SST BENEFITS CONSULTING

COUNTY OF SAN BERNARDINO
EXECUTIVE SUMMARY
DEFINED CONTRIBUTION PLANS
4th QUARTER 2010

	4th Qtr	1 Yr.	3 Yr.	5 Yr.
457 Plans Performance	12.21	10.70	-4.66	3.55
Customized Benchmark	11.95	10.79	-4.68	2.16
Difference	**0.26**	**-0.09**	**0.02**	**1.39**
401(k) Plan	9.51	15.94	-0.32	5.09
Customized Benchmark	9.98	16.51	-0.92	3.69
Difference	**-0.47**	**-0.57**	**0.60**	**1.40**
Retirement Medical Trust	9.24	15.90	0.22	4.85
Customized Benchmark	9.27	17.29	1.32	4.79
Difference	**-0.03**	**-1.39**	**-1.10**	**0.06**

PORTFOLIO ANALYSIS:

ASSETS:	
457 Assets	$ 388,853,044
401(k) Assets	$ 81,703,892
401(a) Assets	$ 1,109,293
RMT Assets	$ 36,668,471
P/T Assets	$ 37,187,790
TOTAL Assets	**$ 545,522,490**

Due to the appreciation of mutual fund assets, the total assets in all of the County of San Bernardino plans have increased from $514 million at the end of the third quarter, 2010, to $545 million at the end of the fourth quarter, 2010. The assets as of December 31, 2009 were $507 million.

The 457 assets in the Ameritrade Self Directed Brokerage Account are $1,950,526 and in the 401(k) the assets are $962,268.

457 PLAN CASH POSITION:

The stable value crediting rate for the fourth quarter was 2.00%. The first quarter 2011 crediting rate is 2.00%. The percentage of assets in the fixed interest bearing account decreased from 37.59% in the third quarter to 35.13% in the fourth quarter. The reduction was due to the greater appreciation of the mutual funds.

401(k) PLAN CASH POSITION:

The percentage of assets in the fixed interest bearing account changed very little. The assets in the Stabilizer decreased from 28.77% in the third quarter, to 26.64% in the fourth quarter. The reason for the decreased percentage of assets in the Stabilizer was due to the appreciation of mutual fund values.

RETIREMENT MEDICAL TRUST CASH POSITION:

There was a small decrease in the percentage of assets in the fixed interest account, with 81.13% now in the ING General account. The fixed interest account will credit an interest rate of 3.30% for the first quarter, 2011. This is a ten basis point change from the fourth quarter 2010 rate of 3.40%.

457 PLANS MUTUAL FUNDS POSITION:

The underperformance is due to the high mutual fund allocation to Growth Fund of America, Perkins Small Cap and Capital World.

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 was a positive 0.06, a good improvement over the previous quarter's -0.14 and better than the benchmark of 0.04 (over three years).

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 22.25 which is higher than the benchmark of 21.92.

The Alpha, a measurement of the value added by the investment manager is 0.59. Beta is a measure of the degree of change in value that can be expected, given a change in value in the comparable index. The Beta is at 1.01 (over three years).

401(k) MUTUAL FUNDS POSITION:

The underperformance is due to the high mutual fund allocation to Growth Fund of America, Perkins Small Cap and Capital World.

The Sharpe Ratio for the 401(k) portfolio improved and is now 0.07, which is better than the benchmark of 0.04 (over three years). The three-year Standard Deviation for the portfolio is 22.41 which is higher than the benchmark of 21.80. The Alpha is 0.73 and the Beta is 1.03.

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<u>RETIREMENT MEDICAL TRUST (RMT) MUTUAL FUNDS POSITION</u>:

The RMT underperformed the customized benchmark due to a high mutual fund allocation to Growth Fund of America and Thornburg Growth, which had underperformed to the benchmark.

The Sharpe Ratio for the RMT portfolio is 0.09 and is worse than the benchmark of 0.14. The three-year Standard Deviation for the portfolio is 21.22 which is higher than the benchmark of 19.97. The Alpha is -0.99 and the Beta is 1.06. The negative Alpha is caused by performance against the Beta. The performance was not as good as expected based on the portfolio risk.

<u>PERFORMANCE OF INDEX FUNDS VS. ACTIVELY MANAGED FUNDS</u>:

	4th Q 10	**1 year**	**3 year**	**5 year**
Large Cap				
Vanguard Institutional Index	**10.75**	**15.05**	**-2.80**	**2.32**
American Growth Fund	10.26	12.28	-2.74	2.52
Columbia Marisco	15.19	17.13	-6.00	3.49
Janus Contrarian	4.72	11.16	-7.54	3.60
Parnassus Inv Eq	8.01	8.89	2.60	7.17
Main Stay ICAP Select Equity	10.60	17.71	-1.67	4.09
Columbia Div Eq Inc	12.35	16.70	-3.85	2.87
Mid Cap				
Vanguard MidCap Index Signal	**13.58**	**25.62**	**0.90**	**4.39**
Thornburg Core Gr	12.87	10.32	-7.40	1.06
Fidelity Adv Lev Co	18.24	24.71	-2.55	5.32
Columbia MidCap Value	14.08	23.22	-1.10	4.64
Small Cap				
Vanguard Small Cap Index	**15.55**	**27.72**	**3.58**	**5.39**
Baron Growth	15.46	24.01	0.42	4.51
Royce Value Plus	14.87	20.25	0.29	4.48
Perkins Small Cap Value	10.19	17.87	7.99	7.82
Invesco U.S Small Cap Value	17.65	30.00	7.23	9.14

The index funds have an advantage of low cost. Index funds cannot avoid any sector or stock that meets the capitalization boundaries. Also, unlike actively managed funds, index funds are devoid of cash holdings. This is a disadvantage in some markets but can be an advantage in other markets, like the market we are currently experiencing.

<u>MUTUAL FUNDS</u>

The following pages contain noteworthy information on particular mutual funds. The numbers on the left indicate their order on the Rate of Return sheet located after the next tab.

1. **AMERICAN FUNDS GROWTH FUND OF AMERICA**

The Growth Fund of America has long been an anchor in many portfolios. It has provided competitive rates of return for many years and garnered well deserved attention. But the fund has seen tremendous fund inflows because of this popularity, and consequently, has grown to an enormous $161 billion. There has been a concern among analysts for a few years that the size would be prohibitive to efficient portfolio management, but the vast resources of the very seasoned nine person management team has been able to keep the critics quiet with excellent relative performance.

There has been some underperformance, however, the primary reason for which is that this growth fund is more sensitive to stock prices than most and is simply not willing to "pay up" for growth. This fund also looks for stocks with low to medium Betas, but the market has recently rewarded stocks with higher Betas. This strategy typically leads to lower fluctuation, but can also lead to a higher than average cash position during extended bull markets. Currently, the fund is holding nearly 8% of the assets in cash, a significant departure from its peers, who average less than 3% in cash. A substantially higher than average cash position in an equity market that demonstrated significant appreciation in 2010 also affected performance against the peer group.

Additionally, the international investments of 14%, which is double the peer average, negatively affected performance over the one year period. In all three measurable periods, 2010 was the first year this fund underperformed its benchmark, although by only 0.52 and 0.37 for the three and five year periods, respectively.

Management has decided to approve an increase in its total allowable international exposure to 25%, which may indicate that they are looking for new ways to differentiate. The depth and breadth of experience of this investment team deserves the highest accolades in the industry, but performance will be even more scrutinized going forward.

Recommendation: Watch List due to Performance

2. **COLUMBIA MARISCO 21ST CENTURY Z**

This fund is more of an "All-Cap" fund than a Large Cap fund. The manager pulled out of the 3rd quartile doldrums in 2010, finishing back in the first quartile (after two years in the 3rd). A heavy weighting in financials will hurt this fund if bank stocks experience weakness and its ability to buy small and mid-cap stocks will likely hurt the fund if large cap stocks outperform.

3. **JANUS CONTRARIAN**

The manager, like most of his peers, looks for companies that are well managed and have the capability to increase returns on invested capital. What sets him apart is he will look for those opportunities regardless asset class. 39% of the assets are invested in mid cap stocks and 12.5% are invested in small cap stocks. There are risks with the go anywhere style of this manager; the standard deviation is 30% higher than the peer group.

With 38% of the assets invested in foreign stocks, this fund borders on being classified as a global or world fund. The underperformance is due to this substantial over weighting to foreign stocks. The strategy followed by this fund has paid off over time. The fund has gained an annual average of 5.7% dating back to March, 2000, while the peer group has lost 0.4%.

4. **PARNASSUS INV EQUITY INCOME**

Manager Todd Ahlsten has done a great job with this fund despite severe restraints as to where he can invest. 2010 was a tough year for the fund as it trailed its peers and index by a rather wide margin, though the philosophy behind the manager's stock picks has not changed and Ahlsten believes time will vindicate his portfolio. Ahlsten has, according to Morningstar, virtually all of his liquid net worth in this fund - a good sign. We believe the recent softness in returns will be short lived and those with a social bent will be well served over the long run by Parnassus.

5. **VANGUARD INSTITUTIONAL INDEX**

This index fund performs consistently well as a passively managed index fund at a very low cost, 0.05%.

6. **COLUMBIA (FORMERLY RIVERSOURCE) DIVERSIFIED EQUITY INC**

RiverSource, subsidiary of Ameriprise, acquired the Columbia family of funds from Bank of America last year and has changed the names of all of their fund families (RiverSource, Seligman and Threadneedle) to the Columbia moniker. After a very tough 2008, this fund has done a good job of climbing out of the basement, rising from 4th quartile to the first quartile in 2009 and 2010.

The two key managers have been contributing to the overall success of this fund since 2004. The only negative to performance in 2010 were financial institutions that did not fare well. Bank of America, J. P. Morgan Chase and Goldman Sachs are top six portfolio holdings.

7. **MAINSTAY ICAP SELECT EQUITY I**

Funds that focused on mega-cap, high-quality stocks suffered over the past few years, but Mainstay Select Equity is an exception. The managers of this fund have continued a long string of outperformance against the category and index. The fund has finished in the top quartile in 7 of the past 8 years and has only placed below the second quartile twice since 2000. Consistency in stock picking philosophy has led to consistent returns.

8. **THORNBURG CORE GROWTH R5**

This fund has fallen on tough times. After putting in a very poor performance in 2008 the fund rebounded nicely in 2009, but has trailed ever since. This is a bit surprising considering smaller stocks beat larger stocks and this fund has such a profile (weighted-average market cap of only $11 billion).

The build up in the Health Care sector has been a key cause of this fund's, (and many others), underperformance. The risk in this fund has not been adequately compensated for over most time periods. The fund is trailing its peers over 1, 3, 5 and 10 years and the fourth quarter performance worsened against the peer group. This is the third consecutive quarter on the Watch List.

Thornburg has 1.34% of the 457 / 401(a) assets and 621 participants invest in this fund. 53 participants invest 0.56% of the 401(k) assets in this fund. 76 participants invest 0.70% of the RMT assets in this fund.

Recommendation: Deletion

9. FIDELITY ADVISOR LEVERAGED COMPANY STOCK

This fund was developed to capitalize on Fidelity's high yield research via equities. The fund ties itself to companies with less than stellar balance sheets and performance is strong when riskier, financially weaker stocks perform well, i.e. 2009, (a return to top quartile performance).

Manager Soviero does not need a sustained risk led rally in order to succeed. He has had top quartile performance seven consecutive years prior to the disastrous 2008. Aside from 2008, when the fund experienced a drop of 53.67%, he has done so very successfully.

The fund is a diversified portfolio of 202 stocks but covers a very wide swath of asset classes which include large, mid, small cap of both growth and value. This type of fund has inherent risks associated with it and the standard deviation is 41% higher than the benchmark average.

10. VANGUARD MID CAP INDEX SIGNAL

Based upon the nature of mid cap indices, the Vanguard Mid Cap Index actually beats the index and is in the top quartile which is very unusual for an index fund.

11. COLUMBIA MID CAP VALUE OPPORTUNITY R5

After a very difficult year in relative performance in 2008, the Columbia Mid Cap Value fund seems to be reverting back to its normal track of good performance. The fund has a very seasoned management team in place that is known for keeping an eye on risk. The fund ranked in the top third of it its peer group and came in the top 16% just in the 4th quarter. The Sharpe Ratio is higher than the benchmark and that is driven by the above average standard deviation.

12. BARON GROWTH

Ron Baron is finding most of his great stocks in the mid-cap range, though most remain at the smaller end of the mid-cap range. Mid Cap is typically in the $3 - 10 billion market cap range and this fund's average market cap is around $3 billion. Given the great history of Baron, it makes sense to allow the portfolio the flexibility to chase larger fare when it feels there is value or when he simply wants to hold onto a stock that has grown out of the typical small cap range.

Recent performance was influenced by the significant under weighting to the Industrial sector. Two years of 3rd quartile performance may not be appealing to most, but the fund returns of 34% and 24% in 2009 and 2010, respectively, are not bad. This portfolio tends toward less speculative stocks and will normally trail when more speculative stocks are in favor, as they have been the past few years. Overall, Baron is doing what many investors want, buying quality small companies that have the potential to double in five years.

13. ROYCE VALUE PLUS INVT

The Royce Value Plus fund had a respectable absolute return of 20.25% but missed its benchmark index by 6.69% lagging almost 90% of its peer group. Despite the 2010 poor performance it only trails the three and five year benchmarks by 0.48 and 0.03 respectively. The fund had a larger than category average to the banks which were disappointing this year and had a few missteps with stock selection, particularly technology stocks, which led to the year's underperformance. This highlights one of the funds risks of having a tendency to make larger bets in small firms and larger than average industry weightings.

Another reason for the dismal performance in 2010 is the heavy weighting in international stocks, nearly three times the average of the peer group.

The portfolio has considerable style drift containing names in the small value to mid cap space. The managers maintain a three to five year time horizon with most of their stock selections and they prize small companies in healthy financial condition. The fund has an experienced investment team with Whitney George as lead or co-manager of the fund. The managers have sizable investments of their own in this fund.

Recommendation: Watch List due to Performance

14. PERKINS SMALL CAP VALUE T

This fund replaced Keely Small Cap Value in November, 2010.

Bob Perkins and his team are not hesitant about holding cash when valuations do not merit investment, as demonstrated by the current 16% cash position of this fund. Along with a few sectors that did not pan out in 2010, the cash position dragged on returns in a market driven by the most high-beta speculative stocks. The 2010 performance follows three years where Perkins navigated fund performance around mine fields to achieve top quartile performance. In fact, despite the performance in 2010 this fund is in the top five percent of its category over the recent three year period, (Keely ranks in the 93rd percentile for the same period).

This fund is designed to buy stocks at reasonable valuations and to protect participants capital in down markets (this doesn't mean no losses, it means smaller losses) and the current screaming bull market in highly valued stocks makes this style out of favor. We believe this manager has the discipline to execute and that participants will be well served by including this fund in their portfolios.
The Sharpe ratio is more than three times higher than their peer group which further supports the point that the managers are adverse to risk and that is also supported by a standard deviation that is 14% lower than the average. Morningstar rates this five star fund as having "low risk".

The style has drifted toward blend. This is a common trait of small cap value funds as the equity markets rally. A significantly lower than average investment in the defensive Utility sector contributes to this drift.

15. VANGUARD SMALL CAP INDEX

Based upon the nature of small cap indices, the Vanguard Small Cap Index is within acceptable expense and tracking error margins for the one (1), three (3) and five (5) year periods.

16. INVESCO US SMALL CAP VALUE

Performance has been consistently strong with less risk than the typical small cap fund. The style has drifted toward blend. The BETA, 0.92, is lower than the average for this category, 1.18; so historically this fund has taken less risk than its peers. A lower than average weighting to the Financial sector aided performance against the peer group.

The lead manager has left Invesco and the new lead manager has had previous management experience with a mid cap fund. The new lead manager, R. Coleman, runs a deeper value portfolio than his predecessor and holds onto stocks a little longer.

Additionally, Invesco purchased Van Kampen and they have announced their intentions of merging this fund with Van Kampen Small Cap Value. The management team will be the one that is now managing Invesco Small Cap Value.

WATCH LIST DUE TO MANAGER CHANGE AND MERGER OF FUNDS

17. AMERICAN FUNDS CAPITAL WORLD GROWTH AND INCOME

The Capital World Growth and Income fund has been a solid performing fund for many years and has done especially well in more difficult markets. Since its inception in 1993, it has outperformed the category index 14 out of the last 16 years.

The very seasoned management team of eight focuses on dividend paying companies at reasonable prices. This approach to management has historically served the fund well, but in 2010, primarily in the second quarter when Europe's growth prospects were looking dim, the fund's performance suffered due to a larger weighting towards Europe than its peers. Performance in the 3rd and 4th quarters was more consistent with its peer group.

Capital World has 67% of their assets invested in international stocks while the average global fund has only 55% of their assets invested in international stocks. Due both to the stronger dollar and the economic weakness of many European countries, the domestic stocks substantially outperformed the international stocks. Global/world funds with a greater concentration of domestic stocks outperformed Capital World.

18. DFA INTERNATIONAL SMALL CO I

This fund is doing exactly what it was designed to do, tracking the return of the small international stocks. Broad diversification is a primary component of this passively managed strategy. The fund trends more toward value than growth as the low P/E and higher than average dividend yield indicates.

19. Dodge & Cox International

Dodge & Cox invests more heavily in emerging markets than their peers and also invests in developed countries that do most of their business in emerging countries. The one bet that hurt performance was in the pharmaceutical industry where values were low and stocks were purchased at what looked like bargain prices, but that industry performed poorly in 2010. This fund ranks in the top 6%, 9% and 5% for the one, three and five year measurable periods, respectively, and is a bargain at 0.65%.

20. JANUS ASPEN OVERSEAS

This manager is not afraid to take risks. Brent Lynn loads up on sectors and allocates an above average portion of the portfolio to emerging markets. This strategy hurt in 2008 but has led to enormous outperformance in 2009 and 2010 versus the peer group. This a good fund to hold as a portion of a diversified portfolio. If it is held as a core holding, we recommend the investors have a long time horizon and will hold this fund over full market cycles. The standard deviation is 22% higher than the benchmark average.

21. LOOMIS SAYLES INVESTMENT GRADE BOND Y

The Loomis Sayles Bond fund is a diversified portfolio of many different types of bonds. The management team is not afraid to venture into lower quality corporate bonds, emerging market debt and even some of the troubled governments debt of Europe. A rare trait of the fund is that the manager is the largest shareholder of the fund. A three year Sharpe ratio of .48 indicates that the risk taken for the achieved performance is worthwhile.

Performance for 2010 was 11.52% which under performed its benchmark, multisector bond peer group, by 1.31%. The under performance against the benchmark was due to an under weighting in below investment grade bonds compared to the multisector bond peer group. The riskier below average grade bonds performed better than the investment grade bonds.

Every year, starting in 2002, this fund's performance was in the top quartile with the exception of 2008. In 2008 the lower quality portion of this fund performed much worst than the general bond market and this fund landed in the fourth quartile for that year. The experienced managers take on risks many other bond funds will not and over time have been rewarded, though not without a few bumps along the road.

22. OPPENHEIMER INTERNATIONAL BOND Y

The Oppenheimer International Bond fund has long been a favorite among investors and analysts. Aside from the volatility of 2008, the fund has performed very well relative to its category benchmark index but does so by assuming a meaningful amount of risk. The fund has at many times been courting 50% or more of emerging market debt which has kept the fund in the above average risk category by Morningstar.

The fund did lose one of its managers of the non-US developed markets portion of the portfolio and the emerging markets segment is managed by Sara Zervos who started at the fund in April, 2009. Art Steinmetz, who oversees this fund, has been with the fund since its inception in 1995. 2010's performance landed it in the first quartile beating its benchmark by 1.62%. An Alpha of 0.91 indicates that management adds value from their expertise.

Recommendation: Watch List due to Manager Change

23. PIONEER GLOBAL HIGH YIELD Y

The Pioneer Global High Yield fund outperformed its category index by 4.30% in 2010 as it has every year of the last 10, with the exception of 2008. It has accomplished this by taking on higher than the peer's average of emerging market debt. The funds two star overall Morningstar rating appears to be the lingering effects of 2008's -35.65% return, landing them in the bottom decile for the category. The funds Sharpe ratio of .45 and Alpha score of 2.91 indicates management's ability to add value from their expertise.

24. AMERICAN FUNDS INCOME FUND OF AMERICA

With an allocation of 61% to stocks and 35% to bonds, the fund will fluctuate with the market, but we believe that for those looking for stock exposure, dividends and who are willing to be more concentrated in one asset category (large value) this fund will be a good choice. While the equity portion of the fund is more conservative than its peer group, the bond selections are more volatile with an average credit rating of BB, one category below investment grade. The managers are experienced and have a good track record.

25.-29. VANGUARD TARGET RETIREMENT FUNDS

The Vanguard series of target funds offer investors a conservative bond portfolio with over 75% of the bond holdings rated AAA and no bonds rated Below Investment Grade. Stocks are primarily large cap although the portfolios do contain on average 20-25% small and mid cap stocks. All of the target funds are rated four star and are provided to investors at a below average cost.

30. ING GLOBAL REAL ESTATE I

This fund has done a reasonably good job long term despite short term weakness. The management team has been together about five years. The managers adhere very closely to regional index allocations.

It was recently announced that ING has agreed to sell Clarion Partners to the firm's management and a private equity group, Lightyear Capital. It currently appears that the fund manager will remain with Clarion Partners and continue to manage this fund.

Recommendation: Watch List due to Ownership Change

31.– 33. ASSET ALLOCATION FUNDS

The funds performed well during the recent volatile three year period. The conservative asset allocation trailed the one year benchmark due to holding 50% of its assets in fixed interest versus the benchmark that contains 12.4% of the assets in cash / fixed interest.

WATCH LIST

The Watch List contains funds that did not meet the criteria outlined in the San Bernardino County's 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." There are other reasons to be placed on the Watch List including ownership or manager change.

The funds that are on the Watch List:

1. **American Funds Growth Fund of America – Due To Performance**

8. **THORNBURG CORE GROWTH R5 – DUE TO PERFORMANCE**

13. **ROYCE VALUE PLUS INVT – DUE TO PERFORMANCE**

16. **INVESCO U. S. SMALL CAP VALUE – DUE TO MANAGER CHANGE AND MERGER**

22. **OPPENHEIMER INTERNATIONAL BOND – DUE TO MANAGER CHANGE**

30. **ING GLOBAL REAL ESTATE – DUE TO OWNERSHIP CHANGE**