

INVESTMENT ADVISORY COUNCIL
WEDNESDAY, April 9, 2008

MEETING NO. 354

Members present:

Thomas Barnes
Thomas Fiore, representing Robert Genuario
Michael Freeman
James Larkin, Chairman
William Murray
Denise L. Nappier, Treasurer
Sharon Palmer
David Roth
Carol Thomas
Peter Thor

Absent:

David (Duke) Himmelreich

Others present:

Howard G. Rifkin, Deputy Treasurer
Linda Hershman, Assistant-Deputy Treasurer/Chief of Staff
Lee Ann Palladino, Acting Chief Investment Officer
Gregory Franklin, Assistant Treasurer-Investments
David Holmgren, Principal Investment Officer
Wayne Hypolite, Executive Assistant
David Johnson, Principal Investment Officer
Donald Kirshbaum, Investment Officer
Catherine LaMarr, General Counsel
Shelagh McClure, Director of Compliance
Christine Palm, Communications
Jason Price, Principal Investment Officer
Linda Tudan, Chief Executive Assistant
Lawrence Wilson, Assistant Treasurer-Cash Management
Christina McGinnis, Executive Secretary
Winifred (Winnie) Scalora, Administrative Assistant

Guests:

Bradley Atkins, Franklin Park
Laura Backman, State Street Bank
Joseph Barcic, Mercer Investment Consulting
Rashid Hassan, Mercer Investment Consulting
Robyn Kaplan-Cho, Connecticut Education Association
Harvey Kelly, Leumas Advisors
Lauren B. Leichtman, Levine Leichtman Capital, Partner
Arthur E. Levine, Levine Leichtman Capital, Partner
Jacqueline Lyons, State Street Bank

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2

Julie Naunchek, CSEA-Retiree Council #400
Richard Nuzum, Mercer Investment Consulting

Chairman James Larkin called the Investment Advisory Council ("IAC") Meeting to order at 9:05 A.M.

Approval of Minutes

Chairman Larkin asked for comments on the Minutes of the March 12, 2008 IAC Meeting. **There being no comments, a motion was made by Peter Thor, seconded by Carol Thomas, that the Minutes of the March 12, 2008 IAC meeting be accepted as drafted. The motion was passed unanimously.**

Comments by the Treasurer

Treasurer Denise Nappier began her remarks by extending greetings to all present. She also welcomed Winnie Scalora, the new Administrative Assistant in the Pension Funds Management Division ("PFM"), who will be responsible for the coordination of the IAC meetings, including taking the minutes, and serving as the contact for IAC member questions. Ms. Scalora stated she was pleased to be here and looked forward to working with the IAC members.

Treasurer Nappier gave a brief update on the Pension Obligation Bond ("POB") sale and said the meetings with the rating agencies are complete, and that the high quality credit ratings have been affirmed. Treasurer Nappier then informed the IAC about a series of road shows with the Debt Management staff and Tom Fiore, of the Office of Policy and Management. She further stated that the kick-off meeting was held in Hartford and several team members also went to Boston to present to brokers and institutional investors; a similar presentation is scheduled for New York. Treasurer Nappier said this bond issue will be open to individual investors during a retail sales period; brochures have been sent out to 90,000 teachers; a website for the POB is on the internet at www.buyctbonds.com. She further commented that the POB is scheduled to close on April 30, 2008, and at such time the Teachers' Retirement Fund ("TERF") will have an additional \$2 billion. Treasurer Nappier said these funds will be invested according to the asset allocation plan for the TERF.

Turning to today's agenda, Treasurer Nappier noted that Mercer will present an educational session on active extension strategies for the Connecticut Retirement Plans and Trust Funds' ("CRPTF") traditional asset classes where these strategies, better known as "130/30" or "120/20," will be considered. She pointed out that this strategy can be designed to fit within our existing allocation space for active U.S. equity mandates. Treasurer Nappier stated that Mercer's educational overview will outline the benefits of implementing this strategy, such as increasing the information ratio and the ability to benefit from the stock selection insight of the money managers while at the same time keeping benchmark risk levels intact.

Regarding the Private Investment Fund (“PIF”), Treasurer Nappier said the Managing Principals and Founders of Levine Leichtman Capital Partners, LLC (“Levine Leichtman”), will present an opportunity in Levine Leichtman Capital Partners IV, L.P. (“Levine Leichtman IV”). She commented that Levine Leichtman IV is being formed to make mezzanine debt and structured equity investments in middle market U.S. companies seeking opportunities to work with management teams that do not want to lose control of their companies but need financial support to grow their businesses.

Finally, Treasurer Nappier said that the quarterly Real Estate Fund (“REF”) performance report and corporate governance overview will be provided.

CRPTF Final Performance for March 2008

Lee Ann Palladino, Acting Chief Investment Officer, reported on the developments that have occurred in the market place since the last meeting. She discussed the JPMorgan Chase takeover of Bear Stearns and the Federal Reserve’s initiatives to improve liquidity. Ms. Palladino concluded by stating that, for the first time in nine months, a slight firming is occurring in the credit markets.

Ms. Palladino commented on the sub-prime write-downs at financial firms totaling \$232 billion and its affect on the stock markets, noting that the U.S. and international stock markets have rallied since the Federal Reserve’s implementation of the liquidity efforts.

Regarding February’s results, Ms. Palladino reported on the State Employees’ Retirement Fund (“SERF”) stating the February 29, 2008 value of SERF was \$9.5 billion. She continued that for the fiscal year-to-date, the SERF return fell 3.40% versus the benchmark decline of 5.39%, outperforming the benchmark by 199 basis points. She pointed out that during downward markets our lower risk profile has positioned the CRPTF to outperform in this environment.

Ms. Palladino reported on the long-term performance horizons, stating the 3-year horizon outperformed the benchmark by 83 basis points. She said the 5-year horizon had posted strong relative results; however, the CRPTF underperformed its benchmark by 83 basis points. Finally, Ms. Palladino said that over the longer term, we’ve outperformed the 7-year horizon by 42 basis points.

Ms. Palladino said that on April 30, 2008 PFM is expecting to receive POB sales proceeds in the amount of \$2 billion. She stated that the CRPTF will implement its first phase of the asset allocation rebalance and all the plans and trusts will be rebalanced, including TERF, which will now include the incremental bond proceeds.

Treasurer Nappier pointed out that our performance is in line with the structural design and strategy noting that the CRPTF tends to do better in down markets.

Presentation by Mercer on Active Extension Strategies “130/30”

Joseph Barcic, Richard Nuzum and Rashid Assan, representatives of Mercer, provided an educational overview of active extension strategies, focusing on 130/30. Mr. Barcic clarified the difference between the 120/20 and 130/30 strategies indicating that the lower number represents the amount of short selling that is targeted in the portfolio. Messrs. Nuzum and Assan gave an in-depth overview of the 130/30 strategy. Mr. Assan explained the objective, execution and implementation of the strategy. He further discussed the goal of 130/30, which is to short 30% of the stocks that are expected to under perform, over allocate by 30% to stocks that money managers hold a high conviction for out performance, and still maintain a net 100% position and a risk profile that closely matches the benchmark.

Throughout the presentation Messrs. Barcic, Nuzum and Assan responded to multiple questions from IAC members regarding risk and the difference between the traditional asset managers and hedge fund managers. Treasurer Nappier pointed out that this is an evolving strategy in the institutional market place for pension funds, and that institutional managers are experienced, have multiple strategies, and typically manage more assets than hedge fund managers. Mr. Assan provided a short list of active extension strategies with track records showing the strategies that have outperformed and underperformed their benchmarks. He noted that since this product is fairly young, the long-term tracking records are inconclusive.

Presentation by Levine Leichtman Capital Partners, LLC

Jason Price, Principal Investment Officer, provided opening remarks regarding Levine Leichtman and that it has been recommended that the CRPTF commit up to \$75 million to Levine Leichtman IV, a private equity investment opportunity. He discussed Levine Leichtman IV's fit within PIF and reviewed its compliance with the investment policy guidelines. Mr. Price further added that Levine Leichtman was selected because of its low historical loss ratio, its deep and established team, as well as its strong track record, particularly in down markets, generating an ROI of 1.5 times and an IRR of roughly 23.4%.

Presentation by Levine Leichtman Capital Partners, LLC

Lauren Leichtman and Arthur Levine, of Levine Leichtman, made a presentation to the IAC regarding their structured equity fund, Levine Leichtman IV. Arthur Levine first gave an overview of the firm stating it invests in the lower end of the U.S. middle market. He stated Levine Leichtman has \$3.5 billion of capital under management prior to this fund, has a worldwide network of limited partners, including other major state pension funds, and is a registered investment advisor. Mr. Levine also mentioned the strong investment performance, including 23 realized deals with a 46% IRR.

Ms. Leichtman then reported on the performance of its structured equity funds including the investment track record showing an overall return of 23%. Mr. Levine then commented on CiCi's Pizza, a fully realized portfolio investment. He next explained the firm's proprietary

control and value creation strategy and added that it has had 24 years of successful investing experience and has demonstrated superior investment performance in all economic cycles, particularly in down cycles.

An IAC member asked about the staff at Levine Leichtman and the recent turnover. Ms. Leichtman cited that Levine Leichtman recently expanded and opened offices in Chicago, Dallas and New York, requiring them to bring on new personnel. Mr. Levine added that these managers have 3 to 26 years of experience in commercial banking, investment banking and private equity.

Roll Call of Reactions for Consideration of Levine Leichtman Capital Partners IV, L.P.

Ms. Thomas, David Roth, Sharon Palmer, Mr. Thor, Thomas Fiore, William Murray, Michael Freeman, Thomas Barnes and Chairman Larkin were all in favor of the investment. **Chairman Larkin asked for a motion to waive the 45-day comment period. A motion was made by Mr. Freeman, seconded by Ms. Thomas to waive the 45-day comment period for the Levine Leichtman Capital Partners IV, L.P. The motion was passed unanimously.**

Real Estate Fund Review as of December 31, 2007

David Johnson, Principal Investment Officer, reported on the REF through the quarter ending December 31, 2007. He stated for periods ending December 31, 2007, the 8.2% long-term result is the second highest of the asset classes, boding well for the future performance, and that \$900 million had been funded into the REF. He further added that the REF was up from \$280 million two years ago.

Mr. Johnson said the CRPTF now has 24 active accounts in the real estate area with \$1.58 billion in total commitments. He added that \$504 million is in outstanding commitments, which shows a \$322 million improvement compared to June 30, 2007. Regarding quarterly returns, Mr. Johnson said the REF is still 164 basis points behind NCREIF but the trend throughout the four quarters of 2007 shows steady improvement. Mr. Johnson indicated the REF position is conservative with 60% of the assets fully stabilized and over 80% has been invested in core properties.

Mr. Johnson noted that the details of the liquidating portfolio show overall disappointing returns. He said the core portfolio shows good diversification and the non-core portfolio is performing above index. Finally, Mr. Johnson reviewed each fund commenting on performance and market conditions.

Chairman Larkin thanked Mr. Johnson for his excellent report.

Corporate Governance and MacBride Compliance as of December 31, 2007

Donald Kirshbaum, Investment Officer, reported on the Treasurer's activities related to corporate governance and MacBride compliance. He stated that there were several corporate governance issues in which the Treasury has been active as a shareholder for the current 2008 proxy season. Mr. Kirshbaum said these issues include executive compensation, internal pay equity, say on pay, board of directors' independence, classified boards and diversity, climate risk, and sustainability issues. He then noted that each of these issues is viewed as critical to a company's financial performance and the long-term economic interests of the CRPTF.

In the area of executive compensation, Mr. Kirshbaum reported on issues of independent compensation consulting, persuading Caterpillar and R.R. Donnelly to adopt policies. He said that Abercrombie & Fitch, Supervalu and several other companies were involved in discussions on internal pay equity, and added that a few companies have already adopted the say-on-pay policy. Finally, Mr. Kirshbaum said there is better disclosure and more robust analyses regarding compensation.

Concerning climate change, Mr. Kirshbaum reported on the Investor's Global Warming Shareholder Campaign, the Investor Network on Climate Risk and the February 14, 2008 Investor Summit on Climate Risk at the U.N. Mr. Kirshbaum further added that a press conference is to be held later today announcing that Ford has agreed to set greenhouse gas emissions goals.

Chairman Larkin thanked Mr. Kirshbaum for his report and the successful efforts of the Policy Unit.

Comments by Chairman Larkin

Chairman Larkin said that on April 8, 2008 Treasurer Nappier issued a press release announcing that on April 1, 2008 the Treasury released the Preliminary Official Statement relating to the State's proposed sale of approximately \$2 billion of Taxable General Obligation Bonds.

Other Business

Chairman Larkin reminded the members of the IAC to submit their insurance declaration pages. Deputy Treasurer Howard Rifkin reminded all IAC members to submit their outstanding Statement of Financial Interests Disclosure paperwork to the Ethics Commission, which is due May 1, 2008.

Review of the IAC Budget for the quarter ending December 31, 2007

Ms. Palladino reported that the IAC is under budget for the fiscal year to date by approximately \$4,000. She noted in particular the IAC is under budget in education and travel.

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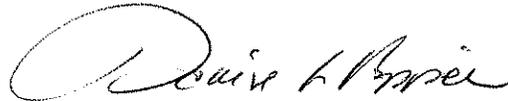
7

Discussion of preliminary agenda for May 14, 2008 IAC Meeting

Chairman Larkin invited IAC members to submit agenda items for the May 14, 2008 meeting. There being no further business, the meeting was adjourned at 11:45 a.m.

An audio tape of this meeting was recorded.

Respectfully submitted,



**DENISE L. NAPPIER
SECRETARY**

Reviewed by



**JAMES T. LARKIN
CHAIRMAN**