

MINUTES OF THE REGULAR BOARD MEETING OF THE
BOARD OF TRUSTEES OF THE EMPLOYEES' RETIREMENT SYSTEM (ERS)

MARCH 10, 2014

CITY FINANCIAL TOWER
201 MERCHANT STREET, SUITE 1200
HONOLULU, HAWAII 96813

Trustees present: Ms. Piliialoha Lee Loy, Chair
Mr. Vincent Barfield, Vice Chair
Ms. Jackie Ferguson-Miyamoto
Mr. Patrick Frane
Mr. Colbert Matsumoto
Mr. Emmit Kane
Mr. Kalbert Young

Trustee excused: Mr. Jerome Rauckhorst

Staff present: Mr. Wesley Machida, Executive Director
Ms. Kanoe Margol, Deputy Executive Director
Mr. Vijoy Chattergy, Chief Investment Officer
Mr. Aaron Au, Investment Officer
Mr. Anthony Goo, Investment Officer
Mr. Karl Kaneshiro, Benefits Manager
Ms. Donna Curry, Program Specialist
Ms. Gerri Konishi, Member Home Loan Assistant
Ms. Jaime Hirata, Recording Secretary
Ms. Raechele Joyo, Secretary
Ms. Wanda Kugiya, Secretary

Attorneys present: Mr. Brian Aburano, Deputy Attorney General (Counsel for the Board)
Ms. Elmira Tsang, Deputy Attorney General (Counsel for ERS staff)

Guests present: Mr. Guy Holappa) Bank of New York Mellon
Mr. Bruce Shain

Mr. Martin Hegarty) BlackRock, Inc.
Mr. Kevin O'Donnell

Mr. Graham Allen) Bradford and Marzec, LLC
Ms. Heather Creeden
Ms. Zelda Marzec

Mr. Michael Humphrey) Courtland Partners, Ltd.
(via conference call)

Mr. John Linder) Pension Consulting Alliance, Inc.
Mr. Neil Rue

Mr. Benjamin Sadoski) UNITE HERE! Local 5 Hawaii

QUORUM/CALL TO ORDER

A quorum being present, Chair Lee Loy, called the regular meeting of the Board of Trustees (Board) of the Employees' Retirement System (ERS), to order at 11:34 a.m.

APPROVAL OF MINUTES
– JANUARY 13, 2014

On a motion made by Trustee Ferguson-Miyamoto, seconded by Trustee Frane, and unanimously carried, the Board approved the minutes of its January 13, 2014 meeting.

PRESENTATION BY BANK OF NEW
YORK MELLON ON CUSTODIAL
BANK UPDATE

Mr. Guy Holappa and Mr. Bruce Shain of Bank of New York Mellon (BNY Mellon), ERS' custodial bank, provided a presentation and update of BNY Mellons' services.

(The Executive Director and Ms. Curry left the meeting.)

PRESENTATION BY BRADFORD
AND MARZEC, LLC ON THE
PERFORMANCE OF THE
EMPLOYEES' RETIREMENT
SYSTEM'S FIXED INCOME
INVESTMENT PORTFOLIO

Mr. Graham Allen and Ms. Zelda Marzec of Bradford and Marzec, LLC (Bradford and Marzec), ERS' fixed income manager, introduced Bradford and Marzec's newest hire, Ms. Heather Creeden, senior portfolio manager. Ms. Creeden reported on her work experience and new role with Bradford and Marzec. Mr. Allen, Ms. Marzec, and Ms. Creeden provided a presentation on the performance of the ERS' fixed income investment portfolio managed by Bradford and Marzec for the ERS, as well as an update on their firm's recent organizational changes.

Mr. Vijoy Chattergy, ERS Chief Investment Officer (CIO), noted that Bradford and Marzec will be meeting with ERS Investment staff for a due diligence site inspection later in the week in their Los Angeles offices. A due diligence report will be presented to the Board in the near future.

There being no further discussion, the representatives from Bradford and Marzec left the meeting.

PRESENTATION BY BLACKROCK,
INC. ON THE PERFORMANCE OF
THE EMPLOYEES' RETIREMENT
SYSTEM'S GLOBAL INFLATION-
LINKED BOND INVESTMENT
PORTFOLIO

Mr. Martin Hegarty and Mr. Kevin O'Donnell of BlackRock, Inc. (BlackRock) provided a presentation on the performance of the ERS' global inflation-linked bond investment portfolio managed by BlackRock for the ERS. Highlights included:

- The portfolio posted 67 basis points of alpha (gross-of-fee) against the Barclays World Government Inflation-linked Bond Index (USD Hedged) in 2013 and 77 basis points since inception.
- The sector allocation of the portfolio at the end of January 2014 was primarily in US, UK, and Euro block inflation linked bonds, approximately 89%.
- Active duration management has contributed to the portfolio for real US and Euro bonds and nominal Euro bonds; however, active duration management detracted from performance for nominal US and real UK bonds.

(Trustee Matsumoto joined the meeting.)

(Ms. Curry returned to the meeting.)

(Mr. Sadoski left the meeting.)

(The Executive Director returned to the meeting.)

ENTER EXECUTIVE SESSION

On a motion made by Trustee Ferguson-Miyamoto, seconded by Trustee Frane, an unanimously carried, the Board entered executive session to:

- Pursuant to HRS § 92-5(a)(4), to consult with the Employees' Retirement System's attorneys on questions and issues pertaining to the Employees' Retirement System's powers, duties, privileges, immunities and liabilities with respect to legislative proposals affecting the Employees' Retirement System.
- Pursuant to HRS § 92-5(a)(4) and (8), to consult with the Board's attorneys on questions and issues pertaining to the Board's powers, duties, privileges, immunities, and liabilities regarding member, retirant, and/or beneficiary requests for waiver of overpayment under HRS § 88-106; appropriate action.

EXECUTIVE SESSION TO CONSULT WITH THE EMPLOYEES' RETIREMENT SYSTEM'S ATTORNEYS ON QUESTIONS AND ISSUES PERTAINING TO THE EMPLOYEES' RETIREMENT SYSTEM'S POWERS, DUTIES, PRIVILEGES, IMMUNITIES AND LIABILITIES WITH RESPECT TO LEGISLATIVE PROPOSALS AFFECTING THE EMPLOYEES' RETIREMENT SYSTEM

EXECUTIVE SESSION TO CONSULT WITH THE BOARD'S ATTORNEYS ON QUESTIONS AND ISSUES PERTAINING TO THE BOARD'S POWERS, DUTIES, PRIVILEGES, IMMUNITIES, AND LIABILITIES REGARDING MEMBER, RETIRANT, AND/OR BENEFICARY REQUESTS FOR WAIVER OF OVERPAYMENT UNDER HRS § 88-106; APPROPRIATE ACTION

EXIT EXECUTIVE SESSION

On a motion made by Trustee Ferguson-Miyamoto, seconded by Trustee Kane, and unanimously carried, the Board exited executive session.

(The Executive Director and Ms. Curry left the meeting.)

PRESENTATION BY COURTLAND
PARTNERS, LTD. ON THE
PERFORMANCE OF THE
EMPLOYEES' RETIREMENT
SYSTEM'S REAL ESTATE
INVESTMENT PORTFOLIO FOR 3RD
QUARTER 2013

Mr. Michael Humphrey of Courtland Partners, Ltd. (Courtland Partners), ERS' real estate investment consultant, via conference call, provided a presentation on the overall performance of the ERS' real estate investment portfolio for third quarter 2013. Highlights included:

- Portfolio market value of \$897,108,768 for the period ended September 30, 2013.
- Outperformed the quarter and year to date benchmarks for the National Council of Real Estate Investment Fiduciaries (NCREIF) Property Index by 0.1% and 4.7% respectively.
- Total number of current investments: 18.
- 2.5% total net return for the quarter; 11.7% year to date.
- 7.3% internal rate of return for total portfolio.
- Current portfolio is 6.9% of total plan assets (versus 7.0% target allocation).
- Total portfolio leverage is 34.6%.

Mr. Humphrey noted that the portfolio was relatively overweight in residential (34.7%). With recent commitments to a number of new managers, the potential exposure to ERS' core managers, Heitman Capital Management and Invesco Real Estate, is forecast to fall to approximately 58.7% of the total portfolio.

ENTER EXECUTIVE SESSION

On a motion made by Trustee Ferguson-Miyamoto, seconded by Trustee Matsumoto, and unanimously carried, the Board entered executive session:

- Pursuant to HRS § 92-5(a)(8), to consider a report from Pension Consulting Alliance, Inc. regarding a survey and review of investment fees.
- Pursuant to HRS § 92-5(a)(8), to consider a report regarding Hu Honua Bioenergy LLC.
- To approve executive session minutes of the January 13, 2014 meeting.

EXECUTIVE SESSION TO
CONSIDER A REPORT FROM
PENSION CONSULTING ALLIANCE,
INC. REGARDING A SURVEY AND
REVIEW OF INVESTMENT FEES

EXECUTIVE SESSION TO
CONSIDER A REPORT REGARDING
HU HONUA BIOENERGY LLC

APPROVAL OF EXECUTIVE
SESSION MINUTES
– JANUARY 13, 2014

EXIT EXECUTIVE SESSION

On a motion made by Trustee Matsumoto, seconded by Trustee Ferguson-Miyamoto, and unanimously carried, the Board exited from executive session.

PARTICIPATORY NOTES (P-NOTES)
INVESTMENT POLICY

The CIO and Pension Consulting Alliance, Inc. (PCA) recommended that the Board should consider and review policy language to include the use of exchange-traded notes (ETNs) and promissory notes (P-notes) as allowable investments in Section C.3.A of the ERS' *Investment Policy, Guidelines, & Procedures Manual*.

On a motion made by Trustee Matsumoto, seconded by Trustee Kane, and unanimously carried, the Board approved the CIO's and PCA's recommended change to Section C.3.A of the ERS' *Investment Policy, Guidelines, & Procedures Manual* to include the use of ETNs and P-notes as allowable investments.

GLOBAL INFLATION LINKED
SECURITIES (GILS) CREDIT
RATINGS INVESTMENT POLICY

The CIO and PCA recommended that the Board should consider allowing the global inflation-linked securities (GILS) manager to allow a treasury/sovereign-issued security to be rated by no less than one Nationally Recognized Statistical Rating Organizations (NSROs), instead of a minimum of two NSROs because there several current and prospective holdings from well-regarded issuers of non-U.S. sovereign bonds (such as Japan and Italy) that are rated by only one NSRO, and in many cases the NSRO rating the bonds have rated the bonds to be of investment-grade quality. The CIO and PCA proposed revised policy language for Section C.3.F.(1) of the ERS' *Investment Policy, Guidelines, & Procedures Manual* to effectuate this change. The proposed change would impact only the GILS manager, who invests largely in bonds sponsored by sovereign governments, and would allow the GILS manager to have a much broader selection of bonds.

On a motion made by Trustee Barfield, seconded by Trustee Matsumoto and unanimously carried, the Board adopted the CIO's and PCA's proposed change to Section C.3.F.(1) of the ERS' *Investment Policy, Guidelines, & Procedures Manual* to allow treasury/sovereign-issued securities to be rated by "one or more" NSRO instead of by "two or more" NSRO.

REPORTS BY TRUSTEES
APPOINTED TO MEET WITH
REPRESENTATIVES OF BRADFORD
AND MARZEC, LLC AND LOOMIS,
SAYLES AND COMPANY, L.P.

The CIO reported on the trustees' meeting with representatives of Bradford and Marzec. The Board placed Bradford and Marzec on "Watch List" status as of February 10, 2014 due to the departure of three out of seventeen senior investment professionals, all of which specialized in credit strategies. The trustees met with the representatives to gain a better understanding of the effects of the recent organizational changes at Bradford and Marzec and to gauge the potential impact these changes could have on the ERS' fixed income portfolio managed by that firm.

The CIO also reported on the trustees' meeting with fixed income manager, Loomis Sayles & Company, as part of the ERS' review of its fixed income allocation. This review is part of an overall strategic review related to the implementation of risk based asset allocation targets.

REPORT BY TRUSTEES
APPOINTED TO ATTEND THE
CHARTERED FINANCIAL
ANALYST (CFA) SOCIETY HAWAII
9TH ANNUAL ECONOMIC
FORECAST

The CIO reported on the trustees' attendance of the Chartered Financial Analyst (CFA) Society Hawaii 9th Annual Economic Forecast that was held on March 4, 2014. The trustees attended this educational function to learn about trends and market developments from investment professionals, to help them better understand investment opportunities and manage the investment portfolio of the ERS, and to address concerns such as the unfunded liability.

OPERATIONS REPORT
– FEBRUARY 2014

Ms. Kanoe Margol, ERS Deputy Executive Director, presented the monthly update on ERS operations and ERS website statistics (top 10 viewed pages) for February 2014. Highlights included:

- 30 ERS members attended the ERS' second "Brown Bag Information Session" for new and mid-career employees during their lunch hour. A survey indicated positive comments on the information that was presented and the question and answer session.
- Update on the status of the ERS' operating expense budget as of January 31, 2014; ERS staff will continue to provide the Board with a monthly update on the operating expense budget.
- Top ten viewed web pages of the ERS' website included the benefits calculator - still holding at number one since October 2013.

NEXT BOARD MEETING
– MARCH 17, 2014

Chair Lee Loy announced that the next Board meeting is scheduled for March 17, 2014 (special Board meeting).

ADJOURNMENT

On a motion made by Trustee Barfield, seconded by Trustee Ferguson-Miyamoto, and unanimously carried, Chair Lee Loy adjourned the meeting at 1:58 p.m.

**REDACTED
SIGNATURE**

Wesley K. Machida
Executive Director

WKM: jh