These minutes are Approved and Final. Full Board review and decision took place at the November 18, 2014 Regular Meeting of the Board.

MONTANA BOARD OF INVESTMENTS
DEPARTMENT OF COMMERCE
2401 Colonial Drive, 3rd Floor
Helena, Montana

MINUTES OF THE MEETING
August 19 - 20, 2014

BOARD MEMBERS PRESENT:

Mark Noennig, Chairman
Gary Buchanan
Karl Englund
Jack Prothero
Marilyn Ryan
Jon Satre
Sheena Wilson

BOARD MEMBERS ABSENT

Kathy Bessette
Quinton Nyman

LEGISLATIVE LIAISONS PRESENT:

Senator Dave Lewis
Representative Kelly McCarthy

STAFF PRESENT:

Polly Boutin, Associate Financial Manager
Jason Brent, CFA, Alternative Investments Analyst
Geri Burton, Deputy Director
Dana Chapman, Board Secretary
Richard Cooley, CFA, Portfolio Manager, Fixed Income/STIP
Frank Cornwell, CPA, Associate Financial Manager
Craig Coulter, Alternative Investments Analyst
Roberta Diaz, Investment Accountant
David Ewer, Executive Director
Julie Flynn, Bond Program Officer
Tim House, Equity Analyst/Investment Operations Chief
Ethan Hurley, CAIA, Portfolio Manager, Alternative Equities
Ed Kelly, Alternative Investments Analyst
Teri Kolnik, CFA, Alternative Investments Analyst
Eron Krpan, Investment Data Analyst
Herb Kulow, CMB, Portfolio Manager, In-State Loan Program
Tammy Lindgren, Investment Accountant
April Madden, Investment Accountant
Gayle Moon, CPA, Financial Manager
Rande Muffick, CFA, Portfolio Manager, Public Equities
Kelsey Poore, CPA, Investment Accountant
Jon Putnam, CFA, FRM, Fixed Income Investment Analyst
John Romasko, CFA, Fixed Income Investment Analyst
Nathan Sax, CFA, Portfolio Manager, Fixed Income
Clifford A. Sheets, CFA, Chief Investment Officer
Steve Strong, Equity Investment Analyst
Louise Welsh, Senior Bond Program Officer
Dan Zarling, CFA, Director of Research

GUESTS:

Becky Gratsinger, CFA, RVK, Inc.
Jim Voytko, RVK, Inc.
Mark Higgins, CFA, RVK, Inc.
Jonathan Kowolik, RVK, Inc.
Brad Sanders, Bureau Chief, State Procurement Bureau
Sheri Scurr, Legislative Services Division
Mike Heale, CEM Benchmarking

CALL TO ORDER

Board Chairman Mark Noennig called the regular meeting of the Board of Investments (Board) to order at 10:30 AM. As noted above, a quorum of Board Members was present.

Board Chairman Noennig asked for public comment. There was no public comment. Chairman Noennig called for any corrections or revisions to the Board minutes from the May 20-21, 2014 Board meeting.

> Board Member Jack Prothero made a Motion to approve the May 20-21, 2014, Board Meeting minutes. Member Marilyn Ryan seconded the Motion. The Motion carried 7-0.

ADMINISTRATIVE BUSINESS

Audit Committee Report

The Audit Committee met prior to the Board meeting. Committee Chairman Jon Satre reported the Committee reviewed and approved the 2014 Fiscal Year Internal Controls Report prepared by Galusha, Higgins & Galusha. The Committee also approved revisions to the Internal Controls Policy. Staff from Legislative Audit Division was on site in June and will return in September; the Board's Fiscal Year 2014 Financial - Compliance Audit report is due late fall. Executive Director David Ewer stated staff is coordinating a disaster and emergency preparedness meeting for this fall, including security system updates. Meetings will occur annually going forward.

Human Resource Committee Report

The Human Resource Committee met prior to the Board meeting. Human Resource Committee Chairman Karl Englund reported on MBOI staffing. Ms. Gayle Moon introduced new accounting staff member Ms. Kelsey Poore. Ms. Poore graduated, with honors, from the University of Montana where she was on the cheer squad. She attained her CPA designation in May 2013. Ms. Poore will take over the real estate and enterprise transactions. Ms. Polly Boutin spearheaded the hiring and she will conduct the training. Mr. Dan Zarling introduced Mr. Craig Coulter, the new alternative investments analyst. Mr. Coulter is a graduate of Michigan State and received his MBA from Grand Valley State. His experience includes working with alternative investments at the state of Michigan. MBOI now has four alternative investments analysts.

Loan Committee Report

The Loan Committee met prior to the Board meeting. Committee Chairman Jack Prothero advised the Committee approved three Bond Program loans:

- Sun Prairie Village County Water and Sewer District for $320,000 increase for a total loan of $1,719,000 to interim finance its water system improvement project,
- MSU Bozeman for $1.8 million to renovate the Strand Union Building ballrooms.
- City of Libby for $3.2 million to interim finance the Flower Creek Dam replacement project.

No loans require full Board approval. The In-State Loan Program had no items before the Committee.

Public Employees' Retirement System (PERS) and Teachers' Retirement System (TRS) Updates

TRS Representative Marilyn Ryan reported the Denver JP Morgan conference she and Member Jon Satre attended in Denver was worthwhile. The conference covered substantial information on purchasing and managing real estate including multi-family financing. Discussions highlighted the geographical and practical risks associated with overseas investments, such as infrastructure in China. Member Jon Satre added the focus on infrastructure in China provides a possibility for higher returns, and is beneficial to China, but comes with a lot of associated risk. The general outlook is optimistic for core real estate. The conference size was small, with 25-30 participants, which contributed to its success.

Member Ryan reported Daniel Trost has replaced Bob Pancich on the TRS Board. The board has not appointed a new chairperson yet. Installation of the new computer system has suffered delays, but otherwise is going well. The GABA (Guaranteed Annual Benefit Adjustment) litigation is ongoing. The plaintiffs filed for summary judgment on July 28, 2014; the decision is still pending.

PERS Representative Member Sheena Wilson reported PERS has begun preparation on bills for the 2015 Montana Legislature to infuse cash into both Game Wardens and Sheriffs retirement systems to bring the plans up to actuarial soundness.

Legislative Liaisons Comments

Senator Dave Lewis stated President Obama has signed a new bill allowing veterans the option of going to private health care providers if services are not readily available at Veterans' Administration (VA) facilities. Senator Lewis also reported that state employee health care plan increases, including higher deductibles, might be coming to address higher costs.

Representative Kelly McCarthy did not have anything to report at this time.

EXECUTIVE DIRECTOR'S REPORT

Overall Comments

Executive Director David Ewer presented his executive director's memo.

A. Follow up requests from Members:

In response to a request by Member Prothero, staff will present information on risk management strategies for the fixed income internally managed portfolio later in the agenda.

B. The quarterly cost report is included in the Board packet.

C. The Board's one day meeting is Tuesday, October 7, 2014. The meeting will be a full day and the Loan Committee will meet prior to the meeting. Board members set priorities for preferred topics for the day including: a presentation by RVK, Inc., covering practices of other investment boards vs. MBOI; an outside asset manager will be brought in to present; a private equity manager has been invited to present; and an economist is invited but has not been confirmed yet.

D. Staff is recommending revisions to the Governance Policy to include all the statutory criteria requirements for Board Membership. Full Board approval is needed to revise the Policy.

> Board Member Sheena Wilson made a Motion to approve the staff recommended changes to the Governance Policy. Member Jon Satre seconded the Motion.

Responding to a question from Member Buchanan, Chairman Noennig stated the Governance Policy is the Board's guidance. The proposed revision does not materially change the Policy, but rather adds clarification by incorporating statute language on Board Membership and is a housekeeping item. The Motion carried 7-0.

MONTANA LOAN PROGRAMS

In-State Loan Program

Mr. Herb Kulow presented an update of the commercial and residential loan program portfolios. As of July 31, 2014, the commercial loan portfolio totaled $100,446,742.98, the lowest it has been since 2000. Currently there is approximately $39 million in the pipeline. On June 6, 2014, First Interstate Bank bid $800,000 at the scheduled sheriff's sale for Vann's warehouse property in Lolo. They were the sole bidder. The remaining MBOI balance is now $560,000, 70% of the purchase price, and resulted in a write down by staff of $62,279.95. First Interstate Bank has listed the property for sale at $1.1 million. If the property sells for more than $800,000, MBOI may recover a portion of the loss.

Responding to Board Member questions, Mr. Kulow stated the property appraised at $800,000. If it sells for less than the appraised amount, MBOI would realize an additional loss.

Mr. Kulow reported the residential loan portfolio totals $11,646,119.48 as of July 31, 2014. Four past due loans total $243,199.67. All past due loans are guaranteed. Veterans' Administration (VA) loans have leveled off. No VA loans are past due. Outstanding VA loan reservations total $1,457,261. The current yield for the VA loan portfolio is 2.3% (2.8% minus the 50 basis point service fee).

The Loan Committee approved a participation loan for $2.568 million (80%), to FM, LLC and Harris Manufacturing, Inc., at a special conference call meeting on June 30, 2014. The loan request came from First Interstate Bank. Total loan amount is $3.21 million. The manufacturing plant, located across from Town Pump in Bonner, outside of Missoula, makes pressure vessels which are transported to the oil sands in Canada. The company has a four-year contract with General Electric and expects to create up to 40 new jobs.

BOND PROGRAM REPORTS

Activity Report

Ms. Louise Welsh reviewed the quarterly Activity Summary Report and presented the staff approved loans. The Loan Committee approved three loans. Ms. Welsh also presented the fiscal year end Loan Detail Report and noted loans are concentrated primarily for counties, cities, school districts and universities. Responding to a question from Member Satre, Ms. Welsh explained counties not utilizing INTERCAP have other funding sources available; they are aware of the program. The maximum loan term for INTERCAP loans is 15-years, which may restrict use for larger projects needing longer terms.

Staff approved loans:

Borrower:	City of Harlowton
Purpose:	Interim loan in anticipation of Rural Development (RD) long-term financing for wastewater system improvements
Staff Approval Date:	April 1, 2014
Board Loan Amount:	$ 711,000
Other Funding Sources:	$ 889,000
Total Project Cost:	$1,600,000
Term:	1 year

Borrower:	Pondera County
Purpose:	Purchase and refinance various types of hospital equipment
Staff Approval Date:	April 24, 2014
Board Loan Amount:	$622,578
Other Funding Sources:	$ 0
Total Project Cost:	$622,578
Term:	3 years

Borrower:	Anaconda-Deer Lodge County
Purpose:	Rehabilitate historic street lights in Lighting District #150
Staff Approval Date:	April 28, 2014
Board Loan Amount:	$ 500,000
Other Funding Sources:	$ 500,000
Total Project Cost:	$1,000,000
Term:	15 years

Borrower:	Town of Stanford
Purpose:	Repair municipal pool and purchase a Bobcat Skid-Steer Loader
Staff Approval Date:	April 30, 2014
Board Loan Amount:	$28,000
Other Funding Sources:	$30,204
Total Project Cost:	$58,204
Term:	3 years

Borrower:	Turner Public School Districts
Purpose:	Install a new heating system
Staff Approval Date:	May 12, 2014
Board Loan Amount:	$344,000
Other Funding Sources:	$ 57,111
Total Project Cost:	$401,111
Term:	5 years

Borrower:	Lewis & Clark County
Purpose:	Finance road improvements for Lincoln Rural Improvement District
Staff Approval Date:	May 9, 2014
Board Loan Amount:	$89,846
Other Funding Sources:	$ 0
Total Project Cost:	$89,846
Term:	7 years

Borrower:	Lewis & Clark County
Purpose:	Finance road improvements for Lambkin Rural Improvement District
Staff Approval Date:	May 9, 2014
Board Loan Amount:	$33,502
Other Funding Sources:	$ 0
Total Project Cost:	$33,502
Term:	7 years

Borrower:	Town of Hobson
Purpose:	Finance repairs to municipal pool
Staff Approval Date:	May 20, 2014
Board Loan Amount:	$54,407
Other Funding Sources:	$ 0
Total Project Cost:	$54,407
Term:	10 years

Borrower:	Town of Stevensville
Purpose:	Interim loan in anticipation of Rural Development (RD) long-term financing for wastewater system improvements
Staff Approval Date	June 3, 2014
Board Loan Amount:	$ 800,000
Other Funding Sources:	$3,042,000
Total Project Cost:	$3,842,000
Term:	1 year

Borrower:	Lewis & Clark County
Purpose:	Finance road improvements for Augusta Rural Improvement District
Staff Approval Date:	June 4, 2014
Board Loan Amount:	$37,331
Other Funding Sources:	$ 0
Total Project Cost:	$37,331
Term:	7 years

Borrower:	Kester School District #23
Purpose:	Provide a teacherage on school property
Staff Approval Date	June 11, 2014
Board Loan Amount:	$54,940
Other Funding Sources:	$ 0
Total Project Cost:	$54,940
Term:	5 years

Borrower:	Malta School District
Purpose:	Replace boiler in elementary school
Staff Approval Date	June 13, 2014
Board Loan Amount:	$120,000
Other Funding Sources:	$ 0
Total Project Cost:	$120,000
Term:	5 years

MONTANA UNIVERSITY SYSTEM

Borrower:	Montana State University – Billings
Purpose:	Repair and replace Petro Residence Hall roof
Staff Approval Date	June 5, 2014
Board Loan Amount:	$560,000
Other Funding Sources:	$ 0
Total Project Cost:	$560,000
Term:	10 years

INTERNALLY MANAGED FIXED INCOME RISK EXPOSURES

Mr. Cliff Sheets, CFA, CIO, Mr. Nathan Sax, CFA, Portfolio Manager, Fixed Income and Mr. Rich Cooley, CFA, Portfolio Manager, Fixed Income/STIP

Mr. Cliff Sheets presented the breakdown of fixed income assets managed internally by staff. Staff manages 91% of the total $8.04 billion fixed income assets held as of June 30, or $7.4 billion. Each pool has its own policy statement and the Board must approve any changes in policy. Policies address and control risks at the highest levels and are reviewed annually.

Mr. Nathan Sax reviewed the risks and constraints as set out in policy. Policy sets limits on duration and maturity, allowable ranges vs. the benchmark, permitted and prohibited investments and limits on holdings based on a dollar value or as a percent of the total account. Policy also limits credit and issuer risk, although staff is generally more conservative than policy allows.

Mr. Sheets added policy sets broad guidelines and caps an individual name at 2%, not exceptionally large. The portfolio is diversified more prudently vs. policy, which allows for unusual events such as two corporations merging, suddenly increasing the size of a single name.

Mr. Sax stated the Core Investment Bond Pool (CIBP) is underweight in treasuries and overweight in corporates, providing a yield advantage over the benchmark. Responding to a question from Member Prothero, Mr. Sax noted ranges are kept reasonable and on the wide side which accommodates the frequent changes in the index. Ms. Becky Gratsinger added ranges are appropriate and not a cause for concern; the team has done a nice job of diversification. Mr. Jim Voytko noted that flexibility avoids the need for frequent adjustments to the ranges.

Fixed income staff meets weekly and monthly to discuss strategy and look ahead to market outlook for the next 3 – 6 months. Mr. Sheets stated fixed income plays a critical function in the overall pension portfolio primarily in terms of providing diversification.

Responding to a question from Member Prothero, Mr. Sheets explained staff uses the Merrill U.S. Broad Index because it is free and works well as a proxy for the Barclays Aggregate, which is costly. Barclays is available monthly on a snapshot basis. Mr. Sax added income determines most of the return in fixed income portfolios, and that holding bonds providing a yield advantage over the long term gives an advantage over the index. Tracking error of the internally managed portfolios is low, as the portfolio return tracks close to the benchmark resulting in less volatility and less risk. Ten years ago, the portfolio deviated more and by taking on added risk. The portfolio today has over 250 holdings which guards against an unforeseen credit event.

Mr. Rich Cooley advised the $1.18 billion fixed income portion of State Fund Insurance has approximately 200 securities. Income return is the primary goal. The account policy limits holdings with less than an A rating and the portfolio is overweight corporates and underweight treasuries to add yield. A primarily buy and hold strategy is used. Mr. Sheets noted the $1.18 billion is the fixed income only portion of State Fund. The portfolio also contains equities and real estate to increase overall portfolio return.

Mr. Cooley stated the investment policy statement for the Short Term Investment Pool (STIP) is more restrictive for sectors, maturities and ranges.

In conclusion, Mr. Sheets stated staff measures and monitors the key risks of interest rate sensitivity and sector exposure at the portfolio level and reviews individual issuers. The approach is disciplined, with tactical changes made within the restraints of policy.

Member Prothero thanked staff for all their hard work and Member Buchanan commended staff on keeping costs low for internally managed fixed income. Mr. Sheets stated costs are about 2.5 basis points and added it is fortunate to have the internal resources to manage over $7 billion of the total fixed income portfolio.

CUSTODIAL BANK REQUEST FOR PROPOSAL (RFP)

Mr. David Ewer, Executive Director, Ms. Geri Burton, Deputy Director, Mr. Jonathan Kowolik, Senior Consultant, RVK, Inc. and Mr. Brad Sanders, Bureau Chief, State Procurement Bureau

Executive Director Ewer thanked staff for all their hard work during the RFP process and presented his memo on the Custodial Bank Proposal and Staff Recommendation. The state received three responses: State Street Bank, J.P. Morgan and BNY Mellon. The scoring process consisted of three sections: cost proposals, written responses and interviews in Helena by the three respondents. Scoring of the three sections allowed for a maximum possible score of 1,000 points.

Ms. Geri Burton explained the RFP process. A committee of Board staff, in consultation with the State Procurement Bureau and RVK's Mr. Jonathan Kowolik, wrote the RFP. The team met weekly since the start of the process last spring. The RFP was completed and issued in April, responses were due in May and the three respondents participated in interviews in Helena the last week of July. The Board's staff committee with input from the State Procurement Bureau and RVK reviewed and scored each step.

Mr. Brad Sanders stated the Department of Administration's RFP process is fairly rigid and the Procurement Bureau participated in the complete process. The Bureau notified 140 vendors of the RFP and complied with all state law requirements. The Board answered nearly 100 questions from respondents. State law requires awarding the contract to the high scorer, and may not go to the second highest scorer. (If the contract is not awarded, the RFP process must start over from the beginning.)

Executive Director Ewer asked Jonathan Kowolik to explain his role in the RFP process.

Mr. Kowolik works out of the New York office of RVK, Inc., specializing in vendor operations, vendor relationships and transitions, and has participated in over 50 competitive vendor reviews in recent years. Mr. Kowolik participated throughout the RFP process as a subject matter expert and provided commentary as an RFP reviewer and worked with staff to develop the RFP. He attended the weekly committee meetings via phone and traveled to Helena for the interview presentations by the three respondents.

Mr. Kowolik noted the field of custodial banks has consolidated significantly with only four commonly observed and generally qualified entities (Bank of New York Mellon; JP Morgan; Northern Trust; and State Street) capable of managing the scope of services required by the MBOI as a large US Asset Owner. Northern Trust opted not to respond to the RFP. They sent a letter; however, it did not offer any reasoning for not responding.

RVK indicated that MBOI received reasonable responses from the respondents to the customized RFP issued. RVK further noted that the evaluation process contemplated by RFP and performed by the MBOI carefully considered the key success drivers of the relationship – People, Process, Technology and Reasonable Economics. RVK concluded with its concurrence that the Board accept the Staff Recommendation that the Board move to accept the scoring of the custodial bank RFP and to recommend the State's Procurement Bureau, working with Board Staff and RVK, proceed in entering into a custodial banking contract with State Street Bank (under either a relationship with or excluding securities lending).

Executive Director Ewer stated it is likely the status quo will continue with State Street managing securities lending, although the option to outsource is available.

Mr. Sheets added securities lending is working as is, but should be considered individually and the current use of commingled cash collateral is something to be discussed separately. Mr. Kowolik noted best practices in securities lending are evolving but recognition of the potential for an increase in risk accompanying increasing returns is prudent. Furthermore, clients should have the option to prudently shift away from securities lending and therefore, including/excluding securities lending under a clearly priced economic framework may be a useful consideration.

Deputy Director Geri Burton noted the current contract fee charged by State Street for securities lending is an 80/20 split.

Responding to a question from Member Sheena Wilson, Ms. Gayle Moon stated that during the three presentations, staff became aware of alternative software programs available. New transfer agent options may be possible under the new contract.

Member Jack Prothero asked if State Street has resolved past issues satisfactorily. Ms. Moon advised the current team is working very hard to provide the needed client servicing.

Mr. Sheets added past performance discrepancies that occurred with private equity regarding distributed gains, which required corrections by State Street, were resolved long ago and performance measurement activities are slowly improving. Mr. Eron Krpan, our new data analyst, continually monitors State Street data and occasionally issues still come up. The system is not perfect; however, and is complicated by the asset pool structure, which is somewhat unique to MBOI. Ongoing monitoring is necessary, but would be required with any custodial bank. Alternatives to State Street's proprietary Private Edge system for private equity performance evaluation are available, and may ultimately prove superior if we wanted to pursue these.

Mr. Kowolik stated Private Edge provides a reasonable service. The RFP evaluation team shared with State Street the need for improvement and the scores reflected such areas of shortcomings. The team also voiced concerns over recent staffing changes and the resulting disruption to service. Ms. Moon added when the Alameda, California office closed, key knowledgeable personnel chose not to move to work in the Sacramento office. Biweekly team meetings via conference call started over a year ago and have helped resolve issues. In addition, onsite visits by State Street personnel, three times per year, are ongoing.

Deputy Director Burton stated that staff and the Procurement Bureau will complete final contract negotiations. Mr. Brad Sanders clarified the contract is refined, not negotiated, as it is structured according to the original RFP. Mr. Kowolik added he would assist finalizing the contract if needed.

Member Karl Englund asked for clarification on the existing relationship with State Street Bank.

Mr. Kowolik stated MBOI has a very complex relationship with State Street, and while existing issues have been the focus throughout the RFP process, generally, the relationship works well and State Street has worked to fit the unique needs presented by MBOI. It is common for such relationships to experience some temporary or ongoing issues. The RFP process spotlights issues and although it can identify a replacement, it can also allow for a process transition of sorts with an existing custodial bank – through validation of areas of strength and customization as well as the potential implementation of new processes and functionality in response to areas of market-relative weakness.

Ms. Becky Gratsinger stated in addition to transition risk, there is no guarantee the same areas of concern will not arise and be a factor with a new custodial bank.

> Board Member Gary Buchanan made a Motion to accept staff's scoring of the custodial bank RFP and to recommend the State's Procurement Bureau, working with Board staff and the RVK consultant, to proceed in entering into a custodial bank contract with State Street Bank. Member Jack Prothero seconded the Motion. The Motion carried 7-0.

CEM BENCHMARKING ANALYSIS

Mr. Mike Heale, CEM Benchmarking

Executive Director Ewer introduced Mr. Mike Heale from CEM Benchmarking. CEM conducts an independent analysis of the MBOI returns and cost structure. This is the fourth year in a row CEM has conducted the analysis, providing the benefit of longer-term data. Mr. Heale stated that this year the comparison included 46 public funds. The peer group is consistent, although varies slightly from year to year. The cost analysis focus compares a custom peer group of 20 U.S. public sponsors with a median size of $10.7 billion. Costs are evaluated to determine if they are reasonable and cost effective.

The MBOI 4-year net return ranks in the top quartile at 11.3% vs. the public median of 10.4% and the peer median of 10.2%. The 4-year policy return of 11.5% is above the public median of 10.4% and the peer median of 10.1%. (Policy return is the return you could have earned passively by indexing investments according to policy mix.) The standardized benchmark used for private equity neutralizes benchmark noise and impacts policy return by 40 basis points due to the premium benchmark set by MBOI for private equity. The benchmark used is based on a lagged, investable small cap market index.

The higher MBOI 4-year average policy mix returns vs. the U.S. public universe are due to higher allocations to private equity and U.S. stocks, which both performed well. A zero allocation to poorly performing hedge funds, vs. the U.S. public universe allocation average of 4%, was also beneficial.

MBOI 4-year net returns for total fund and by asset class outperformed the U.S. public average. Investment costs totaled $49.1 million, or 56.7 basis points, compared to the peer average of 67.9 basis points.

Portfolio costs have trended down since 2010, declining 12 basis points, due primarily to an increase in passive investments from 14% in 2010 to 34% in 2013. The actual management cost of $49.1 million would have cost $54.7 million when applying the costs paid by peers for similar asset class exposures.

The two biggest factors affecting costs are implementation style, such as fund of fund vs. direct investments for private equity, and passive vs. active investments. MBOI invests less with external active managers, 46% vs. peers at 68%, and within alternative asset holdings invests 17% in fund of funds vs. peers at 18%.

Combined savings over the period were quite good, accounting for savings of $5.622 million per year, or 6.5 basis points. Paying more does not always offer rewards, so managing costs is important.

Member Prothero asked Ms. Gratsinger to comment.

Ms. Gratsinger stated any opportunity to lower costs is beneficial. The recent asset allocation restructuring of the portfolio has had a positive impact and resulted in outperformance vs. peers, but continued improvement will taper off. In addition, market conditions over the past four years have favored the portfolio restructure.

Member Englund asked what effect indexing the entire portfolio would have.

Mr. Heale stated even with indexing there are costs. Asset mix drives returns and it is possible to implement added value with active investing. To realize greater savings, major style changes would be required. Negotiating lower fees is a possibility as well. Costs in the U.S. have increased significantly over the past 10 years, due largely to increases in more expensive asset classes. The 11.3% 4-year net return is very good.

GUIDE TO INVESTMENT PERFORMANCE ANALYSIS

RVK, Inc. – Ms. Becky Gratsinger, CFA, Mr. Jim Voytko and Mr. Mark Higgins, CFA

Mr. Mark Higgins reviewed the Retirement Plans Comparative Performance report. The nine plans have nearly identical allocations and returns. Net and gross returns are calculated. Using the median of peer funds greater than $3 billion, returns are compared and ranked on a gross of fees basis. Net return after fees is what generates growth.

Mr. Cliff Sheets added that returns are driven by a compounding factor. Strong returns amplify the difference in gross vs. net return percentage, whereas weak returns have a compressing effect.

Mr. Higgins explained that the Public Employees' benchmark is a composite of the weighted average roll up of the underlying benchmarks used to measure the underlying investments. Ranking vs. peers is more meaningful over longer periods and low percentile numbers are good when compared to peers. Mr. Higgins noted that analyzing performance and the impact of real estate and private equity are only meaningful over a long period. Short-term underperformance of private equity in particular is reflective of the tendency of this asset class to lag in a strong bull market in public equities.

Chairman Noennig asked if the benchmark used for private equity is the most appropriate one.

Mr. Higgins stated that a premium is necessary to reflect the fact that private equity investors need to be properly compensated for the risk and illiquidity of the asset class.

Mr. Higgins reviewed the risk and review comparison, which compares MBOI to a universe of 45 peers. The charts show standard deviation, Sharpe Ratio, excess return, downside risk and beta. The standard deviation measures portfolio volatility. The Sharpe Ratio calculates the risk adjusted return, whether your risk is providing the desired added return. A higher ratio indicates better performance. The beta measures sensitivity of the portfolio to movements in the U.S. equity market. A beta of 1 means the portfolio moves in accordance with fluctuations of the equity markets. Ms. Gratsinger added that greater diversification helps lower beta to less than one. Mr. Higgins stated lowering risk without lowering the rate of return is ideal. Five years ago, the portfolio carried the same risk, but returns were lower, so this has improved over time.

Mr. Higgins presented a summary of the investment pools and corresponding benchmarks. He stated the S&P 1500 Composite Index is an appropriate benchmark for the Montana Domestic Equity Pool (MDEP) as it includes variations in style, growth vs. value, and small, mid and large cap equities. The International Custom Benchmark used currently for the Montana International Investment Pool (MTIP) is the MSCI All Country World ex-US IMI index, a broad index of international equity markets, including both developed and emerging market equities.

The Retirement Funds Bond Pool (RFBP) and the Trust Funds Investment Pool (TFIP) use the Barclays US Aggregate Bond Index, a broad measure of core U.S. fixed income with a high concentration of U.S. Treasury bonds and does not include high yield "non-core" securities.

The benchmark used for the Montana Real Estate Pool (MTRP), the NCREIF ODCE Index (Net), works well for performance but holdings vary compared to the MBOI portfolio which suffered from poor timing on entry into the real estate market.

The Short Term Investment Pool (STIP) uses the 1-Month Libor Index benchmark, which provides a reasonable fit for the portfolio. STIP also uses the iMoney Market Fund (Gross) Median index which measures the performance of peer median institutional money funds, however it reports gross of fees, whereas MBOI is net of fees.

The Montana Private Equity Pool (MPEP) uses the S&P 1500 + 4% as the index. The public equity benchmark, plus a 4% premium on expected return, takes into account the increased risk and illiquidity of private equity. The returns lag a quarter, as compared with public equity markets; therefore, returns over the longer periods of 7 or 10 years should be considered.

Ms. Gratsinger reviewed the asset classes in relation to beta for the total fund. The portfolio beta for all asset classes combined is 0.60. Equities drive the portfolio, so it is important to have low beta assets such as fixed income, real estate and private equity to offset and lower overall portfolio beta.

Mr. Higgins reviewed the Domestic Equity Managers Comparative Performance provided each quarter by RVK, Inc. Comparative performance is shown for quarterly, annual, and for 1, 3, 5, 7 and 10-year periods, as well as inception to date. Gross and net of fees figures are included and performance compared to managers using similar strategies.

ADJOURNMENT

The meeting adjourned for the day at 4:01 PM.

CALL TO ORDER

Board Chairman Mark Noennig called the regular meeting of the Board of Investments (Board) to order at 8:00 AM. As noted above, a quorum of Board Members was present. Chairman Noennig called for public comment. There was no public comment.

FISCAL YEAR 2015 BUDGET

Executive Director David Ewer presented his budget memo. Each August staff presents the budget before the Board; the biennial budget is presented every other year. The budget contains many components.

- Operation costs are charged against the Board's seven investment pools and All Other Funds. The legislature sets the maximum amount allowed to be charged in House Bill 2; fees are paid through an Internal Service Fund. The amount for FY 2015 is $5,234,796. The Department of Commerce (Commerce) works with Board staff through the executive planning process to set the budget, and requires confirmation by the Board. The Budget Office structures the parameters according to current law to set the two-year budget. Commerce will complete the budget next week; no firm figures are available yet. Staff requests the Board authorize staff to work with the Department of Commerce to set the budget.
- The second major component of the budget is the Enterprise Fund, which funds the INTERCAP Bond Program. The program is voluntary for participants, as opposed to an internal service fund, which requires participants to pay operational charges.
- Custodial banking fees for depository banking are paid according to statutory authority granted by the legislature and are also charged against the Board's investment pools and All Other Funds.
- External investment manager fee payments are authorized by statute under the unified investment program.

Mr. Ewer presented the fiscal year 2015 operating budgets for both the Board's Internal Service Fund and the Enterprise Fund, shown in Table I and Table II, respectively. Both show the comparison to fiscal year 2014. Table IA breaks down investment research services, which are costly, but enables staff to parse data in useful ways.

Deputy Director Geri Burton stated there were no big changes in the 2015 budget over the prior year. Legal services increased and there were minor adjustments, but nothing out of the ordinary.

Senator Dave Lewis asked for clarification on the operation of the reserve fund.

Deputy Director Burton explained that internal service funds are allowed to keep a 60-day working capital balance for contingencies or to cover unexpected expenses. Board staff monitors the 60-day working capital balance to prevent overcharging for services, in which case no charge against the investment pools would be taken.

Executive Director Ewer asked the Board to approve the proposed FY 2015 budget amounts, (Staff Recommendation #1) as detailed in Tables I and II.

> Board Member Gary Buchanan made a Motion to approve staff Recommendation #1 approving the proposed FY 2015 budget for the Board of Investments and the Bond Program. Member Sheena Wilson seconded. The motion carried.

Executive Director Ewer asked the Board to authorize staff to work with the Department of Commerce to complete the 2016-2017 biennium budget, setting the maximum rate allowed to be charged, for submission to the Governor's Budget Office.

Board Member Sheena Wilson made a Motion to approve staff Recommendation #2. Member Marilyn Ryan seconded. The motion carried.

CONSULTANT REPORT

RVK, Inc. – Ms. Becky Gratsinger, CFA, Mr. Jim Voytko and Mr. Mark Higgins, CFA
Mr. Mark Higgins gave a market overview for the quarter ending June 30, 2014. Asset class returns were broadly positive for the quarter. Great returns over the last five years have been good for the portfolio. Positive events are affecting markets. Market perception is that the Federal Reserve will maintain its accommodative policy. Interest rates continue to go down. European Union data is not very comforting and the Russian skirmish with Ukraine is a concern. U.S. jobs increased at a rate of about 250,000 per month and the national unemployment rate is now 6%.

Negative geopolitical issues concerning Russia and the Ukraine, and Israel and the Gaza Strip continue. Generally, emerging markets rallied. U.S. equities are richly priced. The S&P 500 was up 5.25% for the quarter, the Russell 2000 lagged a bit and MSCI EAFE returned 4.09% for the quarter. The MBOI overweight in emerging markets has hurt the Montana International Investment Pool (MTIP). The Barclays US Aggregate Bond Index returned 2.05% and the MCREAF Odyssey Index core real estate returned 2.93%.

Member Jon Satre asked if there was concern about Asia or China.

Mr. Higgins noted without transparency, it is hard to predict. There was talk of a hard landing, as the inability to maintain the high growth rate was a concern, but that has lessened.

Mr. Higgins reviewed the comparative performance of the retirement plans. Fiscal year to date performance was strong, returning a 17.16%, exceeding actuarial rates comfortably by 10 percentage points. Returns produced a great dent in the funded status of plans, but the similar returns are not expected to continue over the next five years. Private equity and real estate lagged benchmarks for the quarter, but is attributable to the benchmark issue. Performance ranking is in the top quartile over three years and in the top half over seven years. The portfolio overweight in equities has helped performance.

Mr. Sheets added the most obvious extra return comes from domestic stocks vs. international stocks compared to peers. This has made a huge difference despite the emerging market allocation. Returns were good for real estate and private equity. The market bottomed in March 2009; performance over the last five years is as good as it gets.

Responding to a question from Member Jon Satre, Mr. Higgins stated it is hard to predict if and when a correction is coming. Mr. Sheets added the next five years will not be as good, but the fundamental climate suggests the economic expansion could continue. Corporate profits will be good and will drive the market. Growth has been slow throughout the world. Asset allocation must be looked at for the long term. The portfolio is very equity centric; if we have a 10% down quarter, we will feel it substantially.

Mr. Higgins stated the real factor is corporate profit margins; they are currently at an all-time high. Asset allocation is reviewed annually; a drastic cut in U.S. equity is not recommended. Risk adjusted returns look solid and of the asset class pools, domestic equity had absolute returns of 25% for the year, very positive. Relative performance and tracking error are also improving. MTIP has more emerging markets than peers, but should be attractive going forward. RFBP and TFBP look good over the long term. The real estate portfolio added 10.57% over three years and is a good diversifier. Private equity looks good over all time periods.

Mr. Higgins reviewed the comparative performance of the domestic equity managers. Analytic Investors is a concern and has struggled. Two managers, Nicholas and Iridian have had exceptional returns since inception, and although welcome, they are unlikely to continue at that level. Artisan has had some difficulty lately, but still looks good over the long term.

Mr. Higgins reviewed international equity managers. Alliance Bernstein has been on the watch list for an extended period. Many clients have terminated them, and we have discussed possibly terminating as well. Their bet on a big recovery has not paid off and they have lost key personnel in the last two to three years.

Mr. Sheets and Mr. Rande Muffick noted discussions are ongoing as to the best approach with Alliance Bernstein.

Mr. Higgins reported Hansberger did improve in 2013, but has underperformed calendar year-to-date and they remain on the watch list. Madison Asset Management acquired Hansberger and there is always concern when these types of changes occur. The current team is good and they have shown improvement. Martin Currie was added to the watch list due to performance and the recent acquisition by Legg Mason. The regulation issues they had with China have been resolved.

Mr. Higgins stated the international portfolio performance is disappointing year to date; tracking has tightened. The fixed income external managers are performing well. Reams looks good over the long term, but has suffered over the short term. Post Advisors underwent management changes and personnel departures, but is coming back and turnover is winding down.

INVESTMENT ACTIVITIES/REPORTS

Retirement Systems Asset Allocation Report

Mr. Cliff Sheets presented the asset allocation reports for the asset classes of the nine pension funds for the quarter and fiscal year ending June 30, 2014. The quarter was very positive with a 3.9% return and all pools had positive returns. Assets increased by $300 million for the quarter, net of distributions and the quarter-end portfolio value was $9.8 billion. Asset allocation weights were generally unchanged, except for a decrease in private equity from 11.8% to 10.5%, due to the $138 million secondary sale and a reduction of excess liquidity held in the pool; however, strong returns of 4.7% for the quarter lessened the impact.

Total equity fell from 68.1% to 67.5%, with a 0.5% increase in domestic equity and a 0.3% increase in international equity. Fixed income returned 2.1% for the quarter. Purchases of $28 million added to fixed income for the quarter helped to keep within the policy range of 22% – 30%, but strong equity performance continues to have a dilution effect. Subsequent to 9/30/14, an additional $47 million has been added to the fixed income pool. The real estate allocation was down slightly for the quarter to 8.7% and returned 2.9% for the quarter. STIP cash levels increased due to net sales for the quarter.

Member Jon Satre asked if the allocation target for private equity was around 11% - 12%.

Mr. Sheets stated it is a challenge to stay within ranges for private equity, as there is no control over the timing and magnitude of capital calls; however, the goal is to stay within the policy range of 9%-15%. The choice to conduct the secondary sale was due to the unique favorable market conditions allowing the pruning of certain holdings at optimal valuations. Mr. Hurley gets credit for the success of the secondary sale. A stock correction could easily see a jump up the private equity allocation by half a percent given the effect on the denominator, or total portfolio value.

Executive Director Ewer added staff uses a disciplined approach to stay within the asset ranges according to policy and recently cash was moved into fixed income to increase the allocation in order to stay within the required range. Fixed income plays a critical role, and while not expected to be a big winner, it is important to keep the allocation within its range.

Mr. Sheets reviewed the asset allocation reports for the fiscal year. The net increase in market value for pension assets was about $1.29 billion for the year, driven by market conditions. Even fixed income saw a 5% return for the year. The total equity allocation increased very slightly to 67.5% (from 67.4%). Total return for the year was 17.17%. There were significant sales of domestic equities and private equity. International equities increased to 17.8% from 16.6%; private equity allocation decreased 2% due to the secondary sale, but returned 16.5% for the year. Fixed income allocation fell slightly to 21.7% but still realized a return of 5.2%. Real estate allocation fell to 8.7% from 9.2% due to relative returns.

Senator Lewis asked if the net new investment balance reflects a withdrawal of $152 million, and where the cash went.

Mr. Sheets explained the net sale of $152 million out of the long-term asset pools acted to increase STIP as well as partially used to pay benefits. This use was necessary given the net negative cash flow of the plans.

Mr. Sheets then reviewed asset allocation as compared to peers in a custom peer group compiled by State Street. Compared to the median, MBOI is a little higher than median in domestic equities, slightly lower for international equities, fixed income is right at the median and cash is below the median. Real estate is above the median, and private equity is very close to the median.

In comparing pension performance to the same State Street peer group, the absolute returns have been very high over five years and relative performance has improved over the 5, 7 and 10-year periods compared to the median.

Representative Kelly McCarthy asked if the cash flow figures are characteristic of an aging, maturing pension plan.

Mr. Sheets responded it is natural to see a benefit-related net cash outflow over time as the number of retirees grows, although he was not sure how we compare to other plans. Cash outflows depend on the maturity of the plan. Mr. Higgins added aging plans are a national trend and many plans are in similar situations, but it varies from plan to plan. Mr. Sheets stated the annual asset allocation review will occur at the November Board meeting, including a detailed cash flow analysis.

<u>Montana Domestic Equity Pool (MDEP)</u>

Mr. Rande Muffick reported on the Montana Domestic Equity Pool (MDEP) for the quarter ending June 30, 2014. Domestic equity returns are good; through today, the S&P 500 is up 7.25% year to date. Economic momentum continues and market volatility is below normal. The quarter saw some shifting between cap sizes; in the second quarter, small caps sold off. The market is climbing back again; but higher stock market levels mean some sort of correction is more likely as the market has been due for a correction for a while. Global geopolitical concerns and financial stress issues can cause problems. China is a very closed system with slowing growth. The largest risk for a market correction is inflation data - inflation is starting to rise and if markets sense the Fed is behind the curve on the raising of interest rates then this would not be good for stock prices. A gradual increase in inflation is good; it means the economy is picking up.

Mr. Muffick reviewed activity for the quarter. The 130/30 managers are bumping up against the top of the range ceiling; JP Morgan will be trimmed a bit. Domestic Pool small cap positions have been pared back a bit, but they have been overweight for some time. If interest rates increase, small caps may struggle.

Managers struggled a bit over the quarter; the relative performance of the pool is about 20 basis below the benchmark. Growth managers are still seeing relative performance gains but value managers are struggling. Performance of all cap sizes has been consistent for 12 months with robust 20% returns for all market caps. The two new midcap managers have done really well since they have been on board. Long-term small caps will be pared back more as well as the 130/30's, depending on their weight vs. the policy range.

Montana International Equity Pool (MTIP)
Mr. Muffick reported on the Montana International Equity Pool (MTIP). International markets have performed in line with the U.S. market overall. There was a brief correction, but small caps did not dip as much as in the U.S. Structural rigidity in Europe complicates things. Emerging markets are attractive on a valuation basis and have had difficulties as of late, but realized double-digit returns for the quarter. An overweight in emerging markets has helped the pool; going forward they should generally follow the U.S. stock market.

Thus far, the overweight in domestic equities has worked to our favor. Although international markets are looking cheaper, over the long term the advantage is with U.S equity.

There is no question the external managers have struggled, but the restructuring should help. Both new small cap managers, American Century and Templeton, have done well since hired last spring.

Public Equity External Manager Watch List
Mr. Muffick reported the addition of Martin Currie to the watch list this quarter. The underperformance for Alliance Bernstein is cyclical and should improve with rising interest rates, as long as rates do not rise too quickly. It will be disappointing if they show no improvement over the next 6 to 9 months. Both growth managers, Hansberger and Martin Currie, have suffered and both have undergone ownership changes. Martin Currie lost a lot of assets and has had regulatory issues. Any change in ownership is always an issue and so warrants inclusion on the watch list.

Responding to a question from Member Prothero, Mr. Muffick stated there is no set time limit for improved performance for the three managers, but Staff continues to monitor them closely.

Responding to Board member questions, Mr. Muffick stated managers must provide notification in the event of being acquired and receive consent under our contract to go ahead with an acquisition. RVK provides a write up when entities change ownership. If a manager is terminated, transition costs are incurred and a transition manager is used. Mr. Higgins added managers are monitored closely and personnel changes are scrutinized.

PUBLIC EQUITIES MANAGER WATCH LIST
August 2014

Manager	Style Bucket	Reason	$ Invested (mil)	Inclusion Date
Alliance Bernstein	International – LC Value	Performance	$118.7	August 2012
Hansberger	International – LC Growth	Performance, Ownership Change	$121.4	May 2013
Martin Currie	International – LC Growth	Performance, Ownership Change	$120.8	August 2014

Montana Private Equity Pool (MPEP)
Mr. Ethan Hurley presented the Montana Private Equity Pool report for the quarter ending March 31, 2014. Net positive cash flows continue for the pool. There were four new commitments since the last Board meeting (shown in the table below). The portfolio is well diversified by strategy with the largest exposure in buyouts. Industry exposure is spread mostly across the five main industry sectors. Geographic exposure is focused on North America, which has the deepest and most liquid private equity market in the world. Pool exposure is mostly in direct investments. Fund of funds will continue to decline. The overall portfolio has an IRR of 12.73%, net of all fees, since inception, which is 500

basis points above the actuarial rate of return. Private equity has been a good diversifier in addition to providing a high level of return.

Member Jack Prothero asked if there were any new issues or concerns.
Mr. Hurley stated there are no new areas of concern, and just 11 out of 114 managers are reporting negative returns and some of those are due to the "J" curve effect.

Representative Kelly McCarthy asked for details of the private equity secondary sale.

Mr. Hurley stated eight partnerships, with a total net asset value as of 9/30/13 of $126 million, were sold. There were two different buyers. Transaction dates were April 7, May 12 and June 30 for net proceeds of approximately $120 million with transaction costs of roughly 60 basis points. The sale went well and most holdings sold at a premium with a blended price of 106% of NAV realized overall. A high level of detail was required for the transaction and Mr. Hurley and Mr. Sheets participated in weekly conference calls mapping out the procedures. Staff had not conducted a sale like this previously and it was a good learning experience. A lot of legal documentation was required and review of these required the use of specialty counsel. Three brokers visited on site and a good one was retained at a reasonable price. The broker fee is based on a set percentage of net asset value on the date of record.

Selling of contracts is legally intensive and takes staff time, as well as having accounting ramifications. The timing of the sale and market conditions were very favorable in staff's view.

Mr. Sheets stated funds were chosen based on a combination of factors, including those which would be readily received by the market, and managers we did not expect to re-up with.

The new commitments made since the last board meeting are shown in the table below:

Fund Name	Vintage	Subclass	Sector	Amount	Date
Kinderhook Capital Fund V, LP	2014	Buyout	Diversified	$20M	5/30/2014
The Catalyst Fund IV, Parallel Limited Partnership, LP	2014	Distressed	Diversified	$15M	5/30/2014
Guardian Capital Partners Fund II, LP	2014	Buyout	Diversified	$20M	6/9/2014
Veritas Capital Fund V, LP	2014	Buyout	Diversified	$20M	7/9/2014

<u>Montana Real Estate Pool (MTRP)</u>
Mr. Hurley presented the Montana Real Estate Pool report for the quarter ending March 31, 2014. Cash flows for the quarter were positive for the second quarter in a row for non-core funds. The portfolio is broadly diversified by strategy and geographic exposure, and is balanced by property type. The pool includes the Montana office buildings. The pool includes 10.4% of market value in foreign exposure. The time weighted return was generally positive with a net return of 2.5% for the quarter. The portfolio is conservatively leveraged and within policy restraints.

Staff made one commitment since the last Board meeting of $20 million to Harbert US Real Estate Fund V, LP, shown below.

Fund Name	Vintage	Subclass	Sector	Amount	Date
Harbert US Real Estate Fund V, LP	2012	Value Add	Diverse	$20M	5/22/2014

<u>Partnership Focus List</u>
There were no changes to the MPEP or MTRP Focus lists since the last Board Meeting.

Fixed Income

Mr. Nathan Sax presented the Fixed Income overview and strategy for the quarter ending June 30, 2014. The yield on the U.S. Treasury 10-year note dropped for the second quarter in a row. First quarter real GDP of -2.9% was revised to -2.1% and the initial report of second quarter GDP showed a strong rebound of 4.0%. Real GDP projections for calendar year 2014 are approximately 2%. The Fed is expected to conclude quantitative easing in October and the market expects they will begin to raise the Fed funds rate in 2015.

Corporate bond yield spreads are tight but have recently widened out a bit. Geopolitical events have had an effect. Unemployment figures have improved, although part-time employment rates went up. The current unemployment rate is 6%.

Mr. Sax reviewed the Retirement Funds Bond Pool (RFBP). The internally managed Core Internal Bond Portfolio (CIBP) makes up 75.34% of the pool. The (CIBP) has 18.1% in treasuries vs. 35.26% for the Barclays Aggregate Index. Reams has an overweight in treasuries at 50%, which has hurt their relative performance given a higher return from the spread sectors, combined with a short-of-benchmark duration. Aberdeen has bounced back and outperformed the index by 62 basis points over the three-year period. High yield manager Post Advisors ranked in the 10th percentile over the last three years and has done quite well overall. Portfolio allocation to high yield has helped relative performance.

There was one addition to the below investment grade investment list. PPL Energy Supply was downgraded to B after announcing a spin-off of its energy division.

Fixed Income External Managers Watch List

Post Advisors has remained on the watch list for the past year due to organization instability, although performance has been excellent. Larry Post left the company and the new CIO is Henry Chung. They have yet to hire a Chief Operating Officer. Reams Asset is a new addition to the watch list due to performance after four consecutive quarters of underperformance vs. the benchmark.

Short Term Investment Pool, State Fund Insurance & Treasurer's Fund Report

Mr. Rich Cooley gave an overview of the Short Term Investment Pool (STIP) for the quarter ending June 30, 2014 and reported there was not much change over last quarter. The Fed funds rate remains 0 – 25 basis points; unchanged for the past five and a half years. There is speculation the Fed may start to raise rates in mid-2015 if the economy is on steady footing. How much rates will rise remains a question. There were no real changes in levels of investments or spreads. The STIP balance at quarter end was $2.5 billion, down $100 million from three months ago.

Purchases over the quarter included $80 million of floating rate corporate notes, $25 million in fixed rate Yankee CDs, $25 million in floating rate Yankee CDs and $25 million of fixed rate agencies.

The STIP portfolio is within all policy guidelines for liquidity, diversification and average days to maturity, currently 57 days, compared to the policy maximum of 60 days. The STIP current net yield is just under 11 basis points, compared to the benchmark one month LIBOR rate of 15 basis points. The difference is due largely to the ongoing daily deposits to the reserve fund. Current deposits to the reserve fund total $11,000 per day, or $4 million per year.

Executive Director Ewer added it is not staff's intent to deplete the reserve fund to pay down the legacy assets from the structured investment vehicles (SIV), as we are still receiving payments on those investments. Policy dictates a reserve fund be maintained which acts as a contingency to guard against future potential losses.

Mr. Cooley reviewed the Treasurer's Fund for the quarter ending June 30, 2014. There were purchases of $30 million in securities for the quarter with a maximum maturity of three years. The short end of the curve steepened up a bit so longer term securities were picked up to add yield.

Mr. Cooley presented an overview of the State Fund Insurance portfolio for the quarter ending June 30, 2014. Spreads tightened and interest rates continued to drop. The 10-year Treasury yield decreased by 19 points from 2.72% to 2.53% for the quarter. Total fixed income holdings outperformed the benchmark by 5 basis points during the quarter and by 71 basis points over one year. Long-term returns compared to the fixed income benchmark were +94 basis points for three years, +137 basis points over five years, and +49 basis points for the ten years ending June 30, 2014. Equities and real estate continue to add substantial return to the portfolio.

RECAP

Executive Director Ewer asked Board members for any "to do" items for the next Board meeting. There were none.

Being no further business, the meeting was adjourned at 12:16 PM.

Next Meeting
The next regular meeting of the Board will be October 7, 2014 in Helena, Montana.

Complete copies of all reports presented to the Board are on file with the Board of Investments.

BOARD OF INVESTMENTS

APPROVE: Mark E. Noennig
Mark E. Noennig, Chairman

ATTEST: David Ewer
David Ewer, Executive Director

DATE: November 18, 2014

MBOI:drc
9/29/14