PUBLIC SAFETY PERSONNEL RETIREMENT SYSTEM

BOARD OF TRUSTEES INVESTMENT COMMITTEE MEETING

May 25, 2011

MINUTES

Members Present:	Mr. Alan Maguire, Acting Chair
	Mr. Richard Petrenka, Trustee
	Mr. Lauren Kingry, Trustee, Trustee
Others Present:	Mr. Ryan Parham, Chief Investment Officer
	Mr. Marty Anderson, Deputy Chief Investment Officer
	Mr. Pascal Stalder, Risk Officer
	Mr. Paul Corens, Alternatives Investment Analyst
	Mr. Mark Steed, Senior Analyst
	Mr. Shan Chen, Investment Analyst
	Mr. Mark Selfridge, Investment Analyst
	Ms. Bridget Feeley, Internal Audit and Compliance Officer
	Mr. Allan Martin, Partner, NEPC, Inc.
	Mr. Don Stracke, NEPC, Inc.
	Mr. Lincoln Smith, Consultant, Albourne America, LLC
	Mr. Jay Rose, Partner, StepStone Group
	Mr. Jose Fernandez, Founding Partner, StepStone Group
	Mr. Marc Lieberman, Partner, Kutak Rock

1. Call to Order, Roll Call, Opening remarks.

Chair Alan Maguire called the meeting to order at 9:03 a.m.

2. Review, discussion and possible approval of Investment Committee Minutes from March 30, 2011 and April 27, 2011.

Mr. Maguire asked the Committee if there were any questions about the minutes as distributed. Hearing none, he called for the motion

Recommendation 05-32-11	At 9:05 a.m.
Motion:	To approve the Minutes of April 27, 2011 as distributed.
Moved by:	Alan Maguire
Seconded by:	Richard Petrenka
Discussion:	
In Favor:	Unanimous
Motion Passes:	Passes

Recommendation 05-33-11	At 9:05 a.m.
Motion:	To submit the Minutes of March 30, 2011 for the record.
Moved by:	Lauren Kingry
Seconded by:	Richard Petrenka
Discussion:	
In Favor:	Unanimous
Motion Passes:	Passes

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

Mr. Stalder reported that for the month of April the portfolio was up 46 basis points over the benchmark. He said the notable contributor to that was the GTAA portfolio which is 430 basis points above benchmark. He said other notable items include the Absolute Return portfolio which was also positive and the Real Assets portfolio which was up 169 basis points over benchmark. However, the Credit Opportunities portfolio was a negative 58 basis points relative to the benchmark. He said that for the fiscal year-to-date the total fund is up 135 basis points over the benchmark. He said the notable contributors to that out performance were the GTAA, Absolute Return, Real Assets and Credit Opportunities portfolios, all of which out performed their benchmarks.

Mr. Petrenka asked with regard to the Credit Opportunities portfolio if there was anything trending or was the month of April just a low month. Mr. Stalder responded that it was just a one month event. Mr. Parham added that everything is performing to expectations and the managers who are active in that space continue to report that opportunities are migrating down the capital structure.

Mr. Maguire commented that the Committee now has new members and requested that for the next few months Staff remind the Trustees what their span of responsibility is within the Investment Department.

4. Presentation by Investment Department Staff, Albourne America LLC and representatives of Louis Dreyfus Investment Group (who may attend by phone), and discussion and possible **Recommendation** regarding a possible investment of up to $25 million in the LD Commodities Alpha Master Fund LTD or appropriate feeders, blockers, or associated or parallel funds of same.

Mr. Corens introduced himself to the committee and gave a brief overview of the Louis Dreyfus Commodities Alpha Fund. He said the Fund is a globally diversified commodities hedge fund that is being proposed for the commodities portion of the Real Assets portfolio. He said this Fund will be the first fund in the portfolio to solely target soft commodities. He said the Fund is a discretionary commodities trader focused on global agricultural market fundamentals. The team will generally target value-oriented direction trades, arbitrages, and inefficient pricing spreads and will focus on grains, rice, cotton, sugar, cocoa and citrus products along with the transportation and distribution of these commodities. He briefly described the Fund's strategy, investment team and organization. He said the Fund currently has $2 billion under management and is currently closed to new investors. However, Staff in conjunction with Albourne has been able to negotiate access to the fund as the Alpha Fund team rebalances their investor base. He said that it is anticipated that the commitment should be deployed over a 6 to 12 month period. He concluded by saying that the Staff and Albourne are recommending up to a $25 million commitment to the LD Commodities Alpha Master Fund LTD or appropriate feeders, blockers, or associated or parallel funds of same.

Mr. Lincoln Smith, Consultant with Albourne America introduced himself. He said Albourne has conducted extensive front and back office due diligence on the Fund and can support the recommended investment into it. He said this is a fundamental discretionary commodities fund. He said they use a bottom-up qualitative and quantitative fundamental approach based on internal research, various third party research and general market intelligence. He said the commodities market is very supply/demand driven. Louis Dreyfus is involved in all aspects of the supply chain and they therefore have a very deep understanding of the supply/demand dynamics. He said in choppy trading environments as we saw last year, this Fund was been able to produce solid returns and perform well. He said Albourne does think they have an edge and recommends the investment in this Fund.

Mr. Petrenka asked how many ways there are to invest with Louis Dreyfus. Mr. Smith responded that they do have some other funds but this is the main fund and the one that is tapping in to the bulk of their knowledge. Mr. Petrenka asked if all information available to Louis Dreyfus is available to this fund's managers. Mr. Smith responded that this is the investment arm of Louis Dreyfus and they get all the investment information the same as the proprietary traders within the Louis Dreyfus group.

Mr. Petrenka asked for further clarification on the Fund's terms.

Recommendation 05-34-11	At 9:30 a.m.
Motion:	To recommend to the full Board a possible investment of up to $25 million in the LD Commodities Alpha Master Fund LTD or appropriate feeders, blockers, or associated or parallel funds of same.
Moved by:	Richard Petrenka
Seconded by:	Lauren Kingry
Discussion:	
In Favor:	Unanimous
Motion Passes:	Passes

5. Presentation by Investment Department Staff, Albourne America LLC and Stark Investments representatives and discussion and possible **Recommendation** regarding a possible investment of up to $30 million in the Stark ABS Opportunities Fund or appropriate feeders, blockers, or associated or parallel funds of same.

Mr. Steed introduced himself to the Committee. He presented an overview of the Stark ABS Opportunities Fund offering which he said will compliment the Credit Opportunities portfolio. He said the Fund seeks an attractive rate of return, relative to the level of risk assumed, by investing in protection on mortgage-centric structured products using Credit Default Swaps (CDS). He said a CDS is a contract between two parties referencing a specific security as it has to do with securities' ability to pay principle and/or interest, much like an insurance policy. He said The Stark ABS Opportunities Ltd. fund buys CDS on Residential Mortgage Backed Securities (or RMBS). Residential mortgage loans are obligations of borrowers. The rate of defaults and losses on residential mortgage loans will be affected by a number of factors, including general economic conditions and those in the geographic region where the mortgaged property is located, the terms of the mortgage loan, the borrower's "equity" in the mortgaged property and the financial circumstances of the borrower. The mortgages can be bundled or "securitized" by the hundreds into one security, which investors refer to as a mortgage-backed security (MBS). He said the thesis here is that the Federal and State pressure on mortgage servicers not to foreclose on properties securing the payment obligation of borrowers has caused mortgage servicers' liquidation rates to slow beyond what would be expected given the breadth of the crisis. He said Investment Staff and Albourne believes there will be eventual losses to tranches of residential mortgage-backed securities when the servicers ultimately liquidate such properties. The team at Stark Investments will then seek to indentify RMBS that are 1) likely to experience a credit event within the next twelve to twenty-four months and where 2) the price of credit protection does not account for these defaults and can be acquired at an attractive cost. Given that the single-name CDS market is small and illiquid, the Stark team can leverage their proprietary network and knowledge to gain an informational advantage and exploit the arbitrage.

Mr. Steed said the Stark ABS fund compliments the Credit Opportunities Portfolio given the portfolio's current long exposure to RMBS and whole loans. He said that even though it is not a perfect hedge, structural headwinds for one manager may provide abundant opportunity for the other. He said that while the Staff recognizes the immense complexities of the U.S. residential market, the Staff believes the recommended commitment of $30 million is sized appropriately so as to mitigate downside losses.

Mr. Smith said that Albourne has not conducted back-office due diligence on this particular Fund but they are very aware of Stark's other funds and are very comfortable with Stark as an organization. He said that Albourne concurs with Staff that the investment has been sized correctly and it does fit in the Credit Opportunities portfolio. He said that from that perspective Albourne has no problem supporting the investment.

Mr. Petrenka asked if there is that much opportunity in this market to get it priced right. Mr. Steed responded that Staff raised this question with Stark. He said that in an efficient market this would have been identified quickly and the arbitrage would have been negotiated away. However, single name CDS on RMBS is not an efficient market as it is a very opaque and illiquid market. He said this Fund is very small and there are still some pockets of dislocation. He concluded by saying that Stark with their expertise should be able to capture some of the idiosyncratic opportunities.

Mr. Petrenka asked about the payment history of the counterparties. Mr. Steed responded that that is one of the two main risks, in that, any time you are dealing in CDS counterparty risk, there is a material risk that has to be recognized because the performance of the Fund is based upon that counterparty paying out the insurance. He said Starke's counterparties are the larger banks including: JP Morgan, Goldman Sachs and Deutche. Mr. Smith added that Stark has the ability to pick and chose the CDS deals they go into and part of that selection process is dependent on who the counterparties are.

Recommendation 05-35-11	At 9:46 a.m.
Motion:	To recommend to the full Board a possible investment of up to $30 million in the Stark ABS Opportunities Fund or appropriate feeders, blockers, or associated or parallel funds of same.
Moved by:	Richard Petrenka
Seconded by:	Lauren Kingry
Discussion:	
In Favor:	Unanimous
Motion Passes:	Passes

6. Presentation by Investment Department Staff and StepStone Group and discussion and possible **Recommendation** regarding a possible investment of up to $20 million in the Pátria – Brazilian Private Equity Fund IV, L.P. or appropriate feeders, blockers, or associated or parallel funds of same managed by Pátria Investimentos S.A.

Mr. Chen introduced himself and then presented a brief overview of the Pátria – Brazilian Private Equity Fund IV, L.P. which is a Brazil-focused, mid-market, equity growth fund. He said that the Staff is recommending a $20 million investment in the Fund. He said Staff has done due diligence on many emerging market private equity funds, especially those in the BRIC countries, since the beginning of the year and that the Staff believes it is crucial for the System to continue to diversify the portfolio globally and capture returns from the emerging markets while managing the risk. He said Staff likes the fundamentals of the Brazilian economy, especially their abundant natural resources and growing middle class. He said Patria was selected because they have demonstrated operating skill and they have a good reputation in Brazil, coupled with a strong team and good track record. He said both StepStone and Albourne conducted due diligence on Patria and have confidence in this group.

Mr. Rose, Partner and Mr. Fernandez, Founding Partner with StepStone Group introduced themselves. Mr. Fernandez gave a brief overview of the due diligence that StepStone has conducted in Brazil and stated that they have found Patria to be the best opportunity in the market. He said one of the reasons for their conclusion is that Patria has the largest team in Brazil. They also have a very long tenure in Brazil and have been investing in private equity there since 1994. He said they have created a very strong internal culture that has prevented turnover of their investment professionals. He said the investment professionals are supported by an administrative team that includes accountants, legal and back office personnel who support the entire Patria platform.

Mr. Fernandez said that Patria has a very disciplined approach and focuses on buy and build opportunities where they take control of a company so that they can achieve meaningful change and drive that change. He said they always place at least one full-time person with the operating company at the CFO or Director level so that they are “guarding the purse”. He said Patria has raised three previous funds, two of which have ranked in the top quartile of their respective vintage years when compared to U.S. buyouts of the same vintage. He said only two of Patria’s investments have lost capital and these investments were made 12 and 14 years ago when Patria was a much younger firm and Brazil’s macroeconomic issues were more of a concern than they are today. He said StepStone believes that they have learned through those investments and that their disciplined approach is why they haven’t lost any capital since 1999. He said Patria has the best track record in Brazil among all private equity investors who have made more than 4 investments in Brazil. He said with respect to their structure that Blackstone recently purchased a 40% stake in Patria’s management company and StepStone conducted extensive due diligence on this transaction and believe it to be a net positive for the Firm as they get access to all of Blackstone’s training programs for their personnel, the capital received is all being reinvested into the Patria platform, and as the Patria partners explained, this was a way for them to unlock the value of the platform they have built and put that money to work back into their platform because they believe the can earn better returns for the investments they are going to make over the next 5 to 10 years than the original increase in value that the platform would have.

Mr. Petrenka asked if their approach is opportunistic or if they are trying to diversify across industries versus where the Brazil economy is now. Mr. Fernandez responded by sayingthat what is really attractive in emerging markets, and in Brazil in particular, is the opportunity to take advantage of the growth of the middle class and identifying the sectors that will prosper because of that like: health care, education, and lower end consumer goods. He said they are not opportunistic in the sense of taking advantage of something that presents itself. They examine a sector for at least a year before they make an investment and are very thoughtful about which sectors they should be looking at, given the demographics and growth of the middle class.

Recommendation 05-36-11	At 10:09 a.m.
Motion:	To recommend to the full Board a possible investment of up to $20 million in the Pátria – Brazilian Private Equity Fund IV, L.P. or appropriate feeders, blockers, or associated or parallel funds of same managed by Pátria Investimentos S.A..
Moved by:	Richard Petrenka
Seconded by:	Lauren Kingry
Discussion:	
In Favor:	Unanimous
Motion Passes:	Passes

7. Report by NEPC representative(s) on the Third Fiscal Quarter (First Calendar Quarter) Performance of the System.

Mr. Martin referred to the document, Investment Performance Analysis through March 31, 2011, that was included in the material distributed to the Trustees. He said that this report covers information through March 31. He gave a brief overview of the current economic environment and NEPC's observations and expectations for opportunities. He presented the report and discussed the analysis contained in the report with the Committee.

Mr. Petrenka asked what Mr. Martin sees happening with Real Estate. Mr. Martin responded that it will be a trade-off between people who have been burned badly who do not want to return to real estate even though this is the very time when it is most attractive to return. He said there will probably be funds that never go back to the 10% to 12% they had allocated to real estate. NEPC thinks the median public fund will probably be 6% to 8% in Real Estate. He said as this overhang progresses through there will be opportunities and those public funds that have more nimbleness will be able to take advantage of those opportunities.

Mr. Petrenka asked, with regard to rebalancing, if there is a particular time period in which to reevaluate. Mr. Martin responded that there is a lot of discussion on that point. He said there are some funds that have very small ranges and once the fund is out of range, staff is instructed to move back to target. There are some advocates for larger ranges where the staff has more freedom to make the call and add value or not. There are managers that can be hired to make that call. He said there is a lot of debate on this topic and a lot of it is reflective of the philosophy of the Board. If the ranges are wide, staff has significant latitude; but if the ranges are narrow then the staff will lack latidude.

8. Report by the System's Compliance Auditor and discussion regarding investment compliance, holdings and transactions as of April 30, 2011.

No report was given.

9. Report by Investment Department Staff and/or legal counsel, and discussion by them with the Committee (and possible recommendation by the Committee to the Board of Trustees) about recent legal developments and issues (including settlement discussions) involving the investments of the Arizona PSPRS Trust, the System or the System's sister plans (EORP or CORP) (collectively, the "Plans"). Such discussion (and recommendations) may include legal issues (and disputes involving) the Plans' custodians, lenders, securities lending agents, investment contracts, vendors, advisors, investment managers or joint venturers (as well as any investments managed by the Plans' investment managers or joint venturers). The Committee may vote to discuss these

matters in Executive Session pursuant to A.R.S. §§ 38-431.03(A)(2),(3),(4) and (7), as set forth in item 10. (**Estimated time: 5 minutes; 10:53 – 11:03 a.m.)**

No report was given.

10. **Executive Session for Legal Matters.** Discussion with legal counsel (and possible recommendation to the Board of Trustees) about legal developments and issues (including settlement discussions) involving the Plans' investments, including legal matters concerning the Plans' custodians, lenders, securities lending agents, investment contracts, vendors, advisors, investment managers or joint venturers (as well as any investments managed by the Plans' investment managers or joint venturers). 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)(2),(3),(4) and (7). (**Estimated time: 5 minutes; 11:03 – 11:08 p.m.)**

An Executive session was not convened.

3. Call to the Public

No members of the public came forward to speak.

4. Schedule next meeting

The next Investment Committee meeting was scheduled for June 29, 2011 at 10:00 a.m. It was noted that the June meeting date is on the agenda for the afternoon Board meeting and that it is contemplated that the June 29 meeting will be rescheduled to another date. The Committee agreed to meet on the date the Board decides to hold the June meeting.

5. Adjournment

Recommendation 04-37-11	At 10:54 a.m.
Recommendation:	To adjourn
Moved by:	Richard Petrenka
Seconded by:	Lauren Kingry
Discussion:	
In Favor:	Unanimous
Motion Passes:	Passes

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Mr. Alan Maguire, Chair, Trustee, Mr. Richard Petrenka, Trustee

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Mr. Lauren Kingry, Trustee