

INVESTMENT ADVISORY COUNCIL
Wednesday, September 9, 2015

MEETING NO. 426

Members present:

Janice (Jan) Carpenter
Thomas Fiore, representing Benjamin Barnes
Joshua Hall
David (Duke) Himmelreich
Steven Muench
William Murray
Denise L. Nappier, Treasurer
Carol Thomas, Interim Chair
Peter Thor

Absent:

Laurence Hale

Others present:

Richard Gray, Deputy Treasurer
Deborah Spalding, Chief Investment Officer
David Barrett, Director of Communications
Joanne Dombrosky, Principal Investment Officer
Linda Hershman, Chief of Staff
Wayne Hypolite, Executive Assistant
Catherine E. LaMarr, General Counsel
Christina McGinnis, Executive Secretary
Christine Shaw, Chief Compliance Officer
Linda Tudan, Executive Assistant
Lawrence Wilson, Assistant Treasurer

Guests:

Bradley Atkins, Franklin Park
Gustave Christakos, Deutsche Bank
Amy Dunn, Deutsche Bank
Will Greene, Loop Capital Markets
Eduardo Gonzalez, Edgon Financial LLC
Mark Johnson, Cliffwater, LLC
Robin Kaplan-Cho, Connecticut Education Association
Robert Kochis, The Townsend Group
Kevin Meehan, Goldman Sachs Asset Management
Justin Rico Oyola, SEIU
Claire Shaugnessy, AonHewitt Investment Consulting
Diane Smola, AonHewitt Investment Consulting

With a quorum present, Interim Chair Carol Thomas called the Investment Advisory Council ("IAC") meeting to order at 9:04 a.m.

Approval of Minutes of the July 8, 2015 IAC Meeting

Chair Thomas called for a motion to approve the minutes of the July 8, 2015 IAC meeting. **William Murray moved to approve the minutes of the July 8, 2015 IAC meeting as drafted. The motion was seconded by Jan Carpenter. There was one abstention, Joshua Hall. There being no further discussion, the Chair called for the vote. The motion passed unanimously.**

Comments by the Treasurer

Treasurer Denise L. Nappier began her opening remarks by welcoming the IAC members back after the August break. She then discussed the June 30, 2015 fiscal year end investment performance for the two largest plans in the Connecticut Retirement Plans and Trust Funds ("CRPTF"); the Teachers' Retirement Fund ("TERF") and State Employees' Retirement Fund ("SERF"), which posted 2.79% and 2.84%, respectively. Treasurer Nappier then reported the three and five year returns for the TERF of 9.96% and 9.72%%, respectively, and the SERF performance for the same time horizon was 9.99% and 9.82%, respectively. She continued that, because the outlook for investment returns had reverted to more sustainable levels and that the markets had moved into a financial environment that likely will not yield similar results to the robust returns of the past few years, it was imperative that we consider a more realistic investment assumption for the CRPTF, adding that reason dictated that if the assumptions were set at levels unlikely to be attained, pursuing the strategies to meet those assumptions only would erode the financial health of the CRPTF over the long term.

Next, Treasurer Nappier announced that, after having considered the feedback from the IAC and the due diligence process conducted by the investment staff and the Private Investment Fund ("PIF") consultant, Franklin Park Associates ("Franklin Park"), she had decided to commit up to \$75 million to Clearlake Capital Partners IV, L.P., a private investment opportunity which will primarily be focused on special situations, distressed and value investments. She noted that the commitment was contingent upon successful negotiation of the partnership documents.

Next, Treasurer Nappier discussed the agenda, and stated that an investment opportunity would be presented for the IAC's consideration; Crow Holdings Realty Partners VII, L.P, a value-add Real Estate Fund ("REF") opportunity. She added that the general partner is Crow Holdings Realty Advisors VII, headquartered in Dallas, Texas, and that she was considering an investment of up to \$100 million and that the fund would primarily focus on acquiring, renovating, redeveloping or repositioning a variety of core and non-core real estate properties across the country.

Finally, Treasurer Nappier introduced and welcomed Richard Gray, Deputy Treasurer to the Office of the State Treasurer ("OTT"). She then gave a brief overview of his professional background with the State of Connecticut and his tenure at the University of Connecticut where he served as the Vice President for Finance and Chief Financial Officer and Executive Vice President for Administration.

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Treasurer Nappier then acknowledged that former Deputy Treasurer Christine Shaw was now Chief Compliance Officer, having replaced Shelagh McClure upon her retirement. Lastly, Treasurer Nappier welcomed Linda Hershman, Chief of Staff, who had returned to the OTT on a part-time basis.

Update on the Market, the Connecticut Retirement Plans and Trust Funds (“CRPTF”) Final Performance for Months Ended June 30, 2015 and July 31, 2015

Deborah Spalding, Chief Investment Officer, 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 June 30, the TERF and SERF, the two largest pension plans, returned 2.79% and 2.84%, respectively, for Fiscal Year 2015. Focusing specifically on TERF, Ms. Spalding said that the performance was driven by total global equity returns of 2.23%, representing 53.06% of the portfolio; total fixed income returns of -2.03%, representing 20.37% of the portfolio; and a 10.79% return for alternative investments, representing 21.50% of the TERF. Ms. Spalding said the performance remained solid over the longer term, with the TERF and SERF returning 9.72% and 9.82%, respectively, over the five-year horizon. She then provided an update on the capital market environment, its impact on the performance of the CRPTF and the economic outlook. Next, she reported that as of July 31, the TERF and SERF returned 0.38% and 0.41%, respectively, for fiscal year to date 2015. Focusing specifically on TERF, Ms. Spalding said that the performance was driven by total global equity returns of 0.69%, representing 52.87% of the portfolio; total fixed income returns of -0.11%, representing 20.35% of the portfolio; and a 0.23% return for alternative investments, representing 21.08% of the TERF. Ms. Spalding said the performance remained solid over the longer term, with the TERF and SERF returning 8.87% and 8.95%, respectively, over the five-year horizon.

Next, Ms. Spalding commented on the Watch List and stated that Pacific Investment Management Company had concluded the leadership transition, has had strong performance and a stabilized organization, and that Treasurer Nappier had removed the firm from the Watch List. She continued that Grantham, Mayo, Van Otterloo & Co, which manages both a non-US developed market portfolio and an emerging market portfolio was added to the Watch List due to underperformance the last one, three, five and seven-year periods. Ms. Spalding stated that the Watch List addition would cover only the emerging market portfolio.

Lastly, she gave a brief overview on the Connecticut Horizon Fund (“CHF”), specifically the public markets and the performance of the four fund-to-fund managers, a \$1.07 billion program. She stated that as of quarter ended June 30, 2015, the CHF was down 14 basis points (“bps”); since inception the CHF had returned 6.94% versus the benchmark of 7.26%.

Claire Shaughnessy, Partner, and Diane Smola, Senior Consultant, of AonHewitt Investment Consulting (“AHIC”), reported on the Combined Investment Funds for the quarter ended June 30, 2015. Ms. Shaughnessy provided a market overview with comments on the public market global equities and fixed income markets. She commented on the economic highlights and said higher volatility and divergence to continue in the market was expected.

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Next, Ms. Smola provided a summary of the returns for the individual plans and trusts within the CRPTF. She reviewed the performance attribution as of June 30, 2015 for the TERF, the SERF and the Municipal Employees' Retirement Fund. She then provided a report on the CHF as of June 30, 2015 and said that the fiscal year to date returns were 3.3% for the quarter ended June 30, 2015. Ms. Smola stated that since inception the public market CHF returned 7.0% versus its benchmark return of 7.3%, an underperformance of 40 bps.

Thomas Fiore and Duke Himmelreich posed questions surrounding performance and benchmark, to which AHIC answered satisfactorily.

Presentation by and Consideration of Crow Holdings Realty Partners VII, L.P.

Ms. Spalding provided opening remarks and introduced Crow Holdings Realty Partners VII, L.P. ("Crow VII"), a REF investment opportunity. She introduced the REF consultant to the CRPTF, Robert Kochis, Principal of The Townsend Group. Ms. Spalding stated that Treasurer Nappier was considering an investment of up to \$100 million in Crow VII, a \$1.6 billion value-add real estate fund. She stated that the General Partner of the fund was Crow Holdings Realty Advisors VII, L.P., a Dallas, Texas-based institutional investment manager. Next, Ms. Spalding gave an overview of the investment merits of the Crow VII. She said the commitment to Crow VII would be an opportunity to meet the REF target allocation goals and enhance the REF portfolio returns.

Presentation by Crow Holdings Realty Partners VII, L.P.

Crow VII, represented by Robert McClain, Head of Investment Strategies, Cynthia Silverthorn, Portfolio Manager, and Dan Feeney, Head of Retail Investment Strategy, made a presentation to the IAC. Mr. McClain began by introducing Ms. Silverthorn and Mr. Feeney and gave a brief overview of the firm's track record, executive team, investment strategy and fund performance. He stated that Crow VII had experience through multiple market cycles and has made 310 real estate investments across seven funds that generated a weighted average Internal Rate of Return of 24%.

Ms. Silverthorn then gave an overview of Crow VII's strategy and stated that the firm had raised \$5.4 billion, of which the Crow family had committed over 15%. Mr. Feeney then discussed Crow VII's investment approach and Mr. McClain described the target allocation approach.

Lastly, Ms. Silverthorn spoke about the firm's diversification strategy. IAC members posed questions regarding union involvement and issues surrounding Fund IV, to which Mr. McClain answered satisfactorily.

Roll Call of Reactions to Crow Holdings Realty Partners VII, L.P.

Messrs. Fiore, Hall, Himmelreich, and Murray, Steven Muench, Peter Thor, Ms. Carpenter and Chair Thomas called provided feedback to Treasurer Nappier on Crow VII. All the IAC members supported an investment in Crow VII.

Chair Thomas called for a motion to waive the 45-day comment period. **A motion was made by Mr. Thor, seconded by Mr. Murray, to waive the 45-day comment period for Crow Holdings Realty Partners VII, L.P. There being no discussion, the Chair put the question to a vote and the motion was passed.**

Real Estate Fund Review as of March 31, 2015

Ms. Spalding reported on the performance of the REF for the quarter ended March 31, 2015, and the portfolio diversification versus investment guidelines and its NCREIF Property Index (“NPI”) benchmark. Ms. Spalding then reviewed the unfunded commitments, new commitments and new acquisitions for the Core Separate Account and fund vehicles within the REF. She reported that as of March 31, 2015, the REF returned 2.6% for the quarter, and 14.0%, 12.6% and 11.8% on a net basis over the past 1, 3 and 5-year horizons, respectively. She remarked that the REF had underperformed its NPI benchmark by 102 bps over the quarter and by 127 bps over the one-year horizon. Finally, Ms. Spalding discussed the trending improvement in the REF portfolio returns, which have outperformed its NPI benchmark 10 out of the last 12 quarters, which she attributed to the CRPTF’s steady pace of investment in accordance with policy allocation and the ongoing improvement across many real estate markets.

Mr. Kochis provided the IAC with an overview of the REF portfolio, along with a discussion of global economic outlook, broader real estate markets and commented on the 4th quarter growth by property type, and the impact on various sectors of the commercial real estate market. He then reviewed the portfolio vintage year diversification and stated that over the last 10 years the portfolio had a strong vintage year exposure.

Alternative Investment Fund Review as of June 30, 2015

Ms. Spalding reported on the Alternative Investment Fund (“AIF”) for the quarter ended June 30, 2015, assisted by Mark Johnson, Senior Managing Director of Cliffwater LLC. She gave an overview of the executive summary, portfolio overview, benchmark performance, portfolio investment activity and fund level performance.

Ms. Spalding reported that as of June 30, 2015, nearly 90% of the AIF committed capital was allocated to the fund-of-hedge fund portfolio. She stated that the diversified fund-of-hedge fund portfolio within the AIF had gained 2.6% for the quarter ended June 30, 2015. She noted that the result outperformed the HFRI Fund-of-Funds Composite Index return of 0.1%, and outperformed the broad HFRI Fund Weighted Composite Index return of 0.3%. Ms. Spalding added that the fund-of-hedge fund portfolio earned 4.5% for the twelve months ended June 30, 2015, slightly outperforming the HFRI Fund-of-Funds index return of 3.8% and the broad HFRI Fund Weighted Composite Index return of 2.4%. She commented that the AIF fund-of-hedge fund portfolio continued to be well-diversified across underlying managers and strategies.

Ms. Spalding next reported on the AIF exposure to real assets and opportunistic investments, and noted that the performance results were as of March 31, 2015. She stated that the real assets and opportunistic portfolios continued to perform well, with a combined net internal rate of return

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since inception of 8.1%. Ms. Spalding remarked that no capital was contributed to the partnerships in the third quarter.

Next, Mr. Johnson commented on the fund-of-hedge fund portfolio, real assets and opportunistic portfolio, and the AIF and CHF portfolios.

Private Investment Fund Review as of March 31, 2015

Ms. Spalding reported on the PIF for the quarter ended March 31, 2015. She introduced the PIF consultant, Bradley Atkins, Chief Executive Officer of Franklin Park, who assisted in presenting the quarterly report.

Ms. Spalding presented a portfolio overview as well as benchmark performance and portfolio investment activity. She said the PIF portfolio returned 13.3% for the twelve months ended March 31, 2015, versus a gain for the S&P 500 of 12.7% over the same period. She further commented on the portfolio's 3-year, 5-year and 10-year returns of 12.1%, 12.4% and 10.0%, respectively, versus the S&P 500's returns of 16.1%, 14.5% and 8.0% for those timeframes.

Mr. Atkins provided an overview of the private equity landscape, market update, and initial public offering activity. He also discussed the performance of the US buyout and venture capital portfolios by vintage year.

Next, Mr. Atkins reported on the CHF and stated that inception to date returns were 5.5% through March quarter, as the portfolio continued to emerge from the J-curve.

Treasurer Nappier acknowledged the ten years of service that Franklin Park provided to the CRPTF, and commended Franklin Park's entire team and Brad Atkins in particular, for its expertise and the strong customer service it continually provided as its benchmark for conducting business. She added that the firm was instrumental in assisting the CRPTF and the PIF after the Silvester scandal in the State Treasury. Finally, Treasurer Nappier extended best wishes to the staff of Franklin Park for what she said would be, without a doubt, a clearly successful future.

Short-Term Investment Fund Review as of June 30, 2015

Lawrence Wilson, Assistant Treasurer, reported on the performance of the Short Term Investment Fund ("STIF") for the quarter ending June 30, 2015. Mr. Wilson said the STIF earned an average annualized yield of 14 bps during the quarter, outperforming its benchmark by 10 bps, thereby earning an additional \$1 million for its state and local government investors. He stated that for the twelve month period ended June 30, 2015 the fund returned 15 bps, outperforming its benchmark by 12 bps, thereby earning an additional \$5.6 million. He noted that the fund's daily liquidity currently was 62% of assets; 63% 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; and that its reserves totaled \$50.5 million.

Securities Lending Review as of June 30, 2015

Amy Dunn, Director of Client Services, and Gustave Christakos, Assistant Vice President, of Deutsche Bank, reported on Securities Lending activity for the quarter ended June 30, 2015 and fiscal year 2015. Ms. Dunn provided an executive summary and reviewed the process by which Deutsche Bank generates income for the portfolio and securities lending activity for the CRPTF. She discussed the intrinsic value lending strategy and then reported second quarter securities lending returns of 11.03 bps, or \$5.1 million, net of fees, on the \$18.5 billion lendable portfolio. Ms. Dunn also noted that \$3.6 million of those earnings were derived from lending activity and \$1.5 million was earned from reinvestment of collateral; since inception, October 1, 2013, net of fees, earnings were \$24.4 million from securities lending and fiscal year ended June 30, 2015, net of fees, earnings were \$13.1 million. She stated that the highest demand was for international equities and that it resulted in \$2.6 million of total client earnings and that domestic equity was another strong contributor with earnings of \$1.6 million. She said that over 18% of the cash collateral was invested overnight, and the balance invested in maturities of up to three month with a weighted average maturity of 44 days. Ms. Dunn added that all cash collateral was invested in indemnified repurchase agreements collateralized by readily liquid and marketable securities at values of 102% or greater.

Next, Ms. Dunn discussed the market opportunities and reviewed earnings and performance highlights.

Other Business

Chair Thomas invited the IAC members to submit agenda items for the October 14, 2015 IAC meeting. She then reminded the IAC members that, due to a state holiday on Wednesday, November 11th, the IAC meeting would be held on Tuesday, November 10th.

Executive Session

A motion was made by Mr. Himmelreich, seconded by Mr. Hall that the Investment Advisory Council adjourn the Regular Session at 11:59 a.m. and enter into Executive Session to consider a personnel matter. The motion was passed unanimously. Richard Gray, Deputy Treasurer, participated in the Executive Session.

Regular Session

Chair Thomas reconvened the regular session at 12:34 p.m. She noted that no votes were taken during the executive session.

Consideration to Retain Consultant Gary Hudepohl & Associates

Treasurer Nappier presented her recommendation to retain Gary Hudepohl ("Hudepohl") to assist in acquiring a candidate for the Deputy CIO position and to extent Hudepohl's current contract. She asked that the IAC consider approving her recommendation.

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Chair Thomas asked for a motion to approve the recommendation to retain Hudepohl to assist in acquiring a candidate for the Deputy CIO position and to extend Hudepohl's current contract.

A motion was made by Mr. Thor, seconded by Mr. Himmelreich, to approve the retention of Gary Hudepohl to assist in acquiring a candidate for the Deputy Chief Investment Officer position and to extent Hudepohl's current contract. The motion was passed unanimously.

There being no further business, Chair Thomas called for a motion to adjourn the meeting. **Mr. Himmelreich moved to adjourn the meeting and the motion was seconded by Mr. Hall. There being no discussion, the meeting was adjourned at 12:37 p.m.**

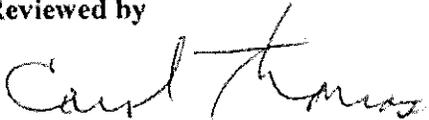
This meeting was electronically recorded.

Respectfully submitted,



**DENISE L. NAPPIER
SECRETARY**

Reviewed by



**CAROL THOMAS
INTERIM CHAIR**