**VERMONT PENSION INVESTMENT COMMITTEE**
**May 24, 2011**

**VPIC Members Present:**
STEPHEN RAUH, CHAIR
BETH PEARCE, VICE-CHAIR, Vermont State Treasurer
VAUGHN ALTEMUS, Governor's Delegate, term expiring June 30, 2014
STEVEN JEFFREY, VMERS Representative, term expiring June 30, 2014
DICK JOHANNESEN, Governor's Delegate, term expiring June 30, 2014
JOSEPH MACKEY, VSTRS Representative, term expiring June 30, 2011
ROBERT HOOPER, VSERS Representative, term expiring June 30, 2012

**VPIC Member(s) *Absent*:**
NONE

**VPIC Alternate Members Present:**
THOMAS MCCONNELL, VSTRS *Alternate*, term expiring June 30, 2013
THOMAS GOLONKA, VMERS *Alternate*, term expiring June 30, 2012

**VPIC Alternate Member(s) *Absent*:**
KEVIN GAFFNEY, VSERS *Alternate*, term expiring June 30, 2012
KAREN PAUL, *Alternate* Governor's Delegate, term expiring June 30, 2012

Also attending:
Members of Vermont State Employees' Retirement System (via telephone)
Members of Vermont State Teachers' Retirement System (via telephone)
Steve Wisloski, Deputy State Treasurer
Matt Considine, CFA
Monica Chiren, Clerk
Bill Griffin, Chief Assistant Attorney General
Jaye Pershing Johnson, Assistant Attorney General
Linda Deliduka, VRTA Alternate Representative, VSTRS Board of Trustees
Chris Levell, CFA, and Kevin Kondry, NEPC LLC
David Driscoll and Kai Peterson, Buck Consultants, LLC

**CALL TO ORDER:**

The Chair, Mr. Rauh, called the Tuesday, May 24, 2011 meeting to order at 8:30 a.m., which was held in the 4th Floor Conference Room, 109 State Street, Montpelier, VT.

The Chairs of the Vermont State Employees' Retirement System (VSERS) and Vermont State Teachers' Retirement System (VSTRS) also called their boards' respective meetings to order.

**<u>ITEM 1:</u> Joint Meeting of VPIC, VSERS and VSTRS to Discuss and Adopt Actuarially Assumed Rates of Return**

Mr. Driscoll and Mr. Peterson reviewed the experience studies for VSERS and VSTRS for the five years from July 1, 2005 through June 30, 2010, and provided a detailed explanation of the "select-and-ultimate" methodology of determining an actuarially assumed rate of return on the systems' pension investments. They explained that in contrast to using a single rate of return, select-and-ultimate assumes a different rate of return for each year in the analysis, based upon a multi-factor analytical model of the expected return of various asset classes based upon variables such as inflation, gross domestic product, and unemployment. Due to current difficult economic conditions, the expected return in Year 1 is only 6.5%, while the longer-term equilibrium or "ultimate" expected return in Years 16 and after is 9.0%. The equivalent single rate of return for VSERS is approximately 8.1%, and for VSTRS is approximately 7.9%.

Mr. Hooper inquired as to whether any other pension plans use select-and-ultimate; Mr. Driscoll and Mr. Peterson replied that to their knowledge no State-level plans use it, however that it is gaining wider acceptance as a rigorous methodological approach to measuring pension liabilities.

**Ms. Pearce motioned, and Mr. Altemus seconded, the adoption of select-and-ultimate interest rate assumptions to determine the annual required pension contribution for fiscal year 2012 and going forward for VSERS and VSTRS. The Committee unanimously approved.**

The VSERS and VSTRS boards unanimously approved the motion for their respective systems, and adjourned their meetings at 9:15 a.m.

**<u>ITEM 2:</u> Agenda Approval, Announcements, and Minutes of April 26, 2011 Regular Meeting**

Mr. Rauh announced that the joint meeting to review and discuss the VMERS experience study would occur at the June 28 meeting. Mr. Wisloski advised the Committee that the Treasurer's Office would prepare the annual VPIC meeting and education session attending report for fiscal year 2011 as required by State statute.

**The Committee approved the Agenda.**

**On a motion by Mr. Hooper, seconded by Mr. Jeffrey, the Committee unanimously approved the minutes of the April 26, 2011 Regular Meeting.**

**<u>ITEM 3:</u> Review of Contracts**

**On a motion by Mr. Mackey, seconded by Mr. Altemus, the Committee unanimously approved a one-year extension of VPIC's contract with ISS to monitor investments in terrorist or genocide linked countries.**

**On a motion by Mr. Mackey, seconded by Mr. Hooper, the Committee unanimously approved moving the current holdings in the SSgA Russell 2500 index separately-managed fund into SSgA's S&P 400 Mid-Cap alternative, subject to successful contract negotiations.**

*The Committee entered executive session to discuss a contract matter at 9:45 a.m., and exited at 10:15 a.m.*

Mr. Wisloski reported that the target date for execution of the Wellington DAS contract amendment to switch the fund's beta source from the Barclay's Aggregate to 10-Year U.S. Treasury STRIPS was July 1, and the target for funding PIMCO's Unconstrained Bond Strategy was August 1.

*The Committee took a brief recess from 10:15 to 10:25 a.m.*

**<u>ITEM 4:</u> Use of iPads and Electronic Media**

The Committee discussed the possibility of moving to mostly paperless meetings, with presentation materials made available on iPads or notebook computers, and distributed either on the Treasurer's website or via a VPIC intranet. Mr. Golonka indicated that the Montpelier City Council meeting materials are all made available online and that software is available that enables users to make handwritten notes with a stylus on PDF files.

**Mr. Considine agreed to follow up with Mr. Golonka to explore possible paperless technologies for VPIC.**

**<u>ITEM 5:</u> Review of Managers on NEPC's Watch List**

Mr. Levell reported that Mellon (global asset allocation), Acadian (established international equity) and Post Advisory (high yield bonds) remain on NEPC's watch list. NEPC no longer includes Mellon in global asset allocation manager searches and was monitoring the implementation of Mellon's new global expanded alpha strategy, being launched July 1. Acadian's outlook has improved and may be removed from the list while Post's outlook remains less certain as that firm's leadership is in transition.

**NEPC agreed to arrange for Mellon Capital personnel to attend the June 28 meeting.**

**<u>ITEM 6:</u> Changes to Fixed Income Portfolios and Benchmarks**

The Committee discussed switching the beta source for Allianz Structured Alpha from the Barclays Aggregate to 10-Year Treasury Notes. NEPC confirmed that Allianz plans to purchase on-the-run (most recently issued) 10-Year Notes as they are issued, using sale proceeds from the liquidation of the previously purchased (off-the-run) 10-Year Note. NEPC stated the Treasury market has become liquid enough that there is not a persistent yield disadvantage to VPIC from selling off-the-runs to purchase on-the-runs.

**Mr. Jeffrey motioned, Mr. Altemus seconded, and the Committee unanimously approved switching the Allianz beta to 10-Year Treasury Notes on September 30th to correspond to the maturity of the current Barclays Aggregate swap.**

**The Committee also decided: (1) to retain the Barlcays Aggregate as the benchmark for PIMCO Core Plus; (2) to add an absolute return benchmark to be provided by NEPC for**

**PIMCO Unconstrained Bonds; and (3) to add a 10-Year T-STRIPS benchmark for Wellington DAS; and (4) a 10-Year T-Note benchmark for Allianz.**

**<u>ITEM 7:</u> Equity to Global Asset Allocation Discussion**

NEPC recommended that VPIC increase its global asset allocation exposure, specifically in risk parity, by 3% and, correspondingly, reduce PIMCO StocksPLUS (domestic large cap equity) by 1% and Acadian and Mondrian (established international equity) by 1% each. Mr. Levell stated that this would be expected to provide better inflation and deflation protection than traditional equities.

**The Committee asked NEPC to initiate a search for global asset allocation risk parity managers.**

*Mr. Johannesen joined the meeting at 12 noon.*

**<u>ITEM 8:</u> NEPC Q1 Portfolio Review**

NEPC reviewed performance results for the first quarter of 2011. Performance for the individual plans was as follows:

**VSTRS:**
The market value at quarter-end was **$1.502 billion,** the gross quarterly return was 3.4%, and the public funds median ranking was in the 84th percentile. The one-year return of 14.1% ranked in the 42nd percentile, three-year return of 3.5% ranked in the 65th percentile, and a five-year return of 4.2% ranked in the 64th percentile of the median public fund universe.

**VSERS:**
The market value at quarter-end was **$1.356 billion,** the gross quarterly return was 3.4%, and the public funds median ranking was in the 78th percentile. The one-year return of 14.5% ranked in the 32nd percentile, three-year return of 4.1% ranked in the 46th percentile, and a five-year return of 4.5% ranked in the 50th percentile of the median public fund universe.

**VMERS:**
The market value at quarter-end was **$388 million,** the gross quarterly return was 3.5%, and the public funds median ranking was in the 74th percentile. The one-year return of 14.3% ranked in the 36th percentile, three-year return of 4.4% ranked in the 37th percentile, and a five-year return of 4.7% ranked in the 39th percentile of the median public fund universe.

**BURLINGTON:**
The market value at quarter-end was **$121 million,** the gross quarterly return was 3.4%, and the public funds median ranking was in the 80th percentile. The one-year return of 14.5% ranked in the 32th percentile, and the three-year return of 3.9% ranked in the 53rd percentile. The inception date of this municipal deposit was November 1, 2007; therefore, further performance data was achieved prior to it joining VPIC. Burlington's five-year return of 4.1% was reported in the 70th percentile of the median funds universe.

**ITEM 9:** **Hedge Fund Shadow Portfolio**

In order to assist VPIC in evaluating the performance of its newly-added fund-of-funds mandates, NEPC provided performance information for five types of hedge fund strategies (global macro, credit, event driven, long-short equity, and multi-strategy) for managers both on and off NEPC's focused placement list (FPL).

**Mr. Rauh asked NEPC to provide performance for the four direct hedge funds previously suggested by NEPC in addition to performance for five core hedge fund strategies just reviewed.**

**ITEM 10:** **VPIC Economic and Financial Market Dashboard**

The Committee discussed the Economic and Financial Markets Dashboard and, based upon the sharp slowdown in 1st quarter GDP, uptick in unemployment, flat equity market performance since February, and renewed concerns about solvency of peripheral European countries, maintained its 12-month forward expectation for U.S. GDP at 2.5%, and for CPI at 3.0%. The Committee also lowered its outlook for both large cap domestic equities and commodities from "positive" to "neutral."

**ITEM 11:** **Director of Investments Report**

Mr. Considine and Mr. Wisloski reviewed the manager contributions to total return and alpha over the past quarter and year; that VPIC's "underwater" amount in securities lending had declined to $1.7 million; that asset allocation remained within 0.5% of target for VPIC's major asset classes; and that VPIC's assets under management increased to $3.453 billion as of April 30.

**ITEM 12**: **Other or New Business**

**Mr. Rauh confirmed that NEPC would provide risk analytics for the June meeting.**

**Ms. Pearce indicated that the Treasurer's Office would discuss operation risk management at the June meeting.**

**ITEM 13:** **Adjournment**

**On a motion from Mr. Jeffrey, seconded by Mr. Hooper, the Committee unanimously voted to adjourn at 3:20 p.m.**

Respectfully submitted,

Monica Chiren, Clerk