# PARS: County of Contra Costa

## Fourth Quarter 2014

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# DISCUSSION HIGHLIGHTS

## U.S. Economic and Market Overview

The U.S. economy continued to represent perhaps the brightest opportunity across global markets in the fourth quarter of 2014 and for the full year. The continuing strength of the U.S. economy, as represented by two consecutive quarters of 4% or higher annualized GDP growth, provided investors around the world with sufficient reasons to add to their holdings of U.S. stocks, bonds, and dollars. As 2014 came to a close, a series of positive economic indicators, some at their highest levels in a decade, highlighted the domestic economy's slow but steady recovery from the Great Recession. These included:

- Consumer Sentiment – Final December 2014 figure of 93.6 is highest since January 2007.
- Consumer Spending Growth – Continued improvement with 0.6% growth in November.
- Rising Average Earnings – Up 1.7% in 2014 and annualized wage growth of 5% predicted for 2015.
- Non-Farm Payroll Growth – Averaged 206,000 jobs per month since the beginning of 2012 with total growth exceeding 7 million jobs.
- Unemployment – 5.6% at year-end and lowest since June 2008.
- Corporate Merger and Acquisition activity – 2014 had highest value of deals in 7 years.
- U.S. Dollar – Continued strength in 2014 against the world's major currencies.

Given the welcome news from the U.S., one might think that domestic Treasury rates would be higher, but economic issues around the world continued 2014's flight to quality U.S. debt, pushing rates even lower during the 4$^{th}$ quarter. These issues include potential deflation in Europe, China's transition from a country of manufacturers to one of consumers, and Japan's seemingly endless effort to restore economic growth. By year-end, the gap between domestic and international developed economies was perhaps best expressed by the spread between 10-year U.S. Treasuries and the equivalent German government bond of 1.6%, a difference which stood at its highest level in the last 25 years and spotlights investors' global growth concerns about global growth.

As 2014 drew to a close, weakness in non-U.S. economic growth weighed on returns with nearly all international equity indices posting negative numbers (for the quarter MSCI EAFE was -3.57% and MSCI EM was -4.50%; for the year MSCI EAFE was -4.90% and MSCI EM was -2.19%) despite the U.S. being firmly in positive territory (for the quarter S&P 500 was +4.93%; for the year S&P 500 was +13.69%). While this global disparity has created diverging returns, and potentially appealing opportunities, it has punished globally diversified investors. HighMark has been and is continuing to call for Central Bank actions aimed at helping to remedy the situation – a quantitative easing (QE) program enacted by the European Central Bank (ECB) is expected in the near-term and should help rekindle risk asset prices.

Finally, in a continuation of a global story that began when oil hit its recent highs in June, the 4$^{th}$ quarter saw crude oil prices extend their drop. This sell-off, at first, was hailed as constructive and beneficial to consumers, but by the end of the 4$^{th}$ quarter, the plunge became so severe that many wondered if it might trigger a crisis among unstable, petroleum-dependent countries such as Russia. While we expect these geopolitical effects to be ongoing, we will likely see negative earnings out of the energy complex being offset by the uptick in consumer spending – and we are watching closely to see whether this will also act as a stimulus abroad, most notably in China.

The backdrop of these broad macro events seen in the 4th quarter, and the ongoing divergence of domestic versus international economies, has created many opportunities for investors with long-term horizons. While 2015 may likely see these trends continue, many investors will be looking to the much anticipated Fed rate hikes to hopefully signal more normal times ahead.

## Market overview/Performance Discussion

### Total Plan

The County of Contra Costa OPEB Plan returned 1.86% in the fourth quarter, which underperformed the County's Plan benchmark return target of 2.92%. Detractors to performance for the quarter included underperformance in the large-cap, small-cap, REIT equity, global equity, and fixed income segments. Underweight allocations to REITs, and an overweight allocation to international/global equity were the most impactful detractors, as REITs were the leading asset class during the quarter, and international equity markets were the largest detractor, turning in a negative rate of return during the fourth quarter. Positive contributions came from the alternative asset class investments and mid-cap equity. Alternatives outperformed both stocks and bonds for the quarter.

### Domestic Equity

All major domestic equity indices were up during the quarter, led by small-cap, with the Russell 1000 +4.88%, Russell Mid-Cap +5.94%, and Russell 2000 +9.73%. The relative strength seen in small-cap stocks was a reversal of the trends seen throughout the year as at the start of the quarter the performance gap between large-cap and small-cap was over 15% – the gap at the end of the year was just over 8%. Perhaps most importantly, 4th quarter returns for small-cap helped this index end the year in positive territory and ensured that domestic equities outpaced all major international indices. Interestingly, the U.S. stock market, as depicted by the broad-based Wilshire 5000 Index has not had a negative quarter for 2.5 year now, which is the 2nd longest winning streak in the history of the index (the longest streak was a 3.5 year stretch during the second half of the 1990's).

During the quarter, all sectors of the Russell 1000 were positive except for Energy (-10.7%), Telecom (-4.2%), and Materials (-1.8%). Consumer Discretionary (+8.7%) and Consumer Staples (+8.2%) were two of the best performing sectors as low oil prices acted as a tailwind. For the full year, the Energy sector was the only area of the Russell 1000 that had a negative return (-7.8%). Style wise, Value very slightly outperformed Growth in large- and mid-cap, while slightly underperforming in small-caps; these trends were also seen for the full year. Domestic equity valuations continue to remain somewhat elevated, with large cap trading at 16.2x P/E versus their 20-yr average of 16.1x and 15.4x a year ago; mid-cap and small cap are similar, with mid-cap trading at 18.6x versus their 20-yr average of 16.5x and small-cap trading at 18.1x versus their 20-yr average of 17.3x.

Active managers continued to struggle during the 4th quarter, which contributed to large-cap mutual fund managers posting their worst relative performance in several decades. This was seen across a wide spectrum of styles and sizes due to several reasons. First, the dispersion of returns has been lacking: when stocks' returns don't vary by much, it is very difficult to add much value by choosing the best ones. Higher dispersion typically goes hand-in-hand with higher volatility which is something that, despite the many macro events that dominated headlines this year, did not really surface for equities. Secondly, there was a fairly unusual negative effect exhibited in the size premium: smaller companies significantly underperformed larger companies by the most in 15 years and small companies tend to be areas of the market where active managers can gain an advantage. Finally, active equity managers entered 2014, and the 4th quarter, bracing for interest rates to increase: instead rates have decreased and have made expensive areas of the market, namely utilities and REITs, even more expensive, and therefore risky. We suspect that this painful run of active manager underperformance may be nearing the end, as volatility has recently begun to increase due to oil price effects on earnings, which should add to stock dispersion, small caps relatively outperforming in the 4th quarter resulting in a shrinking of the relative return gap, and interest rates are unlikely to go much lower from here with the consensus view that the Fed is poised to increase rates.

- **The Plan's large-cap funds returned 4.08% in the quarter, which underperformed the Russell 1000 Index return of 4.88%.**
  - The Sentinel Common Stock Fund returned 4.09% in the quarter, which underperformed the benchmark. The Fund ranked in the 58th percentile of the Morningstar Large Cap Blend Universe.
  - The Columbia Contrarian Core Fund slightly trailed its benchmark with a 4.69% return. The Fund ranked in the 44th percentile of the Morningstar Large Cap Blend Universe.
  - The Harbor Capital Appreciation Fund returned 3.26% in the quarter, which underperformed the Russell 1000 Growth Index's return of 4.78%. The Harbor Fund ranked in the 77th percentile of the Morningstar Large Cap Growth Universe.
  - The T. Rowe Price Growth Stock Fund returned 4.30% in the quarter, which underperformed the Russell 1000 Growth Index. The Fund ranked in the 56th percentile of the Morningstar Large Cap Growth Universe.
  - The T. Rowe Price Equity Income Fund was eliminated from the Plan on December 24. The Fund returned 3.02% in the quarter, which ranked in the 69th percentile of the Morningstar Large Cap Value Universe.
  - The Dodge and Cox Stock Fund was added to the Plan on October 23. The Fund's fourth quarter return was 2.21%, which underperformed the Russell 1000 Value Index return of 4.98%. The Fund ranked in the 78th percentile of the Morningstar Large Cap Value Universe.
  - The Loomis Sayles Value Fund posted a 3.82% return which underperformed the Russell 1000 Value Index, and ranked in the 55th percentile of the Morningstar Large Cap Value Universe.

- **The mid-cap equity segment returned 6.16% in the quarter, which slightly outperformed the Russell Mid-Cap Equity Index return of 5.94%.**
  - The TIAA-CREF Mid-Cap Value Fund returned 5.96% in the quarter, which slightly trailed the Russell Mid-Cap Value Index return of 6.05%. The Fund ranked in the 33rd percentile of the Morningstar Mid-Cap Value Universe of managers.
  - The Ivy Mid Cap Growth Fund returned 6.36% in the fourth quarter, which outperformed the Russell Mid Cap Growth Index 5.84% return. The Fund ranked in the 29th percentile of the Morningstar Mid-cap Growth Universe.

- **The small-cap equity segment returned 6.85% in the quarter, which underperformed the Russell 2000 Index return of 9.73%.**
  - The T. Rowe Price New Horizons Fund returned 6.98%, and underperformed the Russell 2000 Growth Index return of 10.06%. This performance ranked in the 69th percentile of small cap growth managers as measured by Morningstar.
  - The Columbia Small Cap Value Fund II return of 6.76% underperformed the Russell 2000 Value Index's return of 9.40%. This ranked in the 54th percentile of Morningstar's Small Cap Value Universe.

**Real Estate**

Declines in fixed income yields, combined with a fourth quarter GDP growth rate of 5%, proved to be a powerful combination for REIT investors during the quarter. U.S. REITs were the top performing asset class for both the quarter and calendar year. On the heels of a third quarter where REITs posted a negative return, the fourth quarter saw REITs thrive and recover. Occupancy rates improved to new highs, funds from operations grew stronger, and net operating income growth also posted gains. The continued improvement in the employment situation has been a catalyst for REIT industries such as hotel, shopping center, regional mall, and to some extent, the apartment sector. The DJ Wilshire REIT Index returned 15.1% during the fourth quarter, as almost every REIT industry category posted double digit returns. Manufactured homes (+21.1%) was the leading sub-sector, followed by health care (+16.8%), hotels (+16.4%), apartments (+16.1%), shopping centers (+15.3%), and regional malls (+14.5%). For the year, the DJ Wilshire REIT Index returned +31.8%.

- The Nuveen Real Estate Securities Fund returned 13.91% in the fourth quarter, which underperformed the Wilshire REIT Index return of 15.13%. The Fund placed in the 64th percentile of the Morningstar Real Estate Manager's Universe.

**Global/International Equity**

The U.S. dollar continued to negatively impact investor returns in both emerging and developed international equity markets. In local currency the MSCI-EAFE Index gained 1.8%, but declined -3.5% in U.S. dollars. Similarly, the MSCI Emerging Market Index was flat in local terms, but declined -4.5% in dollar terms. The steepest declines in the market were seen in Eastern Europe, specifically in Norway and Russia. With Russia (-32.9%) relying on 50% of their government revenues being sourced from energy, and external financing limited by Western sanctions, the currency was pressured and declined significantly. China held up relatively well (+7.2%) in this negative environment for international equities, but concerns about future growth rates may negatively impact Chinese equities in the future. "Official" growth rates that are announced by the government indicate growth of ~7%. However, when other measures of growth are reviewed, such as electricity consumption, rail freight volumes, and nominal retail sales, a growth rate closer to ~4% is potentially more accurate. China is attempting to transition from an export led economy to one based more on domestic consumption, and this transition may be difficult to execute. The biggest wild card though in international markets continues to be Europe. The European Central Bank President Mario Draghi is following through on his pledge to increase the Bank's balance sheet through quantitative easing measures, in an attempt to increase levels of inflation and help the region emerge from their economic malaise. The QE program that was unveiled in the first quarter of 2015 exceeded many estimates of both the magnitude and length of the program. While there are other structural issues that the Eurozone needs to address to establish lasting growth, this QE program is likely a step in the right direction.

- **The Plan's international/global equity segment returned -3.85% in the quarter. This return underperformed the MSCI-EAFE Index -3.57%.**
  - The Dodge & Cox International Stock Fund's -4.66% return underperformed the MSCI-EAFE Index in the quarter, and ranked in the 86th percentile of the Foreign Large Blend Universe as measured by Morningstar.
  - The Nationwide Bailard International Equity Fund registered a -1.1% return in the fourth quarter, and outperformed the MSCI-EAFE Index. The Fund ranked in the 16th percentile of the Morningstar Foreign Large Blend Universe.
  - The MFS International Fund's return of -2.17% beat the index and ranked in the 69th percentile for foreign large cap growth managers as measured by Morningstar.
  - The Templeton Global Opportunities Fund's return of -3.89% in the quarter underperformed the MSCI-ACWI benchmark return of 0.41%, and ranked in the 94th percentile of the Morningstar World Stock Index Universe.

- The DJ Euro-Stoxx 50 ETF returned -2.06% in the quarter, which outperformed the MSCI-EAFE Index.
- The Schroder Emerging Market Equity Fund returned -4.54% and ranked in the 50th percentile of emerging market equity managers, which was in-line with the MSCI Emerging Market Index return of -4.50%.

**Fixed Income**

The Barclays Capital U.S. Aggregate Bond Index returned 1.8% in the fourth quarter as U.S Treasuries gained 1.9%, while Investment-Grade corporate bonds and agency Mortgage-Backed Securities both returned 1.8%. The combination of the end of the Federal Reserve's quantitative easing along with slower global growth and possible further monetary stimulus in the Eurozone led 10-year U.S. Treasury yields to decline 32 basis points and 30-year bond yields to fall 45 basis points for the fourth quarter. The 30-year bond returned 10.1% during the quarter and an impressive 29.4% for the year, a reversal from the -15% loss sustained in 2013. Investment-grade corporate bonds advanced 1.8%, underperforming equivalent duration U.S. Treasury securities by -114 basis points. High yield corporate bonds lost -1.0%, underperforming equivalent-duration U.S. Treasury securities by -230 basis points. This was the second consecutive quarter of negative excess returns for the High Yield Index after outperforming for each period since the fourth quarter of 2011. Both investment-grade and high yield corporate bond spreads widened during the quarter, primarily due to slower global growth and the implications from significantly lower oil prices. Investment grade corporate bond spreads ended 2014 at +144 basis points, +24 wider for the quarter and +16 bps wider for the year. High yield bond spreads finished at +504 basis points, wider by +64 bps for the quarter and +104 basis points for the year.

Despite continued robust job growth in the U.S., global economic conditions deteriorated during the fourth quarter causing interest rates to decline once again. Forecasts for 2015 global GDP growth have steadily deteriorated from 3.2% at mid-year to 2.7% at year-end, coinciding with the decline in oil prices and the widening of corporate bond spreads. However, U.S. GDP likely expanded by at least 2.5% in 2014 while adding nearly 3 million new jobs, giving the Fed some room to lift interest rates from the near-zero floor where they have been for six years now. If recent trends continue, the Fed will likely raise interest rates in mid- to late 2015, although Fed policy remains dependent on incoming data. Any rate increase, however, should not be seen as a tightening in the traditional sense of being a response to rising inflation. Rather the Fed is anxious to move further away from the unconventional policies they have pursued for the last six years. The Fed has become increasingly concerned that monetary policy may have reached a point of diminishing returns, and may in fact be sowing the seeds of future instability by maintaining the current policy of stable interest rates. We continue to believe that a significant rise in interest rates is still some distance away, and will only occur as a result of a rise in inflation. In fact, in the current environment of 2% wage growth and declining commodity prices, particularly crude oil, inflation expectations have been falling, not rising. High quality corporate bonds continue to be relatively attractive, particularly now that spreads, +144 at year-end, have moved closer to their historical average level of +160 basis points. We are therefore maintaining our overweight to Investment-grade corporates and asset-backed securities while underweighting mortgage-backed securities.

- **The Plan's fixed income segment returned 1.27% in the quarter, which underperformed the Barclays Aggregate return of 1.79%.**
  - The separately managed fixed income portfolio returned 1.33% which underperformed the benchmark. The portfolio would have ranked in the 45th percentile in the Morningstar Intermediate Term Bond Manager Universe.
  - The PIMCO Total Return Bond Fund gained 1.32% in the quarter, which placed it in the 45th percentile of Morningstar's Intermediate-Term Bond Universe. The Fund underperformed the BC Aggregate Index.

- The Pimco High Yield Bond Fund was added to the portfolio on October 27. For the quarter, the Fund returned 0.42%, which underperformed the Merrill Lynch BB/B return of 0.75%.

## Alternative Investments

Alternatives posted a very strong 4th quarter, with the HFRI FOF Market Defensive Index +2.78%. 4Q14 alternative asset returns were relatively muted, with the notable exception of the AQR Managed Futures Fund (+9.79%). The Managed Futures fund was able to take advantage of strong market trends during the quarter in currencies, commodities, and fixed income. All other alternative strategies had a relatively quiet quarter, with Eaton Vance Global Macro +0.41%, JPMorgan Market Neutral +0.83%, and the Arbitrage Fund +1.01%. During the quarter, the Plan's alternative assets outperformed the benchmark by returning +3.53%. Alternative benchmarks and investments can be notoriously noisy on a quarterly basis, so it is perhaps most important to look at the Plan's alternative returns with a longer-term view. The 2014 return (still too short of a time frame, but more instructive than a quarter) for the Plan's alternative investments have exceeded HighMark's cash plus 4% expectations for the asset class and returned +5.01%. Also, it is worth noting that the Plan's alternative assets outperformed the Plan's fixed income sleeve which has been positioned defensively for a rise in interest rates; our expectation is that the Plan's alternative assets should outperform the Plan's fixed income investments when rates do eventually rise.

- **The alternative investment segment returned 3.53% in the fourth quarter, which exceeded the Hedge Fund Research Institute Market Defensive Index return of 2.78%.**
  - The Arbitrage Fund returned 1.01% in the quarter which ranked in the 20th percentile of Morningstar's market neutral universe.
  - The JP Morgan Research Market Neutral Fund returned 0.83%, which placed the Fund in the 27th percentile of the Morningstar market neutral universe.
  - The Eaton Vance Global Macro Absolute Return Fund posted a 0.41% return, which placed in the 18th percentile of the Morningstar non-traditional bond universe.
  - The AQR Managed Futures Fund's return of 9.79% ranked in the 23rd percentile of Morningstar's managed futures fund universe.

## Asset Allocation/Portfolio Transitions

In October a 1.0% allocation to high yield was established. We invested in the Pimco High Yield Bond Fund.

In October we increased our small-cap exposure to equal weight vs. the Plan benchmark by adding 2.5% to the allocation. This was split evenly between value and growth and was sourced by a reduction in mid-cap (-0.5%), large-cap (-0.25%), and global equities (-1.75%).

In October we began to transition from the T. Rowe Price Income Equity Fund to the Dodge and Cox Stock Fund. The T. Rowe Price Fund was replaced due to performance issues and the entire position was transitioned out of by quarter end.

# INVESTMENT STRATEGY

## As of December 31, 2014

## Tactical Asset Allocation

| Asset Class | % Portfolio Weighting: Target | Current Portfolio | Over/Under Weighting | Rationale |
|---|---|---|---|---|
| **Cash** | 1.0% | 1.0% | 0.0% | |
| **Fixed Income** | 38.0% | 36.5% | -1.5% | ▪ Fixed income is currently underweight versus the target allocation given our expectation of an increase in interest rates. We forecast the Fed Funds rate to be at 1.0% by the end of 2015. Within fixed income, the account is positioned defensively with an overweight to shorter-duration bonds. |
| **High Yield** | 0.0% | 1.0% | 1.0% | ▪ With spreads widening in the high yield sector, we re-established a modest position in high yield. |
| **Alternatives** | 10.0% | 11.3% | 1.3% | ▪ The overweight allocation in alternatives seeks to mitigate the impact of a decline in the bond market, due to a potential rise in interest rates. |
| **Real Estate (REITS)** | 4.0% | 2.0% | -2.0% | ▪ We maintained an underweight to REITs throughout 2014 due to concerns about valuation, as well as the anticipated impact of a rising interest rate environment on the asset class. With REITs returning over 30% in 2014, the asset class is trading at elevated valuations. We remain underweight. |
| **Global Equity** | 7.0% | 7.0% | 0.0% | ▪ Global Equities, as represented by the MSCI-ACWI ended the quarter trading at a reasonable valuation level of 14.2X next year's earnings. However, we reduced this allocation to a neutral weighting this quarter to fund an increase in the small cap equity allocation. |
| **International (Developed)** | 9.0% | 9.9% | 0.9% | ▪ We maintain our overweight to international developed equities. Attractive valuations in Europe, coupled with the ECB's quantitative easing program, should aid a recovery in the Eurozone. Japan should still benefit from the reform of the Government Pension Investment Fund and the BOJ's QE program. The valuation levels of the MSCI EAFE, at 14.2X forward PE and the MSCI Europe Index, at a 14X forward PE level, compel us to maintain a slight overweight vs. the Plan benchmark. |
| **International (Emerging)** | 0.0% | 1.5% | 1.5% | ▪ We maintain a modest 1.5% allocation to emerging markets, however worries remain about both Russia and Brazil entering recessions, and additional concerns exist surrounding a slowdown in China. The MSCI-Emerging Market Index trades at an 11X forward PE level. |
| **Total Domestic Equity** | 31.0% | 30.8% | -0.2% | |
| **Large Cap** | 17.0% | 18.8% | 1.8% | ▪ We maintain our overweight to large cap equities as valuations on a relative basis to mid- and small-cap remains attractive. |
| **Mid Cap** | 6.0% | 4.0% | -2.0% | ▪ We increased our underweight to mid-cap equities during the quarter, based on valuation concerns, with the Russell Mid-Cap Index trading at a 18.6X forward PE ratio. |
| **Small Cap** | 8.0% | 8.0% | 0.0% | ▪ We increased the allocation by 2.5% in the quarter, moving to a neutral allocation. Through the third quarter, small - caps were trading in negative territory for the year, making valuations slightly more attractive. An additional consideration is that small-cap stocks are less impacted by foreign exchange issues that larger multi-national corporations are facing. |

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# Asset Allocation
# Period Ending December 31, 2014

| Asset Allocation | 9/30/2014 Market Value | 9/30/2014 % of Total | 12/31/2014 Market Value | 12/31/2014 % of Total | Target Allocation |
|---|---|---|---|---|---|
| **Large Cap Equities** | | | | | |
| Columbia Contrarian Core Z | 7,132,056 | 4.8% | 7,664,736 | 5.0% | - |
| Sentinel Common Stock I | 4,699,734 | 3.2% | 4,584,860 | 3.0% | - |
| T. Rowe Price Equity Income Fund | 3,269,943 | 2.2% | 0 | 0.0% | - |
| Dodge & Cox Stock Fund | 0 | 0.0% | 3,083,467 | 2.0% | |
| Loomis Sayles Value Fund | 4,819,515 | 3.3% | 5,385,449 | 3.5% | - |
| Harbor Capital Appreciation Instl | 4,121,952 | 2.8% | 4,199,167 | 2.7% | - |
| T. Rowe Price Growth Stock Fund | 4,103,278 | 2.8% | 4,238,760 | 2.7% | - |
| **Total Large Cap Equities** | **28,146,478** | **19.1%** | **29,156,438** | **18.8%** | **17.0%** |
| | | *Range* | | *Range* | *13-32%* |
| **Mid Cap Equities** | | | | | |
| TIAA-CREF Mid-Cap Value Instl | 3,289,792 | 2.2% | 3,111,006 | 2.0% | - |
| iShares Russell MidCap Growth Fund | 0 | 0.0% | 0 | 0.0% | - |
| Ivy Mid Cap Growth Fund I | 3,215,888 | 2.2% | 3,086,702 | 2.0% | - |
| **Total Mid Cap Equities** | **6,505,681** | **4.4%** | **6,197,707** | **4.0%** | **6.0%** |
| | | *Range* | | *Range* | *2-10%* |
| **Small Cap Equities** | | | | | |
| Columbia Small Cap Value Fund II | 3,925,980 | 2.7% | 6,233,931 | 4.0% | - |
| T. Rowe Price New Horizons Fund | 3,982,218 | 2.7% | 6,172,512 | 4.0% | - |
| **Total Small Cap Equities** | **$ 7,908,198** | **5.4%** | **$ 12,406,443** | **8.0%** | **8.0%** |
| | | *Range* | | *Range* | *4-12%* |
| **International** | | | | | |
| Nationwide Bailard Intl Equities Fund | 4,150,857 | 2.8% | 4,592,308 | 3.0% | - |
| Dodge & Cox International Stock Fund | 4,612,286 | 3.1% | 5,080,857 | 3.3% | - |
| MFS International Growth Fund | 3,066,841 | 2.1% | 3,444,044 | 2.2% | - |
| Schroder Emerging Market Equity | 2,163,672 | 1.5% | 2,317,803 | 1.5% | - |
| SPDR EURO STOXX 50 ETF | 2,917,950 | 2.0% | 2,277,948 | 1.5% | - |
| **Total International** | **$ 16,911,606** | **11.5%** | **$ 17,712,960** | **11.4%** | **9.0%** |
| | | *Range* | | *Range* | *4-16%* |
| **Global** | | | | | |
| Templeton Global Opportunities A LW | 13,026,434 | 8.8% | 10,780,958 | 7.0% | - |
| **Total Real Estate** | **$ 13,026,434** | **8.8%** | **$ 10,780,958** | **7.0%** | **7.0%** |
| | | *Range* | | *Range* | *4-12%* |
| **Real Estate** | | | | | |
| Nuveen Real Estate Secs I Fund | 2,879,439 | 2.0% | 3,062,198 | 2.0% | - |
| **Total Real Estate** | **$ 2,879,439** | **2.0%** | **$ 3,062,198** | **2.0%** | **4.0%** |
| | | *Range* | | *Range* | *0-8%* |

| Asset Allocation | 9/30/2014 Market Value | 9/30/2014 % of Total | 12/31/2014 Market Value | 12/31/2014 % of Total | Target Allocation |
|---|---|---|---|---|---|
| **Fixed Income** | | | | | |
| Core Fixed Income Holdings | $ 46,384,556 | 31.5% | 48,951,347 | 31.6% | - |
| PIMCO Total Return Instl Fund | 7,262,196 | 4.9% | 5,939,841 | 3.8% | - |
| PIMCO High Yield Instl | 0 | 0.0% | 1,552,903 | 1.0% | - |
| **Total Fixed Income** | **$ 53,646,752** | **36.4%** | **$ 56,444,090** | **36.5%** | **38.0%** |
| | | *Range* | | *Range* | *30-50%* |
| **Alternatives** | | | | | |
| AQR Managed Futures I | $5,427,660 | 3.7% | 5,952,207 | 3.8% | - |
| Arbitrage I | $3,722,225 | 2.5% | 3,883,214 | 2.5% | - |
| Eaton Vance Glbl Macro Abs Ret I | $5,234,880 | 3.6% | 5,405,203 | 3.5% | - |
| JP Morgan Research Market Neutral I | $2,233,350 | 1.5% | 2,322,926 | 1.5% | - |
| **Total Alternatives** | **$ 16,618,115** | **11.3%** | **$ 17,563,550** | **11.3%** | **10.0%** |
| | | *Range* | | *Range* | *5-20%* |
| **Cash** | | | | | |
| Money Market | $ 1,562,338 | 1.1% | 1,514,319 | 1.0% | - |
| **Total Cash** | **$ 1,562,338** | **1.1%** | **$ 1,514,319** | **1.0%** | **1.0%** |
| | | *Range* | | *Range* | *0-5%* |
| **TOTAL** | **$ 147,205,042** | **100.0%** | **$ 154,838,664** | **100.0%** | **100.0%** |

# Investment Summary

# Period Ending December 31, 2014

| Investment Summary | | Fourth Quarter |
|---|---|---|
| **Beginning Value** | **$** | **147,494,207.30** |
| Net Contributions/Withdrawals | | 4,832,721.47 |
| Fees Deducted | | -41,946.76 |
| Income Received | | 6,287,064.19 |
| Market Appreciation | | -3,443,399.95 |
| Net Change in Accrued Income | | 89,733.32 |
| **Ending Market Value** | **$** | **155,218,379.57***|

*Ending Market Value differs from total market value on the previous page due to differences in reporting methodology. The above ending market value is reported as of trade date and includes accruals. The Asset Allocation total market value is reported as of settlement date.

## Selected Period Performance

# PARS/COUNTY OF CONTRA COSTA PRHCP

**Account 6746038001**

**Period Ending: 12/31/2014**

| Sector | 3 Months | Year to Date (1 Year) | 2 Years | 3 Years | Inception to Date (47 Months) |
|---|---|---|---|---|---|
| Cash Equivalents | .00 | .02 | .02 | .02 | .02 |
| *iMoneyNet, Inc. Taxable* | *.00* | *.01* | *.02* | *.02* | *.02* |
| Fixed Income ex Funds | 1.33 | 4.74 | 1.63 | 2.88 | 4.32 |
| Total Fixed Income | 1.27 | 4.70 | 1.70 | 3.44 | 4.43 |
| *BC US Aggregate Bd Index* | *1.79* | *5.97* | *1.89* | *2.66* | *3.99* |
| Total Equities | 1.98 | 4.77 | 15.69 | 16.19 | 10.23 |
| Large Cap Funds | 4.08 | 9.97 | 21.76 | 20.47 | 13.33 |
| *Russell 1000 Index* | *4.88* | *13.24* | *22.77* | *20.62* | *15.18* |
| Mid Cap Funds | 6.16 | 9.72 | 20.16 | 17.97 | 12.30 |
| *Russell Midcap Index* | *5.94* | *13.22* | *23.52* | *21.40* | *14.94* |
| Small Cap Funds | 6.85 | 5.60 | 23.29 | 20.61 | 14.29 |
| *Russell 2000 Index* | *9.73* | *4.89* | *20.67* | *19.21* | *13.24* |
| REIT Funds | 14.58 | 30.64 | 15.30 | 16.09 | 12.94 |
| *Wilshire REIT Index* | *15.13* | *31.78* | *15.86* | *16.43* | *13.91* |
| International Equities | -3.85 | -3.68 | 7.28 | 11.77 | 4.53 |
| *MSCI EAFE Index* | *-3.57* | *-4.90* | *8.05* | *11.06* | *4.22* |
| *MSCI EM Free Index* | *-4.50* | *-2.19* | *-2.39* | *4.04* | *-1.45* |
| *MSCI AC World Index* | *.41* | *4.15* | *13.11* | *14.10* | *8.07* |
| Alternatives | 3.53 | 5.01 | | | |
| *HFRI FOF Market Def* | *2.78* | *6.31* | *3.38* | *1.67* | *-.33* |
| Total Managed Portfolio | 1.86 | 4.62 | 8.79 | 9.86 | 6.98 |
| *County of Contra Costa* | *2.92* | *6.92* | *9.69* | *10.19* | *7.90* |

Inception Date: 02/01/2011

* Benchmark from February 1, 2011 to June 30, 2013: 18% Russell 1000 Index, 6% Russell Midcap Index, 8% Russell 2000 Index, 8% MSCI AC World ex US Index, 10% MSCI EAFE Index, 45% Barclays Aggregate Index, 4% DJ Wilshire REIT Index, 1% Citigroup 3 Month T-Bill Index. From July 1, 2013: 17% Russell 1000 Index, 6% Russell Midcap Index, 8% Russell 2000 Index, 7% MSCI AC World ex US Index, 9% MSCI EAFE Index, 38% Barclays Aggregate Index, 4% DJ Wilshire REIT Index, 10% HFRI Fund of Funds Market Defensive Index, 1% Citigroup 3 Month T-Bill Index

# COUNTY OF CONTRA COSTA

## For Period Ending December 31, 2014

| Fund Name | Inception | 3-Month Return | Rank | YTD Return | Rank | 1-Year Return | Rank | 3-Year Return | Rank | 5-Year Return | Rank |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **LARGE CAP EQUITY FUNDS** | | | | | | | | | | | |
| Sentinel Common Stock I | (7/13) | 4.09 | 58 | 10.62 | 63 | 10.62 | 63 | 18.54 | 63 | 14.27 | 45 |
| Columbia Contrarian Core Z | (7/13) | 4.69 | 44 | 12.92 | 31 | 12.92 | 31 | 22.07 | 10 | 15.93 | 10 |
| T. Rowe Price Equity Income | | 4.30 | 56 | 8.83 | 65 | 8.83 | 65 | 21.68 | 15 | 15.84 | 17 |
| Harbor Capital Appreciation Instl | | 3.26 | 77 | 9.93 | 53 | 9.93 | 53 | 20.52 | 31 | 14.48 | 42 |
| Loomis Sayles Value Fund | (7/11) | 3.82 | 55 | 10.76 | 48 | 10.76 | 48 | 21.58 | 8 | 14.35 | 28 |
| Dodge & Cox Stock | (10/14) | 2.21 | 78 | 10.40 | 54 | 10.40 | 54 | 23.71 | 1 | 15.56 | 9 |
| **Idx: Russell 1000** | | **4.88** | **--** | **13.24** | **--** | **13.24** | **--** | **20.62** | **--** | **15.64** | **--** |
| **MID CAP EQUITY FUNDS** | | | | | | | | | | | |
| TIAA-CREF Mid-Cap Value Instl | | 5.96 | 33 | 12.85 | 19 | 12.85 | 19 | 20.37 | 46 | 15.64 | 39 |
| **Idx: Russell Mid Cap Value** | | **6.05** | **--** | **14.75** | **--** | **14.75** | **--** | **21.98** | **--** | **17.43** | **--** |
| Ivy Mid Cap Growth I | (5/14) | 6.36 | 29 | 8.20 | 38 | 8.20 | 38 | 16.89 | 67 | 15.73 | 33 |
| **Idx: Russell Mid Cap Growth** | | **5.84** | **--** | **11.90** | **--** | **11.90** | **--** | **20.71** | **--** | **16.94** | **--** |
| **SMALL CAP EQUITY FUNDS** | | | | | | | | | | | |
| Columbia Small Cap Value II Z | | 6.76 | 54 | 4.61 | 42 | 4.61 | 42 | 18.87 | 35 | 15.55 | 20 |
| **Idx: Russell 2000 Value** | | **9.40** | **--** | **4.22** | **--** | **4.22** | **--** | **18.29** | **--** | **14.26** | **--** |
| T. Rowe Price New Horizons | | 6.98 | 69 | 6.10 | 19 | 6.10 | 19 | 22.50 | 6 | 21.43 | 1 |
| **Idx: Russell 2000 Growth** | | **10.06** | **--** | **5.60** | **--** | **5.60** | **--** | **20.14** | **--** | **16.80** | **--** |
| **INTERNATIONAL EQUITY FUNDS** | | | | | | | | | | | |
| Dodge & Cox International Stock | | -4.66 | 86 | 0.08 | 9 | 0.08 | 9 | 15.23 | 4 | 7.89 | 7 |
| Nationwide Bailard Intl Eqs InSvc | | -1.10 | 16 | -1.94 | 15 | -1.94 | 15 | 12.98 | 12 | 6.37 | 18 |
| MFS International Growth I | | -2.17 | 69 | -5.10 | 58 | -5.10 | 58 | 8.95 | 77 | 5.90 | 53 |
| Templeton Global Opportunities A LW | | -3.89 | 94 | -4.06 | 93 | -4.06 | 93 | 13.84 | 57 | 6.80 | 88 |
| **Idx: MSCI EAFE** | | **-3.57** | **--** | **-4.90** | **--** | **-4.90** | **--** | **11.06** | **--** | **5.33** | **--** |
| **Idx: MSCI ACWI** | | **0.41** | **--** | **4.16** | **--** | **4.16** | **--** | **14.10** | **--** | **9.17** | **--** |
| Schroder Emerging Market Equity | (11/12) | -4.54 | 50 | -4.61 | 70 | -4.61 | 70 | 4.30 | 50 | 1.41 | 56 |
| **Idx: MSCI Emerging Markets** | | **-4.50** | **--** | **-2.19** | **--** | **-2.19** | **--** | **4.04** | **--** | **1.78** | **--** |
| SPDR EURO STOXX 50 ETF | (6/14) | -2.06 | 88 | 0.77 | 73 | 0.77 | 73 | 6.57 | 56 | 7.76 | 100 |
| **REIT EQUITY FUNDS** | | | | | | | | | | | |
| Nuveen Real Estate Secs Y | | 13.91 | 64 | 31.28 | 17 | 31.28 | 17 | 16.32 | 14 | 17.28 | 9 |
| **Idx: Wilshire REIT** | | **15.13** | **--** | **31.78** | **--** | **31.78** | **--** | **16.43** | **--** | **17.26** | **--** |

# COUNTY OF CONTRA COSTA

| Fund Name | Inception | 3-Month Return | Rank | YTD Return | Rank | 1-Year Return | Rank | 3-Year Return | Rank | 5-Year Return | Rank |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **BOND FUNDS** | | | | | | | | | | | |
| Fixed Income Portfolio | | 1.33 | 45 | 4.74 | 69 | 4.74 | 69 | 2.88 | 67 | -- | -- |
| Pimco Total Return Inst'l | | 1.32 | 45 | 4.69 | 71 | 4.69 | 71 | 4.26 | 22 | 5.14 | 37 |
| **Idx: BarCap US Aggregate Bond** | | **1.79** | **--** | **5.97** | **--** | **5.97** | **--** | **2.66** | **--** | **4.45** | **--** |
| PIMCO High Yield Instl | (11/14) | 0.42 | 10 | 3.31 | 13 | 3.31 | 13 | 7.77 | 41 | 8.26 | 35 |
| **Idx: Merrill Lynch US High Yield BB-B** | | **0.75** | **--** | **5.34** | **--** | **5.34** | **--** | **8.37** | **--** | **9.05** | **--** |
| **ALTERNATIVE FUNDS** | | | | | | | | | | | |
| Arbitrage I | (7/13) | 1.01 | 20 | 1.64 | 39 | 1.64 | 39 | 1.08 | 61 | 1.94 | 35 |
| AQR Managed Futures | (7/13) | 9.79 | 23 | 9.69 | 40 | 9.69 | 40 | 7.31 | 2 | -- | -- |
| Eaton Vance Glbl Macro Abs Ret | (7/13) | 0.41 | 18 | 3.03 | 18 | 3.03 | 18 | 2.28 | 72 | 2.23 | 69 |
| JPMorgan Research Market Neutral Instl | (7/13) | 0.83 | 27 | 3.38 | 25 | 3.38 | 25 | 3.38 | 22 | 0.36 | 62 |

Data Source: Morningstar, SEI Investments

*Returns less than one year are not annualized. Past performance is not indicative of future returns. The information presented has been obtained from sources believed accurate and reliable. Securities are not FDIC insured, have no bank guarantee and may lose value.*