

**PUBLIC SAFETY PERSONNEL RETIREMENT SYSTEM**  
**BOARD OF TRUSTEES INVESTMENT COMMITTEE MEETING**

August 18, 2010

**MINUTES**

Members Present: Ms Lori Roediger, Trustee, Chairperson  
Mr. Tim Dunne, Trustee

Others Present: Mr. Ryan Parham, Chief Investment Officer  
Mr. Marty Anderson, Deputy Chief Investment Officer  
Mr. Paul Corens, Alternatives Investment Analyst  
Mr. Mark Steed, Senior Analyst  
Mr. Mark Selfridge, Investment Analyst  
Mr. Shan Chen, Investment Analyst  
Ms Michele Weigand, Investment Contracts Paralegal  
Mr. Allan Martin, Managing Partner, New England Pension Consultants  
("NEPC")  
Mr. Don Stracke, Senior Consultant, NEPC  
Mr. John Shearman, Partner, Albourne America LLC  
Mr. Tom Cawkwell, Albourne America LLC  
Mr. Marc Lieberman, Partner, Kutak Rock

A. Call to Order

Chairperson Lori Roediger called the meeting to order at 10:10 a.m.

Review, discussion and possible approval of Investment Committee Minutes from May 26, 2010, June 23, 2010, and June 28, 2010.

<b>Recommendation</b>	At 10:15 a.m.
<b>08-1-10</b>	
<b>Recommendation:</b>	Motion to approve the Minutes.
<b>Moved by:</b>	Tim Dunne
<b>Seconded by:</b>	Lori Roediger
<b>Discussion:</b>	
<b>In Favor:</b>	Unanimous
<b>Motion Passes:</b>	Passes

C. Review, discussion and possible recommendations to the Board of Trustees regarding:

1. Presentation by the Investment Department Staff, New England Pension Consultants (NEPC) and Franklin Templeton Investments representatives and discussion and possible **Recommendation** regarding an investment of up to \$60,000,000 in Franklin Templeton Emerging Markets Debt Opportunities Fund or appropriate feeders, blockers or parallel funds of same.

Mr. Parham report that Investment Staff is considering up to \$70 million in this strategy as opposed to \$60 million. Ms. Roediger asked what influenced that change. Mr. Parham stated that the decision has to do

with optimization of the entirety of the strategy. He said that there are two or three additional managers that are being considered for this space and that as Investment Staff optimizes the historic returns for the investments under consideration that it was felt a slight overweight to Franklin Templeton was best. Mr. Lieberman commented that the agenda for the Board meeting reflects an investment of up to \$70 million so the recommendation can be for up to \$70 million.

Mr. Parham stated that Investment Staff likes moving into emerging market debt (EMD) because the structure of the markets continues to represent a favorable environment.

Mr. Stracke referred to NEPC's memorandum "Emerging Market Debt Manager Recommendation" that was included in the meeting material. He summarized the Asset Allocation Policy adopted by the Board in June which targeted 20% of the Trust's total portfolio to fixed income. He said of that 60% is in US markets and 40% in Non-US markets and in particular a 3% exposure to EMD. He said that emerging markets is a strategic focus for NEPC due to the growth aspects and the healthy balance sheets and income statements in those markets. He said that one of the reasons NEPC focused on this area early is because it is a good diversifier and there is a yield pick up over the US fixed income markets. He said that in regard to the structure of this asset class that Investment Staff and NEPC are considering having two core EMD managers and some hedged exposure, both long and short investments, which would pull down the over-risk of the emerging market exposure.

Mr. Stracke said that NEPC in conjunction with Investment Staff developed a list of 50 managers in this space which were then screened and from those a short-list of 15 managers was developed. He said that NEPC then meet with all the managers on the short-list both on-site and at NEPC's office. He said that NEPC then came up with a focused placement list or their recommended list of six emerging market managers noting any of which would be a good fit. He said that Investment Staff and NEPC felt that Franklin Templeton was the most appropriate manager for this mandate given their absolute return approach; focus on a "pure" exposure to emerging markets as defined by income levels in each country, and the greater diversification through the inclusion of more countries including frontier countries.

Mr. Thomas J. Dickson, Senior Vice President/Regional Director Institutional Business Development and Institutional Client Services and Ms Claire Husson, Portfolio Manager, Emerging Markets Debt Research Analyst, both from Franklin Templeton introduced themselves to the Board. Mr. Dickson referred to the presentation booklet distributed to the Board. He gave a brief overview of the Firm's investment management platforms noting that as of June 30, 2010, the total Fixed Income platform had \$234.4 billion in AUM and of that \$67 billion is managed in dedicated emerging markets assets. He gave a brief description of the Firm's global office locations, the EMD Opportunities Team's capabilities and the internal resources available to the team.

Ms Husson summarized their absolute return approach explaining that for them, any country that is not effectively a developed economy is potentially an investable emerging market. She said they employ top-down risk controls. They have a large opportunity set because they use hard and local currency issuers which increases their investment universe. She explained that historically, they have found excellent opportunities in less efficient markets and they have invested in local currencies since the fund's inception so they understand the complexities of the local markets. She discussed the EMD investment process which employs bottom-up research to determine country selection, currency selection and issue selection.

Mr. Dunne asked what their percentage limit is to any particular issuer. Ms Husson responded that they limit their risks by credit risks which means for any given company, if it is rated BB then they cannot invest more than 5% and if it is B then the limit is 2.5%. She said that effectively they do not go beyond 10% of the bond but in addition they have the aggregate risks put in place.

Ms Roediger asked if something gets downgraded and they are out of compliance if they automatically have to sell that or do they have flexibility to take into consideration the spreads. Ms Husson responded

that effectively they do not have weighting constraints for the credit bracket which can represent no more than 20% of the portfolio and effectively they would need to reduce from 4% to 2.5% but since they have never invested up to 5% in a given company that case has not present itself because they prefer diversifying as much as possible.

<b>Recommendation</b>	At 10:40 a.m.
<b>08-2-10</b>	
<b>Recommendation:</b>	Motion to approve a recommendation to the full Board for the investment of up to \$70,000,000 into the Franklin Templeton Emerging Debt.
<b>Moved by:</b>	Tim Dunne
<b>Seconded by:</b>	Lori Roediger
<b>Discussion:</b>	
<b>In Favor:</b>	Unanimous
<b>Motion Passes:</b>	Passes

2. Presentation by Investment Department Staff, Albourne America LLC and Jefferies Asset Management, LLC representatives and discussion and possible **Recommendation** regarding a possible investment of up to \$40,000,000 in a separate account or a commingled fund (or any appropriate feeder, blocker or parallel fund of same) employing the Jeffries Diversified II Commodity Program strategy.

Mr. Anderson gave an overview of the real assets allocation and the commodities exposure that was put in place in the past. He explained that exposure can be described as relative value in nature that is being less directional but able to capitalize on the rising or falling markets based on what is going on in the commodity. He said the Investment Staff wants to add some directional exposure that will add beta and the potential to outperform the index.

Mr. Shearman summarized the due diligence conducted by Albourne and said that they are very comfortable with the investment and that they are pleased to be adding this component because it finally gets the program up and rolling holistically. He said in aggregate this should achieve what we want with the existing alpha component and now add the beta component. He said this will improve the risk adjusted return of the entire program and achieve what we are trying to achieve through unexpected inflation.

Mr. Adam De Chiara, Portfolio Manager, Jefferies Asset Management Commodity Division gave a brief background, as it relates to the Jefferies experience in the long-only commodity strategies. He discussed the CRB Index and the forward price curve and volatility and Jefferies yield approach. He said that job as an active manager to try to position the portfolio to capture backwardation when the market moves in that direction and when they are moving away from backwardation or are perpetually in a contango to try to select portions along the price curve to minimize the negative yield associated with that. He said from a risk management standpoint they have extensive practical experience trading these markets and liquidity and risk management is a key focus of what they do. He said their targeted tracking error against the underlying benchmark is about 200 bps a year and they are looking to generate somewhere in the neighborhood of 300 to 500 bps of outperformance above the benchmark.

Ms. Roediger asked if most of the movement was based on fundamentals and producers or end user hedging or funds having to roll on specific dates.

Mr. De Chirara responded that it can be a combination on both depending on the market and the particular event involved. He said that in his experience, theoretical and empirical, the impact of passive long exposure rolling over fixed windows of time have lessened because markets are efficient and people have come to anticipate it and position around it. He said that for every long position in a commodities

futures contract there is an offsetting short position and that is different than equities and fixed income. He said most of the opportunity they see is from three to twelve months forward and what is driving the evolution of the curves out there is typically more of the fundamentals. He said their job as managers is to try to capitalize on the markets that are moving towards backwardation and earn that yield and try to side step the negative yield associated with the more oversupplied markets.

Mr. Dunne asked if they were “black box” technical.

Mr. De Chirara responded that they rely heavily on quantitative models that they have developed over the years as their first line of analysis. He said their focus is on trying to stay in the liquid portions of the curve, adjusting positions as they see the liquidity developing. He said that prudent risk management decisions cannot really be done utilizing formulas so they do utilize quantitative analysis of the curves. He said it is at the core of what they do but at the end of the day it is a discretionary investment process.

Mr. Dunne asked if there was a ceiling on account size and what size account Jefferies felt they could effectively manage.

Mr. De Chirara responded that there are a number of things going on in the commodities space related to the CFTC and the capacity constraints they expect to be coming. In addition, they are currently between commitments that have not yet funded yet which will bring their AUM just under \$1 billion. He said their view is that somewhere around \$5 billion is where they will hard stop the portfolio. He said the reason for that is; if you do the math you can say a manager like them can manage \$10 billion or somewhere north of that but, his experience has been that liquidity is critical and it is virtually impossible to manage risk in the commodities space if you are pressing up against liquidity thresholds. He said that looking at their strategies and the depth and length of the forward curves, having managed multi- billion dollar portfolios of commodity indexed long-only outperformance that his view is \$5 billion is very comfortable and allows them to do everything they need to do without having any diminution of their return or their risk profile.

<b>Recommendation</b>	At 11:05 a.m.
<b>08-3-10</b>	
<b>Recommendation:</b>	Motion to approve a recommendation to the full Board for the investment of up to \$40,000,000 in the Jefferies Asset Management Program.
<b>Moved by:</b>	Tim Dunne
<b>Seconded by:</b>	Lori Roediger
<b>Discussion:</b>	
<b>In Favor:</b>	Unanimous
<b>Motion Passes:</b>	Passes

3. Presentation by Investment Department Staff and JMI Equity representative and discussion and possible **Recommendation** regarding an investment of up to \$40,000,000 in JMI Equity Fund VII, L.P. or appropriate feeders, blockers or parallel funds of same.

Mr. Steed gave a brief overview of JMI Equity Fund VII. He said that JMI is a growth equity fund that invests in software, internet and business services companies. He said the Firm boasts a net IRR of 42% and a realized multiple on capital of approximately 2.4x for recent funds and 3.2x across all funds. He said that Investment Staff conducted due diligence in conjunction with StepStone and found JMI to be more growth-oriented showing an ability to add greater value through revenue enhancements compared to their peers and believes this is one of the reasons JMI had the strongest cash-on-cash returns of its peer group. Mr. Steed stated that Albourne also had several meetings with JMI and would have an opinion of this investment.

Paul Barber, General Partner, JMI Equity said they are fundamentally growth equity investors focused on

software businesses. He said they have been around for 18 years and they are about to make their 99<sup>th</sup> investment. He said they have had 55 realizations during that time and have sold 4 companies this year and the average return on invested capital on those four deals was 4.4x a high 30s IRR. He said there niche is to find companies that have not raised traditional venture capital. He said that 70% of the time they are first institutional capital in what they call “boot strap” businesses. He said selectively they also do buy-outs and recaps of later stage companies which generally they have some history with. He said JMI has 24 investment professionals split between Baltimore and San Diego. He discussed their sourcing and due diligence mechanism.

Ms Roediger asked how these companies are not on the radar of traditional venture.

Mr. Barber responded that some are but there is a geographic inefficiency. He said most of the venture is in Northern California or the Northeast and also they invest in software niches, the boot strap companies, where they feel they can add alpha by bring in teams to help scale the business.

Mr. Dunne asked how they see this environment in comparison to five years ago or five years forward as being a cost effective time to by.

Mr. Barber responded that they are in the market everyday so they will look at 500 companies a year trying to find five that are really exciting. When the global economic crisis hit two years ago they pressed the pause button and did no new investing for 14 months. He said part of that was they have 35 portfolio companies and they could tell that none of them could forecast their numbers. He said late last year they did two new invests and this year they will do their third so they are not back to historical levels yet. He said the key for them is to find the market segments that are growing faster and the companies that are innovating.

Ms. Roediger referred to the presentation material distributed to the Board and asked what was meant by the statement that they are able to effectively arbitrage.

Mr. Steed stated that by that description he meant that they have effectively been able to time the markets to find dislocations when it is effective to be a late stage investor and it is profitable to be a buy-out investor in their spaces. He said they have afforded themselves the ability to invest across the size spectrum and avoid getting pigeon holed.

<b>Recommendation</b>	At 11:30 a.m.
<b>08-4-10</b>	
<b>Recommendation:</b>	Motion to approve a recommendation to the full Board for the investment of up to \$40,000,000 in JMI VII.
<b>Moved by:</b>	Tim Dunne
<b>Seconded by:</b>	Lori Roediger
<b>Discussion:</b>	
<b>In Favor:</b>	Unanimous
<b>Motion Passes:</b>	Passes

4. Presentation by Investment Department Staff regarding increasing the previously approved investment managed by and Fischer Francis Trees and Watts (“FFTW”) or its subsidiaries or affiliates in an actively managed U.S. Inflation-Linked Bonds (TIPS) strategy investment vehicle from up to \$50,000,000 by an additional allocation of up to \$40,000,000.

Mr. Parham stated that the Trust is currently invested in this strategy with an allocation target of up to \$50,000,000 and Investment Staff is asking to increase that from \$50,000,000 as an upper cap to \$90,000,000. He said the Investment Staff likes the TIPS strategy and the additional allocation will help

staff to achieve asset allocation targets. He said that there are days that we have more cash than we would like and because the strategy is very liquid, it is high quality and it gives inflation protection. He said this investment is housed in the real assets portfolio and that this incremental increase will provide more maneuverability as far as achieving the total asset allocation goals.

Mr. Dunne asked why this is in the real assets rather than fixed income allocation.

Mr. Parham responded that it is the nature of the real return. He said one of the strategic objectives that Staff hopes to satisfy in real assets is inflation protection. He it was a strategic decision made more than a year ago with the concurrence NEPC to put this investment in real assets but there is an agreement that it could be in fixed income as well.

Ms. Roediger asked if it were in fixed income if it would through off the allocation.

Mr. Parham responded no.

<b>Recommendation</b>	At 11:38 a.m.
<b>08-5-10</b>	
<b>Recommendation:</b>	Motion to approve a recommendation to the full Board for investment of an additional \$40,000,000 bringing the total allocation up to \$90,000,000 into the FFTW U.S. Inflation-Linked Bonds strategy.
<b>Moved by:</b>	Tim Dunne
<b>Seconded by:</b>	Lori Roediger
<b>Discussion:</b>	
<b>In Favor:</b>	Unanimous
<b>Motion Passes:</b>	Passes

5. Presentation by Investment Department Staff and NEPC representatives and discussion and possible **Recommendation** regarding the approval of a revision to the Appendix I *Asset Allocation Policy* of the PSPRS Amended and Restated Statement of Investment Policies adding “3-month LIBOR, +3%” as the benchmark for the Global Tactical Asset Allocation (GTAA).

Mr. Anderson stated that the GTAA investments were moved out of Equities and into its own asset class as of July 1 per the recently adopted revised Asset Allocation Policy. He said that when this asset class was carved out there were discussion regarding what the appropriate benchmark should be because the strategies migrate over time in that they may be long equities, short equities, long debt, short debt, commodities, currencies and all of those various assets. He said that a number of alternatives were weighed over a period of time and Staff did some data crunching along with NEPC and Albourne and had with discussions with the managers. He said the conclusion was that the least worse alternative was the 3-month LIBOR, + 300; the idea being that the LIBOR is a cash benchmark and then the 300 bps above that. He said this will achieve something that was agreed upon as being rational and it reflects the idea that the managers are suppose to add alpha over a cash return over long periods of time. He said there will certainly be tracking error and that was one of the things that they were trying to modify but it was concluded based on the data that there really isn't one so this represents the idea that they are providing that real return over cash.

Mr. Martin said that he felt Mr. Anderson articulated it well and that when you look at the various managers at the end of the day that you want a strong absolute return number but we will also look at how they do in terms of how they change the portfolio.

Mr. Dunne asked where the asset class is now in terms of its target.

Mr. Anderson responded that we are slightly above that currently because the CTA just funded and equities have come down.

<b>Recommendation</b>	At 11:45 a.m.
<b>08-6-10</b>	
<b>Recommendation:</b>	Motion to approve a recommendation to the full Board a change to the Asset Allocation Policy adding "3-month LIBOR, +3% as the benchmark for GTAA.
<b>Moved by:</b>	Tim Dunne
<b>Seconded by:</b>	Lori Roediger
<b>Discussion:</b>	
<b>In Favor:</b>	Unanimous
<b>Motion Passes:</b>	Passes

6. Report by Investment Department Staff and discussion regarding the Month Ended and Fiscal Year-to-Date performance/portfolio update.

Mr. Selfridge provided a brief review of the month end performance. He stated that the reports provided to the Board represent final performance numbers for the Total Fund with the exception of the NCREIF which is published on a quarterly basis about six weeks after the quarter ended. He noted the performance does not factor in the GTAA benchmark as it has not yet been approved by the Board but if it were included it would be slightly less than 3% for July and another 2 to 3 bps for the Total Fund benchmark. He said the GTAA outperformed the proposed benchmark by about 4.5%. He reported the short-term investments were at about 4% at the end of last month because Staff was preparing for the funding of the final component of the GTAA strategy, BlueTrend, at \$100 million on August 2. He said portfolio was slightly overweight in equities and credit opportunities.

Mr. Martin briefly discussed the Investment Performance Analysis conducted by NEPC for the quarter and fiscal year ended June 30, 2010.

7. Report by Investment Department Staff and discussion regarding the Fiscal Year-Ended June 30, 2010, performance for the Arizona PSPRS Trust and the individual Plans comprising the Trust: Public Safety Personnel Retirement System (PSPRS), Elected Officials' Retirement Plan (EORP), and Corrections Officer Retirement Plan (CORP).

Mr. Parham reported that historically there were variations in the performance of each of the respective plans because they were not in the trust structure and as the Plans grew one may receive more cash than another and thus buy more securities. He said there remains a slight discrepancy between the Plans even after moving to the Trust structure because of one real estate asset that in the current market probably has no value. This asset was not unitized along with the other assets because the bank that held debt on the project would not allow the asset to be unitized without the payment of extraordinary fees. He said that for all intents and purposes the respective returns for each of the three plans, CORP, EORP and PSPRS is identical with some rounding error that is insignificant and immaterial.

8. Report by Compliance Auditor and discussion regarding investment compliance, holdings and transactions as of July 31, 2010.

There was no report.

9. Presentation by legal counsel and discussion and possible **Recommendation** regarding approval of proposed revisions to the PSPRS Amended and Restated Statement of Investment Policies to conform with recent changes to the Arizona Revised Statutes including, changing the reference from Fund Manager to Board of Trustees where appropriate.

This item was not discussed.

10. Report by Investment Department Staff and/or legal counsel and discussion regarding recent developments and legal issues (including settlement discussions) involving the Trust's custodians, lenders, securities lending agents, vendors, advisors, investments or investment managers or partners (as well as any investments managed by the Trust's investment managers or partners). The Board of Trustees may vote to discuss this matter in Executive Session pursuant to A.R.S. §§ 38-431.03(A)(3),(4) and (7), as set forth in item D(1).

This item was not discussed.

- D. Executive Session for Legal Matters.** Discussion with legal counsel for legal advice, and discussion with and instruction to legal counsel regarding (i) ongoing or threatened legal action involving the Arizona PSPRS Trust, the System or the System's sister plans (EORP or CORP) (the "Plans"); (ii) legal issues affecting the Plans and the Trust, and any issues regarding the Trust's or Plans' vendors, advisors, contracts, legal rights, personnel, or investments. The Investment Committee may vote to discuss these matters, wholly or in part, in Executive Session pursuant to A.R.S. §§ 38-431.03(A)(1),(2),(3),(4) and (7).

1. Discussion with and instruction to legal counsel regarding legal issues, and settlement discussions, if any, arising in connection with the Arizona PSPRS Trust's real estate, private equity, hedge and other investments, including those managed (or formerly managed) by the Pivotal Group, ApexCapital Management, and Desert Troon Limited, pursuant to A.R.S. §§ 38-431.03(A)(3), (4) and (7), and including claims raised by Millard and Scott Seldin with respect to an indirect investment in Anthology.

An Executive Session was not convened.

- E. Call to the Public**

No members of the public came forward to speak.

- F. Schedule next meeting**

The next Investment Committee meeting has yet to be determined. The Annual Meeting of the Board of Trustees has been scheduled for September 15 and 16 but there has been discussion to forego the Committee meetings which are typically held in the morning prior to the Board meeting.

- G. Adjournment**

<b>Recommendation</b>	At 12:17 p.m.
<b>08-7-10</b>	
<b>Recommendation:</b>	Motion to adjourn.
<b>Moved by:</b>	Tim Dunne
<b>Seconded by:</b>	Lori Roediger
<b>Discussion:</b>	
<b>In Favor:</b>	Unanimous
<b>Motion Passes:</b>	Passes

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Ms. Lori Roediger, Trustee, Chairperson

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Mr. Tim Dunne, Trustee