INVESTMENT ADVISORY COUNCIL
Wednesday, June 9, 2010

MEETING NO. 377

Members present:	Thomas Fiore, representing Robert Genuario* Michael Freeman David (Duke) Himmelreich Stanley (Bud) Morten William Murray Denise L. Nappier, Treasurer Joseph (Joe) D. Roxe, Chairman Carol Thomas Peter Thor
Absent:	Thomas Barnes Sharon Palmer David Roth
Others present:	Howard G. Rifkin, Deputy Treasurer Linda Hershman, Assistant Deputy Treasurer/Chief of Staff M. Timothy (Tim) Corbett, Chief Investment Officer Lee Ann Palladino, Deputy Chief Investment Officer Wayne Hypolite, Executive Assistant Catherine LaMarr, General Counsel Shelagh McClure, Director of Compliance Meredith Miller, Assistant Treasurer-Policy Christine Shaw, Director of Government Relations Linda Tudan, Executive Assistant Winifred (Winnie) Scalora, Administrative Assistant
Interns:	Marcus Anderson, Office of the Treasurer Joshua Arons, Office of Policy and Management Caroline Banfield, Office of the Treasurer Jonathan Jenson, Office of the Treasurer
Guests:	Bradley Atkins, Franklin Park Associates, LLC Joseph Barcic, Mercer Investment Consulting Scott Booth, The Townsend Group Robert Calabrese, State Street Bank and Trust Narayan Chowdhury, Franklin Park Associates, LLC Sean Gill, NEPC Neil Hickey, Old Mutual Asset Management Robin Kaplan-Cho, Connecticut Education Association Harvey Kelly, Leumas Advisors Louis Laccavole, SOC Teachers' Retirement Board Kevin Norton, BNY Mellon

*** Arrived at 9:05 a.m.**

Carl O'Connell, BNY Mellon
Tony Pietro, The Townsend Group
Johnson Shum, State Street Bank and Trust
Scott Schwind, Rogerscasey

With a quorum present, Chairman Joseph Roxe called the Investment Advisory Council ("IAC") meeting to order at 9:00 a.m.

Approval of Minutes of the May 12, 2010 IAC Meeting

Chairman Roxe asked for comments on the Minutes of the May 12, 2010 IAC meeting. **There being no comments, a motion was made by Carol Thomas, seconded by David Himmelreich, that the Minutes of the May 12, 2010 IAC meeting be accepted as drafted. The motion was passed unanimously.**

Comments by the Treasurer

Treasurer Denise Nappier began her remarks by acknowledging the college interns. She then asked the Office of the Treasurer ("OTT") interns to introduce themselves to the IAC. Next, Treasurer Nappier commented about the OTT's progress on the search for legal counsel for the Alternative Investment Fund. Discussion ensued about whether the firms needed to present to the IAC. Treasurer Nappier stated that legal services are under the definition of investment services, and her recommendation to contract for such services, therefore, is subject to IAC for review and feedback. She said her recommendation would be on the IAC agenda at the August 11, 2010 meeting, but that finalists' presentations before the IAC are not required.

Regarding today's agenda, Treasurer Nappier stated that the quarterly presentations for the Private Investment and Real Estate Funds ("PIF" and "REF") would be a more in-depth discussion on strategy, performance, and the portfolio holdings of these two illiquid asset classes of the Connecticut Retirement Plans and Trust Funds ("CRPTF"). With respect to the performance of the CRPTF, she said that according to the Trust Universe Comparison Service ("TUCS"), the CRPTF performed in the 26th percentile for the two-year period ended March 31, 2010, or better than 74% of its peers that participated in this survey with assets of one billion dollars or more.

Chief Investment Officer's Update on the Market, CRPTF Final Performance for the Month Ended April 30, 2010, Combined Investment Funds Review as of March 31, 2010, Watch List Update and Connecticut Horizon Fund Review for the Quarter Ended March 31, 2010

M. Timothy Corbett, Chief Investment Officer ("CIO"), provided an update on the capital market environment. He stated that the financial markets appeared to be moving to a new stage and that correlations between asset classes were decreasing, valuations were no longer cheap, and sector selection within the portfolios was becoming more important. Mr. Corbett said that since April

30, 2010 the equity markets and the higher risk sectors of the fixed income markets were all down and there was a flight to quality in investment-grade bonds. He added that this downturn was due to the European sovereign debt crises, and he commented about different possible scenarios that could play out along with a weaker euro over the next two years. Mr. Corbett then remarked about the expected opportunities amongst these threats. He stated that the weaker euro would aid the core European French and German export economies, and there would be growth in global capital spending, particularly from emerging market economies. Mr. Corbett added that Europe has not had the credit strains that were seen in the US in 2008, but while there have been some concerns with the European banking system, the central banks were currently better armed to prevent a major liquidity crisis in the banking sector. He commented that the global economy was much healthier now than it was in 2008 with less leverage in the household and financial sectors. Finally, Mr. Corbett said that inflation was trending lower in developed markets, allowing the Federal Reserve to hold off on increasing rates and reducing liquidity.

Mr. Corbett reported that the performance for the CRPTF for the month ended April 30, 2010 was positive with a .83% return, bringing assets for the Combined Investment Fund ("CIF") to $23.6 billion. Fiscal year-to-date returns were up 20.4%, and annualized returns for the trailing seven-year period were up to 7.13%. He said that the strong fund performance was led by domestic and emerging equity markets and the fixed income funds. Mr. Corbett stated that the Inflation Linked Bond Fund matched its index with a return of 2.37% for the month. He also noted that only two of the eight public markets underperformed their benchmarks for the month ended April 30, 2010 and that only one had underperformed over the trailing three months. Finally, he commented about the performance of the Mutual Equity Fund and the active extension ("130/30") strategies. In response to Mr. Himmelreich, Mr. Corbett said that over the last two years there was an indiscriminate flight to quality followed by a flight to risk, but this cycle was currently stabilizing and the CRPTF's managers were generally beginning to outperform. Discussion ensued about market timing with respect to active versus passive managers, the active extension strategy and long versus short managers.

Mr. Corbett then presented the overall investment results for the CIF for the quarter ended March 31, 2010. He reported that all but one of the CRPTF's public market funds outperformed their benchmarks, but the PIF and REF did not meet their benchmarks for the first quarter of the 2010 calendar year. However, Mr. Corbett noted that there was a quarterly lag for reporting the PIF and REF and that the market valuations reported for these funds were actually based on the results as of December 31, 2009.

Joseph Barcic, Principal of Mercer Investment Consulting, Inc., said that the past three years were most difficult in terms of capital market returns and volatility in both public and private markets. He said that given the volatility in Europe, it was difficult to predict the CIF's returns for the near future and that this uncertainty would also affect domestic markets. Mr. Barcic stated that it was important to understand that the numbers reported for PIF and REF were still only estimates and that results could not be determined until assets were liquidated. In response to Peter Thor's questions, Mr. Barcic said that he did not expect inflation to be a near-term issue and that consumer confidence probably wouldn't improve in the near term due to the current unemployment rate and housing issues.

Chairman Roxe commented on the European economy and noted that the underlying economic issues could further deteriorate. In response to the Chairman's question regarding the global equity markets, Mr. Corbett said that it was important to focus on the long term, remain consistent with the CRPTF's investment strategy, and find ways to identify and potentially hedge these tail risk scenarios on a dynamic basis to mitigate downside losses. Chairman Roxe requested a discussion about the cost and appropriateness of hedging strategies at the next IAC meeting. Deputy Treasurer Howard Rifkin noted that these discussions have occurred at prior IAC meetings and added that it was important to not abandon the asset allocation approach while making tactical decisions. In response to Stanley Morten, Treasurer Nappier stated that the asset allocation and liability study would be launched during the 2011 calendar year.

Mr. Corbett provided an update on the CRPTF Watch List. He stated that AXA Rosenberg, which has two mandates, small-to-mid cap domestic equities and large cap core equities in an active extension strategy, was added to the Watch List due to a coding error in their risk model and portfolio optimization process. He added that compounding that issue, the error was not reported in a complete and timely manner by senior investment officers in accordance with the firm's policies. Regarding BlackRock Investment Management, LLC, Mr. Corbett stated that the fixed income mandate remained on the Watch List due to organizational and investment process changes, but added that BlackRock's performance had improved. He reported that Goodwin Capital Advisors, Inc. remained on watch due to an organizational change, but he said that its performance continued to be strong.

Finally, Mr. Corbett presented a report on the Connecticut Horizon Fund ("CHF") for the quarter ended March 31, 2010. With respect to the public markets, he reported an underperformance relative to the CHF's benchmark of 13 basis points ("bps") and 77 bps, respectively, for the quarter ended March 31, 2010 and the trailing year; but stated that the CHF outperformed its benchmark by 55 bps since inception. Regarding the four fund-of-fund managers, Mr. Corbett reported robust returns for the trailing year and that all had outperformed their benchmarks since inception. Mr. Corbett stated that there were no manager changes or graduations, and he provided details on the individual managers' performance for the quarter. Regarding the private equity portfolio within the CHF, he stated that only 22.5% of available capital had been committed to underlying sub-fund managers and 13% had been invested.

<u>Private Investment Fund Review as of December 31, 2009</u>

Lee Ann Palladino, Deputy CIO, reported on the PIF for the quarter ended December 31, 2009. Bradley Atkins, Chief Executive Officer, and Narayan Chowdhury, Managing Director, Franklin Park Associates, LLC, provided additional comments on the PIF. Ms. Palladino began by remarking about the objectives and goals of the PIF, and she stated that the guidelines and parameters of the Investment Policy Statement ("IPS") were used to structure the PIF portfolio to generate desired return streams. Ms. Palladino also noted that the presentation would respond to several comments made by the IAC regarding the performance attributions of the PIF and include some in-depth discussion on individual fund manager performance. She stated that as of December 31, 2009, $1.4 billion remained in unfunded capital and the PIF market value totaled $1.8 billion for a total exposure of $3.2 billion. Ms. Palladino reported that the fund earned a net internal rate of return ("IRR") of 7.7% since inception and stated that the PIF outperformed its private market benchmark, the S&P 500 public market equivalent ("PME"), by 500 bps in every time horizon and effectively met its policy objective. Chairman Roxe commented about the difference between pre- and post-1999 funds within the PIF with regard to performance attribution and stated it would add value to separately report performance for pre-1999 funds versus the more recent funds. Treasurer Nappier commented that this type of reporting may be useful occasionally and for narrow purposes, but added that such reporting was also one dimensional and might prove to be confusing because the performance of the CRPTF incorporates the returns of all funds and by vintage year. She emphasized that she has fiduciary responsibility for all fund assets and has, as necessary and appropriate, negotiated commitment reductions and amendments to limited partnership agreements to some of the legacy funds, and that these investment-related decisions could ultimately have influenced fund performance. Finally, Chairman Roxe stated that in terms of evaluating classes of investing relative to each other, a report that separated various time horizons would be helpful for both the PIF and REF.

Mr. Atkins commented on market trends, and more recent trends in limited partnership agreement negotiations including the level of fees. Mr. Chowdhury provided comments about performance measurement options, benchmarking limitations and return calculations. Ms. Palladino then contrasted the differences in calculations between the time-weighted returns and net IRR. Mr. Morten asked how State Street Bank computed the performance numbers that are reported on a monthly basis, to which Ms. Palladino stated that State Street Bank would provide this information. Mr. Atkins stated that the private equity asset class outperformed public equity over twenty, ten, five and three-year horizons and that its returns were net of fees, expenses and carried interest. He then provided highlights on various funds within the PIF.

Real Estate Fund Review as of December 31, 2009

Ms. Palladino provided a report on the REF for the quarter ended December 31, 2009. Scott Booth, Principal, and Tony Pietro, Associate, of The Townsend Group ("Townsend"), provided additional comments on the REF. Ms. Palladino first commented on the CRPTF's strategic intent for investing in real estate, which was to provide diversification to the portfolio, preserve capital, generate attractive risk-adjusted returns, provide current income and capital gains, and hedge against inflation. She then provided a portfolio overview noting that the REF underperformed its benchmark for the following reasons: 1) The National Council of Real Estate Investment Fiduciaries Property Index ("NCREIF") was unlevered and the CRPTF's REF was levered at 59%; 2) NCREIF solely includes core properties whereas the REF included core, value add and opportunistic; and 3) NCREIF reports on a gross basis, but the REF reports both gross and net. Ms. Palladino then commented about the investment performance by strategy for the REF and highlighted the performance of the older and newer funds.

Mr. Pietro provided an overview of the indices that were being utilized by the CRPTF to evaluate the REF's performance. Mr. Booth explained the differences between Real Estate Investment Trusts ("REITs") and core real estate investment funds. In response to Mr. Morten, Mr. Booth commented about the real estate investment correlations and the appraisal lag.

Mr. Booth then reported on the 2006 through 2009 Vintage Year REF investments. He then provided an overview of the real estate related investment universe from an asset allocation perspective. In conclusion, Mr. Booth commented about the distressed real estate opportunities. He said that lower risk-return debt strategies can be more correlated with fixed income, and it is this area that has markedly corrected. He added that the opportunity going forward is the higher risk-return debt oriented strategies targeting areas where greater dislocation and distress persist.

Short-Term Investment Fund Review as of March 31, 2010

Lawrence Wilson, Assistant Treasurer-Cash Management, reported on the performance of the Short-Term Investment Fund for the quarter ended March 31, 2010. Mr. Wilson reported that the STIF had an average annualized yield of 0.26%, 21 bps above its benchmark, resulting in an additional $2.6 million for state and local governments invested in the STIF. He stated that for the 12-month period, the STIF had a return of 44 bps, 28 bps over its benchmark, resulting in an additional $13 million for state and local governments. In response to Chairman Roxe, Mr. Wilson elaborated on the STIF's bank deposit strategy. Finally, Mr. Wilson reported that $13 million was earned above the benchmark during the last 12 months for the Connecticut Treasury, state agencies and local governments invested in the STIF.

Securities Lending Review as of April 30, 2010

Johnson Shum, Vice President of State Street Bank, provided a review of Securities Lending activity for the quarter ended March 31 and the month ended April 30, 2010. Mr. Shum began by providing an earnings and performance review noting that spreads have declined. In terms of loan balances, he reported that average lendables increased 8.6% and were up to $14 billion for the first 10 months of FY 2010, driven by the increase in lendables of non-U.S. equities. He reported earnings of $3.8 million for the quarter ended March 31, 2010. Finally, Mr. Shum stated that Connecticut's collateral investment fund continued to be conservatively managed with a focus on maintaining liquidity.

Other Business

Chairman Roxe invited IAC members to submit agenda items for the August 11, 2010 IAC meeting. Treasurer Nappier stated that her intentions to contract for legal advisory services would be presented at the August IAC meeting. Chairman Roxe stated there would also be a discussion on strategies for tail risk mitigation.

Comments by the Chairman

Chairman Roxe commented on today's meeting.

There being no further business, the meeting was adjourned at 12:30 p.m.

An audio tape of this meeting was recorded.

Respectfully submitted,

DENISE L. NAPPIER
SECRETARY

Reviewed by

JOSEPH D. ROXE
CHAIRMAN