State of Alaska
ALASKA RETIREMENT MANAGEMENT BOARD
MEETING

Location:
Dena'ina Convention Center
600 West Seventh Avenue
Anchorage, Alaska

MINUTES OF
June 24, 2016

Friday, June 24, 2016

CALL TO ORDER

CHAIR GAIL SCHUBERT called the meeting of the Alaska Retirement Management Board (ARMB) to order at 9:02 a.m.

ROLL CALL

Six ARMB trustees were present at roll call to form a quorum. Commissioner Sheldon Fisher arrived late.

Board Members Present
Gail Schubert, *Chair*
Robert Johnson, *Vice Chair*
Gayle Harbo, *Secretary*
Kristin Erchinger
Commissioner Sheldon Fisher
Tom Brice
Bob Williams

Investment Advisory Council Members Present
Dr. William Jennings

Department of Revenue Staff Present
Gary M. Bader, Chief Investment Officer
Bob Mitchell, Deputy Chief Investment Officer
Scott Jones, State Comptroller
Pamela Leary, Director, Treasury Division
Judy Hall, Board Liaison

Department of Administration Staff Present
Kevin Worley, Chief Financial Officer, Division of Retirement & Benefits (DRB)
John Boucher, Deputy Commissioner

Consultants, Invited Participants, and Others Present
Melissa Bissett, Buck Consultants
David Kershner, Buck Consultants
Larry Langer, Buck Consultants
Steven Center, Callan Associates, Inc.
Paul Erlendson, Callan Associates, Inc.
Stuart Goering, Department of Law, Assistant Attorney General
Leslie Thompson, Gabriel Roeder Smith
Katie AmRhein, Hancock Timber
Karen McQuiston, Jennison Associates
Sheetal Prasad, Jennison Associates
Peter Reinemann, Jennison Associates
Sarah Lukin, PT Capital
Hugh Short, PT Capital
Mead Treadwell, PT Capital
Brad Owens, Retired Public Employees of Alaska
Eric Shirbini, Scientific Beta North America
Marc Zieger, Scientific Beta North America

PUBLIC MEETING NOTICE

JUDY HALL, Board Liaison, confirmed public meeting notice requirements had been met.

APPROVAL OF AGENDA

MRS. HARBO moved to approve the agenda. MS. ERCHINGER seconded the motion.

GARY M. BADER, Chief Investment Officer, requested to move Item 15B. Investment Action S&P 600 to Item 7B., immediately following the presentation of Item 7A. S&P 600.

VICE-CHAIR ROBERT JOHNSON requested an addition to the agenda discussing the statement of legislative intent regarding transfer of management responsibilities and a possible draft resolution to be discussed under Item 4. Treasury Division Report.

The Maker of the Motion and the Second to the Motion agreed to the friendly amendments to the agenda.

The agenda was approved as amended.

PUBLIC/MEMBER PARTICIPATION, COMMUNICATIONS, AND APPEARANCES

BRAD OWENS, Vice-President of Retired Public Employees Association of Alaska (RPEA), stated House Bill (HB) 256 could impact pension funds and affect the role of the ARMB in managing assets. The bill requests a report be delivered by October 15th addressing whether the management responsibility of the pension funds' assets currently managed by the ARMB should be transferred to the Alaska Permanent Fund Corporation (APFC). RPEA strenuously objects to any change from the current responsibility of the management of pension funds the Legislature specifically assigned the ARMB.

MR. OWENS stated the RPEA believes the APFC is not representative of the interests of the pension funds dedicated to state retirees. The distinct difference in perspective could result in a loss of primary focus on the needs and goals of the pension funds. Any effort to consolidate management could result in a blended approach with more attention provided to the APFC. RPEA believes any savings would likely come at the expense of the pension funds' management, rather than from the APFC. The proposed transfer of assets to a single entity ignores the principles of diversification and the long, excellent working relationship between the ARMB and staff would be negatively impacted or lost. RPEA urges the ARMB to oppose any transfer proposed under HB 256.

MR. OWENS noted RPEA publically states the use of any pension fund assets in preparing the report could constitute a clear misuse of funds and violate the State's fiduciary duties to protect and use the pension funds for the sole and primary benefit of retirees and beneficiaries.

HUGH SHORT, CEO of PT Capital, introduced team members SARAH LUKIN, Chief of Staff, and MEAD TREADWELL, President. PT Capital is the first Alaskan private equity firm and has raised $300 million in their Arctic-focused fund. MR. SHORT expressed his goal to follow up with MR. BADER regarding PT Capital as an emerging manager based in Alaska. He expressed his appreciation to the members and is pleased CHAIR SCHUBERT is presiding.

MR. BADER asked if PT Capital's objective is to make investments solely in Alaska. MR. SHORT explained the firm has the ability to deploy 60% or greater of the fund within Alaska, up to 25% within Canada, and up to 15% within Iceland and Greenland. MR. SHORT described a very cautious and patient approach to acquisitions within the Alaska market is held now because of the cyclical downturn and noted some buy opportunities and attractive valuations.

APPROVAL OF MINUTES: April 21-22, 2016

<u>MRS. HARBO moved to approve the minutes of the April 21-22, 2016 meeting. MR. WILLIAMS seconded the motion</u>.

The minutes were approved.

REPORTS

1. CHAIR REPORT

CHAIR SCHUBERT expressed her appreciation to the involved Trustees for their continued work on complex issues addressed by the Actuarial Committee.

2. COMMITTEE REPORTS

A. Audit Committee

VICE-CHAIR JOHNSON stated he was honored to be appointed Chair of the Audit Committee. The Committee met the day before the Board meeting. Robust discussions occurred with KPMG regarding GASB 68, materiality of matter, patterns and practices from particular employers, medical cost savings, and the use of proxy statements. No actions were taken.

B. Actuarial Committee

MS. ERCHINGER reported the Actuarial Committee met the day before the Board meeting and covered three action items that will come before the Board today. The first was a recommendation to accept GRS' certification for FY15 PERS and TRS, DC, National Guard and Naval Militia, and JRS valuations. The second was a recommendation to accept Buck's FY15 valuation for those same plans. The third was a recommendation the Board accept the updated audit findings and the resolution of those findings to date.

MS. ERCHINGER stated the issue of persistent material health gains and the migration from proxy data to more actual data was discussed. The Department of Administration is considering the issuance of an RFP to improve the quality of available retiree data. There was discourse regarding the upcoming 2016 valuation and changes to the proxy data issue and the rehired retiree liability load assumption. Minor adjustments were made to the timeline to give the actuary and review actuary more time in between meetings.

3. RETIREMENT & BENEFITS DIVISION REPORT

A. Buck Consulting Invoices (Informational)

KEVIN WORLEY, Chief Financial Officer, DRB, provided the Buck Consulting quarterly report ended March 31, 2016.

B. Membership Statistics

MR. WORLEY provided the membership activity quarterly report ended March 31, 2016. He reviewed the expected decrease in both PERS and TRS DB and expected increase in both PERS and TRS DC. MR. WORLEY reported he received the GFOA Certificate of Achievement in Financial Reporting for PERS CAFR in the mail.

MS. ERCHINGER congratulated staff for receiving the award and expressed appreciation for their hard work.

C. DRB Update

JOHN BOUCHER, Deputy Commissioner, Department of Administration, provided the DRB update and noted there was essentially no legislation that affected the retirement system that passed. DEPUTY COMMISSIONER BOUCHER anticipates the reappearance in the next session of HB 4002, extending benefits to the deceased members of peace officers and fire fighters. The DRB is contemplating a reorganization to reinstate the director position which was removed two years ago. DEPUTY COMMISSIONER BOUCHER will report on the progress during the next several months.

CHAIR SCHUBERT expressed her support for HB 4002.

4. TREASURY DIVISION REPORT

Treasury Division Director PAMELA LEARY reported that the budget bill passed by the Legislature is the budget MS. LEARY reported on in April. It is with the Governor, awaiting his response. The budget bill supports the continued progress of staff in managing the ARMB assets and growing internal asset management. The budget bill also includes the intent language that directs the Department of Revenue, in consultation with the APFC, to evaluate whether management responsibility of State and ARMB assets should be transferred to APFC.

MS. LEARY provided a copy of the response letter from COMMISSIONER HOFFBECK to RPEA summarizing the Department will be cooperating with the language and working with APFC to see if potential synergies or savings exist between the Treasury and APFC in light of the current fiscal situation. APFC is engaging KPMG to issue a report of the data metrics, risks and opportunities of options, and potential costs and savings under three scenarios; 1) all assets of the ARBM moved to APFC, 2) a subset of Treasury assets, including ARMB assets, moved to APFC, and 3) all assets of the APFC moved to the Treasury.

STUART GOERING, Department of Law, Assistant Attorney General, stated the Department of Law agrees with the position the legislative intent is not a binding legal requirement upon anyone in the executive branch or elsewhere. The Governor is generally advised during the bill review that legislative intent is nonbinding. This bill review is confidential and is protected by attorney/client privilege and deliberative process privilege.

MR. GOERING stated the legislative intent was directed to the Department of Revenue. The Department of Law generally advises agencies that receive intent language to attempt to comply with the spirit of the intent language. MR. GOERING suggested it might be worthwhile for the ARMB to consider meaningful recommendations regarding possible future structural changes that would be valuable and in the best interest of the funds in the event the Legislature and/or Governor decide to pursue APFC management responsibility.

VICE-CHAIR JOHNSON asked if statements of legislative intent may be subject to line item veto. MR. GOERING does not know of any use of the line item veto for statements of legislative intent. The line item veto is typically limited to actual appropriation items.

MS. ERCHINGER requested clarification of the issue of the Board's fiduciary responsibility and trust funds, since the funds are held in trust by the State of Alaska, but do not belong to the State of Alaska. MS. ERCHINGER asked if discussion has occurred regarding the relationship APFC has with the State of Alaska. MR. GOERING indicated he is unaware of the discussions because he has not participated in any discussions. MR. GOERING does not believe the intent language transfers fiduciary responsibility from the ARMB, but rather transfers the actual investment management functions from the Treasury. MR. GOERING explained APFC is an independent entity that has an existence separate from the State of Alaska, but is also an arm of the State with the authority to manage funds for State agencies. MR. GOERING commented it would not be appropriate for the fiduciary responsibilities of the ARMB to be transferred.

CHAIR SCHUBERT inquired as to the reason the bill only contemplated consultation with APFC and no consultation with the ARMB. MS. LEARY had no information. CHAIR SCHUBERT commented the Department of Revenue has developed an excellent investment staff that has provided real investment results. CHAIR SCHUBERT expressed hope this bill does not unsettle the investment staff. She noted the ARMB will be watching this bill closely and would not object to consultation as the bill moves forward.

<u>VICE-CHAIR JOHNSON moved to adopt Resolution 2016-10 relating to legislative intent concerning the transfer of Board management responsibilities. MRS. HARBO seconded the motion.</u>

VICE-CHAIR JOHNSON commented the lack of clarity of the statement of legislative intent regarding the transfer of management responsibilities is a fundamental problem that invades specifically the fiduciary space the ARMB currently has under law. The intentions to save funds during troubled times in the state is appreciated and an analysis on various savings should be conducted. VICE-CHAIR JOHNSON agreed the close working relationship with staff and the ARMB built over years is excellent. He believes the statement of intent would potentially handoff significant investment functions to APFC, separate from the State of Alaska, and this could give rise to problems from Washington, D.C. and elsewhere.

VICE-CHAIR JOHNSON submits the statement of intent is simply not a good idea and has a tendency to mix and match apples and oranges in the fashion of affiliating key elements of what the ARMB does with other agencies. VICE-CHAIR JOHNSON expressed his concern as an Alaskan citizen with the possibility of APFC changing the focus from its mission and utilizing assets for critical state investment responsibilities. VICE-CHAIR JOHNSON believes it is important to keep a robust investment operation within the Department of Revenue.

VICE-CHAIR JOHNSON requested the Board adopt the resolution which opposes the statement of intent, asks the Governor to use his line item veto power, if it exists, provides that the Legislature seek interview of Board of Trustees' input, and recommends a copy of the resolution be provided to the Governor, the Legislature, and APFC.

<u>MRS. HARBO moved for unanimous consent.</u>

DEPUTY COMMISSIONER BOUCHER requested a roll call vote be taken since neither Commissioner was present.

Motion for unanimous consent failed.

CHAIR SCHUBERT asked if the word legislature should be legislative statement on page two, item three. VICE-CHAIR JOHNSON agreed. The error was corrected with no objection.

A roll call vote was taken, and the motion passed unanimously.

5. CIO REPORT

MR. BADER reviewed the CIO Report provided to the Board. He reported the pension funds and health trust funds had been rebalanced several times since the last meeting and the dates were listed in the report. MR. BADER provided a review of each of the 21 transaction items provided in the CIO Report.

MR. BADER asked for a motion authorizing staff to request legal counsel draft a paper on whether or not it is permissible for the Board to create an emerging manager sleeve, and secondly, to ask Callan to provide a report to the Board on how frequently emerging managers are used by other large pension funds.

MRS. HARBO moved to authorize staff request legal counsel to draft a paper on whether or not it is permissible for the Board to create an emerging manager sleeve, and secondly, to ask Callan to provide a report to the Board on how frequently emerging managers are used by other large pension funds. MR. BRICE seconded the motion.

MR. BRICE requested the due diligence process include other opportunities the MMP sleeve may present.

A roll call vote was taken, and the motion passed unanimously.

6. FUND FINANCIAL REPORT

State Comptroller SCOTT JONES and Chief Financial Officer of the Division of Retirement and Benefits KEVIN WORLEY presented the Fund Financial Report. MR. JONES reviewed the financial statements for the fiscal year-to-date through April 30th, 2016. The approximate numbers are: the PERS system ended with $16 billion, the TRS system with $7.9 billion, the JRS with $170.3 million, the National Guard and Naval Militia (NGNMRS) with $36 million, SBS with $3.4 billion, and Deferred Comp with $805.4 million, for a total of $28.2 billion, of which $23.1 billion is non-participant directed assets and $5.1 billion is participant-directed assets. This is a year-to-date decrease in assets of 2.79%, mostly due to cash flows and approximately .69% was related to investment income. All of the funds are near their bands and within the set asset allocation.

MR. JONES reviewed the updated financial statements as of the end of May. The non-participant directed assets were approximately $23.1 billion and participant-directed assets were approximately $5.1 billion, for a total of $28.2 billion.

MR. WORLEY reviewed the one payment for health reimbursement received in April. Payroll reports are consistently being received from employers. The general inflows and outflows are consistent with what has been received during the fiscal year. MR. WORLEY discussed the disbursement report, highlighting the separation from service and retirement line at 90%. Over the last few months, there has been an uptick in folks leaving service and taking their funds out of the plan. Many of these withdrawals have met the IRS hardship definition, including losing their home or medical treatments, to receive funds without waiting the 60-day required timeframe.

MR. BRICE stated the Defined Contribution Committee worked with the Department surveying people who are separating to get a better understanding of the reasons for cashing out accounts. MR. BRICE asked for an update on that process. MR. WORLEY noted part of the issue found was members did not understand the fee structure. Another issue found that members erroneously thought they had to transfer their funds when they left State employment. Empower/Great-West is working on an education program for members mainly via web, mailers, and email due to the cuts to the travel program.

DEPUTY COMMISSIONER BOUCHER noted the education efforts are a renewed area of emphasis within the last year for the agency to try to retain some of the funds and educate the members on the possibilities they have. DEPUTY COMMISSIONER BOUCHER stated he will cover educational topics and other concerns at the Defined Contribution meeting in September.

MR. WILLIAMS suggested creating an educational campaign to inform participants of their choices and consequences of their choices.

Discussion continued regarding education to participants and MR. WORLEY reiterated Chief Pension Officer LEA and her staff have made education a high priority. The members who are cashing out their accounts have to talk to counselors regarding consequences. There are also counseling sessions regarding tax consequences and hardship cash-outs.

7. S&P 600

A. Presentation

MR. BADER informed this presentation is a request for the Board's approval for Department of Revenue internal staff to implement a small cap investment strategy benchmarked to the S&P 600 Index. Currently staff internally manages about $1.6 billion in assets in addition to the $1.1 billion of internally managed fixed income assets. MR. BADER described the breakdown of these investments.

MR. BADER noted the three goals of internally managing money are; 1) to lower the aggregate investment management fees, 2) for staff to become increasingly proficient, and 3) to manage assets in Alaska for Alaskans, which helps the economic health of Alaska. These goals can be realized if an internally managed portfolio can earn more on a risk-adjusted basis after fees than if the funds were placed with an external investment manager.

MR. BADER continued his detailed presentation explaining the S&P 600 Index is designed to track companies that meet specific inclusion criteria to ensure they are liquid and financially viable. He gave specific examples of each. MR. BADER believes the S&P 600 Index mandate will be a strong contributor to the portable alpha strategy approved by the Board at the February meeting.

B. *Action: S&P 600*

VICE-CHAIR JOHNSON moved to authorize staff to make an initial investment of $75 million to an internally-managed, domestic, small cap portfolio benchmarked against the S&P 600 Index. MRS. HARBO seconded the motion.

A roll call vote was taken, and the motion passed unanimously.

CHAIR SCHUBERT recessed the meeting from 10:34 a.m. to 10:45 a.m.

8. ADOPT ASSET ALLOCATION
Resolution 2016-08:
DB PERS/TRS/JRS
PERS/TRS/JRS Retiree Health Trusts
Retiree Major Medical HRAP/ODD

MR. BADER noted there were concerns expressed by Board members at the last meeting regarding the new recommendation of a global asset allocation, as opposed to maintaining a domestic sleeve and an international sleeve. MR. BADER informed the Board that staff, Callan, and the IAC all were equally comfortable with keeping the status quo, in terms of asset buckets for the asset allocation recommended to the Board. The substance of the asset allocation will have the same effect as what was previously recommended.

MR. BADER presented, in the interest of time, a new resolution containing the same asset classes as currently held, instead of a global asset allocation. The full presentation given by MR. ERLENDSON at the previous meeting remains the same with the one change from global asset allocation to the current domestic and international allocations. MR. BADER outlined the differences between the current asset allocation and the recommendation today. The expected return for PERS and TRS asset allocation remains at 7.1%. Public equity and the risk are slightly less in the current asset allocation. Cash is 2% less. Alternatives have increased. The military return and risk are the same as last year, with cash down from 3% to zero, and fixed income up 3%.

MR. WILLIAMS moved to adopt Resolution 2016-08. MS. ERCHINGER seconded the motion.

A roll call vote was taken, and the motion passed unanimously.

Resolution 2016-09: DB NGNMRS

MRS. HARBO moved to adopt Resolution 2016-09. MR. WILLIAMS seconded the motion.

A roll call vote was taken, and the motion passed unanimously.

9. ACTUARIAL REVIEW/ACCEPTANCE-CERTIFICATION OF FY15 VALUATIONS

A. Introduction

MS. ERCHINGER reported the Actuarial Committee met with Buck Consultants and Gabriel Roeder Smith (GRS) the previous day and will present unanimous recommended action items to the Board. The only change from what appears in the packet was a request to Buck and GRS to agree on specific changes in language in the valuation report with regard to the proxy data and the potential risks associated with the use of proxy data.

B. GRS Review Comments
National Guard Naval Militia Retirement System and Judicial Retirement System: FY15 Roll-Forward

CHAIR SCHUBERT introduced LESLIE THOMPSON of GRS, who presented the review comments of the NGNMRS and JRS. MS. THOMPSON reported the new timeline, providing additional time to perform the review, proved to be successful. The National Guard Naval Militia Retirement System (NGNMRS) and Judicial Retirement System (JRS) roll-forward valuation had no audit findings and GRS was able to replicate every number.

Update: DB and DCR Systems Previously Reviewed

MS. THOMPSON advised that Buck implemented the recommended changes given by GRS. Buck will identify those in their presentation. The issues remaining on the checklist for further review during the experience study include, people being rehired and the resulting upward pressure on contribution rates. MS. THOMPSON expressed appreciation to Buck for their explanation of the large retiree medical gains outlined in their modeling. Buck addressed the GRS concerns regarding pension data being used to value retiree medical data by diligently creating disclosure statements to coincide with the actuarial standard of practice.

VICE-CHAIR JOHNSON advised six of the Board members were at the recent Actuarial Committee meeting where hours of discussion occurred regarding the issues reviewed by MS. THOMPSON. He expressed his appreciation to MS. THOMPSON for her work and suggested the minutes of the Actuarial Committee be reviewed for additional information.

C. Summary Presentation:
NGNMRS and JRS Roll Forward
Update: DB and DCR Systems Previously Reviewed

CHAIR SCHUBERT introduced LARRY LANGER, DAVID KERSHNER and MELISSA BISSETT of Buck Consultants, who presented the roll-forward valuations for NGNMRS and JRS and provided an update on DB and DCR systems. MR. LANGER expressed appreciation for the efforts of DRB, Actuarial Committee, and GRS in assisting with the valuation results.

MR. KERSHNER reviewed the details of the preliminary numbers reported in April compared to the final numbers reflecting the recommended changes from GRS for the PERS and TRS DB plans and the PERS and TRS DCR plans.

MS. ERCHINGER believes it is critical to mention the funding ratios were down in the 60% range before the Legislature appropriated the $3 billion into the retirement systems. The funding ratios are now 78% for PERS and 83% for TRS. The Legislature also extended the amortization period by an additional nine years, which decreased the State assistance contribution rate. MS. ERCHINGER noted the Actuarial Committee will have future conversations regarding meaningful ways to keep the funding ratio high.

DEPUTY COMMISSIONER BOUCHER expressed congratulations to the Board members for addressing the funding problem and believes this official release of numbers is a milestone for this plan and a major success for Board and staff.

MR. KERSHNER reviewed the roll-forward valuation results for NGNMRS and JRS. He explained the liabilities are rolled forward and the actual assets are used to determine the funded ratios and contribution rates. The JRS funded ratio increased from 71.9% to 75.6%, and the employer contribution as a percentage of payroll changed from 76.49% for FY17 to 74.21% for FY18. The NGNMRS funded ratio stayed the same at 98.8%. The employer contribution is expressed as a dollar amount and changed from $867,000 to $907,000, primarily due to the difference in the expense load.

MS. ERCHINGER recognized the trend of reducing employer contribution rates. She believes the Alaska retirement plan will compare favorably to other states' retirement plans.

D. Board Discussion/Questions
Action: Board Acceptance of GRS Certification for
FY15 PERS/TRS, DC Plan Valuations
NGNMRS and JRS Roll-Forward Reports

MS. ERCHINGER, as Actuarial Committee Chair, moved to accept the review and certification of actuarial reports by GRS. No second needed.

A roll call vote was taken, and the motion passed unanimously.

Action: Board Acceptance of FY15 Buck Valuations for PERS/TRS, DC Plan Valuations NGNMRS and JRS Roll-Forward Reports

MS. ERCHINGER, as Actuarial Committee Chair, moved to accept the actuarial valuation reports prepared by Buck Consultants for the PERS, TRS, PERS DC for Occupational Death and Disability and Retiree Medical Benefits, TRS DC for Occupational Death and Disability and Retiree Medical Benefits, and the roll-forward valuation reports for JRS and NGNMRS as of June 30, 2015, as amended by mutual agreement of Buck Consultants and GRS, subject to such cover letter as the ARMB may deem appropriate. No second needed.

A roll call vote was taken, and the motion passed unanimously.

Action: Board Acceptance of Audit Findings Report and Proposed Resolution of Findings

MS. ERCHINGER, as Actuarial Committee Chair, moved to accept the resolutions and findings as indicated on the audit findings lists dated June 23, 2016. No second needed.

A roll call vote was taken, and the motion passed unanimously.

10. PERFORMANCE MEASUREMENT - 1ST QUARTER

MR. ERLENDSON reported the performance of the funds in general has been meeting objectives. He believes the Brexit decision does not fundamentally change the risk exposure that is appropriate for the portfolio. MR. ERLENDSON commented the ARMB policy is sound, prudent and long-term in nature. The portfolio's investment managers are qualified, informed and prudent. He stated the monitoring of the Brexit situation will continue and Board and staff will remain informed.

VICE-CHAIR JOHNSON inquired if there were any specific issues regarding Baillie Gifford. MR. ERLENDSON expressed no immediate concern and noted the bulk of those working at Baillie Gifford are UK citizens.

MR. ERLENDSON continued with an economic overview through the end of March. The real GDP growth has been below average at around 2%. The developed markets are expected to have struggles trying to reach the long-term historical average growth rates. Inflation continues to be very moderate, even with the slight uptick in oil prices. The employment participation rate is the lowest it has been since the 1970s at 62.2%. This is due to reasons such as early retirement, becoming disabled, or participation in college. Bond yields around the world remain low, with some countries' yields below zero.

MR. ERLENDSON reviewed the volatile first quarter in the equity markets. Expectations are the market volatility will continue to increase in the short-term. It is vitally important to rebalance and keep asset allocation targets in place during the volatile times. Emerging markets was the strongest performing asset class for the quarter and expected growth rates are twice that of the developed world. The currency exposure was a significant detractor last year because of the strong dollar, costing investors about 5% after conversion. The dollar started to weaken in the first quarter. Real estate has been one of the best performing asset classes over the last five years providing strong double-digit returns. REITs have remained strong over this time period as well.

MR. CENTER discussed the PERS plan as an illustrated example of all the retirement plans. The asset allocation remains very close to the target allocation. As compared to its public fund peers, the plan's allocation is underweight fixed income and overweight global non-U.S. equities. Over three years, the plans are exceeding the benchmark and are above the median versus peers. Most of the drivers of performance have come from the active managers within the plan, some positive performance from private equity and a little drag on the real assets side. The actuarial return target has been difficult to keep up with since the 2008 financial crisis. The total fund performance has exceeded the target benchmark for many periods, which is closing the gap with the actuarial return target.

MR. CENTER reported on the total domestic equity exposure within the plan over the last quarter, which trailed both the S&P 500 and the Russell 3000 benchmarks. Most of the underperformance was driven by active managers because of the high level of volatility during the first quarter. The alternative equity portfolio had a very strong quarter dampening the overall portfolio volatility during this period of distress. Utilities were the strongest performing sector within the U.S. equity space.

MR. CENTER described the emerging market trend on the international portfolio that drove performance during the first quarter. The long-term international portfolio performance compares quite strong versus benchmarks. MR. CENTER informed the fixed income portfolio strategy is unique with exposure to very high quality bonds, non-U.S. bonds, and high yield bonds. Overall, the bond portfolio returned 3.8% for the quarter. The absolute return portfolio did well versus the benchmark. There are no concerns at this time with the constituents within the absolute return portfolio.

MR. CENTER reviewed the stoplight page representing the Balanced and Target Date Fund options within the Defined Contribution plan and stated there were no areas of concern. The social responsible equity space has been very difficult for managers to add value over time. There are not many strategies that have performed well versus a non-socially responsible benchmark. MR. CENTER stated there are no concerns with the passive strategies held in the plans.

UNFINISHED BUSINESS

1. **Calendar**
   Action: Adopt Proposed 2017 Calendar

MS. HALL noted the calendar updates. The September meeting location has been changed from Fairbanks to Anchorage. The Audit Committee will have the annual teleconference meeting for financial statements on November 3rd, 2016.

MS. HALL stated the proposed 2017 calendar was included in the Board's packet and requested approval.

MRS. HARBO moved to accept the proposed 2017 calendar. MS. ERCHINGER seconded the motion.

VICE-CHAIR JOHNSON expressed disappointment with the absence of an education conference in October. He understands travel is restricted during these fiscally restrained times, but is concerned about fulfilling the statutory mandate for the Board's education. MR. BADER stated staff is working on addressing the statutory mandated education requirement while adhering to the limitations of travel placed by the Administration and will have more information at the September meeting. Options may include dedicating one day of the September meeting to education only, carving out a portion of every Board meeting solely for education, sending Board members to a conference covering a broad range of topics, or calling in specialists to supplement education.

The motion passed unanimously.

2. Disclosure Report

MS. HALL indicated the Disclosure Report was included in the Board's packet. There was nothing unusual to report.

3. Legal Report

MR. GOERING had nothing new to report.

CHAIR SCHUBERT recessed the meeting from 11:57 a.m. to 1:17 p.m.

11. GLOBAL VS REGIONAL PORTFOLIOS

CHAIR SCHUBERT welcomed KAREN MCQUISTON of Prudential, the parent company of Jennison Associates. MS. MCQUISTON informed the advisory work she will present was completed before she transitioned to the investment management business of Prudential. Jennison manages both global and regional world equity portfolios and researched the dynamics from an institutional perspective of the active management investments in global and regional portfolios. The global portfolios are benchmarked to the MSCI ACWI or the MSCI World Index. The regional portfolios are standard long-only mutual funds benchmarked to the MSCI ACWI and consist equally of U.S. large cap, EAFE, and emerging market funds.

MS. MCQUISTON stated research shows individual security performance was more linked to industry and sector rather than country. She discussed the three sections of research; 1) global investments compared to regional investments, 2) the role of active management, and 3) the role of combining global and regional approaches. MS. MCQUISTON explained graphics illustrating the risk/return charts over multiple five-year periods for global and regional funds. She reported on the reduced risk findings when managers were randomly combined in groups of five, 10, and 20 managers. The combination of global funds produced a median excess return distribution of around 200 basis points. The combination of regional funds produced a median excess return distribution of approximately 160 to 170 basis points.

MS. MCQUISTON discussed information ratio, which is excess return over tracking error, and noted the tracking error is decreased when global managers are combined, and decreased more when regional managers are combined. The global approach tended to have a slightly lower overall relative volatility than the regional approach. The regional approach was closer to the index volatility.

MS. MCQUISTON stated the three ways the study measured actively managed funds were; 1) the level of concentration, 2) the level of active share, and 3) tracking error relative to the index. Both the excess return and information ratio increase with the combination of active funds, and the tracking error for both global and regional approaches increases with active funds. Global funds have reduced relative volatility with actively managed funds. The study showed actively managed funds are not necessarily riskier than the index. The study showed global managers and more active managers tended to present greater excess returns and the regional approach and less active managers tended to keep a tighter tracking error. The study showed the combination of global and regional approaches reduced both tracking error and overall volatility.

DR. JENNINGS highlighted the practice of generating excess return by rebalancing the global equities portfolio. He cautioned more concentrated managers take on more risk and the managers shown in the study are a subset that have survived for five years or more.

MR. WILLIAMS asked if the study was able to sort for quality of managers. MS. MCQUISTON advised this study utilized random managers and did not address past performance.

12. SCIENTIFIC BETA NORTH AMERICA

CHAIR SCHUBERT introduced MARK ZIEGER, Director, and ERIC SHIRBINI, PHD., Global Product Specialist, of Scientific Beta who presented the benefits of multi-smart factor investing. MR. ZIEGER explained Scientific Beta is part of the French EDHEC-Risk Institute business school and has been in the market since 2012. Scientific Beta does not manage money. The company is an index provider, giving the tools for portfolio management to invest assets according to a 100% transparent rules-based approach. The indices focus on smart beta, which is the systematic harvesting of factor risk premium to achieve a smooth out-performance of the benchmarks at a cost effective price. The company has attracted approximately $10 billion mainly from pension plans and sovereign wealth funds.

MR. SHIRBINI continued the presentation explaining smart beta wraps the well-known, well-understood risk factors into an index strategy, which is rules-driven and very cost effective. The beta element in smart beta refers to the risk factors. The smart element in smart beta refers to the way access to the risk factors is provided. Scientific Beta uses empirical evidence from years of studies to determine their main risk factors and include the equity market itself, value factor, momentum factor, low-risk factor, and size factor. Each of these factors contains an economic rationale to explain its relevancy. MR. SHIRBINI continued a detailed explanation of the risk factors utilized in smart beta.

MR. SHIRBINI noted smart beta is providing the performance of active managers in a very cost effective way and active managers have pushed back claiming a crowding effect will decrease returns as flows into successful smart beta strategies increase. MR. SHIRBINI explained markets do not respond to the crowding effect as suggested by active managers. The markets do not have a correction because everyone is invested in them. Markets have a correction because of some economic fundamental happening in the market at a particular point in time. The same is true for risk factors and has nothing to do with crowding.

MR. SHIRBINI reviewed the index construction strategy utilized to provide exposure to the risk factors. The first stage is to choose 250 stocks out of the S&P 500 with the highest risk exposure and the second stage is to apply a cap-weighted factor to give a well-diversified portfolio. MR. SHIRBINI continued the presentation describing the technical process of the index selection.

COMMISSIONER FISHER requested further explanation as to why only four risk factors are used rather than the known broader range of factors. MR. SHIRBINI replied the value and size factor were first documented in academic studies in 1990. The momentum factor was added in 1997. The low volatility factor was added in 2006. Academics have come up with two new factors within the last two years; quality and high profitability/low investment. The newest two can be included, if requested. MR. SHIRBINI explained there are hundreds of factors and Scientific Beta uses the four risk factors that are well-established, have empirical data, and have delivered performance.

COMMISSIONER FISHER asked for additional information regarding the crowding effect. MR. SHIRBINI gave the example if everyone invested in the S&P 500 and at some point, the S&P 500 had a correction, the reason for the correction is not that there were too many investors. The correction occurred because something happened in the economy. The same is true for the other factors as well. The factors will experience a draw-down at some point and a reward at some point. There is no market timing. The intent is to hold onto the risk factors through the cycles.

MR. WILLIAMS asked if MR. SHIRBINI has any studies that show crowding is not occurring and has not been an issue. MR. SHIRBINI advised there are studies showing the risk factors are cyclical. He believe the best thing to do is let the cycles happen and get the additional 2.5% to 4% reward for holding through those cycles. MR. ZIEGER informed the individual factors happen at different times in the cycle and combining different factor portfolios may provide a smoothing effect as shown in the performance review.

DR. JENNINGS commented the four risk factors used by Scientific Beta are well-established, well-accepted and academically sound. He noted this presentation is similar to one presented in New York suggesting a dedicated allocation for part of the long-term portfolio utilizing risk factor data.

MR. ERLENDSON requested additional information on the mechanics of managing the portfolio and examples of who has utilized this strategy. MR. SHIRBINI discussed some of the built-in rules for the portfolio. For all of the portfolio indices, turnover does not exceed 30% annually. The S&P 500 Index typically has a 4% turnover per year. The portfolio may not contain more than 10 times the weight of an individual security that exists in the index. MR. ZIEGER informed some of the public plans that utilize this strategy include State Board of Administration in Florida, Ohio State Teachers, Colorado Fire and Police, and City of Austin. He noted the index models are rules-based and completely transparent.

13. JENNISON ASSOCIATES

CHAIR SCHUBERT introduced PETER REINEMANN, Managing Director, and SHEETAL PRASAD, Portfolio Manager, from Jennison Associates. MR. REINEMANN informed Jennison has a full 11 years relationship with the ARM Board. MS. PRASAD has been with Jennison since 2007. MR. REINEMANN provided background information on Jennison, who manages approximately $167 billion in total assets. Jennison's capacity-constrained strategies include small cap, SMid cap, and mid cap growth. MR. REINEMANN informed Jennison has been going through the iterative process of selecting a chief executive officer since January and expects the process to be complete by the end of the year. The previous CEO took a position with another investment manager. MR. REINEMANN stated the firm is operating quite successfully in this challenging period for active managers.

MS. PRASAD informed there has been no change in the exemplary investment team or the process since the last update before the Board. MR. BADER requested more information on the roles of listed executives JASON SWIATEK and JOHN MULLMAN. MS. PRASAD explained MR. MULLMAN is the head of the small and mid cap team. MR. SWIATEK is the lead of the small cap portfolio team.

MS. PRASAD reviewed the detailed quantitative process used to select the portfolio of stocks. It includes a collaborative effort between the analysts and the portfolio managers, who use the models, thesis statements, and quarterly write-ups to guide the investment process. The ARMB portfolio annualized return since its 2005 inception is 9.9% versus 7.7% for the Russell 2000. MS. PRASAD showed performance numbers for the portfolio in various different market environments.

MS. PRASAD explained the tough start to the beginning of this year relates to interest rates and is viewed as a short-term issue. The portfolio is currently overweight banks, which is a sector that has been challenged by the low interest rates. The portfolio is currently underweight utilities, which is a sector that has done very well since they are often a substitute for bonds.

MS. PRASAD reviewed a few of the specific portfolio stocks and their favorable characteristics. She reported the portfolio has a steady nature with a high earnings growth and a low P/E multiple compared to the Russell 2000. The portfolio turnover remains consistent at 40% to 60% and the portfolio is built from the bottom up. No sector is more than 200 basis points overweight or underweight. MS. PRASAD shared the selection process for the companies. She noted the managers get to know the companies over time and are able to build larger positions as the companies execute.

MS. PRASAD discussed the current market environment and believes there are many cross-currents in the economy now, including the Brexit decision and other global issues in terms of infrastructure. The U.S. consumer seems relatively healthy. Housing and autos are strong for now. Oil remains low and manufacturing is in a recession. MS. PRASAD believes the low growth environment will remain for the medium term. There are still good industries and great businesses available. The mergers and acquisition activity has opportunity and the portfolio has had five acquisitions year-to-date.

CHAIR SCHUBERT recessed the meeting from 2:58 p.m. to 3:08 p.m.

14. HANCOCK TIMBER

MR. BADER introduced KATIE AMRHEIN, Senior Portfolio Manager, of Hancock Timber Resource Group, who provided a detailed presentation reviewing the timberland portfolio. The Hancock Timber Resource Group has roughly $11.5 billion in assets under management that involve over six million acres in investments across the globe. Timberland provides diversification benefits, an inflation hedge, and has a low to negative correlation with major asset classes. The timberland portfolio focuses on total return, looking for both income and appreciation in investments.

MS. AMRHEIN explained the domestic portfolio is managed by the Hancock Forest Management affiliate. The management is in-house and aligned with investor objectives. The third-party certification for the Alaska portfolio is provided by SFI. The primary goal of the real assets portfolio is to generate attractive returns in assets which provide diversification and inflation hedging to the total portfolio. The strategy is a lower risk/lower return, conservative, low leverage approach with a focus on high quality assets with stable returns.

MS. AMRHEIN reviewed the portfolio was initiated in 2009 and the committed capital came in over a period of time totalling $244 million. Contributions since inception total $77 million and distributions totaled $12 million. The current NAV is $99 million. The three wholly owned investments are currently held in the U.S. and are Tallapoosa, a 20,000-acre property with a market value of $41 million, Fishhawk, a 3,700-acre property with a market value of $23 million, and Elk River, a 10,000-acre property with a market value of $33.2 million.

MS. AMRHEIN continued the presentation comparing the rolling five-year average objective of 5% to the portfolio's five-year return of 7.3%. The NCREIF Timberland Index for the same period returned 6.6%. The portfolio has averaged a 2.1% cash yield over the previous five years. MS. AMRHEIN described the driver for portfolio performance in the near-term is the recovery in the demand for residential construction.

VICE-CHAIR JOHNSON asked if fire insurance is available for these properties. MS. AMRHEIN indicated there is no fire insurance, but the properties are actively maintained which minimizes the fire risk. She noted fire damage historically in the U.S. has been minimal and there has been one catastrophic fire event in Australia in 2009.

MR. ERLENDSON requested discussion about global economic activity and markets for timber. MS. AMRHEIN indicated this portfolio benefitted from the post-global financial crisis phenomena of Asia markets coming back into the Pacific Northwest on a cycle to acquire timber, which coincided with a period with the U.S. dollar was relatively weak. That cycle has passed. The domestic market now has the capacity to consume the volume generated from the Pacific Northwest.

15. INVESTMENT/PROCUREMENT ACTIONS

A. Scientific Beta

MR. BADER invited BOB MITCHELL, Deputy CIO, to join him and answer relevant questions. MR. BADER outlined the presentation by Scientific Beta. It is the desire of staff to bring more assets under internal management. This action requests the Board's permission to subscribe to the indexes provided by Scientific Beta so staff may invest internally. The cost of the contract will be negotiated between four and six basis points.

MR. BRICE moved to authorize staff to contract with Scientific Beta to receive the constituents of the multi-beta multi-strategy indices, subject to successful fee and contractual negotiations, and to invest up to $200 million in a domestic equity strategy benchmarked against the S&P 500 Index. MRS. HARBO seconded the motion.

A roll call vote was taken, and the motion passed unanimously.

B. Manager Review

MR. BADER noted the manager review termination of Luther King Small Cap is provided in the Board packet. The ARMB has been investing with Luther King Asset Management since 2005. Over the last 10 years, Luther King's investment returned 4.36% versus the index of 5.26%. The return has not measured up to the standard staff believes is appropriate for small cap holdings. Regrettably, staff is asking the Board authorize termination of Luther King's association in the small cap space.

MRS. HARBO moved to authorize staff to terminate the Board's association with Luther King in the small cap space. MR. WILLIAMS seconded the motion.

A roll call vote was taken, and the motion passed unanimously.

C. Contract Extension - GRS

MR. BADER reported the contract with GRS runs out on June 30th, and this is a request for the Board to authorize staff to renew the contract.

MRS. HARBO moved to authorize staff to renew the contract with Gabriel Roeder Smith. MR. BRICE seconded the motion.

VICE-CHAIR JOHNSON expressed he is in favor of the extension and believes MS. THOMPSON on behalf of GRS provides excellent service.

A roll call vote was taken, and the motion passed unanimously.

NEW BUSINESS

None

OTHER MATTERS TO PROPERLY COME BEFORE THE BOARD

None

PUBLIC/MEMBER COMMENTS

None

INVESTMENT ADVISORY COUNCIL COMMENTS

None

TRUSTEE COMMENTS

MS. ERCHINGER specifically requested Resolution 2016-10 that passed earlier in the meeting be distributed directly the Alaska Permanent Fund Corporation Trustees, as well as the management. MS. ERCHINGER requested KPMG's scope of work regarding cost benefit analysis of the potential for shifting management responsibilities either to the Department of Revenue or to the Alaska Permanent Fund Corporation also include a specific analysis of the impact of savings or costs accrued to the retirement systems.

MS. ERCHINGER offered sincere appreciation to the entire investment staff of the Department of Revenue. She suspected the legislative intent language may have been unsettling to staff. MS. ERCHINGER stated more and more investments have been moved in-house based on the excellent track record of the Department of Revenue staff and Trustee's growing confidence in the tenure, qualifications, and impressive investment performance of those same staff. MR. BADER informed he will pass MS. ERCHINGER's requests onto the Permanent Fund Corporation, who is managing the KPMG contract.

VICE-CHAIR JOHNSON shares MS. ERCHINGER's compliments to the excellent staff.

FUTURE AGENDA ITEMS

None

ADJOURNMENT

There being no objection and no further business to come before the Board, the meeting was adjourned at 3:45 p.m. On June 24, 2016, on a motion made by MRS. HARBO and seconded by MR. WILLIAMS.

Chair of the Board of Trustees
Alaska Retirement Management Board

ATTEST:

Gayle Harbo

Corporate Secretary