

# GMO

North America | Europe | Asia-Pacific

## **Fresno County Employees' Retirement Association**

April 2, 2008

Bill Nemerever

*Presentation*

# Presenter

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**William Nemerever** Mr. Nemerever is a member of the executive committee and co-manages GMO's global fixed income area with Tom Cooper. Prior to joining GMO in 1993, he worked at Boston International Advisors where he founded the quantitative global fixed income effort. Previously, he was in charge of several Fidelity Investments fixed income groups, head of the fixed income department at State Street Bank & Trust Co., a portfolio manager at Wells Fargo, and a portfolio manager, equity analyst and actuary at John Hancock. Mr. Nemerever earned his B.S. in Mathematics at the University of Washington and his M.S. in Actuarial Science from Northeastern University. He is a CFA charterholder.

# Agenda

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- Firm Update
- Strategy Review
- 2007 Performance
  - *Interest Rates*
  - *Currencies*
  - *Collateral*
- Outlook

# GMO Overview

## Distinctive Approach

- We apply a blend of proven traditional judgments and innovative quantitative methods to find undervalued securities.
- Our success is based on a disciplined, value-oriented, risk-controlled investment philosophy and a commitment to investment research.



## Experience

GMO has successfully managed money since our founding in 1977.

## People

- 94 investment professionals
- More than 400 employees worldwide

## Assets of \$139 Billion\*

- \$121 billion in equities (\$91 billion non-U.S.)
- \$18 billion in fixed income
- \$39 billion in asset allocation\*\*
- \$9 billion in absolute return strategies\*\*

## Defining Characteristics

**Motivation** *We are a private partnership*

**Focus** *Investment management is our only business*

**Discipline** *We carefully manage risk, seeking long-term capital appreciation*

**Stability** *We have exceptionally low turnover of investment professionals*

\* As of 2/29/2008 (prelim.)

\*\* Asset allocation and absolute return assets are accounted for within underlying strategies and should not be double-counted.

Represents assets from both GIPS and non-GIPS compliant firms. There are two GIPS compliant firms. The first is Grantham, Mayo, Van Otterloo & Co. LLC ("GMO"), an independent investment adviser registered under Investment Advisers Act of 1940. GMO's accounts are managed by investment management offices in Boston, MA and Berkeley, CA. GMO has total assets of \$126,634,997,472. The second firm is defined as GMO U.K. Limited and its subsidiary firm, namely GMO Woolley Limited (collectively "GMO UK"). GMO UK was established to manage mandates primarily for UK and other European clients. GMO UK is authorized and regulated by the Financial Services Authority in the United Kingdom. GMO UK firm assets are \$5,774,731,144.

# Fresno County Employees' Retirement Association

*Performance net of fees and expenses (\$U.S.)*

## Periods Ending December 31, 2007

	Month	Quarter	YTD	Annualized			Since Inception *	Market Value (000)
				1 Year	3 Year	5 Year		
<b>Global Bond (3/12/99)</b>	-1.40 %	-0.40 %	2.76 %	2.76 %	1.72 %	7.62 %	6.09 %	76,203
<i>JPMorgan Global Gov't. Bond</i>	-0.53	3.96	10.81	10.81	3.14	6.71	5.88	
Value Added	-0.87	-4.36	-8.05	-8.05	-1.42	0.91	0.21	

\* Periods of less than a year are not annualized

## Periods Ending February 29, 2008

	Month	YTD	Annualized			Since Inception *	Market Value (000)
			1 Year	3 Year	5 Year		
<b>Global Bond (3/12/99)</b>	1.16	4.69	6.50	3.48	7.89	6.52	79,780
<i>JPMorgan Global Gov't. Bond</i>	2.40	6.21	16.50	5.67	7.41	6.48	
Value Added	-1.24	-1.52	-10.00	-2.19	0.48	0.04	

\* Periods of less than a year are not annualized

# Investment Process Overview

*First we replicate the benchmark, then we combine a variety of strategies to add value*

## Benchmark Replication

Invest in bonds, currencies, short-term high-quality debt & derivatives to generate benchmark-like returns

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### Currencies

Relative Value

Momentum-Plus

Security Selection

#### *Opportunity Set:*

Australian dollars  
Canadian dollar  
Euro  
Yen  
New Zealand dollar  
Norwegian krone  
Swedish krona  
Swiss franc  
U.K. pound  
U.S. dollar

+

### Bonds

Market Selection

Rate Anticipation

Yield Curve

Volatility

#### *Opportunity Set:*

Australian interest rates  
Canadian interest rates  
Euro-area interest rates  
Yen interest rates  
  
Swedish interest rates  
Swiss interest rates  
U.K. interest rates  
U.S. dollar interest rates

+

### Emerging Country Debt

Issue Selection

Asset-Backed Securities

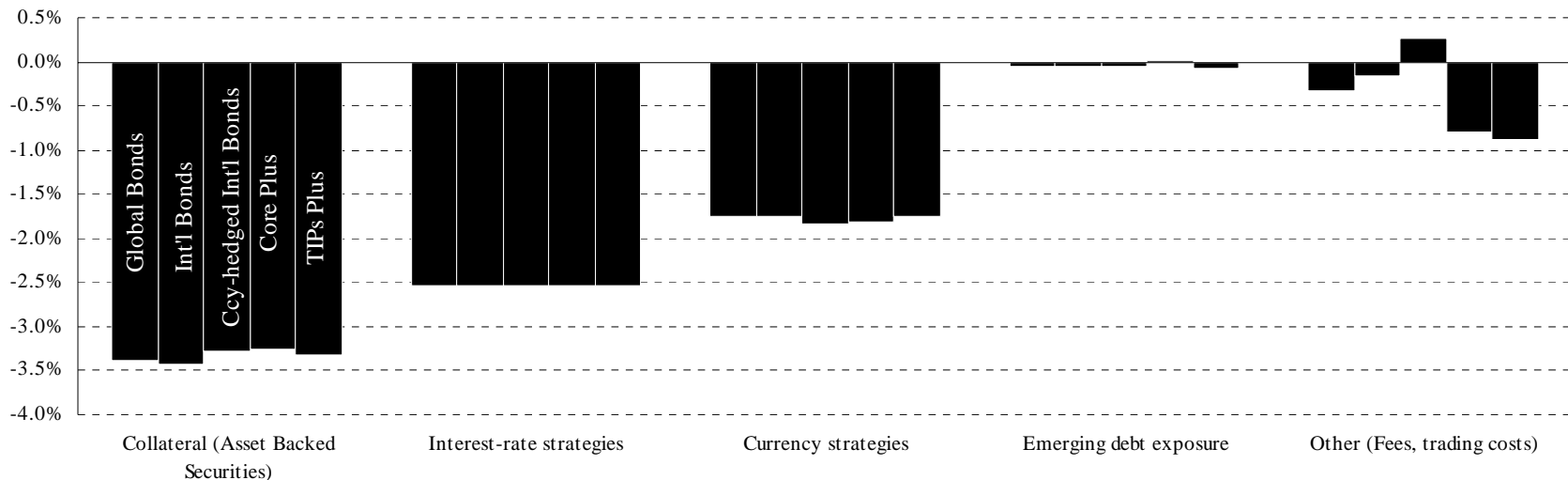
Issue Selection

#### *Opportunity Sets:*

Emerging Country Debt  
JPMorgan Emerging Market Bond Index Global and related sovereign, hard currency emerging country debt exposures  
  
Asset-Backed Securities  
AAA, floating-rate ABS with various collateral types

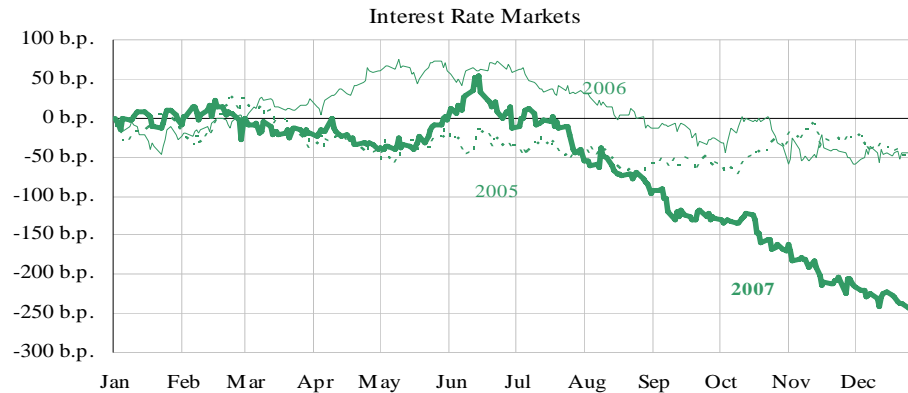
# Performance Summary: 2007

- Performance in 2007 was poor: about 800 bps of underperformance
- About 40% resulted from the unexpected and significant mark-to-market losses on collateral investments used by the portfolios
- About 30% resulted from the underperformance of our interest-rate strategies, with particular underperformance of value factors
- About 20% resulted from the underperformance of our currency strategies, including shocks to our risk model



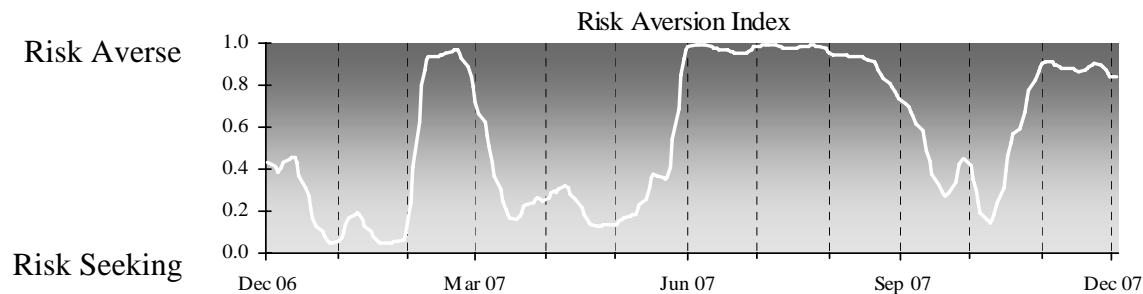
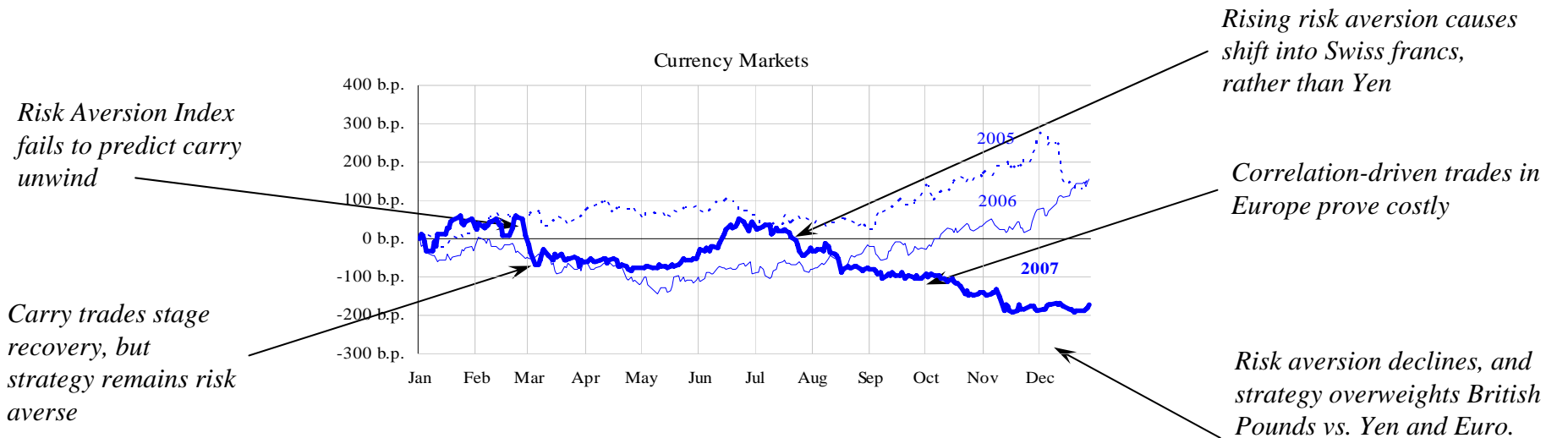
# Interest-Rate Strategy Performance: -254 basis points

- Most of the underperformance was due to market selection; other interest-rate strategies had much smaller contributions
- Most of the underperformance came in the second half of the year



# Currency Selection: -180 basis points

- We began the year in a risk-seeking mode. On February 26<sup>th</sup> Chinese stock market decline and Greenspan comments threw markets in to risk averse mode. Our risk Aversion Index was too late in predicting the carry unwind.
- During the summer and fall, our currency models were unable to navigate the rapidly changing risk environment. In particular, the preference for Swiss francs over Japanese yen during a risk aversion episode was costly.



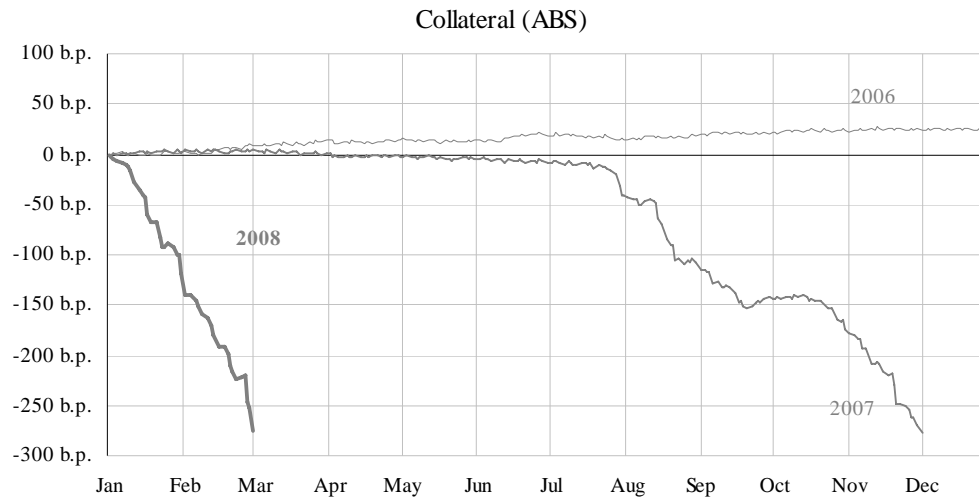
# Collateral Portfolio Objectives

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- AAA+ Credit Quality
- Price Stability
- Benchmark: Three-month LIBOR

# Collateral Performance

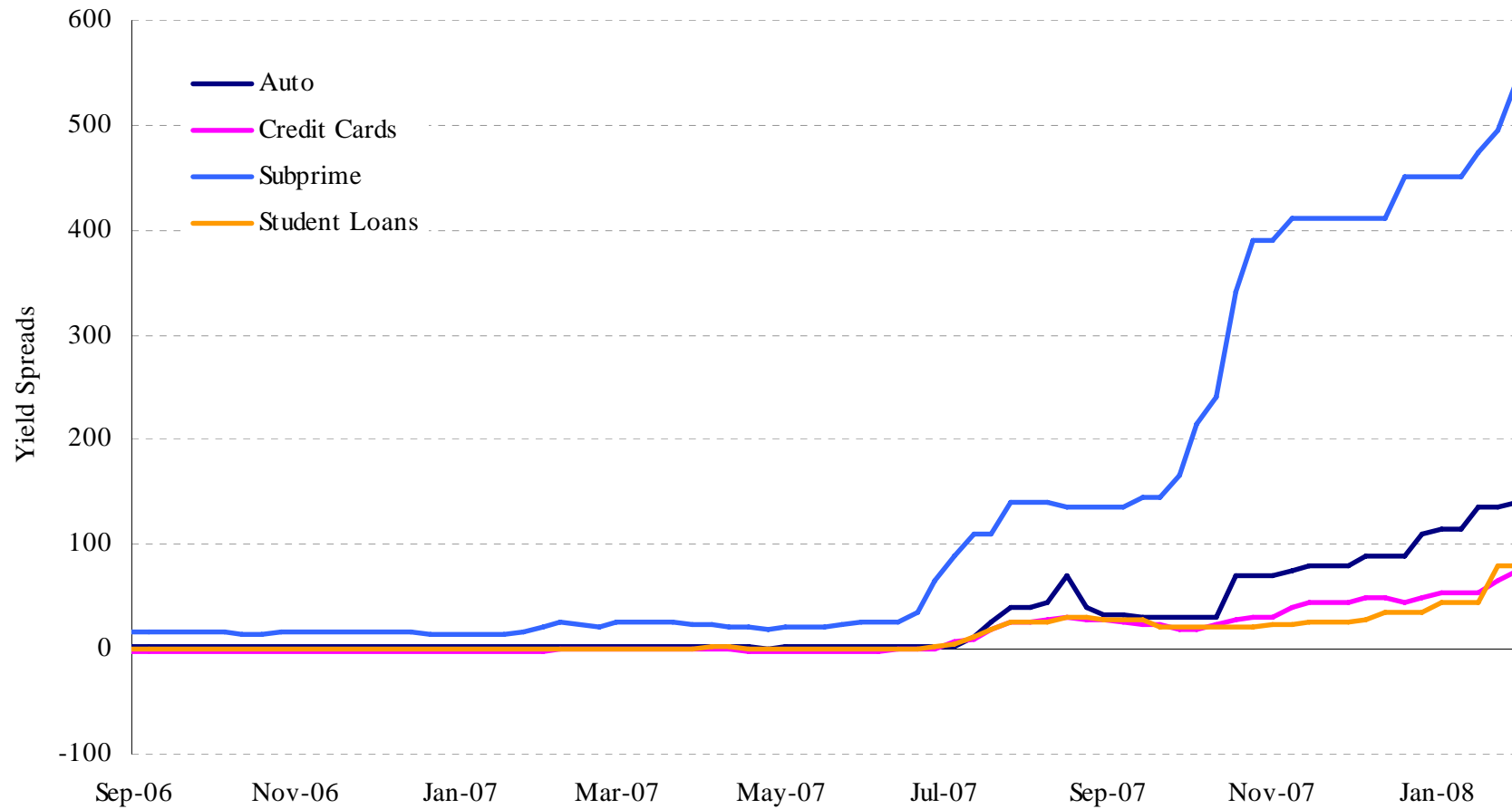
- Our funds invest roughly 90% of their assets in top-quality asset-backed securities
- Although we own the highest-quality assets, rising liquidity premia has meant lower bid-side market prices



# Asset-Backed Spreads

*Widening spreads, greater volatility*

Three Year AAA  
Senior Tranche



# Outlook

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- Our strategy struggles when markets shift rapidly to new regimes or when cross-market correlations approach one – we reviewed our modeling techniques and have reallocated our risk budget temporarily given the unprecedented market volatility.
- Interest rate and currency strategy alphas have rebounded in 2008.
- Mark-to-market losses on collateral investments should be recouped, and the asset class offers opportunities though we anticipate continued near-term volatility.
- We remain confident in the Strategy's ability to meet its long-term objectives for FCERA.

# Fixed Income Team Biographies

# Capsule Biographies: Fixed Income

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## ***William Nemerever***

Mr. Nemerever is a member of the executive committee and co-manages GMO's global fixed income area with Tom Cooper. Prior to joining GMO in 1993, he worked at Boston International Advisors where he founded the quantitative global fixed income effort. Previously, he was in charge of several Fidelity Investments fixed income groups, head of the fixed income department at State Street Bank & Trust Co., a portfolio manager at Wells Fargo, and a portfolio manager, equity analyst and actuary at John Hancock. Mr. Nemerever earned his B.S. in Mathematics at the University of Washington and his M.S. in Actuarial Science from Northeastern University. He is a CFA charterholder.

## ***Thomas Cooper***

Mr. Cooper co-manages GMO's global fixed income area with Bill Nemerever. Before joining GMO in 1993, he was a managing director at Boston International Advisors. Prior to joining Boston International, he worked at Goldman Sachs Asset Management, Western Asset Management and State Street Bank & Trust Co. Mr. Cooper received his M.B.A. from the University of California (Berkeley) and earned a B.A. from Oberlin College. He is a CFA charterholder.

## ***Steve Edelstein***

Mr. Edelstein works with GMO's global fixed income group as a portfolio manager. Prior to joining GMO in 1995, he was a vice president and fixed income options and futures strategist with Morgan Stanley. Mr. Edelstein has also worked with First Boston in the fixed income proprietary trading, government trading and risk management groups, and as a financial model builder and programmer with Lehman Brothers' Kuhn Loeb. He holds his M.S. in Economic and Social Statistics from Cornell University and earned a B.S. from the State University of New York at Oneonta.

## ***George Estes***

Mr. Estes is responsible for credit analysis for GMO's emerging country debt portfolios. Prior to joining GMO in 1996, he was director for Latin America and Canada for the Burger King Corporation. Mr. Estes holds a B.A. in German from the University of Virginia and an M.B.A. in Finance from the University of California at Berkeley.

## ***Mark Mueller***

Dr. Mueller is the director of research for the Algorithmic Trading group, which he co-started in 2003. Since joining GMO in 1997, he has also served as the director of research for the Fixed Income group. Prior to joining GMO, he worked at Goldman Sachs in the fixed income proprietary trading group, and earlier at Morgan Stanley as a quantitative analyst in equity derivatives. Dr. Mueller holds a B.S. in Physics from the Massachusetts Institute of Technology and a Ph.D. in Physics from Stanford University.

## ***Tina Vandersteel***

Ms. Vandersteel is a member of the global fixed income group. She serves as a portfolio manager for emerging markets currencies and also as a product manager for all strategies within the global fixed income group. Prior to joining GMO in 2004, she worked at J.P. Morgan Chase & Co. in fixed income research, developing quantitative arbitrage strategies for emerging markets and high yield bonds. Ms. Vandersteel earned her B.A. from Washington & Lee University. She is a CFA charterholder.

# Capsule Biographies: Fixed Income

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**Allan Berliant** Mr. Berliant is a member of the global fixed income group. Prior to joining GMO in 2003, he worked at Hartford Investment Management Company as director of asset-backed securities. Previously, he was a vice president within Structured Asset Research at Zurich Scudder Investments. Mr. Berliant earned his B.S. from The Johns Hopkins University and his M.B.A. from University of Chicago.

**Max Golts** Dr. Golts is a member of GMO's global fixed income group, focusing on quantitative research. Prior to joining GMO in 2005, he worked on fixed income analytics and strategies for State Street Global Markets. Previously, he did volatility research at Fort Hill Capital Management. Dr. Golts earned his undergraduate degree from Kiev University and his Ph.D. in Mathematics from Yale University.

**Andy Gossard** Mr. Gossard works with GMO's global fixed income group, focusing on technology and research. Prior to joining GMO in 2005, he was an associate software engineer for 170 Systems. Mr. Gossard earned his B.S. in Computer Science from the University of Michigan.

**Gregory Jones** Mr. Jones works with GMO's global fixed income group, focusing on quantitative research. Prior to joining GMO in 2007, he was a Teaching Fellow at Harvard University. Mr. Jones earned his B.S. in Mathematics and Physics from the University of Missouri, Columbia and his Ph.D. in Physics from Harvard University.

**Tracey Keenan** Ms. Keenan works with GMO's global fixed income group as a finance/repo trader. Prior to joining GMO in 2002, she held various positions at Standish Mellon, most recently as assistant vice president of fixed income trading. She earned her B.A. in political science from Stonehill College and her M.B.A. in Finance from Suffolk University.

**Justin Klosek** Mr. Klosek is a member of the global fixed income group. Prior to joining GMO in 2002, he worked on the fixed income teams of both Morgan Stanley Asset Management and Long-Term Capital Management. Mr. Klosek earned his B.S.E. in Civil Engineering and Operations Research from Princeton University and his M.S. in Civil Engineering from Massachusetts Institute of Technology. He is a CFA charterholder.

**Madelyn Tucker** Ms. Tucker is a trader for the global fixed income group. Prior to joining GMO in 1997, she worked at Fidelity Investments where she traded asset backed corporate and mortgage securities, and monitored benchmarks for trust funds. Prior to that, she was director of financial systems development at Cherry Webb. Ms. Tucker earned her M.B.A. from the Simmons School of Management.

**Susan Wisialko** Ms. Wisialko is a member of the global fixed income group. Prior to joining GMO in June 2007, she was the Managing Partner of Fixed Income Analytics, LLC, a boutique consulting firm providing independent credit research in structured products. Her experience includes almost 20 years experience structuring, analyzing and marketing asset-backed transactions at State Street Capital Markets, Merrill Lynch Money Markets Marketing, and Standard and Poor's. Susan earned a B.A. in Spanish from Dartmouth College.

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