

**CONTRA COSTA COUNTY EMPLOYEES' RETIREMENT ASSOCIATION**

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July 19, 2006

The Board of Retirement met in special session at 1:00 p.m. on Wednesday, July 19, 2006 in the Conference Room of the Contra Costa County Employees' Retirement Association, 1355 Willow Way, Suite 221, Concord, CA.

Present: Richard Cabral, Dave Gaynor, John Gioia, Brian Hast, Paul Katz, Louis Kroll, Sharon Naramore, William J. Pollacek, Jerry Telles, and Clifton Wedington.

Staff: Marilyn Leedom, Retirement Chief Executive Officer; Cary Hally, Retirement Chief Investment Officer; Toni Warren, Retirement Administration Manager.

Outside Professional Support:      Representing:  
Ashley Dunning      Steefel, Levitt & Weiss  
Bob Helliesen      Milliman, USA  
Tim Price      Milliman, USA

**Other Attendees:**

Luz Casas	Contra Costa County Employees' Retirement Association (CCCERA) Staff
Mihir Worah	PIMCO
Ethan Leidingner	Goldman Sachs
Kevin Dachille	OFI Institutional
Tim Muffley	OFI Institutional
Mike Keough	Goldman Sachs
Jonathan Fraade	AIG Financial Products
Stephanie King	PIMCO
Lloyd Sawchuk	Self
Dante Siracusa	Contra Costa Courts
John Miller	PIMCO

**1. Public Comment**

No members of the public offered comment.

**2. Commodities Education Session**

Helliesen began by noting his delight with the distinguished panel present to discuss investing in Commodities. He then introduced and provided a brief background for the panel members, noting their presentations would go from conservative to more progressive in investing in futures.

**John Fraade - AIG**

Fraade began by noting, historically, commodity index returns have been comparable to the returns of stocks but with lower volatility. Commodity futures markets are large liquid markets regulated by the Commodity Futures Trading Commission (CFTC). Exposure to commodity indexes can be gained in a variety of ways. For large institutional investors, the most common vehicles are: managed accounts, OTC derivatives such as swaps and options, index-linked securities, and futures contracts.

Fraade reviewed risk and return by asset class, annualized monthly returns from 1959 to 2006. He noted commodity futures have delivered equity-like returns with similar volatility. He then reviewed spot vs. futures returns with inflation adjusted performance from 1959 to 2005. He stated commodity futures returns are not the same as spot returns.

Fraade noted commodity futures returns historically exhibit negative correlations to stock and bond returns and have maintained performance when equity returns are under stress. Commodity index investments represent a small percentage of a deep liquid OTC commodity derivatives market.

The two major commodity futures indexes are the Dow Jones-AIG Commodity Index (DJAIGCI) and the Goldman Sachs Commodity Index (GSCI). Both the DJAIGCI and the GSCI are broad-based indexes representing unleveraged, long only positions in a fully-collateralized basket of exchange traded futures on physical commodities. Both indexes have the transparency, liquidity and diversity sought by institutional investors.

Gioia was present for subsequent discussion and voting.

Fraade reviewed sector exposure in both the DJAIGCI and the GSCI indexes. He concluded by noting the long term performance of the DJAIGCI and the GSCI is comparable; however, annual returns of the two indexes can vary. Historical volatility of the DJAIGCI is lower than GSCIT volatility, but both indexes can diversify investment portfolios and hedge inflation.

**Mihir Worah - PIMCO**

Worah began by reviewing major considerations for investing in commodities, both for return potential and diversification benefits.

Potential sources of excess return from active management are over/underweighting commodity exposure, collateral management, and the potential to capitalize on structural inefficiencies within commodities futures markets. He noted implementation of basic indexes, as well as structural strategies, can be done with derivatives for efficiency.

He introduced and explained two terms used in commodity trading: "backwardation" and "contango". He noted historically backwardation has been preferable.

Worah concluded by reviewing the key requirements of a commodity manager. They must have an understanding of various instruments used to gain the most efficient commodity exposure. When swaps are used, managers must have: established International Swaps and Derivatives Association (ISDA) documents with client-friendly terms; demonstrated ability to assess and diversify counterparty risk; tested back-office procedures, margin flow management and the strong ability to perform in periods

of market disruption. The manager should have expertise in managing collateral (liquidity and incremental return) and across multiple structural performance strategies.

Kroll was not present for subsequent discussion and voting.

**Kevin Dachille - OFI**

Dachille began by discussing the *GSCI* vs. the *DJAIG* indexes noting both indexes have outpaced inflation in higher inflation years and both indexes have produced similar returns over the long-term. *GSCI* has produced greater volatility than *DJAIG* while both the *GSCI* and *DJAIG* have similar negative correlations to other asset classes.

He noted the important link between volatility and correlation: covariance. The portfolio diversification is greater with higher volatility when there are asset classes with negative correlation. Over the past 15 years, the *GSCI* has provided greater negative covariance (diversification).

Dachille concluded by discussing the implementation of passive vs. active commodities management.

**Ethan Leidinger - Goldman Sachs**

Leidinger began by noting it is possible to generate excess returns through a diversified set of strategies with three broad categories: relative value, timing and event driven. He stated the primary objective is to achieve *GSCI* index exposure. However, he noted, one might also attempt to add alpha via early rolls of individual futures and yield enhancement.

He then discussed forecasting the relative attractiveness of individual commodities in the *GSCI* index using intermediate-term momentum, implied yield, value, long-term reversal, inflationary fears, and term spread for investment themes.

He concluded by noting over time, both inexpensive and high-momentum assets have provided significantly higher returns.

**Panel Discussion**

There was a great deal of discussion on the volatility of the *GSCI* index. The two indexes for commodities have similar returns and *GSCI* has more volatility. It was discussed that one of the primary reasons for investing in commodities is the diversification benefits of the asset class' negative correlation. Commodities would be constrained at 2% of the portfolio.

**3. Commodities**

Some indicated their reluctance to vote on commodities investing at this time. They suggested the investment be revisited and placed on a future agenda.

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After continued discussion that investing 2% in commodities came out of an asset allocation study and is appropriate, there was a **motion** to proceed with investing in commodities.

It was **M/S/C** to call for the question. (Yes: Cabral, Gaynor, Gioia, Hast, Katz, Pollacek, Telles, and Wedington)

On the original motion, it was **M/S/C** to instruct Milliman to go forward, through the RFP process, with commodity investments and to bring recommendations back to the Board. (Yes: Gaynor, Gioia, Hast, Katz, Pollacek, Telles, and Wedington; No: Cabral)

**4. October 25, 2006 Meeting Date**

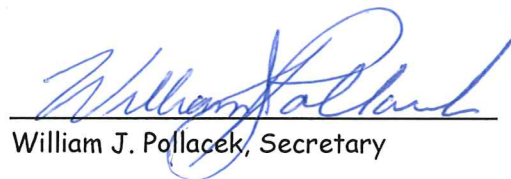
It was **M/S/C** to change the October 25, 2006 meeting to October 18, 2006 at 9:00 a.m. (Yes: Cabral, Gaynor, Gioia, Hast, Katz, Pollacek, Telles, and Wedington)

**8. Miscellaneous**

- (a) Staff Report - Leedom noted Annual Benefit Statements were mailed on July 18, 2006.
- (b) Outside Professional Report - nothing further
- (c) Trustees' Comments - nothing further

It was **M/S/C** to adjourn. (Yes: Cabral, Gaynor, Gioia, Hast, Katz, Pollacek, Telles, and Wedington).

  
Clifton Wedington, Chairman

  
William J. Pollacek, Secretary