



ND STATE INVESTMENT BOARD MEETING

Friday, March 22, 2013, 8:30 a.m.
Workforce Safety & Insurance
1600 E Century, Bismarck, ND

REVISED AGENDA

- I. **CALL TO ORDER AND ACCEPTANCE OF AGENDA**
- II. **ACCEPTANCE OF MINUTES (February 22, 2013)**
- III. **EDUCATION**
 - A. Risk Factor Asset Allocation - Mr. Schulz (to follow) (45 min)
- IV. **GOVERNANCE**
 - A. Administration
 - 1. Search Committee Update - Search Committee (Enclosure)
 - 2. Interim Executive Director & Interim CIO Annual Review Committee (10 min)
 - 3. Audit Committee Liaison Report - Mr. Gessner (Enclosure) (5 min)
- V. **LEGISLATIVE UPDATE** - Mr. Schulz, Ms. Flanagan (Enclosure) (15 min)
- VI. **INVESTMENTS (Moved to Address Later on the Agenda)**
 - A. "Watch List" Discussion (Enclosure) (30 min) - Mr. Schulz
 - B. Bank of North Dakota (to follow) - Mr. Schulz
Possible Executive Session for Attorney Consultation
N.D.C.C. §44-04-19.1(2), N.D.C.C. §44-04-19.1(5) and N.D.C.C. §44-04-19.2
- VII. **OTHER**

Next Meetings:
SIB meeting - April 26, 2013, 8:30 a.m. - Workforce Safety & Insurance
SIB Audit Committee meeting - May 17, 2013, 1:00 p.m. - State Capitol Peace Garden Room
- VIII. **ADJOURNMENT**

**NORTH DAKOTA STATE INVESTMENT BOARD
MINUTES OF THE
FEBRUARY 22, 2013, BOARD MEETING**

BOARD MEMBERS PRESENT: Drew Wrigley, Lt. Governor, Chair
Mike Sandal, Vice Chair
Levi Erdmann, PERS Board
Kim Franz, TFFR Board
Lance Gaebe, Land Commissioner
Mike Gessner, TFFR Board
Adam Hamm, Insurance Commissioner
Howard Sage, PERS Board
Kelly Schmidt, State Treasurer
Cindy Ternes, Workforce Safety & Insurance
Bob Toso, TFFR Board

STAFF PRESENT: Connie Flanagan, Fiscal & Investment Officer
Bonnie Heit, Office Manager
Fay Kopp, Interim Executive Director
Leslie Moszer, Compliance Officer
Darren Schulz, Interim CIO
Susan Walcker, Investment Accountant

OTHERS PRESENT: Paul Erlendson, Callan
Jan Murtha, Attorney General's Office
Bryan Reinhardt, PERS

CALL TO ORDER:

Lt. Governor Wrigley called the State Investment Board (SIB) meeting to order at 8:30 a.m. on Friday, February 22, 2013, at Workforce Safety & Insurance, 1600 E Century, Bismarck, ND.

A quorum was present for the purpose of conducting business.

AGENDA:

MR. SANDAL MOVED AND MR. GESSNER SECONDED TO ACCEPT THE FEBRUARY 22, 2013, AGENDA.

AYES: COMMISSIONER GAEBE, TREASURER SCHMIDT, MR. SANDAL, COMMISSIONER HAMM, MS. FRANZ, MS. TERNES, MR. GESSNER, MR. ERDMANN, MR. TOSO, MR. SAGE, AND LT. GOVERNOR WRIGLEY

NAYS: NONE

MOTION CARRIED

MINUTES:

The minutes were considered from the January 25, 2013, meeting,

MR. ERDMANN MOVED AND MR. SAGE SECONDED TO ACCEPT THE JANUARY 25, 2013, MINUTES AS WRITTEN.

AYES: MR. GESSNER, COMMISSIONER GAEBE, MR. SAGE, MS. TERNES, TREASURER SCHMIDT, MR. TOSO, COMMISSIONER HAMM, MS FRANZ, MR. ERDMANN, MR. SANDAL, AND LT. GOVERNOR WRIGLEY

NAYS: NONE

MOTION CARRIED

INVESTMENTS:

Bank of North Dakota (BND) - Mr. Schulz informed the SIB staff and Ms. Murtha have had ongoing discussions with BND representatives on the transition of the Pension Trust assets from a Barclays Capital Government Index mandate to a Barclays Capital Long Treasury Index. Both entities are in favor of a third party review to analyze the loss incurred as a result of the implementation delay. Staff had reached out to Brady Martz and EideBailly of which both firms declined.

After discussion, the SIB directed staff to contact the State Auditor's Office and if that is not a viable option, continue searching for a party preferably in state.

COMMISSIONER GAEBE MOVED AND TREASURER SCHMIDT SECONDED TO DIRECT STAFF AND COUNSEL TO CONTINUE TO SEARCH FOR A QUALIFIED THIRD PARTY AND AUTHORIZED THE SIB CHAIR, ON BEHALF OF THE SIB, TO ENTER INTO A CONTRACT BASED ON STAFF RECOMMENDATION.

AYES: MS. FRANZ, MR. ERDMANN, COMMISSIONER GAEBE, MR. GESSNER, COMMISSIONER HAMM, MR. SAGE, MR. SANDAL, TREASURER SCHMIDT, MS. TERNES, MR. TOSO, AND LT. GOVERNOR WRIGLEY

NAYS: NONE

MOTION CARRIED

Callan Associates - Mr. Erlendson provided an update on the economy, capital markets and expectations, and asset class performance for the quarter ending December 31, 2012. Mr. Erlendson followed up with performance reviews of the Pension Trust and Insurance Trusts for the quarter ending December 31, 2012.

Discussion took place on Calamos. Calamos manages a global opportunity equity product in the Pension Trust global equities asset class. Performance concerns and personnel changes have occurred in the firm which warrants additional due diligence.

TREASURER SCHMIDT MOVED AND MR. GESSNER SECONDED TO PLACE CALAMOS ON WATCH FOR ADDITIONAL DUE DILIGENCE AND DIRECTED STAFF TO PLACE CALAMOS ON THE AGENDA TO REVIEW PERFORMANCE CONCERNS AND PERSONNEL CHANGES.

AYES: TREASURER SCHMIDT, MR. GESSNER, COMMISSIONER HAMM, MS. TERNES, COMMISSIONER GAEBE, MR. SAGE, MR. TOSO, MR. SANDAL, MR. ERDMANN, MS. FRANZ, AND LT. GOVERNOR WRIGLEY

NAYS: NONE

MOTION CARRIED

Discussion took place on Governance Policy E-11, Investments/Performance Related Investment Manager Review and to place review of the policy on the agenda at a future meeting.

Mr. Erlendson reviewed an analysis of management fees paid by the SIB for the period of July 2011 - June 2012. The analysis determined fees paid during this time period are in line with industry standards.

The SIB recessed at 10:35 a.m. and reconvened at 10:50 a.m.

GOVERNANCE:

Search Committee - Mr. Sandal updated the SIB on the ED/CIO search. The closing date for receipt of applications was January 31, 2013. HRMS received 200 applications and is in the process of completing their evaluation of the applications received based on the evaluation criteria established for minimum qualifications. The Search Committee received input from the SIB, Callan, staff, and Mr. Geissinger on the evaluation criteria for minimums and attributes above and beyond minimums. After HRMS completes their screening, the top 30 will be evaluated for their qualifications above and beyond the minimums. After completing telephone interviews and background checks, the Search Committee is hoping to narrow the field and bring candidates before the SIB in April.

Mr. Sandal also stated HRMS did a very good job. They were timely and thorough.

LEGISLATIVE UPDATE:

Ms. Flanagan and Mr. Schulz reviewed the following bills with the SIB; HB 1022 - RIO Budget Bill, HB1143 - Relating to investment of the Legacy and Budget Stabilization Funds, HB 1167 - relating to the definition of earnings of the Legacy Fund, HB 1249 - relating to the membership of the State Investment Board, HB1304 - relating to the divestiture of state investment funds in certain companies liable to sanctions under the Iran Sanctions Act of 1996; and to provide an expiration date, HB1395 - relating to membership of the Legacy and Budget Stabilization Fund Advisory Board, SB2124 - provides for the legislative management to study methods to assure that the Legacy Fund provides the lasting benefits intended by the voters, and SB2150 - relating to restriction of per diem compensation for members of boards and commissions established by statute, and HCR3018 - relating to transfer of a portion of the earnings of the Legacy Fund to the Legacy Scholarship Fund.

The SIB discussed HB1304 and their actions at their January 25, 2013, meeting where they voted in favor of a neutral stance and directed staff that testimony to the Legislative committees, on behalf of the SIB, be neutral and include factual information, administrative time, and costs of implementation. HB1304 passed the House 84-9 on February 21, 2013.

After taking into consideration the timeframe stated in the bill for divestment of the funds, costs that would be allocated to all of the SIB client's funds, implications, and staff time,

MS. TERNES MOVED AND TREASURER SCHMIDT SECONDED THAT THE SIB OPPOSE HB1304 AND DIRECTED STAFF TO PROVIDE TESTIMONY IN OPPOSITION OF THE BILL.

AYES: MR. SANDAL, MS. FRANZ, MR. GESSNER, MR. TOSO, MR. ERDMANN, MS. TERNES, COMMISSIONER HAMM, AND TREASURER SCHMIDT

NAYS: MR. SAGE, COMMISSIONER GAEBE, AND LT. GOVERNOR WRIGLEY
MOTION CARRIED

Mr. Schulz informed the SIB RV Kuhns is nearing completion of the asset allocation study and spending policy of the Legacy Fund and is expecting a draft in the next couple of weeks.

ADJOURNMENT:

With no further business to come before the SIB, Lt. Governor Wrigley adjourned the meeting at 11:55 a.m.

Lt. Governor Wrigley, Chair
State Investment Board

Bonnie Heit
Assistant to the Board

Board Education Risk Factors and Asset Allocation

March 22, 2013

Darren Schulz

Interim Chief Investment Officer

ND Retirement & Investment Office (RIO)

State Investment Board (SIB)

History of Institutional Asset Allocation

▶ **Pre-1970s**

- ▶ Assets invested mainly in fixed income: emphasis on capital preservation
- ▶ Large trust companies predominant investment managers
- ▶ “Prudent Man Standard” main decision-making guide

▶ **1970s**

- ▶ First S&P Composite Index fund established in 1973
- ▶ ERISA passed in 1974
- ▶ Initial use of equities by institutional investors (“balanced” portfolios)
- ▶ Concept of risk control in a portfolio context: asset diversification

▶ **1980s**

- ▶ Rise of boutique asset managers
- ▶ Early adopters investing in Real Estate and Private Equity (aka “LBO funds”)
- ▶ Total Return orientation
- ▶ Crash of 1987 and the demise of portfolio “insurance”

History of Institutional Asset Allocation

▶ 1990s

- ▶ Big increase in equity exposure
- ▶ “Prudent Expert Standard” becomes main decision-making guide
- ▶ International equity/fixed income widely adopted

▶ 2000s

- ▶ Popping of Internet/TMT bubble highlighted over-reliance on public equities
- ▶ Movement away from original Mean Variance Optimization
- ▶ Rise of “endowment model”: broader use of Alternative Investments, including hedge funds, and emerging market investments
- ▶ Prevalence of LDI strategies, primarily among Corporate sponsors

▶ TODAY

- ▶ “New Normal”: coping with low-return environment
- ▶ Risk control/downside protection and Risk Parity (equal risk from risk factors)
- ▶ Investment strategies global in scope
- ▶ Need to be opportunistic to enhance returns and hedge against losses

Asset Allocation Today

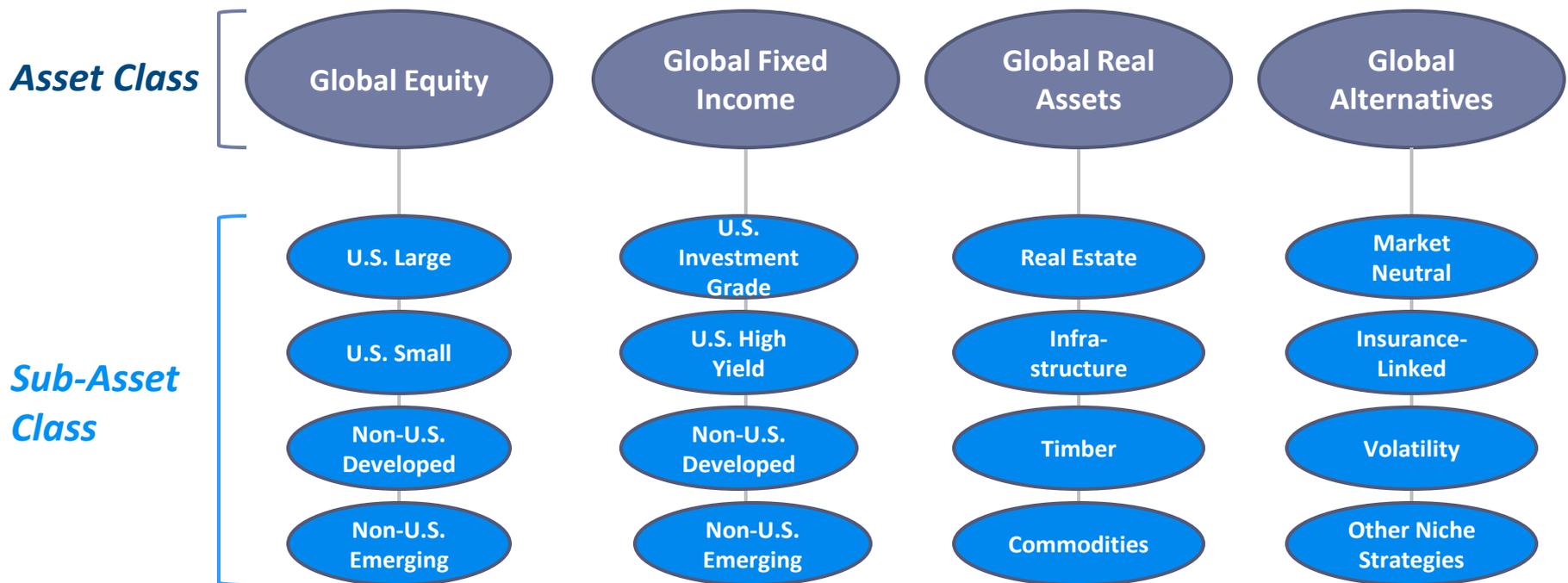
- ▶ The integration of global financial markets in recent decades has made it **more challenging than ever to construct diversified portfolios that deliver an acceptable rate of return.**
- ▶ The global financial crisis provided a stark and costly reminder that **diversification benefits often disappear when needed most.** It has prompted many investors to take a fresh look at their asset allocation processes and their reliance on Modern Portfolio Theory.
- ▶ **Risk factor analysis** has gained visibility in recent years. While it does not change the fundamental opportunity set facing investors, it is a **powerful tool that can improve upon the ability to understand and communicate the inherent risks of investing.** It can be applied as an integral component of the asset allocation process.

What Is An Asset Class?

- ▶ An asset class is a group of individual investments whose returns are dependant upon a common set of risk factors or return drivers.
- ▶ The correlation of individual asset returns are high relative to other members of the asset class and the asset class as a whole, and lower to other asset classes.
- ▶ An asset class is properly defined when the asset classes held together provide the desired diversification benefits.
- ▶ Asset classes should be as independent as possible (minimal overlap) and in aggregate should cover the investment universe (minimal gaps).

Distinction Between Asset Classes and Sub-Asset Classes

- ▶ The finer the distinctions between various “asset classes,” the higher the resulting correlations.
- ▶ Typical asset allocation relies on sub-asset classes (such as large cap or small cap U.S. equity or non-U.S. developed equity).



Current Asset Allocation Framework

GLOBAL EQUITIES

Investment represents an ownership claim on the residual income from productive resources.

The return to equity holders is impacted by the growth of net revenue and income, hence common risk factors include economic and productivity growth.

High return volatility can be mitigated by diversification and tilts to areas with attractive relative valuations.

Includes domestic and international equities – both publicly traded and privately held.

Economic role: Capital accumulation



GLOBAL ALTERNATIVES

Investment represents niche/specialized strategies with low asset class beta.

Economic role: Robust diversification through non-traditional return drivers/risk factors

GLOBAL FIXED INCOME

Investment represents a legal obligation between a borrower and the lender.

The return to fixed income is driven by the future course of interest rates, which are influenced by expectations for future growth and inflation, and default rates.

Economic role: Capital protection

GLOBAL REAL ASSETS

Investment represents ownership in physical assets, as opposed to financial assets.

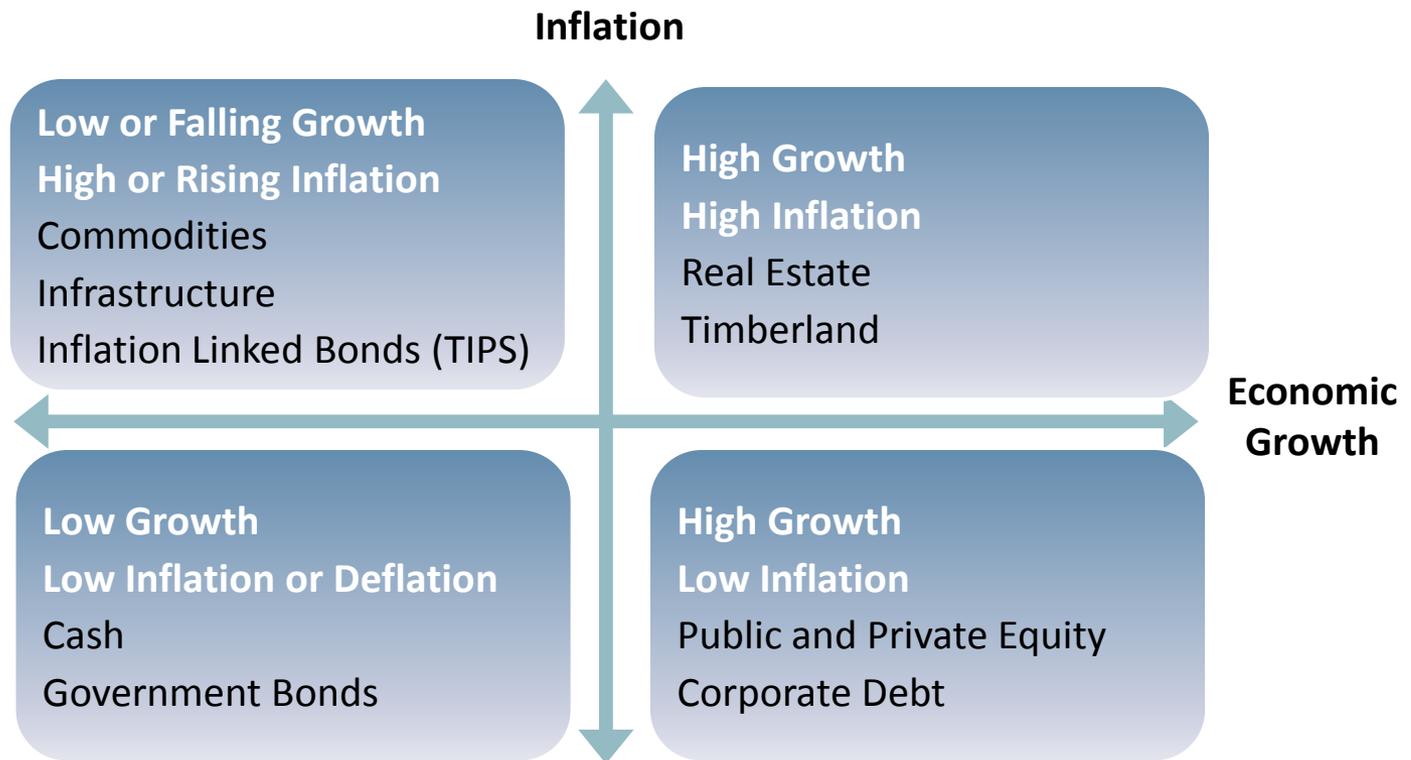
Returns are expected to be positively correlated to unanticipated inflation.

Includes real estate, infrastructure, timber and commodities.

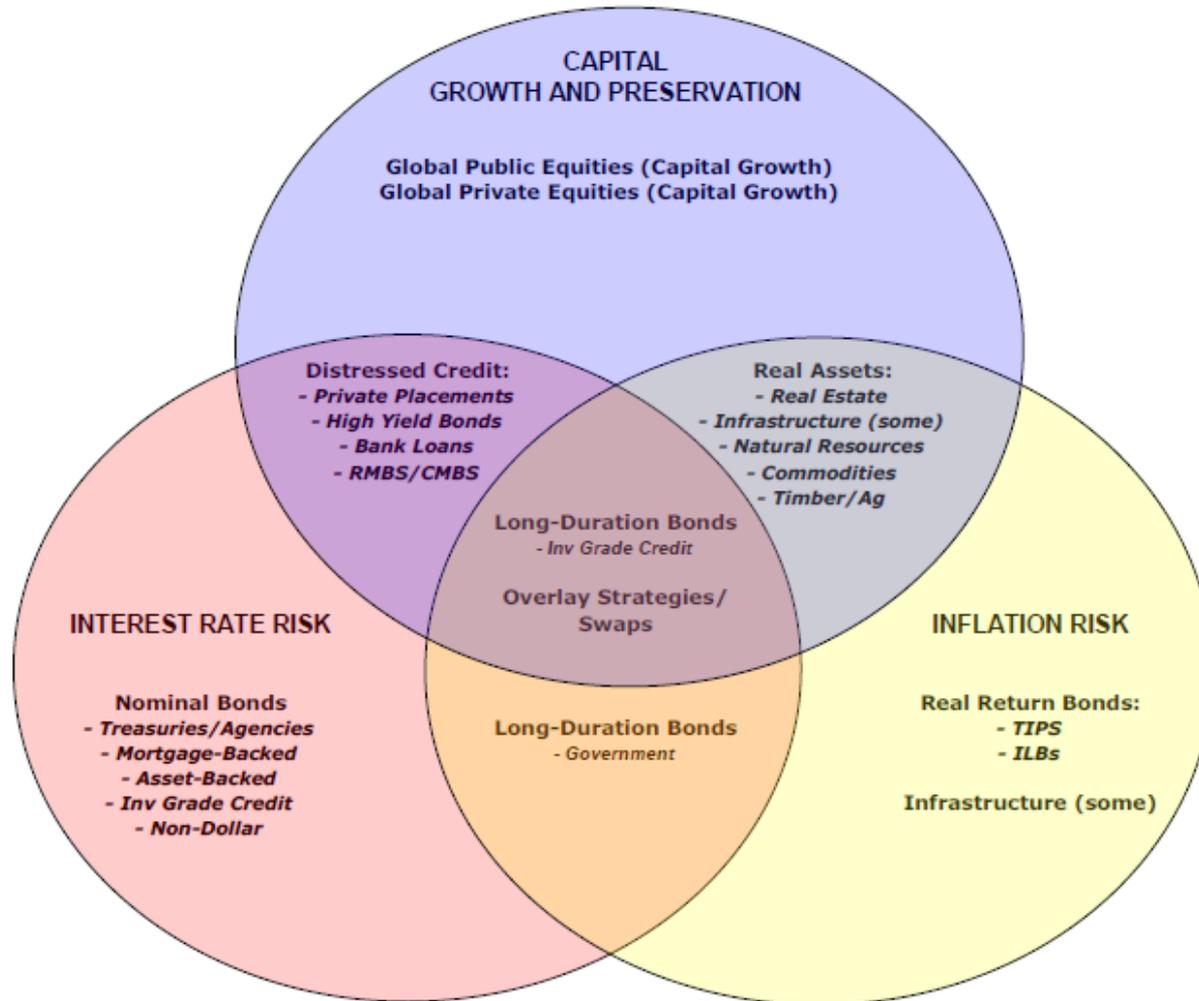
Economic role: Inflation protection

Role of Assets Based on Economic Scenarios

- ▶ Bucketing asset classes based on their response to macroeconomic scenarios combines the transparency of investing with asset classes with the granularity of a factor-based approach.



Role of Current Asset Framework in Hedging Risks



Comparative Asset Allocation Models

- ▶ CALPERS' structure provides a combination of return-seeking and hedging portfolios that allow for better risk management and capital allocation.

AAC: Alternative Asset Classifications

AAC	Consists of	Purpose	Proposed target %	New range (plus, minus)
Growth	Public Equity, Private Equity	Positive exposure to economic growth – equity risk premium	63	7
Income	Fixed Income	Provide income return	16	5
Real	Real Estate, Infrastructure, Forestland	Provide long horizon income return that is less sensitive to inflation risk	13	5
Inflation	Commodities, Inflation-Linked Bonds	Public market investments with positive inflation exposure	4	3
Liquidity	Cash, Nominal Gov't Bonds	Hedge equity and deflation risks provide liquidity	4	3

Source: CALPERS

Comparative Asset Allocation Models

- ▶ Alaska Permanent Fund combines equity and credit exposure (“Company Exposure”) and “Special Opportunities” allocation provides implementation flexibility.

Risk Class	Asset Class	Risk Class Target	Asset Class Target
Cash		2%	2%
Interest Rates		6%	
	U.S. Government Bonds		4%
	International Developed Government Bonds (currency hedged)		2%
Company Exposure		53%	
	Global Credit		11%
	Global Equity		36%
	Private Equity		6%
Real Assets		18%	
	Real Estate		12%
	Infrastructure		3%
	U.S. Treasury Inflation Protection Securities		3%
Special Opportunities*		21%	
	Absolute Return Mandate		6%
	Real Return Mandate		7%
	Distressed Debt		1%
	Mezzanine Debt		1%
	Structured Credit		1%
	Other (future opportunities)		5%

Source: Alaska Permanent Fund

Asset Allocation Solutions for the New Normal

Traditional Asset Allocation Approach

- ▶ Mean variance optimization
- ▶ Backward-looking and statistically driven
- ▶ “Set it & forget it”
- ▶ Focus on asset class diversification
- ▶ Historical returns
- ▶ Use volatility as sole risk measure, thus ignoring “fat tails”

Risk Factor Asset Allocation Approach

- ▶ Risk factor optimization
- ▶ Forward-looking and driven by macroeconomic regimes
- ▶ Regime-specific assumptions for return and risk
- ▶ Focus on risk factor diversification
- ▶ Tail risk management
- ▶ Multiple dimensions of risk

Risk Factor Analysis

- ▶ The objective of risk factor analysis is to identify the underlying investment risks that describe the return variation in a particular portfolio or asset.
- ▶ Extensive academic literature suggests that certain factors (such as size and value in equity markets) are associated with long-term risk premia.
- ▶ Ang (2010) provides an intuitive analogy to describe the relationship between risk factors and investments:

Factor risk is reflected in different assets just as nutrients are obtained by eating different foods. Peas, wheat, and rice all have fiber. Similarly, certain sovereign bonds, corporate bonds, equities, and credit default derivatives all have exposure to credit risk. Assets are bundles of different types of factors just as foods contain different combinations of nutrients.

Risk Is Not Simply Volatility



Risk Factor Building Blocks Example

- ▶ Further segmentation of Alaska Permanent Fund risk factor building blocks based on primary risk factors.



Source: Alaska Permanent Fund

Risk Factor Building Blocks Example

- Risk factors can be grouped in a myriad of ways. In some cases finding marketable proxies (liquidity, leverage) can be challenging to find.

The Periodic Table of Factors

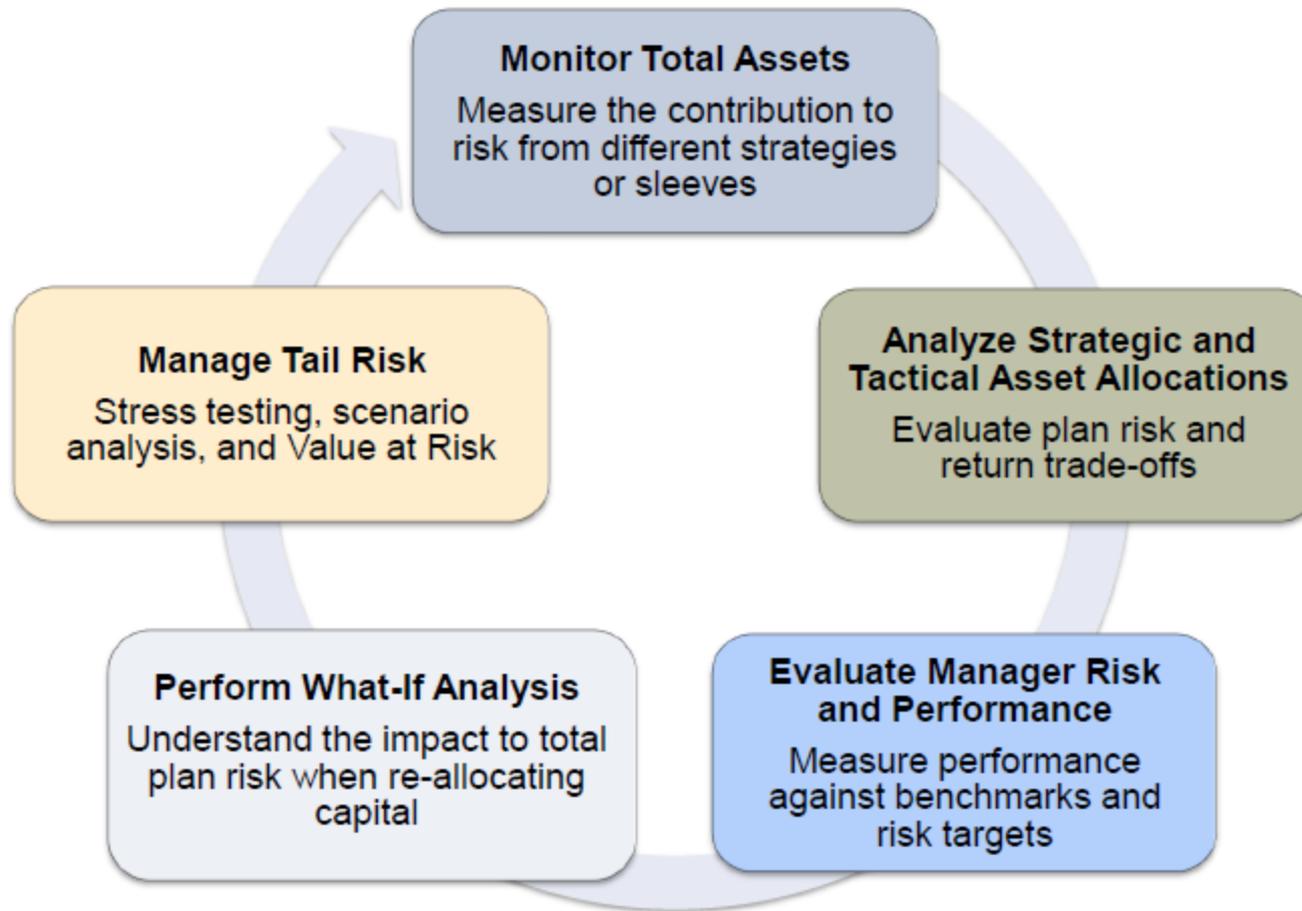
Macroeconomic	Regional	Equity	Fixed Income	Other
GDP Growth	Sovereign Exposure	Size	Duration	Liquidity
Productivity	Currency	Value	Convexity	Leverage
Real Interest Rates	Emerging Markets (Institutions + Transparency)	Momentum	Credit Spread	Real Estate
Inflation			Default Risk	Commodities
Volatility				Capital Structure

Source: Callan

BarraOne Risk Analytics

- ▶ BarraOne provides a common factor framework that clients can use to help them identify sources of risk and performance across multi-asset class strategies and plans.
- ▶ Powered by the Barra Integrated Model, a common factor model covering global equity, fixed income, commodity, currency, real estate, and private equity markets, BarraOne helps risk managers identify the fundamental market characteristics driving volatility.
- ▶ Multiple views of risk are provided, including common factor, stress testing, Value at Risk, and sensitivity-based analytics. In addition, the flexibility to tune risk model parameters allows users to define multiple horizon models, consistent with their view of market and volatility environments.

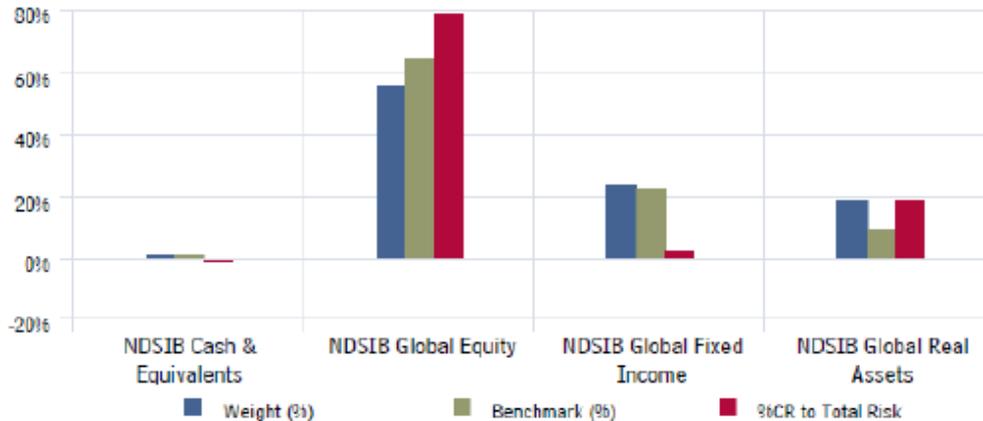
Managing Investment Decisions with BarraOne



Source: MSCI

Total Portfolio Analysis – SIB Pension Pool

Risk Summary		Asset Class Contribution to Risk							
Statistic	Value	Asset Class	Mkt Value	Weight (%)	Benchmark Weight (%)	Total Risk	Risk Contribution	%CR to TF	
Total Risk	14.50	Total	3,656,164,261	100.00	98.24	14.50	14.50	14.50	100.00
Benchmark Risk	16.04	NDSIB Cash & Equivalents	51,936,243	1.42	1.00	0.11	-0.00	-0.00	-0.00
Active Risk	2.03	NDSIB Global Equity	2,037,066,197	55.72	64.91	20.70	11.47	79.11	
Portfolio Beta	0.90	NDSIB Global Fixed Income	875,236,802	23.94	23.10	3.96	0.35	2.38	
Cont. to Eff. Duration	1.16	NDSIB Global Real Assets	691,925,019	18.92	9.23	15.04	2.68	18.51	



- Remember that all risk statistics in BarraOne are forward looking
- The long-term version of the Barra risk models are calibrated to forecast risk 6-12 months in the future
- Global Equity has a 56% weight in the portfolio, but contributes more than 79% of the Total Risk
- Global Fixed Income has a 24% weight in the portfolio, but contributes only 0.35% of the forecast Total Risk of 14.5%

Source: MSCI BarraOne

Risk Factor Breakdown – SIB Pension Pool

Risk Decomposition						
Risk Source	Portfolio			Active		
	Risk Contribution	% Risk	Correlation	Risk Contribution	% Risk	Correlation
Total Risk	14.50	100.00	1.00	2.03	100.00	1.00
Local Market Risk	13.34	92.00	0.99	1.97	97.02	1.00
Common Factor Risk	13.31	91.83	0.99	1.92	94.65	0.99
Equity	12.43	85.71	0.98	2.08	102.39	0.87
Fixed Income	0.26	1.77	0.30	-0.01	-0.37	-0.25
Private Real Estate	0.63	4.35	0.55	-0.15	-7.36	-0.13
Selection Risk	0.02	0.16	0.04	0.05	2.36	0.15
Currency Risk	1.16	8.00	0.54	0.06	2.98	0.41

- Risk is first decomposed into Local Market Risk and Currency Risk
- Local Market Risk is then decomposed into Common Factor Risk and Selection Risk
- Common Factor Risk can be further decomposed into asset classes:
 - Equity – Industry and Style factors
 - Fixed Income – Term Structure and Spread factors
 - Other Asset Classes
- Equity Risk is the primary driver of both Total Risk and Active Risk

Source: MSCI BarraOne

Other BarraOne Uses

Manager Selection

- ▶ Load the holdings of a potential manager and understand changes to total risk, active risk, and exposures

Manager Optimization

- ▶ Choose from standard, risk target, long/short, and efficient frontier optimization

Time Series Analysis

- ▶ Monitor changes in risk factors over time
- ▶ Decompose risk changes into changes in weight, standalone volatility, and correlation

Risk Budgeting

**STATE INVESTMENT BOARD SEARCH COMMITTEE
MINUTES OF THE
MARCH 12, 2013, TELECONFERENCE MEETING**

BOARD MEMBERS PRESENT: Drew Wrigley, Lt. Governor, Chair
Lance Gaebe, Land Commissioner
Mike Sandal, PERS Board
Kelly Schmidt, State Treasurer
Bob Toso, TFFR Board

STAFF PRESENT: Bonnie Heit, Office Manager
Darren Schulz, Interim CIO

OTHERS: Tricia Opp, State Procurement

CALL TO ORDER:

Lt. Governor Wrigley called the State Investment Board (SIB) Search Committee meeting to order at 11:00 a.m. on Tuesday, March 12, 2013.

The SIB Search Committee meeting was held for the purposes of discussing the evaluation process thus far for the applications received for the ED/CIO position of RIO. HRMS, the Search Committee, and staff evaluated the applications. The Search Committee discussed their evaluation process to date and concurred that changing the course of the search is justifiable in order to move forward and find the best possible candidate based on the attributes that are needed for the position.

The Request for Proposal for Executive Recruitment Services was issued on March 6, 2013. The deadline for submitting proposals is March 27, 2013. Mr. Sandal, Commissioner Gaebe, and Treasurer Schmidt will work with State Procurement to evaluate the proposals received. The Search Committee is hoping to have an Executive Recruitment consultant in place by the first part of May 2013.

The Search Committee directed staff to draft a letter notifying the existing applicants that if they wished to continue to be considered for the position that they could do so by applying directly to the executive recruitment service selected by State Procurement and the Search Committee once the firm is in place. The applicants are also to be informed that updates and information will be made available on the SIB's web site.

The Search Committee also directed staff to draft a letter notifying the SIB clients on the status of the recruitment process.

ADJOURNMENT:

With no further issues to come before the Search Committee, Lt. Governor Wrigley adjourned the meeting at 11:45 a.m.

Lt. Governor Wrigley, Chair
State Investment Board

Bonnie Heit
Assistant to the Board

March 15, 2013

Letter to Applicants

The Search Committee of the ND State Investment Board has completed their review of applications received for the Executive Director/Chief Investment Officer position of the ND Retirement and Investment Office.

The Committee has decided to expand the search for the position by enlisting the services of an executive recruitment service, and is in the process of selecting an executive recruitment consultant for that purpose.

If you wish to be considered further, you will need to apply through the executive recruitment service selected by the Search Committee. Updates and information will be made available on the State Investment Board's web site <http://www.nd.gov/rio/News/default.htm>.

Thank you for your time and interest in the Executive Director/Chief Investment Officer position.

Sincerely,

Drew H. Wrigley
Lieutenant Governor
Chairman, State Investment Board
(701) 328-4222
pmoser@nd.gov

March 15, 2013

Letter to Clients

As Chairman of the State Investment Board, I wanted to give you an update on the recruitment process for the Executive Director/Chief Investment Officer position of the ND Retirement and Investment Office.

The State Investment Board's Search Committee, with assistance from the State's Human Resource Management Services (HRMS) agency, placed the job opening in various relevant newspapers and with investment related associations throughout the nation. HRMS received 200 applications. The applications were reviewed by HRMS personnel and a sub-set of the Search Committee. After review of the applications, the Search Committee has decided that it is necessary to expand the search for the Executive Director/Chief Investment Officer position and we will be enlisting the services of an executive recruitment service. The Search Committee is in the process of selecting an executive recruitment consultant and hopes to have a consultant in place by the first part of May 2013. Updates and information will be made available on the State Investment Board's web site <http://www.nd.gov/rio/News/default.htm>.

Please do not hesitate to contact me during this interim period. We appreciate the confidence that you have placed in the State Investment Board and our professional staff, and we value your input.

Sincerely,

Drew H. Wrigley
Lieutenant Governor
Chairman, State Investment Board
(701) 328-4222
pmoser@nd.gov

**STATE INVESTMENT BOARD SEARCH COMMITTEE
MINUTES OF THE
MARCH 4, 2013, TELECONFERENCE MEETING**

BOARD MEMBERS PRESENT: Drew Wrigley, Lt. Governor, Chair
Lance Gaebe, Land Commissioner
Mike Sandal, PERS Board
Kelly Schmidt, State Treasurer
Bob Toso, TFFR Board

STAFF PRESENT: Darren Schulz, Interim CIO

CALL TO ORDER:

Lt. Governor Wrigley called the State Investment Board (SIB) Search Committee meeting to order at 1:30 p.m. on Monday, March 4, 2013.

The SIB Search Committee meeting was held for the purposes of discussing the status of the evaluation process for the applications received for the ED/CIO position of RIO.

HRMS completed their review and scoring of the applications for both minimum qualifications and attributes above and beyond the minimums. The top 30 applications were then evaluated by Mr. Sandal, Treasurer Schmidt, Mr. Schulz, and Ms. Flanagan. Evaluation results indicated that of the 30 applications reviewed none brought all of the necessary skills needed for the position.

After discussion, the Search Committee concurred to expand the search for the position by enlisting the services of an executive recruitment service. The Search Committee directed staff to work with State Procurement personnel and issue a Request for Proposal for executive recruitment services and release it the week of March 4, 2013.

ADJOURNMENT:

With no further issues to come before the Search Committee, Lt. Governor Wrigley adjourned the meeting at 1:55 p.m.

Lt. Governor Wrigley, Chair
State Investment Board

Bonnie Heit
Assistant to the Board

**ND STATE INVESTMENT BOARD
AUDIT COMMITTEE MEETING**

**FRIDAY, FEBRUARY 22, 2013, 1:00 p.m.
WORKFORCE SAFETY AND INSURANCE
1600 E CENTURY AVENUE, BISMARCK, ND**

AGENDA

- 1. CALL TO ORDER & APPROVAL OF AGENDA**
- 2. APPROVAL OF NOVEMBER 16, 2012, MINUTES** (enclosed)
- 3. REPORT ON FISCAL 2013 SECOND QUARTER INTERNAL AUDIT ACTIVITIES -**
Mr. Mason, Ms. Thorsen (enclosed) **(Committee Approval)**
 - A. School District Audits (enclosed - questions only)
 - B. Executive Limitations Audit (enclosed)
- 4. AUDIT COMMITTEE CHARTER** - work on revision (enclosed)
- 5. COMMITTEE MEETING WITH INTERIM EXECUTIVE DIRECTOR**
- 6. COMMITTEE MEETING WITH INTERNAL AUDIT SUPERVISOR**
- 7. UPDATE ON EXECUTIVE DIRECTOR SEARCH** - Mr. Sandal
- 8. OTHER**
Next SIB Audit Committee Meeting - Friday, May 17, 2013, 1:00 p.m.,
Peace Garden Room - State Capitol.
- 9. ADJOURNMENT**

**STATE INVESTMENT BOARD
AUDIT COMMITTEE MEETING
MINUTES OF THE
NOVEMBER 16, 2012 MEETING**

COMMITTEE MEMBERS PRESENT: Rebecca Dorwart, Chair
Lonny Mertz, Vice Chair
Mike Gessner, TFFR Board/Liaison to the SIB
Mike Sandal, PERS Board
Cindy Ternes, Workforce Safety & Insurance

STAFF PRESENT: Connie Flanagan, Fiscal & Investment Officer
Bonnie Heit, Office Manager
Fay Kopp, Interim Executive Director
Les Mason, Internal Audit Supervisor
Darren Schulz, Interim Chief Investment Officer
Dottie Thorsen, Internal Audit

OTHERS PRESENT: Thomas Rey, CliftonLarsonAllen

CALL TO ORDER:

Ms. Dorwart called the State Investment Board (SIB) Audit Committee meeting to order at 1:00 p.m., on Friday, November 16, 2012, at Workforce Safety & Insurance, 1600 E Century, Bismarck, ND.

A quorum was present for the purpose of conducting business.

AGENDA:

The Audit Committee considered the November 16, 2012 agenda.

MR. SANDAL MOVED AND MS. TERNES SECONDED TO ACCEPT THE AGENDA FOR THE NOVEMBER 16, 2012, MEETING.

**AYES: MS. DORWART, MR. SANDAL, MS. TERNES, MR. MERTZ, AND MR. GESSNER
NAYS: NONE
MOTION CARRIED**

MINUTES:

The Audit Committee considered the minutes from the October 16, 2012, meeting.

MR. GESSNER MOVED AND MR. SANDAL SECONDED TO ACCEPT THE OCTOBER 16, 2012, MINUTES AS WRITTEN.

**AYES: MR. GESSNER, MS. DORWART, MR. SANDAL, MS. TERNES, AND MR. MERTZ
NAYS: NONE
MOTION CARRIED**

FINANCIAL AUDIT REPORT JUNE 30, 2012:

Mr. Thomas Rey reviewed CliftonLarsonAllen's audit of the financial statements of the Retirement and Investment Office (RIO) for the Fiscal Year Ending June 30, 2012. Mr. Rey reported CliftonLarsonAllen issued an unqualified opinion of the financial statements.

Ms. Flanagan informed the Audit Committee RIO has been awarded the Certificate of Achievement for Excellence in Financial Reporting by the Governmental Financial Officer's Association (GFOA) for the past 14 consecutive years.

The Audit Committee thanked staff for their excellent work on the audit report.

MS. TERNES MOVED AND MR. MERTZ SECONDED TO ACCEPT CLIFTONLARSONALLEN'S AUDIT REPORT OF THE FINANCIAL STATEMENTS OF RIO FOR THE FISCAL YEAR ENDING JUNE 30, 2012.

**AYES: MS. TERNES, MR. MERTZ, MS. DORWART, MR. SANDAL, AND MR. GESSNER
NAYS: NONE
MOTION CARRIED**

INTERNAL AUDIT ACTIVITIES:

Mr. Mason reviewed the Internal Audit Division's work activity for the first quarter of FY2013.

School District Audit Reports - The objective is to complete 43 or more school district audits during FY2013. Currently, seven audits were completed, six audits are in progress, information on three more school districts has been received, and information is being requested for 12 additional districts.

TFFR File Maintenance - Ms. Thorsen reported she reviewed the first quarter of FY2013 transactions. There were no exceptions noted.

MR. GESSNER MOVED AND MS. TERNES SECONDED TO ACCEPT THE INTERNAL AUDIT DIVISION'S WORK ACTIVITY REPORT FOR THE FIRST QUARTER OF FY2013.

**AYES: MS. DORWART, MR. GESSNER, MR. MERTZ, MR. SANDAL, AND MS. TERNES
NAYS: NONE
MOTION CARRIED**

CHARTER:

The Audit Committee reviewed their Charter. Mr. Mason is to electronically distribute the Charter to the Audit Committee with his suggested changes. Audit Committee members are to submit their changes to Ms. Dorwart. The Charter will be reviewed at the February 22, 2013, meeting.

FY 2013 WORK PLAN:

The Audit Committee reviewed a revised Internal Audit work plan for the period of July 1, 2012 - June 30, 2013 which reflected the discussion and changes from the November 16, 2012, meeting.

MS. TERNES MOVED AND MR. SANDAL SECONDED TO ACCEPT THE REVISED INTERNAL AUDIT WORK PLAN FOR THE PERIOD OF JULY 1, 2012 - JUNE 30, 2013.

AYES: MS. DORWART, MR. SANDAL, MS. TERNES, MR. MERTZ, AND MR. GESSNER

NAYS: NONE

MOTION CARRIED

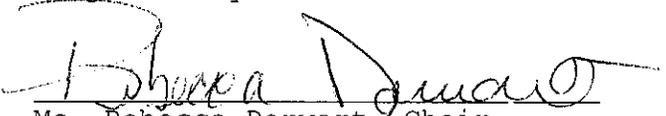
OTHER:

The next Audit Committee meeting is scheduled for February 22, 2013, at 1:00 p.m. at Workforce Safety & Insurance.

ADJOURNMENT:

With no further business to come before the Audit Committee, Ms. Dorwart adjourned the meeting at 2:15 p.m.

Respectfully Submitted:


 Ms. Rebecca Dorwart, Chair
 SIB Audit Committee


 Bonnie Heit
 Assistant to the Audit Committee

Legislative Bill Tracking Status Report As of March 15, 2013

1. HB1022 – RIO Budget Bill

1/08/2013 – Introduced, first reading, referred to Appropriations Committee

1/16/2013 10:00 am – Committee Hearing - House Appropriations-Government Operations

- Fay, Connie and Darren provided testimony to the committee. The tone was positive. The bill will be assigned to a sub-group who will follow-up with us on any further detail needed.

1/23/2013 2:30 pm - House Appropriations-Government Operations (follow-up)

- Fay provided general information on TFFR plan but there were no specific budget related questions.

2/15/2013 9:30 am – House Appropriations-Government Operations (additional discussion)

- Connie and Darren provided information regarding the fiscal note for HB1304 which had been discussed by the full Appropriations committee the day before and given a “Do pass” recommendation.
- Committee approved an amendment to add one additional FTE for an “Investment Analyst” position and related costs and then gave amended bill a “Do pass” recommendation.

2/22/2013 – Full Appropriations Committee gave amended bill a “Do pass” recommendation (19-3)

2/25/2013 – Amendment adopted and second reading passed on House Floor (92-0)

3/14/2013 8:30 am – Senate Appropriations Committee Hearing

- **Fay, Connie and Darren provided testimony to the committee. The tone was positive. No action was taken.**

2. HB1167 – Relating to the definition of earnings of the legacy fund

This bill defines earnings for purposes of Title X, Section 26 of the state constitution as interest and dividends only, not capital gains. (The bill, as introduced, erroneously references Title IX rather than Title X.)

1/11/2013 – Introduced, first reading, referred to Finance and Taxation Committee.

1/21/2013 9:15 am – Committee Hearing - House Finance and Taxation

- Darren and Connie attended the hearing. Darren provided neutral testimony describing relationship between realized and unrealized capital gains. Amendment will be necessary to correct title reference. No questions were asked.

1/31/2013 – Reported back amended, “Do pass” (14-0)

- Amendment corrects title reference and replaces “capital gain” with “unrealized gains on investments”.

2/01/2013 – Amendment adopted, placed on calendar

2/04/2013 – Passed on House floor (91-0)

3/22/2013 9:00 am – Committee Hearing – Senate Government and Veterans Affairs

3. HB1249 – Relating to the membership of the state investment board.

This bill would provide for two additional members on the state investment board; one appointed by the majority leader of the senate and the other appointed by the majority leader of the house of representatives.

1/14/2013 – Introduced, first reading, referred to Government and Veterans Affairs Committee.

1/24/2013 8:00 am – Committee Hearing - House Government and Veterans Affairs

- Darren, Connie and Fay attended hearing. Darren provided clarification on questions asked of the bill sponsor and followed up with additional information about the SIB program at the request of the chairman.

1/30/2013 – Reported back amended, “Do pass” (12-1-1)

- Amendment changes appointment responsibility from majority leaders to chairman of legislative management.

1/31/2013 – Amendment adopted, placed on calendar

2/01/2013 – Re-referred to Appropriations Committee (fiscal note)

2/11/2013 – Reported back amended, “Do pass” 14-4

- Amendment sets compensation and expense reimbursement for legislative members to NDCC 54-35-10 (\$157) and indicates legislative council (not RIO) will pay those expenses.

2/12/2013 – Amendment adopted, placed on calendar

2/13/2013 – Passed on House Floor (63-27)

3/07/2013 9:45 am – Committee Hearing – Senate Government and Veterans Affairs

- Darren, Connie and Fay attended the hearing as well as the Lt. Governor who provided testimony in opposition of the bill. The committee took no action on the bill.

4. HB1304 – Relating to the divestiture of state investment funds in certain companies liable to sanctions under the Iran Sanctions Act of 1996; and to provide an expiration date

This bill would require certain restrictions, monitoring and reporting of “scrutinized companies” relating to the Iran Sanctions Act of 1996, within the state investment board portfolios.

1/14/2013 – Introduced, first reading, referred to Government and Veterans Affairs Committee.

2/07/2013 2:30 pm – Committee Hearing – House Government and Veterans Affairs

- Darren presented neutral testimony regarding costs and other considerations. Representatives for TFFR and PERS as well as Treasurer Schmidt presented testimony in opposition.

2/11/2013 – Reported back amended, “Do pass” (8-5)

- Amendment requires exclusive benefit rule be applied before any other provisions for any public employees retirement system fund.

2/12/2013 – Amendment adopted. Re-referred to Appropriations

2/15/2013 – Reported back, “Do pass” (20-2); placed on calendar

2/21/2013 – Passed on House Floor (84-9)

3/07/2013 9:15 am – Committee Hearing – Senate Government and Veterans Affairs

- Darren, Connie and Fay attended the hearing. Darren provided testimony on behalf of the SIB in opposition of the bill. Fay provided testimony on behalf of TFFR in opposition of the bill. Treasurer Schmidt also provided testimony in opposition. No one other than the bill sponsor spoke in favor of the bill. The committee members asked many good questions of all those who testified but took no action on the bill.

5. HB1395 – Relating to membership of the legacy and budget stabilization fund advisory board.

This bill would add two members to the advisory board, appointed by the chairman of the legislative management.

1/21/2013 – Introduced, first reading, referred to Political Subdivisions Committee

2/15/2013 10:00 am – Committee Hearing – House Political Subdivisions

2/22/2013 – Reported back amended, “Do pass” (13-0-2)

- Amendment stipulates the two additional members will have “experience in the investment field”

2/25/2013 – Amendment adopted; Second reading passed on House Floor (90-2)

3/22/2013 9:20 am – Committee Hearing – Senate Government and Veterans Affairs

6. SB2124 – Provides for the legislative management to study methods to assure that the legacy fund provides the lasting benefits intended by the voters

1/09/2013 – Introduced, first reading, referred to Industry, Business and Labor Committee

1/14/2013 11:00 am – Senate Industry, Business and Labor Committee

- Committee heard testimony from bill drafter and various interested parties and gave the bill a Do-pass recommendation (7-0).

1/15/2013 – Passed on Senate Floor (46-0)

3/07/2013 8:00 am – Committee Hearing – House Government and Veterans Affairs

3/12/2013 – Reported back “Do Pass” (12-0-2)

3/13/2013 – Second reading, passed (88-6)

7. HCR3018 – Relating to transfer of a portion of the earnings of the legacy fund to the legacy scholarship fund.

This bill proposes a constitutional amendment to section 26 of article X regarding the legacy fund which would direct ten million dollars of the earnings of the legacy fund to a legacy scholarship fund for ND high school graduates who attend ND colleges and meet certain academic performance and other minimum standards.

1/25/2013 – Introduced, first reading, referred to House Finance and Taxation Committee

2/06/2013 10:15 am – Committee Hearing – House Finance and Taxation Committee

2/19/2013 – Reported back amended, “Do pass” (13-0-1)

- Amendment changes bill to a study of the most beneficial use of the earnings of the Legacy Fund (similar to SB2124)

2/20/2013 – Amendment adopted, placed on calendar

2/21/2013 – Second reading, adopted

3/22/2013 9:45 am – Committee Hearing – Senate Government and Veterans Affairs

SIB Manager Review Policy

March 22, 2013

Darren Schulz

Interim Chief Investment Officer

ND Retirement & Investment Office (RIO)

State Investment Board (SIB)

Current Manager Review Policy

Factors influencing a Manager Review:

- ▶ Significant changes in organizational structure
- ▶ Significant changes in investment philosophy
- ▶ Significant deviation in portfolio management from stated philosophy (style drift)
- ▶ Substandard investment performance
- ▶ Diminished confidence in manager

Manager Review Procedures:

- ▶ Information submitted to, or generated by, the Board and if warranted the Board takes action to initiate a Manager Review
- ▶ SIB suggests appropriate action to facilitate Review based on situation and input from Investment Director
- ▶ Investment Director reports findings at a subsequent meeting

Current Manager Review Policy

Manager Review Procedures (continued):

- ▶ After considering findings, SIB may:
 - ▶ Remove manager from Review status
 - ▶ Suggest additional action to facilitate Review
 - ▶ Relieve manager of duties
- ▶ Where continued investigation is warranted, it is the responsibility of the Investment Director to maintain awareness and consideration of the Review until the situation is resolved.
- ▶ In serious situations, Investment Director is granted the authority to place a manager under Review, freeze assets if necessary, and report on such action at the next SIB meeting.
- ▶ Investment Director is responsible for documenting Manager Review process to include: reason for Review, action taken, results of investigation, action taken by SIB, and notification to manager and consultants of investigation and conclusions.

Hiring and Firing Investment Managers

Considerations:

- ▶ Manager decisions should be considered within the broader asset allocation or sub-allocation framework.
- ▶ Manager evaluation process should focus more on qualitative factors, and be supported with a diligent quantitative review.
- ▶ Quantitative review should not focus primarily on performance, but rather on a variety of metrics, including fees, appropriate peer comparisons, multiple investment cycles, as well as risk assessment.
- ▶ Consider the burden of transition costs, and how Manager Review policies are utilized.

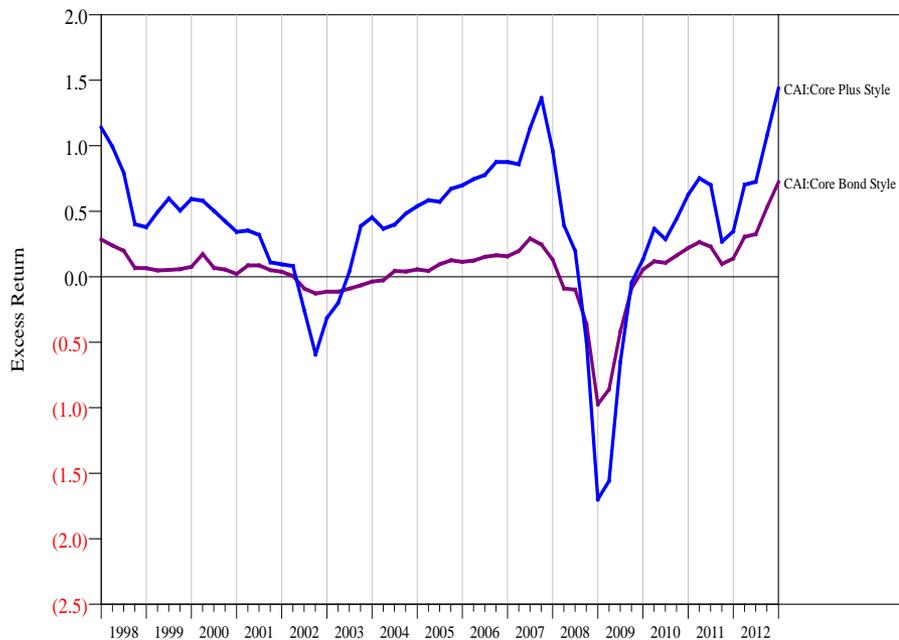
Setting Reasonable Expectations

- ▶ Expectations of sustained, sequential outperformance are unrealistic and likely detrimental.
 - ▶ Any manager with a superior long-term track record is virtually certain to underperform, for multiple periods within that excellent record.
 - ▶ A Plan will face numerous temptations along a path of long-term excellence to pass them over for other mandates, reduce their allocation, or terminate them.
- ▶ The expectation of outperformance by all plan managers is at odds with the desirability of risk mitigation through mandate and manager diversification.
 - ▶ If all managers are outperforming at the same time, odds are quite high the mandates created are not diversified and will tend to underperform as a group in a different market regime.

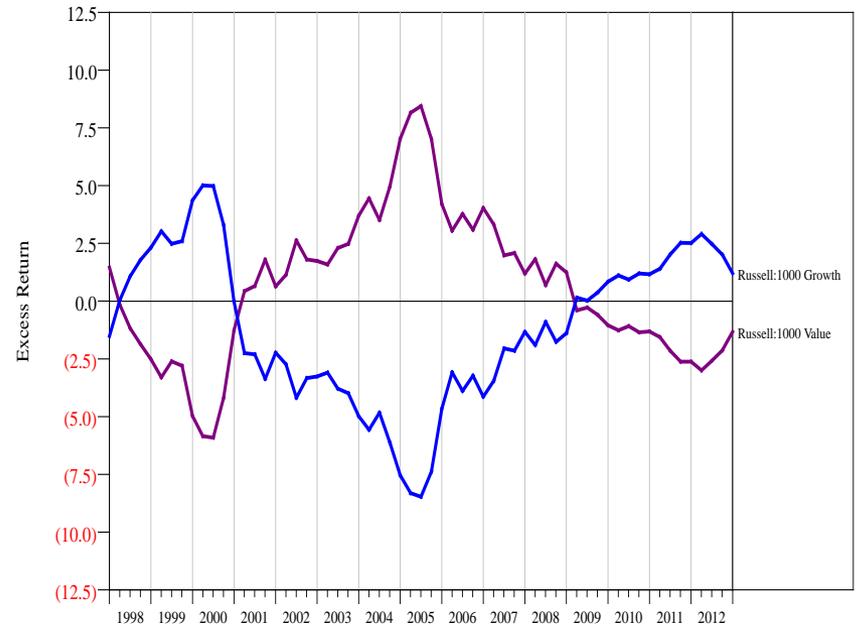
Investment Cycle Awareness

- ▶ Most investments go through cycles, and cycles imply reversion.

Rolling 20 Quarter Excess Return Relative To Barclays:Aggregate Index
for 15 Years Ended December 31, 2012



Rolling 20 Quarter Excess Return Relative To Russell:1000 Index
for 15 Years Ended December 31, 2012



Incumbent Evaluation

- ▶ The wisdom of an evaluation decision is best judged not merely by the manager's relative performance data, but also by:
 - ▶ How well the manager's results fulfilled the **mandate** chosen by the Board.
 - ▶ How well the manager performed versus **direct peers** – those with strategies and products that target a similar mandate.
- ▶ Transitioning funds from one manager to another always carries with it a potential performance penalty (**transaction costs**) for the total fund and the asset class composite.

Incumbent Evaluation

Transition Costs

- ▶ Average Implementation Shortfall Measures by Asset Class
 - ▶ US Equities Large Cap 19 basis points
 - ▶ US Equities Small-Mid Cap 36 basis points
 - ▶ Non-US Equities 32 basis points
 - ▶ Emerging Markets 67 basis points
 - ▶ US Fixed Income 43 basis points
 - ▶ Non-US Fixed Income 63 basis points

Source: State Street Global Markets

Incumbent Evaluation

- ▶ Manager Watch Lists can be useful, but they can also lead to poor termination outcomes if the Review criteria alone become the criteria for the termination decision.
 - ▶ The objective of a Watch List Policy should be to help identify managers that deserve closer scrutiny and ongoing monitoring.
 - ▶ **Watch Lists should not be viewed as Action Lists.**
 - ▶ Managers should not be terminated simply for being on the Watch List for “n” periods of time, as even good managers will experience periods of underperformance.
 - ▶ It is dangerous to focus attention only on trailing returns (and trailing ranks), which are most common Watch List quantitative factors.

Incumbent Evaluation

- ▶ The inherent biases or portfolio positioning that led to outperformance often lead to subsequent underperformance.
- ▶ Consider the **drivers** of positive or negative performance:
 - ▶ Examples: financials, technology, energy, low quality rally, credit spreads, duration, flight to quality.
 - ▶ Are those factors likely to persist? – they often don't
- ▶ Review conviction in:
 - ▶ The manager and their investment process
 - ▶ The stability of the team and firm
- ▶ Consider rebalancing rather than terminating.

SIB Managers Currently Under Review

Manager	Pool	Review Inception	Reason	Status
Bank of North Dakota	Pension, Insurance	Oct-12	Pension transition error	Remedy pending, Staff recommends termination and transition to State Street
Calamos	Pension	Feb-13	Nick Calamos resignation as co-CIO, Gary Black hiring as co-CIO	Ongoing review, on-site visit pending
Clifton Group	Pension, Insurance	Nov-12	Acquisition by TD Bank Group	Ongoing review, acquisition closed
Credit Suisse	Pension, Insurance	Aug-12	Credit Suisse announced intention to divest Customized Fund Investment Group (CFG)	Ongoing review, sale pending
Epoch Investment Partners	Pension	Dec-12	Acquisition by Parametric Portfolio Associates	Ongoing review, on-site visit pending
Loomis Sayles	Pension	Oct-12	Full Discretion co-PM Kathleen Gaffney departure	Ongoing review of two additions to Full Discretion team and Dan Fuss succession plan
State Street	Pension	Jun-12	Process change: Addition of dynamic component to existing static model	Ongoing review of dynamic model, contingent upon global equity mandate structure review

Manager Review – Bank Of North Dakota

Executive Summary

Recommendation

Staff recommends terminating the passive fixed income mandates managed by the Bank of North Dakota as a result of the investment process employed by the Bank of North Dakota in the management of index mandates and the availability of pure passive mandates with a lower management fee and less tracking error. As of February 28, 2012, the Bank of North Dakota managed approximately \$47 million in Pension Trust (BC Long Treasury) and \$113 million in Insurance Trust (BC Government/Credit) passive fixed income assets.

Rationale

I. Investment Process

The Bank of North Dakota's investment process is dependent upon on a monthly cycle of index data downloads from Wilshire, account reconciliations, and trade rebalancing necessary to align the accounts to the benchmark indices. Based on past experience, the average completion date for the rebalancing process falls between the 15th and 20th of the month. Furthermore, position exposure monitoring to review portfolio holdings for sources of index deviation occurs monthly. In the opinion of Staff, this monthly process is less efficient from a risk budgeting standpoint, as it creates additional active risk (tracking error) in obtaining fixed income beta exposure.

II. Lower Cost Alternative with Lower Tracking Error

Bank of North Dakota's current management fee for fixed income passive management is 6 basis points. Historically, the Bank of North Dakota pension fixed income mandate has exhibited tracking error ranging from 35 basis points to 275 basis points over rolling 5-year periods and 170 basis points since inception, while the insurance mandate has exhibited tracking error ranging from 25 basis points to 85 basis points over rolling 5-year periods and 57 basis points since inception.

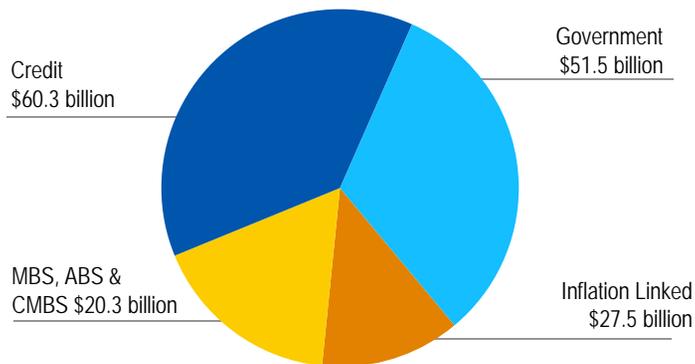
After seeking fee proposals from a number of institutional passive fixed income managers, Staff found a lower cost index solution with State Street Global Advisors, which offers BC Long Treasury and BC Government/Credit commingled accounts at an asset-weighted management fee of 4 basis points. The BC Long Treasury and BC Government/Credit commingled composite tracking error is significantly lower at 3 basis points and 8 basis points, respectively, over the last five years.

In conclusion, Staff recommends the termination of both pension and insurance passive fixed income mandates with the Bank of North Dakota and transition of incumbent assets to State Street Global Advisors.

Low Cost, Broad Market Exposure

- \$328.4 billion total global indexed bonds under management
- Size and scale helps to manage transaction costs
- Seasoned portfolios help to provide low tracking error

US Fixed Income Index Assets
 \$159.5 billion as of December 31, 2012



Account Type	Assets (\$M)
Separately Managed	\$43,920
Commingled	70,746
Mutual Funds	23,152
ETFs	21,699

New Strategies

Short Duration High Yield

International Treasury

Crossover/Split-Rated Corporate Bonds

1-5 Year IG Floating-Rate Notes

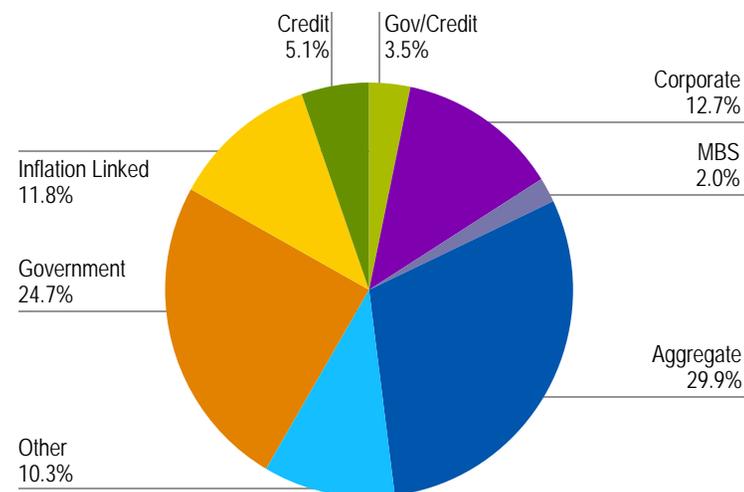
Issuer Scored Corporate Index

Emerging Market Corporate Debt

SSgA Global Beta Capabilities

Experience	<ul style="list-style-type: none"> • Among the largest Fixed Income managers; beta strategies managed since 1996 • Managers have more than 13 years experience on average
Size and Scale	<ul style="list-style-type: none"> • 40 beta strategies offered across the globe • Approximately 100 commingled fixed income beta vehicles worldwide • Management against 45 Global, 60 US and 95 European benchmarks • Sizable, seasoned portfolios help consistently manage index returns
Exposure	<ul style="list-style-type: none"> • Management in more than 30 currencies • Coverage of more than 1,000 issuers from 40 different countries
Coverage	<ul style="list-style-type: none"> • Management across 7 investment centers (Boston, London, Montreal, Singapore, Sydney, Paris and Tokyo)
Access	<ul style="list-style-type: none"> • Offerings across 12 index providers globally • Broad selection of indices allows for creation of portfolios with custom benchmarks, client-specific durations and individualized rebalancing

Indices Under Management*



Global Team

- More than 35 portfolio managers, dedicated beta trading desk
- More than 33 additional beta investment professionals (traders, credit analysts, quantitative analysts, product specialists)
- About 40 operations, accounting and information technology staff around the globe

* As of December 31, 2012. Other includes: Cash, Custom Indices, Multi-sector indices, Securitized ABS and CMBS and Swaps.

Long U.S. Treasury Index Strategy

31 DECEMBER 2012

FIXED INCOME | FACT SHEET

Investment Objective

The Strategy seeks an investment return that approximates as closely as practicable, before expenses, the performance of its benchmark index over the long term.

Benchmark

Barclays U.S. Long Treasury Bond Index

Investment Strategy

The Strategy is managed using a "passive" or "indexing" investment approach, by which SSgA attempts to replicate, before expenses, the performance of the Index. The Strategy will not necessarily own all of the securities included in the Index.

The Strategy may attempt to invest in the securities comprising the Index, in the same proportions as they are represented in the Index. However, due to the diverse composition of securities in the Index and the fact that many of the securities comprising the Index may be unavailable for purchase, it may not be possible for the Strategy to purchase some of the securities comprising the Index. In such a case, SSgA will select securities for the Strategy comprising a portfolio that SSgA expects will provide a return comparable to that of the Index.

SSgA expects that it will typically seek to replicate index returns for the Portfolio through investments in the "cash" markets - actual holdings of debt securities and other instruments - rather than through "notional" or "synthetic" positions achieved through the use of derivatives, such as futures contracts or swap transactions (except in the unusual case where SSgA believes that use of derivatives is necessary to achieve an exposure that is not readily available through the cash markets).

The Strategy's return may not match the return of the Index.

Key Facts

- Is passively managed
- Does not normally use futures or other derivatives to create "notional" or "synthetic" index exposures
- May lend its portfolio and enter into repurchase agreements (See applicable governing documents for a Portfolio's authority to lend. Participation in a securities lending program may adversely affect the investment returns and risk profile of the Portfolio. See "Selected Risk Factors-Securities Lending Risk; Risks of Investment Collateral" in the Strategy Disclosure Document)
- May invest in other investment pools, including other State Street products
- Is not a leveraged strategy
- Will not sell securities short

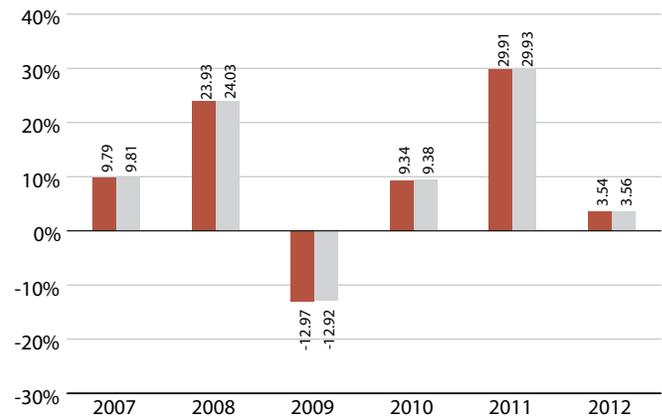
Risk Management

SSgA monitors the overall risk of the Strategy, in order to avoid unintended risk relative to the Index. SSgA manages portfolio characteristics and transaction costs in a manner intended to provide a return as close as practicable to the benchmark return.

Performance

Total Returns	Composite	Benchmark
Q4 2012	-0.77%	-0.77%
YTD	3.54%	3.56%
1 Year	3.54%	3.56%
3 Year	13.72%	13.75%
5 Year	9.67%	9.71%
10 Year	N/A	N/A
Inception to Date (May 2003)	7.62%	7.67%

Calendar Year Returns



■ Long U.S. Treasury Index Composite
■ Barclays U.S. Long Treasury Bond Index

All returns greater than 1 year are annualized. Performance shown represents past performance. Past performance is not a guarantee of future results. Current performance may be lower or higher than the performance shown above. The performance figures contained herein are provided gross of investment management fees and reflect all items of income, gain and loss and the investment of dividends and other income. Index returns are unmanaged and do not reflect the deduction of any fees or expenses. Index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income.

Performance of certain portfolios within the Composite is net of administrative costs. The performance figures above do not take account of the mark to market value of the units of the securities lending cash collateral pools held by any of the Portfolios in the Composite. If the mark to market unit value of the securities lending cash collateral pools were reflected, the performance may be lower. Please see the securities lending risk factor in the Strategy Disclosure Document for more information. Performance returns are calculated in US dollars.

Investment Manager

The Strategy is managed by State Street Global Advisors (SSgA), the investment management division of State Street Bank and Trust Company, and a global leader in providing investment management services to clients worldwide. SSgA has been selected by many worldwide industry leaders to provide premier investment management services. To learn more about SSgA, visit our web site at www.ssga.com.

For the purpose of complying with the Global Investment Performance Standards (GIPS®), the firm ("SSgA-Global") is defined as all portfolios managed across the global offices of State Street Global Advisors (SSgA) and SSgA Funds Management, Inc., with the exception of business units which are held out to the market place as distinct business entities - the Office of the Fiduciary Advisor (OFA) and Charitable Asset Management (CAM). Prior to 1/1/2011, SSgA-Global also excluded its wrap fee business (Intermediary Business Group [IBG]) and assets accounted for on a book value basis (global cash and stable value assets). In January 2011, SSgA acquired the Bank of Ireland Asset Management Limited (now known as SSgA Ireland Limited), a GIPS® Compliant firm. On 1/1/2012 SSgA Ireland Limited assets were merged into SSgA-Global.

The performance figures contained herein do not reflect the deduction of advisory fees which could reduce the return.

The Long U.S. Treasury Index Composite (the "Composite") seeks to match the total rate of return of the Barclays Long U.S. Treasury Bond Index each calendar year.

The Barclays U.S. Long Treasury Bond Index is a trademark of Barclays, Inc.

To receive a complete list and description of SSgA-Global's composites and/or a GIPS® compliant presentation, please contact your SSgA Representative.

This document provides summary information regarding the Strategy. It should be read in conjunction with the Strategy's Disclosure Document, which is available from SSgA. The Strategy Disclosure Document contains important information about the Strategy, including a description of a number of risks.

Supplemental Information**Characteristics**

Average Credit Quality	AAA
Average Effective Convexity	3.82
Average Effective Maturity	24.36
Average Yield to Worst	2.66%
Composite Assets Under Management (\$M)	\$3,636.32
Effective Duration	16.73
Total Number of Holdings	39

Top Issuers

US/T	99.98%
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Sector Allocation

TREASURY	99.98%
CASH	0.02

Supplemental Information**Credit Quality Breakdown**

Aaa	100.00%
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Important Message About Risk

There are risks involved with investing, including possible loss of principal. Risks associated with fixed income securities include, but are not limited to, interest rate risks; the risk of issuer default, and inflation risk. This effect is usually pronounced for longer-term securities. Any fixed income security sold or redeemed prior to maturity may be subject to a substantial gain or loss. Government bonds and corporate bonds generally have more moderate short-term price fluctuations than stocks, but provide lower potential long-term returns. U.S. Treasury Bills maintain a stable value if held to maturity, but returns are generally only slightly above the inflation rate.

Additionally, an investment in the Strategy is subject to a number of risks, which include but are not limited to: Call Risk, Cash Position Risk, Conflict of Interest Risk, Counterparty Risk, Credit Risk, Custodial Risk, Debt Securities Risk, Defensive Investing Risk, Derivatives Risk, Extension Risk, Geographic Concentration Risk, Income Risk, Index Risk, Inflation-Indexed Securities Risk, Interest Rate Risk, Investment Risk, Issuer Risk, Large Shareholder Risk, Leveraging Risk, Limited Investment Program Risk, Liquidity Risk, Lower-Rated Securities Risk, Market Risk, Market Disruption and Geopolitical Risk, Mortgage and Other Asset-Backed Securities Risk, Municipal Obligations Risk, Portfolio Turnover Risk, Prepayment Risk, Repurchase Agreement Risk, Risk of Investment in Other Pools, Tax Risk, U.S. Government Securities Risk, Valuation Risk, and Variable and Floating Rate Securities Risk. You should refer to the Strategy's Disclosure Document for a complete description of the risks of investing in the Strategy.

Risk management does not promise any level of performance or guarantee against loss of principal. SSgA encourages investors to seek the advice of well-qualified financial and tax advisors, accountants, attorneys and other professionals before making any investment or retirement decision.

Securities Lending

The Strategy may participate in an agency securities lending program sponsored by State Street Bank and Trust Company (the "lending agent") for the purpose of lending (up to 100%) of the Strategy's securities and investing the collateral in a collateral reinvestment fund (the "Collateral Pool"). The Collateral Pool is not a money market fund registered with the U.S. Securities and Exchange Commission or FDIC-insured bank deposits or otherwise guaranteed by SSgA or State Street Bank and Trust Company or any of their respective affiliates. The net asset value of the Collateral Pool is subject to market and other conditions, will fluctuate and may decrease in the future. Investors may lose money by participating in securities lending and through investments in the Collateral Pool. For more information on SSgA's securities lending program and the Collateral Pool you should review the "SSgA Securities Lending Program Disclosure", the "US Cash Collateral Strategy Disclosure Document" and the current fact sheet for the Collateral Pool (which include the mark-to-market unit prices) in conjunction with the Strategy's Disclosure Document which contains important information about the Strategy including a description of a number of risks. Copies of these documents are available on SSgA's Client's Corner or you may contact SSgA.

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U.S. Government/Credit Bond Index Strategy

31 DECEMBER 2012

FIXED INCOME | FACT SHEET

Investment Objective

The Strategy seeks an investment return that approximates as closely as practicable, before expenses, the performance of its benchmark index over the long term.

Benchmark

Barclays U.S. Government/Credit Bond Index

Investment Strategy

The Strategy is managed using a "passive" or "indexing" investment approach, by which SSgA attempts to replicate, before expenses, the performance of the Index. The Strategy will not necessarily own all of the securities included in the Index.

The Strategy may attempt to invest in the securities comprising the Index, in the same proportions as they are represented in the Index. However, due to the diverse composition of securities in the Index and the fact that many of the securities comprising the Index may be unavailable for purchase, it may not be possible for the Strategy to purchase some of the securities comprising the Index. In such a case, SSgA will select securities for the Strategy comprising a portfolio that SSgA expects will provide a return comparable to that of the Index.

SSgA expects that it will typically seek to replicate index returns for the Portfolio through investments in the "cash" markets - actual holdings of debt securities and other instruments - rather than through "notional" or "synthetic" positions achieved through the use of derivatives, such as futures contracts or swap transactions (except in the unusual case where SSgA believes that use of derivatives is necessary to achieve an exposure that is not readily available through the cash markets).

The Strategy's return may not match the return of the Index.

Key Facts

- Is passively managed
- Does not normally use futures or other derivatives to create "notional" or "synthetic" index exposures
- May lend its portfolio and enter into repurchase agreements (See applicable governing documents for a Portfolio's authority to lend. Participation in a securities lending program may adversely affect the investment returns and risk profile of the Portfolio. See "Selected Risk Factors-Securities Lending Risk; Risks of Investment Collateral" in the Strategy Disclosure Document)
- May invest in other investment pools, including other State Street products
- Is not a leveraged strategy
- Will not sell securities short

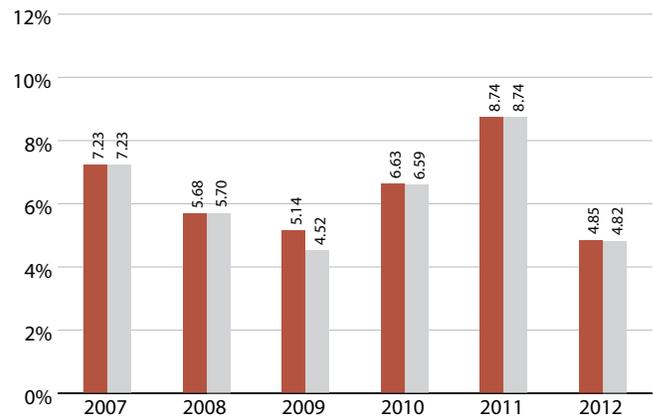
Risk Management

SSgA monitors the overall risk of the Strategy, in order to avoid unintended risk relative to the Index. SSgA manages portfolio characteristics and transaction costs in a manner intended to provide a return as close as practicable to the benchmark return.

Performance

Total Returns	Composite	Benchmark
Q4 2012	0.40%	0.37%
YTD	4.85%	4.82%
1 Year	4.85%	4.82%
3 Year	6.73%	6.70%
5 Year	6.20%	6.06%
10 Year	5.30%	5.25%
Inception to Date (Jan 1997)	6.28%	6.26%

Calendar Year Returns



■ U.S. Government/Credit Bond Index Composite
■ Barclays U.S. Government/Credit Bond Index

All returns greater than 1 year are annualized. Performance shown represents past performance. Past performance is not a guarantee of future results. Current performance may be lower or higher than the performance shown above. The performance figures contained herein are provided gross of investment management fees and reflect all items of income, gain and loss and the investment of dividends and other income. Index returns are unmanaged and do not reflect the deduction of any fees or expenses. Index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income.

Performance of certain portfolios within the Composite is net of administrative costs. The performance figures above do not take account of the mark to market value of the units of the securities lending cash collateral pools held by any of the Portfolios in the Composite. If the mark to market unit value of the securities lending cash collateral pools were reflected, the performance may be lower. Please see the securities lending risk factor in the Strategy Disclosure Document for more information. Performance returns are calculated in US dollars.

Investment Manager

The Strategy is managed by State Street Global Advisors (SSgA), the investment management division of State Street Bank and Trust Company, and a global leader in providing investment management services to clients worldwide. SSgA has been selected by many worldwide industry leaders to provide premier investment management services. To learn more about SSgA, visit our web site at www.ssga.com.

For the purpose of complying with the Global Investment Performance Standards (GIPS®), the firm ("SSgA-Global") is defined as all portfolios managed across the global offices of State Street Global Advisors (SSgA) and SSgA Funds Management, Inc., with the exception of business units which are held out to the market place as distinct business entities - the Office of the Fiduciary Advisor (OFA) and Charitable Asset Management (CAM). Prior to 1/1/2011, SSgA-Global also excluded its wrap fee business (Intermediary Business Group [IBG]) and assets accounted for on a book value basis (global cash and stable value assets). In January 2011, SSgA acquired the Bank of Ireland Asset Management Limited (now known as SSgA Ireland Limited), a GIPS® Compliant firm. On 1/1/2012 SSgA Ireland Limited assets were merged into SSgA-Global.

The performance figures contained herein do not reflect the deduction of advisory fees which could reduce the return.

The U.S. Government/Credit Bond Index Composite (the "Composite") seeks to match the total rate of return of the Barclays Government/Credit Bond Index each calendar year.

The Barclays U.S. Government/Credit Bond Index is a trademark of Barclays, Inc.

To receive a complete list and description of SSgA-Global's composites and/or a GIPS® compliant presentation, please contact your SSgA Representative.

This document provides summary information regarding the Strategy. It should be read in conjunction with the Strategy's Disclosure Document, which is available from SSgA. The Strategy Disclosure Document contains important information about the Strategy, including a description of a number of risks.

Supplemental Information**Characteristics**

Average Credit Quality	AA3
Average Effective Convexity	0.76
Average Effective Maturity	7.99
Average Yield to Worst	1.54%
Composite Assets Under Management (\$M)	\$959.49
Effective Duration	5.94
Total Number of Holdings	4,897

Top Issuers

US/T	53.28%
FNMA	2.67
FHLMC	2.41
FHLB	1.10
EIB	0.87
GE	0.81
KFW	0.81
JPM	0.78
BAC	0.77
GS	0.68

Sector Allocation

TREASURY	53.29%
CORPORATE - INDUSTRIAL	17.79
CORPORATE - FINANCE	10.21
NON CORPORATES	7.98
AGENCY	6.98
CORPORATE - UTILITY	3.45
CASH	0.31

Top Countries

UNITED STATES	88.12%
CANADA	2.03
SUPRANATIONAL	2.00
UNITED KINGDOM	1.20
GERMANY	1.16
BRAZIL	0.82
MEXICO	0.78
AUSTRALIA	0.47
NETHERLANDS	0.39
JAPAN	0.36

Supplemental Information**Credit Quality Breakdown**

Aaa	62.07%
Aa	6.48
A	15.78
Baa	15.67

Important Message About Risk

There are risks involved with investing, including possible loss of principal. Risks associated with fixed income securities include, but are not limited to, interest rate risks; the risk of issuer default, and inflation risk. This effect is usually pronounced for longer-term securities. Any fixed income security sold or redeemed prior to maturity may be subject to a substantial gain or loss. Government bonds and corporate bonds generally have more moderate short-term price fluctuations than stocks, but provide lower potential long-term returns. U.S. Treasury Bills maintain a stable value if held to maturity, but returns are generally only slightly above the inflation rate.

Additionally, an investment in the Strategy is subject to a number of risks, which include but are not limited to: Call Risk, Cash Position Risk, Conflict of Interest Risk, Counterparty Risk, Credit Risk, Custodial Risk, Debt Securities Risk, Defensive Investing Risk, Derivatives Risk, Extension Risk, Geographic Concentration Risk, Income Risk, Index Risk, Inflation-Indexed Securities Risk, Interest Rate Risk, Investment Risk, Issuer Risk, Large Shareholder Risk, Leveraging Risk, Limited Investment Program Risk, Liquidity Risk, Lower-Rated Securities Risk, Market Risk, Market Disruption and Geopolitical Risk, Mortgage and Other Asset-Backed Securities Risk, Municipal Obligations Risk, Portfolio Turnover Risk, Prepayment Risk, Repurchase Agreement Risk, Risk of Investment in Other Pools, Tax Risk, U.S. Government Securities Risk, Valuation Risk, and Variable and Floating Rate Securities Risk. You should refer to the Strategy's Disclosure Document for a complete description of the risks of investing in the Strategy.

Risk management does not promise any level of performance or guarantee against loss of principal. SSgA encourages investors to seek the advice of well-qualified financial and tax advisors, accountants, attorneys and other professionals before making any investment or retirement decision.

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POLICY TYPE: INVESTMENTS

POLICY TITLE: PERFORMANCE RELATED INVESTMENT MANAGER REVIEW

The North Dakota State Investment Board (SIB) recognizes the inherent importance of assessing an investment manager because of performance. Thus, the following process of evaluation includes quantitative *and* qualitative input. This procedure is structured to assist the SIB in recognizing potentially distressed investment managers, initiating a formal review process, and providing guidelines for termination if necessary. Note: The “Manager Review” terminology or concept is not meant to cause the manager to make substantive changes in investment philosophy, style, or strategies. Rather, it is intended to define a period of close scrutiny of the manager’s activities, circumstances, and investment results.

Factors which may result in a Manager Review:

Significant changes in organizational structure

Significant changes in investment philosophy

Significant deviation in portfolio management from stated philosophy (style drift)

Substandard investment performance

Diminished confidence in manager

Manager Review Procedures:

Information is submitted to, or generated by, the Board which initiates consideration of a Manager Review.

If warranted, the Board takes action to initiate a Manager Review.

Based on the situation and with input from the Investment Director, the SIB suggests appropriate action to facilitate the Review. Action may include telephone conferencing, local or on-site visits with manager, investigation by consultants, appearance of manager before a select committee of the SIB, or appearance of the manager before the SIB. Investment Director initiates investigation of situation based on direction from SIB.

The Investment Director report’s findings to SIB at a subsequent meeting.

After considering findings of the Manager Review, SIB may:

- Remove manager from Review status
- Suggest additional action to facilitate Manager Review
- Relieve manager of duties

POLICY TYPE: INVESTMENTS

POLICY TITLE: *PERFORMANCE RELATED INVESTMENT MANAGER REVIEW*

In the case where continued investigation is warranted, the Investment Director will report new information and/or recommendations to the SIB as appropriate. It will be considered the responsibility of the Investment Director to maintain awareness and consideration of the Review until the situation is resolved.

It is important to recognize that situations occasionally arise of such a serious nature that a Manager Review process must be immediately initiated. In such cases, the Investment Director is granted the authority to place an investment manager under Review, including the freezing of assets if necessary, and report on such action at the next meeting of the State Investment Board.

In every case, the Investment Director is responsible for documenting the Manager Review process including recognition of:

- Reason of Manager Review
- Action taken to investigate the situation
- Report on results of investigation
- Report on resultant action taken by SIB
- Notification of investigation and conclusions to manager and consultants

A complete record of Manager Review activities and history shall be maintained at the ND Retirement and Investment Office.

Policy Implemented: June 27, 1997.