

INVESTMENT ADVISORY COUNCIL  
Wednesday, March 9, 2016

**MEETING NO. 430**

**Members present:**

Joshua Hall  
David (Duke) Himmelreich  
Michael LeClair  
William Murray  
Carol Thomas, Interim Chair  
Peter Thor\*

**Absent:**

Thomas Fiore, representing Benjamin Barnes  
Michael Kramer  
Steven Muench  
Denise L. Nappier, Treasurer

**Others present:**

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

\*Arrival 9:09a.m.

**Guests:**

Tyler Christian, StepStone Group, LP  
MariLu Cleary, Morgan Stanley  
Michael Elio, StepStone Group, LP  
Will Greene, Loop Capital Markets  
Mark Johnson, Cliffwater LLC  
Robin Kaplan-Cho, Connecticut Education Association  
Pete Keliuotis, Cliffwater LLC  
Aditya Raina, StepStone Group, LP  
Matt Redeker, StepStone Group, LP  
Justin Rico Oyola, SEIU (Capital Stewardship Program)  
Claire Shaughnessy, AonHewitt Investment Consulting  
Liz Smith, Alliance Bernstein  
Diane Smola, AonHewitt Investment Consulting  
Michael Stark, The Townsend Group

With a quorum present, Interim Chair Carol Thomas called the Investment Advisory Council ("IAC") meeting to order at 9:02 a.m.

**Approval of Minutes of the January 13, 2016 IAC Meeting**

Chair Thomas called for a motion to approve the minutes of the January 13, 2016 IAC meeting. **William Murray moved to approve the minutes of the January 13, 2016 IAC meeting as drafted. The motion was seconded by Duke Himmelreich. There being no further discussion, the Chair called for the vote. The motion passed unanimously.**

**Comments by the Treasurer**

Richard Gray, Deputy Treasurer, provided the opening remarks in Treasurer Denise L. Nappier's absence and welcomed new IAC member Michael LeClair. Mr. LeClair then introduced himself and stated that he worked at Stifel as Senior Vice President of Investments and described his responsibilities. Mr. Gray then added that the Treasurer was attending Women in Private Equity conference in California and was receiving a lifetime achievement award.

**Update on the Market, the Connecticut Retirement Plans and Trust Funds Final Performance for Month Ended December 31, 2015 and January 31, 2016**

Deborah Spalding, Chief Investment Officer ("CIO"), announced that after giving consideration to the feedback from the IAC and to the due diligence process conducted by the investment staff and our general investment consultant, AonHewitt, Treasurer Nappier has decided to hire Ashmore Investment Management Ltd; Fidelity Institutional Asset Management; Payden & Rygel and Prudential Fixed Income for the Emerging Market Debt mandate, pending successful contract negotiations.

Ms. Spalding then provided an update on the capital market environment, its impact on the Connecticut Retirement Plans and Trust Funds ("CRPTF") performance and the economic outlook. She reported on the period ended December 31, 2015 for the pension plans, Teachers' Retirement Fund ("TERF"), the State Employees' Retirement Fund ("SERF") and the Municipal Employees' Retirement Fund ("MERF"). With respect to TERF, Ms. Spalding said that it returned 2.66% for the quarter; 61 basis points ("bps") under its customized benchmark. She stated that calendar year 2015 ended in positive territory up 0.97%, 102 bps ahead of its benchmark. Ms. Spalding said that SERF was up 2.58% for the quarter, underperforming its benchmark by 63 bps. In contrast, it ended calendar year 2015 up 0.95% versus the benchmark which was down 5 basis points. MERF was up 1.54% for the quarter underperforming the benchmark by 82 bps. However, it ended calendar year 2015 in positive territory, up 75 bps, versus its benchmark that was down 78 bps.

She then reported on the investment performance for the month ended January 31, 2016 for the TERF, the SERF and the MERF. Ms. Spalding stated that TERF was down 3.11% versus 3.47% for the benchmark; SERF was down -3.03% versus -3.44% for the benchmark and MERF was down -2.37% versus -2.87% for the benchmark.

Ms. Spalding then commented on the Watch List and said two managers have been added; Lazard Asset Management LLC, which manages a portion of Tier III of the Liquidity fund, was put on Watch due to underperformance. She continued that Aberdeen Asset Management, an

emerging market equity manager was added following a series of acquisitions by the company and concern about Aberdeen's management of its capacity and retention of key personnel as it continues its strategy of diversifying through acquisitions. Ms. Spalding stated that Grantham, Mayo, Van Otterloo & Company remained on the Watch List due to underperformance for the emerging market portfolio only.

Lastly, Ms. Spalding gave an overview of testimony made by Treasurer Nappier on two bills to the Appropriations Committee; An Act Concerning Principal Investment Officers of the Treasury that would bring them within the class of personnel approved by the State's Independent Investment Advisory Council. She added that if the bill was enacted it would give the Treasurer Nappier the ability to fulfill the principal fiduciary responsibilities for the State's pension and trust funds, and to meet the investment objectives and expectations associated with the safeguarding and management of fund assets. Ms. Spalding stated the second bill was An Act Concerning Establishing the Anticipated Rate of Return for Investments in State Retirement Plans that would transfer to the IAC the task of setting the investment return assumption that would apply to each of the State's pension plans in place of the current process of the investment return assumption being established by the coordination of State Employee Retirement Commission ("SERC"), Teachers' Retirement Board ("TRB"), the plans' actuaries and the Treasury's general investment consultant.

Next, Claire Shaughnessy, Partner, and Diane Smola, Senior Consultant, of AonHewitt Investment Consulting, reported on the Combined Investment Funds for the quarter ended December 31, 2015. Ms. Shaughnessy provided a market overview with comments on the economic highlights, public market global equities and fixed income markets. She added that the monetary policy divergence, dollar strength and lower oil prices equated to higher volatility moving forward.

Finally, Ms. Smola provided a summary of the returns for the plans and trusts within the CRPTF. She reviewed the performance attribution as of December 31, 2015 for the TERF, SERF and the MERF. Ms. Smola stated that for the FYTD, the plans did provide downside protection during the difficult market environment, with TERF and SERF outpacing their benchmarks by 50 bps and MERF outpacing its benchmark by 70 bps. Ms. Smola then provided a report on the Connecticut Horizon Fund ("CHF") as of December 31, 2015 and said that the CHF contributed returns of 3.9% and underperformed its benchmark by 60 bps during the first quarter net of fees; and that since inception there was an underperformance of 40 bps. Ms. Smola then gave an overview on the public markets, specifically diversity statistics and manager allocation.

### **Consideration for the Search Process for Legal Counsel and Services**

Catherine LaMarr, General Counsel, provided an overview for the search for legal counsel which included the project plan timeline and the screening/selection criteria for ten legal counsel and services assignments. She stated that the legal service agreements to the Combined Investment Fund ("CIF") are scheduled to expire at the end of November 2016 and she anticipated the retention of multiple law firms given the significant volume of work and the potential for legal conflicts. Ms. LaMarr stated that one of the services, Cybersecurity Counsel, was new to the

Office of the Treasurer and contracting for these services would assist this Office to access cyber risks and to address matters that may arise relative to cyber-attacks.

Mr. Murray and Peter Thor posed questions regarding cybersecurity counsel to which Ms. LaMarr answered to their satisfaction.

Chair Thomas called for a motion to endorse the legal counsel search. **A motion was made by Mr. Thor, seconded by Joshua Hall, to accept the project plan of the legal counsel search. There being no discussion, Chair Thomas put the question to a vote and the motion passed unanimously.**

### **Alternative Investment Fund Review as of December 31, 2015**

Ms. Spalding reported on the Alternative Investment Fund (“AIF”) for the quarter ended December 31, 2015. She introduced the AIF consultant to the CRPTF, Pete Keliuotis, Senior Managing Director and Mark Johnson, Senior Managing Director of Cliffwater LLC. Mr. Keliuotis began and gave an overview of the executive summary, portfolio overview, benchmark performance, portfolio investment activity and fund level performance.

He reported that as of December 31, 2015, the HFRI Fund Weighted and Fund-of-Funds Composite Index returned -1.1% and -.05%, respectively. He noted that the HFRI Fund Weighted Composite Index returned 0.72%, largely driven by equity long/short strategies and global macro strategies, which provided strong diversification benefits during the quarter. Mr. Keliuotis noted that the portfolio’s three-year annualized return of 7.25% continued to outpace the HFRI Fund-of-Funds Composite Index return of 5.38% as well as the Fund Weighted Composite Index return of 5.35%.

Next, Mr. Johnson commented on the AIF exposure to real assets and opportunistic investments and noted that the performance results were as of September, 30, 2015. He stated that the net IRR for the program performance since inception was 5.37%, ahead of its benchmark return of 3.08%. He remarked that \$20 million of capital was contributed to the partnerships in the third quarter and \$8.8 million of capital was distributed back to the CRPTF.

### **Private Investment Fund Review as of September 30, 2015**

Ms. Spalding reported on the Private Investment Fund (“PIF”) for the quarter ending September 30, 2015. She introduced the PIF consultant, Michael Elio, Partner of StepStone. Mr. Elio gave an overview of the portfolio overview and performance, market update and quarterly highlights. He stated that the PIF’s fund investments with vintages 2002 through 2014 have performed well, generating a net IRR of 12.1%. Mr. Elio reported that during the third quarter, September 30, 2015, the portfolio made \$103.4 million of contributions and received \$187.5 million of distributions, for a net cash inflow of \$84.1 million. He added that during this quarter, net of cash flow activity, the valuation of the portfolio had decreased by approximately \$19.9 million or 2.4% and was primarily driven by two buyout funds that decreased in value by \$22.0 and \$14.0 million, respectively. Mr. Elio then reviewed the portfolio diversification and stated that for the quarter ending September 30, 2015, it was primarily concentrated in funds targeting investments

in North America, which represented 94.6% of total exposure as of quarter-end, and that StepStone would be looking outside of North America for investments.

#### **Real Estate Fund Review as of September 30, 2015**

Ms. Spalding reported on the performance of the Real Estate Fund (“REF”) for the quarter ended September 30, 2015. She introduced the REF consultant to the CRPTF, Michael Stark, Associate of The Townsend Group. Mr. Stark gave an overview of the market and performance.

Mr. Stark remarked that the REF was 6.4% of the CIF quarter ended September 30, 2015 versus its target allocation of 7%, with \$605 million of unfunded commitments. He added that the core strategy was the highest contributor to the overall portfolio performance and contributed 95 bps to total net returns.

He reported that as of September 30, 2015, the REF returned 2.9% for the quarter, and 14.0%, 13.7% and 12.4% on a net of fee basis over the past 1, 3 and 5-year horizons, respectively. Mr. Stark added that it has been a consistent performance over the last five years and ten of the last 13 quarters, the CRPTF outperformed its benchmark on a net basis.

#### **Securities Lending Review of December 31, 2015**

Michael Sweeney, Vice President and Gustave Christakos, Assistant Vice President for Deutsche Bank, reported on Securities Lending activity ended for the quarter ended December 31, 2015. Mr. Sweeney provided an executive summary and discussed the intrinsic value lending strategy, and then reported fourth quarter securities lending returns of 9.32 bps, or \$3.5 million, net of fees, on the \$16.8 billion lendable portfolio. He also noted that \$1.45 million of those earnings were derived from lending activity and \$2.08 million was earned from reinvestment of collateral.

Mr. Sweeney stated that the highest demand was for domestic equities and that it resulted in \$2.07 million of total client earnings and that international equity was another strong contributor with earnings of \$607 thousand. He said that over 18% of the cash collateral was invested overnight, and the balance invested in maturities of up to three month with a weighted average maturity of 46 days. Mr. Sweeney added that all cash collateral was invested in indemnified repurchase agreements collateralized by readily liquid and marketable securities at values of 102% or greater.

Next, Mr. Sweeney discussed the market commentary and performance highlights.

#### **Short-Term Investment Fund Review as of December 31, 2015**

Michael Terry, Principal Investment Officer, reported on the performance of the Short Term Investment Fund (“STIF”) for the quarter ended December 31, 2015. Mr. Terry said the STIF earned an average annualized yield of 0.21% during the quarter, outperforming its benchmark by 14 bps, thereby earning an additional \$1.6 million for its state and local government investors. He stated that for the twelve month period ended December 31, 2015 the fund returned 0.17%,

outperforming its benchmark by 12 bps, thereby earning an additional \$6 million for investors. He noted that the fund's daily liquidity currently was 60% of assets; 77% of STIF's assets were invested in securities issued, insured or guaranteed by the U.S. government or federal agencies, in repurchase agreements backed by such securities, or in money funds comprised of such securities; and that its reserves totaled \$50.5 million.

**Other Business**

Chair Thomas invited the IAC members to submit agenda items for the April 13, 2016 IAC meeting.

**Comments by the Chair**

There being no further business, Chair Thomas called for a motion to adjourn the meeting. **Mr. Himmelreich moved to adjourn the meeting and the motion was seconded by Mr. Thor. There being no discussion, the meeting was adjourned at 11:08 a.m.**

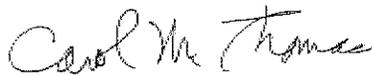
**This meeting was electronically recorded.**

Respectfully submitted,



**DENISE L. NAPPIER  
SECRETARY**

Reviewed by,



**CAROL THOMAS  
INTERIM CHAIR**