

**Minutes
Investment Advisory Council
May 16, 2013**

The Investment Advisory Council (IAC) met at 10:00 A.M. Thursday, May 16, 2013 in the Board Room – First Floor, 60 Empire Drive, St. Paul, Minnesota.

MEMBERS PRESENT: Jeff Bailey, John Bohan, Kerry Brick, Dennis Duerst, Kim Faust, Doug Gorence, Laurie Hacking, Jay Kiedrowski, Judy Mares Lazar, Gary Martin, Malcolm McDonald, Mary Vanek and Elaine Voss.

MEMBERS ABSENT: Denise Anderson, Dave Bergstrom, and Kristin Hanson (for Jim Schowalter)

SBI STAFF: Howard Bicker, Jim Heidelberg, LeaAnn Stagg, Tammy Brusehaver, Patricia Ammann, Stephanie Gleeson, Mike Menssen, Ryan Hill, John Griebenow, J.J. Kirby, Charlene Olson and Melissa Mader.

OTHERS ATTENDING: Ann Posey, Callan Associates Inc.; Micah Hines, Bert Black, Celeste Grant, Christie Eller, Edgar Hernandez, SEIU; Margaret Martin, Center of the American Experiment; Don Leathers, REAM.

The minutes of the February 19, 2013 meeting were approved.

Mr. Bicker gave members a brief update on the search process for a new Executive Director. He said the Committee will be interviewing three search firms out of the six which responded to the RFP.

Executive Director's Report

Mr. Bicker, Executive Director, referred members to Tab A of the meeting materials, and he reported that the Combined Funds had outperformed its Composite Index over the ten year period ending March 31, 2013 (Combined Funds 9.2% vs. Composite 9.0%) and had provided a real rate of return over the latest 20 year period (Combined Funds 8.2% vs. CPI 2.4%).

Mr. Bicker said that the Combined Funds' assets increased 0.7% (corrected later to be 4.9%) for the quarter ending March 31, 2013 due to positive market performance. He said that staff is in the process of rebalancing the asset mix back to targets, and he stated that the Combined Funds outperformed its Composite Index for the quarter (Combined Funds 6.1% vs. Composite 5.8%) and for the year (Combined Funds 11.0% vs. Composite 10.6%). Mr. Kiedrowski complemented staff on the Combined Fund's outperformance over all time periods.

Mr. Bicker reported that the domestic stock manager group matched its target for the quarter (Domestic Stocks 11.1% vs. Domestic Equity Asset Class Target 11.1%) and underperformed for the year (Domestic Stock 14.1% vs. Domestic Equity Asset Class Target 14.6%). He said the international stock manager group outperformed its target for the quarter (International Stock 4.1% vs. International Equity Asset Class Target 3.2%) and for the year (International Stock 9.9% vs. International Equity Asset Class Target 8.4%). Mr. Bicker stated that the bond segment outperformed its target for the quarter (Bonds 0.1% vs. Fixed Income Asset Class Target -0.1%) and for the year (Bonds 5.4% vs. Fixed Income Asset Class Target 3.8%). He stated that the alternative investments returned 2.7% for the quarter and 11.7% for the year. He concluded his report with the comment that, as of March 31, 2013, the SBI was responsible for over \$65 billion in assets.

Mr. Bicker referred members to Tab B of the meeting materials for an update on the budget and travel for the quarter. He said that the SBI had submitted legislation authorizing the SBI to invest in swaps, and he reported that there are currently two versions of the bill but that the swap language is identical in both bills. In response to a question from Mr. Bailey, Mr. Bicker briefly reviewed other legislation that impacts the various retirement systems. In response to questions, Ms. Vanek explained several changes being proposed in legislation for the Highway Patrol Fund and the Police and Fire Fund which will improve their funded status. Mr. Bicker stated that Tab B contains updated information on Sudan and Iran. Ms. Eller of the Attorney General's Office confirmed that there is currently no litigation involving the SBI.

SBI Administrative Committee Report

Mr. Bicker referred members to Tab C of the meeting materials and began his discussion on the FY14 Management and Budget Plan.

Mr. Bicker referred members to page 5 in Tab C of the meeting materials and discussed the proposed Workplan for FY14 and a number of major projects. He noted that staff will review transition management and that if swap legislation passes, staff will examine how swaps could be utilized by the SBI going forward. Mr. Bicker said that staff will also evaluate the use of derivatives securities and strategies in the Fixed Income Program. He added that staff will also be continuing to work on implementing a municipal bond investment pool, and he briefly reviewed several legal and accounting issues that still need to be resolved. He stated that a review of the investment options for the Unclassified Retirement Plan is also scheduled for next fiscal year. Mr. Bicker stated that staff will assess the impact of tri-party repo market reform and convert the current trading and internal control system to a new system with a new provider.

Mr. Bicker referred members to page 9 of Tab C of the meeting materials for information on the FY13 budget and the SBI's proposed budget for FY14 and FY15. He stated that the proposed budget includes several increases for severance costs, upfront cost for the new accounting systems, and various costs associated with the search and hiring of a new Executive Director.

Mr. Bicker referred members to page 11 of Tab C for information on the Continuing Fiduciary Education Plan, and he noted that staff had updated the SBI's Disaster Recovery Plan.

After a brief discussion, members and staff agreed to add a section to the proposed workplan titled "Transition Issues" stating that the new Executive Director shall meet with all parties involved in the investment process to develop on-going goals and objectives.

Mr. Bicker referred members to Tab E of the meeting materials and briefly reviewed staff recommendations regarding three managers. He said that staff is recommending the termination of INVESCO Global Asset Management, an international equity manager, due to organizational changes and continued underperformance. Mr. Gorence moved approval of staff's recommendation, as stated in Tab E of the meeting materials. Ms. Mares seconded the motion. The motion passed.

Mr. Bicker stated that staff is recommending the termination of UBS Global Asset Management, a domestic equity manager, due to staff turnover, loss of institutional assets and underperformance. Mr. Gorence moved approval of staff's recommendation, as stated in Tab E of the meeting materials. Ms. Mares seconded the motion. The motion passed.

Mr. Bicker reported that staff is also recommending the termination of another domestic equity manager, New Amsterdam Partners, due to continued performance concerns and the decision to eliminate the large core mandate. Mr. Gorence moved approval of staff's recommendation, as stated in Tab E of the meeting materials. Mr. McDonald seconded the motion. The motion passed. In response to a question from Ms. Faust, Mr. Bicker confirmed that the international assets were reallocated to the passive international manager and the active domestic assets were reallocated to active managers to minimize misfit within the equity segment. In response to a question regarding organizational changes at INTECH from Ms. Hacking, Mr. Bicker confirmed that staff is monitoring the situation. A brief discussion followed regarding the process the SBI uses when re-allocating funds when managers are terminated.

Mr. Bicker referred members to Tab F of the meeting materials and stated that staff is recommending new investments with three existing private equity managers, CVC Capital Partners, EBF & Associates and Varde Partners. He stated that staff is also recommending an extension of the fundraising time deadline for the SBI's commitment to Public Pension Capital (PPC) from June 30, 2013 to December 31, 2013. Mr. McDonald moved approval of all four of staff's recommendations as stated in Tab F of the meeting materials. Ms. Faust seconded the motion. A brief discussion followed on sizes of the various commitments. Ms. Mares suggested extending PPC's deadline to June 30, 2014, and staff and members agreed to that change. Mr. McDonald and Ms. Faust agreed to amend the motion to reflect the change. Ms. Voss noted she was recusing herself from the vote due to an affiliation with one of the proposed investments. The amended motion passed.

Mr. Bicker noted that the SBI Policy Book was ready for distribution to members for their reference. Ms. Vanek thanked staff for their work in preparing the book.

Mr. Kirby made a presentation regarding alternative investment commitment modeling. Mr. Bicker stated that staff will be preparing some recommendations for consideration at the August 2013 meeting.

The meeting adjourned at 11:25 A.M.

Respectfully submitted,

A handwritten signature in cursive script, reading "Howard Bicker".

Howard Bicker
Executive Director