

State of Rhode Island and Providence Plantations

STATE INVESTMENT COMMISSION

Monthly Meeting October 27, 2010

A State Investment Commission (SIC) meeting was held in Room 135, State House, Providence, Rhode Island on Wednesday, October 27, 2010. Mr. Dingley (designee for General Treasurer Frank Caprio) called the meeting to order at 9:08 a.m.

Membership Roll Call. Present were: Ms. Rosemary Booth Gallogly, Mr. Michael Costello, Mr. Thomas Fay, Mr. Robert Gaudreau, Mr. Robert Giudici, Mr. Andrew Reilly and Mr. Mark Dingley (designee for General Treasurer Frank Caprio) establishing a quorum. Also present were: Ms. Sally Dowling, of Adler Pollock, & Sheehan, and Mr. Michael Murphy, of Rodio & Ursillo, Legal Counsel to the Commission; Mr. Allan Emkin and Mr. John Burns of Pension Consulting Alliance (PCA), General Policy Consultant to the Commission; Mr. Scott Reining of Pacific Corporate Group, Ms. Lisa Tyrrell and Mr. Nicholas Katsikis of State Street Corporation and members of the Treasurer's staff. Dr. Robert McKenna and Ms. Marcia Reback were not present.

State Investment Commission Minutes. Mr. Dingley (designee for General Treasurer Caprio) entertained a motion for approval of the minutes for the meeting of September 22, 2010. Ms. Booth Gallogly

moved, Mr. Reilly seconded, and the subsequent motion passed. The following members voted in favor: Ms. Booth Gallogly, Mr. Costello, Mr. Fay, Mr. Gaudreau, Mr. Giudici, Mr. Reilly and Mr. Dingley (designee for General Treasurer Frank Caprio).

VOTED: To approve the Minutes of the September 22, 2010 monthly meeting.

General Consultant Report. Mr. Burns asked the group to turn to the PCA handout Investment Market Risk Metrics – October 2010. He stated that risk is a topic PCA will be addressing on a regular basis going forward. He reviewed the report summary, the highlights of significant items and a matrix in the report. He commented that the yield curve slope is at a very unusual position and interest rate risk is at an unusual position relative to history. He also pointed out that typically PCA will perform capital market assumptions annually in January, however, at mid-year they lowered the expected return estimate for fixed income. The 10-year duration for Treasury Bonds is as high as it has ever been which is a function of interest rates being so low. If interest rates spike up 100 basis points, the principal is reduced by 8.7%. The 10 year is only one bond; nevertheless it demonstrates the risk potential in the current market.

Mr. Fay asked what the change was in the rate of return estimate for fixed income.

Mr. Burns stated it went from 4 to 3.

The board members discussed the Rhode Island TIPS allocation relative to the existing perilous environment.

Ms. Booth Gallogly asked about the security of the fund's TIPS allocation.

Mr. Goodreau commented that the Rhode Island TIPS portfolio is safe. In the future scaling out of TIPS may be a consideration.

Ms. Booth Gallogly asked if fixed income managers are doing anything to mitigate risk.

Mr. Goodreau replied that our managers will not protect us from this type of risk. The manager's mandate is to be 95% invested.

Mr. Fay commented that in the current environment we are still in a position where deflation and the issues associated with it are compelling. Therefore, care with structuring the portfolio in the near term is vital.

Short-term Investments. Mr. Dingley stated that at the last meeting Mr. Izzo and Mr. Marr introduced the topic of a Local Government Investment Pool (LGIP). There is a handout with additional information on this matter in the material packet.

Ms. Booth Gallogly commented that this is a great idea. Due to issues that occurred in the fall of 2008, she would like to see language that assures the State is not taking responsibility for other entities' deposits.

Mr. Izzo stated that the same level of safety will apply to the LGIP as any other short-term investment.

Legal Counsel Report. Legal Counsel had no report.

Selection of Custodian for Rhode Island OPEB System. Mr. Dingley introduced the topic of selection of a custodian for the Rhode Island Other Post Employment Benefits (OPEB) System. OPEB is a mechanism to finance the state's retiree health benefits. He stated a copy of the legislation that established OPEB and its 2011 funding, as well as a draft copy of the OPEB Trust, are in the material packet.

Mr. Dingley explained that the OPEB system is like the judicial or municipal retirement plans that have separate trusts. The OPEB Trust would be put together with our existing funds solely for investment purposes and would utilize the custodial services of State Street.

The group discussed various aspects of the topic including: funding, cash flow, actuarial impact and SIC policy.

Mr. Costello asked if the funds are co-mingled.

Mr. Dingley explained that the funds would be co-mingled for investment purposes only but the earnings and liabilities are separate just like the municipal employees fund that is currently co-mingled.

Ms. Booth Gallogly commented that this issue has been worked on for several years and recommends approval by the board.

Mr. Giudici asked if there are liquidity issues on a short-term basis.

Mr. Izzo stated that liquidity issues are not a concern.

Mr. Costello stated that he conceptually agrees with the measure but would like to see a separate policy statement for OPEB that would be reviewed annually.

Mr. Dingley (designee for General Treasurer Caprio) entertained a

motion to approve the OPEB Trust using the SIC custodial relationship, subject to the adoption of appropriate investment policies and guidelines by the SIC for the OPEB Trust. Mr. Costello moved, Ms. Booth Gallogly seconded and the subsequent motion passed.

The following members voted in favor: Ms. Booth Gallogly, Mr. Costello, Mr. Fay, Mr. Gaudreau, Mr. Giudici, Mr. Reilly and Mr. Dingley (designee for General Treasurer Caprio).

VOTED: To approve the OPEB Trust using the SIC custodial relationship subject to adoption of appropriate investment policies and guidelines by the SIC for the OPEB Trust.

Chief Investment Officer Report. Mr. Goodreau had no report.

Treasurer's Report. Treasurer Caprio had no report.

New Business. There was no new business.

There being no new business, Mr. Dingley (designee for General Treasurer Caprio) entertained a motion to adjourn. Ms. Booth Gallogly moved, Mr. Gaudreau seconded and the subsequent motion passed. The following members voted in favor: Ms. Booth Gallogly, Mr. Costello, Mr. Fay, Mr. Gaudreau, Mr. Giudici, Mr. Reilly and Mr. Dingley (designee for General Treasurer Caprio).

VOTED: To adjourn the meeting.

There being no further business, the meeting was adjourned at 9:54 a.m.

Respectfully submitted,

**Frank T. Caprio
General Treasurer**