These minutes are Approved and Final. Full Board review and decision took place at the May 24 & 25, 2016 Regular Meeting of the Board.

MONTANA BOARD OF INVESTMENTS
DEPARTMENT OF COMMERCE
2401 Colonial Drive, 3rd Floor
Helena, Montana
MINUTES OF THE MEETING – February 23, 2016

BOARD MEMBERS PRESENT:
Mark Noennig, Chairman
Karl Englund, Vice Chairman
Kathy Bessette
Terry Cohea
Quinton Nyman
Jack Prothero
Marilyn Ryan
Jon Satre
Sheena Wilson

LEGISLATIVE LIAISONS PRESENT:
Representative Kelly McCarthy
Senator Bob Keenan

STAFF PRESENT:
Polly Boutin, Associate Financial Manager
Jason Brent, CFA, Alternative Investments Analyst
Geri Burton, Deputy Director
Dana Chapman, Board Secretary
Frank Cornwell, CPA, Associate Financial Manager
Craig Coulter, Alternative Investments Analyst
Joseph M. Cullen, CFA, CAIA, FRM Chief Investment Officer
Roberta Diaz, Investment Accountant
David Ewer, Executive Director
Julie Feldman, CPA, Financial Manager
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, CIPM, Investment Data Analyst
Tammy Lindgren, Investment Accountant
April Madden, Investment Accountant
Rande Muffick, CFA, Portfolio Manager, Public Equities
Mary Noack, Network Administrator
Kelsey Poore, CPA, Investment Accountant
Jon Putnam, CFA, FRM, CAIA, Fixed Income Investment Analyst
John Romasko, CFA, Fixed Income Investment Analyst
Nathan Sax, CFA, Portfolio Manager, Fixed Income
Steve Strong, Equity Investment Analyst
Louise Welsh, Senior Bond Program Officer
Dan Zarling, CFA, Director of Research

GUESTS:
Meg O'Leary, Executive Director, Department of Commerce
Jim Voytko, RVK, Inc.
Mark Higgins, CFA, RVK, Inc.
Leah Tietz, Montana University System, Workers' Comp
Herb Kulow, CMB, Portfolio Manager, In-State Loan Program (Contracted)

CALL TO ORDER
Board Chairman Mark Noennig called the regular meeting of the Board of Investments (Board) to order at 11:33 a.m. As noted above, a quorum of Board Members was present. Chairman Noennig advised video recording of the meeting was underway and called for public comment. There was none. Chairman Noennig called for comments or revisions to the November 17-18, 2015 Board Meeting Minutes.

Member Jon Satre made a motion to accept the November 17-18, 2015 Board Meeting Minutes as presented. Member Marilyn Ryan seconded the motion. The motion carried.

ADMINISTRATIVE BUSINESS

Audit Committee Report

The Audit Committee met prior to the Board meeting. Committee Chairman Jon Satre noted most Board members were present at the meeting. Staff reported on the FY 2015 Financial Audit which has been presented to the Legislative Audit Committee. BOI had a clean report. The Committee reviewed the FY2016 Risk Assessment Model and Internal Control Testing Schedule and the proposed revisions to the Internal Controls Policy. These documents were approved by the Committee as recommended by staff.

The 2016 financial compliance audit by the Legislative Auditors is set to begin in the spring. The audit determines BOI compliance with statutes. The Committee reviewed staff changes. Jon Putnam is the new internal manager of Montana State Fund and John Romasko is the new Short Term Investment Pool (STIP) manager. Chairman Satre thanked staff for stepping into their new roles.

Committee Chairman Satre noted the revisions to the Internal Controls Policy addressed recent changes to STIP, minor changes to the In-State Loan Program and changes to INTERCAP wiring documents. The Committee reviewed and approved all staff recommended changes.

> Committee Chairman Satre moved to approve the changes to the Internal Control Policy as presented by staff. Member Sheena Wilson seconded the motion. There was no discussion. The motion carried.

Chairman Satre stated the Committee reviewed the 2016 Audit Checklist and noted not many items have been checked off yet as the meeting was the first one of the year.

Human Resource Committee Report

The Human Resource Committee met prior to the Board meeting. Committee Chairman Karl Englund noted all Board members were present. The Committee discussed proposed changes to the organization structure of investment staff as proposed by Chief Investment Officer Joe Cullen and Executive Director Ewer. The proposed changes were reviewed in detail; all proposed changes regarding new functional roles and reporting responsibilities have been discussed with staff. The changes realign staff duties and in some cases, staff supervisor reporting. The proposed changes will require revisions to the organizational chart, which the Board will need to approve. The new organizational chart will be presented for approval by the Board at the April meeting. All changes were vetted in detail by the Committee and met with general approval.

Loan Committee Report

The Loan Committee met prior to the Board meeting. Committee Chairman Jack Prothero stated the Committee had several loans to approve. The first loan presented by contract employee Mr. Herb Kulow includes an equipment loan and a real estate loan. The equipment loan to primary borrower Kettlehouse Brewing Company, LLC, is for brewery equipment for a brewing facility in Bonner. The total equipment loan amount is $2,849,000; BOI's 77% BOI participation amount is $2,193,730. The real estate loan to primary borrower K3, LLC, a real estate holding company of Kettlehouse Brewing, will be used to construct a brewing manufacturing facility. The total real estate loan is $3,291,000; BOI's loan participation of 77% is for $2,534,070. Both loans are guaranteed by the borrowers. The BOI total combined loan amount for the two loans is slightly under $5 million. The Loan Committee approved both loans.

The second loan presented to the Committee is a bond purchase from the Department of Natural Resources and Conservation (DNRC) to fund water projects. The loan term is 20 years at 4% interest rate for $2,573,976. The loan was approved by the Committee. BOI has an ongoing relationship with DNRC.

The Committee approved three INTERCAP loan requests. The first was a $1,205,000 loan to the City of Harlem, a bond anticipation note (BAN) in anticipation of USDA Rural Development Services (RD) long term financing when the project is completed. The loan will be used for wastewater system improvement projects in Harlem. Chairman Prothero requested that staff expand on the interim financing process at the next Loan Committee Meeting.

The Committee also approved a loan for $1,663,809 to the Board of Regents on behalf of the University of Montana - Missoula. The campus is purchasing two new energy efficient buses. The Committee also approved a University of Montana - Missoula loan through the Board of Regents for $1 million to finish the Adams Center basement and a loan for $1,089,300 for a Montana Tech project in Butte to remodel the chemistry building.

The Committee also approved two policy changes for the In-State Loan Program, which requires full Board approval. The first is a change in the Veteran's Home Loan Policy, which increases the stated policy insurance deductible from $1,000 to the current industry standard of $1,500, thereby bringing the policy into compliance with industry standards.

> Chairman Jack Prothero made a motion to approve the VA Loan Policy revisions. Member Terry Cohea seconded the motion. The motion carried.

The second policy considered by the Committee is a revision in the Commercial Loan Policy. The Policy contained a ceiling limit on hotels as a portion of the Permanent Coal Trust Fund (Perm Coal); however, the Perm Coal has increased and BOI has not increased loans to hotels/motels; therefore, the policy restriction no longer applies. Staff is requesting Board approval to remove the policy restriction. The current hotel/motel concentration of the loan portfolio is well under the limit.

> Chairman Prothero made a motion to approve the revision to the Commercial Loan Policy. Member Cohea seconded the motion. The motion carried.

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

PERS Representative Sheena Wilson reported MPERA held a meeting with the Employee Investment Advisory Council, which Mr. Tim House participated in. The goal is to engage employees and human resource people as a tool for recruitment. The PERS CAFR (Comprehensive Annual Financial Report) is complete and a new actuary, Cavanaugh Macdonald Consulting, LLC, has been selected to replace the prior actuary, which dropped out due to non-compliance in the RFP process. The computer system project continues to move along and a go live date is anticipated by May for the employer section of the system. Member Wilson presented a retirement benefit summary detailing benefits received around the state. Yellowstone County receives $41 million per year, which is not surprising; however, even Petroleum County, with a population of less than 500 people, receives PERS benefits totaling $200,000 per year. Member Wilson added it is useful to see how important BOI is for the flow of benefit money when examining the retirement benefits paid over one year.

TRS Representative Marilyn Ryan reported the TRS Board met on December 3; she participated by phone. One staff change was reported. IT manager Rick Bush has retired and has been replaced by John Noble, who worked as the IT manager in the Governor's office since 2006. Kristen Williams was also added to staff. The TRS privacy and security information policy has been revised. Other state agencies offer education reimbursement when the education is relevant to employment; TRS has approved a reimbursement for staff modeled after other state agencies. Drake Law Firm has been hired to handle contested cases. A problem area with the University System occurred where a retiree started working at Helena College, and when changing jobs, TRS was not notified; therefore, the individual was not contributing to TRS as required by law. This has occurred with other university systems in the state as people change positions, without the understanding that retirees are on different systems, with full salary and benefits. The problem was identified and corrected with a positive resolution. New procedures have been implemented which address occasions when retirees join the staff of universities.

Legislative Liaison Comments

Senator Bob Keenan had nothing to report.

Representative Kelly McCarthy reported on a couple of items. The state's bureau of economics presented its findings a couple of weeks ago in Billings. The price of oil is down, and gas and coal are depressed; beef and wheat are down; however, there is no area in the state that is not still growing. The reason is that 20 years ago a lot was done to diversify the Montana economy, and it is paying off. In the past, manufacturing growth had more of an impact; however, now Montana has a more diversified economy. One impact on the economy is the lack of work force talent, and as baby boomers retire, it is a struggle to replace them. The solutions include a more creative approach to the work force, with a more creative approach to building talent. The state of North Dakota will pay businesses to up to $3,000 to bring in interns; Montana is now competing with its neighbors for talent. The production taxes gained by the state from oil and gas comprise only 2% of the state's budget. For Alaska, that figure is 95%; however, Montana remains the number one financially healthy state.

EXECUTIVE DIRECTOR'S REPORT

Overall Comments

Executive Director Ewer presented his report and reviewed the two member requests from the last meeting. First, the Board asked that private equity and real estate policy guidelines, including leverage constraints, be included in the quarterly reports. Mr. Ethan Hurley has included these. The second item, Member Sheena Wilson provided input on the revisions to the Annual Report.

Director Ewer presented the quarterly cost report, and the monthly pension snapshot, which the Board receives monthly via email.

Director Ewer reviewed the Ethics Policy. Staff is required to sign the Policy annually, as a condition of employment. All staff have signed and turned in the Policy for this year. Director Ewer strongly urged all Board members to sign the Policy signature page and return it.

Director Ewer provided an update on the FY 2015 Annual Report and Financial Statements. BOI received a clean FY15 Legislative Audit report; there were no recommendations for either the Internal Service Fund or the Enterprise Fund Financial Statements. Staff reported to the Legislative Audit Committee.

Director Ewer presented his memo on emergency preparedness and disaster recovery, which is an item on the Systematic Work and Education Plan. In its fifth year, the Work Plan goal is to bring every material matter before the Board. All computer and communication systems are backed up regularly and staff is in the process of researching surveillance camera options for the parking lot and common areas in the building.

Member Satre stated BOI monitors and has procedures in place for the onsite computer systems, and asked whether other associated entities, such as State Street Bank, provide information about their systems, in the event they go offline.

Executive Director Ewer acknowledged it would be a problem and one way the scenario is addressed is in the qualifications required through the custodial bank RFP process. Certification of backup systems and redundancies are stipulated in the RFP. BOI staff have visited on site, although not recently. State Street has a mission control center located at an offsite facility and the site is vetted.

Deputy Director Geri Burton added the SSAE 16 Report (Statement on Standards for Attestation Engagements) is received annually.

Executive Director Ewer added State Street has a requirement that BOI meets due diligence.

Julie Feldman added auditors visit State Street each year. The SAS 70 Audit has been replaced by the SSAE 16 Report, which is utilized to report on internal controls for providers. BOI reviews it annually to ensure all requirements are met, and to verify our controls are working and that a written report is prepared and submitted to the auditors.

Mr. Jim Voytko added if you look at technical failures over the last 5 or 7 years, there is a chain of technologies, which are subject to failure, exchanges and telecom networks that link to BOI. The key is to avoid having investments that would put you in a terrible bind if you were offline for 24 or 48 hours. Reviewing tech and service audits are the best you can do. The question is more whether your infrastructure is heavily redundant, so you avoid reliance on service monitors. RVK also has a recovery plan, which is viewable on request; the plan also includes off site locations.

Director Ewer noted BOI staff has met with State Street, US Bank and Department of Administration personnel, and the group meets annually to review emergency preparedness. If access to the Colonial Building is not possible, major systems are able to keep functioning. BOI staff has special tokens, which allow access to systems at a remote site; this would enable the flow of money to keep paying state bills.

Director Ewer reviewed staff outreach for 2015 and thanked staff who participated in outreach to connect with the public, out in the field, and attending conferences.

Director Ewer provided an update on the STIP participation protocol. The packets have been sent with the Resolutions and associated attached exhibits. All local government participants are required to complete the Resolution and return to BOI by the June 30 deadline. STIP participants understand the importance of having a good process in place.

Director Ewer advised there was an investment loss charged to the STIP Reserve fund. Per policy, any charges to the STIP Reserve require notification to the Board. The investment purchased from an approved name; however, the actual security purchased was not of sufficient credit rating and therefore was not within policy. Policy requires staff act on such an item, and the security was sold. Interest rates were against the sale, resulting in an $80,000 charge to the Reserve. There was no effect on portfolio yield; however, the Reserve was reduced by $80,000. As a result, staff has tightened procedures to avoid future potential losses.

Member Karl Englund asked if there was a failure at time of purchase.

Chief Investment Officer Joe Cullen stated the issue was due in part to the analytical trading system that checks securities; the particular rule was not coded into the system correctly and the error was caught in the review of the portfolio when compared to policy statements. Moving forward, staff will closely review methods to comply with policy statements.

MONTANA LOAN PROGRAMS

In-State Loan Program

Mr. Herb Kulow presented the residential and commercial loan portfolios. The commercial loan portfolio balance was $110,625,265 at the end of January, a slight increase after deducting $549,641 representing other real estate for the Vann's loan in Lolo. The lease purchase option expired in mid-January; however, it was extended to March, which is a good sign and the tenant has done property improvements. The portfolio total includes 104 loans and there is almost $60 million in the pipeline. The portfolio yield is 3.79% and six loans are past due, 8.09% of the portfolio, due to Shoot the Moon, LLC and Purdy-Hatzenbeller Investments. The bankruptcy process is in motion; staff expects a loss of $250,000 to $350,000.

The residential loan portfolio has a balance of $8,281,450 as of January 31 with five loans over 90 days past due totaling $300,459 or 3.63% of the portfolio; four of those are FHA guaranteed. The Veterans Home Loan Program is seeing increases; the portfolio balance was $30,233,183 at the end of January with five outstanding reservations for $808,230. One loan is past due more than 90 days; a demand letter was sent and the loan was brought current. There are no conventional loans in the VA program, all are guaranteed by VA, FHA or by the HUD 184 program, which is an American Indian and Alaska native program; however we have had no requests for the HUD 184.

CONSULTANT REPORT

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

Mr. Higgins noted the quarterly report is a little different this time, providing an overview of capital markets and a snapshot with the executive summary. The 4th quarter was generally positive for risk assets, although January and February were difficult for risk assets compared to quarter end, so comments will include some of the more recent activity.

There were three main factors driving markets:

1. China growth expectations have been a core driver with broad impact; with commodities, iron and copper all showing weakness. Emerging markets have suffered for five years, as well as developed markets; for example, Apple showed weakness in China.

Mr. Voytko added that looking at China, every estimate of GDP or manufacturing, all estimates are lower than the government's, which shows a lack of credibility for the Chinese government. Exports and imports are declining. There is a general lack of faith in government.

Mr. Higgins continued:

2. Oil prices have seen some stability, but have realized a very substantial decline of about 70% since mid-2014. OPEC and Russia are coming together; there is more supply than demand, which causes repercussions in other parts of the economy. High yield debt markets are suffering as is the U.S. stock market. Hopefully, oil has hit its low point and there is some stability now.
3. Many feel the Federal Reserve hike was premature and looking ahead to other expected hikes in 2016, there is a lot of skepticism questioning whether the Fed acted correctly. The Fed could point to indicators; however, it does not feel like the beginning of a tightening cycle. Although unemployment is low, inflation is weak in the 1% range. There are a lot of factors the Fed should have considered; a flight from risk assets ensued.

Mr. Higgins stated going forward, oil prices and Fed policy are both risks. The BOI plans are very well allocated and diversified, and private equity and real estate in particular have helped. This storm will pass.

Mr. Voytko noted the expected returns across all capital markets, the $6 trillion worth of sovereign bonds, such as Germany and Japan, have not been realized in capital markets. The ugliest are energy, high yield and emerging markets, which have taken a big hit, and fixed income has suffered, while equity GDP growth continues to be depressed. For example, Brazil is very challenging on the equity side. Earnings per share are declining moderately and declining prices in risk assets have caused the market recalibration to the current circumstances. When Japan announced negative interest rates, not much happened. It will be a tough year ahead. When BOI entered into real estate, it was painful, but it is now paying off, helping to lower equity beta, with the added advantage of being slightly less sensitive to the stock market decline.

Mr. Higgins presented the Executive Summary. The total fund performance as represented by PERS through December 31 shows a 2% return, something we are not accustomed to. On a relative basis, the portfolio has performed well and continues to rank in the top decile over the last year; and for annualized periods Montana ranks in the top decile over peers, all the way back to the 10-year period.

Mr. Voytko added when the Board recalibrated years ago, there were fundamental changes implemented. It takes a long time to chart a new heading, but over the last seven years, it is not a trivial change. The outstanding peer ranking has been sustained over a very long time.

Mr. Higgins noted some other highlights include the continued improvement in MDEP and MTIP with very good progress and strength over the last three to five years. The RFBP underperformed a bit, as did the fixed income composite in general due to riskier assets in the portfolio; high yield in particular has suffered. However, performance is still well above the median. The private equity pool in a raging bull market will trail the indexes. The relative index returns, plus the 4%, finally experienced a period where private equity performed significantly better, compared to the public markets.

Mr. Voytko added when public markets do well, private equity lags, and when public markets flatten or go down, private equity shows an over performance, as it has recently.

Mr. Higgins noted seven years ago, it was painful to initiate private equity, but it has paid off and we are now seeing the benefits.

INVESTMENT ACTIVITIES/REPORTS

Retirement System Asset Allocation Report

Mr. Joe Cullen stated staff will provide detailed updates, however, there are some changes in the reporting and staff expects there will be some additional adjustments over the next few meetings. Additionally, there will be a few different staff members presenting. Jon Putnam is taking over State Fund and John Romasko has taken over the STIP portfolio.

Mr. Cullen reviewed asset allocation for the retirement systems. For the quarter ending December 31, all assets remained within policies, although two plans dropped slightly below on cash at year-end. Cash historically held at the pension levels is usually between 1-5%. Staff will continue to report on cash, but will also implement increased transparency on cash levels. At the end of December, about 2% of the total pension plans were in cash, which provides the liquidity needed to make benefit payments. Pension assets increased $224 million over the quarter due to appreciation on the equity side at year-end. Net distributions totaled about $76 million for benefits to beneficiaries, about $32.5 million was made up of dividends and interest payments, as well as sales and rebalancing of other asset classes. Total net distribution for the year ending December 31 was $231 million, of which $132.5 million was funded by dividends and interest payments. All plans are well diversified and within policy.

Member Jack Prothero asked when looking with fresh eyes, did Mr. Cullen see anything surprising when looking over the plans from risk standpoint.

Mr. Cullen responded, no, nothing surprising, but with markets you must be prepared for surprises and expect the unexpected. Things have worked well with a well-diversified portfolio and the portfolio has been positioned well. Staff will continue to look at process and allocation moving forward.

Member Satre asked how the decisions are made as to where the proceeds will come from to make disbursements.

Mr. Cullen stated when benefit payment amounts are determined, staff looks first to dividends and interest, and any remaining funds needed are generated from sales of assets above and beyond that amount. Current allocations relative to policy are reviewed or any areas where staff may want to move allocations to. If an asset is at the high end of its range, it may be a candidate to reduce and provide sales. With the recent run up of equities, most benefit payments have been funded through sales of equities; however, that could change going forward. Staff considers total dollar amount, where the allocations are and what the desired target allocation is going forward; it is an ongoing process.

Internal Fixed Income

Mr. John Romasko reported big doings in STIP with the Federal Reserve increase; LIBOR rates mirror that, and the TED spread also went up dramatically in the quarter. STIP holdings are all within policy ranges with liquidity well above minimums during the quarter. Staff made purchases of floating rate securities and Yankee CDs over the quarter and sold a $20 million piece of Bank of America. The largest holders in STIP include the Treasurers Fund as the largest and some municipalities are large holders. Municipalities are voluntary participants, whereas state agencies are required to participate in STIP.

Member Satre asked if the percent of municipalities has changed over the last year.

Mr. Romasko stated yes, municipalities utilizing STIP hit a high at year-end near 30% of the total, which is as high as it has gone. The increase in yield made STIP more attractive, and therefore more entities are investing.

Mr. Romasko compared STIP vs. peers vs. the benchmark, adding the comparison uses the BOI net while peers include total returns. The BOI STIP reserve fund costs about 12 basis points and administrative fees cost another four basis points, producing a net yield of 35 basis points at quarter end. The yield is below the LIBOR rate yield of 43 basis points at quarter end; the biggest reason is the STIP average maturity of 35 days. Historically, STIP has been short and conservative and yields recently have gone well above LIBOR. The STIP Reserve fund balance was $30.5 million, compared to $29.5 million last quarter. The SIVs were down just over $1 million for the quarter.

Mr. Nathan Sax presented internal fixed income management and noted that Mr. Rande Muffick will cover fixed income managed externally. The Federal Reserve increased rates on December 16 from 0-25 basis points to a 25-50 basis points range, and indicated it may raise rates four more times over the upcoming calendar year. The expectation is the Fed will raise rates once or twice more over the next 9-10 months. For 2015, GDP remained about the same as 2014 and the prior two years. The real rate of return is roughly 2% to 2.5%, over the last few years, which looks good relative to the rest of the world, and the dollar is strong, compared to other currencies. Consumers increased their savings, rather than spending, and they are remaining cautious, which has an effect on how fast the economy grows. Reviewing high yield, spreads have gotten wider since mid-2014, which is an indicator of risk and how much investors want to be compensated for risk. High yield spreads tightened significantly in February and March of 2016. Commodities have been declining, and economic development around the world has been declining. Commodity prices did improve, however, also in February/March of this year. The Fed is cognizant of the slowness of economic growth, and knows if rates are raised too soon or too high, growth may slow.

Mr. Sax noted defaults are expected to rise, due in large part to energy. A lot of managers are loath to hold metals, mining, or oil pipelines, etc.

Representative McCarthy asked if we are starting to see defaults.

Mr. Cullen stated there will always defaults, and they are expected to increase; the question on a default is whether you will receive any recovery.

Mr. Sax added that default rates are tracked.

Mr. Voytko stated while you can determine what default rates have been, that does not translate into what default rates are expected to be going forward.

Mr. Cullen added it depends largely on sectors. If the approach of high yield is across sectors and spreads over the longer term, it provides decent risk adjusted returns, net of any defaults.

Mr. Sax noted default and recovery rates are tracked; recovery was at 40 cents on the dollar, however it has declined down to about 30 cents.

Mr. Cullen added more discussion of high yield will occur at the April Board meeting.

Mr. Sax explained staff considers quality and liquidity, and is staying away from smaller issues and less credit worthy bonds and illiquid bonds. While giving up some yield, the approach is to stay more conservative. At year-end 2015, relative performance in the CIBP and TFBP suffered in the fourth quarter because of holdings in certain utilities, including Talen Energy, a spinoff of Pennsylvania Power and Light. Staff believes they will pay off at maturity and therefore are not selling out of it.

The Barclays Aggregate Index returned 452 basis points for 10 years and 144 basis points over three years. However, the returns enjoyed five years ago are not expected to continue over the long term; however, 2016 is off to a good start. The effective duration for the pools is only slightly longer than the index, which has helped over time; the yield to maturity is 276 basis points vs. 253 basis points for the index, a modest yield advantage of about 25 basis points. Treasuries, agencies and mortgages are all underweight compared to the index, and BOI is overweight in corporate bonds and asset backed securities. For credit quality, the portfolio is slightly overweight BBB corporate bonds, single A's are even with the index, AA's are overweight and AAA are about 90% of the index weight. The portfolio emphasizes high quality and high liquidity.

Mr. Sax reviewed below Investment grade holdings. Utilities have dropped to the BB level; Teck Resources is a small weight in the TFBP and Talen energy, a larger weighted security which PA Power and Light spun off, sold to a private equity company, which prompted the bond price to move down. Staff expects them to pay off.

Member Jack Prothero asked if Lehman Brothers is expected to pay off.

Mr. Sax responded it will conclude at some point; however, it could take years. It is the largest bankruptcy in U.S. history.

Executive Director Ewer asked if Lehman Brothers is booked at zero and has been written down.

Mr. Jon Putnam stated yes it has been written down.

Director Ewer noted any dollar received back to BOI is recovery.

MUS Workers Compensation – Investment Policy Statement

Mr. Sax presented the new investment policy statement for the Montana University System's Self-Funded Workers Compensation Program (MUS) and noted Ms. Leah Tietz, Director of Montana University System Workers' Comp was in attendance.

Staff is presenting a recommendation for the new policy for MUS for the Workers' Compensation Program to move beyond investing exclusively in STIP and to allocate up to $5 million in the Trust Funds Investment Pool (TFIP). The fund is an operating account, which requires liquidity; however, it contains excess reserve. The MUS Committee has approved the investment of up to 35% of the account into the TFIP. Staff recommends Board approval.

Executive Director Ewer explained this is a new policy. MUS have invested only in STIP thus far, and BOI does not have individual user policies when investments are in STIP only. MUS has been invested in STIP since 2003.

Member Karl Englund asked if the move is consistent with policy.

Director Ewer stated with an abundance of caution, this is a big change; therefore staff is seeking Board approval. The TFIP policy does not change; however, the client base changes.

Mr. Romasko clarified client changes in policy do come to the Board for approval; there are a lot of participants invested in the TFIP.

Chairman Noennig asked if any client wanting to invest in TFIP is required to come to the Board.

Mr. Romasko replied that is correct.

> Member Jack Prothero made a motion to approve MUS Policy as presented. Member Karl Englund seconded the motion. The motion carried.

Member Sheena Wilson stated PERS is working on a similar idea for the Disability Retirement Pool.

Director Ewer agreed staff is working on it; however, there is no decision about policy changes yet.

Montana State Fund

Chief Investment Officer Cullen stated Mr. Jon Putnam has taken over responsibility for Montana State Fund and will present the quarterly report. Mr. Putnam has been at BOI since 2005, most recently working on the fixed income team. The State Fund portfolio has mostly fixed income, but also includes equity and real estate. Going forward, Mr. Putnam will work with Mr. Rande Muffick in managing all the asset classes within the State Fund portfolio.

Mr. Putnam presented the State Fund report for the quarter ending December 31, and reviewed market values and weight percentages of the current asset classes vs. the current policy ranges. Most of the portfolio is invested in the bond pool to maximize income and secure the safety of principal. There are small allocations to equities and real estate; the real estate is split between two core real estate managers. There were no changes to equity or real estate over the quarter. Mr. Putnam stated at year-end, State Fund transitioned to a calendar year from a June 30 fiscal year. Pursuant to that, they requested that BOI allow cash to go to zero, and therefore were out of policy compliance by January 1. This was a onetime event due to the switchover and staff does not anticipate a reoccurrence.

Member Prothero asked why State Fund would request going to zero cash.

Mr. Putnam advised they had to close out areas to enable the movement to new accounts for the calendar year switchover.

Mr. Putnam reviewed the State Fund bond pool characteristics and noted the effective duration is a bit short relative to the index. Mr. Putnam added State Fund paid out a substantial cash dividend to participants as well.

Member Englund asked how the State Fund dividend works; and whether they provide BOI with advance notice to build up cash.

Mr. Putnam stated yes, BOI received advance notice and there was no issue with raising the cash.

Mr. Putnam reviewed the State Fund sector weights. There is an underweight in treasuries and agencies, which is typical for this portfolio and an overweight in financials, which performed well. As for the commodities sectors, energy has been beaten up, and there is a slight overweight to energy; however, the portfolio remains solid, with high quality assets. One exception is Marathon Oil, which is in exploration; it was out 700 basis points in the last 3-4 months, but the portfolio has a short position and it looks like they will be all right over the long term. Durations will be moved back towards neutral for the portfolio. Over the quarter staff sold $20 million in short durations; however, the portfolio is still underweight in duration.

Mr. Putnam reviewed performance for the quarter and stated the portfolio looks good in for all time periods vs. the custom index, and managed to beat the Barclays Gov/Credit Intermediate index. The portfolio is underweight duration and overweight financials, which were positives; however, so far in the first quarter financials are taking a beating. Equities were strong in the 4th quarter, but have given back in the first quarter. Core real estate has been very strong; the three-year returns will show up next quarter, as April 2013 was the start of the real estate investment. Returns for real estate have been double digit and it provides a nice income component to it, as well as a good diversifier. However, double-digit returns in core real estate are not expected going forward.

Retirement Fund Bond Pool (RFBP)

Mr. Cullen turned over the presentation of the Retirement Funds Bond Pool (RFBP) to Mr. Rande Muffick. Mr. Muffick stated the RFBP is comprised of the core internal portfolio and the external portion that is managed by Reams, Neuberger Berman and Post Advisory. Performance for the bond pool lagged a bit in this quarter, due mostly to widening spreads, as well as high yield difficulties. The Barclays High Yield Index was down just over 2%.

Member Terry Cohea asked if Post Advisory is high yield.

Mr. Muffick replied yes, as well as Neuberger Berman. Post is a concentrated manager; they take big positions and have no exposure to energy, which has worked well compared to the benchmark, which does contain energy. Duration of the RFBP is a bit less than the benchmark. The internal bond portfolio traditionally has a longer duration, but when rolled up it is less than the benchmark. The average quality is still A1, which is good considering all the talk of downgrades. The sector weights show the attractiveness of spread products. You can see the effect of high yield in credit quality; most non-investment grade comes from Reams high yield holdings, as about 1% is non-investment grade.

Director Ewer asked how the Barclays Index works when securities are downgraded.
Mr. Cullen responded when securities are downgraded, they drop out of the Barclays Gov/Credit Index and drop into the Barclays High Yield Index.

Responding to a question from Member Englund, Mr. Sax stated the RFBP was started 1995; however, the start dates of managers are later, for example Reams started in 2008.

Trust Fund Bond Pool (TFBP)
Mr. Muffick presented the Trust Funds Investment Pool. The pool includes the Trust Funds Bond Pool (TFBP) as the largest member and includes lesser amounts of real estate as well as high yield with Post. Fund performance is even with the benchmark; however, the internal fund lagged a bit due to spread product. Post did well in the quarter, even though it is high yield, due mostly to the lack of energy holdings. Real estate also did well. Post did so well that allocation of high yield went up by a couple percentage points due to the outperformance of managers.

Montana Domestic Equity Pool (MDEP) and Montana International Equity Pool (MTIP)
Mr. Muffick presented the Montana Domestic Equity Pool for the quarter ending December 31. The U.S. market environment for the 4th quarter shows returns across the board were positive; large cap growth led with 7.3%, outperforming small and mid-caps by a bit and growth stocks did well compared to value stocks. Energy and mining did not do well. For active management industry wide, large cap stocks and active managers did not do well for the quarter. Even small cap managers suffered, mid-caps did a better job at beating the benchmark. BOI managers did the opposite as three of four managers did well; mid-caps struggled the most, small caps were mixed and growth performed the best.

Mr. Muffick reviewed the characteristics of the pool and capitalization weights. Staff did raise some cash in December and sold some spiders (Standard & Poor's Depository Receipt SPDR), enough to increase cash levels. Energy is underweighted a bit, as many managers are staying away from the energy sector. Staff wanted to show the difference between active managed accounts, taking away passive accounts, to look only at active manager positions. It makes quite a bit of difference and shows mega and giants, and the overweight to midcaps. Active accounts have a much bigger capitalization preference. The result is staff is looking at allocating more active money in smaller caps.

Member Terry Cohea asked with the overweight of small and midcaps, when compared to passive, it is only a slight tilt.

Mr. Muffick agreed yes, exactly.

Director Ewer asked if the strategy is still working at after four years.

Mr. Muffick stated yes, although for the long term, we will see some volatility. Small and mid-caps have struggled vs. large caps and when the economy experiences turbulence, you can see underperformance.

Mr. Mark Higgins added the capital market assumptions are due in April, and while you will see small and mid-caps underperform for the short term, over the long term they will outperform.

Mr. Voytko added when the portfolio was restructured the odds are weighted in your favor by taking active manager risk where you are taking it. Small caps will underperform when market sentiment sees the market is headed for trouble.

Mr. Muffick added that energy is underweighted by active managers and active managers as a whole are pretty well diversified by economic sector.

Mr. Muffick reviewed performance. For the three months just ended there is a portfolio lag of 25 basis points, due to manager selection. Three out of four large cap managers outperformed which offset the underperformance of the small and mid-caps to some degree.

Mr. Muffick presented the Montana International Equity Pool (MTIP) for the quarter ending December 31. The markets did well in the 4th quarter, although not as good as the U.S. due to the stronger dollar. After January 1, however, 4th quarter gains have been given back. Small caps did well compared to large caps and growth did well vs. value, due to energy and commodities concerns. Emerging markets lagged, due in part to oil producing nations and active management did well in large and small caps, outperforming industry wide. BOI large cap managers did well; all outperformed their benchmarks. All three small cap managers in MTIP struggled, although this seems to be an aberration. Occasionally, lesser quality small caps can outperform better quality small caps.

Mr. Muffick reviewed the exposure reports for MTIP. The portfolio is overweight emerging markets vs. the benchmark when passive is included. The active account rollup is quite different and active is more overweight mid and small caps. Reviewing exposure by sector, energy is a slight overweight; managers as a whole are underweight financials and overweight consumer discretionary. Concerns about Europe and China banking systems continue.

Reviewing country weightings on an active basis, emerging market is 4.5% underweight, as managers are cognizant of emerging market concerns; China is also underweight.

Member Terry Cohea posed a global question. Although international exposure is important, and BOI is at about 14% international, when reviewing the 10 year numbers for MDEP, domestic equity has averaged a 7% return while international equity only 2.4%. Private equity allocation is about half of international so it follows that there is a lot of emphasis on international; therefore, how long is it wise to be patient.

Mr. Muffick replied BOI has done well in underweighting international. Expected return over the long term is still above U.S. markets, and emerging markets expectations are even higher over the long term. While favoring U.S. vs. international developed markets, most growth will come from emerging markets. However, the U.S. markets are more mature and the U.S. labor market is much more mobile than Europe.

Member Englund observed that since inception, June 2009, only international large cap passive has come close for performance.

Mr. Cullen noted all play key roles regarding return goals and diversity. The overweight of U.S. has helped over time; however, at different times international will do better than domestic. At an asset allocation level, it takes study to be mindful of the past but also to look forward.

Mr. Muffick added there has been a huge appreciation of the U.S. dollar, and all indices are dollar denominated. If you take the dollar away, the 30% difference is the currency penalty. In local markets, performance was much better, as a U.S. investor, currency risk is a factor.

Mr. Jim Voytko stated there are several reasons to overweight domestic equities including the relative merits of investing internationally. However, if you are already underweight international, 45% of the entire equity universe is outside of the U.S.; therefore, you would be making a bet against the rest of the world.

Member Englund stated that makes sense, until you look at numbers.

Mr. Voytko agreed, when comparing the numbers over 10 years, it does.

Mr. Muffick reviewed performance for the quarter. Managers performed well with the small cap tilt adding slightly as they did better than large caps internationally. The cap weights will remain the same for small vs. large, the same as domestic.

There were no changes to the Watch List; however, the two managers on the list, Artisan and Alliance Bernstein, have seen some improvement.

Montana Private Equity Pool (MPEP)

Mr. Ethan Hurley presented the Montana Private Equity Pool report for the quarter ending September 30, 2015.

Fund Name	Vintage	Subclass	Sector	Amount	Date
Axiom Asia Private Capital, IV, LP	2016	Buyout/Venture FoF	Diversified	$25M	12/16/15
McCarthy Capital Fund VI, LP	2016	Buyout	Diversified	$25M	12/15/15

There were two commitments of $25 million each to Axiom Asia and McCarthy Capital; McCarthy is a new manager.

Member Satre asked if Axiom is invested in Asia.

Mr. Hurley responded yes, they are an existing manager invested in higher growth regions of the world.

Member Satre stated this is the third BOI commitment to Axiom, and asked if the funds are similar.

Mr. Hurley responded, yes, the funds are similar and although they make slight tweaks from fund to fund, they are consistent.

Representative Kelly McCarthy asked Mr. Hurley what drew him to the new manager, McCarthy Capital.

Mr. Hurley stated McCarthy is looking at smaller companies and putting in $50+ million into a $353 million fund, which represents a significant alignment of interest. They are located in Omaha, Nebraska and are very easy to work with. BOI staff interviewed all of the Boston affiliate employees.

Mr. Hurley reviewed the cash flow, which was again positive at quarter end; 14 of the last 16 quarters were cash positive. MPEP is diversified by strategy, overweight buyouts, but diversified broadly and there is no attempt to over or underweight any specific industry.

Member Cohea asked about the low allocation to the energy sector.

Mr. Hurley stated it is not by design, although has played out that way over time. There are private equity general partners who have energy commitments, which have not been called yet.

Mr. Hurley stated direct commitments continue to rise vs. fund of funds. Looking at periodic return comparisons, the portfolio continues to be an accretive asset class.

Mr. Hurley presented a new addition to the report, a snapshot of holdings at year-end; all numbers are updated through December 31, 2015. The global private equity index provided by State Street Bank shows the portfolio is roughly performing in line with the 2500 underlying private equity funds tracked by State Street.

Member Cohea asked if unfunded commitments of nearly $600 million is a higher than average amount.

Mr. Hurley responded, it is about average.

Chairman Noennig asked where the money is committed.

Mr. Hurley stated it is spread across asset classes or in cash.

Montana Real Estate Pool (MTRP)

Mr. Hurley reported there were no new commitments for real estate since the last Board Meeting. On January 22, the trade settled which divested interest in Clarion Fund, a core real estate fund which staff had been trimming; proceeds were used for liquidity needs. By the end of last year, in relation to the rest of the BOI managers, Clarion was investing in riskier assets, value added type real estate transactions with higher leverage. Staff chose to divest completely as real estate ranges went up and BOI dropped into a higher fee band.

Member Cohea asked about the structure of real estate and the ability to exit out of a fund when you want, and if real estate has different arrangements.

Mr. Hurley stated yes, but only with open-ended core real estate funds. As with private equity, the market for closed-end real estate funds is a very illiquid market where you potentially take a large hair cut if sold. However, core real estate has open ended funds and provide liquidity options on a quarterly basis. Although open-ended, they are open-ended in name only. When the real estate market shifts negatively, there may not be enough liquidity to fulfill all the redemption requests. Therefore, an exit can be hindered until the market stabilizes.

On the cash flow side, MTRP had a negative quarter, due mostly to two fund closings with large capital calls which required BOI cash.

The portfolio is well diversified, and broadly geographically diversified, as well as diversified by property exposures. Staff makes no attempt to over or underweight. Reviewing time weighted returns, the portfolio continues to move in a positive direction and the IRR is moving in a positive direction (closed end). Reviewing the commitment summary, holdings changes as of 12/31/15 are due to cash flows. The portfolio is conservatively leveraged and within all policy constraints.

Mr. Hurley reported there were no changes on the watch list.

Member Prothero asked if any managers were making progress.

Mr. Hurley stated none have made drastic improvements, and there is not much that can be done about it, as selling would be at a loss. Real estate is performing better than during 2008-2009.

Carried Interest – Update

Mr. Hurley stated there has been a lot of scrutiny and media attention, critical mass, building in the limited partner community regarding disclosure of transparency on fees and carried interest. The media has painted general partners as hiding carried interest; however, it is reported in financial statements, so they are not hiding it. BOI has been getting information from real estate general partners. There has been a recent effort put on private equity general partners, and a template was developed with accounting staff to send out to the GPs. BOI has requested quarterly disclosures, and ILPA, a non-profit group has developed a reporting template. BOI has publicly endorsed the ILPA reporting template. None of our GPs do not want to do business with us, but BOI is climbing on board with the rest of the limited partners to standardize the reporting.

Member Englund asked why this is happening now.

Executive Director Ewer stated there has been a lot of bad press and prominent articles written.

Member Cohea asked is the question only on carried interest and not distributions.

Mr. Hurley stated yes and no. When a GP is entitled to carried interest, no check is cut or cash distributed, they simply take their share of the carried interest when the investment is realized and taken from profits.

Director Ewer added it is not accounted for; the portion the GP makes in the process, as BOI books our 80 but not their 20. We want to track it; is not an accounting phenomenon.

Mr. Hurley stated many times there will be a bullet; financial statements are consistent with LP agreements, and a water fall which addresses carried interest. As a limited partner, it is reported to us, but it is not on our BOI balance sheet.

Mr. Voytko added when looking at profit sharing, you want to know what each party's share was, the management fees and offsets. General partners were not cheating anyone; however, they were not all reporting in the same way. ILPA is trying to uniformly present the profit sharing.

Member Englund referenced Odyssey Partners and asked how often is it necessary to have face to face contact.

Mr. Hurley responded annually, often during the annual general meetings, or any other time of year at the manager's location; staff does need to be in front of each manager each year.

CONSULTANT REPORT

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

Mr. Higgins presented the RVK quarterly performance report for the quarter ending December 31, 2015. Reviewing the summary of retirement plan performance as represented by PERS, a lot of the trailing return is due to the private equity pool and the underperformance of U.S. and international equity; however, peer rankings are very strong, in the top decile. The portfolio metrics illustrate the effectiveness of the program over five and ten year analysis. The Risk/Return matrix demonstrates less risk with higher return as desired and BOI is doing both over five and ten years with a top decile ranking for risk adjusted return.

Mr. Voytko added the reports show not only how well BOI has done, but also how much risk was taken; the BOI position shows less risk, with more return, whereas, higher returns with more risk means more volatility.

Mr. Higgins reported both domestic equity and international equity are improving substantially; the international pool has fared a little better. The RFBP exposure to high yield, although will generate a better long-term return, showed a bit of underperformance over one year. The TFIP exposure to real estate has helped. The private equity pool is finally proving its value, especially over one year. Five years ago vs. the index, private equity was trailing by double digits, but has closed in on the benchmark and is slightly positive over 7 years. STIP is becoming more attractive as interest rates are rising and realized a 14 basis points return advantage, and gross of fees is performing well. Private equity has showed excess returns, which means the public market has slowed down.

Mr. Voytko added the 2014 annual return fell 8.96% below the public equity benchmark; today however, it is the complete opposite.

Mr. Higgins reviewed peer rankings. Domestic equity is looking good, international equity is lagging, but it is hard to determine the peer group. The RFBP and TFIP both look good.

Mr. Voytko stated as Mr. Cullen pointed out, in recent times, domestic equity has been tapped for providing liquidity to pay benefits when necessary. Beta sensitivity to equity markets shows steady management, vs. sensitivity to the U.S. stock market, there are no huge ups and downs.

Mr. Higgins concurred; the current program is functioning well.

Member Prothero asked Mr. Higgins and Mr. Voytko if they have any manager concerns.

Mr. Higgins responded the RVK manager research team reviews managers on an ongoing basis. Artisan has struggled over the long-term, but there are no recommendations at this time to take any action on any of the portfolio managers.

Mr. Kulow requested to reconvene the Loan Committee to approve an increase in the DNRC loan amount, approved earlier in the Committee meeting. Upon speaking with Ms. Anna Miller, Bureau Chief of DNRC to advise her BOI had approved the $2,573,976 loan, Ms. Miller requested the reserves and financing costs be included, increasing the total loan amount to $3 million. Mr. Kulow recommended the Committee approve the increased loan amount.

Executive Director Ewer noted he approved of the increase.

> Loan Committee Chairman Jack Prothero made a motion to approve the increase in the loan amount to DNRC from $2,573,976 to $3 million. Member Kathy Bessette seconded the motion. The motion carried.

BOND PROGRAM REPORTS

Activity Report
Ms. Louise Welsh reviewed the quarterly Activity Summary Report as of December 31, 2015, and noted there were 24 loans committed over the quarter totaling $8.6 million. Funded loans for the quarter totaled $9.2 million to 32 borrowers and included loans for vehicles, buildings and roads.

Member Karl Englund inquired about the loan to the Broadwater Hospital District for $474,000 to be utilized for Medicaid reimbursement.

Ms. Welsh explained Medicare calculates the amount each hospital receives, but if the payments amount to overcompensation, the hospital must reimburse Medicare/Medicaid for the overpayment.

Ms. Julie Flynn further explained in Broadwater County's case, the nursing home closed down for a time and when it was recertified and reopened, a new Medicare/Medicaid formula was applied generating the new revenue figures, which were incorrect resulting in a large reimbursement being paid back.

Member Satre asked if it is true that Broadwater County has been experiencing a lot of financial difficulty.

Ms. Flynn stated yes, however they appear to be headed in the right direction.

Mr. Satre stated they now have the $474,000 debt, in addition to the normal operating expenses on top of the recent economic problems.

Ms. Flynn replied yes; however, a tax levy was successfully voted to specifically pay debt service on the $474,000 INTERCAP loan.

INTERCAP PROGRAM OVERVIEW

Ms. Welsh presented an overview of the INTERCAP Bond Program (INTERCAP). INTERCAP's inception stems from the combination of the Board with the Montana Economic Development Board in 1984 as part of the "Build Montana" program. The Board was charged with both board's missions including implementing programs under the Montana Finance Consolidation Act (MFCA) in the Montana Code Annotated, Title 17, Chapter 5, Part 16, as well as various coal tax loan programs. In 1987, INTERCAP was created to assist local governments finance their capital projects using low-interest loans. INTERCAP is an enterprise fund, run as a business, providing services to Montana government agencies for a fee in the form of loan interest; it is a self-supporting program. The Board issues tax exempt Annual Adjustable Rate Tender Option Municipal Finance Consolidation Act Bonds (Bonds) to provide the pool of cash available to fund the INTERCAP loans Resolution 219 specifies the Board can enhance the Bonds and cover the Bond debt service by replenishing the Bond reserve, if needed, through the Perm Coal, Treasurers' Fund and STIP.

Ms. Welsh presented the quarterly Activity Summary. The previous Bond rate was 23 basis points and the new rate for 2016 is 52 basis points. The Bonds were oversubscribed again, and so were fully remarketed. At 52 basis points, the maximum spread allowed is 1.50, therefore 2.02% is the maximum allowable rate charged to borrowers. The new 2016 loan interest rate to borrowers has been set at 1.55%.

The Board's current enhancement on the Bonds is $106,445,000; however, that amount will decrease to $97,340,000 after March 1, as the 1997 Bonds will be redeemed. On a side note, Montana Facilities Finance Authority (MFFA) anticipates a full call of their Board enhanced $3,625,000 Montana Developmental Center bonds in April. No outside bond insurance company is used; BOI guaranties the bonds. Doing so enhances the marketability of the bonds and assists INTERCAP in obtaining the lowest possible loan interest rates to eligible governmental units that provide essential services and facilities to Montanans. Tendered Bonds are remarketed each year and if not purchased, the Board purchases, although to date, the Board has never been called on to cover. Even without the anticipated redemptions, the funds designated as the guaranty provide 8x the coverage. Bondholder interest is expected semi-annually on September 1 and March 1, therefore loan repayments have semiannual due dates of August 15 and February 15.

With the reduced amounts of bonds outstanding, the 52 basis points will amount to about $500,000 for a total exposure of $97.85 million. Perm Coal STIP is the first in line to provide the guaranty if called upon. A new bond issue can occur at any time of year though it is preferred to issue during the remarketing period to reduce cost and avoid two Bond rates in effect for the year.

Ms. Welsh reviewed the Bonds remarketing process and stated 20 days before the March 1 closing date BOI is notified of the amount to be tendered and remarketed. 74% of the bonds were tendered; The United Services Automobile Association (USAA) retained their bonds and added more to their portfolio; Vanguard tendered and did not come back; and BNY Private Wealth, Neuberger Berman, Fidelity, Columbia Asset Management, Northern Trust and JP Morgan all invested.

BOI is paid a credit enhancement fee of a 1.3% onetime payment on a new Bond issue and 25 basis points of the principal amount of tendered bonds actually purchased. BOI has realized $1.5 million paid in fees. The fee price is set at the discretion of the Board; the Executive Director is reviewing the fee for possible future revisions. So far, the Board has not been called on to replenish Bond reserves to pay debt service or purchase tendered bonds.

The tax-exempt Bonds used to fund INTERCAP loans are remarketed every February, and the high rating makes the bonds very attractive. A new Bond will be issued in 2017; for every Bond issue, a reserve is held back. The remarketing cost is ~18 basis points, and Bond terms are for 20 and 25 years. The Board's guaranty directly affects the rating. Moody's rating is Aa3 and Fitch's rating is AA; ratings are based on the fiscal capacity of the Board, its total leverage, and the relative size of outstanding and proposed debt compared to funds available to pay. The State of Montana Fitch rating is AA+. High quality bonds translate into lower rates for the borrowers. The municipal markets, other similarly rated credit, and supply and demand, are all taken into consideration. In 2008, the market environment was a challenge for remarketers. The finance team used to prepare and market the Bonds consists of Underwriter/Remarketing Agents, Underwriter's Counsel, Board Counsel, Bond Counsel and Trustee.

Borrowers consist of local governments, state agencies and universities, and thus far, INTERCAP has never suffered a loss. This is due to a reasonable underwriting process and the basic credit soundness of Montana local governments. Loans have no origination fees and there are no prepayment penalties.

INTERCAP benefits Montana; close to $473 million has been distributed throughout the state since inception of the program for various projects. 75% of all Montana cities/towns and counties in addition to almost half the school districts have used INTERCAP.

RECAP OF STAFF TO DO LIST AND ADJOURNMENT

Executive Director Ewer reviewed items on the "to do" list for the next Board meeting:

1. By consensus, the October 4 Board Meeting is rescheduled to Thursday, October 6.
2. The revised Organization chart will be finalized and presented at the April Board meeting. Managers and portfolio managers will be directing staff under the new supervisor arrangements. Executive Director Ewer and Deputy Director Burton will be assisting in the process.
3. Staff will provide more detail to the Loan Committee regarding INTERCAP loans involving the Rural Development program.

Being no further business before the Board, the meeting adjourned at 4:54 p.m.

Next Meeting

The next regular meeting of the Board will be April 5, 2016 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: May 24, 2016

BOI:drc
3/31/16