BWC Board of Directors

Investment Committee Agenda

William Green Building
Thursday, September 23, 2010
Level 2, Room 2
9:30 a.m. – 11:30 a.m.

Call to Order
Bob Smith, Committee Chair

Roll Call
Linda Byron, Scribe

Approve Minutes of the August 26, 2010 Meeting
Bob Smith, Committee Chair

Review and Approve Agenda*
Bob Smith, Committee Chair

Discussion Items

1. Monthly and Fiscal Year to Date Portfolio Value Comparisons
   - August 2010/July 2010
   - August 2010/June 2010

   Bruce Dunn, Chief Investment Officer

2. Month-End Portfolio Asset Allocation Values
   - August 2010/July 2010

   Bruce Dunn, Chief Investment Officer

3. CIO Report – August 2010

   Bruce Dunn, Chief Investment Officer

4. CIO Recommendations
   New Investment Strategy Considerations
   State Insurance Fund

   Bruce Dunn, Chief Investment Officer

5. MWBE Investment Policy Recommendation, first reading

   Bob Smith, Committee Chair
   Mercer Team
   Bruce Dunn, Chief Investment Officer

6. Mercer Presentation on Real Estate as an Asset Class, second discussion
    - Peer Investor Activity

        Bob Smith, Committee Chair
        Mercer Team

7. Committee Calendar

        Bob Smith, Committee Chair
        Bruce Dunn, Chief Investment Officer

Adjourn

Bob Smith, Committee Chair

<u>Next Meeting: Thursday, October 21, 2010</u>

* Not all agenda items may have materials
** Agenda subject to change

Ohio Bureau of Workers' Compensation
Invested Assets Market Value Comparison
TOTAL FUNDS

Asset Sector	Market Value August 31, 2010	% Assets	Market Value July 31, 2010	% Assets	Increase(Decrease) Prior Month-End	% Change	Market Value June 30, 2010	% Assets	Increase(Decrease) Prior Fiscal Year-End	% Change
Bonds	14,021,595,598	70.0%	13,699,457,182	70.1%	322,138,416	2.4%	13,537,054,766	71.2%	484,540,832	3.6%
Equity	5,424,400,862	27.1%	5,538,792,286	28.3%	(114,391,424)	-2.1%	5,154,562,423	27.1%	269,838,439	5.2%
Net Cash - OIM	54,220,350	0.3%	68,556,694	0.4%	(14,336,344)	-20.9%	64,622,125	0.3%	(10,401,775)	-16.1%
Net Cash - Operating	474,510,606	2.4%	188,221,036	1.0%	286,289,570	152.1%	217,413,398	1.2%	257,097,208	118.3%
Net Cash - SIEGF	44,811,060	0.2%	44,740,803	0.2%	70,257	0.2%	47,335,733	0.2%	(2,524,673)	-5.3%
Total Net Cash	573,542,016	2.9%	301,518,533	1.6%	272,023,483	90.2%	329,371,256	1.7%	244,170,760	74.1%
Total Invested Assets	$20,019,538,476	100%	$19,539,768,001	100%	$479,770,475	2.5%	$19,020,988,445	100%	$998,550,031	5.2%

OIM: Outside Investment Managers
SIEGF: Self-Insured Employers' Guaranty Fund

Market Value of Bonds and Stocks includes accrued investment income.

Net Cash includes the impact of net trade receivables/payables, accrued money market earnings, and accrued investment manager fees.

August 2010/July 2010 Comparisons

- Net investment income in August 2010 was $199 million representing a monthly net portfolio return of +1.0% (unaudited).
- Bond market value increase of $322.1 mm comprised of $45.0 mm in interest income and $391.0 mm in OIM realized/unrealized gains ($95.3 mm net realized gain), offset by $108.4 mm in OIM/TM net bond sales and by $5.5 mm in operations redemptions, representing a monthly net return of +3.1% (unaudited).
- Equity market value decrease of $(114.4) mm comprised of $8.1 mm of dividend income and $(244.6) mm in net realized/unrealized losses ($26.9 mm net realized gain), offset by $122.1 mm in OIM/TM net equity purchases, representing a monthly net return of -3.7% (unaudited).
- Net cash balances increased $272.0 mm in August 2010 largely due to increased operating cash balances of $286.3 mm, offset by $14.3 mm in OIM/TM net purchases. JPMorgan US Govt. money market fund had 30-day average yield of 0.11% for August 2010 (0.10% for July10) and 7-day average yield of 0.11% on 8/31/10 (0.11% on 7/31/10).

August 2010/June 2010 FYTD Results

- Net investment income for FYTD2011 was $755 million largely comprised of $111 mm of interest/dividend income and $646 mm of net realized/unrealized gains ($130 mm net realized gain), offset by $1 mm in fees, representing a FYTD2011 net portfolio return of +3.9% (unaudited).
- Bond market value increase of $485 mm for FYTD2011 comprised of $97 mm in interest income and $505 mm of net realized/unrealized gains ($107 mm net realized gain), offset by $111 mm in OIM/TM net bond sales and by $6 mm in operations redemptions, representing a FYTD2011 net return of +4.3% (unaudited).
- Equity market value increase of $270 mm for FYTD2011 comprised of $14 mm in dividend income, $141 mm in net realized/unrealized gains ($22 mm net realized gain) and $121 mm in OIM/TM net equity purchases, offset by $6mm in miscellaneous asset redemptions, representing a FYTD2011 net return of +3.6% (unaudited).

Ohio Bureau of Workers' Compensation
Investment Asset Allocation - Combining Schedule

As of August 31, 2010

(in thousands)

	SIF	% Trust	DWRF	% Trust	BLF	% Trust	PWRF	% Trust	MIF	% Trust	SIEGF	% Trust	ACF	% Trust	Totals	% of Total
Bonds	**$ 12,859,867**	**69.9%**	**$ 897,874**	**71.1%**	**$ 219,410**	**80.7%**	**$ 25,438**	**98.7%**	**$ 19,006**	**97.8%**	**$ -**	**0.0%**	**$ -**	**0.0%**	**$ 14,021,595**	**70.0%**
Long Credit	5,699,272	31.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	5,699,272	28.5%
Long Government	1,499,539	8.2%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	1,499,539	7.6%
Long Gov/Credit	-	0.0%	-	0.0%	3	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	3	0.0%
TIPS	3,103,042	16.9%	459,095	36.3%	110,350	40.6%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	3,672,487	18.3%
Aggregate	2,558,014	13.9%	438,779	34.7%	109,057	40.1%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	3,105,850	15.5%
Intermediate Gov/Credit	-	0.0%	-	0.0%	-	0.0%	25,438	98.7%	19,006	97.8%	-	0.0%	-	0.0%	44,444	0.2%
Stocks	**5,010,521**	**27.2%**	**362,407**	**28.5%**	**51,473**	**18.9%**	**-**	**0.0%**	**-**	**0.0%**	**-**	**0.0%**	**-**	**0.0%**	**5,424,401**	**27.1%**
Russell 3000	3,401,817	18.5%	239,435	18.9%	32,858	12.1%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	3,674,110	18.3%
MSCI ACWI ex-U.S.	1,599,651	8.7%	122,665	9.7%	18,572	6.8%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	1,740,888	8.8%
S&P 500	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%
Dividends Receivable	9,018	0.0%	307	0.0%	43	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	9,368	0.0%
Miscellaneous	35	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	35	0.0%
Net Cash & Cash Equivalents	**517,091**	**2.8%**	**5,059**	**0.4%**	**1,167**	**0.4%**	**342**	**1.3%**	**418**	**2.2%**	**44,811**	**100.0%**	**4,654**	**100.0%**	**573,542**	**2.9%**
Total Cash & Investments	**$ 18,387,479**	**100.0%**	**$ 1,265,340**	**100.0%**	**$ 272,050**	**100.0%**	**$ 25,780**	**100.0%**	**$ 19,424**	**100.0%**	**$ 44,811**	**100.0%**	**$ 4,654**	**100.0%**	**$ 20,019,538**	**100.0%**

Market value of bonds includes accrued investment income.
Net cash and cash equivalents includes the impact of net trade receivables/payables, accrued money market earnings, and accrued investment manager fees.

State Insurance Fund (SIF)

Overall SIF allocation to 70% bonds/30% stocks from 80% bonds/20% stocks was completed in December, 2009 (new asset allocation transitions began in July, 2009). Transitions included the Russell 3000, Barclays US Aggregate, the Long Credit/Government split and four tranches of the international equity mandate which completes the overall new asset allocation for SIF by asset class. Final placement transitions to approved target investment managers were completed in Second Quarter, 2010.

All equity indices returns decreased for the Russell 3000 (-4.71%), S&P 500 (-4.51%) as well as the MSCI ACWI ex-U.S. (-2.75%) in the month of August. As a result the equity allocation decreased to 27.2% for the month from 29.2% for the prior month-end. Additionally, all bond indices returns increased for the Barclays Capital Government Long Term Index (+6.63%), Barclays Capital Long Credit Index (+4.04%), U.S. TIPS Index (+1.72%) as well as the U.S. Aggregate Bond Index (+1.29%) in August. The SIF poor equity performance was offset by a positive bond indices resulting in the overall bond asset allocation increasing from 69.5% at the end of July to 69.9% at end of August.

Cash allocations increased from 1.3% at end of July to 2.8% at end of August largely due to seasonally increased SIF operating cash of $288.6 million offset by $1million in decreased net SIF investment manager cash balances.

Disabled Workers' Relief and Coal Workers' Pneumoconiosis Funds (DWRF and BLF)

BWC Board of Directors' Investment Committee approved the Coal Workers' Pneumoconiosis Fund new asset allocation at the December, 2009 meeting and the Disabled Workers' Relief Fund new asset allocation at the January, 2010 meeting (see Fund Asset Allocation chart insert.) Transitions were completed in August through early September, 2010 for the the Barclays U.S. Aggregate, U.S. TIPS, Russell 3000 and the MSCI ACWI ex U.S. asset classes and final placement of funds to approved target investment managers.

PWRF, MIF, SIEGF

BWC Board of Directors' Investment Committee approved/confirmed the PWRF Fund new asset allocation and the MIF Fund new asset allocation at the March, 2010 meeting. The SIEGF analysis is anticipated for early 2011.

Fund Asset Allocation:

	Equity	Bonds	Cash	Total
SIF	30%	69%	1%	100%
DWRF	30%	69%	1%	100%
BLF	20%	79%	1%	100%
PWRF		99%	1%	100%
MIF		99%	1%	100%
SIEGF			100%	100%
ACF		Not Applicable		

SIF: State Insurance Fund	DWRF: Disabled Workers' Relief Fund	PWRF: Public Work-Relief Employees' Fund	SIEGF: Self Insured Employers Guarantee Fund
	BLF: Coal Workers' Pneumoconiosis Fund	MIF: Marine Industry Fund	ACF: Administrative Cost Fund

9/16/2010

Ohio Bureau of Workers' Compensation
Investment Asset Allocation - Combining Schedule

As of July 31, 2010

(in thousands)

	SIF	% Trust	DWRF	% Trust	BLF	% Trust	PWRF	% Trust	MIF	% Trust	SIEGF	% Trust	ACF	% Trust	Totals	% of Total
Bonds	**$ 12,440,879**	**69.5%**	**$ 1,000,414**	**78.6%**	**$ 214,229**	**78.7%**	**$ 25,147**	**98.6%**	**$ 18,788**	**98.2%**	**$ -**	**0.0%**	**$ -**	**0.0%**	**$ 13,699,457**	**70.1%**
Long Credit	5,459,344	30.5%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	5,459,344	27.9%
Long Government	1,407,755	7.9%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	1,407,755	7.3%
Long Gov/Credit	-	0.0%	738,240	58.0%	159,416	58.6%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	897,656	4.6%
TIPS	3,046,708	17.0%	262,174	20.6%	54,813	20.1%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	3,363,695	17.2%
Aggregate	2,527,072	14.1%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	2,527,072	12.9%
Intermediate Gov/Credit	-	0.0%	-	0.0%	-	0.0%	25,147	98.6%	18,788	98.2%	-	0.0%	-	0.0%	43,935	0.2%
Stocks	**5,221,802**	**29.2%**	**261,497**	**20.4%**	**55,493**	**20.4%**	**-**	**0.0%**	**-**	**0.0%**	**-**	**0.0%**	**-**	**0.0%**	**5,538,792**	**28.3%**
Russell 3000	3,571,461	20.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	3,571,461	18.2%
MSCI ACWI ex-U.S.	1,644,992	9.2%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	1,644,992	8.5%
S&P 500	-	0.0%	261,022	20.4%	55,392	20.4%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	316,414	1.6%
Dividends Receivable	5,314	0.0%	475	0.0%	101	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	5,890	0.0%
Miscellaneous	35	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	35	0.0%
Net Cash & Cash Equivalents	**236,758**	**1.3%**	**13,024**	**1.0%**	**2,383**	**0.9%**	**351**	**1.4%**	**335**	**1.8%**	**44,741**	**100.0%**	**3,927**	**100.0%**	**301,519**	**1.6%**
Total Cash & Investments	**$ 17,899,439**	**100.0%**	**$ 1,274,935**	**100.0%**	**$ 272,105**	**100.0%**	**$ 25,498**	**100.0%**	**$ 19,123**	**100.0%**	**$ 44,741**	**100.0%**	**$ 3,927**	**100.0%**	**$ 19,539,768**	**100.0%**

Market value of bonds includes accrued investment income.
Net cash and cash equivalents includes the impact of net trade receivables/payables, accrued money market earnings, and accrued investment manager fees.

State Insurance Fund (SIF)

Overall SIF allocation to 70% bonds/30% stocks from 80% bonds/20% stocks was completed in December, 2009 (new asset allocation transitions began in July, 2009). Transitions included the Russell 3000, Barclays US Aggregate, the Long Credit/Government split and four tranches of the international equity mandate which completes the overall new asset allocation for SIF by asset class. Final placement transitions to approved target investment managers were completed in Second Quarter, 2010.

All equity indices returns notably increased for the MSCI ACWI ex-U.S. (+9.03%), S&P 500 (+7.01%) as well as the Russell 3000 (+6.94%) in the month of July. As a result the equity allocation increased to 29.2% for the month from 27.9% for the prior month-end. Additionally, all bond indices returns increased for the Barclays Capital Long Credit Index (+2.27%), U.S. Aggregate Bond Index (+1.07%), Barclays Capital Government Long Term Index (+0.21%), as well as the U.S. TIPS Index (+0.14%) in July. The SIF strong equity performance overshadowed the positive bond indices resulting in the overall bond asset allocation decreasing from 70.6% at end of June to 69.5% at end of July.

Cash allocations slightly decreased from 1.5% at end of June to 1.3% at end of July largely due to decreased SIF operating cash of $35.3 million slightly offset by a miscellaneous asset redemption of $6.3 million (increase in cash balances) and $3.9 million increased investment manager cash balances.

Disabled Workers' Relief and Coal Workers' Pneumoconiosis Funds (DWRF and BLF)

BWC Board of Directors' Investment Committee approved the Coal Workers' Pneumoconiosis Fund new asset allocation at the December, 2009 meeting and the Disabled Workers' Relief Fund new asset allocation at the January, 2010 meeting (see Fund Asset Allocation chart below.) Transitions include the Barclays U.S. Aggregate, U.S. TIPS, Russell 3000 and the MSCI ACWI ex U.S. Final placement of funds to approved target investment managers are anticipated to be completed in late Summer, 2010.

PWRF, MIF, SIEGF

BWC Board of Directors' Investment Committee approved/confirmed the PWRF Fund new asset allocation and the MIF Fund new asset allocation at the March, 2010 meeting. The SIEGF analysis is anticipated for late 2010/early 2011.

Fund Asset Allocation:

	Equity	Bonds	Cash	Total
SIF	30%	69%	1%	100%
DWRF	30%	69%	1%	100%
BLF	20%	79%	1%	100%
PWRF		99%	1%	100%
MIF		99%	1%	100%
SIEGF			100%	100%
ACF		Not Applicable		

SIF: State Insurance Fund
DWRF: Disabled Workers' Relief Fund
BLF: Coal Workers' Pneumoconiosis Fund
PWRF: Public Work-Relief Employees' Fund
MIF: Marine Industry Fund
SIEGF: Self Insured Employers Guarantee Fund
ACF: Administrative Cost Fund

8/18/2010

INVESTMENT DIVISION

TO:	Marsha Ryan, Administrator BWC Investment Committee BWC Board of Directors
FROM:	Bruce Dunn, CFA, Chief Investment Officer
DATE:	September 17, 2010
SUBJECT:	CIO Report August, 2010

Fiscal Year 2011 Goals

The Investment Division has three major goals for the new fiscal year 2011. These goals and brief comments on action plans for each goal follow:

1. Provide support and execute new BWC Investment Policy resulting from investment consultant Asset-Liability studies and from Board actions impacting/revising the BWC Investment Policy.

2. Explore for investment consideration and subsequently initiate implementation processes pertaining to appropriate identified subject matters.

3. Continued establishment and execution of appropriate internal investment controls and compliance procedures.

Strategic Goal One – PORTFOLIO TRANSITION

The Investment Division executed a comprehensive portfolio transition strategy in multiple stages throughout fiscal year 2010 for the State Insurance Fund that was completed at the end of May, 2010. This completed transition activity evolved from an asset-liability study of BWC investment consultant Mercer in which a new asset allocation strategy was approved by the BWC Investment Committee and Board of Directors at their respective March, 2009 meetings. Such new approved investment strategy target asset allocations for the State Insurance Fund were subsequently reflected in a new Investment Policy Statement approved by the BWC Investment Committee and Board of Directors at their respective April, 2009 meetings.

Mercer also completed and presented for consideration a strategic asset allocation analysis on the Disabled Workers Fund and the Coal Workers Fund at the December, 2009 and January, 2010 Investment Committee meetings. The Investment Committee and Board of Directors approved the new targeted asset allocation recommendations of Mercer and the CIO for each of these specialty funds at these respective meetings. The BWC Investment Policy Statement reflecting the new portfolio asset allocation targets for these two specialty funds were reviewed and revised by the Board of Directors at these respective meetings.

A transition manager was selected by the Investment Division in the fourth quarter of FY2010 to implement and execute the necessary asset class mandate shifts approved by the Board for both of these specialty funds. All necessary legal contracting with both the transition manager and each of the target commingled fund investment managers approved by the Board was completed in July, 2010. The final transition strategy was also approved by the BWC CIO in July, 2010. The transition of these specialty fund assets was then implemented and largely completed in August, 2010. Details on the transition activity of each of these specialty fund assets are provided in the Transition Activity Summary section later in this CIO Report.

The Investment Division is committed to support and implement any revisions to the BWC Investment Policy Statement that may include additional identified asset classes or investment management style changes that are considered under Strategic Goal Two which follows. As always, the CIO will report on Investment Policy compliance to the Investment Committee and Board via this monthly CIO report with any exceptions noted and addressed.

Strategic Goal Two – NEW INVESTMENT CONSIDERATIONS

Over the latter half of fiscal year 2010, the Investment Division began to explore with Mercer the potential employment of active management of each bond and stock asset class targeted as mandates of the State Insurance Fund. Mercer provided two education sessions on active versus passive investment management with the Investment Committee in March and April, 2010. The CIO provided specific recommendations at the May, 2010 Investment Committee meeting regarding current State Insurance Fund fixed income and equity classes to be considered for active management.

The consideration of Minority-or-Women-Owned (MWBE) investment managers to manage a portion of BWC assets is currently being addressed by the Investment Committee. Mercer provided two education sessions on MWBE manager utilization by institutional investors in Investment Committee meetings in June and July, 2010. A proposal for consideration on MWBE asset management next steps for the Bureau was made by Mercer and the CIO at the August, 2010 Investment Committee meeting. A proposed investment policy addressing MWBE investment managers that would amend Section VIII of the Investment Policy Statement is being offered for consideration by Mercer and the CIO at the September, 2010 Investment Committee meeting. Any engagement of asset management of targeted BWC funds by MWBE managers would likely result in active management of such funds.

A first presentation on real estate as an asset class was made by Mercer to the Investment Committee at the August, 2010 meeting. A second presentation on peer investor investments in real estate assets will be made by Mercer at the September, 2010 Investment Committee meeting.

Mercer also provided to the Investment Committee at its August, 2010 meeting an updated investment policy decisions chart related to potential investment strategy revisions for consideration by the Investment Committee. Some of these topics are outlined above. At the request of the Chair and Vice Chair of the Investment Committee, the CIO will present his investment strategy recommendations for the State Insurance Fund, including strategy priorities and estimated implementation timelines to completion, at the September, 2010 meeting. A written memo dated September 14, 2010 addressing these CIO recommendations has been distributed to the Board.

For any new investment consideration approved by the Investment Committee and Board in fiscal year 2011, the Investment Division will planfully coordinate and implement all action steps necessary to achieve such objectives. Any new objectives involving the selection of new investment managers will typically require the crafting and issuance of a RFP by the Investment Division working with the assistance of the Legal and Fiscal and Planning Divisions.

The BWC Fiscal and Planning Division currently manages all cash balances of each of these portfolios, including operating cash, with virtually all cash being invested in a single U.S. government money market fund managed by JP Morgan that is utilized as an overnight cash sweep vehicle. The Investment Division is exploring expanding the use of other higher yielding money market funds available as well as direct investments in short-term money market investments (commercial paper, certificates of deposit, repurchase agreements, etc.) in order to improve investment income and returns on its cash investments while maintaining desired liquidity. In addition, the Investment Division is in the early stages of exploring the increasingly common institutional investor practice of utilizing contracted cash management overlay services to more effectively control/reduce cash balances exceeding projected nearer term operational cash needs. This excess cash can instead be directed to existing BWC outside managers to earn projected higher returns and reduce market value variances to portfolio allocation targets. The CIO will provide a report detailing cash management recommendations to the Investment Committee and Board when appropriate after further research.

In the Deloitte Comprehensive Study Report provided to the Board in December, 2008 and presented at the Actuarial Committee meeting, Deloitte recommended BWC explore the consolidation of each of the Disabled Workers Fund, Coal Workers Fund and Marine Industry Fund into the State Insurance Fund for efficiencies, cost savings and added financial strength under a combined fund. Further research to combine such specialty funds into SIF will be performed internally by appropriate BWC Divisions, including the Investment Division. It is fully recognized that any combining of specialty trust funds will take Bureau initiative and will require legislative change.

Strategic Goal Three – INTERNAL INVESTMENT PROCEDURES

The Investment Division will continue to maintain as well as establish and improve internal investment policies and procedures that are written and documented. Among the procedures addressed as well as revised/updated in fiscal year 2010 were policies and procedures regarding the selection of transition managers, as well as revising/updating policies and procedures on investment manager background checks/fingerprinting, asset class rebalancing, RFP/RFQ/RFI processes, vendor invoice payments and passive investment management review.

Among the policies and procedures that will be addressed in fiscal year 2011 will be administrative areas such as Investment Division internal budgeting, travel, electronic storage of investment documents/records and document file retention schedules of RIM documents. Internal processes will also be developed for the monitoring of active style investment managers in advance of the future selection and engagement of any such active managers resulting from any new active management investment strategy approved by the Board. The formulation of proper detailed policies and procedures with regards to potential Investment Division cash management of portfolio assets will also be essential before any such actions occur.

Communication with and support of the BWC Internal Audit Division in reviewing existing/new investment-related policies and procedures and providing suggested improvements is a valuable resource for the Investment Division. The BWC Internal Audit Division will be engaged as appropriate in auditing identified Investment Division internal policies and processes.

Transition Activity Summary – Disabled Workers Fund / Coal Workers Fund

The transition activity of invested assets for both the Disabled Workers Fund (DWRF) and Coal Workers Fund (BLF) were both implemented and completed over the month of August, 2010. These transitions involved the transitioning of all invested assets from three legacy asset class accounts to four new targeted asset class accounts for each Fund in order to achieve the new respective target asset allocations of these two specialty Funds, as approved by the Board in December, 2009 (for BLF) and January, 2010 (for DWRF).

The planning for these two transitions occurred over several months prior to its implementation in August, including selecting a transition manager and finalizing transition strategy. The DWRF transition involved initially transferring in early August all invested securities assets and cash with a total market value (MV) on transfer dates of $1.273 billion. Such securities and cash were transferred <u>in-kind</u> to the new transition account from the following three portfolios: (1) State Street Global Advisors (SSGA) managed Long Duration Fixed Income (LDFI) separate account ($743.1 million MV); (2) SSGA managed TIPS Fixed Income separate account ($263.6 million MV); and (3) Northern Trust (NT) managed S&P 500 Equity commingled account ($266.8 MV). The BLF transition initially involved transferring at the same time as DWRF all invested securities assets and cash <u>in-kind</u> with a total market value on transfer dates of $271.6 million to the new transition account from the following three portfolios: (1) SSGA managed LDFI separate account ($159.9 million MV); (2) SSGA managed TIPS Fixed Income separate account ($55.1 million MV); and (3) NT managed S&P 500 Equity commingled account ($56.6 million MV).

The in-kind transfer of all securities from these three legacy accounts of DWRF and BLF resulted in the following respective realized capital gain amounts (unaudited) reported for August 2010:

Legacy ($millions)	**DWRF**	**BLF**
LDFI	53.8	11.6
TIPS	5.3	1.1
S&P 500	46.3	9.8
Total	105.4	22.5

The BWC transition manager received during the first week of August all of these transferred in-kind securities into the respective transition accounts to be managed by the transition manager. The goal of the transition manager was to trade these assets transferred into the transition account as efficiently and expeditiously as possible in order to achieve the new target asset allocation approved by the Board for each of DWRF and BLF as reflected in the BWC IPS as follows:

	DWRF	**BLF**
TIPS FI	35%	40%
U.S. Aggregate FI	34%	39%
U.S. Equity (Russell 3000)	20%	13%
Non-U.S. Equity (ACWIxUS)	10%	7%

The BWC transition manager began the two Fund transitions on August 9 and largely achieved the above target allocations in the first trading day for both transitions. For each mandate except for U.S. Aggregate Fixed Income, the target portfolio composition was also essentially achieved by the end of the first day of transition activity trading. For the U.S. Aggregate Fixed Income targeted portfolio, it was important for the transition manager to achieve a duration target matching the benchmark index in the first day of trading and such duration target was in fact achieved. The transition manager then focused over the next 7-8 trading days in building a U.S. Aggregate benchmark sample portfolio of holdings that closely resembled the index. The objective of the transition manager for each of the four distinct asset class transition portfolios for each of the two Funds was to build a portfolio of securities that would be completely accepted by the target commingled fund manager so as to initiate a no-cost in-kind transfer of portfolio securities in exchange for commingled fund units of equivalent market value.

By working closely with each target commingled fund portfolio manager, the transition manager was successful in converting each of the four target asset class portfolios for respective units owned of the Board approved commingled funds during the transition period. These target commingled funds for the U.S. TIPS Fixed Income, U.S. Aggregate Fixed Income and Russell 3000 Equity mandates are each managed by SSGA. The Non-U.S. Equity ACWIxUS commingled fund is managed by BlackRock.

Under the direction of the CIO, the units of each of these four commingled funds were transferred on August 31, 2010 from the two respective transition accounts to the new commingled fund targeted accounts set up for each of DWRF and BLF. The market value of these four commingled funds transferred from the transition accounts on August 31 was an aggregate $1.260 billion for DWRF and $270.4 million for BLF.

The stock and bond markets moved in opposite directions during the core August 9 to August 31 transition period for both Funds. Bonds performed reasonably well and stocks performed poorly during this transition period. The U.S. Aggregate fixed income index returned +1.0% and the U.S. TIPS benchmark index returned +1.2% over this period, whereas the Russell 3000 Equity index returned -6.3% and the ACWI ex-US index returned -5.4%. These asset account transfers from the transition accounts combined with the securities trading activity within the transition accounts resulted in net realized capital losses (unaudited) of $12.5 million for the DWRF transition account and $0.8 million for BLF. The DWRF transition account returned -1.07% and the BLF transition account returned -0.24% in August 2010. The positive returns for bonds could not overcome the significant negative return of equities held in the transition accounts. The BLF transition portfolio had better performance than the DWRF transition portfolio because BLF maintained a 20% equity asset allocation strategy in transition whereas the DWRF transition portfolio increased its equity portfolio from 20% to the new targeted 30% strategy objective on August 9 during the first day of trading for the DWRF transition account.

In summary, the CIO was very satisfied with the execution of the transition strategy by the transition manager. The transition was well organized and trading activity was performed efficiently. The CIO was especially impressed with the communication and coordination that occurred between the transition manager and each of the target commingled fund portfolio managers so as to assure an efficient in-kind exchange of securities for commingled fund units of ownership at no additional trading cost.

BlackRock ACWI ex-US Common Trust Funds Update

Total assets under management (AUM) by BlackRock in passive managed commingled (common) trust funds (CTF) involving the ACWI ex-US Index were $20.1 billion as of 7/31/10, representing a $3.0 billion AUM increase since 12/31/09. Included in this increase for 2010 to date is the new BWC investment for SIF of $1.6 billion in a newly launched CTF available to non-lending (securities), non-ERISA clients such as BWC that occurred in February, 2010. During this seven-month period, the ACWI ex-US benchmark index declined 3.0% in total return.

Of the $20.1 billion AUM invested in ACWI ex-US benchmarked CTF's managed by BlackRock as of 7/31/10, $14.5 billion represented pension fund investors with the remaining $5.6 billion representing non-pension fund investors. The BlackRock CTF funds offered are divided between pension funds and non-pension funds as well as further divided between securities lending and non-lending. Lending funds represented $16.3 billion AUM or 80% of the $20.1 billion of CTF AUM passively managed by BlackRock to this index. As a result of these two client type trends, BWC is in a minority CTF class on two fronts being both a non-pension fund and a non-securities lender.

There are currently two other BlackRock clients holding units specifically in the same CTF non-lending, non-pension "B" fund that BWC now owns for each of SIF, DWRF and BLF. One other client is a small direct holder at $9 million and the other holder is a BlackRock ACWI (including U.S.) non-ERISA, non-lending CTF Superfund with $227 million invested in this "B" fund as of 9/10/2010. There are in turn two BlackRock clients holding units in this ACWI Superfund. The combined BWC investment in this CTF "B" fund is currently over $1.8 billion market value which represents 89% of current outstanding units of this "B" fund.

Compliance

The investment portfolios were in compliance with the BWC Investment Policy at the end of August, 2010.

DATE: September 14, 2010

TO: BWC Investment Committee
BWC Board of Directors

FROM: Bruce Dunn, CFA, Chief Investment Officer

SUBJECT: **CIO Recommendations**
BWC New Investment Strategy Considerations
State Insurance Fund

BACKGROUND

Over the course of calendar year 2010 to date, much time has been devoted in BWC Investment Committee meetings to introducing and discussing new investment-related topics for consideration. These topics have included active versus passive investment management, emerging and minority-or-woman-owned investment managers (MWBE) and institutional commercial real estate investments. The BWC investment consulting team of Mercer has led these Committee meeting discussions. In the opinion of the CIO, Mercer provided outstanding background and market information on these topics as well as their perspectives based on experiences. This process has been very useful towards formulating judgments regarding potential applicability of these topics to BWC investment strategy.

The CIO has been asked by the Investment Committee to provide his recommendations addressing these and any other relevant investment topics/strategies as well as their prioritization for implementation. This memorandum of recommendation will specifically address and prioritize four new Phase I investment strategies to be considered as well as address three new proposed Phase II investment strategies for the State Insurance Fund (SIF).

Timeline charts for suggested strategy implementations for each recommended Phase I and Phase II strategy are provided as attachments to this memorandum. More specificity on these suggested timelines is provided at the end of each strategy commentary. The RFP creation and evaluation process requires much attention and time commitment of the BWC investment staff with support of other divisions of the Bureau such as Legal and Fiscal & Planning. It is expected that the BWC investment consultant firm will assist the BWC investment staff in providing appropriate RFP questions for submission as well as being actively involved in the manager selection processes. Appropriate changes to BWC investment policy will need to be addressed for each strategy recommendation. In addition, appropriate internal control policy and procedures must also be formulated and in place prior to contracting and funding of additional investment managers selected to execute new investment strategies. The timelines offered by the CIO for potential Phase I and Phase II investment strategy implementation reflects the sensitivity of staff time to both the RFP process and the subsequent increased need to monitor additional investment managers selected from a thorough evaluation process.

PRIORITY ONE – PHASE I
Long Duration Credit Fixed Income Active Management

In an active investment management presentation made to the Investment Committee at its May 27, 2010 meeting, the CIO recommended four asset classes of the State Insurance Fund for active management consideration. Of these four asset classes, long duration credit fixed income was given the only first priority recommendation by the CIO for active management consideration and implementation. This first priority consideration for this asset class was based on a combination of (a) its size and consequent opportunity, (b) the results of the Mercer manager database and (c) the ability of an active credit fixed income manager to control/reduce credit risk.

Long Duration Credit Fixed Income is the largest SIF portfolio asset class at a 28% target investment policy asset allocation. This asset class has a current approximate market value of $5.5 billion in the SIF portfolio representing approximately 30.2% of total SIF assets. The Mercer manager database for the U.S. Long Duration fixed income asset class shows performance for the median active manager and Mercer "A/A-" rated active manager exceeded the benchmark index return by a significant 0.8% and 1.4% per annum, respectively, over the most recent ten-year period offered by Mercer. There was also a high 1.0 average information ratio per annum for this asset class as represented in the Mercer database for its "A/A-" rated active managers.

As pointed out in the referenced May, 2010 CIO presentation, strong opportunities exist for a skillful active long duration credit manager to add incremental returns above the benchmark. This can be achieved through in-depth fundamental credit research and understanding of key industry sector trends, consequently over/underweighting many credits and controlling/reducing risk by eliminating/avoiding prominent deteriorating credits having major negative impacts on the benchmark return. In contrast to an active manager, a passive index manager must hold/retain all important credits in the benchmark index at an approximate index weighting even though those holdings will include declining credits. As a result, the passive manager cannot defensively reduce credit risk like active managers. The passive index manager must retain and ride down declining credits experiencing significant market value declines until such credits are removed from the benchmark index due to downgrades to junk quality status.

The CIO confirms his recommendation presented in May, 2010 that **20%** of the targeted 28% SIF asset allocation towards the long duration credit fixed income asset class be targeted towards active management. Based on a recent market value of $18.4 billion of SIF invested assets, a 20% target represents approximately $3.7 billion. Based on the recent ten-year performance period results from the Mercer database that was presented to the Investment Committee in March-April 2010 for median active manager performance as well as for Mercer "A/A-" rated managers, active management "value added" net excess investment income returns over the benchmark index (after represented estimated management fees) ranges from $20 million (for median managers) to $40 million (for "A/A-" Mercer rated managers) per annum at this 20% active management target recommendation.

It is the present expectation of the CIO that no more than four or five active long credit fixed income managers would be chosen and presented for Board approval as a result of the RFP selection process. Some diversification of managers by style of management and philosophy is desirable in the opinion of the CIO.

Timeline Estimate: RFP issuance in January 2011; finalist manager recommendations in May-June 2011; manager fundings in August-September 2011.

PRIORITY TWO – PHASE I
MWBE Investment Managers Strategy

As represented at the August, 2010 Investment Committee meeting, the CIO supports the Manager-of-Manager (MoM) structure for the selection of MWBE managers. There are experienced MoM firms who specialize in the continuous monitoring of a broad list of MWBE managers who manage assets in one or more of the asset classes of the current SIF portfolio. Any MoM firm recommended for engagement to the BWC Investment Committee/Board will result from a RFP selection process focusing on the specific strengths of the firm towards MWBE managers concentrating in SIF asset classes. It is anticipated that at most two MoM firms will be selected from the RFP process. The focus will be on the selection of the best MoM firm(s) who will in turn select top-tier MWBE managers that have delivered performance returns to clients that exceed benchmark targets in their chosen asset class. It is the opinion of the CIO that the MoM firm should select the best MWBE managers for BWC that can provide "alpha" or excess returns above a SIF benchmark index approved for MWBE management in the BWC Investment Policy Statement. For example, a determination may be made by a MoM firm that the best estimated excess return available to BWC from MWBE managers are in the large-cap equity asset class, despite the fact that the large-cap equity class overall is not an asset class that was previously recommended for active management consideration by the CIO.

Much will be learned by the RFP Selection Committee in closely evaluating the responses of MoM candidate firms. The CIO does believe that an initial MWBE funding level via MoM firms representing a targeted **1%** of SIF investment assets (currently around $180 million) is a realistic initial objective for this recommended new strategy.

Timeline Estimate: RFP issuance in April 2011; MoM finalist manager recommendation(s) in August-September 2011; MoM manager fundings in November-December 2011.

PRIORITY THREE – PHASE I
Cash Management Overlay Strategy

The CIO believes that employment of an effective cash overlay strategy will make more efficient use of operational cash balances for the SIF portfolio and earn higher investment income over time while also reducing asset class market value variances to portfolio allocation targets. Cash overlay strategies are commonly utilized by many institutional investors to capture the higher expected risk premium returns above cash returns that exist for bond and stock target asset classes.

For example, the SIF portfolio has a 1% cash allocation target reserved for operational liquidity needs but during most periods of the year, operational cash balances (excluding outside manager cash held) exceeds this 1% target and in certain months may even exceed 2%. A skilled cash overlay manager could utilize an appropriate portion of cash above a minimum cash maintenance target (such as 1%) to obtain representation via liquid exchange-traded futures contracts that closely match the returns of stock or bond benchmark indexes of SIF. The cash overlay manager would target the purchase of futures contracts to increase representation of asset classes that are under targeted asset allocation and, likewise, sell futures contracts of asset classes that are above targeted asset allocation due to market trends. The goal of a cash overlay strategy is to strive to always maintain an equivalent cash target portion not much higher than 1% and redirect excess cash towards approved investment policy asset classes that are expected to earn long-term expected returns (say 4-6% for bonds and 8-9% for stocks) well above cash returns.

An effective managed cash overlay strategy reduces the likelihood that asset allocation rebalancing via physical securities may need to occur. This is advantageous to the SIF portfolio in that appropriate ongoing rebalancing via futures contracts through a cash overlay strategy is significantly less costly in terms of incurred transaction costs compared to the trading of physical securities to achieve rebalancing.

The BWC CIO and Director of Investments have performed research and due diligence on the merits of a cash management overlay strategy periodically over the past several years. The elimination of the "cash drag" of cash balances above, for example, the 1% cash target for SIF during this environment of minimal cash equivalent returns could result in an estimated 8-12 basis points ($15-20 million) of additional total return for the SIF portfolio per annum, according to a very experienced leading cash overlay manager highly respected by the BWC senior investment officers who extensively analyzed BWC cash drag over a recent two-year period.

The CIO recognizes that the topic of cash management overlay strategy has not yet been presented and discussed in detail with the Investment Committee. When appropriate, the CIO will provide a report focused on cash management detailing the cash management overlay strategy recommendation to the Investment Committee and Board for consideration and possible approval before proceeding with the issuance of a RFP for the services of an outside cash management overlay manager. It is the expectation of the CIO that only one outside cash overlay manager would be recommended from the RFP to be issued.

Timeline Estimate: RFP issuance in July 2011; single finalist manager recommendation in November 2011; approved manager implementation in January 2012.

PRIORITY FOUR – PHASE I
<u>Real Estate Investment Strategy</u>

The CIO supports a 2.5% to 3.0% initial target allocation to real estate investments. Mercer provided an excellent presentation on real estate as an attractive asset class for investment consideration by BWC at the Investment Committee meeting of August, 2010. Real estate as an asset class provides further diversification to the SIF investment portfolio with a relatively low correlation to the returns of the other bond and stock asset classes for SIF. A well-managed core fund real estate strategy should be the initial focus for SIF, in the opinion of the CIO. As described by Mercer, private core real estate funds are large commingled funds organized as limited liability corporations (LLC) that are professionally managed by experienced professional real estate management firms with proven track records. These core real estate funds are typically open-ended in structure with investors typically being institutional investors, including many public funds. These core real estate fund portfolios consist of high quality, well-leased commercial real estate that are diversified by property type and geographic location. These core real estate funds typically provide a higher level of income to investors than investment grade bonds and also provide some capital appreciation potential from property sales. These real estate funds provide attractive inflation hedging benefits to SIF with property values and leasing income being positively correlated to inflation rates.

As in the case with private equity partnerships, the RFP process is not an efficient method for the selection of private core real estate funds by larger institutions such as BWC. For institutions such as BWC considering real estate investments via the selection of operating funds with existing property portfolios, the direct involvement of their investment consulting firm or a specialty real estate advisor in the selection process is the norm for building exposure to the real estate asset class. This would especially apply to BWC which has had no prior experience in investing in diversified real estate pools. The selection process of real estate funds and private equity funds requires prospective investor patience for the opportunity to participate as either a new investor or add-on investor. The capital raising period is largely dictated by the sponsoring real estate investment manager. In discussions with Mercer, it is the expectation of the CIO that Mercer will introduce BWC to a group of highly rated and recommended successful core real estate funds offering the investment attributes desired by BWC.

<u>Timeline Estimate</u>: Mercer indicated in its presentation of August, 2010 that a new real estate allocation could take 3-5 years to fully execute. It would be the intention of the CIO to seriously explore core real estate fund opportunities beginning early in fiscal year 2011 with recommendations for approval of several core real estate funds occurring over the second half of calendar year 2011 and first quarter of 2012. Once more conservative core real estate fund investments totaling approximately 2% of total SIF assets (currently $350-375 million) are completed sometime in 2012, additional investments totaling perhaps 1% of SIF assets can be explored in higher risk value-added real estate funds as well as public global REITS as suggested by Mercer in its recommended total real estate investment strategy presented last month. Value-added real estate funds are closed-end funds with funding characteristics similar to new private equity funds, whereby capital commitments are funded as needed by the manager typically over a 3-4 year time frame. One important issue that must be addressed by the Investment Committee and Board, with the advice of Mercer and the CIO, is what current SIF asset class targets are to be reduced to accommodate a 2.5% or 3% real estate target asset allocation.

PHASE II PRIORITIES
<u>Active Management Investment Asset Classes</u>

The CIO recommends that Phase II of investment strategy implementation be focused on the selection of a group of active investment managers for each of three additional asset class mandates of the SIF portfolio. As previously recommended by the CIO in his active investment management presentation made to the Investment Committee in May, 2010, these three asset class mandates are (1) U.S. Small/Mid Cap Equity, (2) Non-U.S. Equity and (3) U.S. Aggregate Fixed Income.

As the attached Phase II timelines display, the CIO anticipates that the investment manager selection process for these three mandates will be staggered and staged over an estimated 1½ year timeframe from 4Q2011 through 1Q2013. Each of the three active management mandates for Phase II consideration will require an estimated nine months to complete a thorough RFP process from RFP issuance to evaluation and selection to Board approval to contracting/funding the new investment managers. It is the expectation of the CIO that between three and five top-tier skilled active managers would be chosen and recommended for Board approval for each of these recommended mandates. Specific comments and recommendations for active management of each of these three mandates follows.

PRIORITY ONE – PHASE II
U.S. Small/Mid Cap Equity Active Management

Similar to the long duration credit asset class, the CIO believes that U.S. Small/Mid Cap Equity is a compelling asset class for active investment management. The SIF target portfolio allocation for this asset class is currently effectively at 4% as the SIF U.S. equity benchmark All Cap Russell 3000 index with a SIF allocation target of 20%. The Russell 3000 index is comprised of 80% large cap stocks and 20% small-mid cap stocks (as represented by the Russell 2500 index comprising the bottom 5/6 of stocks of the Russell 3000 benchmark index by market cap). The Mercer investment manager database previously presented to the Investment Committee/Board indicated the median active manager gross performance in this asset class space exceeded the Russell 2500 benchmark index return by 1.8% per annum over the past ten years ended September 2009 or more than double the median management fee of 0.77%. The Mercer "A/A-" rated manager database showed U.S. small/mid cap core active managers returned an average 5.4% per annum above the benchmark return before management fees over the period 2000-2009 which was easily the highest value added U.S. bond or stock asset class in the Mercer database.

The U.S. small/mid cap equity sector offers many opportunities for skillful managers to add impressive incremental returns above the benchmark index. Among these opportunities are that U.S. small and mid-cap equity markets are: (i) less efficient markets with less common knowledge and information allowing for fundamental due diligence and detailed understanding of specific companies to be rewarded; (ii) many stocks to select from in constructing and managing a portfolio allows for excellent research to be rewarded; and (iii) value versus growth weightings and sector weightings above or below index weightings can result in significant value added to performance.

The CIO recommends that the entire SIF portfolio allocation towards U.S. Small/Mid Cap Equity, estimated at an effective **4%** current asset allocation, be directed to active management. A 4% allocation represents approximately $725 million based on the current SIF portfolio market value. A gross excess return of 2% to 3% above the benchmark reduced by estimated management fees of 75 bp per annum (as represented in Mercer database) on $725 million would provide net excess or value add returns of $8-16 million per year. An excess return of 5.4% per annum provided by the Mercer "A/A-" rated universe of managers over 2000-2009 would provide a value added investment income (after deducting 75 bp of management fees) of almost $34 million per annum.

Timeline Estimate: RFP issuance in November 2011; finalist manager recommendations in March-April 2012; manager fundings in June-July 2012.

PRIORITY TWO – PHASE II
<u>Non-U.S. Equity Active Management</u>

The SIF target asset allocation for this asset class is 10% of total invested assets. The MSCI ACWI ex-U.S. benchmark index for this asset class is presently comprised of approximately 77% developed country markets and 23% emerging markets by market value weighting. The benchmark index is currently comprised of the MSCI EAFE index (21 developed countries), Canada and 22 emerging market countries comprising the MSCI Emerging Markets index. The ACWI ex-U.S. benchmark index currently comprises over 1,800 companies. The Mercer investment manager database results for the developed country equity EAFE benchmark index shows solid gross excess return of 1.11% per annum for active managers since 1986, compared to a median management fee of 0.63% per annum. Over the recent ten years to September 2009, the median active manager gross performance exceeded the EAFE index by an impressive 2.3% per annum with only a slightly higher standard deviation than exhibited by the benchmark index.

Opportunities allowing skillful active managers to add incremental returns above respective benchmark indexes include: (1) ability to overweight/underweight individual country exposure; (ii) ability to overweight/underweight many companies and industries within specific countries base on growth prospects and relative value; (iii) most developed country stock markets and all emerging market country stock markets are less efficient than U.S. stock markets, therefore creating significant value added opportunities rewarding good research; and (iv) manager opinions and positioning on foreign exchange rates of key currencies can also provide additional returns versus the benchmark return which is always expressed in U.S. dollars.

The CIO recommends that one-half or **5%** of the 10% target for the SIF asset class mandate towards Non-U.S. Equity be allocated for active management, with the remaining 5% targeted for this asset class to continue to be passively managed. A 5% allocation towards active management for this asset class for SIF currently is approximately $900 million. For this 5% recommended allocation, the median gross excess return performance of 2.3% represented in the Mercer investment manager database over the recent ten-year period would equate to a net excess return of approximately $15 million per annum after average management fees of 63 basis points as represented by Mercer.

<u>Timeline Estimate</u>: RFP issuance in March 2012; manager recommendations in July-August 2012; manager fundings in October-November 2012.

PRIORITY THREE – PHASE II
<u>U.S. Aggregate Fixed Income Active Management</u>

The SIF target asset allocation for this asset class is 15% of total invested assets. The BarCap U.S. Aggregate index is the broadest and most popular U.S. fixed income benchmark index (over 8,000 issues) with many active fixed income managers focused on outperforming this benchmark. These fixed income managers are considered "core" fixed income managers who benchmark to this broad U.S. Aggregate index. The Mercer investment manager database shows an average gross excess return of 0.54% per annum for active managers over this broad benchmark index since 1987 or more than double the median management fee of 0.25% per annum. Over a ten-year period ending September 2009, the Mercer database showed upper quartile manager returns were 0.80% per annum above the benchmark index before management fees.

Given the breadth of the composition of the U.S. Aggregate fixed income index, opportunities for skillful active managers to add incremental returns above this benchmark index include: (i) overweight/underweight important benchmark sectors (U.S. Treasuries, U.S. Agencies, MBS, CMBS, corporates, taxable municipals, sovereigns, supranationals) depending on manager relative value perception and other market/economic considerations; (ii) overweight/underweight segments within important benchmark sectors such as corporate credits and residential MBS coupon rate brackets; and (iii) adjust duration of portfolio (within prescribed limits) to take advantage of shape of yield curve and yield curve changes.

Similar to active long duration credit managers, astute active core fixed income managers can sell declining credit holdings before being downgraded significantly by rating agencies. Passive index managers must retain such holdings until those holdings are downgraded to junk bond status after much price erosion has occurred and are then forced to sell such holdings in unison with many other institutional investors also prohibited from owning junk bonds, further aggravating loss of value.

The CIO recommends that **9%** of the 15% targeted towards SIF U.S. Aggregate fixed income asset class allocation be considered for active management, with the remaining 6% asset class allocation remaining passively managed. A 9% allocation to active management of this asset class for SIF currently amounts to approximately $1.65 billion. For this recommended allocation, an upper quartile active management return of 0.80% above the benchmark would amount to approximately $9.0 million in incremental annual income, after estimated management fees of 25 basis points per annum.

<u>Timeline Estimate</u>: RFP issuance in July 2012; finalist manager recommendations in November-December 2012; manager fundings in February-March 2013.

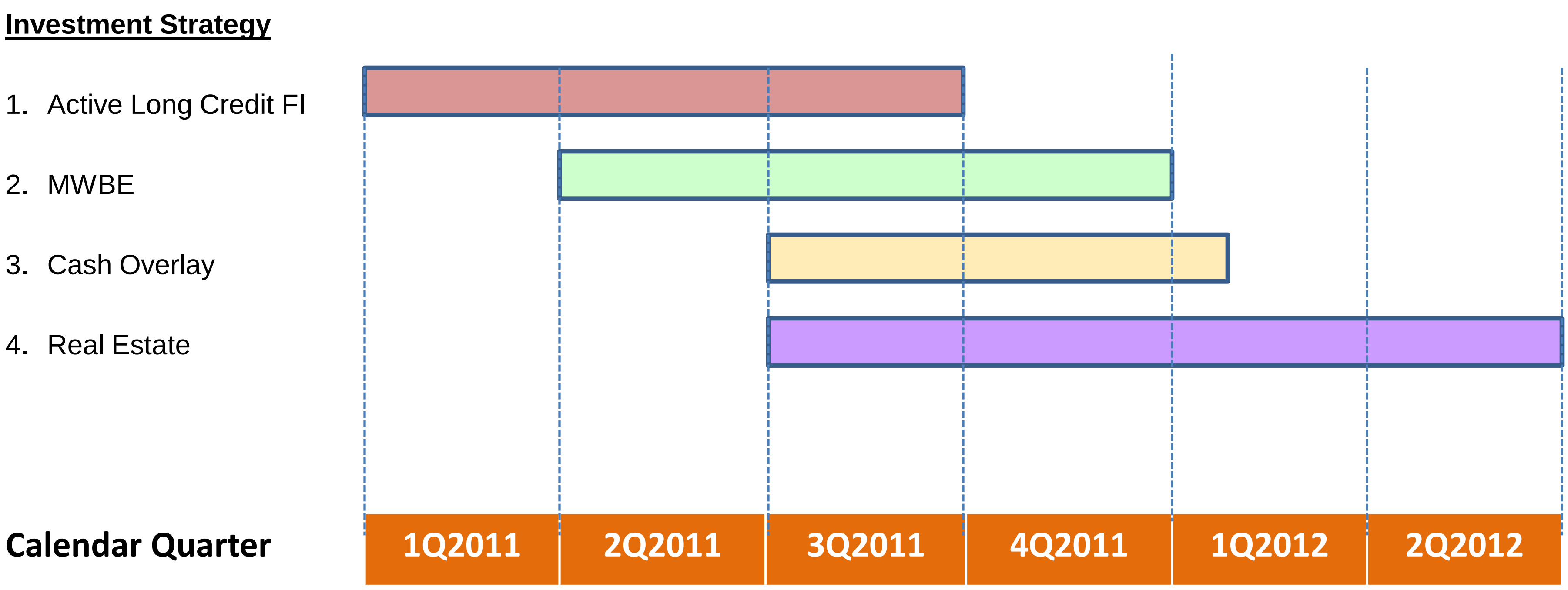
SUMMARY

The CIO believes strongly that each of the investment strategies listed as recommended Phase I or Phase II implementations will improve long-term expected returns of BWC invested assets and provide more diversification of asset classes, investment managers and investment management styles.

The CIO is recommending that a targeted 39% of SIF asset allocation be actively managed. Active management fixed income and equity strategies recommended are 20% long duration credit fixed income, 9% U.S. Aggregate core fixed income, 5% non-U.S. equity, 4% small/mid cap equity and 1% MWBE. In addition, a recommended 2.5% to 3.0% initial allocation to institutional quality commercial real estate investments, via well-managed commingled real estate funds, will provide further portfolio diversification and some inflation hedging benefits. The SIF portfolio would have the potential opportunity to achieve higher expected long-term incremental net investment income with a diversified group of experienced, highly regarded top-tier active style investment managers.

With the recent completion of all required asset allocation transition activities for each of the State Insurance Fund, Disabled Workers Fund and Coal Workers Fund, the CIO and Investment Staff is committed to carrying out and executing these proposed State Insurance Fund investment strategies in whatever priority and timeframe is determined by the Investment Committee and the Board. Regarding Investment Division staffing requirements, the CIO is of the opinion that at least two and likely three investment professionals will need to be added to the current BWC Investment staff to help carry out the proposed new strategies and subsequently closely monitor the additional BWC investment managers associated with these strategies. The first two staff additions would be targeted over fiscal year 2012 as proposed Phase I strategies are being implemented and the proposed Phase II strategies come into focus beginning late in calendar year 2011. A third investment staff professional would likely be added in fiscal year 2013 as the Phase II strategies progress to implementation completion.

Recommended Phase I Priorities
Implementation Timelines
State Insurance Fund



Investment Strategy Timeline reflects period from RFP issuance to expected funding of directed assets

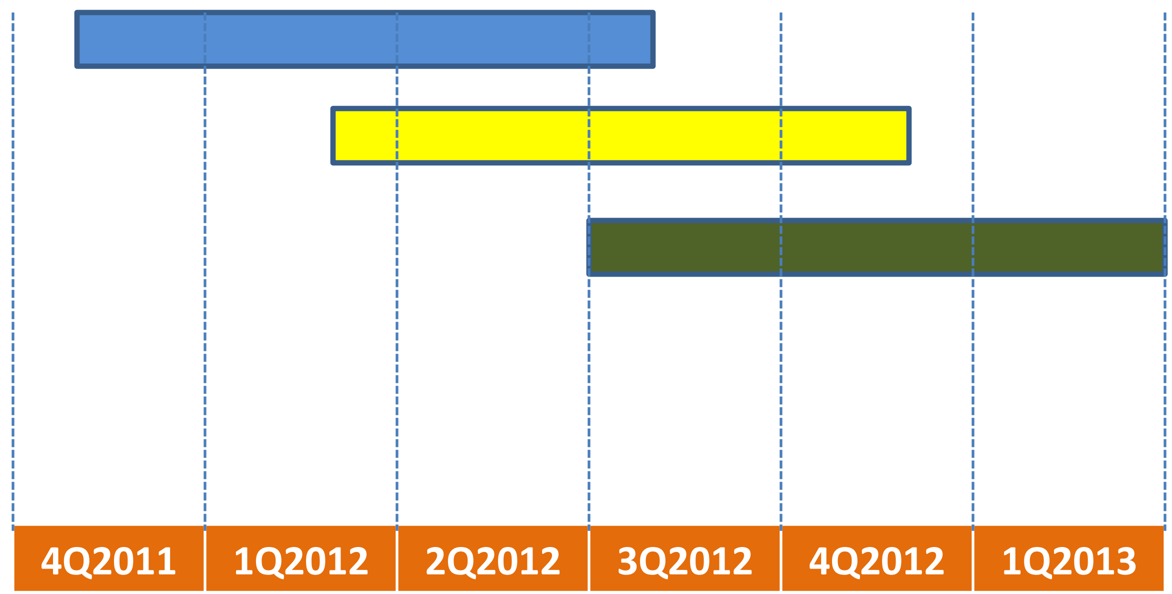
(Real Estate Strategy excepted)

Prepared by Investment Division
September 14, 2010

Recommended Phase II Priorities
Implementation Timelines
State Insurance Fund

Investment Strategy

1. Active U.S. Small/Mid Cap Equity
2. Active Non–U.S. Equity
3. Active U.S. Aggregate FI

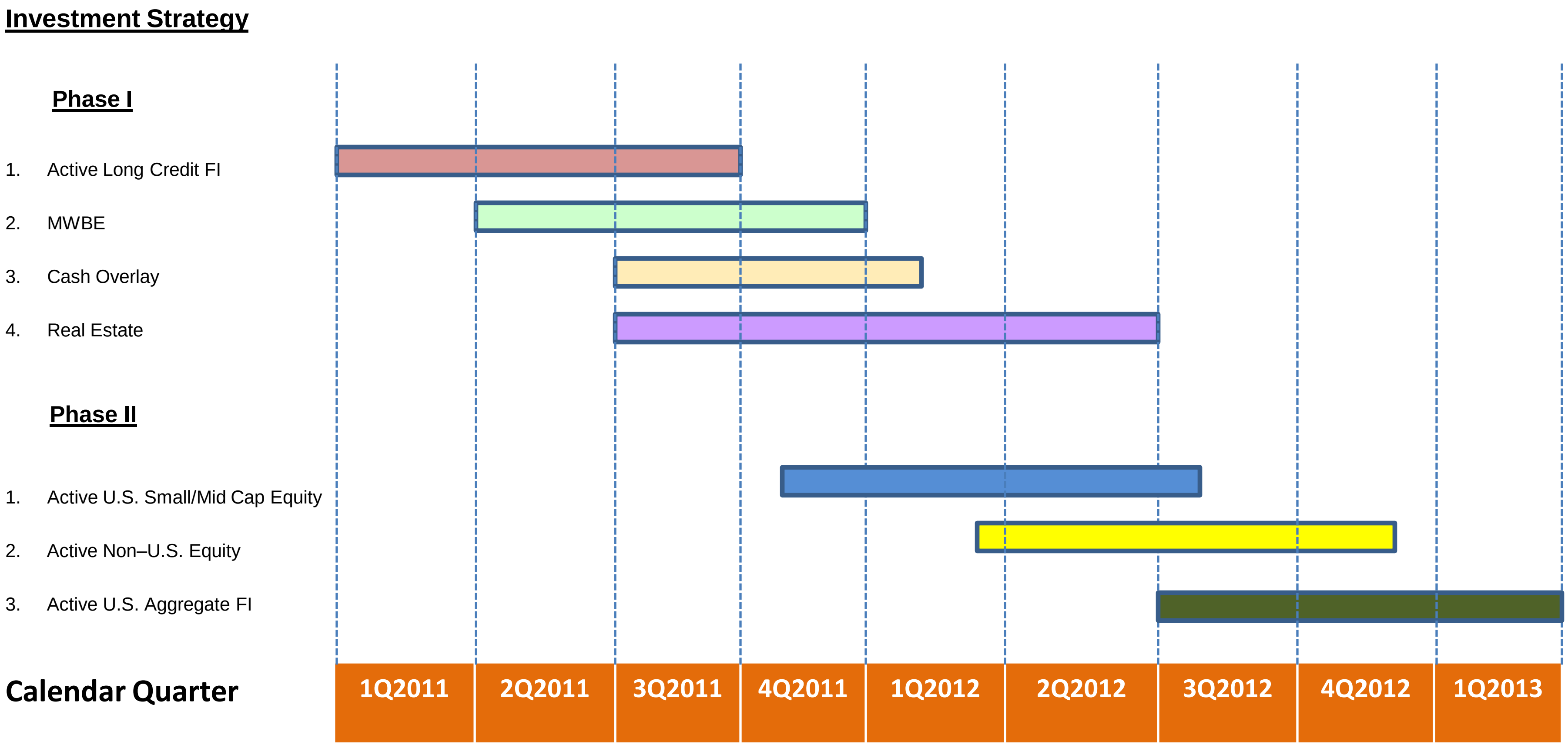


Calendar Quarter

Investment Strategy Timeline reflects period from RFP issuance to expected funding of directed assets

Prepared by Investment Division
September 14, 2010

Recommended Phase I & II Priorities
Implementation Timelines
State Insurance Fund



Investment Strategy Timeline reflects period from RFP issuance to expected funding of directed assets

(Real Estate Strategy excepted)

Prepared by Investment Division
September 22, 2010

MERCER

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Memo

To:	BWC Investment Committee
	BWC Board of Directors
Date:	September 23, 2010
From:	Guy M. Cooper
	Jordan Nault
	Kweku Obed
Subject:	Suggested Investment Policy Changes – Section VIII

We are pleased to offer suggested amendments to the Bureau's Statement of Investment Policy. These modifications expand on Section VIII of the existing Statement of Investment Policy and embody policies appropriate for the implementation of a program utilizing qualified minority-owned and/or women-owned investment managers. The proposed language has been crafted in consultation with the Chief Investment Officer and his staff.

DATE: September 15, 2010

TO: BWC Investment Committee
BWC Board of Directors

FROM: Bruce Dunn, CFA, Chief Investment Officer

SUBJECT: **Investment Policy Recommendation**
Section VIII – Fair Consideration/Public Interest Policy

The BWC Chief Investment Officer recommends for consideration and approval the following proposed Policy for fair consideration of qualified Minority-Owned and/or Women-Owned Investment Managers (MWBE) as well as qualified Ohio Managers as defined. This proposed Policy reflects modifications of Section VIII of the BWC Statement of Investment Policy and Guidelines (IPS). These modifications are reflected in red in the proposed Policy. The unmarked proposed Section VIII of the IPS reflecting all such Policy modifications is also provided.

Proposed Section <u>VIII.A</u> specifically represents the suggested investment policy for qualified MWBE investment managers chosen through a Manager-of-Manager (MoM) program process that is recommended by both the CIO and Mercer as BWC Investment Consultant. In this proposed Policy, the Board will delegate authority to any Board approved MoM to identify, select and monitor appropriate MWBE investment managers.

Per research of Mercer, proposed Section <u>VIII.A.iii</u> lists the asset classes that may be eligible for MoM programs and which represent the BWC asset classes with the strongest and deepest MWBE investment management capability. The recommended MoM program target asset allocation for MWBE investment management is 1% of invested assets of the State Insurance Fund.

The proposed Section VIII Fair Consideration/Public Interest Policy has been a joint coordinated effort of Mercer and the CIO with assistance by the BWC Director of Investments.

VII. INVESTMENT POLICY STATEMENT REVIEW

The Board in conjunction with the Administrator, Chief Investment Officer and Investment Consultant will review this policy statement at least once a year, to determine if revisions are warranted and will publish the policy statement and any changes it adopts and make copies available to all interested parties.

It is not expected that this Investment Policy will change frequently; in particular short-term changes in the financial markets should generally not require an adjustment in this Investment Policy.

VIII. FAIR CONSIDERATION / PUBLIC INTEREST POLICY

The Board desires that the BWC Investment Staff and the Investment Consultant identify, research and evaluate qualified Ohio investment managers, minority-owned investment managers and women-owned investment managers. It is the Board's intention to give such investment management firms fair consideration to fulfill the Funds' investment objective; however, the Board is not obligated to hire any qualified Ohio firm, minority-owned or women-owned firm on behalf of the Funds if such hiring is inconsistent with its fiduciary duty to the Funds and their stakeholders or in asset classes that have not been approved by the Board.

A. Qualified Minority-Owned and/or Women-Owned Investment Managers – Criteria

As used in this Investment Policy, a minority-owned investment manager shall be defined as an investment manager that is U.S. domiciled and is majority-owned by one, or any combination, of the following groups: African American, Native American, Hispanic American and Asian American. Additionally, Investment Managers who are majority-owned by women are included in this Policy and defined as women-owned investment managers.

As used in this Investment Policy, minority-owned and/or women-owned investment managers are collectively defined as Minority-or-Women Business Enterprise (MWBE) Investment Managers. Any MWBE Investment Manager must be a registered investment advisor under the Investment Advisors Act of 1940.

i. Process

With regards to MWBE Investment Manager strategy, it is the Board's desire to have Fund assets managed by such qualified firms through a Manager-of-Manager (MoM) program. BWC will not place Fund assets directly with MWBE firms but will instead place Fund assets directly with MoM firms. BWC Investment Staff and the Investment Consultant will identify qualified MoM firms through a selection process approved by the Board. Any MoM firm approved by the Board will be defined as a BWC Investment Manager with all of the duties and responsibilities of Section III.C of this Investment Policy. Any MoM firm must be a registered investment advisor under the Investment Advisors Act of 1940.

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In addition to the requirements above, any

Deleted: qualified Ohio manager, and any minority or women-owned

Deleted: Any Broker must be properly licensed.

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ii. **Monitoring and Responsibilities**

Any MoM approved by the Board will be responsible for identifying and monitoring the selected MWBE investment managers in the MoM portfolio managed for BWC. While the Board is responsible for reviewing and approving this MoM Policy, the Board delegates authority to the MoM to implement this MoM Policy and the MoM acknowledges its fiduciary responsibility for the assets it manages for BWC.

The MoM is responsible for the management of BWC assigned assets within the guidelines and restrictions of this Investment Policy adopted by the Board. The MoM is responsible for identifying and monitoring MWBE compliance to the approved investment guidelines. MWBE managers are hired into or removed from the MoM's portfolio of BWC assets based on information reviewed by the BWC Investment Staff and the Investment Consultant.

iii. **Eligible Asset Classes**

The Board may consider MoM programs that focus on one or more of the following approved asset classes:

1. Large Capitalization U.S. Equities
2. Small Capitalization U.S. Equities
3. Mid Capitalization U.S. Equities
4. Core U.S. Fixed Income
5. Non-U.S. Equities

iv. **Target Asset Allocation**

The MoM investment manager program for MWBE asset allocation will have a 1% target for invested assets of the State Insurance Fund.

B. Qualified Ohio Investment Managers - Criteria

As used in this Investment Policy, a qualified Ohio investment manager is one that meets at least one of the following requirements:

- Maintains its corporate headquarters or principal place of business in Ohio, or
- Employs at least 500 individuals in Ohio, or
- Maintains a principal place of business in Ohio and employs at least 20 Ohio residents.

Any qualified Ohio investment manager must be a registered investment advisor under the Investment Advisors Act of 1940.

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VII. INVESTMENT POLICY STATEMENT REVIEW

The Board in conjunction with the Administrator, Chief Investment Officer and Investment Consultant will review this policy statement at least once a year, to determine if revisions are warranted and will publish the policy statement and any changes it adopts and make copies available to all interested parties.

It is not expected that this Investment Policy will change frequently; in particular short-term changes in the financial markets should generally not require an adjustment in this Investment Policy.

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Ohio Bureau of Workers' Compensation

Asset Allocation in Real Estate by Plan Type

September 23, 2010

Guy M. Cooper
Jordan Nault
Kweku Obed

Asset Allocation in Real Estate
Total Assets of Participating Funds

Type	Number of Funds	Market Value ($, Millions)
Public	40	1,280,563
Union	10	9,219
Corporate	9	53,722
All Funds	59	1,343,505

Data taken from Council of Institutional Investors Asset Allocation Survey 2009; page 1

Asset Allocation in Real Estate
Historic Unweighted Asset Mix

Asset Class	2009	2008
Domestic Equity	30.0%	36.3%
Domestic Fixed Income	27.5%	24.4%
Global / International Equity	14.1%	17.6%
Real Estate	7.9%	6.4%
Private Equity	6.7%	4.4%
Hedge Funds	3.2%	2.0%
Global / International Fixed Income	2.5%	2.7%
Cash Equivalents	2.4%	1.1%
Other	2.1%	1.7%
Emerging Markets Equity	1.4%	2.0%
Commodities / Real Assets	1.1%	0.9%
Venture Capital	1.1%	0.5%

Data taken from Council of Institutional Investors Asset Allocation Survey 2009; page 4

Asset Allocation in Real Estate

Ranges of Asset Allocation in Real Estate

Type	Lowest	Median	Highest	Participation Rate
Corporate	0.2%	4.9%	13.0%	100.0%
Public	0.3%	8.8%	18.6%	97.5%
Union	5.5%	9.2%	18.7%	90.0%

Data taken from Council of Institutional Investors Asset Allocation Survey 2009; page 5

Asset Allocation in Real Estate
Asset Mix by Fund Type

Asset Class	Corporate	Public	Union	BWC [2]
Domestic Equity	25.5%	28.6%	39.7%	19.2%
Domestic Fixed Income	34.2%	25.7%	28.5%	71.5%
Global / International Equity	11.9%	16.0%	8.0%	7.9%
Real Estate	5.2%	8.3%	9.1%	N/A
Private Equity	6.2%	7.3%	5.4%	N/A
Hedge Funds	3.0%	2.2%	7.1%	N/A
Global / International Fixed Income	0.4%	3.6%	< 0.1%	N/A
Cash Equivalents	4.6%	2.2%	1.4%	1.4%
Other	4.9%	1.9%	0.7%	N/A
Emerging Markets Equity	2.1%	1.6%	< 0.1%	N/A
Commodities / Real Assets	0.8%	1.5%	< 0.1%	N/A
Venture Capital	1.1%	1.2%	0.1%	N/A
Total In Equities [1]	59.9%	67.0%	70.0%	27.1%
Number of Funds	9	40	10	N/A

[1] Domestic, global/international, real estate, private equity, hedge funds, other, emerging markets and venture capital

[2] BWC Allocations as of 6/30/2010

Data taken from Council of Institutional Investors Asset Allocation Survey 2009; page 6

Asset Allocation in Real Estate
Asset Mix by Fund Size

Asset Class	Less Than $3 Billion	$3 Billion to $20 Billion	More Than $20 Billion	BWC [2]
Domestic Equity	33.7%	28.4%	27.8%	19.2%
Domestic Fixed Income	28.7%	27.9%	25.8%	71.5%
Global / International Equity	10.3%	16.6%	15.4%	7.9%
Real Estate	8.0%	6.3%	9.4%	N/A
Private Equity	5.1%	5.9%	9.3%	N/A
Hedge Funds	4.9%	2.6%	1.9%	N/A
Global / International Fixed Income	1.0%	4.4%	2.3%	N/A
Cash Equivalents	2.3%	2.7%	2.4%	1.4%
Other	3.9%	1.4%	1.2%	N/A
Emerging Markets Equity	1.0%	1.4%	1.7%	N/A
Commodities / Real Assets	0.6%	1.3%	1.5%	N/A
Venture Capital	0.4%	1.0%	1.4%	N/A
Total In Equities [1]	67.4%	63.7%	68.1%	27.1%
Number of Funds	20	19	20	N/A

[1] Domestic, global/international, real estate, private equity, hedge funds, other, emerging markets and venture capital

[2] BWC Allocations as of 6/30/2010

Data taken from Council of Institutional Investors Asset Allocation Survey 2009; page 7

Asset Allocation in Real Estate

Example - Teacher Retirement System of Texas

Teacher Retirement System of Texas (TRS)

- The Teacher Retirement System of Texas (TRS) includes real estate in its real assets (RA) Portfolio.
- TRS' Investment Policy Statement (IPS) notes that the RE Portfolio will focus on private or public real estate equity, private or public real estate debt, infrastructure, timber, agricultural real estate, oil and gas, real asset mezzanine debt or equity, mortgage-related investments, entity-level investments, real estate investment trusts ("REITs"), master limited partnerships ("MLPs"), non-fixed assets and other opportunistic investments in real estate. Real estate investments are often classified by strategy, including: core; core-plus; value-added; and opportunistic.
- **Teacher's IPS has assigned the following weights to real assets:**
  - Minimum: 5%
  - Maximum: 20%
  - Long Term Target: 15%
- During the second quarter of 2010, the Retirement System made more than $800m in real estate investments – a mixture of core, value-added and infrastructure strategies. (Source: IPE Real Estate)

Asset Allocation in Real Estate

Example - Teacher Retirement System of Texas

Teacher Retirement System of Texas (TRS)

- The largest of the commitments was a $300m allocation to Zachary Hastings Infrastructure Partners. The second investment was a $250m commitment to Stratford Land Fund IV. The remaining $250m allocation was allocated to Lionstone Cash Flow Partners.
- According to HousingWire.com (August 2010), TRS will reportedly invest an additional $1.1bn in real estate between three different firms via a $400m commitment to the JP Morgan Strategic Property fund, a $200m allocation to the Forum Asian Realty Income III and a $500m pledge to General Growth Properties.

Asset Allocation in Real Estate

Example - Ohio Public Employees Retirement System

Ohio Public Employees Retirement System (OPERS)

- The Ohio Public Employees Retirement System (OPERS) includes real estate in its alternatives Portfolio.
- OPERS will allocate $1.6bn to real estate in 2010, targeting stable assets as well as motivated sellers. (Source: IPE Real Estate)
- OPERS will be investing through three main structures: separate accounts; open-ended and closed-end commingled funds .The fund is expected to allocate an estimated $683m to its existing separate account managers.
- Up to $600m could also be invested in the open-ended commingled fund sector, although it will depend on market fundamentals and portfolio valuations.
- A further $225m-$275m is likely to be invested in the closed-end commingled funds, delivering three to five non-US investment partnerships over the year.
- **OPERS IPS has assigned the following weights to real estate:**
  - Minimum: 0%
  - Maximum: 14%
  - Long Term Target: 10%

Asset Allocation in Real Estate

Example - California State Teachers' Retirement System

California State Teachers' Retirement System (CalSTRS)

- The California State Teachers' Retirement System (CalSTRS) includes real estate as a stand alone portfolio.
- CalSTRS allocation within the real estate portfolio as of 6/30/10 was 67% tactical, 32% core, and 1% public.
- The tactical portfolio is comprised of international, opportunistic, land, specialty, and urban investments.
- **CalSTRS IPS has assigned the following weights to real estate:**
  - Minimum: 9%
  - Maximum: 15%
  - Long Term Target: 11%
- During the second quarter of 2010, the Retirement System made two real estate investments totaling $570m – both were tactical.

Asset Allocation in Real Estate

Example - California Public Employees' Retirement System

California Public Employees' Retirement System (CalPERS)

- The California Public Employees' Retirement System (CalPERS) includes real estate as a stand alone portfolio.
- The CalPERS portfolio is comprised of both core and specialized investments. The specialized investments include national housing, single family housing, senior housing, urban, natural resources (timber and agriculture), technology, opportunistic, and international.
- CalPERS real estate investments are acquired and managed through REITs, separate accounts, partnerships, and limited liability companies.
- **CalPERS IPS has assigned the following weights to real estate:**
  - Minimum: 5%
  - Maximum: 15%
  - Long Term Target: 10%

Asset Allocation in Real Estate

Example - New York State Common Retirement Fund

New York State Common Retirement Fund (CRF)

- The New York State Common Retirement Fund (CRF) includes real estate in its alternatives portfolio.
- CRF invests through directly owned real estate, joint ventures, commingled funds, co-investment funds, fund of funds, captive funds and mortgage loans.
- CRF focuses a portion of the real estate portfolio on investments in affordable housing in New York.
- **CRF's IPS has assigned the following weight to real estate:**
  - Long Term Target: 6%

Asset Allocation in Real Estate

Example - Colorado Public Employees’ Retirement Association

Colorado Public Employees' Retirement Association (PERA)

- The Colorado Public Employees' Retirement Association (PERA) includes real estate as a stand alone portfolio.
- **PERA’s IPS has assigned the following weights to real estate:**
  - Minimum: 4%
  - Maximum: 10%
  - Long Term Target: 7%

Asset Allocation in Real Estate

Recent Allocations to Real Estate

Plan	Allocation to Real Estate	Date
TRS	5.8%	August 2009
OPERS	8.4%	June 2009
CalSTRS	9.9%	July 2010
CalPRS	7.5%	June 2010
CRF	6.5%	March 2009
PERA	6.0%	December 2009

Asset Allocation in Real Estate
Mercer Mean-Variance Assumptions

		Geometric Return	Arithmetic Return	Standard Deviation	Beta	Duration	Liquidity
2009	Real Estate Combination[1]	7.3%	8.2%	13.7%	0.75	0.0	4.5
2010	Real Estate Combination[1]	7.4%	8.5%	15.5%	0.75	0.0	4.5

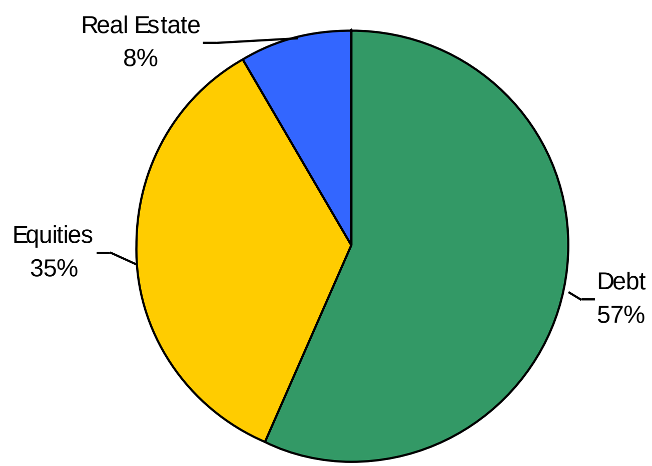
[1] Comprised of 50% Real Estate - Core and 50% Real Estate - REITS

Asset Allocation in Real Estate

Total Market Capitalization by Asset Class

- The size of the worldwide bond market (total debt outstanding) is an estimated $82.2 trillion. Outstanding US bond market debt is approximately $31.2 - $34.3 trillion (BIS /SIFMA).
- The size of the world stock market is estimated at about $40 - 50 trillion (Reuters / SIFMA). The US represents approximately 40% of the world stock market.
- It is estimated that the global Commercial Real Estate (CRE) debt market accounts for approximately 58% of the $12 trillion investable real estate universe (RREEF).
- It is estimated that globally, there are approximately $230 billion of distressed real estate assets; $168 billion of these troubled assets are located in the US while large concentrations also exist in the United Kingdom ($15 billion), Spain ($5.2 billion) Japan ($2.8 billion) and Australia ($2.5 billion).

Estimated Size of Global Fixed Income, Equity, and Real Estate Universes



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12-month Investment Committee Calendar

Date	September	Notes
9/23/2010	1. New Investment Strategies - CIO recommendations 2. MWBE Investent Policy recommendation (1st read) 3. BlackRock ACWIxUS common trust fund update (in CIO Report) 4. Mercer education session, real estate asset class, second discussion	
Date	**October**	
10/21/2010	1. MWBE Investment Policy recommendation (2nd read), possible vote 2. Investment class performance/value annual report (ORC4121.12(F)(12)], possible vote 3. Investment Consultant services RFP issuance approval, possible vote 4. Annual Review Committee Charter (1st read) 5. Brokerage Activity Fiscal Year 2010 summary report	
Date	**November**	
11/18/2010	1. Annual Review Committee Charter (2nd read), possible vote 2. Investment Consultant Performance Report 3Q10 3. Custodial Fiscal Year 2010 annual review (in CIO Report)	
Date	**December**	
12/15/2010		
Date	**January**	
1/20/2011	1. Self Insured Employers Guarantee Fund (SIEGF) Asset Allocation Analysis report and recommendation, first review, possible vote on asset allocation strategy	
Date	**February**	
2/23/2011	1. Investment Consultant Performance Report 4Q10 2. Economist Presentation	

12-month Investment Committee Calendar

Date	March	Notes
3/24/2011		

Date	April	
4/28/2011	1. Investment Consultant services RFP finalist recommendation, possible vote	

Date	May	
5/26/2011	1. Investment Consultant Performance Report 1Q11	

Date	June	
6/15/2011		

Date	July	
7/28/2011		

Date	August	
8/25/2011	1. Investment Consultant Performance Report 2Q11	

BWC Invested Assets
Estimated and Unaudited
As of September 22, 2010

Sept2010 MTD MV Decrease Bonds………… - $ 54 million (-0.4% return)
Sept2010 MTD MV Increase Equities………… +$ 446 million (+8.2% return)

Sept2010 MTD MV Increase Bonds+Equities.... + $ 392 million
(+1.9% Sept10 MTD portfolio return including Cash)

BWC Asset Allocation MV 9/22/10

Bonds*…………	$14,017 million	69.0%
Equities*……….	5,874 million	28.9%
Cash……………	415 million	2.1%
TOTAL………...	$20,306 million	100.0%

* includes nominal cash held by outside managers

Portfolio Return Calendar 2008……… -2.3% (-$444 million net inv. income)
Portfolio Return Fiscal Year 2009…… -1.1% (-$195 million net inv. income)
Portfolio Return Calendar 2009………+8.6% (+$1,505 million net inv. income)
Portfolio Return Fiscal Year 2010…..+12.0% (+$2,050 million net inv. income)

Fiscal Year 2011 YTD

Portfolio Return July10-Aug10 …….. + 3.9% (+$755 million net inv. income)

Prepared by: Bruce Dunn, CFA
BWC Chief Investment Officer