COUNTY of SAN BERNARDINO

EXECUTIVE SUMMARY
Defined Contribution Plans
4th Quarter 2008

County of San Bernardino	4th Qtr%	1 Yr.%	3 Yr.%	5Yr.%
SBC 457 Plans Performance	-22.96	-39.35	-7.54	1.09
SBC 401(k) Plan	-23.10	-39.29	-7.63	1.11
Major Indexes				
Standard & Poor's 500	-21.94	-37.00	-8.36	-2.19
Russell 1000	-22.48	-37.60	-8.66	-2.04
Russell Midcap	-27.27	-41.46	-10.68	-0.71
Russell 2000	-26.12	-33.79	-8.29	-0.93
Barclay's U.S. Aggregate Bond	4.58	5.24	5.51	4.65
MSCI World, ex U.S.	-21.15	-43.56	-7.25	1.91

PORTFOLIO ANALYSIS

Assets: The total assets in all of the County of San Bernardino plans have decreased to $409,084,718, including $847,224 in the self directed brokerage account. The previous quarter the balance was $453,530,956. A total of $7.8 million transferred into the fixed interest account during the fourth quarter.

Based on total assets, excluding the part time employee assets, the total return of the County of San Bernardino portfolio is -6.44%. In a bear market the assets in the fixed interest account have a noticeable impact on the overall performance results.

457 Plan Cash Position: The stable value rate for the fourth quarter was 3.50%. Transfer of assets into the stable value account in the fourth quarter was a little less than the previous quarter with $6.2 million moving from mutual funds. The percentage of assets in the stable value account has increased from 30.8% in the fourth quarter 2007 to 48.33% as of December 31, 2008. Throughout 2008 there has been a significant flight to safety. The 48.33% also reflects a substantial reduction in the value of the mutual funds.

401(k) Plan Cash Position: The percentage of assets in the stable value account has increase from 26.99% in the third quarter of 2008 to 33.92% the fourth quarter. The percentage of assets in the stable value account was 19.27% as of December 31, 2007. $1.6 million transferred to the stable value account during the fourth quarter.

Retirement Medical Trust Cash Position: The fixed interest account rate for the fourth quarter was 4.15%. There was a small increase in the percentage of assets in the fixed interest account with 88.95% now in the ING General Account.

457 Plans Mutual Funds Position:

The 457 portfolio underperformed the benchmark for the fourth quarter and for the one year performance due to the poor performance of several equity funds. Several of the funds that underperformed the benchmark were domestic funds that invest a considerable percentage of assets in foreign stocks. While only a little more than 10% of the County of San Bernardino mutual fund assets are invested in international funds 22.5% of the assets are invested in foreign stocks. The funds that contain a key percentage of the mutual fund assets and most influenced the underperformed of the 457 portfolio are:

Fund Name
Janus Contrarian,
RiverSource Div. Eq. Income
Thornburg Core Growth,
RiverSource Mid Cap Value
Dodge & Cox International Stk.
Oppenheimer Int'l Small Co,
Loomis Sayles Inv. Grade Bond &
Pax World Balanced.

The Sharpe Ratio is a tool that helps determine if the risk the fund or portfolio is taking to achieve the performance is worthwhile. The Sharpe Ratio for the 457 portfolio continues to decline and is now -0.57 which is better than the benchmark of -0.70.

The Standard Deviation is a measurement of the volatility of the portfolio's short term return from the average long term return. The three year Standard Deviation for the portfolio is 17.39. It is higher than the benchmark of 15.69 and the difference is due to the impact of Oppenheimer International Small Company's high standard deviation of 34.76.

The Alpha, a measurement of the value added by the investment manager, is 2.05. The Beta is 1.09.

401(k) Mutual Funds Position:

The 401(k) outperformed the 457 portfolio by only 14 basis points (0.14%) during the fourth quarter and outperformed the 457 portfolio by a miniscule 6 basis points (0.06%) in the one year performance comparison.

The Sharpe Ratio for the 401(k) portfolio continues to decline and is also now -0.58 which is better than the benchmark of -0.70.

The three year Standard Deviation for the portfolio is 17.37. It is higher than the benchmark of 15.41 due also to Oppenheimer International Small Company. There is a slightly greater percentage of 401(k) assets in that fund than in the 457 portfolio. The Alpha is 1.88 and the Beta is 1.11. The higher percentage of assets in the Oppenheimer International Small Company fund also influences a lower Alpha in the 401(k) portfolio due to the substantial under performance of that fund and correspondingly increases the Beta due to the increased risk.

RETIREMENT MEDICAL TRUST Mutual Funds Position:

Only 11.05% of the $19,162,290 assets are in mutual funds, including the risk based asset allocation funds. The substantial under performance to the benchmark is due the fourth quarter performances of the 2020 Target fund and the Loomis Sayles Bond fund.

MUTUAL FUNDS

The following is noteworthy information on the mutual funds.

1. American Funds Growth Fund of America (AGTHX) – Large Cap Growth

This fund continues to hold an 11.40% stake in cash and 16% in foreign stocks. The cash holdings are almost three times that of its peer group and gave this fund an advantage over its peer group. With over 290 stocks, turnover is low at 32% and in this bear market contributes to the portfolio mix of 43% large cap growth stocks, 31% large cap blend, 13% large cap value, and 12% mid caps stocks.

2. Columbia Marsico 21st Century Z (NMYAX) – Large Cap Growth

While the three and five year numbers are still intact, the 2008 performance under performed. Big bets on financial companies once again retarded performance and the concentration in just 38 stocks hurt performance, despite a near 19% cash stake.

3. Janus Contrarian (JSVAX) – Large Cap Blend

This fund is a concentrated fund with only 58 holdings and is considered multi cap as it invests in many asset categories. 30% of the fund is International, 15% of the fund is Emerging Markets, 19% is Mid Cap Value and 28% is Large Cap Growth. There are three big bets on Utilities, Media and Financial Stocks; only Utilities performed better than the overall market.

4. Vanguard Institutional Index (VINIX) – Large Cap Blend

This fund finished up in the second quartile of its large blend peer group in 2008. Net return exceeded peer group averages even with a low expense of 0.05%.

5. Mainstay ICAP Select Equity (ICSLX) – Large Cap Value

Overall the fund held up in 2008. Its return was close to its benchmark and though it is a concentrated value fund it doesn't appear to be making any significant sector bets.

Mainstay ICAP Select Equity is extremely concentrated with only 30 holdings, as such, this fund may tend to be more volatile than funds with greater stock holdings.

6. RiverSource Diversified Equity (RSEDX) – Large Cap Value

The fund is fairly well diversified, has low turnover and a reasonable expense ratio for a managed fund. This fund has a long history of beating its peers having performed better than the peer group average in the past 3 and 5 year periods, however in this latest market turndown, it has not performed well against its peers. An overweight in the financials and industrial materials sectors and an underweight in the healthcare sector affected performance. The fund tends to hold approximately 80% of its holdings in dividend paying common and preferred stock.

7. Thornburg Core Growth (THGRX) – Mid Cap Growth

Until 2008 this fund was a consistent top quartile performer. Morningstar categorizes this fund as a mid-cap growth, however only 33% of the assets are in mid-cap companies. The fund has underperformed its peer group benchmark for the past 1 and 3 year periods. Given its concentrated approach, 30 stocks, this fund is going to have very good performance that may be offset by performance in some years that will be negative. For the risk, this fund doesn’t currently have nearly enough excess return.

8. Fidelity Advisor Leveraged Company Stock (FLVIX) – Mid Cap Growth

2008 was a terrible year for stocks and even worse for managers who make bets and or buy stocks that employ leverage, that is buying stocks in companies that issue debt to finance their business activities. This fund suffered even more due to its heavy concentration in energy and industrial materials. While the fund has a historical good track record it has been hit hard by the credit crisis. Prior to 2008, this fund was in the top quartile of its asset category for seven consecutive years and ranks in the second percentile for performance over five years. In 2008, it fell to the bottom quartile suffering losses significantly greater than their peer group.

9. Vanguard Mid Cap Index (VMISX) – Mid Cap 450 USD

Based upon the nature of mid cap indices, the Vanguard Mid Cap Index is within acceptable expense and tracking error margins for the 3 and 5 year periods.

10. RiverSource Mid Cap Value (RSCMX) – Russell Mid Cap Value

This fund is a mixed bag. It is consistent in terms of style allocation, but the returns are about the same as the index. If we take 2007 out of the mix the returns are about the same as the index or lower. This fund likes energy and 2007 was a great year for energy, but 2008 turned out to be a bad year for energy. It is still beating its peers and index for the 5 year period but not for the 1 and 3 year periods. Underweighting the healthcare and overweighting the industrial goods sectors hurt recent performance in the fourth quarter.

11. Baron Growth (BGRFX) – Russell 2000 Growth

While this fund is categorized as Small Growth in reality it vacillates between small and mid cap companies, but it always buys growth stocks. Because Baron holds onto stocks for almost five years the fund's average capitalization will tend toward the mid cap range. Ron Baron is one of the few proven stock pickers and he did what we expect managers to do in 2008 even though very few accomplished it; he lost less than the benchmark. Whether we compare the fund to a small or mid growth benchmark it performed better. This fund is not against making bets and underperformance at times should be expected, if that is acceptable there are few funds with such apparently good stock pickers.

12. Royce Value Plus (RVPHX) – Russell 2000 Growth

This fund has been managed by James Skinner, since 2007. The fund underperformed in 2007 and in 2008 was pretty close to the benchmark. Royce has a good name in small caps and this fund provides exposure to micro cap stocks as well.
2008 was not spectacular, but the fund did not fall apart, the new manager weathered the storm. Skinner has 13 years working in the small and micro cap arena.

13. Keeley Small Cap Value (KSCVX) – Russell 2000

This small cap blend fund underperformed because of its bet on energy. It had its best quarter ever in 2008 and its worst quarter ever in 2008, both due to energy bets. This manager has shown an ability to come back from setbacks and while it underperformed its benchmark for the year it still has a good record long term. This is a fund that does make bets which will show up in dramatic performance swings as 2008 proved.

14. Vanguard Small Cap Index (NAESX)

Based upon the nature of small cap indices, the Vanguard Small Cap Index is within acceptable expense and tracking error margins for the 3 and 5 year periods.

15. Morgan Stanley US Small Cap Value (MCVAX) – Russell 2000 Value

This is a small blend fund that significantly outperformed its peers and benchmarks in 2008 and over almost every period measured. This is mainly due to the bet against energy, basically underweighting it. These types of bets can hurt performance as well, but this fund has proven consistent.

16. American Funds Capital World Growth and Income (RWIEX) – MSCI World

The fund has beaten its peer average and benchmark handily over the past 1, 3, 5 and 10 years. In a year where foreign stocks performed worse than domestic stocks, this fund only lost a little bit more than the S&P 500, a testament to the success of the strategy. The fund likes to buy blue chips stocks that are beaten down and holds them; it also focuses on companies with strong dividends. This was a tough year and a 38% loss is not easy to take, however this fund performed like an actively managed fund is supposed to perform, losing less in this bear market than its competitors, this was rare in 2008.

17. Dodge and Cox International Stock (DODFX) - MSCI Wld Ex-US/Emerging Markets

Despite two investments that got hit hard, AIG and Royal Bank of Scotland, this fund only underperformed its index by a few points. This is due mainly to the 20% stake in Emerging Markets. Given these facts it's a surprise the fund didn't underperform more. Dodge and Cox is one of those few companies that have a good history of methodical stock picking, it failed a few times last year, but we have confidence that this will meet expectations in the long run.

18. ING Global Real Estate (IGLIX) – MSCI World Real Estate Index

This fund is sub-advised by ING Clarion, a real estate investment group owned by ING. The fund delivers the return of Global REITs (or similar REIT structures in other countries). It is invested about 36% domestic and 59% international mimicking almost exactly the MSCI World Real Estate Index. The returns however have been better than the index consistently. The fund is beating its index handily for the 1, 3 and 5 year periods. The US exposure helped as international real estate has fallen much more than domestic.

19. Janus Aspen International Growth (JAIGX) – MSCI World ex-US

This is an aggressive offering. With 30% of its assets in Emerging Markets this fund underperformed the traditional international fund, it also underperformed a blended index that included Emerging Markets by about 6%. This is the first year since 2002 with a negative performance for the year and the first year with a return under 18% since 2003.

20. Oppenheimer International Small Company (OSMYX) – MSCI EAFE Small

This has become an international fund with a concentration in commodities after historically being a more diversified fund. This is a volatile fund as evidenced by the high standard deviation, 34.76. The concentration in commodities had paid rich dividends during the period of high demand. In 2008, when consumer spending was so low and demand for commodities declined precipitously this fund took a large hit. Participants should be notified that this fund has changed its direction from a diversified international small company fund to a concentrated portfolio with an emphasis on commodities. Initial results in 2009 are looking stronger, however, this fund should be on the **Watch List** and further discussion about this fund should take place.

21. Loomis Sayles Investment Grade Bond (LSIIX) – Barclays Global US Govt/Credit

This bond fund has consistently performed in the top quartile until 2008 and ranks in the top 1% of its peer group over a five and ten year period. While the fund has been hurt by exposure to foreign currency and shareholder redemptions which forced the fund to sell at low prices during 2008, the final months placed this fund back in the top 10% of its category.

22. Oppenheimer International Bond (OIBYX) – Barclays Global Aggregate Bond

The fund has a good track record and held up despite a troubling year for global bonds. The fund is not fully hedged and at times has held 50% in Emerging Markets debt, and therefore will be more volatile than most bond funds.

23. Pioneer Global High Yield (GHYYX) – CSFB Credit Suisse High Yield

As mentioned in our previous quarterly report, this fund invests in low grade bonds both in America and abroad, when a financial panic hits and a flight to safety occurs, this type of fund will have negative results. To counteract the investor's flight to safety the manager has reduced the risk level of this fund by reducing the fund's exposure to emerging markets and cyclical issuers' like retailer's corporate debt. That being said, the 1, 3 and 5 year performance is below the peer group as well as the benchmark index. We recommend this fund be placed on the **Watch List**.

24. American Funds Income Fund of America (RIDEX) – Dow Jones Moderate Allocation

Areas contributing to underperformance are an allocation to Foreign (which the benchmark does not have) and a rather high allocation to high-yield bonds. High Yield bonds have been hit hard during this financial crisis, but now sport above average spreads (compared to Treasury's). The hope is that the credit analysts at Capital Research have done a good job in picking the high yield bonds in this portfolio. This fund is a solid, long term choice for a person looking for a well diversified portfolio that is balanced between stocks and bonds.

The fund has underperformed its benchmark for only the 1 year period but has beaten its peer category in all but the prior 12 months, almost surely due to its high-yield and foreign allocation.

25. PAX World Balanced Fund (PAXIX) - Dow Jones Moderate Allocation

The 4th quarter of 2008 was brutal for this fund. The fund has thus far still managed to beat out its peer group over the 3, 5, 10 and 15 year periods though trailed by about a half percent for the last 12 months. It trails its index for the 1, 3, 5 & 10 year periods – though mainly due to the 4th quarter and the fact that the fund had a higher allocation to stocks (and to foreign and energy stocks) than its more conservative peers.

We maintain that for those investors who want a socially responsible aggressive global balanced fund, PAX World Balanced should work just fine. Its underperformance to the index may be a function of its social mission and the fact that makes it more difficult to beat an index.

26. (26 – 30) Vanguard Target Retirement 2010, 2020, 2030, 2040 & 2050

Vanguard's Target Retirement funds are low in cost and indexed, this has led to outperformance in 2008 as actively managed funds faltered. Over time these funds should provide the best return for the risk taken.

The main issue with Target Date funds is that they assume everyone retiring in a specific year has the same risk profile. This assumption has led to many questioning their value as most target dates are stock heavy.

We still see value in Target Date funds but think that education is the key. People need to understand the risk characteristics of the year they choose and that the more stocks, the more fluctuation.

WATCH LIST

The Watch List contains funds that did not meet the criteria outlined in the Investment Policy. Specifically, if a fund does not meet or exceed the designated benchmark for both the three and five year periods it must be placed on the Watch List.
The two funds that are on the Watch List:

20. Oppenheimer International Small Company – We are concerned about the redemptions and the emphasis on commodity stocks. **We recommend further discussion on this fund.** The Defined Contribution Committee has asked the consultant to suggest a fund that is more diversified as a possible addition to the portfolio.

23. Pioneer Global High Yield – The financial crisis has hit this fund hard and, it has failed the 1, 3 and 5 year peer group benchmark. **This is a fund that will require more observation and discussion.**

Stabilizer – The gap between market and book value has widened and performance has not improved.

ING – Update

The ING Group announced that they will cut 7,000 jobs in 2009, about 5.4% of the work force. ING expects to reduce its operating expenses by $1.3 billion this year with 35% of the reduction from job elimination. In the U.S. the job reductions will come from the economy of scales developing from the acquisition of CitiStreet. The staff reductions we are aware of do not impact or affect ING's partnership with the County of San Bernardino. While there are some personnel changes at ING Investment Management, (Stabilizer), those changes, which have been previously announced to the County, are not viewed as cost reductions but rather philosophical and directional.