State of Alaska
ALASKA RETIREMENT MANAGEMENT BOARD
Meeting

Location
Fairbanks Princess Hotel
4477 Pikes Landing Road
Fairbanks, Alaska

MINUTES OF
September 20-21, 2012

Thursday, September 20, 2012

CALL TO ORDER

CHAIR GAIL SCHUBERT called the meeting of the Alaska Retirement Management Board (ARMB) to order at 9:00 a.m.

ROLL CALL

Nine ARMB Trustees were present at roll call to form a quorum.

Board Members Present
Gail Schubert, *Chair*
Sam Trivette, *Vice Chair*
Gayle Harbo, *Secretary*
Kristin Erchinger
Commissioner Becky Hultberg
Martin Pihl
Tom Brice
Sandi Ryan
Commissioner Butcher

Board Members Absent
None

Investment Advisory Council Members Present
Dr. William Jennings
Dr. Jerrold Mitchell
George Wilson

Department of Revenue Staff Present
Angela Rodell, Deputy Commissioner
Gary M. Bader, Chief Investment Officer
Pamela Leary, State Comptroller

Zach Hanna, State Investment Officer
Steve Sikes, State Investment Officer
Scott Jones, Asst. State Comptroller
Judy Hall, Board Liaison

Department of Administration Staff Present
Jim Puckett, Director, Division of Retirement & Benefits

Consultants, Invited Participants, and Others Present
Robert Johnson, ARMB Legal Counsel
Michael O'Leary, Callan Associates, Inc.
Jennifer Young, Townsend Group
Jeff Maguire, UBS
Tom Anathan, UBS
Anne Pfeiffer, JP Morgan
Ann Cole, JP Morgan
George Duke, LaSalle
Steve Bolen, LaSalle
Arvin Soh, Global Asset Management
Kathryn Cicoletti, Global Asset Management
Doug Bratton, Crestline Investors, Inc.
Sam Levens, Crestline Investors, Inc.
Jim Cunnane, FAMCO
Trish Oppeau, FAMCO
Yves Siegel, Neuberger Berman
Mark Sullivan, Neuberger Berman
Douglas Rachlin, Neuberger Berman
Abel Mojica, Tortoise Capital Advisors
Matt Sallee, Tortoise Capital Advisors

PUBLIC MEETING NOTICE

JUDY HALL confirmed that public meeting notice requirements had been met.

APPROVAL OF AGENDA

MS. HARBO moved to approve the agenda. Mr. Brice seconded the motion.

MR. BADER requested deletion of item B-1, No. 5 under item 14 because Mr. Mitchell could not be present due to aircraft problems and deferred the item to the December meeting.

The agenda was approved as corrected.

PUBLIC/MEMBER PARTICIPATION, COMMUNICATIONS AND APPEARANCES

RON JOHNSON, a retiree from the UAF School of Engineering, addressed his concerns regarding building a sustainable world and the sustainability of the PERS and TRS and other state retirement funds. He commended the board for voting four-to-three to move from a level percent to a level dollar pay down of the $11 billion dollar-plus liability. He addressed the liability and discount rates. He urged the board to deal with this unfunded liability issue and try to create a situation where people who are newly hired who might eventually go on a defined benefit plan. He thanked the Trustees for their service.

APPROVAL OF MINUTES

MR. TRIVETTE moved to approve the minutes of the June 21-22, 2012 meeting, as presented. MS. HARBO seconded the motion.

The minutes were approved without changes.

REPORTS

1. CHAIR REPORT

CHAIR SCHUBERT reported two new Trustees joined the ARMB: Sandi Ryan, TRS Representative, and Tom Brice, the PERS Representative.

MS. RYAN and MR. BRICE introduced themselves to the board.

2. COMMITTEE REPORTS

MR. PIHL reported that the Audit Committee met on September 19, 2012, and the meeting was well-attended. The main topic of the meeting was the update by KPMG on the audit. The audit has gone very well. There has been excellent preparation by the State, full cooperation. Everything seems to be clean and expected. There are a few items to wrap up. The Committee has been receiving the monthly compliance reports from the Department of Revenue. There have been no significant findings in those reports.

Upcoming over the next two to three years, there are two GASB regulations coming, one of which has far-reaching implications on the unfunded liability and disclosures required in financial statements. It will be of interest over the next couple years.

MR. PIHL reported that the Salary Review Committee met on September 19, 2012, and the meeting was well-attended. The main item was an update on the compensation program by Pam Leary. It covered the merit, COLA, and geographic increases over the last year. There is expected to be the regular December 1, 2012 increases, and there will be follow-up on that. Discussions and suggestions were made on how the system works and how it might work better.

CHAIR SCHUBERT reported that the Budget Committee met on September 19, 2012, and discussion was had about the budget, to ensure that there is sufficient money in the budget to cover salaries and manager fees, if the market improves.

MR. TRIVETTE further reported there is additional money in the budget, and there are a couple of issues that the committee needs to make sure there is sufficient money there if they came up, and there are several possibilities such as pension obligation bonds being discussed.

MS. ERCHINGER reported that the Real Assets Committee met on September 19, 2012, and had two presentations on the Real Assets Annual Plan for FY13 and a review by Townsend on the real estate plan. Real assets make up $2.6 billion of the ARMB portfolio. In an action item, the board is going to be asked to adopt the Real Assets Annual Plan, and there will be a number of actions to take relative to implementing the report recommendations from IFS. Two resolutions and three motions will need to be approved during this meeting.

MR. TRIVETTE reported the Defined Contribution Plan Committee met on September 19, 2012, and three 50-minute presentations were made by Prudential, T.Rowe Price and Great-West. They primarily talked about a guaranteed minimum withdrawal of benefits. An item of interest is that it’s an evolving field and not many participants of these three companies are using that option at this point in time. The committee will continue to work with Retirement & Benefits on this topic. Additional research will be done, including work with Callan and some of our Investment Advisory Council members. The committee will then get back together after the first of the year for further discussion.

CHAIR SCHUBERT reported the Legislative Committee met on September 19, 2012, and she was elected Chair. It was an organizational meeting to review and approve a charter. The Legislative Committee approved a recommendation to the board for approval of the charter.

<u>CHAIR SCHUBERT moved the approval of the charter for the Legislative Committee</u>. <u>MR. PIHL seconded the motion</u>.

Without objection, the motion was approved.

3. RETIREMENT & BENEFITS DIVISION REPORT

DIRECTOR PUCKETT reported there was nothing unusual in the statistics. The Division is on track to do another 2,100 retirements this year.

MR. TRIVETTE pointed out, in terms of PERS and TRS, the numbers of terminating members is over 6,000 and that they were paid in excess of $838,000 for nine months. DIRECTOR PUCKETT stated both numbers are correct. MRS. HARBO noted another 1,600 people withdrew about over $14 million.

DIRECTOR PUCKETT reported there was a total of almost $45,000 worth of studies and work done with the Defined Contribution Retirement Health Plan of which the board got a summary of from Deputy Commissioner Barnhill in the last meeting. It is anticipated there will be additional studies for that retiree health plan by the next meeting.

MS. ERCHINGER asked how the decision is made who will be charged for the legislative review work done by Buck and when those charges will be assessed to the retirement plans versus when the Legislature or the General Fund will pay a portion.

DIRECTOR PUCKETT responded that Deputy Commissioner Barnhill will make the determination of whether it is paid by General Funds or the retirement fund.

4. TREASURY DIVISION REPORT

Department of Revenue Deputy Commissioner ANGELA RODELL reported the proposed fiscal year 2014 budget was recommended by the Budget Committee. The total is approximately $47 million. It would be included in the Department of Revenue budget that goes before the Legislature.

CHAIR SCHUBERT reported the Budget Committee took action on the proposed budget on September 19, 2012 and passed a motion to recommend that the board adopt the budget.

<u>CHAIR SCHUBERT moved that the board adopt the fiscal year 2014 budget</u>. <u>MR. TRIVETTE seconded the motion</u>.

MS. ERCHINGER questioned how costs associated with utilization of the actuary will be borne and expressed concern that they not be borne by the participants of the retirement system and requested that should be a consideration in the budget.

Deputy Commissioner ANGELA RODELL responded costs of the actuarial amounts are shared with the Department of Administration. To the extent that needs to increase, there is room in the budget, so any required Buck invoices should be covered.

The motion passed unanimously. 9-0.

5. CHIEF INVESTMENT OFFICER REPORT

MR. BADER reported the first item is to rebalance all retirement funds closer to strategic asset allocation. Four rebalancings have taken place between when we reported at the last meeting. Items one and two are those types of transactions. Item three relates to the termination of Capital International in the emerging market fund, the first step in the beginning of that termination. The fourth and fifth items are to rebalance funds. On the sixth item, move $250 million from short-term fixed income to the U.S. Treasury fixed income pool. The last item relates to placing Brandes Investment Partners on the watch list for performance.

<u>MS. HARBO moved to place Brandes Investment Partners on the watch list</u>. <u>MS. RYAN seconded the motion</u>.

MR. TRIVETTE asked why Brandes should be placed on the watch list. MR. BADER responded Brandes has underperformed for three years.

The motion passed unanimously.

6. FUND FINANCIAL REPORT

Comptroller PAMELA LEARY presented a report for invested assets for the month ending July 31st. The total, as of July 31st, of invested assets is $20.5 billion, broken out between the assets that are directly managed by the portfolio group of 16.8 billion and those directed by participants of 3.6 billion. Ending assets were $11.9 billion for PERS, $5 billion for TRS. Judicial was $131 million, and the National Guard Naval Militia was $32.8 million. The supplemental annuity plan ended July with $2.6 billion, and deferred compensation with $619.5 million.

The $20.5 billion has increased to $20.7 billion, and with the 16.9 billion of the non-participant directed funds, that has grown from $16.9 billion to $17.5 billion, so a 7.5% increase for those assets over the two-and-a-half months.

DIRECTOR PUCKETT reported State of Alaska contributions down at $613 million. This is the annual on-behalf contributions, and they were received by the State in July. The National Guard and Naval Militia Reserves Retirement System info was not entered until August. Under TRS and the DC, there is a sizable withdrawal, which includes the employer and the employee contribution to the individual accounts. This is dependent on the years that the members have worked, and this is due to a seasonal variation. Many of the teachers were cashing out their plans at the end of the school year, and it reflected in this over $1 million withdrawal.

MS. HARBO requested the report for the end of last fiscal year with the figures for the year ending FY12, which DIRECTOR PUCKETT will provide.

CHAIR SCHUBERT thanked the presenters for their reports and recessed the meeting from 9:42 a.m. to 9:48 a.m.

7. BUSINESS AND STOCK MARKET CYCLES

MR. BADER reported on the watch list. When looking at it from peak-to-peak or trough-to-trough, using either of those two methodologies and looking over the entire 168-year period, the average economic cycle was about 56 months or about 47 years. There is a strong relationship between returns in the stock market and the business market cycle.

MR. PIHL AND MR. O'LEARY questioned the 2007-2008 business cycles.

MR. BADER pointed out that the economic cycles have taken longer and longer. So the current could go on for several years, if it follows the trends of the past.

MR. BADER noted Mr. Sikes will present on IFS recommendations and touch on the topic of the three-year versus a six-year period that is being recommended for a change in quantitative measures. Greater emphasis should be placed on the qualitative considerations in a manager than on the quantitative in the short run.

CHAIR SCHUBERT commented on the Ark termination in the mid-'90s. MR. O'LEARY noted they are no longer in business.

MS. HARBO mentioned that Tukman had seven stocks in their portfolio; MR. BADER confirmed 13.

MR. TRIVETTE cautioned careful integration of this knowledge into the system moving forward.

8. REAL ASSETS

A. Real Assets FY13 Annual Plan
Real Estate Guidelines, Policies and Procedures

State Investment Officer STEVE SIKES presented the Fiscal Year 2013 Real Assets Plan. The main recommendation is a recommendation to allocate an additional $200 million to the timberland managers and then some fine-tuning around target the board has adopted.

As of June 30, 2012, the real assets portfolio was 16.6% of ARMB's total portfolio. The majority of that was in real estate at 9.3%. The next largest component was farmland at 4%, then timberland at 1.4%, TIPS at 1.2%, and energy at 0.7%.

The strategy is a lower risk/lower return approach using low leverage, focusing on higher quality assets with stable returns. In terms of the return expectation, the goal is to achieve a 5% net real return over rolling five-year periods and custom benchmarks also employed to evaluate the component performance.

A blended benchmark is used to evaluate the performance, which is 60% NCREIF property index, which is the main private real estate index, then 10% NCREIF farmland index, 10% timberland, and 20% TIPS. The structure of the portfolio is primarily in private illiquid assets requiring long-term hold periods. The exception is, in the real estate portfolio, there is a REIT portfolio, which is a public stock portfolio managed internally, and then the U.S. TIPS portfolio, which is managed by the fixed income group.

In terms of the investments, discretionary authority is given to the board's managers to select the investments and manage the investments.

MS. ERCHINGER questioned the rationale of the use of the benchmark; MR. SIKES responded regarding inflation hedging.

MR. SIKES reported real estate currently dominates at about 56% of the real assets portfolio. Real estate was the first asset class of these the board invested in and so it's the largest. Timberland is the most recent addition to the program, which was started in 2000 or 2008. The most meaningful differences are real estate being about 20% over the target and then timberland being about 16% under the target. The board will be able to achieve these targets over the next five years.

Last year was at 10.36%, below the target benchmark of 11.41%, mainly due to a lower return from real estate and then also a strong return from the TIPS portfolio, which, at 20% of the target, is higher than the actual allocation in the portfolio. The three-year return is very close to the target at 8.23%. The real estate numbers reflect the poor performance experienced during the credit crisis and recession. The farmland numbers are fantastic, five-year annualized return at 10.24% and so that program continues to do very well.

The primary component of the real estate is the core strategy, which is 62% of the portfolio. That returned 11% net for the fiscal year, 12% NCREIF property index.

In terms of transactions, there was one sale by Cornerstone Real Estate Advisors and no acquisitions. The non-core portfolio returned 3.1% net during the fiscal year.

The core structure is four separate accounts and two open-ended funds; the non-core structure is 14 commingled funds and the remaining separate account allocations.

The farmland portfolio was 15.2% net for the fiscal year, which underperformed the benchmark return, which was 17.9%. The board's target is 80% row crop, which the annual plant cycle, and 20% permanent, which is trees and vines type of products and are close to those targets at 81.6% row and 18.4% permanent. Corn is the largest crop type on the row side of things at 22%. There is not expected to be a significant impact on the returns of the farmland portfolio because of the drought.

MS. HARBO commented on not being affected by drought, and MR. SIKES confirmed. An overview of the portfolio is $645 million invested, 92 properties, just over 162,000 acres. The board has two separate account managers, UBS Agrivest and Hancock, and the remaining allocation is $91 million.

The timberland portfolio returned 5.1% net for the fiscal year, which outperformed the benchmark return of 1.1%.

The energy portfolio is unique in that it reflects the investments with EIG Global Energy Partners, formerly TCW and it's not designed to hold all of the board's energy investments. The value of that portfolio was just under $116 million as of June 30.

The TIPS portfolio was valued just under $200 million as of June 30, 2012, managed internally by the Fixed Income Group.

The allocation is very close to the target, 16.6%, but 20% overweight real estate, underweight timberland, 16.5%. The board also has targets around the core and non-core mix, which are relatively close. The target there is 75/25, which is currently at 70/30.

The board established a private real estate mix compared to the public real estate mix at 90% private/10% public, the public being the REIT portfolio, and the portfolio is very close to those targets. The timberland allocation is never expected to get close to its current target of 25%.

MR. SIKES reported the recommendations in this year's plan. At the real assets overall level, no recommended changes to the constituents or the target allocations. For real estate, new allocations or commitments to the funds are not recommended. Continue with the strategy of investing in entry markets and encouraging advisors to sell non-strategic assets and improve the quality of the income stability of those portfolios. No changes to the REIT portfolio strategy or allocation are recommended. A band of plus or minus 10% is recommended to be established around the 90%/10% mix target.

For the non-core funds, offerings in the marketplace will continue to be evaluated, but no commitments are expected. The one recommendation here is to modify the bands, which are currently plus or minus 10% to plus or minus 25% to allow the non-core portfolio to go to zero, if no compelling future opportunities.

No recommended changes to the farmland strategy. In the timberland portfolio, no recommended changes to the strategy, but recommend the board increase the allocations to the timberland managers by $200 million to start down a path of reinvesting anticipated real estate distributions into the timberland sector in order to get the portfolio closer to the board's targets in timberland.

MR. BADER recommends Hancock receive $124 million and Timberland Investment Resources receive $76 million of the $200 million, so each of these advisors has the same total allocation when the pre-existing allocations are considered. If the board approves it, each of the managers will have the same allocation at $244 million.

With TIPS and energy, no recommended changes to the strategy or the allocations.

CHAIR SCHUBERT thanked the presenters and recessed meeting from 10:38 a.m. to 10:57 a.m.

B. Consultant Evaluation of Real Estate Plan: Diversification, Compliance & Performance Measurement

JENNIFER YOUNG of TOWNSEND GROUP reported that the board has invested in two open end core vehicles, UBS Trumbull Property Fund and JP Morgan Strategic Property Fund. The real estate portfolio value is at around $1.5 billion. For the fiscal year ending June 30, 2012, the plan reported a 10.1% total gross return and a 9.2% total net return. The private real estate portfolio represents around 88% of the total investments. As of June 30th, the portfolio lagged its benchmark, posting returns of 8.6% for the one-year period. The core portfolio has produced a total gross return of 8.3% versus 8.4% of the NCREIF Property Index over the same time period. On a three-year basis, there is a performance of 32.4% of the public real estate portfolio.

CHAIR SCHUBERT thanked MS. YOUNG for her presentation.

C. Adoption: Real Assets FY13 Plan & Policies - Board Discussion

MS. ERCHINGER moved the approval of Resolution 2012-30, which adopts the Real Estate Annual Investment Plan for Fiscal Year 2013. MS. RYAN seconded the motion.

The motion passed unanimously.

MS. ERCHINGER moved approval of Resolution 2012-31, which adopts the Revised Real Estate Investment Policies, Procedures, and Guidelines. Motion was seconded by MR. PIHL.

The motion passed unanimously.

MR. BADER requested to move item 14, B1 No. 5 to the December meeting agenda; CHAIR SCHUBERT approved agenda change.

14. IFS ACTION ITEMS (note: *change in agenda to item 14, due to time allowance*)

State Investment Officer STEVE SIKES stated the recommendation is to change the benchmarks in both the McKinley international and domestic portfolios to the growth benchmarks in those respective areas.

MS. HARBO moved to approve the change the benchmarks in both the McKinley international and domestic portfolios to the growth benchmarks in those respective areas. The motion was seconded by MS. ERCHINGER.

The motion passed unanimously.

MR. SIKES recommended moving 5% from the NCREIF Property Index component to the NAREIT Equity Index component, which approximates the 90/10 private/public mix that the board has established for that portfolio. MS. ERCHINGER reported the Real Assets Committee met and concurs with this recommendation.

MS. ERCHINGER moved for approval of the full board to affirm the recommendation to revise the Real Assets benchmark by adding the FTSE NAREIT Equity Index. The motion was seconded by MS. HARBO.

The motion passed unanimously.

MR. SIKES recommends affirmation of the current approach as to the energy investments.

MS. ERCHINGER moved for affirmation of the current approach as to the energy investments. The motion was seconded by MS. HARBO.

The motion passed unanimously.

MR. SIKES reported staff concurs with the recommendation and proposes Resolution 2012-29, which adopts the new guidelines for the internally managed REIT portfolio.

MS. ERCHINGER moved to approve Resolution 2012-29 implementing the IFS recommendation relating to establishing REIT guidelines. MR. PIHL seconded the motion.

The motion passed unanimously.

MR. SIKES reported the recommendation is that the board affirm its current direction with the U.S.-only timberland strategy.

MS. ERCHINGER moved the full board to affirm its current timberland investment strategy of investing exclusively in U.S. timberland on behalf of the Real Assets Committee. MS. HARBO seconded the motion.

The motion passed unanimously.

MR. SIKES reported the recommendation is to approve Resolution 2012-28, which adopts the IFS recommendations relating to the timberland investment guidelines.

MS. ERCHINGER moved for approval of Resolution 2012-28 implementing the IFS recommendation related to timberland investment guidelines. MR. PIHL seconded the motion.

The motion passed unanimously.

MR. SIKES reported the recommendation is to approve Resolution 2012-27 implementing the IFS recommendations relating to the farmland guidelines.

MS. ERCHINGER moved for approval of Resolution 2012-27 implementing the IFS recommendations relating to farmland guidelines. MS. RYAN seconded the motion.

The motion passed unanimously.

MR. SIKES reported the recommendation is to approve Resolution 2012-25, which implements the IFS recommendation and amends the ARMB Manager Watch List Guidelines to review managers based on a six-year performance history relative to the mandates benchmark and pair group.

MS. HARBO moved for approval of Resolution 2012-25, which implements the IFS recommendation and amends the ARMB Manager Watch List Guidelines to review managers based on a six-year performance history relative to the mandates benchmark and peer group. MS. RYAN seconded the motion.

After discussion on the motion, CHAIR SCHUBERT reported the motion would be changed, and under the qualitative factors, it would read, "Below are qualitative factors that may be considered in determining whether an investment manager should be placed on the watch list" rather than terminated.

The motion passed unanimously.

CHAIR SCHUBERT recessed the meeting for lunch from 11:58 a.m. until 1:16 p.m.

9. REAL ESTATE ROUND TABLE

MR. BADER welcomed Jeff Maguire and Tom Anathan with UBS; Anne Pfeiffer and Ann Cole with JP Morgan Asset Management; George Duke and Steve Bolen with LaSalle Investment Management. MR. BADER led the Q&A discussion with the panel.

10. UBS - SEPARATE ACCOUNT & TRUMBULL PROPERTY FUND

MR. TOM ANATHAN provided overview of investment history. They are approximately 35% of multi-family. They have outperformed ODCE on a ten, five, and three-year basis, and are slightly underperformed on one-year basis, and matched it on a quarter.

MR. JEFF MAGUIRE reported the separate account has been managed on behalf of the board 14 years, with 11 individual investments. The account allocation is $305 million, with approximately $40 million to invest. Total returns, over 14 years, are 8.7% gross, just under 8% net. Supply constrained markets for acquisitions are targeted. The weighting toward industrial is 46% within the Separate Account. The board has provided $308 million in total capital, sent back to the board not quite $100 million in distributions from sales and also about $190 million in earnings, so distributable cash flow after our investment management fee, $262 million in real estate.

One of the goals or objectives for the account is to have a 5% net real return on a rolling five-year basis. The Separate Account is a high quality core portfolio. It's totally unlevered, has a history of strong income returns, and leasing efforts over the next three years should drive net operating income substantially higher.

CHAIR SCHUBERT thanked presenters for presentation.

11. JP MORGAN REAL ESTATE

ANNE PFEIFFER, Portfolio Manager of the Strategic Property Fund, welcomed Assistant Portfolio Managers, Ann Cole and Kim Adams. MS. PFEIFFER reported the balance sheet of the portfolio at the end of the June was that the fund's size is $17.5 billion. The gross size is about $23 billion. JP Morgan invests in four traditional sectors in real estate: office, industrial, residential, and retail. The residential sector, at the end of June, is 22.5%, and the office sector is at 43%. The portfolio has about 7% cash at the end of June.

CHAIR SCHUBERT thanked MS. PFEIFFER for her presentation and recessed the meeting for a break from 2:35 p.m. to 2:46 p.m.

12. LASALLE - SEPARATE ACCOUNT & LASALLE MEDICAL OFFICE FUND

CHAIR SCHUBERT welcomed George Duke and Steve Bolen from LaSalle.

MR. DUKE reported exceeding NCREIF, the 12% that NCREIF had last year, and the three-year return has been in excess of 400 points ahead of NCREIF, and they have seven assets, the value just over $200 million.

MR. BOLEN reported on Medical Office Fund. ARMB made this commitment in 2006-2007 timeframe. It's a commingled fund with 11 investors, one of which is LaSalle Investment Management. The investment period expired in April of last year, and the hold period expires in April of 2015, and ARMB is about 10% of the overall capitalized of the fund at $25.4 million.

CHAIR SCHUBERT thanked LASALLE for their presentation.

13. Investment Performance Measurement – Periods Ended 3/31/12

CHAIR SCHUBERT welcomed MICHAEL O'LEARY of Callan Associates, Inc.

Executive Vice President of Callan Associates Inc., MICHAEL O'LEARY, and Senior Vice President, PAUL ERLENDSON, presented a performance review of the retirement fund portfolio and individual participant plans as of March 31, 2012. [*A copy of Callan's slides for this presentation is on file at the ARMB office.]*

MR. O'LEARY said he would provide a brief economic and market summary highlighting some areas that will provide background context for future presentations and recommendations that staff will be bringing forward, first referred to graphs indicating that growth slowed in the second quarter and inflation was not a problem. Next MR. O'LEARY showed a graph showing 10-year treasury rates in 1790. The 1790 number is a hypothetical, but it is amazing to see in a historical context how low interest rates are – almost as low as the post-World War II era. These are the key elements of the economic setting: we're experiencing slow growth and literally unprecedented levels of interest rates.

MR. O'LEARY referred to the slide showing returns for domestic equity, emerging markets and international equity, with spread differences between the markets at extraordinary levels. MR. O'LEARY drew attention to the best performing investment option in the individual accounts plans – the initial balanced fund up over 5%, with the long-term balanced fund up 3+%, both plain vanilla equity/fixed income portfolios. Over the same time period, the best performing asset classes in PERS and TRS were real assets and private equity, which are not represented in either balanced fund. The individual option performances in the Defined contribution Plans were very good – not one of the target date funds had a negative performance. The board and staff should be congratulated for making the policy decisions that put the asset categories in place.

Moving to the PERS and TRS funds, MR. O'LEARY noted that there had been an industry-wide trend moving to a global equity benchmark which the board moved toward, but didn't get there. PERS and TRS would have performed less well with international exposure higher. The performance of PERS for the fiscal year of 47 basis points was behind the target of 102. Underperformance by 57 basis points in domestic equity hurt, but international did slightly better than the benchmark. Real assets was slightly behind its target, with private equity being the biggest contributor to the positive manager effect calculation. Under-allocation to fixed income relative to the target also contributed to underperformance.

For the benefit of the two new board members, MR. O'LEARY reviewed calendar period performance noting that 2008, the meltdown year, showed better than median performance attributable primarily to timing differences because the valuation of real estate was at non-market related levels, as was private equity, but both caught up in 2009. In 2009, the target index is right at median, and relative performance is well below median when the revaluations of real estate and private equity hit the numbers. During the current fiscal year, the valuations lags were a benefit.

MR. O'LEARY noted the heavy equity orientation and wanted the trustees to understand the biases in the asset allocation policy. During asset allocation discussions at least annually, it is pointed out how equity-centric the allocation is with a pronounced equity bias which he feels comfortable with given the unfunded liability and 1.75% on ten-year treasuries isn't going to fill the gap.

MR. O'LEARY next looked at domestic fixed income performance. Most funds' domestic fixed income exposure includes some international bonds as well as domestic bonds – all grouped together. The board's fixed income exposure is comprised primarily of an intermediate U.S. treasury bond portfolio, but also includes a non-dollar bond portfolio managed by Mondrian, a sliver of emerging market debt managed by Lazard, and a below investment grade (junk bonds) fixed income portfolio. The junk bonds did fine, and Treasuries did okay, but non-dollar bonds, which have helped over the long-term hurt, as did the shorter term emerging market debt.

Looking at each of the components of the fixed income allocation, MR. O'LEARY noted that the in-house managed intermediate treasury bond portfolio was up eight basis points over the benchmark; Mondrian was right at the benchmark, down 7 basis points. Looking back three, five, seven and more years, their returns have been very attractive. MacKay Shields, investing in below investment grade bonds, had their best year of relative performance up over 9% for the fiscal year, better than the target index.

MR. O'LEARY reviewed equity performance, noting the domestic equity pool was up 1.81%, below the Russell 3000 at 3.8%. The large cap component was underperformed at 3.19% compared to the Russell 1000 at 4.37%. The small cap equity return for the fiscal year was down, with the active managers underperforming the small cap market. By policy, there is a small cap bias, which hurt performance. The "other" category is comprised of three portfolios whose long-term objective is to generate equity-like returns not correlated to the equity market. First is Analytic, with an option overriding strategy who has met that objective; RCM has not done well, and Advent, who manages a convertible bond portfolio has done well when compared to a universe of convertible bond managers, but has underperformed the S&P 500. There is a question whether this mandate isn't more analogous to a high yield bond portfolio and perhaps should be grouped there.

MR. O'LEARY referred to a graph showing the large cap portfolio breakdown: 82+% of total equity exposure is large cap; 31% is large cap active; 44% is large cap passive. Small cap is 17.8% of the total equity exposure which is more than double the exposure to small cap. MR. WILSON, acknowledging the overweight, wondered if it would be fair to say that some of the money in small cap space has moved up to mid-cap. MR. O'LEARY affirmed that there definitely is mid cap exposure within the small cap component, and there is also small cap exposure within the large cap component. Looking at the weighted median market cap of the large cap portfolio is very close to the weighted median of the index, and a similar chart in the performance book shows that the weighted median market cap is greater than that of the Russell 2000 index, but not by much.

MR. O'LEARY then referred to a graph depicting small cap passive, small cap active and the three components of large cap: active, passive and other. Active large cap, as a proportion of total equity exposure has really been reduced since 2003 in response to the underperformance of active management. Looking at performance for each component, large cap passive did significantly better than large cap active. The same comparison in the small cap pool shows that active small cap managers underperformed, but the three-five and seven-year returns, show an outperformance and the source of underperformance in the small cap pool was the small cap passive piece. In fairness, staff would use the small cap passive in rebalancing, and with money going in and out, there is a day or two-day lag for it to be actually invested in equities. MR. BADER confirmed that there was a cash drag during rebalancing using the small cap passive fund, which hurt returns.

MR. WILSON asked for confirmation whether the numbers included or excluded manager fees. MR. O'LEARY replied that fees were excluded, but once a year net of fee numbers were updated and included in the books sent out. MR. WILSON noted that taking fees into account, active small cap managers had not met their benchmark on a seven-year basis. MR. O'LEARY acknowledged that conclusion, and further noted higher fees in small cap passive.

MR. O'LEARY next referred to page 43, 44 and 45 showing small cap active versus passive on a cumulative basis, with three groupings: small cap, small cap managers in total, and active small cap with a cumulative return lines. This is 12-quarter rolling returns for the last four years, the first data point was four year prior which included the three years before that. Then every quarter, one quarter is added and one quarter drops off. There are a lot of data points with colors used to try and differentiate them. The ellipses account for about 80% of the observations and show that the indexes, active and passive, are all pointed in the same place. On average, active did better than passive, but the index was essentially right there with active. Active was a little bit less volatile, but none of the observations are really significant.

DR. JENNINGS asked if the trend to the overweight in small cap is something Mr. O'Leary sees with other clients, are people maintaining the overweights, or unwinding them? MR. O'LEARY replied that for asset planning purposes, we tend to think of an 80/20 type mix between really large and everything else. One corporate client believed in active management and small cap and had 50% small cap allocation. It is a publicly traded small cap company which explains part of their bias. A more prevalent bias is to have a value bias. The Alaska Permanent Fund has a value bias in its manager structure. MR. WILSON asked about the percentage of clients that have biases. MR. O'LEARY replied that the majority do not, and the reason is that there is an opportunity for error – to have a pronounced bias and have it go against you. There is policy risk in manager structure, so if you have a bias you have to really believe that and accept that there are going to be protracted periods where it works against you.

MR. WILSON said from his perspective one of the most important decisions in the portfolio is to have a bias when most people don't. The portfolio is betting that small cap is going to better than large cap and it's a significant bet and one of the most important that is made.

Moving to the international portfolio, MR. O'LEARY noted that the total exposure is measured against two market indices, EAFE the developed market, and ACWI ex-US developed, which is a combination of developed and emerging. The long term performance is competitive over three, five, seven and ten years, but the last fiscal year was not outstanding. Excluding the dedicated emerging markets managers, the remaining international managers' performance is above the developed market benchmark. The policy document approved by the board limits the magnitude of the exposure in emerging markets that the developed market managers can have which allows managers the flexibility to have some non-index exposure, and it will be easier for staff to control the aggregate emerging market's exposure. In emerging markets, MR. O'LEARY noted that as a group performance is not exciting, but the five-year number is better than median. Lazard, as the only global manager, has done a great job.

MR. O'LEARY noted that the real assets allocation had been a focus of the meeting, with a report on real assets underperformance of the NCREIF, but farmlands' absolute return was terrific. The internally managed REIT portfolio as done well in an absolute sense, and has been right on top of the target, along with the internally managed TIPS portfolio. The absolute return portfolio is a mixed bag. The relative performance of the managers in aggregate has been better than the fund-to-fund peers, but a long way from the absolute target T-Bills plus 5. Is there any type of environment where these funds contribute? It didn't happen in the decline and didn't happen in the recovery. One answer has been that the environment where it isn't all risk on or risk off, with less correlation amongst risk assets. So we are monitoring and there will be continuing discussion during the asset allocation process ahead.

MR. O'LEARY noted that in the defined contribution accounts, the red light/green light exhibit shows more green than anything else. The exception is the RCM social responsibility option in SBS, with a three-year return in the third quartile and the one-year return in the fourth quartile. The returns for the balanced options and target date funds all did a good job.

Looking forward, MR. O'LEARY noted that he was eager to return at the next meeting to discuss the third quarter, with another week to go in the quarter, the S&P 500 is up 19% on a calendar year-to-date basis, and further good news in the international area measured in dollar terms has participated fully this quarter. It's been a really good quarter.

CHAIR SCHUBERT thanked Mr. O'Leary for his presentation.

15. PROPOSED INVESTMENT RESOLUTION

COMMISSIONER BUTCHER reported 20 states have taken actions not to invest in companies that do business in Iran, and many of them, if not most of them, have talked about it from a social investing position. COMMISSIONER BUTCHER emphasized that any decision made with our funds should be made in the sole financial best interest of the State, which is our fiduciary responsibility.

COMMISSIONER BUTCHER moved the adoption of Resolution 2012-32. MR. BRICE seconded the motion.

MR. PIHL requested list of eight companies; COMMISSIONER BUTCHER confirmed he will provide the list.

Deputy Commissioner ANGELA RODELL provided the following list: Air Liquide, China Petroleum, Costain Group, Gazprom, OMV, Petrofac, SGS, and Technew.

The motion passed unanimously.

RECESS FOR THE DAY

CHAIR SCHUBERT recessed the meeting at 4:26 p.m.

Friday, September 21, 2012

CALL BACK TO ORDER

CHAIR SCHUBERT reconvened the meeting at 8:59 a.m. Along with the Chair, Trustees Trivette, Harbo, Erchinger, Hultberg, Pihl, Brice, Ryan, and Butcher were present.

REPORTS (continued)

16. GLOBAL ASSESSMENT MANAGEMENT REPORT

ARVIN SOH and KATHRYN CICOLETTI of GLOBAL ASSESSMENT MANAGEMENT reported on customized accounts and Fund of Hedge Funds and Fund of Funds. Last year, the account was down approximately 2%, and even though that was significantly better than the HFRI Fund of Funds, it did not hit the absolute return. This year, the account is up roughly 5.7% year-to-date, which is significantly better than both the benchmark from the absolute as well as from the relative. MR. O'LEARY asked questions about performance. MR. BADER questioned the volatility.

CHAIR SCHUBERT thanked GAM for their presentation.

17. CRESTLINE INVESTORS, INC. REPORT

MR. BADER reported CRESTLINE INVESTORS manages about $250 million in this strategy. They are also an investor for the Alaska Permanent Fund and one of the original hedge fund hires for this mandate.

MR. DOUG BRATTON, Founder and Chief Investment Officer of Crestline, and MR. SAM LEVENS, Senior Portfolio Manager for diversified funds and on this account, reported the year-to-date 2012 number is positive 2.32, a return of 32 basis points compared to a return objective of 2.95 and comparator benchmark, HFRI Fund of Funds Conservative Index, which is 1.77. For this mandate, they've had very low betas to the equity markets, very low negative betas to the Barclay Ag, and then very low betas to the commodity markets.

MR. BRATTON talked about active management changes they're making in the portfolio to deal with this environment, including the state of hedge funds, market environment, and expectations on returns.

MR. LEVENS explained two account options for new board members, diversified account versus managed account. MR. BRATTON provided overview of what causes hedge fund returns to go up. CHAIR SCHUBERT inquired as to the factors that the board should expect to help CRESTLINE to outperform its benchmark. A discussion on benchmark and treasuries followed.

MR. BRATTON indicated CRESTLINE was put on the watch list because of its acquisition of North Water about two or three years ago. CHAIR SCHUBERT thanked CRESTLINE for their presentation.

18. INVESTMENT ACTIONS

A. Prisma Capital Management Mandate

MR. BADER reported Prisma was hired in January of 2010 to manage an absolute return portfolio for the ARMB. Prisma currently manages about $145 million for the ARMB. At the April 2012 meeting, the ARMB elected to invest an additional $50 million with Prisma. ARMB staff has not invested that money with Prisma at this point. In June of 2012, Prisma was placed on the watch list.

MR. BADER stated this action item is a request that the Alaska Retirement Management Board rescind the decision to invest an additional $50 million with Prisma Capital Partners in a sub-portfolio targeted towards fixed income characteristics.

MR. TRIVETTE moved that the Alaska Retirement Management Board rescind the decision to invest an additional $50 million with Prisma Capital Partners in a sub-portfolio targeted towards fixed income characteristics. MS. RYAN seconded the motion.

MR. O'LEARY stated, in the interest of full disclosure, his daughter is a partner at KKR, so he recused himself from consideration of hiring/firing of anybody that is affiliated with KKR. The motion passed unanimously

B. International Emerging Market Exposure

MR. BADER reported this action item is to ask the board to approve a change in the guidelines to also apply that limit to the EAFE large cap index, emerging market -- the emerging market limitation to the EAFE index. There are two managers that would be affected by this. That would be Cap Guardian and Brandes.

MS. HARBO moved for a change in the guidelines. MR. BRICE seconded the motion. All members were in favor of the motion; none were opposed. Motion carried unanimously.

C. Contract Award

MR. BADER Staff is recommending that the board issue a Notice of Intent to Award a Contract, and subsequent to the expiration of the ten-day period for protest, negotiate a contract with MAP Alternative Investment for risk analysis services.

MS. HARBO moved that the board issue a Notice of Intent to Award a Contract, and subsequent to the expiration of the ten-day period for protest, negotiate a contract with MAP Alternative Investment for risk analysis services. MR. PIHL seconded the motion. All were in favor; none were opposed. The motion carried unanimously.

CHAIR SCHUBERT announced a break for the EXECUTIVE SESSION at 9:58 a.m.

19. EXECUTIVE SESSION

CHAIR SCHUBERT called meeting back to order at 10:10 a.m. and reported there was no action taken in EXECUTIVE SESSION.

20. MANAGER SEARCH - MASTER LIMITED PARTNERSHIPS

MR. O'LEARY described the process at Callan that created the list of managers, and MR. BADER described the selection process for managers to come before the board today. A discussion followed on the selection process.

A. Advisory Research, Inc./FAMCO

JIM CUNNANE, MLP CIO, and TRISH OPPEAU, Vice President, presented and discussed active management and the Alerian Index. They discussed their unique process and indicated they have competitive fees of 50 basis points.

MS. ERCHINGER requested explanation on the float-adjusted market capitalization methodology. DR. MITCHELL questioned the timing of the strategy.

MR. WILSON asked who owns the company and how the team is compensated. MR. CUNNANE stated that the parent company is Piper Jaffrey out of Minneapolis, which is a 100-plus year old investment firm. FAMCO is part of an asset management arm in Piper Jaffrey, and the team is compensated based on the results of the team.

MR. O'LEARY questioned cash flow distributions. MR. CUNNANE stated a typical distribution from an MLP is the cash flow that they're bringing in, minus a cushion for the volatility in their business, minus a cushion to maintain the assets that they own. One of the very positive things about MLPs and very negative things about MLPs, to fund the growth, MLPs require access to the equity market and to the debt market.

CHAIR SCHUBERT thanked FAMCO for their presentation and announced lunch break at 11:47 a.m.

B. Neuberger Berman

CHAIR SCHUBERT called the meeting back to order and welcomed YVES SIEGEL, MARK SULLIVAN, and DOUGLAS RACHLIN from NEUBERGER BERMAN.

MR. RACHLIN, Chief Portfolio Manager, explained they have been managing an MLP strategy since the summer of 1996. MR. RACHLIN discussed performance, including Alerian Index and four pillars that support their investment thesis: 1) recognizing and identifying the current trends and where consumption is going and where to get the products to the individual markets; 2) significantly overweighted in publicly traded general partners, due to Incentive Distribution Rights; 3) there has been a recent trend in the last three or so years of limited partners buying in their general partners and taking out these Incentive Distribution Rights; and 4) 35% or so of portfolio is invested in LPs that do not pay Incentive Distribution Rights.

MR. SIEGEL stated the board should think of NEUBERGER BERMAN as being excellent stewards of their clients' capital. First and foremost, they're focused on safety and sustainability of the yield as well as being focused on growth, but it's that fit of the safety and sustainability of the yield that the really focus on.

MR. SULLIVAN discussed the strength of Neuberger Berman, what Yves and he do on a daily basis in terms of fundamental research. Neuberger Berman is a $200 billion asset manager. Neuberger also has a research department and has the second most management meetings of any asset manager. They look at SEC filings and read research and model each of the companies in their portfolio.

MR. RACHLIN discussed growth and interest rate correlation. They are uniquely focused on separately managed accounts. That is all they do, separately managed accounts. They have about $3 billion in the MLP strategy that we execute. Their average client pays about 120 basis points. If ARMB selects them to manage assets, it will be significantly below that.

CHAIR SCHUBERT thanked NEUBERGER BERMAN for their presentation.

C. Tortoise Capital Advisors

ABEL MOJICA, Head of Corporate Development, and MATT SALLEE, Senior Investment Analyst, reported their approach has been to do everything with a bottom-up approach, bottom-up research. TORTOISE is the largest MLP manager with the largest and most diversified institutional client set.

MR. SALLEE discussed development of resource across the U.S.

TORTOISE'S motto is "Steady Wins," but they think that, for a long-term institutional investor, they have the appropriate approach for long-term kind of low risk institutional investors. Their fee structure is a flat 75 basis points.

MR. BRICE questioned pipeline tariffs, and DR. MITCHELL questioned the timing. CHAIR SCHUBERT thanked the presenters and announced a break at 2:16 p.m.

D. Board Discussion and Selection

CHAIR SCHUBERT called the meeting back to order at 2:30 p.m. MR. BADER led the discussion and pointed to a spreadsheet created by ZACH HANNA and then led discussion on strengths and weaknesses of each presenter.

CHAIR SCHUBERT requested a motion that the Alaska Retirement Management Board directs staff to hire one or more managers to manage up to $200 million in MLP investments, subject to successful contract and fee negotiations.

MR. PIHL moved that the Alaska Retirement Management Board directs staff to hire one or more managers to manage up to $200 million in MLP investments, subject to successful contract and fee negotiations. MS. HARBO seconded the motion. The motion carried unanimously.

MS. ERCHINGER moved that the ARMB invest $200 million equally between Tortoise Capital at $100 million and FAMCO at $100 million. MS. RYAN seconded the motion.

The motion passed. 9-0.

UNFINISHED BUSINESS

1. Disclosure Report

MS. HALL stated that the disclosure report was included in the packet.

2. Calendar

MS. HALL reported the following additions to the calendar: 1) Education Conference on October 25th and 26th; 2) an Audit Committee teleconference October 17th; and 3) a date will be set for a Legislative Committee teleconference meeting early in November.

3. Legal Report

MR. JOHNSON indicated, since the last meeting in June, he has assisted some of the revenue investment contract evaluations, primarily with Mr. Sikes and has assisted Deputy Commissioner Rodell and others in working on a revision to the procedures manual, policy and procedures manual. He attended the National Association of Public Pension Attorneys Conference. At that conference, it was noted the Dodd-Frank bill is slowly being implemented, the Supreme Court decision came down on the Affordable Care Act, and the issue of GASB disclosures was a point that came up.

NEW BUSINESS - None.

OTHER MATTERS TO PROPERLY COME BEFORE THE BOARD

MS. HARBO requested, at the next meeting in December, the board receive some kind of an informational brief introduction to the new GASB rule, that would provide an implication of how those rules are going to affect employers in the state. MR. PIHL stated it was discussed at the Audit Committee Meeting and MR. PUCKETT is going to get a summation version to the board.

PUBLIC/MEMBER COMMENTS

CHARLIE GALLAGHER, the Northern Chair of the Retired Public Employees of Alaska, read a statement by Mr. Jay Dulaney, the RPEA President.

INVESTMENT ADVISORY COUNCIL COMMENTS

DR. MITCHELL commented on a list of 22 major markets in the world and stated we're experiencing a terrific year for equities in 2012. He reported bank stocks are down. Two of the major banks in the U.S. over the last ten years are down. Citicorp is down 87%, and Bank of America is down 71%.

MR. WILSON discussed asset allocation and stated the ARMB has a fairly low allocation to fixed income, which is in the low 20% range, depending upon how it is calculated, and that is very low for public plans. This topic will be taken up over the next, three to six months. One of the more important decisions the board will make is whether the board wants to continue to have, at least, 20% of assets earning somewhere between zero and 1.5%.

TRUSTEE COMMENTS

MS. HARBO commented on two interesting publications, one by the National Institute of Retirement Security called *Pensionomics* available on its website, and the other by Fairbanks Economic Development Corporation titled, "Retirees in Fairbanks are a growing $300 million annual economic stabilizer."

MR. PIHL commented he is increasingly uneasy with the board's 8% interest assumption and would like to have it on the agenda at some time in the near future.

MS. ERCHINGER commented she thinks it would be a good idea for the board to have a discussion and develop some sort of policy, in response to Deputy Commissioner Barnhill's comments that they have a methodology for assessing the actuarial costs that are incurred as a result of looking at the impacts of pending legislation.

MS. ERCHINGER welcomed the new board members, TRUSTEE RYAN and TRUSTEE BRICE.

MS. ERCHINGER stated she hopes the board will continue to work closely with the Division of Retirement and Benefits as it relates to a discussion that was had the Audit Committee regarding employer audits.

MS. ERCHINGER encouraged board members to have participation in the Legislative Committee meeting before the Alaska Municipal League meeting in November.

MS. ERCHINGER expressed appreciation for Dr. Jennings' recommendation on the MLP investment that the ARMB consider limiting its investment to one manager.

MR. TRIVETTE agreed with comments by MS. HARBO regarding money being spent in Alaska by pensioners. MR. TRIVETTE expressed concern about having seven committee meetings in one day and expressed appreciation for new Trustees.

MR. BRICE thanked CHAIR SCHUBERT for her leadership.

MS. RYAN thanked the Trustees for help in getting her up and running on the board.

FUTURE AGENDA ITEMS - None.

ADJOURNMENT

There being no objection and no further business to come before the board, the meeting was adjourned at 3:22 p.m., on a motion by made MS. HARBO and seconded by MR. BRICE.

Chair of the Board of Trustees
Alaska Retirement Management Board

ATTEST:

Gayle Harbo
Corporate Secretary