

VERMONT STATE TEACHERS' RETIREMENT SYSTEM

Meeting of the Board of Trustees

March 21, 2005

Board Members present:

JOSEPH MACKEY, Chairperson (Active No. 29334), term expiring July 1, 2005

JAY KAPLAN, Association of Retired Teachers of Vermont, term expiring July 1, 2008

THOMAS CANDON, representing Commissioner of BISHCA

VAUGHN ALTEMUS, representing Commissioner of Education

JEB SPAULDING, VT State Treasurer

Board Members absent:

JON HARRIS, Vice-Chairperson (Active No. 25669), term expiring July 1, 2007

Also attending:

David Minot, Director of Investment Services

Ellen Griggs, New England Pension Consultants

Steve Jeffrey, Vermont Municipal Employees' Retirement System

Marie Duquette, Vermont Municipal Employees' Retirement System

Jim Reardon, Vermont State Employees' Retirement System

Linda McIntire, Vermont State Employees' Retirement System

Catherine Simpson, Vermont State Employees' Retirement System

William Harkness, Vermont State Employees, Retirement System

Janice Abair, Vermont State Employees' Retirement System

The Chairperson, Joe Mackey, called the meeting to order at 8:45 a.m. on Tuesday, March 21, 2005, held in the Suzanna's Restaurant Conference Room at the Hilltop Inn, Airport Road, Berlin, Vermont.

ITEM 1: Investment Consultant Summary

Ms. Griggs reviewed the selection process to date, and managers selected for finalist presentation. She said on Wednesday, February 16th NEPC met with the Vermont State Teachers' Board to discuss the results of the International Equity Search. The Teachers' initiated the search to find a replacement for the Putnam/EAFE Index Fund currently held by SsgA, and 5 finalists were selected.

ITEM 2: International Equity Manager Finalist Presentations

Acadian Asset Management

Brendan O. Bradley, Senior Vice President and Research Officer, and Jack W. Gastler, Senior Vice President, appeared before the Board. Mr. Gastler stated both he personally, and his firm, were opposed to the privatization of Social Security.

This firm is located in Boston, Massachusetts and was founded in 1977 by Gary Bergstrom, who was previously with Putnam Investments. Mr. Bergstrom also collaborated until 1987 with State Street Global, working on their international index fund. In 1992, Acadian was purchased by United Asset Management ("UAM"), in 2000 UAM was purchased by Old Mutual PLC, and is a registered investment advisor. Acadian is now an affiliate of Old Mutual, and holds 20% equity stake in their future growth. Total firm assets were approximately \$15.6B with product assets totaling approximately \$1.5B.

Acadian builds their non-US All-Cap MSCI EAFE indexed portfolios from the bottom up using a quantitative process that drives all portfolio security buys and sells as well as country and currency allocations. Acadian customizes their models by market and sector. They measure over 20 factors and focus on those factors proven most effective at predicting returns. This model uses a number of factors to forecast the returns of country/sector groups on a world-relative basis. Acadian then combines the stock and country-sector expected returns to rank the entire universe of securities from most to least attractive. Value added is largely driven by security selection (65%) with smaller amounts from sector, country and currency selections. Acadian runs a well-diversified, actively managed, portfolio with approximately 140 names with the product's market capitalization focus on all caps.

Grantham, Mayo, Van Otterloo & Co. (GMO)

Thomas Hancock, Director of International Developed Markets, and Andrew A. Tamoney, Business Development and Client Services, appeared before the Board. Mr. Tamoney advised the Board that GMO does not contribute to any organization in support of the privatization of Social Security.

This company has offices located in Boston, Sydney, London, and Zurich and is 100% employee owned. Grantham, Mayo, Van Otterloo & Company is organized as a partnership. Active employees currently own the business with Mr. Grantham, Mr. Mayo, and Mr. Van Otterloo owning over 75% of the partnership. GMO has \$81B in total assets and \$6.5B in product assets.

GMO builds their World ex-US, Intrinsic Value, MSCI EAFE indexed portfolio through a quantitative combination of top down/bottom up strategies. The International Intrinsic Value Fund is constructed using an optimization process that weighs the tradeoff between a stock's return forecast and its contribution to the risk of the portfolio in comparison to the benchmark. The Fund uses disciplined value techniques to assess countries, sectors (big vs. small, cyclical vs. defensive), currencies, and stocks. Risk and return forecasts are made for sectors, currencies and stocks using historical, current and future estimates of financial data that relate the current economic scenario to future return patterns. The majority of value added comes from security selection with smaller portions of value added generated from sector selection, country and currency selection. GMO is the most diversified of the group and would hold approximately 350 securities with the product's market capitalization focus on all caps.

Mondrian Investment Partners, Ltd.

Clive Gilmore, Deputy Managing Director, and Patricia M. Karoli, Executive Vice President, appeared before the Board. Mr. Gilmore advised the Board Mondrian Investment Partners does not and would not contribute to any organizations in support of the privatization of Social Security.

This company has offices located in London, and Philadelphia. Mondrian recently completed a management led buyout from Delaware. They are a partnership with ownership spread across most employees (senior management owns 55%) as well as Hellman and Fredman LLC. The firm assets total approximately \$31B with 87% in this product's assets.

Mondrian is a value-oriented, qualitative/defensive manager who builds their S&P/Citigroup PMI EPAC portfolio using a bottom-up/top-down hybrid process to identify securities and markets that provide the greatest inflation adjusted returns. Mondrian's strategy begins with bottom-up fundamental analysis at the company level, in addition to the fundamental company analysis; portfolio managers evaluate attractive countries for favorable political, economic, and monetary environments. From this information, a country

allocation policy is set. Approximately 90% of Mondrian's research is conducted internally. Value added is 45% from security selection, and 30%, 20% and 5% from country, currency and sector selection, respectively with a typical portfolio consisting of 35-55 securities. The product's market capitalization focus is on all caps.

Pyrford International Plc.

Bruce Campbell, Chief Executive & Chief Investment Officer, and Paul Simons, Senior Research Analyst, appeared before the Board. Mr. Campbell advised the Board Pyrford International, does not contribute to any organizations in support of the privatization of Social Security.

This company's main office is located in London. Pyrford International was formed in 1991 following the purchase of Elders Investment Management (EIM) from the Australian-based Elders IXL Ltd. EIM was managed by Bruce Campbell who headed the buyout in 1991 in partnership with Euro Equity Holdings - a European investment Company. In October 2001, approximately 20% of Pyrford's equity was acquired by Strategic Investment Group Ventures LLC, a partnership between the Strategic Investment Group of Arlington, Virginia and the California Public Employees' Retirement System (CalPERS).

Pyrford's MSCI EAFE index investment strategy is based on a quantitative and qualitative, top-down, value-driven approach. They believe that they can produce superior, risk-adjusted returns over the long-term (i.e. 3-5 years) for their clients by utilizing fundamental analysis of world economies and markets. This process leads Pyrford to invest in those markets in which they feel value exists. They can, therefore, at times be absent from major markets and their country allocations can differ markedly from the relevant index or peer group averages. The first stage in the process is the country allocation and the next stage is stock selection. 60% of their value added comes from country selection and 40% comes from securities selection. Pyrford holds approximately 75-80 names and the product's market capitalization focus is on all caps. Pyrford has \$2.7B in total assets and \$1.8B in product assets.

UBS Global Asset Management

Kai Sotorp, Head of the America, Shawn Lytle, Managing Director and Portfolio Manager, and Steve Wilde, Executive Director Client Advisor, appeared before the Board. Mr. Sotorp advised the Board, UBS is committed to Defined Benefit systems, and while the firm does not take positions in political debates, UBS Asset Management Division does not support the privatization of Social Security.

UBS is located in Chicago, IL. and is a bank-affiliated advisor. In 1998 UBS was formed as a result of a merger between the Swiss Bank Corporation and the Union Bank of Switzerland. The firm assets total approximately \$482B with product assets totaling \$10.7B.

UBS's MSCI World (ex-U.S.) Equity Index, core (with value tilt) investment philosophy, is a combination of top down/bottom up research and is based upon the belief that discrepancies exist between price and fundamental value, both across and within non-U.S. equity markets. They are organized to take advantage of these discrepancies using a disciplined approach to measure fundamental value from the perspective of a longer-term investor. The non-U.S. strategy reflects the decisions about the relative attractiveness of the asset class, the individual equity markets, currencies, the industries across and within those markets and the individual companies. The primary decision rests with the country equity market allocation. At the

aggregate equity market level, a quantitative approach is used to establish value based on fundamental considerations. The fundamental value of each country's aggregate equity market takes into account differences between countries in growth, inflation and interest rates, risk and exchange rates. This product is driven in large part to security selection. 70% of their value added comes from security selection, 13% from sector decisions, 12% from country selection and 5% from currency selection. This well-diversified portfolio has approximately 110 names and the product's market capitalization focus is on large caps.

ITEM 3: Board Discussion

The Board discussed the finalist presentations. The Board overwhelmingly agreed to retain Mondrian Investment Partners, Ltd.

Mr. Kaplan made a motion seconded by Mr. Mackey, to instruct NEPC to enter into contract negotiations with Acadian Asset Management for 50% of the SSgA (after rebalancing) allocation, and add an additional 50% of the allocation to Mondrian Investment Partners, Ltd.

Mr. Spaulding made a motion seconded by Mr. Altemus, to amend the original motion to consider the entire international equity asset class allocation, and split the total, 50% to Mondrian and 50% to Acadian. Upon discussion, Mr. Spaulding withdrew his motion, and Mr. Altemus withdrew his second.

A vote on the original motion failed. Mr. Spaulding, Mr. Altemus, and Mr. Candon voted no. Mr. Mackey and Mr. Kaplan voted yes.

Mr. Spaulding made a motion seconded by Mr. Altemus, to hire Acadian Asset Management to replace SSgA and fund them with 50% of the total international equity asset class allocation and 50% to the existing manager, Mondrian. Motion failed, Mr. Spaulding, Mr. Altemus, and Mr. Candon voted yes. Mr. Mackey and Mr. Kaplan voted no.

Mr. Spaulding questioned why some members of the Board wanted to alter the prior 50/50 allocations between international equity managers. Mr. Kaplan said he that he understood Mondrian's product and methodology, he liked them and the people, historical allocations were not always 50/50, and wanted to reward Mondrian for past performance. Mr. Mackey said he believed the issue on the table was only the balance in SSgA, not the entire asset class allocation.

The Board agreed to take the matter up at the March 22, 2005 meeting.

Adjournment:

On a motion by Mr. Kaplan seconded by Mr. Altemus, the Board unanimously voted to adjourn at 3:55 p.m.

Respectfully submitted,

Donna Holden, Board Coordinator
For Cynthia Webster, Secretary to the Board