

INVESTMENT ADVISORY COUNCIL
Wednesday, November 12, 2014

MEETING NO. 419

Members present:

Janice (Jan) Carpenter
Laurence Hale
Joshua Hall
David (Duke) Himmelreich
Steven Muench
William Murray
Carol Thomas, Interim Chair
Peter Thor

Absent:

Denise L. Nappier, Treasurer
Thomas Fiore, representing Benjamin Barnes

Others present:

Christine Shaw, Deputy Treasurer
Lee Ann Palladino, Chief Investment Officer
Deborah Spalding, Deputy Chief Investment Officer
David Barrett, Director of Communications
Gary L. Carter, Principal Investment Officer
Joanne Dombrosky, Principal Investment Officer
Catherine LaMarr, General Counsel
Shelagh McClure, Director of Compliance
Christina McGinnis, Executive Secretary
Terrence Purcell, Principal Investment Officer
Cherie Santos-Wuest, Principal Investment Officer
Michael Terry, Principal Investment Officer
Linda Tudan, Executive Assistant

Guests:

Jonathan Hogstad, Service Employees International Union
Mark Johnson, Cliffwater, LLC
Peter Keliuotis, Cliffwater, LLC
Robin Kaplan-Cho, Connecticut Education Association
Rob Kochis, The Townsend Group
Kevin Meehan, Goldman Sachs
Lisa Rotenberg, Goldman Sachs
Claire Shaugnessy, Hewitt EnnisKnupp, Inc.
Michael Stark, The Townsend Group
Liz Smith, Alliance Bernstein

With a quorum present, Interim Chair Carol Thomas called the Investment Advisory Council (“IAC”) meeting to order at 9:00 a.m.

Approval of Minutes of the September 10, 2014 IAC Meeting

Chair Thomas called for a motion to approve the minutes of the September 10, 2014 IAC meeting. **William Murray moved to approve the minutes of the September 10, 2014 IAC meeting as drafted. The motion was seconded by Jan Carpenter. There was one abstention, Laurence Hale. There being no discussion, the Chair called for the vote. The motion passed unanimously.**

Comments by the Treasurer

Christine Shaw, Deputy Treasurer, provided the opening remarks in Treasurer Denise L. Nappier’s absence and stated that Treasurer Nappier had no investment-related decisions to announce.

Update on the Market, the Connecticut Retirement Plans and Trust Funds (“CRPTF”) Final Performance for Months Ended August 31 and September 30, 2014

Lee Ann Palladino, Chief Investment Officer (“CIO”), provided an update on the capital market environment, its impact on the performance of the CRPTF and the economic outlook. She reported that as of September 30, the Teachers’ Retirement Fund (“TERF”) and State Employees’ Retirement Fund (“SERF”), the two largest pension plans, both returned -1.01, for fiscal year to date 2015. Focusing specifically on TERF, Ms. Palladino said that the performance was driven by total global equity returns of -2.05%, representing 55% of the portfolio; total fixed income returns of -1.51%, representing 20% of the portfolio; and a 2.24% return for alternative investments, representing 21% of the TERF. Ms. Palladino said the performance remained solid over the longer term, with the TERF and SERF returning 9.15% and 9.22%, respectively, over the five-year horizon. Ms. Palladino presented the quarterly performance of the remaining trust plans.

Ms. Palladino announced that the transition of the Global Inflation Linked portfolio was completed. She added that the Treasurer decided to terminate two U.S.-centered global inflation link managers which were no longer a strategic fit. Ms. Palladino then stated that due to the exit of William Gross, CIO of the Pacific Investment Management Company (“PIMCO”), Treasurer Nappier, through an abundance of caution, decided to place PIMCO on the Watch List while the succession plans of the firm are assessed.

Next, Ms. Palladino gave a presentation on the Alternative Investment Fund (“AIF”). She introduced Mark Johnson, Senior Managing Director of Cliffwater, LLC (“Cliffwater”), AIF consultant to the CRPTF, and Terrence Purcell, Principal Investment Officer (“PIO”), who assisted her with the presentation. Ms. Palladino, Mr. Johnson and Mr. Purcell reviewed the

Investment Policy Statement (“IPS”) parameters of the AIF. They discussed how the program was strategically designed to utilize a fund-of-hedge fund platform to provide expertise in the management of hedge fund strategies, utilization of proprietary risk systems to evaluate the portfolio, thorough due diligence and flexible portfolio construction. They commented on the market for hedge fund strategies, and concluded by discussing how the CRPTF program had performed versus its strategic intention. Specifically, they discussed that since inception in February 2011, the Prudence Crandall portfolio had generated annualized returns of 5.46% per year which fell within the IPS guidelines of generating returns and volatility between the equity and fixed income markets, strong risk-adjusted performance as measured by the Sharpe Ratio, and a low correlation to equities and fixed income. Performance had exceeded expectations as it outperformed its customized benchmark as well as the HFRI fund-of-hedge fund index and the broader HFRI index. They noted that the hedge fund portfolio had not been exposed to a full market cycle and had not yet demonstrated the full downside protection benefit of the strategy. Mr. Murray, Mr. Hale and Peter Thor posed questions regarding hedge funds, to which Mr. Johnson, Ms. Palladino and Mr. Purcell answered satisfactorily.

Alternative Investment Fund Review as of September 30, 2014

Mr. Purcell reported on the AIF for the quarters ended September 30, 2014 and June 30, 2014. His report consisted of an executive summary, portfolio overview, benchmark performance, portfolio investment activity and fund level performance. Mr. Johnson of Cliffwater assisted in presenting the quarterly report.

Mr. Purcell reported that as of September 30, 2014, roughly 87% of the AIF’s committed capital was allocated to the fund-of-hedge fund portfolio. He stated that the diversified fund-of-hedge fund portfolio within the AIF had declined 0.43% for the quarter ended September 30, 2014. He noted that this result trailed the HFRI Fund-of-Funds Composite Index return of 0.55%, and also modestly trailed the broad HFRI Fund Weighted Composite Index return of 0.26%. Mr. Purcell added that the fund-of-hedge fund portfolio earned 6.85% for the twelve months ended September 30, 2014, outperforming the HFRI Fund-of-Funds index return of 6.45% but narrowly trailing the broad HFRI Fund Weighted Composite Index return of 7.03%. He commented that the AIF’s fund-of-hedge fund portfolio continued to be well-diversified across underlying managers and strategies.

Mr. Purcell next reported on the AIF’s exposure to real assets and opportunistic investments, and noted that the performance results were as of June 30, 2014. He stated that the real assets and opportunistic portfolios continued to perform well, as the combined net internal rate of return since inception rose 1% in the June quarter to 13.95%. He remarked that an additional \$11.8 million of capital was contributed to the partnerships in the second quarter, bringing the cumulative capital contributions to \$144.9 million.

Next, Mr. Johnson commented on the fund-of-hedge fund portfolio and general hedge fund industry trends.

Real Estate Fund Review as of June 30, 2014

Cherie Santos-Wuest, PIO, reported on the performance of the Real Estate Fund (“REF”) for the quarter ended June 30, 2014. She welcomed the REF consultants, Rob Kochis, Principal and Michael Stark, Associate, of The Townsend Group, who assisted in presenting the quarterly report.

Ms. Santos-Wuest reported on the REF’s overall performance, the quarterly as well as the 1, 3 and 5-year results, and the portfolio diversification versus investment guidelines and its NCREIF Property Index (“NPI”) benchmark. Ms. Santos-Wuest then reviewed the unfunded commitments, new commitments and new acquisitions for the Core Separate Account and fund vehicles within the REF. She reported that the REF returned 3.6% for the quarter, as of June 30, 2014, and 11.7%, 11.7% and 7.5% on a net basis over the past 1, 3 and 5-year horizons, respectively. She also noted that the REF had outperformed its NPI benchmark by 65 basis points “bps” over the quarter and by 46 bps over the one-year horizon. Finally, Ms. Santos-Wuest discussed the trending improvement in the REF investment returns, having outperformed its benchmark 8 out of the last 10 quarters, which she attributed to the CRPTF’s steady investment in accordance with policy allocation, ongoing improvement across many real estate markets, and general partner selection.

Mr. Kochis and Mr. Stark provided the IAC with an overview of the broader real estate markets and commented on capitalization rates, vacancy trends, U.S. labor force growth, and their impact on various sectors of the commercial real estate market.

Mr. Thor and Duke Himmelreich posed questions regarding the apartment market and real estate performance, to which Mr. Kochis and Ms. Santos-Wuest answered to their satisfaction.

Short-Term Investment Fund Review as of September 30, 2014

Michael Terry, PIO, reported on the performance of the Short Term Investment Fund (“STIF”) for the quarter ending September 30, 2014. Mr. Terry said the STIF earned an annualized yield of 15 bps during the quarter, outperforming its benchmark by 13 bps. He stated that for the twelve month period ended June 30, 2014 the fund earned an annual return of 14 bps, outperforming its benchmark by 12 bps. He noted that currently the STIF had \$4.5 billion in assets and \$50.3 million in reserves. Finally, Mr. Terry reported that the fund’s weighted average maturity was 41 days at the end of the period; daily liquidity was 59% of assets; 54% of STIF’s assets were invested in securities issued, insured or guaranteed by the U.S. government or federal agencies, in repurchase agreements backed by such securities, or in money funds comprised of such securities.

Mr. Terry also provided an economic overview including current information on economic growth, the inflation rate and the short-term yield curve.

Other Business

Chair Thomas presented the draft IAC Meeting Schedule for the 2015 calendar year. **Mr. Hale moved to accept the IAC Meeting Schedule for the 2015 calendar year. The motion was seconded by Steven Muench. There being no discussion, the Chair called for the vote. The motion passed unanimously.**

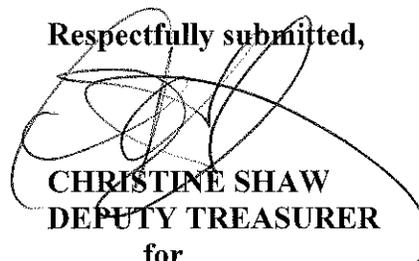
Chair Thomas provided an overview of materials she gathered from a presentation by HESTA, a \$11 billion Australian superannuation pension fund, and its new approach to assessing the reasonableness of management fees. Chair Thomas said the fee methodology was in the early stages of development and that it had not been presented for wide utilization, but she felt it warranted further monitoring given the IAC's concern over the risk of excessive fees. She indicated that HESTA's methodology led to lower fees for some managers of the Australian fund, and resulted in termination of other managers that refused to lower fees. Finally, Chair Thomas commented that such a methodology should be explored as part of the next Asset Liability Study, and added that this methodology could have far-reaching impact on fee reduction efforts across the industry.

Chair Thomas invited the IAC members to submit agenda items for the December 10, 2014 IAC meeting.

There being no further business, Chair Thomas called for a motion to adjourn the meeting. Mr. Thor moved to adjourn the meeting and the motion was seconded by Mr. Murray. There being no discussion, the meeting was adjourned at 11:05 a.m.

This meeting was electronically recorded.

Respectfully submitted,



**CHRISTINE SHAW
DEPUTY TREASURER
for
DENISE L. NAPPIER
SECRETARY**

Reviewed by



**CAROL THOMAS
INTERIM CHAIR**