

INVESTMENT ADVISORY COUNCIL
Wednesday, November 9, 2011

MEETING NO. 390

Members present:

Thomas Fiore, representing Benjamin Barnes
Michael Freeman
Laurence N. Hale
David (Duke) Himmelreich
William Murray
Sharon Palmer*
Joseph (Joe) D. Roxe, Chairman
Carol Thomas
Peter Thor

Absent:

Thomas Barnes
Stanley (Bud) Morten
Denise L. Nappier, Treasurer

Others present:

Jonathan Harris, Deputy Treasurer
Christine Shaw, Chief of Staff
Lee Ann Palladino, Interim Chief Investment Officer
Gary L. Carter, Interim Deputy Chief Investment Officer
Joanne Dombrosky, Principal Investment Officer
Gregory Franklin, Assistant Treasurer
Donald Kirshbaum, Investment Officer-Policy
Catherine LaMarr, General Counsel
Shelagh McClure, Director of Compliance
David Rivera, Director of Communications
Reginald Tucker, Investment Officer
Linda Tudan, Executive Assistant
Winifred (Winnie) Scalora, Administrative Assistant

Guests:

Jeanna Cullins, Hewitt EnnisKnupp, Inc.
Mary Dunleavy, State Street Bank & Trust
Will Greene, Loop Capital Markets
Alex Kamunya, NEPC, LLC
Harvey Kelly, Leumas Advisors
Louis Laccavole, SOC Teachers' Retirement Board
Kevin Norton, BNY Mellon
Kevin Vandolder, Hewitt EnnisKnupp, Inc.

With a quorum present, Chairman Joseph D. Roxe called the Investment Advisory Council ("IAC") meeting to order at 9:04 a.m.

* In at 9:20 a.m.

Approval of Minutes of the October 12, 2011 IAC Meeting

Chairman Roxe asked for comments on the Minutes of the October 12, 2011 IAC meeting. **There being no comments, a motion was made by Michael Freeman, seconded by Carol Thomas, that the Minutes of the October 12, 2011 IAC meeting be accepted as drafted. The motion was passed with the exceptions of Thomas Fiore, David Himmelreich and William Murray who abstained due to their absence from the last meeting.**

Chief Investment Officer's Update on the Market and Connecticut Retirement Plans and Trust Funds Final Performance for the Quarter Ended September 30, 2011

Lee Ann Palladino, Interim Chief Investment Officer ("CIO"), announced that Treasurer Nappier had decided to select Hewitt EnnisKnupp, Inc. as the preferred vendor for the risk management mandate to the Connecticut Retirement Plans and Trust Funds ("CRPTF"), contingent upon successful contract negotiations.

Ms. Palladino continued the dialogue on the Asset/Liability Study by stating that the CRPTF is faced with three macro themes that may impact the asset allocation over the next market cycle: 1) the continued deleveraging of the developed markets; 2) investment in a low interest rate environment; and 3) the growth of the emerging markets. She commented on these themes in terms of their impact on global growth, the outlook for return over the next five to seven years, and how the themes may impact the upcoming Asset/Liability Study. Ms. Palladino then gave an update on key strategic questions that were being pursued as part of the Asset/Liability Study: 1) the ability to provide liquidity to meet the retirees' payroll; 2) assessment of the liabilities; 3) risk tolerance; and 4) capital market returns.

In response to Chairman Roxe's statement regarding the timeline for the completion of the Asset/Liability Study, Ms. Palladino stated that preparation for the first meeting of the Asset Allocation Sub-committee was almost complete. Further, Ms. Thomas stated that as Chair of the committee, her preference was to first conduct the study on each of the Trusts. Discussion ensued among the IAC members regarding the education of the legislators on the status of liabilities to the low funded level of the State Employees' Retirement Fund ("SERF"); the disconnect between the establishment of the earnings objectives for the Teachers' Retirement Fund ("TERF") and SERF at 8.5% and 8.25%, respectively; market returns and the process for conducting an Asset/Liability Study. Chairman Roxe stressed the importance of scheduling frequent meetings in order to get the study completed in a short period of time.

Ms. Palladino next reported on the performance for the CRPTF for the quarter ended September 30, 2011. She stated that during the month and quarter ended September 30, 2011, TERF returned negative 5.57% and 10.25%, respectively; and SERF returned negative 5.63% and 10.41%, respectively. Ms. Palladino stated that due to the easing of the European debt crises concerns during October 2011, there was a rebound of the global equity markets and that the projected loss was about 4% fiscal year-to-date.

Chairman Roxe stated that this had been a very choppy market, but added that by being diversified some of the downside was ameliorated.

Update on the Cash Flow Report for the Teachers' Retirement Fund and State Employees' Retirement Fund

Gary Carter, Interim Deputy CIO, presented the Cash Flow Report projections for Fiscal Year ("FY") 2012 for the TERF and SERF, and provided an update on actual cash flows for FY 2011. Mr. Carter noted that cash flow had been one of the key elements taken into consideration in setting the structure for the investment portfolio. He reported that the actual cash needed for FY 2011 was less than what was projected. Mr. Carter stated that the favorable variance was primarily attributable to the lower than projected capital calls of \$285.6 million actual versus \$410.4 million projected for the Real Estate Fund ("REF") and greater than projected distributions calls at \$477.6 million actual versus \$199.0 million projected from the Private Investment Fund. He stated that actual employer and employee contributions as well as projected benefit payments were very close to the 2011 projections for both SERF and TERF. Mr. Carter reported that Liquidity Fund balances met targeted levels.

Relative to FY 2012, Mr. Carter reported that cash from employee and employer contributions and investment income was projected to cover approximately 82% and 95% of TERF and SERF benefit payments, respectively. He added that the anticipated cash deficits in FY 2012 were projected at about \$319 million and \$89 million for TERF and SERF, respectively, and he noted that both were decreases from actual deficits realized in FY 2011. Mr. Carter said that the FY 2012 projections indicated that employer contributions would increase by about \$176 million and \$180.4 million for TERF and SERF, respectively; and at this point there were no projected material changes relative to employee contributions or benefit payments.

Chairman Roxe stated that during FYs 2011 and 2012 cash from employee and employer contributions falls short by about \$1 billion in order to meet the pension retirement payrolls. He said that liquidating 5% of the portfolio in a down market to meet that shortfall at a time when both portfolios are substantially underfunded is a serious problem. Mr. Freeman noted that Treasurer Nappier shared these concerns over the course of her administration, and had incorporated cash requirements into the investment strategy and asset allocation studies. Mr. Fiore stated that the SEBAC agreement of August 2011 would result in projected budget savings in FY 2012 and 2013, but would likely result in lower contributions to the SERF. Mr. Murray added that while cash flow deficits were known for the last five to seven years, the economic downturn had worsened the situation. Chairman Roxe agreed that the negative cash flow outlook cannot be ignored and noted that it was important to address this issue.

Approval of Treasurer's Adopted Revisions to the Investment Policy Statement Appendix

Ms. Palladino presented Treasurer Nappier's adopted revisions to the Investment Policy Statement ("IPS") Appendix A, Section II, and Appendix B, Section I, for consideration of approval by the IAC. She noted that Treasurer Nappier had accepted the input from the IAC relative to the currency hedging strategies. Regarding the request to modify or delete some of the policy ranges with regard to the REF property type and geography and associated with the REF's benchmark, the National Council of Real Estate Investment Fiduciaries, Ms. Palladino stated that Treasurer Nappier had decided to not include those modifications. She then explained how the current language supported the real estate program and should be included until such time as a thorough evaluation could assess other options. Ms.

Palladino also noted that the modifications to Appendix B, Section I, had not changed from the draft version that was presented at the October 12, 2011 IAC Meeting.

Chairman Roxe clarified that Treasurer Nappier did not want to consider changing the benchmarks to real estate at this time, but would consider changing the benchmark for the REF or any of the other benchmarks during the Asset Allocation Study with the appropriate due diligence.

Chairman Roxe then asked for a motion to approve the Treasurer's adopted revisions to the IPS Appendix A, Section II and Appendix B, Section I, as amended. Mr. Himmelreich entered a motion to approve these amendments. Ms. Thomas seconded the motion. The motion was passed unanimously to approve the amendments to the Appendix of the IPS as adopted by Treasurer Nappier.

Comments by the Chairman

Chairman Roxe commented that the discussion on the Asset/Liability Study was beneficial. Further, he reiterated his concerns regarding cash flow and the objective to meet the pension retirement payrolls.

Executive Session

A motion was made by Mr. Freeman, seconded by Laurence Hale that the Investment Advisory Council adjourn the Regular Session at 10:15 a.m. and enter into Executive Session to consider an employment matter. The motion was passed unanimously. Deputy Treasurer Jonathan Harris participated in the Executive Session.

The Investment Advisory Council adjourned the Executive Session at 10:25 and entered into Regular Session.

Chairman Roxe noted that no votes were taken during the Executive Session.

Deputy Treasurer Harris presented Treasurer Nappier's recommendation to appoint Lee Ann Palladino as Chief Investment Officer, and he asked that the IAC consider approving her recommendation.

Chairman Roxe asked for a motion to approve the recommendation of the appointment of Lee Ann Palladino as Chief Investment Officer for the Connecticut Retirement Plans and Trust Funds. Mr. Himmelreich entered a motion to approve the recommendation. Ms. Thomas seconded the motion. The motion was passed unanimously.

Chairman Roxe and the IAC congratulated Ms. Palladino on her appointment. Ms. Palladino stated that she was honored that Treasurer Nappier recommended her to fill the CIO position and she thanked the IAC for their unanimous approval of her appointment.

Other Business

Chairman Roxe invited IAC members to submit agenda items for the December 14, 2011 IAC

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meeting. He then commented on the updated IAC Committee Assignments. Chairman Roxe noted that the updated IAC Committee Assignments were accepted by the members.

Deputy Treasurer Harris then announced that the Office of the Treasurer had won its appeal before the District Court in the Southern District of California against Amgen Inc. regarding the Securities Litigation in a class action matter. Deputy Treasurer Harris, Chairman Roxe and the IAC members congratulated Catherine LaMarr, General Counsel, for her excellent work.

There being no further business, the meeting was adjourned at 10:35.

This meeting was recorded on audio tape.

Respectfully submitted,



JONATHAN A. HARRIS, DEPUTY TREASURER

for

DENISE L. NAPPIER, SECRETARY

Reviewed by



JOSEPH D. ROXE
CHAIRMAN