1 NEW YORK CITY TEACHERS' RETIREMENT SYSTEM
INVESTMENT MEETING
2 held on Thursday, May 12, 2011
at
3 55 Water Street
New York, New York
4

5
ATTENDEES:
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7 MELVYN AARONSON, Chairperson, Trustee
SANDRA MARCH, Trustee
8 LISETTE NIEVES, Trustee
MONA ROMAIN, Trustee
9 LARRY SCHLOSS, Trustee, Comptroller's Office
RANJI NAGASWAMI, Trustee, Finance
10 NELSON SERRANO, Executive Director, TRS
VALERIE BUDZIK, Comptroller's Office
11 MARTIN GANTZ, Comptroller's Office
MARC GROSS, Comptroller's Office
12 SEEMA HINGORANI, Comptroller's Office
THADDEUS McTIGUE, Comptroller's Office
13 BARRY MILLER, Comptroller's Office
MARC KATZ, TRS
14 SUSAN STANG, TRS
ROBERT C. NORTH, JR., Actuary
15 DAVID MORTON, Rocaton
ROBIN PELISH, Rocaton
16 KAREN SEEMEN, Corporation Counsel
CAROLYN WOLPERT, Corporation Counsel
17 ROBERTA UFFORD
JAMIE SMARR
18 PAUL RAUCH

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2 P R O C E E D I N G S

3 (Time noted: 9:45 a.m.)

4 MR. SERRANO: Good morning, and welcome to

5 this broadcast of the May 12, 2011 investment meeting of

6 the New York Teachers' Retirement System.

7 I am Nelson Serrano, executive director of

8 the retirement system. We will begin today's meeting by

9 calling the role.

10 Melvyn Aaronson?

11 MR. AARONSON: Here.

12 MR. SERRANO: Kathleen Grimm?

13 (No response.)

14 MR. SERRANO: She is not present.

15 Lisette Nieves.

16 (No response.)

17 MR. SERRANO: She's also not present.

18 Sandra March.

19 MS. MARCH: Here.

20 MR. SERRANO: Ranji Nagaswami?

21 MS. NAGASWAMI: Here.

22 MR. SERRANO: Mona Romain?

23 MS. ROMAIN: Here.

24 MR. SERRANO: Larry Schloss?

25 MR. SCHLOSS: Here.

1 MR. SERRANO: So, we do have a quorum. We
2 need to elect an acting chairperson.
3 MS. MARCH: I nominate Melvyn Aaronson.
4 MR. SERRANO: Second.
5 MS. NAGASWAMI: Second.
6 MR. SERRANO: All in favor say "Aye."
7 (A chorus of "Ayes.")
8 Opposed.
9 Abstentions.
10 Hearing none, I'll turn it over to Mel.
11 CHAIRPERSON AARONSON: Thank you very much,
12 Nelson. Thank you, colleagues, for electing me to chair
13 this meeting.
14 And the first part of the meeting is going
15 to be a report from Rocaton on the variable funds.
16 MS. PELISH: Thank you, Mel.
17 Good morning. I think everyone should have
18 the March performance report for the variable funds.
19 I'm going to go fairly quickly in some form, but please
20 stop me if you have any questions.
21 At the end of March, the total assets in the
22 Variable A fund was about $10.4 billion. I'd like to
23 call your attention to -- for managers that were funded
24 during the month of March and the latest investors and
25 Aaronson and Johnson, low volatility strategy in the

1 defensive composite and in the actively managed
2 composite, see T. Rowe Price and Wasatch were added
3 during March.
4 With that, let me turn to page 2 for
5 performance. Modestly positive returns for U.S. equity
6 market during the month of March. You can see that on
7 page 2, the active managers in aggregate added value
8 relative to the index strategies, so that in aggregate
9 the total domestic manager composite was about 60 basis
10 points for the month, for the year-to-date period that
11 translates into a return of 6.6 percent. However, as
12 you know, and as highlighted on page 3, there's a
13 15 percent allocation to international equity strategies
14 within the Variable A portfolio to provide
15 diversification. And the EAFE index for U.S. investors
16 was negative during the month, actually fairly
17 significantly negative by over 2 percentage points.
18 So, with that, even though the international
19 composite actually did slightly better than the index
20 that brought the total Variable A return down to almost
21 flat, but slightly up 5 basis points for the month of
22 March and for the year-to-date period, the return of
23 5.6 percent.
24 MR. SCHLOSS: Robin, these are calendar
25 years?

1 MS. PELISH: No. Those are for the trailing
2 periods ending March.
3 MR. SCHLOSS: The year to date?
4 MS. PELISH: Year-to-date, yes.
5 (Ms. Nieves entered the meeting.)
6 CHAIRPERSON AARONSON: I'd like to announce
7 that Lisette Nieves has joined the meeting.
8 Welcome, Lisette. Thanks for having you
9 here.
10 MS. PELISH: Unless there are any other
11 questions on the Variable A report, we have an
12 up-to-date for the month of March for Variables C, D and
13 E, and a separate handout. And as I mentioned, as
14 international equity market were negative during the
15 month of March, so you can see that the Variable C,
16 which is the international equity fund was down about
17 1.9 percent for the month.
18 Again, modestly ahead of the index which was
19 down 2.2 percent of the year-to-date, this fund has
20 generated a positive return of about 3.2 percent.
21 The Variable D fund, which is the
22 inflation-protected fund, invested one vehicle with
23 PIMCO asset fund, was up almost 100 basis points for the
24 quarter, 73 basis points to be -- for the month, 73
25 basis points to be specific. For the year-to-date

1 period, that is up 2.7 percent.

2 And finally, Variable E, the socially

3 responsive equity fund, which is invested in the

4 Neuberger Berman socially responsive strategy had a

5 positive month of 44 basis points. And for the

6 year-to-date it was up just about 7 percent which is

7 100 basis points ahead of that fund benchmark, the 3500

8 index.

9 Any questions about these funds?

10 We have yet another handout, an estimate of

11 performance for the funds for the month of April. So,

12 as you know, each month using index data, we estimate

13 what Variable A is likely to have performed during that

14 month.

15 So, for the month of April, we see strongly

16 positive returns for the U.S. equity market up about

17 3 percent. And as well as for the fixed income market

18 is up over 100 basis points and particularly strong

19 returns for the EAFE index up over 6 percent.

20 So our estimate for the month of April is a

21 return for the Variable A fund of about 3.4 percent

22 which would yield the calendar year-to-date return of

23 over 9 percent. The all asset fund actually had another

24 good month up almost 3 percent for year-to-date return

25 of 5 1/2 percent. And the Neuberger Berman socially

1 responsive equity fund continued to do well up to
2 3.3 percent for the month of April for calendar
3 year-to-date return of about 10 1/2 percent.
4 So, good numbers during April.
5 And that concludes the public report for the
6 variable funds.
7 CHAIRPERSON AARONSON: Does anybody have any
8 questions for -- thank you very much, Robin.
9 And now, we'll turn to the public portion of
10 the pension fund.
11 MR. SCHLOSS: Let me hand out these colored
12 copies to everybody.
13 (Indicating.)
14 We have PIMCO here last month doing the
15 economy. So, I kind of go fast through the economy.
16 Couple of things have changed. And, again, this is all
17 as of March. March is a very complex month. If you
18 look on page 2 of the handout color copy.
19 It looks like the economy is slowing down
20 again. People revising the rest of this down. They
21 revised the month at the end of the year because of the
22 tax relief and it's not clear what the right numbers is
23 going to be. They grossed themselves up to
24 3 1/2 percent, maybe it's going to be three-ish, but I
25 think it is slowing down.

1 Having said that, if you look at the next
2 page, and I'd say it's slowing down not much to worry
3 about because it's just slowing down; which, again, it
4 should be ramping up. So, any pause is not necessarily
5 a good thing. Capacity utilization at the end is going
6 up.
7 The next page, manufacturing index. It
8 rolled a little, but my guess is it will be going up
9 with the unemployment claims. The trend is still
10 correct. But, again, its volatility in the monthly
11 numbers, the weekly numbers. The unemployment rate,
12 however, was back to 9 percent.
13 So, the yellow light on employment, again.
14 Consumer sentiment went down. But, again, this is
15 March. So, we have to remember what happened in March
16 was the tsunami and the earthquake. So, that probably
17 shook everyone's nerves. And at the same time in March,
18 it had the spread of the conflicts in the north of
19 Africa, the Middle East. So, it's sort of destabilized
20 month.
21 I'm concerned about on page 8, the cost and
22 architectural billings index is just a pre-cursor of
23 industrial construction. So, something to watch going
24 forward. Existing home sales are kind of in the
25 doldrums. The worst part is the next page 10, which is

1 new home starts. There's no reason to build a new house
2 because it's somewhat over than forecloses deem
3 happening. And this is a sector of the economy that,
4 again, the PIMCO just pointed out pretty nicely on the
5 chart last month, that it's just not happening.
6 And if it drags, you've got to pick up to
7 get construction going again. Workers hired again.
8 Retail sales, I can't tell you why it spiked, maybe it
9 was weather-related. It's an anomaly.
10 CHAIRPERSON AARONSON: Sandy and Mona went
11 shopping.
12 (Laughter.)
13 MR. SCHLOSS: All the sales on 12, again,
14 little parts in March, but I think it keeps going up.
15 Zero financing is back. Leading indicators look good
16 again on 13. Inflation is going up. The Fed's focused
17 on, on the one hand, but not worried about it. They
18 say, it's also one of the drags on the consumer because
19 price of gas had gone up, price of food had gone up.
20 So, pay attention, the fed says it's under control.
21 We'll see, a little bit of inflation is good. Too much
22 is not, obviously.
23 How does that affect the markets? If you go
24 to page 16. Recall that the biggest thing in the market
25 probably is what's going on in Europe and what's going

1 on with QE 2 ending in June. The bottom line is people
2 don't like dollar as much as the Europeans raised its
3 interest rate. So, they're going up. And we are
4 holding it down. Therefore, people like the euro better
5 than the dollar.
6 You can see it more graphically with the
7 dollar on page 17. Weak dollar is good for exports.
8 So, it actually benefits us in the short term. We have
9 a weak dollar, it doesn't benefit us in the long term.
10 This LIBOR is flat, which is good, and the banks in
11 Europe, at least, are a little better, at least, calm.
12 I don't think it's better at all, but it's calm. The
13 Vicks versus stock market volatility is very, very calm.
14 So, again, and I would tell you that it
15 could be 100 percent false, but it's calm for now.
16 Because there are very good thing that need to really
17 worry about. If you wanted to be a worrier, with the
18 Fed, with very, very low interest rates, doesn't want
19 you to worry. They want you to take risks.
20 Page 20, the white line in the current yield
21 curve basically the Fed likes it the way it is.
22 Ten-year treasuries are down which is inconsistent with
23 interest rates, with inflation going up. But I would
24 tell you that should be -- that's the real worry factor.
25 So, might not be in the stock market. It's definitely

1 in the bond market. It's the flight to bonds.
2 Treasuries, at least, because people are worried. It's
3 the corollary to that I would say is the price of gold
4 which is north of $1,500 an ounce. So, people don't
5 like paper. So, there is a lot of worries that
6 manifested in perhaps the different places than the
7 stock market.
8 On 22, you can see -- spread is tightening
9 again, people are in search of returns.
10 On page 23, you can see the three large
11 indices, the U.S., EAFE and emerging markets. This is
12 through April. Basically, it shows the evaluations are
13 not excessive.
14 May 4, thank you.
15 And what you will see if you just jump ahead
16 to page 25 -- so, again, if you look at the March
17 numbers, you see the tsunami is that it's clearly as
18 possible in the middle of March all the markets went
19 down, U.S., emerging and EAFE. And then calm came back
20 and they went back up.
21 And if you roll forward, as Robin just said,
22 April is a pretty good month. But, again, what we have
23 to talk about today is just the March numbers and point
24 to point March -- March ended up a little higher than it
25 started for getting deep in the middle, and all the

1 anxiety in the middle. So, March numbers show in the
2 second, things are all right. March MA activity is
3 picking up, that's good. Corporations have a lot of
4 cash in the balance sheet and it's a big signal about
5 the CEO confidence when they start buying businesses.
6 What does that mean to Teachers? Page 27,
7 at $42 1/4 billion, the highest ever. So, we are
8 working well.
9 And if you look on the next page, page 28,
10 on a calendar year basis -- or on a fiscal year basis,
11 where it was at the end of June, we're up substantially,
12 from the mid-30s, to the mid-40s. And fast forward to
13 April, April is about a billion dollars more. So, north
14 of $43 billion. So, again, things look good.
15 The reason they're looking good in our
16 numbers on page 29 is primarily the overweight to
17 equities, particularly U.S. equities. And it's pretty
18 much underweighted fixed income. We're going to talk
19 about opportunistic fixed income later today as a place
20 to make money.
21 But that's the biggest thing that were
22 overweighted to U.S. equities.
23 If you go to page 31, you can see where we
24 made our money last month in U.S. equities and sleeper,
25 if you will, private equity. Private equity, if you

1 recall, is lagging. So, we don't have all the yearend
2 numbers, but these are yearend numbers that we're
3 putting into the returns in all last year. The equity
4 markets went up and the private equity starts to reflect
5 that in a yearend valuations. That's why that's up as
6 much as it is. But, again, last month, in a very
7 complicated month, which was March, we made money for
8 three months. This year to date we have about almost
9 22 percent. But most importantly, three years which
10 includes the mess in 2008, we're back up to 4 percent
11 throughout. So, all back, and then some.
12 On 32, you just glance your eyes down to
13 March, low volatility with basically no runs, no hits,
14 no errors. They were all basically where they were
15 beginning of the month. Now, the April numbers are up,
16 as Robin mentioned, so, again, we'll be making money in
17 April.
18 We don't really have much to talk about on
19 the managers. Next month, we will have a quarterly
20 report so we have more managers commentary in detail.
21 If anyone has any questions, we'll be happy to answer
22 questions on the managers. But, again, overall the
23 portfolio held up very, very well given all the
24 volatility that went on in the month of March, and April
25 is up.

1 So, I think the portfolio is in pretty good
2 shape.
3 Does anyone have any questions on the month
4 of March?
5 (Mr. Smarr entered the meeting.)
6 CHAIRPERSON AARONSON: And before we go on
7 to the next thing, let the record show that Jamie Smarr
8 has joined.
9 Welcome.
10 MR. SCHLOSS: All set on March? That's
11 pretty difficult month, but all is well that ends well.
12 The second part of the agenda is the
13 emerging managers. Seema and Mark are going to walk us
14 through a presentation.
15 MS. HINGORANI: Mark is passing out the
16 color copy version.
17 So, we want to go through some background on
18 the emerging managers program and talk a little bit
19 about what we might propose to the board going forward.
20 So, if you turn to page 2, just a little background on
21 the program. So, emerging managers are those that are a
22 bit smaller, don't have enough assets under management
23 yet they'll be considered as standalone mandates.
24 Teachers has elected to invest the emerging
25 manager through emerging manager of managers, which

1 is -- these are the fund to funds. They will go out and
2 invest in smaller managers. They create a portfolio for
3 us. And they're monitoring these managers on an ongoing
4 basis. They're monitoring not only the performance but
5 the risk of the overall portfolio and they're giving us
6 these updates, at least, month end.
7 And then one last thing on the sub managers
8 which are the underlying managers within these fund to
9 funds. The way that the program had been defined was
10 that an emerging manager would be one until they reach
11 about a billion dollars in assets under management.
12 Slide 3, this gives the history. So, this
13 goes back to November 2007 when Teachers invested
14 $270 million with five of these emerging managers. At
15 that time, the investment totaled about 12 percent of
16 the active portion under U.S. equities investments and
17 almost a percent of total assets.
18 The names of the managers are listed below
19 and the amounts. And as you might remember, we
20 terminated Bivium Capital last year.
21 Turn to the next slide, 4, we give you a
22 sense of where the money is today and the current market
23 value. So, in aggregate, roughly $240 million is
24 invested in four new emerging manager and managers which
25 represents almost 30 percent of the active U.S. equities

1 investments for Teachers and about 50 basis points of
2 the total assets.
3 If you look at slide 5, just to give you a
4 sense of since inception performance of the emerging
5 manager and managers, and I'll just point you to a
6 couple of columns. So, if you scroll down to the bottom
7 row there, the 2010 numbers and you go across to the
8 since inception excess return column, which is towards
9 the far right.
10 These managers have outperformed by 107
11 basis points. This is net of fees and that since
12 inception which is December of 2007. And if you fast
13 forward a little bit to March 31st of this year, that
14 number is -- you're up about 143 basis points net of
15 fees and that's an excess return. So, the program has
16 done quite well. And the benchmark is a Russell 3000
17 index.
18 Turn to the next slide 6, we start going
19 through some of our recommendations. One, is to bring
20 up to Teachers that since we terminated Bivium, back in
21 2010, and that total was about $33 million when we
22 terminated them. We also, you might remember, we
23 terminated Lombardia, which is a developing manager.
24 And at the time, that amount was $135 million. So,
25 roughly $107 million had been terminated.

1 And we shifted that money as you might
2 remember to mid-cap, small cap passive, that
3 reallocation. So, we have wanted to present that, go
4 out and issue an RFP to see who else is out there
5 because the last time we did the RFP, they're about 12
6 managers that submitted. And we think there are
7 probably 15 to 20 out there now that would consider
8 submitting to the RFP.
9 And importantly, since almost 30 percent of
10 your active assets in U.S. equities is the emerging
11 manager program, there are other asset classes that
12 emerging managers could present to us. And one of the
13 other systems, actually, has some money in EAFE, in
14 emerging managers and managers and also in fixed income.
15 And so, we could just see who else was out there across
16 those other asset classes. And we think this would just
17 increase the opportunity for this program for emerging
18 managers and managers which are minority of women on
19 businesses.
20 And so, that would be a proposal to issue an
21 RFP, to see who else is out there, terminated those two
22 managers. We would even consider adding dollar amounts
23 to the program above this $107 million that we
24 terminated.
25 And then on page 6, we talk a little bit

1 about the policy. So, earlier on, I mentioned that
2 currently, the program had limited and capped an
3 emerging manager at a billion dollars firm-wide AUM.
4 And after lots of conversation with Rocaton and with the
5 underlying emerging managers and managers in our
6 portfolio today, we think it's a good idea to increase
7 that amount to $2 billion in terms of firm-wide assets
8 under management. And I could turn it over to Robin to
9 just discuss a little bit about that number. The
10 firm-wide AUM for the policy recommendation.
11 MS. PELISH: So, I think it just widens the
12 opportunity set and makes sense given that it -- I think
13 that is the primary reason. And then if you limit it to
14 a billion, there's also a number of firms that are under
15 a billion, not because they're emerging so much but
16 because they've grown over a billion and then through
17 performance or loss of assets have fallen back under the
18 billion mark. But I think it makes sense to widen the
19 opportunity set.
20 MS. HINGORANI: So, that would be the policy
21 proposal we have. And this would be something that a
22 manager wouldn't be able to emerge or move out of the
23 emerging program into our developing program unless we
24 issue an RFP. And that's currently the case, because we
25 have contracts with the manager of managers, those fund

1 to fund. We do not have contracts with the underlying
2 managers. So, could not just pluck them out and
3 graduate them without issuing an RFP, so that would
4 still be the case.
5 And the last thing that we would suggest is
6 currently there are a few managers that are in our
7 emerging manager and managers fund to funds portfolios
8 and they're also in our developing managers program.
9 And so, we would try to remove that kind of overlap
10 going forward.
11 So, those would be our recommendations.
12 MR. SMARR: So, what's that cut off under
13 developing managers?
14 MS. HINGORANI: So, currently it's 1 to
15 5 billion. And so as we move up the emerging managers
16 to 2 billion, we would move that up to 2 to 5 billion.
17 CHAIRPERSON AARONSON: Any other questions
18 or comments?
19 MS. NAGASWAMI: So, we had a bunch of
20 questions that we've asked our staff.
21 MR. SCHLOSS: Do you have some answers to
22 the questions?
23 MS. NAGASWAMI: We asked for a clarification
24 on the emerging managers versus the developing managers
25 program. We absolutely are supportive of everything

1 we're trying to do here, but the policy just does not
2 appear very clear to us. So, we would hope that we can
3 work somehow with Corporation Counsel so the managers
4 don't get kicked out when they grow. Starting today,
5 we're bumping up against a billion if our managers do
6 what we want them to do. Then they succeed. Then we
7 have to fire good managers and do a new RFP. So, one
8 question is, is there anything we can do --
9 MS. BUDZIK: The question was asked
10 yesterday, so we went over to Karen earlier today. As
11 what Seema said, slightly. There is a provision --
12 there are procurement rules that would allow you to
13 enter into direct relationship with the manager. These
14 assets have grown over the threshold of the emerging
15 manager program. It's subject to board approval. It's
16 subject to performance criteria, a good performer.
17 But there are procurement rules to enter
18 into direct contracts with managers outside of a formal
19 RFP. The other way to do is to issue an RFP, but you
20 could capture the high performing managers as part of --
21 it does actually require you to issue the emerging
22 manager RFP because one of the criteria is that the
23 current contract that they're working under, either
24 expired or has been terminated.
25 And if we do a new emerging manager RFP, we

1 will do new contracts, so the current contracts will
2 either expire or terminate.
3 MR. SCHLOSS: The benefits of increasing the
4 maximum from 1 to $2 billion is to keep those good
5 managers as they grow.
6 MS. BUDZIK: There's that. So, for a
7 manager over the #2 billion that you think is still
8 appropriate is a good manager that you want to retain,
9 you will have the ability to be subject to board
10 approval.
11 MS. NAGASWAMI: I feel confused about where
12 you ended. You say that we still have to do an RFP
13 anyway?
14 MS. BUDZIK: It's kind of a quirky rule but
15 it's the -- yeah, you have to do an RFP because one of
16 the criteria is that the contract that we're managing
17 under now, so that's going to be an emerging manager
18 contract, either expired or has been terminated.
19 MS. NAGASWAMI: But what if it doesn't
20 expire or --
21 MS. BUDZIK: Well, I think when you do a new
22 RFP, you're going to do new contracts, the current
23 contracts will be able to check off that box.
24 MR. SCHLOSS: But it wasn't new contracts
25 that we like you and want to graduate, you'll keep and

1 have your own contract? Is that the easiest way to keep
2 them?
3 MS. BUDZIK: My only concern there is that
4 there is a very specific rule about the graduation --
5 about the process for entering into direct contracts.
6 So, we could talk about that with the Law Department,
7 but either you have options either way for retaining
8 strong managers that have assets that exceeded the
9 limits.
10 MR. SCHLOSS: But the easiest way was to
11 change the contract; is that right? Your contracts, we
12 give people and say, look, you go into the incubator,
13 you get incubated, you grow up, you get your own
14 contract. That would be a very nice way to run it.
15 MS. BUDZIK: It would, but again, I would
16 want to confirm with the procurement people that they
17 wouldn't say no and they got to follow this rule.
18 MS. NAGASWAMI: I wasn't clear from where
19 you started that we needed -- if the contract was not up
20 for renewal, there was no reason for an RFP the way I
21 considered what you are saying. Either there are
22 multiple interpretations --
23 MS. BUDZIK: I think that the reason for a
24 new RFP are the reasons that Seema articulated.
25 MS. NAGASWAMI: Which I think is separate

1 from graduating our existing managers; right? Exactly
2 I'm being -- it's unrelated.
3 MS. BUDZIK: It's unrelated, but I think
4 your question is true, at this new RFP process. I don't
5 want to lose strong managers. These assets have grown
6 over the threshold, and when you answer that question is
7 you won't, you don't have to.
8 MS. NAGASWAMI: It might be unrelated to the
9 RFP, but just, how do we manage this emerging versus
10 developing? So that when actually a manager does
11 exactly what we want them to do, grow, succeed, we don't
12 bump into out own silly rules and policy and was it a
13 procurement issue or was it a policy issue?
14 And I'm not clear about that. I don't know
15 what our investment policy statement would say about
16 graduating people from emerging to developing. And so,
17 I thought it would be very helpful to just review the
18 policy, because I certainly don't understand what it is.
19 MS. HINGORANI: As I understand it, there
20 are no specifics about any of the numbers that we will
21 talk through.
22 MR. SCHLOSS: Right. The way the contracts
23 work -- let's be clear. The contract is not with the
24 underlying managers, it is with the fund to fund
25 manager. So, anything that is not dealing with that

1 contract, you don't have a contract. So, if you're
2 doing what you are supposed to do and you get our
3 threshold, a billion, and we make the guy review the
4 contract with the fund to funds guy, then when I got to
5 get rid of them, we have thrown out a very good manager.
6 That's bad thing with that. You know our system.
7 So, the way we're trying to fix it was, A,
8 increase the cap for a billion to $2 billion, so that if
9 everybody who's in our managers which is doing well, a
10 billion dollars worth of room to grow.
11 And then what we were saying is if we want
12 to be innovative amongst ourselves, we would have some
13 process in the existing contracts with the fund to funds
14 manager. Because, by the way, you can grow out of this
15 and have your own contract. But that's not for the
16 board, if you will, that's for the contract people. So,
17 that's over the legal people to say can you guys fix the
18 contract. That's why it's two things.
19 CHAIRPERSON AARONSON: So let's just
20 recognize --
21 MS. EMERY: I have an overly simplified
22 solution to this technical contracting process. But why
23 do we not contract with capital and these fund to funds
24 managers as discretionary advisors to manage the
25 program, and then we do a direct contract with each

1 underlying manager that they select for us?

2 MS. MARCH: If we hire a manager through an

3 RFP process, and the manager performed well, and we see

4 that there might be a problem because the initial hiring

5 was through a fund of fund A, and now you want the

6 manager to be standalone; I cannot understand why all

7 the eminent attorneys and the contract people cannot

8 figure out why within the initial RFP, and within the

9 initial contract, that language can't be there?

10 MS. BUDZIK: And we can --

11 MS. NIEVES: That's exactly the heart of the

12 issue.

13 MS. BUDZIK: You have two options. One is

14 to put it right in the emerging manager RFP. But we

15 also have a rule. There are two options. One might

16 be --

17 MR. SCHLOSS: What I'm saying is put it in

18 the original contract; right? You get your own

19 contract.

20 MS. NAGASWAMI: If we want you.

21 CHAIRPERSON AARONSON: Your recommendation

22 is that we do an RFP?

23 MR. SCHLOSS: Yes.

24 CHAIRPERSON AARONSON: And that from what I

25 hear from this conversation, in this RFP, all of the

1 questions that have been raised there will be raised in
2 the RFP?
3 MR. SCHLOSS: Well, ultimately, there's a
4 contract for part of the RFP where we get the contract
5 where you want to be. The way it's set up now is wrong.
6 It's not the way we want it to be.
7 MS. MARCH: So, I believe you can set it up
8 the way we would like as a board for it to be, so that
9 when we graduate an emerging manager, they can continue
10 to be in our portfolio.
11 Just as a side note, I think maybe what the
12 industry is doing is that we are keeping emerging
13 managers as emerging managers rather than allowing them
14 to succeed and enter the world of Wall Street. And I
15 did say that, by the way, at a conference recently and I
16 don't think we should be guilty of this. So let's just
17 work it out, Larry, in a new language, okay?
18 CHAIRPERSON AARONSON: So, he request for a
19 permission to do an RFP?
20 MS. NAGASWAMI: So, that's exactly what we
21 are asking, is that in doing the RFP, this is a time for
22 us to review our policy and not just make a 1 to
23 $2 billion change, but make quite -- as Sandy so
24 properly articulated.
25 But we had a couple of other questions, as

1 well, which is -- I just wanted to be sure $2 billion
2 makes a lot of sense, is that the right number? Is
3 there any way that we can look at emerging manager
4 programs, talk to our fund to fund managers to
5 understand whether it should be 3, whether it should
6 be -- and then developing go from 2 to 10, I'm making
7 these numbers up -- but I don't have any sense and I
8 don't know if 10 percent more in the equity market later
9 or 5 percent growth later, we bump up against
10 $2 billion.
11 So, that seems like a really good time to
12 just do a comprehensive policy review, which I don't
13 know when we last did around the emerging market
14 managers/developing manager program. But that was our
15 other question.
16 MS. ROMAIN: These things simultaneously and
17 not know of the process, because the RFP process in and
18 of itself is a lengthy process. And if we are going to
19 make a comprehensive change in policy, then maybe next
20 year, this time we will probably come back with some
21 answers. So, I don't know how lengthy.
22 I don't know if this is going to be to
23 answer your question; but the question right here is, we
24 wanted to do an RFP which is already a lengthy process.
25 And you are saying that policy need to be looked at?

1 The lawyers, everybody can work together and get this
2 done.
3 MR. SCHLOSS: There's a list of things.
4 Change in a contract is within the time frame of the
5 RFP, right, because the RFP has multiple stages. The
6 contract being the last stage and I'd like to think that
7 all of corporation counsel and BAM's counsel working
8 together to get the right contract in two or three
9 months, four months.
10 MS. MARCH: If we ask them, they will lie.
11 MR. SCHLOSS: I have seen that.
12 (Laughter.)
13 MS. MARCH: They will.
14 MR. SCHLOSS: We'll ask then and they will.
15 So, that would be taken care of during the RFP process.
16 Again, to start the RFP process, we really need to agree
17 on is, A, to start and then, B, what are specs; right?
18 And so, the specs get you down to the ceiling; right? I
19 think Rocaton looked that and I know we spoke to the
20 emerging managers to come up with the $2 billion.
21 So, that wasn't just a random number that we
22 pulled out of the air, but I would go back to Robin, as
23 well, perhaps to Seema to go through how we got to the
24 $2 billion number.
25 MS. HINGORANI: We talked to every one of

1 the managers. They gave us all of -- they gave us their
2 list of the underlying managers in the portfolio. They
3 showed us the questions, the AUM at the time we funded
4 and the current AUM. And you can see that in many cases
5 dramatic increase to over a billion dollars and many of
6 the market good guys that we would want to keep in the
7 portfolio.
8 And so, out of the four, one suggested quite
9 a higher number than the $2 billion. But some other
10 analysis didn't quite make as much sense as the other.
11 So, we had a conversation. But everybody, including
12 Robin, hovers around this $2 billion number. You can
13 walk through all the underlying manager detail that we
14 have, and that could be something that we work on
15 together before we write the scope.
16 Because the scope, as you know from the
17 emerging markets, scope that we worked on, that is a
18 process. And it is one where we sat down, reviewed one
19 of your questions together, and the comments. And so,
20 that was complete and that took a week or so to do. And
21 that will be the same thing with this.
22 So, I actually worked on the scope. We can
23 address the policy issue. We can address all your
24 questions. I have the majority of the questions that
25 you have answered already. And some of those getting

1 data back in the underlying managers. Because, again,
2 we don't have -- with my experience here, I don't have a
3 direct relationship with the underlying managers
4 themselves. I have a direct relationship with the fund
5 to fund managers. So, I don't have access to all that
6 data. They have to give it to us and present it to us.
7 So, but we have all that done by the time we're in the
8 process of writing the scope.
9 CHAIRPERSON AARONSON: I think that you have
10 discussed this and we should be able to come to a
11 conclusion of whether we should go ahead with the RFP.
12 And, Jamie, do you have something?
13 MR. SMARR: I just had a question about what
14 you just said. If your contract is with the fund to
15 funds and you are there -- I'm sorry. I'm just
16 wondering if they're now potential for the conflict of
17 interest to let one of those manager lose AUM, hence,
18 they're not going to want to do that.
19 I don't know what their fees are based on.
20 If their fees are based on AUM and... one of those
21 managers out there if they're earning less money. So,
22 has anyone looked at what the potential contract issues
23 are for the manager?
24 MS. HINGORANI: There isn't anything right
25 now that states that we would replace. We can't do

1 that. But they're highly intended to have managers that
2 perform really well for us because if they do perform
3 well, I would expect that we would come back to the
4 board and make a recommendation to increase an
5 allocation to one of the emerging manager or managers.
6 So, I think I all understand that. We had no
7 conversations about that with them. And even with
8 respect to fees that they charge us.
9 Because in my view, that if you're doing
10 really well for us, we want to give you more money to
11 manage likely. And so, reduce your fee, because you are
12 going to make more money any way hopefully over time.
13 MR. SCHLOSS: I would say we're going to
14 restructure the contract a little, that what you want to
15 have is what I'll call incubator and sprinkler. So, if
16 you someone with umbrella get to our head and have a
17 separate contract with them, we should then give the
18 emerging manager the money back. It shouldn't be at a
19 loss for doing their job because someone actually grew
20 up with independent contract which come right back and
21 you say, look, you had $200 million. You had $200
22 million. This guy grew up, he left 950. We're supposed
23 to come right back and give you that 50 back, and grow
24 some more.
25 MR. SMARR: I just want to make sure that

1 the contract allows that. Because otherwise, you might
2 have people sort of keeping --
3 MR. SCHLOSS: It's BAM's job, especially if
4 we have this contract that lets us do that. I would say
5 that's exactly how you want the program to incubate
6 them, get them out of there, give some more money to
7 incubate. Get the cycle going.
8 MS. PELISH: That was always the concept.
9 MR. SCHLOSS: Yes.
10 MS. PELISH: So, the question is at what
11 level do you let them graduate? And I would say it's
12 part of BAM and the consultant's monitoring
13 responsibility to make sure that these programs are
14 filled with very successful $3 billion managers. And
15 that's just the monitoring.
16 MS. EMERY: So, I'm hearing the RFPs for
17 domestic equity, emerging --
18 MS. PELISH: EAFE.
19 MS. EMERY: EAFE and fixed income.
20 Is there data that you can provide us for
21 fixed income and EAFE to show that the emerging
22 markets -- the emerging managers are in this space? Are
23 they currently adding value? I'm thinking fixed income,
24 for example, is a pretty efficient part of the market.
25 Is this an area that we should be focusing on for

1 emerging managers? I just don't have the context on
2 where the recommendation is coming from.
3 CHAIRPERSON AARONSON: I think that as part
4 of this study, if they find that in fixed income, that
5 there's no emerging managers that, who we can invest in,
6 so, we won't.
7 MR. SCHLOSS: Right.
8 CHAIRPERSON AARONSON: But we have to look
9 into it, and I think this cause a dead horse now.
10 So, is there anybody who opposes the
11 Comptroller's Office from doing this RFP with all of the
12 items that we discussed?
13 MS. MARCH: You're looking for consensus?
14 CHAIRPERSON AARONSON: Do we have it?
15 MS. MARCH: You have consensus.
16 CHAIRPERSON AARONSON: Okay. And you can go
17 ahead, Larry. With that, Thank you.
18 MR. SCHLOSS: Thank you.
19 And we will come back to all the questions
20 answered and who is out there and is there fixed income
21 person out there or not, find that out, due to the
22 process, otherwise we can't find out. And the lawyers
23 will hopefully come up the contract it does. As Robin
24 said, what it's supposed to do.
25 We'll be back in a few months, hopefully,

1 with the answer.

2 So, now, we move to the biggest investment

3 topic of any public pension fund, of any pension fund,

4 and that's asset allocation. As you all know, we

5 started working on this last summer. And Robin,

6 Rocaton, has taken the lead on this.

7 MS. PELISH: So, I'm going to take the lead

8 on this presentation, but this is very much a

9 collaboration between Rocaton and BAM. And so, to the

10 extent they want to interject comments, I encourage them

11 to do so.

12 I want to make a couple of comments before

13 we go into the details of this presentation. And we

14 recently had discussions about asset allocation over the

15 years. We've had many discussions about asset

16 allocation at the board. And it's a very intellectually

17 interesting topic. But I do want to emphasize a couple

18 of things.

19 First is that the tools we use to evaluate

20 various asset allocations are a blunt instrument, in

21 that they incorporate a lot of assumptions about

22 expected returns, expected risk, correlations between

23 asset classes. We try to capture capital market

24 behavior, with statistics. And as we all know, that's

25 an effort worth pursuing, but it's a very difficult

1 effort.

2 We spend a lot of time at Rocaton, and I

3 know the BAM spends a lot of time and the board spends a

4 lot of time, understanding and evaluating the quality of

5 a capital market assumptions that are at the heart of

6 that process. But the only thing we know for certain is

7 that none of these numbers will be precisely right. But

8 we hope that they're directionally right.

9 And we spend a lot of time thinking about

10 whether they are directionally right and whether we

11 capture both the risk and return of capital markets.

12 So, that's one point.

13 The other point is that the really useful

14 decisions that come out of this process, I think, are

15 the range of capital markets that we should be investing

16 in; and directionally, how much equity risk should be in

17 the portfolio and how much interest rate risks should be

18 in the portfolio. And those are really the important

19 decisions that come out of these asset allocation

20 processes.

21 These are very large portfolios. We're

22 talking about assets of over $40 billion. So, any

23 change we make involves the movement of millions if not

24 billions of dollars. But whether we allocate 3 percent

25 to a strategy or 4 percent to a strategy involves the

1 movement of a lot of dollars and should be carefully
2 evaluated, we just can't know with precision whether the
3 numbers should be 3 percent or 5 percent. So, I do want
4 to emphasize that we have a lot of data here. We come
5 out with what looks like very precise solutions, but it
6 is a blunt instrument.
7 And I encourage all to think directionally
8 about how much equity risk we want to take, the range of
9 capital markets we want to invest in and the level of
10 risk which we need to take to generate the returns that
11 the system needs. And to the extent possible, avoid
12 getting lost in the weeds.
13 So, with that, let me turn to page 2 and a
14 couple of points at page 2 that I want to highlight.
15 The first of which is that this is this process, the
16 continuum, as you all know. And over time, the asset
17 allocation policy of the pension fund has evolved. New
18 asset classes have been added. And allocations to
19 exists the asset classes have been altered.
20 In general, the direction of the asset
21 allocation policy for the pension funds has been over
22 the past five to seven years to reduce the allocations
23 to U.S. equities and to add new and diversified asset
24 classes. So, I refer on page -- we refer on page 2 to
25 the addition of TIPS and 2005 private real estate which

1 first got funded in about 2006, convertible bonds in
2 2008 and opportunistic fixed income which first became
3 funded in 2008. And, again, this is all consistent with
4 the theme of diversifying new asset classes -- new
5 assets to the fund, not necessarily asset classes that
6 are new to the world, but asset classes that are new to
7 the fund and trying to diversify the sources of risk and
8 return in the portfolio.
9 The take away from this exercise, we
10 believe, is that there are several asset classes that
11 are not currently utilized in the fund including
12 emerging market equities and debt commodities and
13 absolute return strategies that should be considered,
14 again, their diversifying sources of risk and return for
15 the portfolio.
16 And we think that the addition of
17 incremental asset classes will not dramatically change
18 the portfolio because of risk and return. We have to
19 make huge changes to do that. But, nonetheless, we
20 think, again, consistent with the evolution of asset
21 allocation policy for the fund, we can modestly improve
22 the outcome and the range of expected outcome by further
23 diversifying the portfolio.
24 Another point to note on the bottom of
25 page 2 is that the expected returns for most of the

1 asset classes that we are thinking about are fairly
2 modest. Only private equity and emerging market
3 equities have expected returns -- expected compound
4 returns of over 8 percent. That means generating high
5 single digit return is very difficult, given our
6 expectation. And these capital market expectations
7 developed by Rocaton are generally consistent with most
8 of the industry observers.
9 Now, we have over time lowered expected
10 return for most asset classes, but we have not reduced
11 expected volatilities. So, we are in an environment
12 going forward over the next five or seven years, where
13 we expect return to be pretty modest. We don't expect
14 risk to be abated.
15 And finally, we all know that we're
16 operating within an environment that has significant
17 restraint in what we can implement. So, we have a
18 basket clause that we have to recognize and we also
19 have.
20 We have to recognize the fact that the
21 system has to generate a reasonably high level of return
22 to meet its obligations. Anything else before -- any
23 other questions or comments before I launch into the
24 meat of the presentation?
25 The next few pages outline how Rocaton

1 developed its capital market expectations. And I'm not
2 sure that we want to spend a lot of time going through
3 the process. Except to recognize that one of the things
4 we try to do is not only develop long-term assumptions.
5 This is a fund, we all know, that has a very long
6 horizon.
7 Nonetheless, we have to recognize the market
8 environment in which we're making this asset allocation
9 decision. And so, we do, when developing capital market
10 expectations, assess current market conditions. And
11 this goes back to comments that Larry made when he was
12 going through the review of macro and market conditions
13 which -- primarily, we're investing in a period of low
14 interest rates. And rising interest rates or head wind.
15 And we need to recognize that and our assumptions
16 recognize that.
17 So, if we can move to page 8, which takes
18 all of the data that we aggregate and looks at expected
19 returns. And so, what you can see is that -- our
20 expected compound return, if you look at the far
21 right-hand column, for most asset classes of -- we said
22 is below 8 percent. For U.S. Equities, you will see in
23 the middle of the page our compound return forecast is
24 about 7.6 percent.
25 And we have the same expectation for

1 developed non-US market that we do for the U.S. Equity
2 market. We have higher return expectation for emerging
3 markets and for private equity. For real estate, our
4 expectation is just under 7 percent as it is for fund of
5 hedge funds, that's about 7 percent and for commodities,
6 we have a relatively low expected return of
7 3 1/2 percent.
8 Let me point one out one other thing which
9 is the expectation for U.S. fixed income, that's
10 4.3 percent. Our expectation at an interest rates will
11 rise over the next few years -- means that we reduce our
12 equilibrium expectation for fixed income to reflect the
13 fact that the market values of fixed income will decline
14 as the interest rates rise over the next few years.
15 Going out, we're reinvesting at a higher interest rate,
16 but nonetheless, our expectations for fixed income are
17 lower because of this rising interest rate environment
18 that we think we'll find.
19 Let me turn to page 10 for a minute because
20 we focus on return -- up to now -- now, let's look at
21 risk. And these are our expectations as a market
22 forecast as of the end of 2010. Here, we're capturing
23 risk in one number and we all know that risk is a
24 multifaceted concept. But here, we're looking just as
25 the standard deviation of annual returns.

1 And so, let me ask you to look at the U.S.
2 Equity number. Our expectation is for -- as I noticed
3 before, 7.6 percent compound annual return. The
4 year-by-year return that we expect is 9.4 percent, but
5 because there is so much volatility in the equity
6 market, 19 percent -- well, annualized volatility, that
7 compound return is reduced to 7.6 percent compound
8 return.
9 The important thing here is that volatility
10 really has a real cost -- costs you money. And so, what
11 a standard deviation of 19 percent means is that the
12 lowest fifth percentile return outcome is minus
13 22 percent. The highest is 41 percent.
14 So, although, we have an expectation that
15 our return is going to be 7.6 percent, given a 19
16 percent standard deviation of return, the range outcomes
17 could be from negative 22 percent to positive 41
18 percent. That's a very wide range of outcome and that
19 means that equities are really risky asset class. And
20 in fact, we landed outside this chart which is a risky
21 composition. If I could ask you to look at that.
22 (Indicating.)
23 If you look at our current capital
24 allocation of the pension fund, you'll add up all of our
25 equity allocations. We have public equities allocated

1 at 61 percent. That's just how the dollars are
2 allocated.
3 MS. NAGASWAMI: Is this actual --
4 MS. PELISH: Sorry. So, this is a target
5 weight. Our target allocation for the pension fund is
6 that we are going to -- about 61 percent of the dollars
7 invested in public equities. So, because equities are
8 so volatile and because many other asset classes are
9 correlated with equity, that means that equities are
10 expected to contribute 85 percent of the volatility of
11 the fund.
12 That's an important concept. That means
13 that you can't just look at the volatility equity on
14 standalone basis. You have to recognize that equities
15 contribute a disproportion level of risk to the
16 portfolio and that is why over the past decade, we have
17 been suddenly reducing the allocation of public equities
18 and the effort to diversify the sources of risk within
19 the portfolio.
20 So, going back to the major presentation --
21 to the larger presentation, we also have correlation
22 assumptions which are important but I'm not going to go
23 through them unless we have a specific question.
24 Let me turn to page 12, if I can. On
25 page 12, we have the restraints and we ran this asset

1 allocation exercise with two different restraints in
2 terms of the basket clause. And on page 12, you'll see
3 the current basket clause and that asks us a significant
4 constraint to how we can allocate assets to non-U.S.
5 Equities to real estate, to commodities and to absolute
6 return. And in the second case, we assumed that the
7 basket clause was raised. And so, we could actually
8 have more flexibility in allocating to non-U.S. Equities
9 and other asset classes. We ran two different cases.
10 And I think that's all I'd like to say at this point
11 about restraints unless there's any questions.
12 MR. NORTH: I have just one question, where
13 you mentioned the minimum.
14 Does that compel the allocator to put assets
15 in each class or is that all risk?
16 MS. PELISH: It doesn't compel us. And
17 you'll see that, for example, in commodities, we have a
18 3 percent minimum on this page and in some of the cases,
19 we have a zero percent allocation. What it really means
20 is that we don't want to bother investing in an asset
21 class unless it's significant enough to move the needle.
22 Okay. So let's go to page 14. And on
23 page 14, we have a series of efficient frontiers and
24 again, those of you who are familiar with official
25 frontiers efficient, official frontiers just define

1 those portfolios mixes which have the highest expected
2 return for any given level of risk. So, those are the
3 optimal portfolios along the risk spectrum.
4 And what you can see is, not surprisingly,
5 that if you don't have any constraints on your asset
6 mix, which is the farthest out frontier -- the black
7 frontier, you have -- you can generate higher levels of
8 return for each level of expected risk. And as you
9 increase the restraints on the portfolio, first with the
10 33 percent basket clause and then with the 23 percent
11 basket clause, the level of return you can generate per
12 unit of expected risk decline.
13 But we all operate in a universe of
14 constraints, so no one ever invested in an unconstrained
15 portfolio. But we just wanted to show you the degree to
16 which constraints really do reduce expected return per
17 unit of expected risk.
18 The other important takeaway here is that
19 the currently long term target is not a bad target.
20 It's relatively efficient. And that shouldn't be a
21 surprise because we got to the current long term target
22 through a similar process of carefully considering a
23 series of relatively efficient portfolio. It is worth
24 knowing though that there are modest improvements to the
25 efficiency of the current long term target that we think

1 can be obtained again by increasing the diversification
2 of the portfolio modestly from where we currently are.
3 So with what, I'd like to ask you to turn to
4 the alternative portfolio we consider. Now, what we are
5 going to show you are two cases; Case A and B. And we
6 have the same portfolio listed in the handout that you
7 originally got. The only thing we added is -- on the
8 newest handouts, we indicate what the illiquid
9 allocations are for each of the portfolio. And that was
10 left off of the larger handout. But it's the same data
11 other than additional line that indicates approximate
12 illiquid allocation within each one of the portfolios.
13 Now, we distilled these alternative
14 portfolios down to Case A and Case B but I can tell you
15 that in collaboration with BAM, we looked at dozens of
16 portfolio mixes.
17 MR. SCHLOSS: Thousands.
18 (Laughter.)
19 Dozens is too few.
20 MS. PELISH: Somewhere between dozens and
21 thousands.
22 MR. SMARR: So, should we be concerned that
23 the expected come down of compound returns here matches
24 the actuarial investment rate? That's what we are
25 supposed to be doing with matching the ARR?

1 MS. PELISH: I think that you can only take
2 what the capital markets will give you. And it is
3 theoretically possible to raise the expected return of
4 this portfolio, but it is not possible to do that
5 without taking on significantly more equity risk. And
6 without raising the expected volatility of the
7 portfolio's returns significantly.
8 MR. NORTH: If I might add, it is always the
9 chicken and egg problem. The board thinks the goal is
10 to get the actuarial assumed rate of return, which is
11 just one assumption within a packaged designed to
12 properly fund the system.
13 And the actuaries believe the board should
14 be deciding what they are comfortable with on a risk
15 basis to get an expected return. And the actuary will
16 either agree with those assumptions or not in creating
17 discount rate assumptions.
18 I believe you should focus on the latter
19 approach of what the board is comfortable with,
20 understanding implications, and designing an asset
21 allocation that you feel fits it.
22 MS. NAGASWAMI: As a corollary to that,
23 Robin, the expectations here are five to ten-year
24 expectations, and in thinking about the actuarial
25 investment rate, you're looking now at decades. And so,

1 in terms of how the compounding would work that Robin
2 described -- she's describing fixed income yields
3 returns, really low as rates rise, higher returns over
4 the actuary investment rate period should be achievable
5 relative to the reality of today's evaluation.
6 MS. PELISH: Yes.
7 (Laughter.)
8 I think that's absolutely right.
9 MR. NORTH: And I do agree with the theory,
10 but I don't necessarily agree with the inputs and the
11 assumptions.
12 MS. NAGASWAMI: To be continued.
13 MR. SCHLOSS: We think about the
14 assumptions. It's all crystal ball, right? The only
15 thing you know is that they're wrong. You just hope
16 you're leaning in the right general direction and then
17 you and your manager need to be nimble and not have been
18 down along the way, you will be fine. But Jamie's real
19 question, though, is that 7 should be 8. Close enough
20 for government work -- or I would say, close enough for
21 the market work.
22 (Laughter.)
23 Again, you can't get it to just be 8 on the
24 button without moving -- based on the assumptions in the
25 most fundamental things that Robin said was there's only

1 two numbers that are more than 8. And it's private
2 equity and emerging markets. So, if you want to get to
3 8, you just forward in those two baskets and your math
4 gets you to 8. You might not like it.
5 MS. NAGASWAMI: These are pre-fees?
6 MS. PELISH: Yes. This is pre-fees, but I
7 would say this is all passive, as well.
8 It's very small and I wouldn't worry too
9 much about the fees -- what I was saying is the
10 actuarial context.
11 The total pension funds are 10 to 15 basis
12 points. So, it's ending up being noise.
13 MR. NORTH: I would just observe that, first
14 of all, the mechanics of the current employer
15 contribution, the 8 percent assumption that's gross of
16 fees, and any fees are reimbursed in the employer
17 contribution two years later. That's mechanically how
18 we do it now.
19 Part of the reason it's done is that the
20 individual boards -- when I last set interest
21 assumptions were beginning to diversify, were
22 diversifying at different rates. And the
23 diversification has been coming with ever-increasing
24 fees.
25 All of the funds, once upon a time, did

1 their portfolios with less than 10 basis points of
2 expense. The average across the systems now is closer
3 to 50 basis points. Teachers is a little less because
4 they have a much higher percentage allocation to passive
5 equity. But a lot of this discussion is all about
6 diversifying, all of which is into more expensive asset
7 classes.
8 When I make my new recommendations, if I
9 could find a way to do it easily and it would work, I
10 would prefer to talk in terms of net rate of return for
11 discount rates, simply because it's easier. There was a
12 reason for the approach we took several years ago when
13 setting the assumption but that whole issue of fees is
14 something that, I think, cannot be dismissed at all.
15 Also coming under expected actuarial
16 standards of practice, the use any alpha in the
17 development of an expected rate of return will be likely
18 forbidden; because collectively across all systems,
19 there is no alpha. Everybody believes they'll get the
20 alpha and other people lose.
21 So, we might be the best; but the actuary
22 may not be permitted to make any adjustments for it.
23 But that's just some background track on the thing and I
24 wouldn't underestimate fees, they are growing, Robin.
25 MS. PELISH: Yes; that's true. That is

1 true. And there's no alpha assumptions in these.

2 Let me call your attention to page 15, we

3 have a long term target in the first column and then

4 Case A, Case B.

5 So, what you'll see, first high level and

6 long term target has 70 percent of its assets targeted

7 to both public and private equity. In both Case A and

8 Case B, we moved down from that 70 percent level to

9 Case A, 65 percent; Case B, 67 percent. We call

10 something -- equities that are simply not fixed income.

11 So, you'll see we grouped commodities as

12 equities and we include absolute return as equities.

13 And while absolute return has definitely a strong

14 positive correlation with equities, commodities do not.

15 So, that the should be noted. But the asset allocation

16 that is changing most significantly in both of these

17 cases is the U.S. Equity allocation. What you see it's

18 declining from 38 percent in the current long term to 30

19 percent, Case A; 25 percent in Case B.

20 Similarly, non-U.S. developed markets are

21 declining from 16 percent and then 9 percent.

22 Those assets are being reallocated to

23 emerging market equities you see that rising from

24 currently 3 percent to more than double that. We're

25 suggesting that commodities be considered, that's in

1 Case B. Private equity is going up by a few percentage
2 point and real estate is largely staying where it is.
3 Absolute return is introduced in Case A and Case B and 3
4 and 5 percent.
5 In terms of fixed income, we're suggesting
6 that Core+5 be reduced slightly. Those assets are being
7 reinvested in convertibles and TIPS and the
8 opportunistic fixed income sector. We're suggesting
9 that time yield be reduced slightly and that emerging
10 markets debt be introduced.
11 You see the use of the basket clause in both
12 Case A and Case B would go up to 24 percent and
13 32 percent. And we're currently at about 10 percent
14 invested in illiquid assets. And if you add private
15 equity plus real estate plus assuming that about half of
16 opportunistic fixed income at about half of absolute
17 return investments are illiquid, that 10 percent rises
18 so 15 and 17 percent cases A and B.
19 So, what do you get from moving all that
20 money around? You are at the same level of expected
21 compound return but your risk in terms of standard
22 deviation has moved down slightly to 12 percent to about
23 11 percent. And that translates into a worst case
24 outcome of -- in the worst case -- worst 1 percent
25 outcome. See at the bottom of the page of a loss of

1 $8 billion in the current long term target to a loss of
2 $7 billion in Case A and $6.7 billion in Case B.
3 So, lots of numbers -- and again, you know,
4 sort of sense of false precision here. We can't be this
5 precise. We're talking about future behavior very, very
6 complex -- global public and private markets. But
7 again, the trend continues towards encouraging
8 diversification out of the riskiest asset classes -- we
9 know public equities are the riskiest asset class.
10 Let's move slightly -- let's continue to move slightly
11 out of that. Those asset classes into other
12 diversifying asset classes and that should help us
13 reduce the risk of the portfolio. And that is what we
14 are talking about in both Case A and Case B.
15 Because absolute return has not yet been
16 approved by this board and other asset classes that
17 haven't been approved. We ran the same analysis
18 excluding absolute return and you see that on page 3 and
19 it yields the same results with slightly different
20 allocations, again, we continue to reduce public equity
21 but we reallocate the 3 and 5 percent targets to -- from
22 absolute returns into other asset classes so not a
23 significant change. Again, what we're saying is we
24 think we can accomplish similar goals with and without
25 absolute return.

1 MS. NAGASWAMI: So, another way to think
2 about that will be -- you showed us, Robin, the risk
3 allocation, if you look at the beta versus active risk
4 of the current portfolio versus the proposed portfolio.
5 What something like hedge fund or opportunistic does is
6 just move us into the active risk?
7 MS. PELISH: Yes.
8 MS. NAGASWAMI: So, that's another shift --
9 MS. PELISH: Yes.
10 MS. NAGASWAMI: -- in the portfolio in terms
11 of alpha opportunity that accounting systems won't
12 capture but manager skill which we think we obviously
13 with help could capture in a significant way. This time
14 we get captured in a mean, variance framework.
15 MS. PELISH: Yes. There's a lot that
16 doesn't get captured in a mean variance framework.
17 That's one of the inflation risks, capture in a mean
18 variance framework -- lot of risks. So, if we move back
19 to the main presentation, on page 17, what you can see
20 is that we are trying to provide some sense of what it
21 really means to move from the long term target to Case A
22 or Case B over time because we are not talking about
23 significant shifts.
24 We're moving fair amount of money out of
25 public equities into other asset classes but we're

1 talking about expected returns that are very similar,
2 what we think except from the current target and modest
3 detriments on expected risk.
4 Nonetheless, because we're investing $40
5 billion, even modest improvements yield significant
6 results in terms of real dollars. And so, at the end of
7 ten years, we think we can improve the outcome by
8 somewhere from $400 to $600 million. So, it's an effort
9 worth making.
10 We have some historical analysis about the
11 different cases versus the long term target on pages 19
12 and I think it's worth spending a minute on.
13 If you can see on page 19, we can try to
14 take a look at how the current target would have
15 performed versus Case A and B over various -- over
16 couple of recent time periods. And on the top of
17 page 19, we look at the credit crisis, July '07 to March
18 2009.
19 And then, we've looked even farther back to
20 the tech bubble and I'm sure you all remember what
21 occurred between 2000 and 2003. And what you can see is
22 that in each of those crisis being more diversified than
23 the current target would have helped us slightly. We
24 would have ended the period somewhat better off. Again,
25 we're not talking about -- this is a process of

1 evolution, not revolution modest improvements like
2 continuing the process of diversifying. In each case,
3 we would have been modestly better off. But again,
4 modest improvements on a basic $40 billion are written
5 yields real dollars.
6 MR. NORTH: Robin, taking the time periods
7 in which public equity markets did particularly poorly,
8 we didn't show the benefits of being in the public
9 markets preceding the tech bubble or the snap back from
10 March 2009.
11 Is the main point of your graph to show the
12 diversification as opposed to the absolute amounts here?
13 MS. PELISH: Yes. Thank you for making that
14 point. And if we had shown the period, there's another
15 chart and I wish we had inserted but if we had shown the
16 period of market moving up and then, the market crisis
17 and then the snap back, you would still yield the same
18 results because public equities have not come back
19 fully. It's not recovered fully from the crisis. So,
20 we have the same directional results.
21 MS. NAGASWAMI: Can I offer an additional --
22 that is very useful in here. Standard deviations
23 indicate, Bob, as you know so well, plus or minus as if
24 the world were normally distributed; when in fact, all
25 observations will show that there's in fact negative

1 tail.

2 So, in other words, there are far more

3 chances of losing a lot of money than making a lot of

4 money. And it is so much -- you know the compounded

5 down 50 to make up 100 to get to the same place.

6 So, I think downside risk is probably the

7 most pernicious risk that comes from any -- not just

8 ours, any high risk portfolio. So, this really serves

9 to illustrate that there is much higher chance of that

10 negative standard deviation rather than the positive.

11 MR. NORTH: Yes. That's absolutely true,

12 and most modeling doesn't -- historically, it's done

13 simple by normal distribution. Sometimes more normal,

14 doing it more sophisticatedly.

15 And you're absolutely right with the

16 conclusion. One thing I'd like to emphasize, though,

17 that's even more of an issue for the City Retirement

18 Systems in general, less a little bit so for Teachers

19 is: To the extent, we had negative cash flow over the

20 period, when we have it, if you go down 50 percent, you

21 have to go up more than 100 to get back to even; which

22 is why, like you projected now, if you don't take into

23 account cash flow, there's a lot of assets which you may

24 not have available to recover from.

25 So, the point about the downside risks is

1 important, and we have to pay particular attention on
2 that, not for the final asset value, but also for the
3 illiquidity and issues of payments being made.
4 MS. NAGASWAMI: I think Robin would be the
5 first to agree that what follows something like this
6 should be an asset liability study to understand those
7 relationships.
8 MS. PELISH: We have more analysis on the
9 following pages of the range of rolling three-year
10 returns -- five-year returns based on history. And I
11 know that there is a healthy bubble of skepticism about
12 picking certain periods of time and taking a look of how
13 various asset mixes would have done because one thing we
14 know is that history doesn't exactly repeat itself.
15 Nonetheless, I think that if you look at
16 these periods of time, again, it purports to basic
17 tenets that improving the diversification of the current
18 target helps out not only in terms of expected returns
19 but also in terms of protecting us from the worst-case
20 outcomes.
21 And what we can see is that there can be
22 significant and prolonged periods of compound negative
23 returns. And those periods occur more often than what
24 we predicted by normal distributions. We have some
25 additional detail on pages 24 and 25, we'll try to

1 address one of the weaknesses of mean variance which is
2 kind of analysis -- we typically go through an asset
3 allocation which is to say, let's look at how various
4 asset classes perform in periods of time when economic
5 growth is strong and then weak; and as well as periods
6 of time when inflation is rising as well as falling.
7 And again, what we're trying to point to
8 here is that being diversified among asset classes --
9 outside of asset classes like U.S. Equities. Equities
10 do well when economic growth is strong and when
11 inflation is moderate. And so, increasing allocations
12 to other classes which can -- like TIPS or inflation
13 linked bond or absolute return strategies or emerging
14 debt which can generally do better than equities when
15 inflation is rising, benefits the portfolio and allows
16 it to do better over time in a variety of macroeconomic
17 environments.
18 MS. NAGASWAMI: Can I stop you for a moment
19 there, Robin? This is one of my Bob North slides.
20 Bob, I think part of what we are trying to
21 do here is not take risk off the table to a level where
22 we won't earn return. We're just trying to reallocate
23 the risk so that the portfolio does well in a range of
24 environments.
25 MS. PELISH: Right.

1 MS. NAGASWAMI: So that has the benefit of
2 reducing the overall risk but, in fact, should in theory
3 have the benefit of improving our return pattern. And
4 that, I think, this chart really slows you in a way that
5 you can't see from a mean variance framework.
6 So, it's a smaller allocation of the sources
7 of risk not going in and saying we're taking a risk off
8 the table and it should concern you because, then, we
9 would be reducing our chance to make money. It's just
10 simply saying if we can find less correlated sources of
11 risk, then we have two things we can do -- as you saw in
12 Robin's scenario did not reduce the expected return but
13 reduced the overall risk.
14 You know this, but I just need to say it
15 again.
16 (Laughter.)
17 MS. PELISH: So, Larry, where would you like
18 to go now?
19 MR. SCHLOSS: Well, does anyone have any
20 questions? That was very in depth. When I think
21 about -- one of the purposes of the exercise was, A, we
22 haven't done it for five years. So, we've got to do it
23 in five years -- more than every five years; right?
24 MS. PELISH: Yes.
25 MR. SCHLOSS: B, the purpose of having it in

1 our monthly report is make sure we talk about it every
2 month or, at least, look at it every month; C, is to
3 avoid what just happened to it in 2008; right? We just
4 went back down -- TIPS. Here we are, back again, we're
5 in the highest level. Now, we're back at the highest
6 level. What do we want to do going forward and what
7 changes do we want to implement strategically when we
8 have to start with this road map?
9 So then, we have RFPs, hire managers, try to
10 get the best people. I guess what I'd like us to do is
11 sort of agree that this is what we want to work toward
12 A, B, C, why we'll have to deal with the basket clause.
13 So, right now, we have a lot of room.
14 So, once you start implementing this --
15 getting on this journey which is -- it looks like it's
16 not that big as journey but there are new asset classes
17 and there are a lot of new managers required once you
18 start to get on it or it -- I don't want to have happen
19 is a downdraft comes and all of a sudden, they want to
20 start worrying about the basket clause as we're going to
21 get closer to the basket so it's been all to get
22 ourselves organized to change the basket clause, which
23 is up in Albany and the Comptroller's Office.
24 I'm sure it will work with all these
25 appropriate parties and sort of figure out how to do

1 that. That's sort of a corollary. It comes out of
2 this, and the reason that we're looking at both 23 and
3 the 30 -- 35 percent basket cases complicit on moving
4 down the road, it's in three fundamental changes in the
5 path. And we should -- personally, I'd say we shouldn't
6 worry about it because when I looked across the other
7 public pension funds, I don't think it was that radical.
8 And we just happen to have this regulatory
9 issue that we need to deal with. That actually stay on
10 the road. I can tell you that we're excited about this
11 asset allocation because we like to get the risk down.
12 But again, you'll see more different people show up the
13 BAM because some of the new asset classes that we don't
14 have and you'll see it's expanding where the money is.
15 So, it all fits with the corporate plans that we're
16 talking about last week see because you'll see more body
17 to get this plan executed.
18 Again, I'd like to think that we get back
19 together whenever we execute. The first part and we
20 talk about it some more because the most fundamental
21 thing that Robin said was these are assumptions. And
22 all I know is 12 months with different assumptions.
23 Different assumptions next week. And then, we just
24 continue this dialog of how do we feel but where we are
25 in a volatility where stage, where are we in these

1 markets and we just kind of keep looking to make sure
2 that we're comfortable. Again, one of the things when I
3 look at this that I like a lot about it is trying to get
4 money to more different kinds of managers that can do
5 more different kinds of things.
6 So, later, we're going to talk about
7 opportunistic fixed income. These are nimble fixed
8 income people. We don't have nimble fixed income
9 people -- people that manage our money in various
10 buckets but that's how we look at stuff and we'll see
11 these guys later.
12 And so trying to make big tankers like
13 Teachers which, is $43 billion, nimble -- complicated
14 the way we have our process and stuff. So, I think
15 Robin did a great job laying it out. The issues are
16 clearly right in front of us all. And I think it's --
17 again, we're working on it for probably nine months. We
18 totally supported -- I just want to hear, I guess, we
19 would like the board to approve it. We just have to
20 ratify things so we can sort of put this project aside
21 and start taking --
22 CHAIRPERSON AARONSON: Sandra?
23 MS. MARCH: A basket clause is essential.
24 The change in the basket clause is essential. If we are
25 to move forward and the change in the basket clause is

1 not going to happen unless we have all parties joining
2 together in this state to talk to the people who change
3 the laws. It's not going to happen because the
4 Comptroller's Office goes up and does it by themselves.
5 It's not going to happen. It's the representatives of
6 the employees go up and talk about it on their own.
7 It's not going to happen if the Mayor's Office goes up
8 and talk about it on their own.
9 It's only going to happen if we join forces
10 and all of our lobbyists in Albany are directed to do
11 something they, oftentimes, do not do, work together to
12 get this accomplished. We've made some great changes in
13 terms of our ability to do RFPs and other things because
14 all of the parties work together to get it accomplished.
15 And I don't know how we do it but I would hope that the
16 message will go forth from here that we need to work
17 with our people in Albany to get this done and I think,
18 as one of the representatives of the employees, we will
19 talk to our lobbyist.
20 But we have to have everybody talking to
21 their lobbyist and they have to be a joint memo that
22 goes out. You have to do this in the halls where it
23 counts or we're not getting a change in the basket
24 clause.
25 CHAIRPERSON AARONSON: Right. May I also

1 add that same basket clause exists for the New York
2 State Retirement System.
3 MS. MARCH: Right.
4 MR. SCHLOSS: For Common Teachers.
5 CHAIRPERSON AARONSON: The Teachers, the
6 Police, Fire and local and state employees. And I think
7 we have to make sure we reach out to people, the
8 Comptroller for the state, the unions representing the
9 state employees, and get them all on board.
10 And something we haven't been able to do in
11 this particular area we've been attempting time to time,
12 to get the basket clause or change, we've never been
13 able to succeed. But now, it's even more important and
14 if we work together as a team, not only the City but the
15 City and the State, I think we can accomplish it.
16 MR. SCHLOSS: I have spoken in the past to
17 the counterparties in New York State Teachers and New
18 York State Common. They have the same issues with the
19 basket clause. They have different reasons, for
20 instance, in New York Teachers. It is very big in real
21 estate. But in the basket clause, the same in the New
22 York State Common. We will coordinate with them and we
23 will coordinate with the Mayor's Office, but, again, a
24 City thing in to the a Comptroller's office thing. It
25 is not a Teachers, it's not the Mayor's Office, it's

1 different --

2 MS. NAGASWAMI: With all systems structural.

3 MR. SCHLOSS: All New York City getting

4 together with the other state -- you're totally right.

5 They have to be a very organized, synchronized,

6 approach; as opposed to sporadic conversations. And

7 we'll take -- we had a meeting on this yesterday.

8 MR. McTIGUE: We acknowledge a lot of

9 stakeholders.

10 MR. SCHLOSS: So, we will move this as a big

11 rock. We'll all move it together.

12 MS. MARCH: Since we have a board meeting at

13 the end of this month, and we'll have some kind of

14 report where we are in moving the ball. The three

15 teacher trustees will take the message to whom. We have

16 to bring the message prior to the board meeting, and I

17 hope the other parties will do the same.

18 MR. SCHLOSS: I couldn't tell you to speed

19 with which to move.

20 MS. MARCH: This is why I speed my accounts

21 here. Albany is going home at some point. They have to

22 accomplish their budget. They have other issues they

23 want to handle. They are going to be gone by the time

24 the end of June, the beginning of July comes.

25 So, if I know my simple mathematics, we have

1 a matter of six weeks to accomplish this.
2 MR. SCHLOSS: But we don't need it this
3 time. We don't need to try --
4 MS. MARCH: We don't need it now?
5 MR. SCHLOSS: No. I look at it next year.
6 MS. MARCH: Next year? We have plenty of
7 time to do it.
8 MR. SCHLOSS: Exactly. Organized plan to be
9 laid out.
10 MS. MARCH: And we do not need a report at
11 the board.
12 MS. NAGASWAMI: And that's the assumption is
13 Case A; right?
14 MR. SCHLOSS: Right.
15 MS. NAGASWAMI: That were the same. And we
16 can make some significant -- we can improve it within
17 the basket clause.
18 MR. SCHLOSS: Look on page 91, we have
19 9.8 percent left. We have plenty of -- we have room.
20 MS. MARCH: We have 9.8 -- that's tiny.
21 MR. SCHLOSS: On a funded basis. And we
22 have room. Have you said that we should try to do it
23 next year. The markets move, but the perfect plan for
24 next year.
25 MS. MARCH: I think our target should be,

1 that we are all together by January 1st of 2012; which
2 is the beginning of the next legislature session.
3 MS. NAGASWAMI: Robin, I have a question. A
4 lot of the returns that we are seeing in this entire
5 exercise are really driven by 60-year lows in interest
6 rates, right, in these many ways, because of equity risk
7 and having moved a lot.
8 And I want to point out, and if you look at
9 with Rocaton has just done in terms of reestimating
10 volatility. As you said, Marc said it's going to be --
11 it's not more volatile in the future. My question is
12 we'd laid out of plan for Case A versus Case B. And a
13 lot of Case A versus Case B assume that interest rates
14 don't change and bet for the best way to diversified
15 because it's the same return of scenario.
16 MS. PELISH: They both assume
17 interest exchange is the same, what rate --
18 MS. NAGASWAMI: In the same level, right.
19 Because of the basis for it. But I think my question
20 is, will you come back to is a lot sooner if we get a
21 bear market in bonds and we can diversify without the
22 basket clause or liquidity being given up, if bond yield
23 high enough at some point to justify that
24 diversification?
25 My broader question is valuation. And Larry

1 talks a lot about a lot of the creative things. BAM is
2 trying to find ways to make it more nimble. Our biggest
3 risk is the policy portfolio not the Alpha that we have
4 in our managers.
5 And my question is, how would you encourage
6 us as the board to think about the asset allocation
7 process and rather the -- we have a few years or every
8 year in a way, if there is a huge shift in assumption
9 because of valuation. Shouldn't we come back and look?
10 MS. PELISH: The simple answer is yes. But
11 I would encourage us to think about the issues being
12 raised, separate from asset allocation. So, will you
13 approve asset allocation targets? We're looking out
14 over five to seven-year time period. And we're setting
15 targets and ranges.
16 I think what you're talking about is what
17 clients are starting to implement. It is process by
18 which you decide where do I want to be in that range and
19 have market valuations moved to such an extreme that I
20 want to move down or up in that range? And that has
21 actually occurred. I think in terms of high yield
22 bonds -- in terms of the high yield allocation --
23 MR. SCHLOSS: The high bonds is a great
24 example. And we thought it had its run. We were at the
25 up end of the range and we went over marked the four

1 month, the bottom of the range. And it's in the process
2 for the stock market and that went up -- pretty
3 straightforward. Stay tuned. But that's moved in the
4 right direction. That's why I like having it monthly so
5 we can see it and you can ask questions, why are
6 you where you are?
7 And we have to justify it, because it is, I
8 think, one of the managers. I forget who said we took
9 over in the asset allocation.
10 But we are tickling things, which is why we
11 have a lot of cash, because we're a little anxious.
12 MS. PELISH: Because the asset allocation
13 assumptions really can never be nimble enough, because
14 we are looking at. And even though we -- if we expect
15 rates to rise but we're -- we don't know how it's going
16 to rise -- we don't know how they'll rise in next 12
17 months or in the next 48 months.
18 And we make some gross assumptions. I just
19 don't think this process is refined enough or nimble
20 enough. The setting of the target policy is nimble
21 enough to be able to react quickly in market conditions.
22 But I think we set the ranges appropriately. And look
23 at that data monthly and then move within the ranges.
24 That's what I would suggest.
25 MS. NAGASWAMI: So, the ranges we have now

1 are good enough. You think that these are good ranges
2 and around these asset classes which we talked, but how
3 we might set those because --
4 MS. PELISH: Yes. I can't say that I
5 actually reviewed the ranges lately. I think they are
6 reasonable. Could they be improved? That's something
7 worth considering.
8 MR. SCHLOSS: Interesting. You mention that
9 the private equity is a number. And a former private
10 equity consultant, our primary equity consultant both
11 urge the board in several locations. I think the
12 private equity is a range because it is not moveable.
13 We are going to do some moving, Barry will talk about
14 the secondary stuff in general, that's something
15 completely out of our control.
16 And we shouldn't worry about missing the
17 number. We think about private equity also in a range.
18 Even though we have a number here, it will never take
19 asset. And it moves literally because of some
20 combination of funding of stuff you've committed to and
21 100 percent, then, after that by denomination by the
22 whole fund.
23 So, we should think about -- if there's more
24 than usual amount of flexibility perhaps built into your
25 private equity number. And, again, more out of our

1 control with real estate -- real estate is similar. An
2 asset but you can't move it, you want to move.
3 MR. NORTH: I might observe that I think the
4 whole discussion of range is good one. And personally,
5 I'm a big fan that having the specific percentage target
6 for a class. But I think you're right, illiquid assets
7 should have both some range for -- if you are going to
8 allow for ups and downs and then for some protection
9 against market forces which don't stay marked at their
10 specific level and move around. It's the denominator
11 effect problem.
12 And that all can be set out, discussed and
13 anticipated. But one thing I'd just like to throw out
14 for a thought process is, I do not know how one would
15 provide the authority, determine how you measure whether
16 it's being executed well.
17 But you look at the smaller fixed income
18 classes, opportunistic fixed, we've actually operated
19 high yield this year somewhat opportunistic by
20 decreasing its exposure. Is opportunistic fixed really
21 a better way of thinking a convertibles opportunistic
22 high yield and emerging market debt?
23 If you could figure out a way to create some
24 degree of nimbleness within the entire capacity of fixed
25 income -- it may be illogical, but something I think

1 might be worth thinking about because relatively small
2 classes in which you may want to have some managers,
3 have some opportunities to be nimble, including possibly
4 going out of class entirely for a period of time.
5 So, I just throw that out as something that
6 might be considered by Rocaton and BAM. Again, in
7 thinking about this, whether maybe the asset class
8 should be bigger but it should be confined a little more
9 -- generally.
10 MS. PELISH: Flexibly?
11 MR. NORTH: Flexibly; thank you.
12 It's something to consider.
13 MR. SCHLOSS: I think you've got a great
14 point. I think what you will find is the opportunistic
15 managers don't traffic in those asset class -- yet, but
16 they will. If I look at ten years, emerging
17 markets debt will be in there. And your business will
18 evolve such as a traffic in emerging markets debt,
19 that's more readily active.
20 But we hear later the managers, you will see
21 that they are really corporate debt guys -- debt, and
22 they -- the real estate debt. And neither of those, the
23 way they're defined -- the guys who have converts in
24 them are the hedge fund guys. They are trying to sweep
25 the convertible hedge against the small sort of stuff

1 like that.

2 So, you've got to think a little bit out of

3 asset classes into how the managers are set up. But,

4 again, some of the asset classes mature, you will find

5 to get picked up a Commodity CTA, which is commodities

6 is in the hedge fund bucket and mushed in there.

7 When we talked about hedge funds,

8 specifically, you will find all of a sudden you've got

9 some commodity managers without an allocation to

10 commodity managers, but we hired CTA managers" how did

11 that happen in the hedge fund bucket? So, it's picked

12 up.

13 MR. NORTH: Your point about maybe ten years

14 from now, the world of investing looks different. This

15 board has always been on the leading edge of everything,

16 so saying that it's a positive on that score from

17 whatever its done.

18 But to the extent the asset allocation has

19 to be somewhat shoehorned into the existing structure,

20 that's fine. I just throw it out there as -- the

21 expansion result is smaller bucket sizes for the asset

22 classes.

23 There is some overlap between the risk

24 reward intentions of some of those classes in terms of

25 diversification. And whether or not that might be a

1 possible consideration in terms of the execution of the
2 policy, a policy which is clear, desiring further
3 diversification without too much return loss.
4 CHAIRPERSON AARONSON: Thank you, Robert.
5 MR. SCHLOSS: One last comment on Bob.
6 The line, if you look at some of these
7 numbers, the line between high yield opportunistic fixed
8 income overlaps, it completely overlaps because if you
9 take the straight high yield, one step out is distressed
10 debt, that's broken high yield. You'll see below.
11 So, we have different managers for that
12 because the way we currently have these RFPs high yield
13 excludes that, that makes no sense. But trading in the
14 firm that's her, as oppose to me. It's the same firm,
15 but because of the way it's set up somebody processes
16 the RFPs, with introduced rigidity into the asset
17 allocation which actually don't exist in the market.
18 Somebody out of fixed income, which is
19 trying to get rid of that. So you might see high yield
20 go down because opportunistic goes up, but during the
21 exact -- when you got this same exposure you had before.
22 Just call it something else.
23 CHAIRPERSON AARONSON: We will take Bob's
24 nod as a agreement. So, let's move on.
25 MS. NAGASWAMI: For BAM, can we have a

1 little bit more education around emerging markets debt
2 and perhaps a refresher on convertibles? We are going
3 from 1:00 to 3:00 -- not knowing the asset class well
4 enough.
5 And my last question -- specifically looking
6 through some of the recommendations; we spend a lot of
7 time in our real estate confrontations with our real
8 estate consultant, Robin, and they haven't done the
9 tactical plan. But talking about core versus non-core,
10 is it 40, 60? Is it 40, 20, 40?
11 And there's a very little shift. It's only
12 1 percent of the total portfolio, but the allocation
13 shift out from our current 40, 60 for non-core and flips
14 it to 60, 40 core, non-core. Now, let's just say to
15 Larry, it would be helpful to talk about that with the
16 real estate consultant because, in fact, from a
17 valuation perspective, they had made a very big point
18 about how price is the core at this point.
19 MS. PELISH: Yes.
20 CHAIRPERSON AARONSON: So, this calls for
21 greater education especially to three topics that Ranji
22 just mentioned. And if you could please have something
23 on it?
24 MR. SCHLOSS: Yes. We'll have in the future
25 agenda.

1 CHAIRPERSON AARONSON: Okay. So, we are
2 finished with our discussion of the asset allocation.
3 And we move on to the next item in your agenda, please.
4 MR. SCHLOSS: Do we have to adopt this? Do
5 we adopt this as an asset allocation?
6 CHAIRPERSON AARONSON: It has to be adopted
7 at a public meeting, and there are still some questions
8 that people are still discussing it. Maybe this will be
9 an interim report as oppose to --
10 MR. SCHLOSS: We are going to bump into some
11 implementation issues on opportunistic fixed income.
12 MS. PELISH: Should we come back with the
13 recommendation at the next meeting?
14 MS. MARCH: Yes, please.
15 MR. SCHLOSS: Okay.
16 MS. PELISH: We should come back with the
17 recommendation.
18 MR. SCHLOSS: A final, final.
19 MS. NAGASWAMI: A question. I heard you say
20 either A versus B is basket clause issue. B is more of
21 a theoretical exercise right now. It is just A?
22 MR. SCHLOSS: It's really A. The A's are
23 with the hedge funds. That's all.
24 MS. MARCH: Is there anything else that we
25 have to cover in the public meeting session?

1 MR. SCHLOSS: No.
2 CHAIRPERSON AARONSON: So, we are going to
3 move into executive session. Do we want to take --
4 MR. SCHLOSS: We need a motion.
5 MS. MARCH: I move, pursuant to public
6 officer law Section 105, that we go into executive
7 session to discuss the proposed acquisition, sale or
8 exchange of securities held by the Teachers' Retirement
9 System; and to discuss proposed pending or current
10 litigation.
11 CHAIRPERSON AARONSON: Is there a second?
12 MR. SCHLOSS: Second.
13 CHAIRPERSON AARONSON: Is there any
14 discussion? Hearing none, we are now in executive
15 session. And now we can have a break.
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18 (At this time the meeting went into executive session.)
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21 CHAIRPERSON AARONSON: Motion to go back
22 into public session?
23 MS. MARCH: I make a motion that we go back
24 into public session.
25 CHAIRPERSON AARONSON: Do I hear a second?

1 MS. NIEVES: Second.

2 CHAIRPERSON AARONSON: Any discussion?

3 Seeing none, we're in public session now.

4 And in public session, what we will do is

5 summarize those things we talked about in executive

6 session.

7 And, Susan, could you do that for us,

8 please?

9 MS. STANG: Absolutely. In the executive

10 session for the variable funds, several managers were

11 presented, no action was taken.

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1 In the executive session of the pension
2 fund, updates on several managers were presented.
3 A contract for our service provider was
4 extended while the RFP is being completed.
5 There were presentations from several fixed
6 income managers which were received and discussed. No
7 action was taken.
8 There was a presentation on the private
9 equity investment. A decision was made which will be
10 announced at the appropriate time.
11 CHAIRPERSON AARONSON: Thank you very much.
12 Do I hear motion to adjourn?
13 MS. MARCH: So moved.
14 MR. SCHLOSS: Second.
15 CHAIRPERSON AARONSON: Any discussion?
16 Seeing none, we're adjourned.
17 (Time noted: 3:07 p.m.)
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2 C E R T I F I C A T I O N

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4 I, Jeffrey Shapiro, a Shorthand Reporter and

5 Notary Public, within and for the State of New York, do

6 hereby certify that I reported the proceedings in the

7 within-entitled matter, on Thursday, May 12, 2011, at

8 the offices of the TEACHERS RETIREMENT SYSTEM, 55 Water

9 Street, New York, New York, and that this is an accurate

10 transcription of these proceedings.

11 IN WITNESS WHEREOF, I have hereunto set my

12 hand this _____ day of _____________, 2011.

13

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15 ____________________________

16 JEFFREY SHAPIRO

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