stating that ERS was within our guidelines, with an overweight to fixed income and real estate. The Fund's value as of June 30, 2008 was $4.71 billion, which is $500 million less than the beginning of 2008. He indicated that from the 1st to 2nd quarter there was about a $115 million swingdown. Mr. Rick talked about the cash flows for the second quarter. He reported that during the 2nd quarter ERS slightly outperformed at -1.2 percent with our benchmark returning -1.3 percent. Mr. Rick stated the cumulative growth of a dollar chart shows an annualized return of 10.0 percent over five years compared to the benchmark return of 8.9 percent. Brief discussion ensued.

Mr. Silber reported that all domestic equity managers are plotting within their expected styles. For the quarter, growth outperformed value and small caps tended to outperform large caps. Within this environment the composite had a return of -2.1 percent during the quarter and underperformed its benchmark return of -1.7 percent. He indicated that the last twelve months relative return versus the benchmark are really impacting the longer term numbers. The domestic equity 5-year performance and statistics show ERS has generated an annualized return of 8.5 percent and, in this case, the alpha of -0.3 percent indicates the composite has not generated an excess return commensurate with the amount of risk taken. Mr. Silber talked about the relative investment performance of the domestic equity managers as of June 30, 2008, stating that unfortunately during the second quarter the majority of the Fund's domestic equity managers underperformed. He indicated the Fund's growth managers, Artisan and Turner, underperformed by the most; the value managers, DFA and Bernstein, also underperformed during the quarter. Mr. Silber reported that Earnest had a nice quarter with outperformance of 2.1 percent and Barclays outperformed by 1.8 percent. He briefly talked about the reasons for some of the managers' underperformance. Brief discussion ensued.

Mr. Silber reported on the international equity composite stating it had a return of -1.6 percent during the quarter, outperforming the benchmark return of -2.3 percent. He stated that although the composite is underperforming year-to-date, it has outperformed in all other time periods. The three and five year numbers are still very solid on both an absolute and relative return basis. The international equity 5-year performance shows it has generated above benchmark returns while taking on more risk than the benchmark. Mr. Silber reported that over the last five years the international equity composite has generated 18.9 percent in annualized returns, which has also outperformed its benchmark by 2.2 percent per year. He indicated that all three international equity managers outperformed their benchmarks during the quarter. William Blair's outperformance of about 30 basis points was mainly due to stock selection within the industrial sector; Brandes' outperformance of 0.1 percent is due to an overweight in Japan, as well as good stock selection and an overweight in the pharmaceutical sector. DFA's international small cap value strategy's outperformance of 0.5 percent was mainly due to stock selection within the materials and industrial sector.

Mr. Thomas reported on the fixed income composite stating that investors moving away from higher quality bonds to lower quality bonds resulted in high-yield bonds rising while treasuries declined. The fixed income composite had a -0.2 percent return, which outperformed the -1.0 percent return of the benchmark. For the second quarter, the fixed income composite was the best performing asset class outside of real estate. Year-to-date and for the one year timeframe, the composite has underperformed the benchmark. Over the three and five year time periods fixed income has outperformed the benchmark. The fixed income 5-year performance and statistics chart shows approximately 1.6 percent of excess return above the benchmark, with a 0.9 information ratio. Mr. Thomas reported that Loomis' outperformance eclipsed Reams' slight underperformance. He indicated that Loomis' corporate and high yield holdings were the main driver for its outperformance, while Reams allocation to mortgage backed securities was the main driver for its underperformance.

Mr. Thomas stated that as of September 3, 2008 the Fund had a market value of approximately $4.6 billion. In July 2008, ERS had a -1.5 percent return, which underperformed the benchmark by 50 basis points. In August 2008, ERS had a -0.1 percent return, which underperformed by 30 basis points. He also noted that year-to-date the Fund is down an estimated 9.2 percent, which underperformed its benchmark by 180 basis points.

Mr. Rick stated that the report from Mercer on the additional manager performance is a good document to see how ERS' managers are doing over the rolling three and five year time periods. Mr. Murphy indicated the Committee members could go through that report and bring any questions back to Mercer. Brief discussion ensued.

Earnest Partners Presentation. As a matter of information, Committee members received a presentation booklet, dated June 30, 2008. Mr. Rick handed out a Performance Update Chart. Mr. Thomas briefly talked about Earnest Partners background. Ms. Ealy indicated that they have not yet been with ERS for what Earnest would consider to be a full market cycle. Over the last three years Earnest has generated annualized outperformance of over 200 basis points. She gave a brief overview of the economic environment and how that climate has impacted ERS' portfolio. She reported that as of June 30, 2008, ERS' portfolio was valued at $211 million, with an estimated annual income of $2.2 million. Ms. Ealy mentioned that that income relates just to dividends and any interest that is earned on the small amount of cash held in the portfolio, which is fully invested at 95 percent in equities. She reported that for the 2nd quarter the portfolio outperformed the benchmark by about 200 basis points. The portfolio is up 5 percent year-to-date because of the negative returns in the 1st quarter, but still down slightly about 2 percent versus the benchmark being down 7.5 percent. On a one year basis, Earnest is outperforming the Russell Mid-Cap by over 800 basis points, with the portfolio being down slightly less than 3 percent versus the benchmark's 11 percent.

Mr. Magee talked about some of the companies Earnest invests in on ERS' behalf. He also talked about sector weighting, stating Earnest has relative overweights in energy, health care, and industrials, and relative underweights in materials, utilities and financials. He briefly touched on the equity portfolio characteristics and risk profile. Mr. Magee reported that Earnest began managing the portfolio with approximately $161 million. After a net withdrawal of $9 million, the investment performance generated just shy of $60 million, which brings the portfolio ending value as of June 30, 2008 to $211 million. Lengthy discussion ensued.

(Earnest Partners was excused at 10:25 a.m.)

Mr. Murphy called for a break at 10:25 a.m. The Committee reconvened at 10:37 a.m.

Dimensional Fund Advisors Presentation. As a matter of information, Committee members received a presentation booklet, dated September 4, 2008. Mr. Rick handed out a Performance Update Chart. Mr. Silber briefly talked about DFA's background. Mr. Spieth indicated the two mandates that ERS has are essentially the same. He indicated that what DFA does is provide exposure to small cap stocks in the United States and small cap stocks with a value bias in both the U.S. and international markets. What is not included is emerging markets, which is not what DFA was hired to do. Mr. Spieth said over long periods of time we know there is a bias towards small companies and value stocks have had higher rates of return than growth stocks and large caps. We also know that recently we have had a flight to quality, so the asset class that ERS is in with DFA, and other classes that are small or value oriented have not done well.

Mr. Spieth stated this flight to quality is in part because of the financial crisis and a lot of things that Wall Street did that they should not have done. He indicated he is talking about the people who put this together; that it was junk and misleading, such as the head of Merrill Lynch. Unfortunately, it permeates a lot into the system. Mr. Spieth said another thing that is going on in the last two weeks such as the political conventions, brings uncertainty to the markets, and there are a whole lot of negative things going on. He said that it is his own belief that, domestically, we have not bottomed out. Brief discussion. Mr. Spieth noted that DFA buys deep value stocks and what they have done is put on a momentum filter, which is something that is not perfect, but it does help when stocks are crashing relative to its marketplace. He stated that if growth or large cap stocks are doing well, DFA will not do as well. When value stocks do well, DFA tends to do much better than the benchmark.

Mr. Spieth indicated that since the last time he was here, DFA has appointed a second generation of people to run DFA: Chief Operating Officer, Chief Investment Officer and Portfolio Manager. There is a transition plan going into place right now for future change in the firm. He went on to discuss DFA's performance against the conventional benchmark. Most of the portfolio has been able to add value without doing traditional stock picking or market timing. Mr. Spieth talked about the historical basis of how DFA invests. He also talked about the market environment through the first six months of 2008, DFA's portfolio construction, and their buy and sell discipline. Lengthy discussion ensued.

(DFA was excused at 11:27 a.m.)

Approval of Asset Liability Study Implementation Plan. As a matter of information, Committee members received a presentation booklet, dated August 20, 2008. Mr. Kryscio directed the sub-committee members to page 4. He said the first thing to do is an equity structure review and fixed income structure review. Mr. Kryscio asked if the sub-committee could give him a general sense to go ahead and do that as it does not involve new asset classes. After brief discussion, the sub-committee's consensus was to proceed to do the equity and fixed income structure reviews at this time.

Acceptance of Artisan Partners Due Diligence Report. As a matter of information, Committee members received a memorandum from Mr. Thomas, dated September 4, 2008. Mr. Thomas said he, Mr. Silber, Mr. Rick, Mr. Allen and Mr. Kryscio went to visit with Artisan in July 2008. While they continue to do what ERS hired them to do, they have struggled as of late. He noted that the stepping down of Carlene Ziegler as the Co-Portfolio Manager for the small cap growth strategy leaves the strategy under-resourced. ERS is hoping at some point in time Artisan will add an investment analyst to address that issue. Mr. Thomas indicated that ERS staff and Mercer would continue to monitor their performance and resource levels. Mr. Kryscio stated that Ms. Ziegler has probably taken less and less role in this portfolio in the last couple of years, but he did not think Artisan would admit to that. It is not a huge concern, it just happened to coincide with some tough performance, which had nothing to do with Ms. Ziegler leaving, but more that their style fell out of favor.

Update on Custody RFP. Mr. Rick reported that ERS has received four responses: JP Morgan, Northern Trust, State Street and Bank of NY Mellon. An internal committee has been reviewing the responses, with Mr. Barmore leading the committee. He stated there are demonstrations scheduled for September 10 and 11 so any Board members are welcomed to attend. Mr. Rick indicated that a recommendation would be drafted after those meetings to present to the A & O Committee for a recommendation to the full Board.

There being no further business, Mr. Murphy adjourned the meeting at 11:35 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 Employes' Retirement System, 789 N. Water Street, Suite 300.)