BWC Board of Directors
Investment Committee
Wednesday, December 16, 2009
Level 2, Room 3 (Mezzanine)
30 West Spring St.
Columbus, OH 43215

Members Present: Robert Smith, Chair
Alison Falls, Vice Chair
David Caldwell
Kenneth Haffey
Larry Price
William Lhota, *ex officio* (absent from approximately 1:00 p.m. to 1:45 p.m.)

Members Absent: None

Other Directors Present: Charles Bryan, James Harris, James Hummel, James Matesich, and Thomas Pitts

CALL TO ORDER

Mr. Smith called the meeting to order at 12:30 PM and the roll call was taken. All members were present.

MINUTES OF NOVEMBER 19, 2009

Mr. Smith opened the floor for any proposed changes to the minutes of November 19, 2009. With no changes proposed, Ms. Falls moved to have the minutes of November 19, 2009 be approved, and Mr. Haffey seconded the motion. The motion passed with a 6-0 unanimous roll call vote.

REVIEW AND APPROVAL OF AGENDA

Mr. Smith asked for any proposed changes to the agenda. With no changes proposed, Mr. Price moved to have the agenda approved, and the motion was seconded by Mr. Caldwell. The motion passed with a 6-0 unanimous roll call vote.

NEW BUSINESS/ACTION ITEMS

1. **Passive Index Manager RFP Finalist Recommendation State Insurance Fund**

Mr. Bruce Dunn, Chief Investment Officer, presented the passive index manager RFP finalist recommendation for the State Insurance Fund (SIF). Mr. Dunn indicated this presentation marked the fourth consecutive monthly manager presentation in accordance with the RFP that was issued in July, 2009.

Mr. Dunn reported the SIF investment portfolio has a targeted twenty percent (20%) asset allocation to U.S. equities. Mr. Dunn noted in April 2009 the Board shifted the benchmark performance index from the Standard and Poor’s 500 Index (S & P 500) to the Russell 3000 Index (Russell 3000).

Mr. Dunn stated the Russell 3000 is not as large as the S& P 500 in terms of assets under management (AUM) by large passive asset managers. The Russell 3000 is growing in popularity because it represents 98% of the U.S. equity market, whereas the S & P 500 primarily contains large and some mid-capitalization equities. Thus, the Russell 3000 provided a much broader view of the U.S. equities market.

Mr. Dunn noted four investment firms were considered for passive index management of the U.S. equities allocation of the SIF: Barclays, Northern Trust Global Investments, Mellon Capital Management, and State Street Global Advisors. The firms were evaluated by the RFP Evaluation Committee. The evaluations concentrated on firms with experience in managing U.S. equities passively with the Russell 3000 as the base performance index. Mr. Dunn noted the Russell 3000 index does not always have 3000 stocks in the index, but the index would typically fluctuate by +/-100 stocks contained in the index during the course of a year. Mr. Dunn reported the Russell 3000 was a dynamic index with monthly rebalancing. Mr. Dunn also noted a Russell 3000 benchmarked portfolio would have smaller stocks incorporated with less liquidity than an S & P 500 benchmarked portfolio. Mr. Dunn said the investment firms selected had a proven track record with significant AUM. As required by the Investment Policy Statement (IPS), 20% of the approximately $17 billion in the SIF would be allocated to U.S. equities that are passively managed under the Russell 3000 index. The two investment firms selected would manage the assets under separate accounts. Mr. Dunn noted the firms should have experience with non-ERISA, non-security lending clients. These requirements, however, limit commingled funds being available to clients such as the Bureau. Mr. Dunn also indicated the investment firms had to be sensitive to the Bureau’s investment policy statement. Given there was large exposure with two of the firms considered on the fixed income side – Barclays and State Street– the Evaluation Committee focused the U.S. equities management to the other two firms.

Mr. Dunn then introduced the first of the two finalists for management of U.S. equities in the SIF, Northern Trust Global Investments (NTGI). NTGI had $200 billion in indexed equities AUM, with $115 billion of that being U.S. equities. Almost $275 billion of $600 billion of total firm AUM were managed passively using quantitative methods. NTGI is the third largest worldwide manger of passively managed assets for institutions. The firm has over thirty years experience in this field. NTGI was one of the first firms to passively manage to the S & P 500, and the firm has been passively index managing to the Russell 3000 for the past ten years. Mr. Dunn reported NTGI had $20 billion in AUM passively managed under the Russell 3000 or one of its component indices, the Russell 1000 or Russell 2000. Mr. Dunn said the Bureau has had previous positive experience with NTGI. The firm presently manages the Disabled Workers' Relief Fund (DWRF) and Coal Workers' Pneumoconiosis Fund (CWPF) for a total of $320 million in combined assets on a commingled basis. Further, up until last October, NTGI was managing $3.75 billion in SIF assets before a transition manager was appointed to manage the SIF equities investments to the Russell 3000 benchmark. During the two and one-half year history of managing these assets, Mr. Dunn reported NTGI had: a tight tracking error; been very responsive to the Bureau; and a dedicated staff to the Bureau's account. Mr. Dunn noted the same team, although now managing under the Russell 3000 instead of the S & P 500, would be in place at NTGI.

Mr. Dunn mentioned the RFP Evaluation Committee is recommending fourteen percent (14%) of the SIF be assigned to NTGI for passive management under the Russell 3000 index. The total AUM for NTGI under this recommendation would be approximately $2.45 billion. In terms of fee structure, Mr. Dunn noted the proposal was attractive because it was a flat fee and not sliding scale. The fee was 1.25 basis points (bp) of AUM per annum with a $50,000 annual minimum fee. Mr. Dunn said the minimum fee was academic as only $400 million was needed in the account for the minimum fee to be exceeded. With the recommendation of $2.45 billion of the SIF to be assigned to NTGI, the annual management fee is projected to be slightly over $300,000. Mr. Dunn noted the 1.25 bp fee structure was higher than the SIF S & P 500 management fee of NTGI, who had charged 0.75 bp. Given the proposed fee was only 0.50 bp higher with many more stocks to manage with varying lesser liquidity, Mr. Dunn believed NTGI's proposal was very competitive.

Guy Cooper and Jordan Nault of Mercer Consulting (Mercer) appeared before the Investment Committee. Ms. Nault confirmed Mercer supported the recommendation, and Mr. Cooper had sat in on the Evaluation Committee discussions regarding the recommendation. Ms. Nault reported there was only one litigation risk identified with NTGI concerning securities lending exposure. Ms. Nault reported NTGI was one of the first firms to admit this risk, and NTGI has put restrictions on funds facing this exposure while adamantly maintaining that the investor clients were treated fairly. Further, NTGI has placed $150 million in a collateral pool to support cash flows, and Ms. Nault believed NTGI was in a defendable position as the issue in litigation was fully revealed in the Northern Trust financial statements.

Ms. Falls noted State Street had similar issues, and inquired if NTGI had put this issue aside. Ms. Nault reported in the negative, but noted the likelihood of payout was less likely in NTGI's case. Mr. Dunn referred to his CIO Report comments on Northern Trust. He noted the parent of NTGI, Northern Trust Corp. (NT), had a 13% Tier One capital ratio, with $6.4 billion in Tier One capital. NT was AA rated, and although NT had accepted TARP funds, the funds were taken because of their low cost of capital, and NT had since returned these funds to the federal government. Mr. Dunn noted NT was truly a trust company and a wealth manager, and NT maintained a leading market share. Finally, Mr. Dunn reported NT had accounts with 25% of the Forbes' 500 wealthiest families, which demonstrated NT was a very well established and respected firm.

Three representatives from NTGI then appeared before the Investment Committee: Mr. Richard Clark, Team Leader of Public Funds; Mr. Chad Rakvin, Chartered Financial Analyst, Director of Global Equity Investment Management; and Mr. Brent Reeder, Team Leader of Domestic Equities. Mr. Clark is the primary relationship manager for NTGI's public clients. Mr. Clark reported great synergies had developed with his team and Mr. Dunn's team over the past two years. Mr. Clark noted NTGI understood the peculiarities of the Bureau's needs, not only to vendors but with access to information and transparency of what NTGI does "beneath the skin." The three NTGI representatives are part of the team handling the Bureau's account, and Mr. Clark reported there were others on the team in Chicago. The team has been consistently in place for the past two years.

Mr. Clark noted NT was a 100 year old company that had a global footprint. Mr. Clark noted 2008 and 2009 has redefined the investment arena, and cream has been rising. Mr. Clark believed NT was one of those firms who represent cream. Mr. Clark reported NT came through the debacle, and the situation is not over now, but NT was one of the standout firms through this challenging time period. Mr. Clark discussed the global scope of NT, and its investment processes and platforms. Mr. Clark noted a core principle of NT was to manage risk prudently and with transparency. Mr. Clark noted NT did accept TARP monies, but NT was one of the first firms to pay the TARP funds back to the federal government. Mr. Clark noted all metrics that a financial analyst would use to evaluate a financial services sector entity would show NT at the top. Mr. Clark concluded by reiterating the strong relationship between NTGI and the Bureau for the past two years.

Mr. Smith inquired if there were any lessons NTGI learned from securities lending in the past year. Mr. Rakvin replied the answer required examining what lending looks like when short term issues in the market place have collateral pools in some instances valued at less than par value. He noted a general shift going from securities lending to non-securities lending by clients. Mr. Rakvin noted he did not know how permanent this situation would be. Some of his clients have avoided securities lending risk in the past, and they will continue to avoid lending risk in the future. He believed a more intrinsic value model moving forward with collateral pools not looking like an enhanced cash fund as part of the solution. Mr. Rakvin did not know exactly how this one in one hundred year event will affect the market place long term. Ms. Falls inquired what kind of bp fees are associated with these collateral pools. Mr. Rakvin noted it depended on the asset class and percentage on loan. Large capitalization equities, for example, with ten percent (10%) available for lending, would be in the range of one to three bp. Mr. Rakvin noted fifty percent (50%) of the total return earned from securities lending is derived from managing the collateral pool, and 50% is generated from rebate fees with counterparty borrowers.

Mr. Rakvin provided a high level overview of NTGI. There were three key business units to NTGI: indexing, active fixed income management, and manager of managers businesses. Mr. Rakvin reported $270 billion is managed quantitatively, which includes fixed income assets and a taxation group. Approximately $115 billion in U.S. equities are managed quantitatively with an additional $76 billion in non-U.S. equities.

Mr. Rakvin noted there were twenty-four investment professionals who report to him globally on four different teams: U.S. Indexing in Chicago; Global Indexing teams in Chicago and London/Tokyo; and Global Quantitative Investment Strategy. U.S. Indexing has $160 billion AUM. The Chicago and London/Tokyo offices of Global Indexing deal with U.S. and non-U.S. clients, respectively. The Global Quantitative Investment Strategy team addresses benchmark issues and serves the other teams in an advisory role. NTGI’s investment professionals come from a wide variety of backgrounds, with portfolio managers having an average of over ten years experience. Mr. Rakvin stated there were numerous managers who have grown up in an indexing environment, some of the portfolio managers have spent their entire career at NTGI, and others have traded on the sell side. The investment professional mix provides a world class product for NTGI’s clients.

Mr. Rakvin stated NTGI's index investment philosophy has a core premise to minimize cost and maximize return and wealth of their clients. NTGI is not merely an account manager, but looks at every scenario to manage forward for their clients. Mr. Rakvin said one global principle is disciplined portfolio construction, and minimizing costs, which includes minimizing commissions, spreads and market impacts, but also using mathematical modeling to reduce risks.

Mr. Rakvin noted there were three steps to the NTGI investment process: portfolio construction; implementation, or how NTGI trades the portfolio or thought processes of when to trade; and risk management. The process' end goal is that the portfolio's volatility and return resemble the benchmark. All factors are examined in implementation, including liquidity of stocks. Illiquid stocks will cost the portfolio more money. For example, if a stock's average trading volume is only 1,000 shares per day, heavy buying will push the price higher. For that reason, Mr. Rakvin noted that a portfolio under their management may not own all Russell 3000 stocks, and the firm uses optimization techniques to determine which stocks to under-weight or over-weight. Typically, the firm tries to manage the portfolio to the benchmark to within three to five bps, and when the firm has to trade the portfolio, the firm wants to be sure it is not trading in illiquidity. All of these issues are contained within the implementation step of the investment process. For risk management, Mr. Rakvin noted NTGI uses risk models to evaluate risk at the sector, individual stock, and portfolio levels. These models are run at start of day, intraday and end-of-day.

Mr. Rakvin said Intelligent Indexing was NTGI's trademarked investment process, with an objective of minimizing wealth erosion and reducing total transaction costs. NTGI examines the expected trading impact of each transaction. For example, trading 1,000 shares of IBM would not move the market, but selling 10 million shares would. Those hidden costs are implemented into the trading strategy. Mr. Rakvin noted it is easy to trade stocks within a benchmark but lost in the analysis is the real wealth erosion by doing the trade. NTGI usually trades for liquidity, but NTGI also trades on index events. For example, the Russell 3000 annual reconstitution is the biggest trading event of the year. NTGI tries to predict how a stock will return based on average trading volatility, for example, but NTGI also considers major events such as a secondary offering of a company. Mr. Rakvin noted the goal of the portfolio is not holding every stock precisely weighted to the benchmark index; rather, guideline compliance examines how the portfolio is impacted.

Mr. Smith noted the representatives of NTGI present are presumably eligible for incentive compensation, and he inquired how that impacted the Bureau. Mr. Rakvin replied the employees are given incentive compensation based on the tracking error of the portfolios they manage; if their portfolios significantly outperformed benchmark indices, NTGI would most likely lose clients. Portfolio tracking error is the biggest focus in quantitative indexed portfolio management. NTGI bought American National Bank as well as the indexing business from Deutsche Bank in 2003. Although the operations are successful, one would not see in the background that integrating these businesses has been the challenge. At least one of these NTGI acquisitions was built off a series of platforms of other acquisitions. Hence, Mr. Rakvin noted he was also compensated for being an investment manager, but half also involved being a software manager. To be successful, NTGI has built a $5 million global investment platform launched in the past year. The platform automates much of the historical practices, so NTGI does not need to hire more investment managers. Overall, holistically this platform would seem to indicate layoffs, and there have been some, but there has been an increase in the net real business because indexing is an area of growth. Mr. Smith asked if the platform was making investments more automated, and Mr. Rakvin confirmed this statement.

During the course of his presentation, Mr. Rakvin had used the term "hobby" to reflect one of NTGI's business ventures. Mr. Harris inquired to the purpose of that statement. Mr. Rakvin responded NTGI did not enter the business with the intention of being a hobby. Mr. Rakvin expanded that Exchange Traded Funds, hereinafter referred to as "ETFs," was a business opportunity that NTGI entered in only a few years ago, which he noted was the worst possible time to do so. The ETFs were designed to mirror global market indices, such as the FTSE, as that was where the action was. However, the ETFs became an area losing money, and it would take a few years for the project to simply break even. Mr. Rakvin concluded the ETFs did not fit into the long term strategy of NTGI. Mr. Clark noted NTGI had not been active in that space, and NTGI's growth is typically done organically. Mr. Clark concluded NTGI realized that the ETFs were not providing a sufficient return on capital, and NTGI has exited that business

The three NTGI representatives then left the Investment Committee so that possible further discussion about NTGI and a vote on the Evaluation Committee recommendation could occur.

Ms. Falls moved that the Investment Committee recommend to the Board of Directors that it approve NTGI as a U.S. equities passive index manager for the State Insurance Fund, representing a targeted fourteen percent (14%) of the total State Insurance Fund assets, for the reasons set for in the presentation of the passive index manager RFP Evaluation Committee dated December 16, 2009, and the memorandum prepared by Mercer Investment Consultants dated December 14, 2009, and upon such terms as are outlined in NTGI's response to the request for proposals issued July 2, 2009 and such other items as are favorable to the Bureau. The motion was seconded by Mr. Haffey, and the motion passed by a 5-0 roll call vote, with Mr. Lhota not present.

2. Mercer Asset-Liability Modeling Report – Second Review Asset Allocation Modeling Recommendations of Mercer Consulting and Chief Investment Officer

Mr. Cooper and Ms. Nault of Mercer appeared before the Investment Committee to present the second review of the Mercer Asset Allocation Modeling Recommendations of the CWPF.

Mr. Cooper noted the CWPF provides benefits to injured workers under the Federal Coal Mine Health and Safety Act of 1969. Mr. Cooper said the fund contains separate assets and is run separately from the SIF. Assets of the CWPF as of June 30, 2009 are approximately $235 million, which is about 1/60th the size of the SIF. The CWPF funds approximately $65 million in liabilities under the current discount rate, which reflected an approximate $170 million of surplus. Mr. Cooper noted the surplus can only be used to fund the liabilities of the CWPF and for no other purpose. In light of this situation, Mr. Cooper noted the best approach to managing such a high surplus would be to pull back on investment risk to retain this funding advantage and not do anything to lose the advantage. However, the CWPF's volatility measures are presently high, so the Bureau should not be doing anything would allow for increased risk exposure.

According to Mr. Cooper, Mercer analyzed seven different options for the CWPF, identified as "Mix A" through "Mix G." "Mix A" was the status quo, and "Mix C" was the current mix of the SIF. "Mix B" was a reallocation of long term bonds to TIPS under the current asset allocation mix. "Mix D" through "Mix G" are variations of a theme of splitting equities between domestic and international equities and elimination of all long term bonds in favor of TIPS. "Mix D" and "Mix F" analyzed whether decreasing or increasing exposure to equities would significantly change the results, and without any significant change realized, these options were dropped from further consideration.

Mr. Cooper noted the status quo of the CWPF presently had a long term expected passive return of 5.9% with a standard deviation of 8.8%. In rough estimates, the standard deviation means in 2/3 of the years, the portfolio will return between +/- 8.8% around the expected 5.9% return or between -2.9% and 14.7%. However, the Percentage of Liability Interest Rate Risk Hedged (%LIRRH), is 292%. Mr. Cooper said this figure tracks how the portfolio of assets will track the portfolio of liabilities, and currently this figure indicates the CWPF is overly hedged. Industry standards have this figure at 80-100%, but no more than 100%. This was the reason to examine the various portfolio mixes. The 292% figure demonstrated the fund had more assets than needed, particularly more long duration bonds than were required; therefore, long term bonds in the CWPF were replaced with TIPS or reallocated to other shorter term duration bond vehicles.

Mr. Cooper did not recommend the Mix C, the SIF representative mix, in this case. While the average return would be higher with a slightly lower standard deviation, the %LIRRH for this portfolio mix only decreased slightly to 223%, which was still too high. Mix B was not recommended for the opposite reason; while transferring from long term corporate bonds almost kept the portfolio at the same passive rate of return with significant reduction in standard deviation, the %LIRRH was at 64%, or less than the targeted 80-100% range. The remaining two options were "Mix E" and "Mix G." Both had: similar splits equities to bonds; a split between domestic and international equities; no assets allocated to long term bonds; and similar expected passive rates of return with similar reduced standard deviation. The %LIRRH for "Mix E" and "Mix G" were 82% and 100%, respectively.

To further analyze the situation, Mr. Cooper discussed five different future economic scenarios over a ten year period: base case, stagflation, recession, inflationary growth, and ideal growth. Mr. Cooper said the current status was not that bad for the CWFP. In the most likely scenario, the funded ratio would be 455% ten years out, and in the worst case, stagflation, the funded ratio would be at 321%. Thus, even in the worst case, the CWFP would have $3 for every $1 needed in liabilities ten years from now.

Examining the proposed asset allocation mixes ten years out under the five different future economic scenarios, Mr. Cooper noted the status quo or "Mix A" was not unreasonable by any means, and "Mix C" provided a higher disparity of returns. With regard to "Mix E" and "Mix G," the results were again very similar noting the only difference was the balancing between bonds and TIPS. When compared to "Mix E," "Mix G" had a decreased exposure to TIPS, not as much protection to the funded ratio in high inflation scenarios, but improvement under the ideal scenario. Mr. Cooper, on behalf of Mercer Consulting, believed "Mix G" represented an improvement over the current investment strategy of the CWFP, noting the funded status volatility reduced due to elimination of long duration fixed income exposure and diversification of equity assets; increased allocation to TIPS makes sense; and fixed income allocation was well diversified between all categories.

Ms. Falls moved that the Investment Committee recommend to the Board of Directors that it approve revision of the asset allocation mix for the Coal Workers' Pneumoconiosis Fund to conform with "Mix G" as discussed in the Mercer Strategic Asset Allocation Analysis Report dated December 16, 2009, and the memorandum of the Chief Investment Officer dated December 16, 2009, and also that the Investment Committee recommend to the Board of Directors that it adopt relevant revisions to the Bureau's Statement of Investment Policy and Guidelines as they are set forth in the attachments to the Chief Investment Officer's Memorandum of December 10, 2009. The motion was seconded by Mr. Caldwell, and the motion passed with a 5-0 roll call vote, with Mr. Lhota not present.

Ms. Falls noted the Investment Committee did discuss and review the page for the new investment policy statement in the materials provided at the meeting today prior to voting on the above motion.

Mr. Haffey commented he liked the analysis presented by Mr. Cooper because it was not merely an X-ray but examined a long term approach. Mr. Haffey inquired to Mr. Dunn if the "Mix G" recommendation could be updated quarterly to see how the recommendation played out on a going forward basis. Mr. Dunn noted tracking would be done by Mercer Consulting, and updates of the CWPF will be provided, as well as all other funds in the Mercer quarterly performance report to the Investment Committee. Mr. Dunn noted Mercer provides information on what Mr. Haffey desired. Mr. Smith indicated the question could be held to see what Mercer provides. Mr. Dunn added he also supported the "Mix G" recommendation of Mercer Consulting, and a similar presentation will be done for the DWRF with asset allocation recommendations. Mr. Dunn noted the index manager RFP still had several months of active life. Proposals by investment managers are still being reviewed, and his department would like to move quickly on selection of investment managers for the specialty funds. Mr. Dunn did note that the SIF investment manager selection process has been largely completed at this time.

DISCUSSION ITEMS

1. **Disabled Workers' Relief Fund**

Mr. Raymond Mazzotta, Chief Operating Officer, discussed the DWRF. Mr. Mazzotta said the fund is currently being examined through funding ratios, investment objectives, and potential investment strategies. Input has been received from Legal, Investment, Actuarial and other departments.

Mr. Mazzotta reported one overarching recommendation was whether the specialty funds needed to be managed as separate funds, or combined into one fund with more flexibility and lower administrative costs. While the concept made sense, Mr. Mazzotta noted such a change would have to be done through legislative action. Mr. Mazzotta indicated this consolidation recommendation would not be proposed in 2010, but likely in 2011 with the next BWC biennial budget. Mr. Mazzotta indicated the Bureau had the internal capability to combine the funds now, especially with DWRF being a "pay as you go fund," and the practice is done with other state agencies. Mr. Mazzotta noted the CWPF was properly funded presently, and this fund could also change with the legislation.

Mr. Price expressed concern over combining the funds because of potential impacts of the availability of minorities and women to manage the investments. Mr. Dunn responded there would be no change in the approach to allowing opportunities to minority or women owned investment firms. The investment firms are provided funds based on asset levels, and if the consolidation is good for one fund, it should be good for all funds. Mr. Smith remarked the solution exists in addressing minority and women run investment firms will be when the funds switch from passive managers to active managers. Critical mass of passive managers is everything, and once the funds go to active management, the opportunities for minority run firms will increase. Mr. Dunn added that, by combining funds, the goal is for better overall fee structure. Small funds, by their nature, require payment of higher fees per dollar invested. Ms. Falls added that presently, there is the SIF and the individual specialty funds. If the funds are combined, the Bureau benefits from scale and diversification. The SIF and the specialty funds will have active managers eventually which will focus on minority managers as well as Ohio based firms. In her opinion, the combination of funds was a good positive path for the Bureau.

Mr. Cooper then appeared before the Investment Committee and presented the five asset allocation mixes that were being considered for the DWRF. "Mix A" was the status quo, and similar to the CWPF, had a 20%-80% ratio of equities to bonds, and a high percentage of long term duration corporate bonds. "Mix B" represented the asset allocation mix of the SIF presently, which provided a higher long term expected passive annual return than "Mix A," 6.6%, and a slightly lower standard deviation of 8.2%. "Mix C" was the asset allocation mix Mercer was leaning towards, which had the lowest standard deviation of 6.4% with a slightly higher long term expected passive annual return of 6.2%. Mr. Cooper noted if the objective pending was to consolidate the DWRF into other funds, then the DWRF may be better to analyze from an interim period and not long term.

Mr. Smith inquired if the DWRF should just mirror the SIF if the suggestion was to consolidate the funds. Mr. Dunn recommended being cautious and treating the fund separately until consolidated. Ms. Falls noted this action would be similar to the CWPF, with an eye to conservatism. Ms. Falls inquired if the Marine Fund could be brought in at this time for review. Mr. Mazzotta responded there was no reason why the Marine Fund could not be examined. Ms. Falls added this request was a recommendation from the Deloitte study. Mr. Cooper replied there would probably be two meetings before the recommendations were completed. Ms. Falls thought, since these allocation mixes were being done for other funds, the analysis may be easier than expected. Mr. Cooper asked if the Investment Committee wanted Mercer to model the projected liabilities. Mr. Dunn indicated he believed modeling the projected liabilities was important. Mr. Dunn wanted to know the projected liability stream for the smaller specialty funds before recommending any changes in investment asset allocation. Mr. Dunn noted the Marine Fund did not contain any equity investments, and all present fixed income investments in that fund had an average duration of only 3-4 years. Mr. Smith said more would be discussed about the Marine Fund in January. Mr. Cooper asked for clarification of what exactly was to be presented to the Investment Committee in January; he understood the final DWRF recommendation would be made at that time with more discussion on the Marine Fund. Mr. Smith concurred with Mr. Cooper's understanding.

2. Monthly and Fiscal Year to Date Portfolio Value Comparisons

Mr. Dunn presented the monthly and fiscal year to date portfolio comparisons.

Mr. Dunn noted investment income was $472 million (2.5%) for the month of November, representing a monthly return of 2.5%. Stocks increased by 5%, and bonds increased by 1.6%. Equities showed a $255 million net gain for November. Short term interest rates continued to be very low, and dropped a little further in November; overall, short-term interest rates were stable over the previous month. Mr. Dunn reported the spread between prime money market funds and government money market fund rates continued to narrow. In fact, Mr. Dunn noted more organizations are subsidizing money market funds because these funds are not profitable. The funds showed a very strong net investment income of $1.7 billion in the first five months, and a five month performance rate of +10%. Mr. Dunn reported the equities markets were a major driver with almost $2 billion of increased market value generated. Mr. Dunn noted part of the equity increase was caused by transitioning $1.2 billion from government bonds to international equities. The equities portfolio had a net return of 18.5% over the past five months.

3. Month-End Portfolio Asset Allocation Values

Mr. Dunn continued his presentation before the Investment Committee to present month-end portfolio asset allocation values. Mr. Dunn noted his focus would be on the SIF, and there was no transaction activity in the month of November. The equity valuation in the SIF increased from 29.2% to 30% in November. This increase was attributable to the outperformance of equities over bonds, again a 5% return in equities versus only 1.6% in bonds. In other words, Mr. Dunn reported the equity allocation went to the target SIF percentage of 30% solely on marketplace activity.

Mr. Dunn noted no asset allocation activity occurred last month because the fourth and final phase of transitioning into international equities was just completed this month when $425 million of Russell 3000 stocks were sold with proceeds moved into international equities. Mr. Dunn indicated all major transitions in the asset re-allocation of the SIF have now been completed, and the $425 million move from domestic equities to international equities was absolutely the right decision because the fund is right at the target allocation for equities at the present time.

Mr. Dunn noted for the month of December through December 15th, interest rates on both ten and thirty year U.S. Treasury bonds are up about 35 bp, and all bond indices are down this month. The SIF is presently showing a 2% decline on bond market value for the month of December with a 1.6% increase in equity market value for a total decrease in market value of $164 million for bonds and stocks. Mr. Dunn noted an overall calendar year to date return through November of Bureau invested assets of 9.6%, which included a modestly negative return for the months of January through June.

4. CIO Report – November 2009

Mr. Dunn presented the Chief Investment Officer Report for November 2009. Mr. Dunn reported it is his intention that $2.4 billion managed by Russell as Bureau transition manager for the US Aggregate benchmarked fixed income assets will be transferred by year’s end to State Street as the finalist target manager. While Russell had done a good job as the transition manager, it was important to transfer the funds to State Street which is now the designated manager.

The entire SIF long term government fixed income mandate is to be managed by Black Rock representing currently almost $1.3 billion in assets. Approximately $525 million of that portion of the portfolio is still managed by State Street, with the remaining approximately $750 million already managed by Black Rock. The remaining $525 million is expected to be transferred to Black Rock by month's end. The Legal Department is working on developing the necessary contracts to make the transfers possible.

Mr. Dunn also noted he and Ms. Lee Damsel, Director of Investments, had met with NTGI in Chicago and State Street in Boston last month to conduct on-site quarterly investment management review meetings.

Mr. Cooper of Mercer Consulting noted Mr. Dunn and his staff had overseen a number of extremely difficult transactions that went off without a hitch. Mr. Cooper personally commended Mr. Dunn and his staff for an excellent job.

5. Committee Calendar

Mr. Smith briefly discussed the Investment Committee calendar. For January, the proposed asset allocation model for the DWRF would be presented. Additionally the fiscal year 2009 annual custodian review will be presented; J.P. Morgan representatives will be present at the meeting. Finally, the second U.S. equities manager recommendation for SIF will be presented. Due to the January schedule, no educational training sessions will be held, but Mr. Smith has tentatively targeted the February through May meetings for some of these sessions.

Ms. Falls requested moving up in the calendar a review of the Self Insured Employers Guarantee Fund. Ms. Falls noted that fund has $54 million in assets currently returning almost nothing in money market accounts, and she was of the opinion changes may need to be done to increase that fund's performance. Mr. Smith concurred with Ms. Falls' request. There was also a discussion of adding placeholders in the February/March agendas for discussion of the Marine and Public Workers' Relief Funds.

ADJOURNMENT

Mr. Haffey moved to adjourn the meeting at 2:15 PM, seconded by Mr. Price. The meeting adjourned with a unanimous 6-0 roll call vote.

Prepared by Michael J. Sourek, Staff Counsel
December 22, 2009