INVESTMENT ADVISORY COUNCIL
Wednesday, July 10, 2013

MEETING NO. 407

Members present:	Janice (Jan) Carpenter Thomas Fiore, representing Benjamin Barnes Joshua Hall David (Duke) Himmelreich William Murray Denise L. Nappier, Treasurer Carol Thomas Peter Thor
Absent:	Neil G. Budnick, Chairman Laurence N. Hale
Others present:	Christine Shaw, Deputy Treasurer Lee Ann Palladino, Chief Investment Officer Gary Carter, Interim Deputy Chief Investment Officer Catherine LaMarr, General Counsel Shelagh McClure, Director of Compliance Joanne Dombrosky, Principal Investment Officer Cherie Santos-Wuest, Principal Investment Officer Reginald Tucker, Investment Officer David Barrett, Director of Communications Linda Tudan, Executive Assistant Winifred (Winnie) Scalora, Executive Secretary
Interns:	Claybourne Couts Tyler Dew Chelsea Haddad George Miles Jeremiah Rankin
Guests:	Rebekah Brown, JP Morgan Asset Management Paul Canning, UBS Realty Investors, LLC Ann Cole, JP Morgan Asset Management Kevin Crean, UBS Realty Investors, LLC Will Greene, Loop Capital Markets Gary Gowdy, UBS Realty Investors, LLC Kevin Howard, JP Morgan Asset Management Robin Kaplan-Cho, Connecticut Education Association Rob Kochis, The Townsend Group

Ronald Lanier, UBS Realty Investors, LLC
Cathy Marcus, Prudential Investment Management, Inc.
Claire Shaughnessy, Hewitt EnnisKnupp, Inc.
Liz Smith, AllianceBernstein Institutional Investments
Michael Stark, The Townsend Group
Larry Teitelbaum, Prudential Investment Management, Inc.
Kevin Vandolder, Hewitt EnnisKnupp, Inc.
Arnold West, Private Citizen

With a quorum present, Acting Chair Carol Thomas stated that Chairman Neil G. Budnick would not attend the meeting, and she called the Investment Advisory Council ("IAC") meeting to order at 9:00 a.m.

Approval of Minutes of the June 12, 2013 IAC Meeting

Acting Chair Thomas called for a motion to approve the minutes of the June 12, 2013 IAC meeting. **There being no comments, a motion was made by Peter Thor, seconded by Joshua Hall, that the minutes of the June 12, 2013 IAC meeting be accepted as drafted. The motion was passed with the exception of Janice Carpenter who abstained due to her absence from the June 12, 2013 meeting.**

Comments by the Treasurer

Treasurer Denise L. Nappier began her comments by welcoming everyone to the first IAC meeting of Fiscal Year ("FY") 2014. Treasurer Nappier said that the Connecticut Retirement Plans and Trust Funds' ("CRPTF") performance was projected to exceed the actuarial investment return assumptions of 8% for the State Employees' Retirement Fund ("SERF") and 8.5% for the Teachers' Retirement Fund ("TERF") with double digit positive performance for the 2013 fiscal year-end. She stated that the May 31, 2013 fiscal year-to-date performance was 14.23%, an increase of 14 basis points ("bps") over the April 2013 performance. Treasurer Nappier said that robust returns of 17.48% and 10.38% were posted for the one-year and three-year time horizons, respectively.

Next, Treasurer Nappier announced that after considering the feedback from the IAC, the extensive due diligence of the Office of the Treasurer's ("OTT") investment staff and the Real Estate Fund ("REF") consultant, The Townsend Group ("Townsend"), she had decided to commit up to $100 million to USAA Eagle Real Estate Fund, L.P. ("Eagle"), a core-plus, open-ended real estate fund managed by USAA Eagle Real Estate Company, contingent upon successful contract negotiations.

Regarding the day's agenda, Treasurer Nappier stated that she was presenting the amendments to the Investment Policy Statement ("IPS"), Appendix A, for the IAC's vote, which she adopted in substantially the same form as the recommended amendments that were presented at the June

12th IAC meeting. She remarked that, as discussed at June's IAC meeting, the IPS revisions were the final outstanding components of the 2012 asset allocation and liability study ("A/L Study"). Treasurer Nappier said that the IPS also clarified the OTT's ability to make tactical asset allocation moves within the upper and lower policy limits of the policy ranges established by the IAC.

Next, Treasurer Nappier stated that she would present for the IAC's consideration the proposed project plan for the currency overlay manager search. She noted that the competitive search would be conducted through a request for proposal ("RFP") process in order to select one or more firms to direct the investments of active and passive currency overlay separately managed accounts in the CRPTF's Developed Markets International Stock Fund ("DMISF"). Treasurer Nappier stated that the CRPTF presently had one currency overlay manager, Pareto New York LLC ("Pareto"), whose contract would expire in February 2014.

Finally, Treasurer Nappier said that three Open Ended Core Funds ("OECFs") would be presented for consideration as opportunities in the REF: JP Morgan Chase Strategic Property Fund ("JPM-SPF"), Prudential Property Investment Separate Account LP ("PRISA") and UBS Trumbull Property Funds ("UBS-TPF", "UBS-TPI" and "UBS-TPG"). She remarked that they were experienced OECFs with solid top-quartile performance. Treasurer Nappier noted that in addition to her presentation of Eagle at last month's IAC meeting, she discussed her intent to pursue a larger strategy for investment in OECFs. She said that the addition of the OECF managers to the existing core and core plus open-end managers would create a strong stable of core managers, and the goal of having a platform of OECF managers was to allow for maximum investment flexibility in maintaining the IPS allocation to core strategies as the REF grew. In closing, she said that the ability to increase or decrease allocations among core real estate managers within the policy guidelines would allow for better management of core real estate queues and liquidity, and it would enhance the REF's ability to remain fully invested and to tactically position the CRPTF's core real estate.

Update on the Market and the CRPTF Final Performance for the Month Ended May 31, 2013

Lee Ann Palladino, Chief Investment Officer, led a discussion concerning the CRPTF's active versus passive investment strategies and said that the CRPTF considered both active and passive strategies in order to manage the risk and return objectives for each of the Combined Investment Funds ("CIF"). Ms. Palladino stated that in terms of implementation, the OTT staff endeavored to make informed and effective decisions surrounding the active/passive allocations and that decisions were addressed during the OTT's annual review process where passive allocations were revised or validated.

By way of background, Ms. Palladino said that the passive discussion would address 1) Hewitt EnnisKnupp's ("HEK") views on the active/passive allocation; 2) the guidance of the IPS as it relates to the active/passive allocation; and 3) the CRPTF's historic management of its active/

passive allocation.

Claire Shaughnessy and Kevin Vandolder, Partners of HEK, commented on HEK's philosophy regarding passive management, and commented on opportunities in the various fund categories that added value through actively managed funds. Mr. Vandolder commented on the themes that supported indexing a substantial portion of U.S. equity investments including market efficiency, benchmark replication and cost. Next, Ms. Shaughnessy highlighted active versus passive management of U.S. equities, non-U.S. equities, core fixed income and high yield fixed income funds.

With respect to the Core Fixed Income Fund ("CFIF"), Mr. Vandolder remarked that the U.S. government dominated the Barclay aggregate, and he said that it had been fairly easy for active managers to successfully underweight the U.S. government segment relative to the Barclay's aggregate benchmark. Regarding high yield fixed income, Ms. Shaughnessy said that Hewitt recommended 100% active management due to the lack of institutional quality passive products. Next, Ms. Shaughnessy summarized the asset class attractiveness for passive management, and said that U.S. equity, non-U.S. developed markets and core fixed income were candidates for a portion of assets to be passively managed.

Next, Ms. Palladino discussed the CRPTF's IPS' guidance on active/passive application. She said that the IPS dictated that passive allocations assured broad diversification to a benchmark and added that the performance relative to the benchmark was based upon the assumption that a portion of the underlying assets would be actively managed. She compared the performance of passive versus active managers for U.S. equities, developed international equities, and core fixed income strategies over the 10-year period as of March 31, 2013. She said most active strategies had struggled verses the passive benchmarks. On a positive note, Ms. Palladino added that the CRPTF had effectively managed its active/passive allocations over time as performance versus the benchmark improved.

In conclusion, Ms. Palladino commented on the portfolios that the CRPTF continued to manage actively at 100%: the Emerging Markets International Stock Fund, Emerging Markets Debt Fund, High Yield Bond Fund and Inflation Linked Bond Fund and stated that the CRPTF reviewed its portfolio construction on at least an annual basis. IAC members posed several questions regarding the active/passive allocation. Treasurer Nappier, Ms. Palladino and HEK staff responded to several comments and reinforced the strategy that resulted in the most appropriate allocation decisions for the CRPTF portfolio.

Presentation and Consideration for Approval of the Treasurer's Adopted Amendment to the Investment Policy Statement Appendix

Ms. Palladino stated that at the June 12, 2013 IAC meeting, Treasurer Nappier presented her draft amendments to the IPS, Appendix A Section I and II, which incorporated the asset allocation plans for the Policemen and Firemen Survivors' Benefit Fund, the State Attorneys'

Retirement Fund and the Other Post-Employment Benefits Trust Fund, and clarified the ability to tactically invest within the upper and lower bands of approved asset allocation policy ranges. She said that at the June 12, 2013 meeting, there had been no formal input by the IAC members, and Treasurer Nappier adopted the changes on July 10, 2013 in substantially the same form as she presented them to the IAC at the June meeting.

Acting Chair Thomas called for a motion to approve the Treasurer's July 10, 2013 adopted IPS Appendix. **William Murray moved for approval of the adopted amendment to the IPS Appendix. Thomas Fiore seconded the motion. The motion was passed unanimously to approve the Amendment to the IPS Appendix as adopted by Treasurer Nappier.**

<u>Consideration for the Search Process for a Currency Overlay Investment Manager for the Developed Markets International Stock Fund</u>

Gary Carter, Interim Deputy CIO, provided a project plan timeline and evaluation/selection criteria for a Currency Overlay Investment Manager for the DMISF. Mr. Carter said that fluctuations in foreign currency values could have a meaningful impact on DMISF returns over the short to intermediate term and an overlay would be utilized to mitigate currency volatility. Mr. Carter reviewed the milestones of the project plan and the selection criteria for the overlay manager search. Finally, Mr. Carter stated that the full details regarding the RFP would be posted July 15, 2013.

Acting Chair Thomas called for a motion to endorse the search process for a Currency Overlay Investment Manager for the DMISF. **Ms. Carpenter entered a motion to endorse the Currency Overlay search, and Mr. Thor seconded the motion. The motion was passed unanimously.**

<u>Presentation by and Consideration of Open Ended Core Funds</u>

Cherie Santos-Wuest, Principal Investment Officer ("PIO"), provided opening remarks and introduced three OECFs: JPM-SPF, PRISA and UBS Trumbull Property Funds ("UBS-TPF", "UBS-TPI" and "UBS-TPG") - all real estate investment opportunities. Robert Kochis, Principal, and Michael Stark, Associate of Townsend, the CRPTF's consultant to the REF, joined Ms. Santos-Wuest. Ms. Santos-Wuest provided an overview of the REF core program and said that although core real estate assets were currently richly priced, they were still attractive to investors because they generated returns at wider spreads to risk-free rates, due to rising property values and increasing rent levels as the overall economy strengthened. Next, she provided a brief summary of core real estate and its long-run role in a diversified portfolio.
Ms. Santos-Wuest then commented on the five funds being presented by the three OECF candidates, and noted that they were some of the industry's most seasoned and best performing OECF managers. She first remarked about JPM-SPF, and said that the fund invested in large-cap, multi-family, industrial, urban office, and retail properties in major metropolitan areas in the U.S.; and the objective of the fund was to invest in high quality markets in major gateway

markets with total returns attributable to 75% current income, and 25% capital appreciation. Ms. Santos-Wuest provided more specifics on JPM-SPF's returns over the three to five year market cycle, and she said that it met the REF's needs with open-ended structure and geographic exposure to strong southwest and Pacific markets.

Next, Ms. Santos-Wuest remarked about PRISA, the first OECF in the U.S., and noted that it was a top quartile performer that invested in all core sectors including office, retail, industrial, multi-family and self-storage. She noted that PRISA's objective was to produce a total return each year to meet or exceed its ODCE index while maintaining the benefit of a broadly diversified and core real estate portfolio. Finally, Ms. Santos-Wuest noted that PRISA was expected to increase the REF's exposure to Pacific markets and provide more exposure to apartment, industrial and non-core sectors.

Next, Ms. Santos-Wuest commented on the three UBS Trumbull Funds: UBS-TPF, a core investment fund; UBS-TPI, a fixed income fund; and UBS-TPG, a core-plus value-add fund. She said that all three funds were open ended, and noted that UBS Realty, located in Hartford, managed the funds. Ms. Santos-Wuest provided background information on the origins of UBS Realty, and she commented on the CRPTF's earlier investments in its funds during the late 1980's and 1990's. Ms. Santos-Wuest said that UBS-TPF sought to provide a 5% real rate of return after inflation, before fees, over a three to five-year period by investing in stabilized, well leased income producing assets in major gateway markets in the U.S. With respect to UBS-TPI, Ms. Santos-Wuest commented that UBS Realty's fixed income fund invested in participating mortgage loans with an equity "kicker" that sought to provide attractive returns and relative low risk. Ms. Santos-Wuest noted that UBS-TPI and UBS-TPF had outperformed their benchmarks through multiple real estate cycles since inception. Finally, she said that UBS-TPG invested primarily in properties and other real estate equity investments and noted that UBS-TPG sought to exceed its benchmark, the NFI-ODCE Index, by at least 200 bps per annum over any given three to five year period. In closing, Ms. Santos-Wuest referred to Townsend's report that said UBS-TPG would provide the REF with immediate increased exposure to accretive multi-family sectors and to Pacific markets while reducing its exposures to non-core sectors in the southeast and mountain markets, in order to achieve geographic and sector diversification and minimize tracking error to the REF's benchmark, the NCREIF Property Index ("NPI").

In response to Mr. Thor, Ms. Santos-Wuest said that all five funds were being considered, and she noted that the investment strategies of each fund focused on different areas of the market and would complement the REF's ability to seek different strategies. Ms. Carpenter posed questions regarding fees to which Ms. Santos-Wuest discussed the proposed fees and stated they would be addressed again during contract negotiations.

Presentation by JP Morgan Asset Management

JP Morgan -- represented by Rebekah Brown, Executive Director; Ann Cole and Kevin Howard, Managing Directors -- made a presentation to the IAC. Mr. Howard introduced the team. Next, Ms. Brown began by providing a snapshot view of its platform and said that JP Morgan's global real assets currently totaled over $64 billion in assets under management, with about $40 billion invested in direct real estate in the U.S. Next, she commented on JP Morgan's view of risk mitigation, a particularly important factor in real estate. Ms. Brown remarked that JP Morgan was in the bottom quartile in terms of risk and in the top quartile in terms of performance, which made it very competitive.

Next, Ms. Cole commented on JP Morgan's investment strategy for its Strategic Property Fund, and she discussed the investment characteristics and its risk and return expectations. She added that its large assets consistently outperformed its peers throughout market cycles in both major and secondary markets on a longer term basis. She said that from a cash perspective, JPM-SPF generated about $800 million of net operating income cash flow from the existing assets and commented on JPM-SPF's consistent outperformance over both the long and short-term.

Presentation by Prudential Investment Management, Inc.

Prudential Investment Management, Inc. ("Prudential") -- represented by Cathy Marcus, Senior Portfolio Manager, and Larry Teitelbaum, Principal -- made a presentation to the IAC. Mr. Teitelbaum provided an overview on Prudential's two firms: Prudential Financial, which had a significant presence in the Hartford area, and focused on insurance, asset management and retirement services; and Prudential Real Estate Investors ("PREI"), which was a leader in global real estate investment management, with over $50 billion of assets under management.

Next, Ms. Marcus commented on PRISA's differentiating characteristics. She said that PRISA targeted a total return of 7.5% to 9.5% over a complete market cycle, while meeting or exceeding the NFI-ODCE Index. She then spoke about PRISA's geographic diversification and said that it remained focused on markets where supply constraints were likely to result in better long-term fundamentals.

In response to Ms. Carpenter's question regarding the San Francisco Bay area, Ms. Marcus said that Prudential's outlook was very bullish on the tech-related markets and was also bullish on other areas such as Austin and Boston. In response to Mr. Fiore's question regarding one of PRISA's more challenged properties, Ms. Marcus stated that the property had been speculative at the time of purchase and PRISA's current guidelines no longer allow speculative purchases. Mr. Teitelbaum added that the property had since improved, attracting two large credit tenants, and that the building's improved leasing and increased valuation provided potential benefit to new investors to the fund.

Presentation by UBS Realty Investors, LLC

UBS Realty -- represented by Ronald Lanier, Executive Director; Matt Lynch, Head of UBS Global Real Estate-US; Kevin Crean, Gary Gowdy, and Paul Canning, Senior Portfolio Managers of UBS-TPF, UBS-TPI and UBS-TPG, respectively -- made a presentation to the IAC.

Mr. Lanier discussed UBS Realty's global platform and noted that 150 senior investment professionals were based in Hartford. Next, he presented a risk-return profile on UBS Realty versus the NFI-ODCE. Mr. Lanier stated that UBS-TPF consistently produced higher returns while experiencing lower risk than competitor funds in its peer group.

Next, Mr. Lynch provided an overview of UBS Global Asset Management Group's platform. He remarked that it had grown out of Aetna, Inc., and that it had increased its assets from $3 billion to $29 billion, along with expansion of its Hartford employment base by over 75% since 1996. He said the Trumbull property funds sought to deliver the best return at the lowest risk and were more income oriented than its competitors.

Mr. Crean then commented on the UBS-TPF portfolio. He said that it was a well-diversified core fund with 182 different investments primarily in existing well-leased assets with an income focus. He said that UBS-TPF utilized diversification as one of the tools to manage risk, and it reviewed property type, geography and economic sector. Next, Mr. Crean said that UBS-TPF did not have liquidity issues like many of its competitors during the Great Recession, due to its low leverage relative to most of its peers. Finally, he commented on UBS-TPF's consistent strategy and proven track record, which has outperformed the NFI-ODCE 78% of the time since inception.

Next, Mr. Gowdy highlighted the UBS-TPI fund. He said that UBS-TPI, which began in 1981, was a conservative hybrid investment vehicle that primarily invested in mortgages with an equity participation, and was a core, open-end, income-oriented U.S. real estate debt fund. Mr. Gowdy said that UBS-TPI had a ten year and inception-to-date annualized returns of 8.4% and 9.5% respectively without the use of leverage.

Next, Mr. Canning commented on UBS-TPG's investment strategy as a value-added investment fund, and stated that it sought to build net operating income from its properties. He discussed UBS-TPG's objectives to exceed the NFI-ODCE by at least 200 bps per annum over any three to five year period. Finally, Mr. Canning commented on the Great Recession's impact on higher-risk, higher-leveraged strategies, and added that as the economy and real estate markets recovered, UBS-TPG's one and three year returns delivered well in excess of its NFI-ODCE benchmark.

The UBS Global Investors team responded to several questions posed by IAC members. In response to Mr. Murray's question regarding the average investment, team members commented on the range of its investors and said it was fairly wide, with 73 investors and an average investment size of approximately $35 million. In response to Mr. Fiore, Mr. Lynch said that the economy would continue to recover at a slow pace, and added that a construction slowdown had reduced supply.

Roll Call of Reactions to the Open Ended Core Funds

Ms. Carpenter posed a question regarding litigation disclosures and potential headline risk for JP Morgan. Ms. Palladino responded that many large banks disclosed litigation, particularly in light of the financial crises, and said that disclosures of any pending legal matters were reviewed by the OTT's legal team.

Mr. Thor, Mr. Hall and Ms. Carpenter agreed that all three funds were strong candidates, but they preferred the UBS Trumbull Property Funds over JPM-SPF and PRISA. Mr. Murray, Mr. Fiore and Chair Thomas said that all three were excellent candidates. Mr. Himmelreich recused himself and said that he had previously represented a principal of one of the candidates under consideration.

Acting Chair Thomas called for a motion to waive the 45-day comment period. **A motion was made by Mr. Murray, seconded by Mr. Hall, to waive the 45-day comment period for the Open Ended Core Funds: JP Morgan Chase Strategic Property Fund, Prudential Property Investment Separate Account LP and UBS Trumbull Property Funds. The motion was passed with the abstention of Mr. Himmelreich.**

<u>Other Business</u>

Acting Chair Thomas stated that the next IAC meeting would be held on September 11, 2013, and she invited the IAC members to submit agenda items for that meeting.

Ms. Palladino presented the IAC budget for the quarter ended March 31, 2013. Acting Chair Thomas added that Chairman Budnick was researching educational presentations for the IAC.

<u>Comments by the Chairman</u>

There being no further business, Acting Chair Thomas adjourned the meeting at 11:56 a.m.
This meeting was electronically recorded.

Respectfully submitted,

Denise L. Nappier

DENISE L. NAPPIER
SECRETARY

Reviewed by

Carol Thomas

CAROL THOMAS
ACTING CHAIR