INVESTMENT ADVISORY COUNCIL
Wednesday, September 8, 2010

MEETING NO. 379

Members present:	Thomas Fiore, representing Brenda Sisco* Michael Freeman David (Duke) Himmelreich*** Stanley (Bud) Morten William Murray Denise L. Nappier, Treasurer**** Sharon Palmer David Roth Joseph (Joe) D. Roxe, Chairman Peter Thor**
Absent:	Thomas Barnes Carol Thomas
Others present:	Howard G. Rifkin, Deputy Treasurer Linda Hershman, Assistant Deputy Treasurer/Chief of Staff M. Timothy (Tim) Corbett, Chief Investment Officer Lee Ann Palladino, Deputy Chief Investment Officer Wayne Hypolite, Executive Assistant Adrian Kingshott, Principal Investment Officer Donald Kirshbaum, Investment Officer Catherine LaMarr, General Counsel Shelagh McClure, Director of Compliance Linda Tudan, Executive Assistant Lawrence Wilson, Assistant Treasurer-Cash Management Winifred (Winnie) Scalora, Administrative Assistant
Guests:	Bradley Atkins, Franklin Park Associates, LLC Joseph Barcic, Mercer Investment Consulting Scott Booth, The Townsend Group Maryellen Fazzino, Morgan Stanley Alternative Investment Partners Rui De Figueiredo, Morgan Stanley Alternative Investment Partners Sean Gill, NEPC Lisa Jones, Morgan Stanley Alternative Investment Partners Robin Kaplan-Cho, Connecticut Education Association Harvey Kelly, Leumas Advisors Alan Kosan, Rogerscasey Louis Laccavole, SOC Teachers' Retirement Board Kevin Norton, BNY Mellon Cynthia Steer, Rogerscasey Alex Thomson, Woodcreek Capital Management Adam Tosh, Rogerscasey

*** Arrived at 9:05 a.m.**
**** Arrived at 9:15 a.m.**
***** Arrived at 9:30 a.m.**
****** Left at 10:30 a.m.**

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With a quorum present, Chairman Joseph Roxe called the Investment Advisory Council ("IAC") meeting to order at 9:02 a.m.

Approval of Minutes of the August 11, 2010 IAC Meeting

Chairman Roxe asked for comments on the Minutes of the August 11, 2010 IAC meeting. **There being no comments, a motion was made by William Murray, seconded by Michael Freeman, that the Minutes of the August 11, 2010 IAC meeting be accepted as drafted. The motion was passed with the exceptions of Stanley Morten and Sharon Palmer who abstained due to their absence from the last meeting.**

Asset Allocation and Tail Risk Management Presentation

M. Timothy Corbett, Chief Investment Officer ("CIO"), provided opening remarks by commenting about his discussions with Chairman Roxe with respect to outside perspectives on asset allocation and tail risk management issues that were confronting other institutional investors in the wake of the "Great Recession". Mr. Corbett then introduced Rui de Figueiredo, Consultant, Portfolio Solutions and Hedge Fund Advisory Group for Morgan Stanley Alternative Investment Partners. He noted that Mr. Figueiredo's presentation, "Time for a Change: Dynamics of Investments and Asset Allocation," was timely with the upcoming asset allocation and liability study and the Connecticut Retirement Plans and Trust Funds' ("CRPTF") initial investment in hedge funds. Chairman Roxe commented about the importance of focusing on these issues and he welcomed Mr. Figueiredo to the IAC Meeting.

Mr. Figueiredo began by outlining the dynamics of asset allocation, the importance of the long-term investment horizon, and the impact of the most recent economic crisis on asset allocations of institutional investors. He further explained that traditional asset allocation fails to distinguish different sources of investment returns: those associated with market movements, ability to produce alpha and ensuring proper compensation for illiquid assets. Mr. Figueiredo said that asset allocation should be ongoing and dynamic because the characteristics of capital market assets change over time, for example due to changes in volatility and correlations. Treasurer Nappier questioned the historic volatility, over a 20-year period, which determined the likely probability of a return. Mr. Figueiredo responded that it was important to target an acceptable level of volatility, and the actual range of volatility should also be used to fine tune predictions of returns. Mr. Figueiredo continued that it was important to consider various horizons and not just look at long-term or short-term horizons and that the long-term should be a product of several short-term horizons.

David Roth asked if this was hedging based on the historical data. Mr. Figueiredo responded that historical data adds value, but it was just as important to balance various expected outcomes and sources of risks into the forecast process. Mr. Roth asked why this was different from traditional asset allocation. Mr. Figueiredo stated that the traditional approaches assumed exposure to the markets and remain constant risk factors.

In conclusion, Mr. Figueiredo reiterated two main points. He commented about the concept of expanding the traditional asset allocation process in terms of risk assessment and multiple time horizons. Finally, he said that assets needed to be actively allocated to three specific categories: Fundamental returns, also referred to as market beta; actively managed portfolio that generate alpha due to the skill set of the management team; and liquidity premiums.

Chairman Roxe posed questions about skewness and kurtosis, to which Mr. Figueiredo responded that negative skewness and high kurtosis predicted the likelihood of more tail risk events. Mr. Corbett said that next month's presentation would build on this discussion with an in-depth review of tail risk management.

Comments by the Treasurer

Treasurer Denise Nappier began her comments by reporting on decisions she had made since the August 11, 2010 IAC meeting after considering the feedback from the IAC, the recommendation of the CIO and the due diligence process performed by Pension Funds Management staff with the consultants. She stated that she had decided to make a $75 million commitment to Wellspring Capital Partners V, L.P., a Private Investment Fund ("PIF") opportunity that focuses on buyouts of mature, middle-market U.S. companies that are attractively valued. Treasurer Nappier reported that she had decided to also hire Frontier Capital Management Company, LLC as a preferred vendor for the small-mid cap ("SMID") growth manager mandate within the Mutual Equity Fund ("MEF"). She added that both hiring decisions were contingent upon successful contract negotiations. Treasurer Nappier said that the decision to hire additional SMID managers emanates from the MEF restructure and that the SMID growth strategy is one of three strategies to be utilized as part of the SMID construction. She noted that the core and value style managers would be presenting at an upcoming IAC meeting.

Treasurer Nappier then commented on her press release of August 26, 2010 regarding the recent Securities and Exchange Commission's ("SEC") approval of a rule on access to the proxy. She said that the SEC had taken a significant step in using its authority to adopt rules under which shareholders could nominate directors using the company's proxy. Treasurer Nappier added that electing the board of directors is the most important stock ownership right that shareholders enjoyed. She added that exercising this right could help put in place a board of directors able to recognize risks that could jeopardize long-term value, enhance a company's bottom line through prudent fiduciary oversight, and conduct business in the best interests of their shareholders. She also noted that the rule dictates that institutional investors must have at least 3% ownership and held the security for three years in order to gain access to the proxy. She concluded that it is imperative that long-term shareholders, such as the CRPTF, have the ability to choose their board representatives. Treasurer Nappier noted that this rule was partly the result of the efforts of the Office of the Treasurer in working for many important corporate governance reforms during the length of her administration, which helped to level the playing field in favor of shareholders' fundamental right to elect board members that serve the companies they own.

<u>Chief Investment Officer's Update on the Market, CRPTF Final Performance for the Month Ended July 31, 2010, Combined Investment Funds Review as of June 30, 2010, Watch List Update, Connecticut Horizon Fund Review for the Quarter Ended June 30, 2010 and Domestic Equity Brokerage Program Review</u>

Mr. Corbett began his remarks by providing an update on the capital market environment, its impact on the performance of the CRPTF and the economic outlook.

Mr. Corbett then reported on the performance for the CRPTF for the month ended July 31, 2010. He stated that the Combined Investment Fund ("CIF") increased 4.45% with pension fund assets at $22.8 billion for an increase of $0.9 billion for the month ended July 31, 2010, and that performance for the 2010 calendar year increased 2.3%.

Mr. Corbett then presented the overall investment results for the CIF for the quarter ended June 30, 2010. Joseph Barcic, Principal of Mercer Investment Consulting, Inc. ("Mercer"), provided additional comments on the CIF. Mr. Corbett reported that during Fiscal Year ("FY") 2010 every plan and trust outperformed its customized benchmark, and added that the three and five-year performances were a bit more mixed but generally positive.

Mr. Barcic then discussed the MEF's performance attribution. He said that the MEF was at a disadvantage over the last four years due to the fact that three of its long-standing money managers performed poorly during this time frame. In response to Mr. Roth, Mr. Barcic stated that Mercer's ratings were not performance driven but were tempered by performance, and he provided his subjective view of the MEF's money managers. Mr. Morten asked whether the CRPTF would have been better off net of fees had it indexed as opposed to choosing active managers. Mr. Corbett said that all of these managers had outperformed their index net of fees over the long term with one exception. He also agreed with Mr. Morten that it was important to understand where positive returns were generated and that they were associated with the managers' skill and not market exposure. Chairman Roxe added that indexing may have helped over the short run, and Mr. Barcic stated that two-thirds of the MEF was already index-like and that structure as well as manager selection were both important.

Mr. Corbett provided an update on the CRPTF Watch List as of June 30, 2010. He stated that AXA Rosenberg, which has two mandates, small-to-mid cap domestic equities and large cap core equities in a 130/30 active extension product, was terminated and that these assets were being transitioned to index products. Mr. Corbett said that Goodwin Capital Advisors, Inc. had been removed from watch because its investment team was stable and its performance had been consistently strong. He stated that BlackRock Investment Management LLC's ("BlackRock") Scientific Equity Risk Controlled mandate, formerly Barclays Global Investors' enhanced risk mandate, would be placed on watch due to its short-term and long-term performance and the significant changes within its organization and leadership. Finally, he reported that BlackRock's core fixed income mandate also remained on Watch due to key personnel changes and organizational investment process changes.

Mr. Corbett then presented a report on the Connecticut Horizon Fund ("CHF") for the quarter ended June 30, 2010. With respect to the public markets, he reported an underperformance relative to the CHF's benchmark of 37 basis points ("bps") and 54 bps, respectively, for the quarter ended June 30, 2010 and the trailing year; but stated that the CHF outperformed its benchmark by 54 bps and 55 bps, respectively for the trailing three years and since inception. Regarding the private equity portfolio within the CHF, he stated that the portfolio was still relatively young and there were no new fund commitments for the quarter ended June 30, 2010.

Finally, Mr. Corbett presented a report on the Domestic Equity Brokerage ("DEB") Program as of March 31, 2010. He stated that the program's share of total commissions improved to 44% and averaged 49% since inception, which was below the target of 60%; however, there was an improving trend and it was up 42%, 40% and 36%, respectively for the last three quarters of 2009.

Private Investment Fund Review as of March 31, 2010

Adrian Kingshott, Principal Investment Officer, reported on the PIF for the quarter ended March 31, 2010. Bradley Atkins, Chief Executive Officer of Franklin Park, provided additional comments on the PIF. Mr. Kingshott began by stating that the PIF's performance reflected the stabilization and marginal strengthening of market values within the portfolio and was up 4% for the quarter ended March 31, 2010, which followed a 6% increase in the prior quarter. He also reported that the PIF returned a net internal rate of return ("IRR") of 18.9%, 4.3% and 9%, respectively, for the one, three and five-year horizons. Mr. Kingshott also stated that during the last quarter of FY 2010, $80 million was invested and $100 million was distributed. He said that a recurring theme, as reported by general partners, was that a double-dip recession was not expected but slow growth would continue in a non-inflationary environment. Discussion ensued about the enormous amount of capital available to invest and the possible effect that would have on future acquisitions and merger market multiples.

In closing, Mr. Kingshott commented on middle-market deal flows and the steadily improving conditions for portfolio exits. Chairman Roxe posed questions about the multiples of EBITDA during different time frames. Mr. Kingshott noted the CRPTF would benefit from rising multiples because more of the PIF's capital was invested than committed and uninvested. He agreed with Chairman Roxe that the higher multiples raised a red flag for future investing and that it was important to select good managers.

Mr. Atkins commented that the amount of unfunded capital in the market was only an approximation and that most of the unspent capital was weighted towards the large mega buyout space where the PIF was underweighted. He stated that the pricing on average was less than 7 times EBITDA for the new private equity deals, but added that because there were so few deals being done this data was really not very meaningful. In closing, Mr. Atkins said that the current environment was allowing the CRPTF to buy deals at very compelling prices. Chairman Roxe commented that he had some concern about the multiples going up.

Real Estate Fund Review as of March 31, 2010

Lee Ann Palladino, Deputy CIO, provided a report on the REF for the quarter ended March 31, 2010. Scott Booth, Principal of The Townsend Group, first provided an overview of the real estate market in general, and said that during the quarter ended March 31, 2010 the real estate market showed signs of improvement. Mr. Booth reported that the performance of the CRPTF also reflected this improvement. He then provided additional examples reflecting the improved health in the public real estate market. With respect to the private real estate market, Mr. Booth stated that top-performing core funds currently were attracting capital to the space. He then commented about the current market conditions including the continued high unemployment rate, the availability of capital, and the percent of real estate with current values in excess of debt owed. Mr. Booth noted that he expected vacancies would continue rising in the short term but that the current condition was still opportunistic.

Mr. Roth posed a question about the REF's recent commitment of $50 million, and Ms. Palladino stated that she expected a 5% to 6% income return and an 8% to 10% total return. Chairman Roxe commented about the commercial real estate in the Northeast and noted that the banks were not foreclosing on distressed property and that foreign investors were supporting the prices of trophy properties.

Ms. Palladino then provided the performance results for the REF, and stated that for the quarter ended March 31, 2010, the REF increased 3.7%, which was positive for the first time in two years and also outperformed its benchmark. She then reviewed each strategy against more comparable benchmarks: core, value-add, and opportunistic. Ms. Palladino commented on the factors that caused the CRPTF to underperform its National Council for Real Estate Investment Fiduciaries ("NCREIF") benchmark over the longer-term horizon including the following: the NCREIF Property Index benchmark was unlevered whereas the CRPTF portfolios are levered; the lack of vintage year diversification especially during the 1999 to 2003 lucrative years for real estate performance; the 1998 underperforming legacy funds, which returned a net IRR of 5.5% versus 8.3% for the median; and the more recent young investments that were impacted by one of the greatest market declines in history.

Finally, Ms. Palladino commented about the U.S. Treasury's PPIP portfolio and noted that it was approaching its one-year anniversary. Overall, Ms. Palladino reported that the PPIP had drawn about 65% to 85% of committed capital with positive performance from about 85% non-agency residential mortgage backed securities and 15% commercial mortgage-backed securities, which helped mitigate some of the REF's market losses. She stated that the PPIP managers were all similar in their return requirements and that the initial expectations of 18% - 20% were being met.

In closing, Ms. Palladino discussed the Investment Policy Statement and its appendix compliance review for the REF and noted that two parameters: 1.) Separate accounts shall not exceed 20% of the target REF and 2) No single manager shall manage more than 25% of the market value of the REF, which were slightly above policy targets. In response to Mr. Roth's question, Ms. Palladino commented that when guidelines are out of compliance, the CRPTF can manage them back into compliance over a one to three-year horizon recognizing the illiquid nature of these REF vehicles. Mr. Booth provided additional comments about specific REF managers and noted that capital was pulled back during the economic downturn in 2008 and 2009 but managers had increased investments during the first two quarters of 2010, especially in distressed assets, which in turn was leading to increased value.

Short-Term Investment Fund Review as of June 30, 2010

Lawrence Wilson, Assistant Treasurer-Cash Management, reported on the performance of the Short-Term Investment Fund for the quarter ended June 30, 2010. Mr. Wilson reported that the STIF had an average annualized yield of 26 bps, 19 bps over its benchmark resulting in an additional $2.3 million for state and local governments invested in the STIF. He stated that for the 12-month period, the STIF had a return of 34 bps, 25 bps over its benchmark, resulting in an additional $11.9 million for state and local governments. Chairman Roxe complimented Mr. Wilson on the results and asked whether alternative benchmarks should also be considered.

Other Business

Mr. Corbett provided a report on the IAC expenses for the FY ended June 30, 2010.

Chairman Roxe invited IAC members to submit agenda items for the October 13, 2010 IAC meeting.

Comments by the Chairman

Chairman Roxe complimented Treasurer Nappier and the staff on the reports in today's meeting and said the IAC is looking forward to next month's in-depth review of tail risk management, a very important subject.

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

An audio tape of this meeting was recorded.

Respectfully submitted,

DENISE L. NAPPIER
SECRETARY

Reviewed by

JOSEPH D. ROXE
CHAIRMAN