BWC Board of Directors

Investment Committee

Thurs., Jan. 24, 2008, 2:00 P.M.

William Green Building
The Neil Schultz Conference Center
30 West Spring Street, 2nd Floor (Mezzanine)
Columbus, Ohio 43215

Members Present: Robert Smith, Chair
Alison Falls, Vice Chair
David Caldwell
James Harris
Larry Price
William Lhota, ex officio member

Other Board Members Present:

James Hummel
Jim Matesich
Philip Fulton
Kenneth Haffey

Call to Order

Mr. Smith called the meeting to order at 2:00 PM and the roll call was taken.

Minutes of Dec. 19, 2007

Alison Falls suggested several changes. On page one, after the first sentence, the presentation made should be incorporated as part of the minutes covering the major areas of the comprehensive slide presentation. The next two sentences should be deleted. On page two, the second paragraph, there was substantial discussion with regard to the risks involved in securities lending. On page three, at the bottom, Ms. Falls indicated that the benchmark change was favored, in large part, due to increased diversification, increased opportunity for higher returns, and decreased risk profile. Mr. Caldwell and Mr. Harris noted the minutes should reflect that their votes with regard to the new benchmark index reflect their desire to invest in America. Mr. Lhota noted that minutes for the Investment Committee should note that he is an ex officio member and that all Committee minutes should list attendance of non Committee member directors. The minutes for December shall be reconsidered for approval next month.

Charter Review

Don Berno, Board Liaison, noted that the Investment Committee Charter indicates that the Committee Chair and Vice Chair are designated by the Board. The Charter further reflects that the ex officio member Board Chair shall not vote if the Chair’s vote will create a tie vote. Upon motion by Mr. Price, seconded by Mr. Harris, the Charter was approved unanimously by all Committee members.

New Business/Action Items

Investment Policy Statement Review

Bruce Dunn, Chief Investment Officer, discussed his memorandum dated January 14, 2008 proposing and recommending changes to the Investment Policy Statement and incorporated into the minutes, by reference, in detail. Mr. Dunn mentioned that the Investment Committee approved in November and December 2007 both a Request for Quote for two ancillary trust funds and a Request for Proposal for the three largest trust funds of the Bureau involving the selection of passive index investment managers. These approvals were provided for the purpose of transitioning from a separate account structure to a commingled account structure for the management of passive indexed investment assets. Mr. Dunn indicated that the recommendations provided in this memorandum are made to eliminate inconsistencies reflected in the IPS between the composition of the BWC fixed income benchmarks and the ownership of foreign-related issues. Mr. Dunn indicated such inconsistencies need to be addressed before the approved RFQ and RFP documents can be issued by the Bureau.

There was discussion of the specifics of the proposed Investment Policy Statement changes of Section IV.C.ii as reflected in the memorandum. Mr. Dunn stated the recommended increase in the limits of foreign government-related debt to 5% from 0% and of Yankee debt to 15% from 10% for the Bureau’s fixed income portfolios in the aggregate would permit outside investment managers to manage effectively to the appropriate fixed income benchmarks in place for the Bureau. Mark Brubaker and Mike Patalsky of Wilshire Consulting indicated their support for such changes to enable outside investment managers sufficient latitude to meet their performance objectives.

Discussion on this issue ensued between the committee members. Ms. Falls raised the issue as to whether or not sector allocation restrictions reflected in this Section IV.C.ii was for active management or passive management of funds. Mr. Dunn responded that sector allocation was applicable for both active and passive management. Mr. Dunn pointed out that the recent changes made to Section IV.C.ii of the IPS with respect to individual Credit Name ownership restrictions are applicable for only actively managed fixed income mandates and are not applicable for passively managed indexed fixed income mandates. Mr. Dunn further explained that for active management, managers could deviate significantly from benchmark sector weights as long as the fixed income portfolios of BWC, in the aggregate, comply with these diversification guideline limits set forth in this Section IV.C.ii. Mr. Smith indicated BWC should stay consistent with benchmark policies for passive managers. Ms. Falls made the observation that for active fixed income managers to beat their benchmark index, such managers have portfolio management strategies that may differ significantly from the composition of a benchmark index. There remains an issue as to what guidelines apply for active managers. .

Mr. Price questioned what the implications were of the phrase “in the aggregate” being added to Section IV.C.ii of the IPS. Mr. Dunn responded that it meant that a specific trust fund portfolio could deviate from the diversification guidelines as long as, in the aggregate when all BWC trust funds are grouped together, the combined trust funds meet these guidelines.

Ms. Falls raised the issue as to what impact will there be on the current IPS when changes occur in the benchmark indices. Mr. Dunn indicated that the Investment Committee will be alerted if the trend of such changes in a benchmark index may require the diversification requirements of the IPS to be readdressed. Ms. Falls also requested that in the future when the Bureau's investment practices are modified, all corresponding parts of the IPS be modified at the same time.

A motion was made by Ms. Falls, and seconded by Mr. Price, as follows: that the Investment Committee of the Workers' Compensation Board of Directors recommend to the Board that it amend section IV.C.ii of the Investment Policy Statement regarding foreign bond ownership limits, in order to correct certain inconsistencies arising from prior changes to the Investment Policy Statement, for reasons outline in the memorandum of the Bureau's Chief Investment Officer dated January 14, 2008. The exact changes adopted by this motion will be incorporated by reference into the minutes of this meeting of the Investment Committee. A roll call vote was taken, and the motion passed 6-0.

Appendices

Mr. Smith stated that the appendices of the IPS are too restrictive, in that they are outdated and in some cases unnecessary. A discussion ensued regarding whether the level of specificity in the appendices of the IPS was necessary. A motion was made by Mr. Smith, seconded by Ms. Falls, as follows: that the Investment Committee of the Workers' Compensation Board of Directors recommend to the Board that appendices 9, 11A, 11B, 12, 13, 14 as well as previously suspended appendix 15 be deleted. A roll call vote was taken, and the motion passed 6-0.

Discussion Items

Calendar of Events

Mr. Dunn highlighted certain future topics on the Calendar of Events, specifically investment risk tolerance, derivatives use and the selection of minority managers.

CIO Report – January 2008

Mr. Dunn discussed his monthly CIO memorandum dated January 11, 2008. The memorandum is incorporated by reference into the minutes. The memorandum discusses six strategic goals for fiscal year 2008. Included in such goals are the hiring of additional members of the investment team with the objective of attaining a full team of 11 staff members, including two support staff. With respect to the private equity sale, there are eight remaining funds to be sold.

Asset Allocation

Mr. Dunn provided a handout that provided the asset allocation ranges and targets between bonds, equity and cash at market value applicable for each of the State Insurance Fund, Disabled Workers Fund and Coal Workers Fund portfolios. The combination of the strong performance of the fixed income markets and the negative return of the S&P 500 index in recent months has resulted in the Total Fixed Income allocation currently being higher than its targeted allocation range and the Total

Equity allocation currently being right at the low end of its targeted allocation range for both the SIF and Coal Workers Fund portfolios. In addition, Mr. Dunn indicated that the cash balances for SIF are at its projected low point for the year. Mr. Dunn pointed out that the asset allocation Rebalancing Policy of the Bureau indicates that should actual asset allocations deviate from the indicated range, the Administrator and CIO will make the necessary adjustments, factoring in projected future cash flows. Mr. Smith commented that the advance in Treasury prices and decline in equity prices since October reflect the types of market changes that should trigger a rebalance of equities and fixed income. Mr. Smith inquired as to whether U.S. treasuries were overvalued. Mr. Dunn indicated yes. Mark Brubaker of Wilshire Consulting, stated that asset allocation rebalancing should be ministerial. Marsha Ryan, Bureau Administrator, inquired as to whether there were any cash flow trends that the Bureau needed to be concerned about. Mr. Dunn replied that cash flow trends have been predictable for the past few years. Mr. Dunn indicated the Bureau's Fiscal and Planning Division projects an increase in cash balances of approximately $400 million by the end of February 2008. Ms. Falls raised the issue as to why cash was not being used for rebalancing. Mr. Dunn stated that it is not expected that these increases in cash flow balances will be applied towards bond or stock investments. In fact, Mr. Dunn indicated the increase in cash balances will cause the equity asset allocation to decline further. Mr. Harris inquired as to whether a rate decrease and economic stimulus package will stabilize the economy. Mr. Brubaker stated that a clearly defined rebalancing policy reflects upon investment best practices in that it eliminates the attempt to forecast future market movements. Mr. Smith asked that the BWC's Rebalancing Policy be reviewed and revised if necessary to make it a clearly defined policy. Mr. Smith noted that criticisms of the Bureau have been made in the past for not taking advantage of the equity markets. Despite these criticisms, the Bureau is now benefiting from its investments in fixed income. Mr. Dunn indicated it is likely that the Bureau may execute an asset allocation rebalancing strategy after further discussion with its external portfolio managers.

Adjournment

Motion was made by Mr. Price and seconded by Mr. Harris, to adjourn the meeting at 3:06 PM.

Prepared by Tom Woodruff, BWC Staff Counsel