MINUTES
PUBLIC MEETING
February 17, 2012
8:30 am
Auditor's Office Suite 240

I. Call to Order/Roll Call

Auditor Tim Berry called the meeting to order at 8:32 am. Other committee members present were, Jon Vanator, Deputy Budget Director, Mike Frick, Chief Deputy Treasurer and Martha Lake. Also present were State Treasurer Richard Mourdock, Kirke Willing; Deputy Auditor, Jaimie Beisel with Great-West Retirement Services (Third Party Administrator to the Plan), Mike Paton of Barnes & Thornburg (Counsel to the Committee and the Administrator), Joe Bill Wiley and Tiffany Spudich with Capital Cities (Investments Consultants to the Committee) and Erin Sheridan with the Auditor of State's Office.

II. Reading of the Minutes

Tim Berry asked for a motion to approve the minutes from the November 18, 2011 meeting. Mike Frick moved to approve the minutes. Martha Lake seconded. The minutes were approved unanimously.

III. Administrators Report

Auditor Berry announced the reinstitution of the state's portion of the match ($15.00) per pay period for all state employees who are participants in the plan. New hires are automatically enrolled into the plan as of 7/1/11. Opt outs are around 3%.

Jon Vanator was introduced as a new board member as the Governor's appointee.

IV. Management Consultants Report

<u>2011 Market Review</u>

Joe Bill Wiley gave an overview of the market for the past year. The results for 2011 showed a sharp slump in all equity segments. Domestic equity returns were down almost 10% through September 2011; a strong fourth quarter brought returns back above zero. International markets were not so fortunate.

Five-year equity returns through 2011 are essentially zero. Ten-year returns are weak as the tech bubble has rolled out of the calculations, and include two downturns. Fifteen-year returns are still below long-run averages, and are back below those of fixed income.

Global markets tended to fluctuate according to the latest macro news, leading to rising correlations among asset returns. The correlation among U.S. stocks reached its highest point on record during the volatility in September, while U.S. stocks were also more correlated with other riskier asset categories. High-quality bonds offered diversification opportunities.

Interest rates are a threat to fixed income returns. Fixed income is a conundrum for investors. No other investment offers the same anchor to windward and protection in a flight to quality. Yet low yields and the prospect of rising rates (eventually) spell dismal returns.

Falling back into a recession is still a concern. An economy near stall speed is vulnerable to shocks. Oil shocks are a perennial threat. The economic outlook is fully expected to meander through a weak recovery, as the combination of recession, financial crisis & deleveraging required time to work through the system. The housing market has yet to truly hit bottom, despite mortgage rates at an all-time low. The "shadow inventory" of homes yet to foreclose still hangs over the market.

Performance & Evaluation Report

US equities finished the 4th quarter of 2011 with double digit returns across style and capitalization. During the quarter, capitalization was inversely related to returns, as small and mid caps performed best at 15.5% & 12.3% respectively, while large caps posted an 11.8% return. High yield and emerging Market debt, most notably, posted a 6.5% and 5.1% return respectively for the quarter. Municipal bonds lead within fixed income styles over a one-year period at a 10.7% return.

Market Overview

Market Environment:

2011 was a year of significant global events: political upheaval in the Middle East; a terrible earthquake and tsunami in Japan; a debt crisis that threatens the world's largest economic union; US political gridlock that seems to drown out most reasonable voices; S&P downgrades on the sovereign debt of nine developed countries and warnings on five others.

Despite the political and economic turmoil that currently dominates the news, corporations continue to perform well. The 4Q2011 earnings season posted record profits, eclipsing the peak levels of the previous quarter. Inflation data remains fairly benign, unemployment is high and there are continued concerns regarding the federal budget.

Equities:

US equities finished the 4th Q of 2011 with double digits returns across style and capitalization. Over the last one-year period, only US large cap equities posted positive results, while small caps, mid caps, and foreign equities finished the year firmly in the red.

Fixed Income:

The 10-year treasury yield bounced around notably during the 4th Q, only to end up just slightly below where it began. With 10-year treasury rates below 2%, investors are suffering negative yields for the safety of U.S. Government obligations

Considerations & Observations

Tiffany Spudich asked the committee to vote on replacing Artio International Equity II due to organization, product, and performance. At the end of September, Artio announced the reduction of its workforce by 25 employees, 11% of headcount. The Fund's last three- and five-year returns fall in the bottom quartile of peers. Capital Cities asked to begin a search for a new manager.

Auditor Berry asked on behalf of the new board members for a brief summary of the process of a search and how it will impact the portfolio.

Tim Berry asked for a motion to approve moving forward on the search for Artio replacement. Mike Frick moved the motion. Martha Lake seconded. The motion was approved unanimously.

Tiffany went on to report both BlackRock Large Cap Value & Wells Fargo Adv Capital Growth were added to the Watchlist. Performance was a contributing factor for both. Wells Fargo however had significant personnel changes most notably the departure of the Co-Portfolio Manager of the Strategy, Mike Harris.

Vanguard Capital Opportunity trails the Index by over four percentage points and ranks in the bottom half of peers over the last one-year time period. Cap cities will conduct a review.

Logan Circle Partners was placed on the Watchlist status in May 2007. The recommendation is to remove them from the watchlist due to a more stable employee base and their short-term performance has rebounded.

Fee Analysis

All of the Funds in the Plans have expense ratios below the median of their perspective peers and The Indiana Retirement Funds (Target date funds) are competitively priced at 33 to 43 basis points. The approximate investment management fees paid would be $3.2 million, based on 12/31/11 market values. Of which, approximately $250,000 would have been provided to the Plan in the form of revenue-sharing.

$1,621,806 in administrative fees was collected by Great West during the calendar year 2011. The actual fees paid to Capital Cities in 2011 were $65,969.18 Capital Cities contract was updated in May 2011.

IV. Old Business

State Board of Finance Annual Report Memo

Indiana Code requires the deferred compensation committee to report to the State Board of Finance at least annually on the status of, and any changes to, the State Deferred Compensation Plan, commonly known as Hoosier S.T.A.R.T. The report indicates no fund changes to the investment portfolio in 2011 although the 9 Target Date Funds and Inflation-Linked Bond Fund options were added. Also as mentioned earlier the re-enactment of automatic enrollment for newly hired state employees.

Agreed Upon Procedures Report

Annually BKD, LLP performs an agreed upon procedures audit on the Hoosier S.T.A.R.T. plan. These procedures are set up to review the State and all participating local governments as well as Great West Retirement Services to make sure Plan participants contributions are being reported and distributed correctly. Any errors in reporting are dealt with individually and corrected. Jaimie Beisel from Great

West expressed his appreciation of the report so that any errors can be corrected. 260 local governments participate in the plan so making sure data/records are updated and correct is a priority to Great West.

V. New Business

No new business was reported.

VI. Adjournment

There being no further business before the Committee the meeting was adjourned at 9:20 a.m. Next scheduled meeting is May 18, 2012 at 9:00 a.m.