

Minutes of the Annual Meeting

Held January 12, 2011 at 11:30 AM* in the State Museum Auditorium

205 West State Street, Trenton, New Jersey

*** 2 hour delay due to inclement weather**

Council Members in Attendance:

Robert Grady, chair

Nicholas Caprio, vice chair

Jeffrey Oram

Andrew Michael Greaney

Timothy McGuckin

James P. Marketti

Richard Klockner

Guy Haselmann

Brendan Thomas Byrne, Jr.

Orin Kramer

Council Members Not in Attendance:

James C. Kellogg*

Marty Barrett*

**please note that there were technical difficulties establishing a conference call connection and these members were not able to participate in the meeting.*

The Regular Meeting was called to order by Chair Grady at 11:40 am.

Roll Call and Meeting Notice

Chair Grady thanked all of the Council members and public attendees for braving the inclement weather. Secretary Adams performed roll call and reported that notice of the Regular Meeting scheduled for January 12, 2011 was sent by mail deposited in the post office, by facsimile and email on December 28, 2010. A copy of the notice was posted in the Division on December 28, 2010, mailed to the Council, Times of Trenton, Star-Ledger, Bergen Record, and Courier Post on December 28, 2010 and filed with the Secretary of State on December 28, 2010. Chair Grady also introduced Chris McDonough to the Council. Mr. McDonough was appointed as Deputy Director for the Division of Investment.

Report from the Division of Pensions and Benefits

John Megariotis, Deputy Director, presented the report from the Division of Pensions and Benefits. He stated that there are roughly 270,000 retirees, comprised of both state and local employees, in the system receiving benefit payments as of December 2010. The payroll for the month of December was approximately \$642 million. The annual payroll is about \$7.7 billion. At the end of FY2010, the annual payroll was \$7.1 billion with 258,000 retirees. Chair Grady asked Mr. Megariotis for an estimate on when retiree payouts will peak, both in terms of number of retirees and payroll. Mr. Megariotis did not have that information available. Council Member Kramer asked about the assumptions and estimates used by the Division and the outlook for the pension system. Mr. Megariotis said that over the next five years, the benefit payroll could be roughly \$9-\$9.5 billion; however, that figure is predicated on a number of factors. Chair Grady asked Mr. Megariotis to provide a letter to the Council regarding the outlook for the pension system. Mr. Megariotis said that the unfunded pension liability according to the actuarial report has grown to \$53 billion, an increase from the June 2010 estimate of \$45 billion. Mr. Megariotis

stated that the funding ratio for State participants is 56.4% for Fiscal Year 2010, down from 62% for Fiscal Year 2009. The funding ratio for local participants in Fiscal Year 2010 is 70.4%, down from 72.1% in Fiscal Year 2009. Council Member Marketti asked Mr. Megariotis for the total unfunded liability. The total unfunded liability of \$53.8 billion is based on \$87.8 billion in actuarial assets versus \$141.8 billion in total accrued liability. This information was based on June 2010 numbers.

Economic Overview by ISI Group

Ed Hyman, Chairman and Founder of ISI Group, made a presentation on the economy and investment outlook. Mr. Hyman has been ranked as the #1 Wall Street economist by *Institutional Investor* for the past 31 years. He said that there are three watershed events ahead: the economy's movement from recovery into expansion; Federal Reserve's unprecedented move to embark on a new round of quantitative easing (QE2); and Obama's move toward the center in order to embrace business. Half of the world's GDP is represented by emerging economies and provide a new force to the world economy. The biggest risk to the economy is the Euro zone. The second largest problem is inflation in the emerging economies. The third problem is the state and local budget issues. Chair Grady asked Mr. Hyman about the risks vs. benefits of quantitative easing and commented that the market has been up 15% since QE2 but that such substantial easing contributed to inflation risk over the long-term. Council Member Byrne asked Mr. Hyman about demographic trends and Chair Grady asked Mr. Hyman to comment on the outlook for domestic equity markets.

Report from the Division of Investment

Division Director Tim Walsh and Pete Keliuotis of Strategic Investment Solutions made a presentation to the Council on risk, diversification and the performance of the pension fund. A copy of the presentation is on file in the Division and published on the Division's website. Chair Grady outlined the mission of the Council to provide investment policy oversight to the Division and to ensure transparency in the state's investment processes. He also stated that the mission of the Division is to maximize risk-adjusted returns while maintaining the highest fiduciary standards. Chair Grady emphasized that neither the Council nor the Division is involved with the funding level or the actuarial assumptions made in relation to the pension fund.

Director Walsh presented the Council with a comparison of the Division's asset allocation versus peer plans, during which Chair Grady pointed out that the Division is underweight in domestic equities relative to its peers. Mr. Keliuotis discussed the different types of risk and how to hedge these risks through asset allocation policy. Director Walsh discussed the use of benchmarks and the use of asset allocation ranges. He also discussed 2011 initiatives for the Division, including the need for technological updates and potential organizational and programmatic changes. Director Walsh provided an overview of the pension fund performance to the Council. Chair Grady noted that the pension performance for fiscal year 2010 was up 13.45%, and commented that the performance gains made by the Division were greater than the benefit payments taken out of the fund during the fiscal year.

Opportunity for Public Comment

Chair Grady advised the Council that there were seven registered commenters and that if time had run out, the remainder of the comments would be heard at the end of the regular meeting, but that he would seek to allow all who wished to comment to do so.

(Secretary's note: There were many unregistered commenters who did not identify themselves.)

Twenty-two members of the public made comments to the Council. These comments focused on the funding level of the pension fund, the security of future pension payments, apprehension about risky investment vehicles, concerns about transparency and fees, and the proposed regulatory changes to raise alternative investment allocation ceilings.

Mr. Anthony Mishkowsky presented the Council with copies of the CWA's response to the proposed regulatory changes.

Chair Grady thanked the commenters for their input and detail. He stated that all of the Council members are mindful of their duty to the beneficiaries of the pension systems and reiterated that the Council does not have any input in determining the level of pension funding contributed by the State, as this is a decision of the Legislature and the Governor. Chair Grady stated that the Division and Council are highly transparent in terms of fees. Director Walsh estimated that roughly \$150 million in fees have been paid out, not only in alternative investment fees, but for brokerage and other related fees as well. Director Walsh stated that the Division is one of the most transparent funds in terms of disclosure. Chair Grady objected to the idea that the Council and the Division were chasing undue risk in an effort to make up the shortfall caused by underfunding. The Division and Council, he stated, are seeking to optimize portfolio construction to maximize return and mitigate risk, with full transparency and an optimized and diversified portfolio. Certain asset classes, he stated, were attractive not because they promised higher yields in absolute terms but because they were uncorrelated with other asset classes, thus providing the pension fund with enhanced downside protection in certain market scenarios. The Chairman stated that the goal of maximizing risk-adjusted returns would be the same if the pension was overfunded, underfunded or if the assets and liabilities matched.

Council Member Byrne commented that the pension fund did 5% better in FY 2010 than the actuarial assumption. He stated that these gains were generated by the hard work and dedication of State employees. He also commented on the pension fund and the efforts of the Division and the Council to keep the pension fund optimized for all beneficiaries.


Council Member Marketti stated his intent to enter a motion at the Regular Meeting for the Council to go on record encouraging the Governor and Legislature to fund the pension system; the motion was debated, however, Mr. Marketti then withdrew the motion until a later date.

Adjournment of Meeting

Chair Grady advised the Council that there would be a short break prior to the start of the Council's scheduled Regular Meeting.

The meeting was adjourned at 2:26 PM.

Respectfully submitted,



Kaitlyn J. Adams
Secretary to the Council