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Trustee

Defined Benefit Plan
Quarter Ended June 30, 2012
Performance Meetings & Annual Manager Reviews

August 29, 2012
Retirement Fund Conference Room

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Board of Trustees Present:
Joe T. San Agustin, Chairman, Board of Trustees
Wilfred P. Leon Guerrero, Ed.D, Chairman, Investment Committee
Gerard A. Cruz, Trustee

Staff Present:
Paula M. Blas, Director
Diane Bernardo, Controller
Rosalie Bordallo, General Accounting Supervisor

Other Present:
Maggie Ralbovsky, Wilshire Associates

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10:00am-10:45am Economic & Capital Market Environment

Maggie Ralbovsky: Okay, I'm going to start with page 4. What a difference a quarter made. If you recall last quarter we talked about a huge rally in the market place because people elected not to think about Europe for the moment in time and for the 2nd quarter however, the huge issue came back and that coupled also with the slowdown in the U.S. which made people start to draw a parallel with this year and last year and the year before. If you think of, if you take a step back, think about 2010 and 2011 in both of those years the year before the Government had some stimulus program done. The first quarter of those 2 years including this year as well had been very strong growth which had made the private sector believe or think there is a possibility that growth was sustainable and then when we enter into the 2nd quarter of all these 3 years, the stimulus effect started to wear off and then it became clear that further stimulus was necessary because the private sector growth was actually spurred by the shot from the stimulus programs which were not self sustaining. So now here today after the 2nd quarter you can see some indicators in the statistics. I circled some important ones, for example, on page 4 you can see in this table I circled CPI which is the inflation indicator, for the 2nd quarter it was zero, the quarter before it was negative, this is very, very low, this is dangerously low. The reason low inflation is bad is because deflation is something that's a slippery slope, when deflationary pressure started to take hold in the market, it's just self fulfilling because people will just be waiting for the price to go down then they wouldn't spend, so it's self fulfilling which is bad. Japan has been dealing with this for 20 years and couldn't get out of it. Now we don't feel like prices are going down but the official measure of the CPI is going down that is one indicator that is negative. Another indicator that is negative is the 2nd bubble on this page you can see that in the June quarter the manufacturing sector was actually below 50, the number 50 is a psychologically important number when people think about below 50 for the purchasing manager index they think of contraction, so this is very close to 50, it's not officially labeled as a contraction but if it's much more less than 50 people may fear a double dip so these are bad indicators to watch which actually made Goldman make a call to say for the September 14th meeting, for the Fed meeting they're going to announce the QE3, that's Goldman's bet, September 14 is the date we want to watch, although most of the other market participants don't believe QE3 will be announced, but they do believe that the Government, the FED is going to extend it's current operational twist which means the Government, the FED is actually going to continue to buy mortgage securities to support the longer end of the yield curve to make the interest rate go down. So, that's what the U.S. looks like which is not terrible, because we just have a sluggish recovery, which has been expected.

Now I'm going to skip the next couple of pages, these next few pages are trying to prove the message which we have delivered in the first page.

I'm going to move to page 10. Page 10 are the returns for the stock market for the past quarter, but you can see that's all negative across the board. Let me address Doris (Brooks) comment earlier to say, the Fund has not been making enough money. Well, the Fund doesn't print money it really has to take advantage of the opportunities in the market place and the market has been very turmoil in the past 10 years, it doesn't have opportunities to make money as we have done a long time ago in the 1980's. So really that is not something that we can change, but with regard to the 7% expected return, if that return expectation is lowered it's actually going to mean lower contribution percentage. Doris Brooks: I know, I'm not saying... where does the Fund stand let's say on a 10 year return because the comment that I was hearing... Maggie Ralbovsky: It's about 6.7. Doris Brooks: No, relative to all of our peers, is that low? Maggie Ralbovsky: We're still in the 80th percentile. 10 years top 3%. Gerard Cruz: And keep in mind, I don't mean to interrupt, but keep in mind 10 years includes 2007 and 2008. Doris Brooks: Right which were rough years. Maggie Ralbovsky: And 2003. Gerard Cruz: And 2003 which was also equally devastating. But to address that question really requires a long answer, you can't do it in a sound byte so it's hard to go through that... Maggie Ralbovsky: Everybody knows that however you could actually point out the fact that interest rates have been going down and if every investment is priced off the interest rate because you can buy Treasury bond for 5%, that's 15 years ago, you can buy Treasuries at 5%, then stocks will be returning more than 5% because people take risks, they demand more return. Today you buy a 10 year Treasury it gives you 1.5%, can you demand 5%, can you demand 6% above that? It is just not there. So when people talk about returns, they really cannot be disconnected with the market environment.

So that aside, we can see that this quarter was a negative quarter which was partially due to the U.S. slow down but mainly due to Spain and European issues, people call his the battle of Spain and actually September 7th is a key date to look at when the ECB is going to announce their supposedly their effort to make the Eurozone a more unified fiscal union. We know that up until this point they were sort of not really a unified fiscal union, they were just a monetary union, but everybody still spends their own money and it doesn't have a coordinated budget and that was part of the reason we came to face a possible breakup of the union because the southern European countries are just spending, spending without the responsibility in the eyes of the northern European union, they just felt like they're saving money to save the southern part of the union.

Now we know that after the end of the 2nd quarter the equity market actually rallied in August especially because this is Dr. Drage's comment, "Euro is not breaking up, we're doing whatever it takes to make this a true fiscal union." That's all, a few words, he didn't say anything as to how they're going to do this, but the market took that optimism and tried to enjoy a little bit rally. Now he is suppose to reveal the details on September 7th, so the market participants on the one side hope they really have a plan, on the other side they're very skeptical because how many times have we hoped and how many times have we been disappointed. So it's possible that September is going to be a very volatile month for the market. So mainly it was because the European situation, U.S. is also going down.

Okay, so we had a negative quarter for the equities and for the fixed income market on page 12. On page 12 you can see that the fixed income market had been where the returns had been generated, we had 2% return for the Aggregate Bond Index. Actually the longer the duration, the better you did, you see the long term Treasury index was up 10% for the quarter. That's when the 10 year Treasury dropped to 1.48%, although that backed up in August when the optimism came back to the market and your Treasury went back to 1.82% I think, 40 basis points rally which was a very dramatic move when Treasuries started at

1.48%. So you can see that the really volatile environment for the fixed income market as well when the Treasury was up 10% for the quarter and was up 32% for the year, for long term Treasury. Gerard Cruz: That's operation twist. Maggie Ralbovsky: Yes, that's operation twist. Gerard Cruz: Because the Fed is buying Treasuries, or I'm sorry, they're buying securities on the long end of the curve, what that does is it brings yields down and brings prices up and so the reduction of that rally are bringing yields down has the effect of causing the securities that you have, the fixed income securities that you have in your portfolio to gain in value. Maggie Ralbovsky: And a few statements that the Fed released they have been saying, we don't expect we'll push rates up until the end of 2013, the end of 2014. Now we're expecting to hear something like the end of 2015. Doris Brooks: Even longer. Maggie Ralbovsky: That's right. Gerard Cruz: That's why mortgage rates are as low as they are. Maggie Ralbovsky: On page 14, this is the non-U.S. equity market. You can see that it did even worse than the U.S. market. The main index which is the top one, ACWI ex US was down 7.4% for the quarter and inside that index there are 2 major components. One component is the EAFE which includes Europe and Japan and Australia and the emerging markets includes the rest of the emerging markets like China, India, Russia, Brazil, Argentina and stuff like that. You can see that the emerging market actually did worse than the EAFE index and partly it was because of the slowdown in China. China had been the growth engine for the world for the past cycle actually, especially after 2008 when the developed markets faltering, China was having 8 or 9% GPD growth in those years, but the most recent thing was actually I think below 7% which was a very, very alarming number. Well we may think that 7% is a great number, but for China they need 7.5% at the minimum to create enough jobs to absorb the population growth, the labor force growth. China had been relying on 2 engines, number one engine was the export and the export business has been very difficult, number one because of the Chinese currency strengthening, number 2 has been because of the very weak demand elsewhere, you export to somebody and nobody is buying so they have seen a lot of foreign factories like Motorola just close all their shops, all their factories in China and some of the car companies are moving their production back to the U.S. and the manufacturing for textiles industry have been moving to South East Asia. A lot of these traditional engines of growth, traditional engines of employment for the Chinese nationals have been moving out of China, they have been experiencing increasing unemployment. So that's the number one engine that's very hard to fix because the Chinese Government cannot do anything to try to promote external demand, there is nothing you can do. The second engine is the property sector, the investment sector, the Chinese GDP is so not balanced like the rest of the world, like you think the U.S. GDP, 75% of the U.S. GDP is consumer spending and that is a very healthy thing when consumers spend, it creates a virtuous cycle because you have the demand to make businesses produce so the consumer can spend, so it is a healthy demand and supply equation.

Now in China the historical growth has been spurred by more than, I think 78% was from investment which mainly the property investment, so every Government, every local Government to show their accomplishment they would convert, they would sell a piece of Government land to some developer to the traditional piece of land would have no fields on it and they would make that into a huge city, huge buildings then the Government could collect taxes from these developments, so that's a very major portion of the engine development. If you think about that, that is not a sustainable thing, how much land you can sell, how many times you can sell land and after you've developed all these things, then what? By some calculation, China has developed the infrastructure for the next 20 years. You build all the apartment buildings that can house people even though they are not being distributed to the people who need it, but rather people who have money are accumulating 5 or 6 different apartments, they're buying these for investment purposes which is an indication of a huge bubble being brewing and the people who actually need housing, if you look at the actual total units being built you should be able to support the population growth but it's not being distributed to the people who need the housing, so in a way you're creating also this tension between the different classes.

So you have this problem and the Government is recognizing that they have a problem and this year is a very sensitive year because it's like every 10 years transition of leadership they have this thing going on so they're trying to beef up the GDP numbers on the service showing to be prosperous they are actually giving money to the rural communities, they just give people if you belong to a rural community. I think it is a last minute effort to try to make peace with these people who couldn't afford anything. At some point this is going to stop and the Government is unable, by many people's view they're unable to transition the economy from an investment driven to a consumption driven because the Government sector is so relying upon the taxation income from the property sector and in order to wean itself from that, it has to cut so much spending, so it's something that it's unable to do.

So that is the huge worry about China hard landing which part of the reason emerging markets is not doing very well and actually there are money managers out there who are forecasting this kind of a bubble burst coming within 3 years. I think GM is one of them who are very outspoken to say the Chinese bubble is going to burst in 3 years. Doris Brooks: I thought it already was. Maggie Ralbovsky: Well, it has not yet, you still see those things going on. Doris Brooks: But things have certainly slowed down. Maggie Ralbovsky: Yes, it's been slowing down. Doris Brooks: What happened to Germany here? Maggie Ralbovsky: Germany is actually one of the most healthiest. Doris Brooks: But look at its returns. Maggie Ralbovsky: It's return is because when people are actually discounting the fact that the Eurozone may break up. Germany has already spent 6% of its GDP to support the peripheral countries. It does have enough money, Germany has enough money to support all those, it's whether they are or they want or they have the will or they have the support, political support to underwrite the entire Eurozone debt. So that is the situation out there. The U.S. is in a terrible slowdown but I guess compared to the rest of the world it's actually the most healthy.

Page 15 I want to show one chart, that's the chart on the bottom. This is an interesting chart to look at which is the decoupling of the market's opinion at different economies in Europe. You can see that the introduction of the Euro in the middle of the chart. After the introduction of Euro these 4 countries their debt are trading very much in tandem, basically the market is viewing them much as the same thing. This is the spread over German, no I'm sorry, this is just the yield not the spread, just the pure yield. Now you can see that after 2008 the decoupling has happened, the market is no longer viewing Spain and Italy the same as Germany and France, actually it's also not viewing France and Germany the same anymore. So the elsewhere of the Eurozone, besides Germany everybody else wants a Eurobond, so basically one bond instead of having all these different sovereign bonds because they know if they have the Eurobond, they're all going to have a lower yield when issuing bonds because it's all going to be trading towards Germany and Germany knows that if they do that, they're borrowing cost is going to go up because the market will discount that risk into the markets. So it is a Germany versus the rest of the Euro kind of discussion right now. There are people who believe that Germany will eventually have to do it with their consensus or not because the already put in so much money into the bail out and if they don't do it, they're just going to lose all that, if they do it they may have a chance to recover, so we'll see. There are other people who think Germany is just using this opportunity to regain their control over the entire Europe.

The real asset, this is the commodity sector, you see that the biggest negative is the commodity index and that is partly because of the slowdown in China, China had been a huge consumer of commodities. If Chinese slowdown continues, the commodity sector probably will not do very well, with the exception of gold, gold even though right now it is being lumped together in the commodities sector, it does have a quasi currency kind of view. I'm going to show you some charts later that showed majority of the currencies in the long run underperformed gold. The people who are now revisiting this issue, we have so much debt issue in the world that the Government has to print money to solve this issue eventually and who is going to win? Gold will become a quasi currency and even though right now it's being lumped together in the commodity sector.

Now I have some charts to show you the global deleveraging. We have talked about deleveraging before, so what is deleveraging? Deleveraging is when the economies are trying to reduce the debt. Doris Brooks: Isn't that good, to reduce debt? Maggie Ralbovsky: Let's take a step back. Starting from 1982, the whole world was in a process called releveraging. In that process everybody is trying to, everybody had the ability to borrow money, the banks could just lend you money and sell to the market place in mortgage backed securities, asset backed securities and all these different derivative backed securities. The releveraging has made the debt level really high; however during this process of releveraging it created a lot of prosperity because you had a lot of liquidity to be invested and to give people to spend to make everything possible, basically if you have liquidity you can make everything possible. In 2008 that has come to a breaking point because it's simply become unsustainable. After that, that's deleveraging. Now deleveraging, is that good or is that bad? Well, it depends on how fast you de-lever because if you do it really, really fast, the pain is actually very, very severe because you basically have to wipe out wealth in the deleveraging process and that's actually what happened in 2008 when house prices dropped, people couldn't pay their mortgages anymore they just basically walked away. Walking away is actually the main default, debt default was the main mechanism in U.S. deleveraging. The reason the U.S. consumer has delevered faster than the rest of the world was because of the default.

In Europe you can't do that, if you just walk away from your house you still owe that debt, your mortgage is still owed and you still have pay from your future salary so it's not an easy thing for you to just default on your mortgage. In the U.S. it's non-recourse, in many, many states it's just non-recourse, like in California you just walk away and then 3 years later you get another loan and you can buy another house. It becomes a rational decision, you can just do that which makes the deleveraging process actually faster. Now the people who hurt in this whole process obviously in the U.S. are the tax payers because the Government basically guaranteed and took over Fannie Mae and Freddie Mac; however those people who own Fannie Mae and Freddie Mac stocks, they were basically wiped out. There are also these other investments that people who invested in the non-agency mortgages, they were wiped out as well, the subprime mortgages, all those were wiped out and anyway, that's beside the point, we're not trying to analyze that. I'm trying to show you the debt level in the world.

Here's the debt level as a percent of GDP. We did draw a line there for 2008, you can see that the deleveraging process is very different in terms of how fast it happened around the world. On the top of the charts you can see Japan and the UK are still levering up, the deleveraging process has not gone very well, partly was because the GDP has been dropping. If you think of this upstairs and downstairs of this equation, if the GDP is not moving up then the debt becomes a heavier burden. Actually Japan is being forecasted as the next shoe to drop. Actually Goldman is projecting that Japan will be out of sources to be issuing bonds by the year 2015 if they keep the current spending level. The reason Japan can sustain so much debt right now, it's close to 500% GDP is because their debt is internal debt. They have this excess cash from the retirement savings and also the excess cash from the corporations just by their own debt. That positive cash flow is going to reverse by 2015 when the aging population starts to take money out of the market and when the corporations excess cash is to be drying up, at some point they will have to rely on external debt and will have no ability to issue debt because who is going to buy JGB for 10 years at 1.8% with the debt level at this point. So it is an issue that is pending, it's just really hanging there. Actually a majority of the people believe Japan is going to default on debt, Japan will default on its debt at some point. Antolina Leon Guerrero: Japan will? Maggie Ralbovsky: Japan will at some point, that's the projection by most people, unless Japan can enter into a structural reform to lower Government spending and enter into a surplus instead of a deficit. Right now it's in a deficit mode, it still has to issue debt to support it. Gerard Cruz: But how do you do that when economic conditions just are not poised for any kind of inflationary pressure? Maggie Ralbovsky: Exactly. It is a huge issue with Japan with the debt level.

Doris Brooks: What debt level is this because you see the... Maggie Ralbovsky: It's a percent of GDP. Doris Brooks: Is that the national debt? Does this include the $16 trillion that the U.S. Government is closing approaching? Maggie Ralbovsky: This is the total debt. It includes that and includes the private sector. This is all public and all private. Doris Brooks: So is this in trillions? Maggie Ralbovsky: Yes. This is percent of GDP. So when you think the U.S. Government debt is approaching $16 trillion, U.S. GDP is $15 trillion, so the U.S. is a little bit over for the public sector over 100%, now you added the private sector. The U.S. is much better compared to the rest of the world even though it's above 200% GDP. The deleveraging is much faster, deleveraging meaning the line is trending down much faster than the rest of the world. Doris Brooks: The line is trending down? Maggie Ralbovsky: After 2008.

It is at the beginning of a de-leveraging process and you study the past de-leveraging process which I have graphed on the next page. It takes about 10 to 20 years, the least it has taken was 10 years. Gerard Cruz: When was the last one? When was the last de-leveraging cycle? Maggie Ralbovsky: Japan is the most recent one. It has already been more than 20 years, it just wasn't a very flexible economy. Doris Brooks: Is this for the world or the U.S.? Maggie Ralbovsky: This is the average for Finnish and Swedish, not the U.S. because the U.S. de-leveraging, the last one was in the 1930's, the Great Depression, so it's too ancient of a decade, this is more recent history, but it tells the same story as every de-leveraging has told us, it takes at least 10 years and could last 20 years. In the U.S. Great Depression case... Gerard Cruz: Or war. Maggie Ralbovsky: War could actually solve that problem too. Doris Brooks: The war hasn't solved this problem. Maggie Ralbovsky: We haven't had a 3rd world war, if we have one it's stimulus and wipe out the old debt and restart.

So, the previous U.S. one took 20 years which was the Great Depression. So anyway, it starts with a severe contraction which is the early stage of recession and that severe contraction is already done, it's done for the U.S. The next phase is the private sector de-leveraging and during the private sector de-leveraging the public sector actually are leveraging up just to make the social pain less painful. So the private sector de-levered first then the public sector started to de-lever. This whole process, this is the process that we are trying to grab here.

Now Europe is at the tail end of the early stage of recession, they're actually still experiencing negative GDP growth. So we can say that the whole world process is actually in the first phase of this, we should expect a very long drawn out process. Gerard Cruz: The U.S. is still in the first phase? Maggie Ralbovsky: No, Europe is. The U.S. is entering the private sector de-leveraging. Gerard Cruz: I think the private sector is pretty much de-levered. Maggie Ralbovsky: No, the household debt is still very higher. Doris Brooks: It's over $20,000, the average household debt. Maggie Ralbovsky: It's still above the trend. Gerard Cruz: Okay, so household is included in that debt. Maggie Ralbovsky: That's right. Gerard Cruz: I was thinking businesses, corporations. Maggie Ralbovsky: I think corporations are doing better, they're more flexible, you can hire people, you can lay off people, the household is less flexible and Government is much less flexible.

We're trying to describe the entire process, eventually it takes printing money. Money printing takes wells transfer and the wells transfer is actually taking hold right now in the U.S. as well when the interest rate is lower than the GDP growth, so basically you're taxing, they have like this stealth tax put on the bond holders, just collecting from the Government debt is paying less than the GDP growth which is a way to collect the wells transfer money, now it also takes default and eventually money printing. Now why does that matter? It matters, I think we talked about this paradigm before and I think it matters in this context to think of the leadership of performance by the different sectors. So, I put these yellow arrows here to show that from the year that from the de-leveraging process to the de-leveraging process to continue to the next phase and eventually to the re-lever again kind of process, different asset classes will have different leaderships. Another thing that's a very interesting study that Bridge Water has done is the fact that during these historical periods, currency and gold, the relationship between currency, they actually studied 750 currencies since 1700 and only 20% of these currencies are still in existence. Among the 20% that's still remaining, they have all devalued by at least 90%, okay, all of them have devalued by at least 90% against gold since the 1700's.

You see that holding cash, I put the table here just to show some of the major currencies here, holding cash versus gold, okay, in the UK pound sterling you lost have lost 99.6%, the U.S. dollar lost 98.7% against gold. So, all these other, Swiss Frank is actually the best performing on which has lost 95.1% during this period. Gerard Cruz: From the 1700's? Maggie Ralbovsky: I'm sorry, from the 1850's, this table is from the 1850's.

Doris Brooks: 750 currencies? Maggie Ralbovsky: 750 currencies and you can see that 20% is still in circulation and 23% ended because of monetary reform and 19% died from debt crisis and 38% died from political transformation. Gerard Cruz: How come gold has kind of leveled off in terms of value over the last year? Maggie Ralbovsky: Because the U.S. dollar has been strengthening.

There are some other things I want to share with the group that are summarized on page 22, because people are now looking at the European Union, the Euro currency and there is this debate whether the Union will sustain and there were 8 currency unions in the past 150 years that Europe has tried to put together and all of them failed. Gerard Cruz: So what do you think the ECB is going to say in September? Maggie Ralbovsky: I think the only thing that could save the Euro for now is have a Pen Euro bond which is basically supported by Germany. Gerard Cruz: But how do you implement fiscal responsibility on all countries that are not in any other way protected? Maggie Ralbovsky: I agree. I don't think it will work, but the market is trying to give the benefit of the doubt. I guess there is so much at stake and also the reason the market is optimistic is that if you look at the entire Eurozone they're actually in surplus, that's why the Euro is so strong right now, the Euro is actually stronger than the U.S. and the U.S. is running deficit and the entire Euro is running surplus, but it is only one country that's running surplus as Germany. So if Germany has the will and it does have the ability to make the entire Eurozone, although if you believe in that, you're ignoring the fact that the cultural difference is so drastic, I think people who live in Europe don't believe that, people elsewhere can believe that because you could mistakenly think Europe as one thing. I think that's a process we eventually will have to...

Joe T. San Agustin: Isn't Germany talking about getting away from the Euro? Maggie Ralbovsky: Germany is not agreeing to... Angela Merkel is not agreeing to the Euro bond because she understands it's Germany that's basically going to guarantee everybody's debt. Joe T. San Agustin: What happens then if the Euro currency... Maggie Ralbovsky: That's another thing they couldn't afford that to break up either. It's unthinkable. There is a parallel to be drawn for 1998 I think when Argentina de-pegged against the dollar, so the Argentina dollar used to be pegged one for one for the U.S. dollar and Argentina debt were all priced against the dollar then they de-pegged that currency and over night the currency devalued 99%. So they basically defaulted all on their debt to the extent they pay 1 cent on the dollar. So that would be one way to wipe out all the debt, start new. Argentina is doing great right now, they're basically transferring wealth.

I think the bottom line, I think last time for us we talked about expanding our investing and our investment opportunity set, I think that's the right thing to do because really the traditional sources of return is being challenged by a very challenging outlook for every

where in the world and we really need to think about finding unconventional sources of return, unconventional ways of expanding our opportunity set.
(End of discussion on Economic & Capital Market Environment)

11:00am-11:45am DB Plan Performance

That being said... Joe T. San Agustin: That being said, where are we now? Gerard Cruz: Do you have an update? Maggie Ralbovsky: I do have an update. Gerard Cruz: This is as of June. Maggie Ralbovsky: July was a good month for us, but June was a tough quarter. Let's look at the returns on page 25. On page 25 we were down 2.6% total fund and also pretty much every composite under performed against its benchmark. Gerard Cruz: Under performed? Maggie Ralbovsky: Yes, under performed. Gerard Cruz: Not fixed income. Maggie Ralbovsky: Fixed income under performed too just in a minor way, I think fixed income under performed by one basis point. For 10 years as of June we were 6.36%, I think there was a question earlier, that actually has beat the benchmark for 10 years.

I think today we're inviting presentations for the real estate managers so maybe you can... Gerard Cruz: They did okay? Maggie Ralbovsky: They did okay, they are not the worst. There are a couple of managers who we will discuss a little more later. Gerard Cruz: Policy index is... Maggie Ralbovsky: Is assuming passively managed. It's assuming everything is passively managed and assuming all the allocation is to the target, we know they're not, we know that number 1, not all the allocation is yet to target, number 2, it is not passively managed.

Doris Brooks: On the year to date, is that for the 9 months ended June 30th? Maggie Ralbovsky: No, calendar year. Doris Brooks: So this is for the 6 months? Maggie Ralbovsky: I'm going to add the calendar year because the question always comes up. I'll add the fiscal year because that question always comes up. Paula Blas: That's only because we operate on a fiscal year basis. Doris Brooks: So my question is, do you know what it is for the 9 months? Maggie Ralbovsky: It's better than this because last quarter was a good quarter. Last quarter of last year was a good quarter. Doris Brooks: So that makes up. Maggie Ralbovsky: Yes, that makes up.

Gerard Cruz: Where do you show us relative to other funds? Maggie Ralbovsky: It's right here, (page 27) you're looking at it. So 1 is a good number, 99 is a bad number. The numbers in the parenthesis are the percentile numbers, for example, for 5 years your return for the total fund is 3.52% and 15th percentile. Doris Brooks: You're in the top 15%. Maggie Ralbovsky: But in the 10 year you're in the top 40%. Doris Brooks: Okay, which is another way of saying we're closer to the bottom. Maggie Ralbovsky: No, top 40. The smaller the number the better, 1 is the best, 100 is the worst. Doris Brooks: Look at the 1st quarter. Maggie Ralbovsky: The 1st quarter you were in the 64th percentile so we didn't do very well. This Fund we have observed last time that it correlates with the performance very strongly because it's a growth... it paid off in the long run because it correlates with that kind of a cycle. Doris Brooks: So this is 3 quarters for the fiscal year? Maggie Ralbovsky: It's 3 quarters for the fiscal year, that's right, so that answers your question. Doris Brooks: For 10 years there are only 51 funds compared to 5 years there were 62 funds? Maggie Ralbovsky: Right, but these are randomly collected funds, they're very consistent with the entire universe.

Joe T. San Agustin: Is that going to affect the trend, what you're projecting in the next 2-3 months? Gerard Cruz: Volatility? Joe T. San Agustin: Yes. What does it mean, what are we looking at next quarter, are we going to go up or down? Maggie Ralbovsky: If September does not mess us up we should be very close to this number here. Joe T. San Agustin: Well this is August now. Maggie Ralbovsky: September 7 is the European Union decision, September 14 is the Fed's decision. Joe T. San Agustin: So there are things that might affect... Maggie Ralbovsky: Things that are being discounted in the market place and these events may disappoint either way or, it may be positive, it may be negative. Joe T. San Agustin: Is the market so volatile that we could be affected by those changes? Maggie Ralbovsky: If you think of 3rd quarter last year, international market was down 20% for that quarter alone, U.S. small cap was down close to 20% in the 3rd quarter which all happened within a month. Joe T. San Agustin: On a quarterly basis, but if you go by a yearly basis, from a historical trend projected based on last quarter, the effect is not going to be so significant because it hasn't shown a significant effect in the last 10 years. Maggie Ralbovsky: Right. If you look at longer term, one quarter is a very small number. Joe T. San Agustin: That's what I mean. On a quarterly basis you have to worry, on annual basis you don't have to. Maggie Ralbovsky: That depends on what you worry about this for. Joe T. San Agustin: I'm worried about stability. Gerard Cruz: Then the long run is what we need to look at, but having said that, you don't get to the long run unless you win on the short run. Joe T. San Agustin: I worry about that but then I do watch and then I can make some adjustments. Gerard Cruz: But the Fund's time horizon is... Joe T. San Agustin: The reporting process we're getting on a monthly basis. Gerard Cruz: But going into the next month and ending this year which is I think is your question, where are we in terms of volatility is the good question to ask the managers as they come in because we know 2 big announcements are going to come on the 7th and the 14th. Joe T. San Agustin: How would that affect... Gerard Cruz: We should ask them, how would they position the portfolio given the 2 big announcements.

Maggie Ralbovsky: Speaking of that, we're going to meet with managers in the small cap tomorrow and today is the REITS. Joe T. San Agustin: Are these REITS all over the world? Gerard Cruz: I think they're primarily U.S. Maggie Ralbovsky: Only U.S. property. Joe T. San Agustin: They don't have anything in China or any where else? Maggie Ralbovsky: No. Joe T. San Agustin: That's where the movement is, there is a lot of real estate movement in Hong Kong. Maggie Ralbovsky: We don't currently have investments there for that, but you do have international to the extent that the properties are publicly traded, you are probably holding something somewhere, but not in the REIT portfolio, the REIT portfolio is only in the U.S.

Let's take a look at your managers on page 37. We have one manager that out performed which is INTECH, all the other managers under performed. We do currently have 2 managers on watch, one is Eaton Vance, one is Numeric and these are the 2 managers who are going to present tomorrow. Both of them are on watch for different reasons, Numeric was on watch because of the departure of their portfolio manager. Gerard Cruz: Was he a manager or was he just client services? Maggie Ralbovsky: No, he was the lead manager, Arup Datta, he was actually the main person in the small cap area. Gerard Cruz: His wife was also a manager? Maggie Ralbovsky: A fundamental manager, she was in a different firm. When he came here to present the timing was curious because after he left he quit and after he quit he said he was going to start his own firm, which he did and then recently he actually folded his firm and joined a competitor. So he was an important person, but after he left I did meet with his other team mates. It appears to me that they really have a very deep bench, his departure is a loss but I really think they have enough resources to keep this process to keep this process going, so I am optimistic that come the end of 2012 we can drop them from the watch list, but right now they're on the watch list until the end of 2012. Antolina Leon Guerrero: But this under performance isn't related to that? Maggie Ralbovsky: No, they're not under performing since inception, they're under performing 50 basis points for this quarter. Joe T. San Agustin: So you're going to watch them until the end of the year? Maggie Ralbovsky: Yes, because of organizational issues, not because of performance issues. They are not under performing since inception. Joe T. San Agustin: But you have them as under performing now. Maggie Ralbovsky: Just for this quarter. They actually out performed, on page 44 if you want to take a look at the numbers, they out performed by 3.5% annualized since inception so this is actually a very good manager, so they're not being on watch for that reason, but rather to see if Arup Datta's departure means anything else.

Eaton Vance is on watch, however because of performance reasons and they have continued to under perform. Gerard Cruz: Did you talk to Nancy (Tooke)? Maggie Ralbovsky: Actually I did. She has been doing this for a long time, for 30 years and she has been following a particular process and historically had been successful, but recently had been very unsuccessful and she had been saying that's because the market was not trading on fundamentals which may be true, at the same time what if this is the new normal? So the question is, can you really just say the market, I'm right, the market is wrong and what if the market doesn't get corrected? Rosalie Bordallo: How long would you keep Eaton Vance on watch? Maggie Ralbovsky: That's a great question because they have been under performing since inception. This manager was hired 2 years ago, less than 2 years ago, so we usually give a manager 3 years because that's what they say, that's a market cycle so I would like to keep them unless they do something else that made us lose confidence. So right now everything seems to be same old, same old with the exception that performance was bad. They're coming tomorrow. The thing that bothered me is they're saying, it's a junk rally, we couldn't do well but the next quarter it becomes a quality rally and they still didn't do well, they didn't catch either wave which was the thing that was a little concerning. Doris Brooks: And their spread is quite large, 5%, 7%. Gerard Cruz: It's not like they have to look outside the measure of currency risk. Rosalie Bordallo: So that's why I'm saying when are we going to...? Maggie Ralbovsky: 3 years will be next year and if in this period if they under perform every quarter then I think probably we should consider...

Another thing I want to show you may also impact their performance was on page 41. If you look at page 41, let me explain this chart. Every stock can be given a score based on how growthy they are, how value-y they are. So what is value? A value stock is a stock that usually pays dividends, trades cheaply on PE ratio basis, for example a utility company. Utility companies tend not to have a lot of growth opportunities, what they do is they collect your bill and then they pay dividends, so they pay their bills and they pay dividends because they don't have a lot of opportunity to invest that money. On the other hand you can look at a stock like Google, it doesn't pay dividends. The reason is that they can use their money in many, many ways to develop new technology and make the company grow. So use these 2 as an example, you can think of a company on a spectrum of very growth oriented versus very value oriented, then depending on where they are on this spectrum you can give them a score, it's actually a quantitatively determined score based on these criteria and a manager can hold these different stocks and as a result, the portfolio will have a score. If you plot the portfolio on this growth and value spectrum you get a portfolio growth value score and same thing you could do for large and small. Now if you look at your current portfolio which is the total portfolio of X, okay that's X as in X ray, that's the total GGRF domestic equity portfolio. The reason you made a comment on growth bias of this portfolio is this is a growth bias portfolio and we did something last year to try to correct it, we actually put an index fund in place of your then core manager which was very, very growthy, so we did some correction of this but still it's a growth oriented portfolio. Antolina Leon Guerrero: Did it move at all? Maggie Ralbovsky: It moved a little bit but we only replaced one manager and you still have, Winslow is a very growth oriented manager and you can see that Eaton Vance is not suppose to be, it's a core manager but it's plotting very, very growth. Gerard Cruz: But Winslow is a growth manager? Maggie Ralbovsky: It has a growth tilt but it's very, very growth right now and it's not being balanced by the end which is Numeric which is but it's not as value orientation but it's not as value as much as Eaton Vance is growth. The same way for the value managers, you have 2 value managers that are plotting value but they're not as value as Winslow is plotting growth which makes the entire portfolio more growthy which will suffer during the growth, during periods like the 3rd quarter, the 2nd quarter because growth faltered.

Rosalie Bordallo: All the managers are shifting to the growth side if you look at it. Gerard Cruz: Are they? Rosalie Bordallo: Yes. Gerard Cruz: I'm not questioning the comment, I'm just question the... based on their holdings? Maggie Ralbovsky: All these are based on their holdings. Rosalie Bordallo: Not what they say they do but based on what they're actually doing. Doris Brooks: What is this suppose to be, growth or value or just in the mid point? Maggie Ralbovsky: Well you want the total, every manager does a different thing, you don't want to micro manager you manager but you in terms of putting together your portfolio, our philosophy is that you want to be more neutral to them because things go into cycles, growth can't out perform, value can't out perform. In the long run the best thing to do if for you is to try to make it closer to the middle. Doris Brooks: But closer to the middle? Even if you're a growth manager? Maggie Ralbovsky: No, no, the total portfolio, the X. You can pick different managers. You could say right now the portfolio is having a growth bias. Doris Brooks: But it's not that great a growth bias right? Maggie Ralbovsky: It's not super, super growth but it is very growthy. That explains why during quarters equity does well, almost every manager out performs. Doris Brooks: But what you're saying is you need to get rid of Eaton Vance. Maggie Ralbovsky: No, that's not the conclusion I want to draw, I want to make an observation of the total portfolio, not a particular manager because like I said, we hire a manager for a particular reason and if we can balance out a manager's factor risk on a total portfolio level that's the goal right, so the current portfolio has a growth factor that's not being balanced by a value factor therefore the total portfolio is not being balanced.

Gerard Cruz: So in terms of the quarter June 30 and then looking at growth versus value, which out performed... Maggie Ralbovsky: It's a negative quarter, so usually in a negative quarter value out performed, in a positive quarter growth out performs and because most of these managers take a drift, they have an underlying growth factor that makes all the managers... Okay, look in this big book which you only have 2 copies... I have a value chart you see, value for this past quarter out performed the previous quarter growth out performed, if you recall the previous quarter, all your managers out performed and this quarter all of your managers under performed. For manager performance in terms of out performance or under performance, also correlates with each other because of this factor correlation, so the underlying factor is correlated.

Gerard Cruz: Are these companies static in these positions or do their positions change? Maggie Ralbovsky: That's a good question. You're value manager does shift a little, historically they were more value-y, now they're more core value, but Winslow is forever growth. Gerard Cruz: But we hired them to be a growth. Maggie Ralbovsky: Yes. So the problem is not that, the problem is the total portfolio, do want not think Eaton Vance was not hired to be a growth manager. Gerard Cruz: But I'm just wondering whether this was a tactical decision in the way of, on the part of the Robeco and MetWest and... Maggie Ralbovsky: I do believe that's the case, I do believe these managers are not forever here. Gerard Cruz: Okay, so when they do then revert to the mean then this will take our position as a growthier looking portfolio? Maggie Ralbovsky: That is true. Usually people have a larger allocation to the core category like an index to control that as an anchor, so the manager's drift does not make the entire portfolio drift this dramatically. We do have an allocation into the Russell 1000 but it's a smaller allocation that's why the entire portfolio is being more driven by the managers drift.

I don't think Eaton Vance is suppose to be this much growth, that's my belief. They're supposed to be a small core manager. Gerard Cruz: Eaton Vance? Maggie Ralbovsky: Yes. Well Numeric is... Maggie Ralbovsky: Numeric is growth. Gerard Cruz: But they're also a quant shop so... Maggie Ralbovsky: Quant shops usually have a value bias.

Gerard Cruz: So what's the take away? Maggie Ralbovsky: The take away is that we need to review the portfolio construction in terms of the factor bet. I do want to have that discussion after the laws are changed because right now we're bumping into the constraint. If you want to add the index fund it bumps into the commingled fund which is a constraint that really shouldn't be used for the commingled fund. Gerard Cruz: Where are we with that? Maggie Ralbovsky: We have an item on the agenda for that. Gerard Cruz: The Legislation. Maggie Ralbovsky: It's in the package. So that's the U.S. equity. For tomorrow's discussion for the small cap managers, for Numeric, we want to discuss whether people are happy... Gerard Cruz: If we were moved, I'm sorry, I don't mean to interrupt again... If the portfolio was theoretically consistent with where we should be which is a shift left... Maggie Ralbovsky: Which should be done. Gerard Cruz: No, what I was going to say was would the impact have been... Maggie Ralbovsky: You would not have all the managers correlate so strongly in terms of performance. Rosalie Bordallo: I think he wants to know if we have shifted more towards... Gerard Cruz: If we were shifted more towards the last quarter, we would have looked better? Maggie Ralbovsky: Yes. Gerard Cruz: But then 2 quarters ago we would have looked worse? Maggie Ralbovsky: Yes. That's true, that is true but in terms of the style volatility that's a structural risk, that's in the long run not being compensated. So, structural risk is the risk that's not being compensated, so it reduces the risk that's not being compensated, that's the goal.

For the 2 managers that we're going to interview tomorrow, for Numeric we want to asses whether people are still motivated, whether they're still happy, because the organization is our concern. Gerard Cruz: Is Nancy (Tooke) coming? Maggie Ralbovsky: I don't think so, I don't think she's coming. Paula Blas: Is she going to be on conference? Maggie Ralbovsky: Eaton Vance is the one we really want to.

Okay, for the international composite we also have under performed with all the managers on page 46. In this composite on the large cap side we have Fisher and Earnest, now these 2 managers do different things. Fisher is a top down manager, meaning they do macro. You recall when the Fisher guy was here he said at that time, we already had a 10% return and he said, they were expecting... Gerard Cruz: Another 20%. Maggie Ralbovsky: Right. Another 20 or total 20. Anyway they were very, very bullish so they were definitely positioning for the bullish run and their whole firm is, their philosophy is based on top down calls so they will have indicators, they will collectively say, we're bullish, it was positioned to be bullish or they were defensive, so they have that kind of component and I think they made a call of a very bullish call. Gerard Cruz: Nobody ever does that. Maggie Ralbovsky: They were really, really bullish when they were here. Do you remember that guy? He was forecasting another 20% run in the market and... This quarter was obviously not a favorable quarter but that kind of view, especially with the international markets phase, so I hope they're right, next month. Gerard Cruz: How are they doing now? Rosalie Bordallo: This quarter they were in the 90th percentile.

Maggie Ralbovsky: Also Fisher since inception they're above the benchmark and they were hired in 2006. Gerard Cruz: They're international developed market. Maggie Ralbovsky: They do have emerging market, they do have like 10 to 15%. Gerard Cruz: They're not suppose to. Maggie Ralbovsky: They do have some. They have I think 10 or 12%.

Earnest, actually these 2 managers are complimentary to each other because Fisher is a top down manager and Earnest is a bottom up manager meaning they really don't know where the market is going, they just try to find a good stock that's trading attractively. Their issue is that they're more concentrated, they hold like 45 securities, maybe 50, no more than 50 securities which means that the manager can be quite dramatically different from the benchmark. We do have this manager very highly ranked, Earnest is actually on our focus list. It's a manager that we think in the long run has the ability to do well, in the short run we do believe they are very much not tracking the benchmark closely because of their style.

Now DFA is also a manager that is on our focus list. This is a manager that is not really making security calls, they're actually doing things other than security selection to add value. It's an international small cap manager, they can add value, most of their value added is to add liquidity to the market, so they hold everything unless the same thing is proven not good to be held. Instead of proving something worthy to be held, they prove something unworthy to be held and they get rid of it. So unless proven guilty, you're innocent, they hold everything. Because they have this kind of approach, they have very, very small stocks. Antolina Leon Guerrero: Small stocks like? Maggie Ralbovsky: Small market cap stocks. There are other managers out there who are demanding those certain stocks and they just provide liquidity so they can trade very effectively and actually add value by trading. So that's the kind of approach that Dimensional has which is a very unique approach and since inception even though this quarter they under performed, if you look at page 51, since inception they actually have done quite well, they added more than 1.8%.

Capital is another manager that is not doing very well and it's a very tired company. They're just too big, they got really, really successful in the 1990's and they got so much money. Usually when people are in the emerging market space in 5 to $10 billion they close out to new money and this company doesn't, they just keep growing. So the bottom line is I think Capital International is a company that is going through generational changes, the oldest generation managers are trying to pass along their source to the next generation. They didn't commit any big sin but they're just getting very large so it's a manager that we watch very closely but not to the point where we want to fire them.

Let's take a quick look at fixed income. Fixed income we have one manager on watch which is Franklin. Gerard Cruz: What page? Maggie Ralbovsky: Page 53.

Why don't we look at page 57. We know that we currently have Franklin on watch because of since inception returns. The reason they are on watch is because their inception was 20 years ago so you know for 20 years usually you get enough of a chance to out perform the benchmark, well they have not. Historically there were some historical reasons, guideline issues so we put them on watch. If you think about our future, hopefully future restructuring of the portfolio, I definitely don't want to do anything right now, I do want to get Legislation passed so we can have the whole sale kind of discussion. Franklin is known for global bonds and global bonds credit kind of... This is sort of not in their... Antolina Leon Guerrero: This is not in their... Maggie Ralbovsky: This is not, they're like a core bond. Gerard Cruz: We acquired them from Fiduciary, they're actually Fiduciary Trust. Maggie Ralbovsky: Yes.

Okay, so let's take a look at REITS because we're going to look at the managers this afternoon. There are 2 things I want to talk about for, not 2 things, one thing I want to talk about for Cornerstone which was there were 2 departures for Cornerstone. I have a more lengthy writing on page 60, this is actually, we view this as a pretty material event, they had 2 analysts departing from a 6 performance team, 2 of them left, therefore we think that this is a relatively material event because they basically cut the team down to 4 people. At the same time they do have 2 performance managers still there, so this is one thing I want us to collectively establish a view for after we talk to them this afternoon. Our team had conference calls with them and we think this a material event and we want to watch them for their future performance. I did look at their July performance, they out performed in July so that's a good sign that hopefully this kind of trend continues but it is a material event I do want to update you on.

Joe T. San Agustin: When the 2 people left were they replaced by a similar number? Gerard Cruz: They haven't been replaced yet. Maggie Ralbovsky: They have 2 analysts left. Joe T. San Agustin: Are they performing at the same rate? Is their performance just as great? Maggie Ralbovsky: Well, their performance has been good since inception and their July performance was good. Joe T. San Agustin: So the departure had no material effect, it had no significant effect? Maggie Ralbovsky: It does have a significant effect. Joe T. San Agustin: How do you quantify that? Can you quantify the impact of their departure? Maggie Ralbovsky: It just happened, July 13 and these 2 people especially impacting the international part and since our portfolio is mainly U.S. it is less impacted than the total. Joe T. San Agustin: How much would that cost us? Maggie Ralbovsky: We have to evaluate that. Joe T. San Austin: They were let go? Maggie Ralbovsky: No, they were not let go, these people quit. Joe T. San Agustin: Maybe because they became a negative impact... Maggie Ralbovsky: No, these were actually considered good analysts who left on their own.
(End of Discussion on DB Plan Performance)

<u>1:00pm - 1:45pm Security Capital</u>

Kenneth Statz: In terms of the presentation, the presentation I think is designed to answer your questions. Why don't we start with the firm first in terms of regulatory changes, changes and all of that stuff, the nuts and bolts and then we'll talk about commercial real estate, where are we, what are the strategies that we're using, what's working, what's not working, but we're going to talk a lot about interest rates this morning because that's what's driving commercial real estate value currently. We're at ultra low interest rates, as we talk through our strategies, know in the back of our minds that we're trying to figure out how you do well in a low interest rate environment, you're doing fine, but how you do owning commercial real estate in an inevitable rise in interest rates, that's what we're going to talk about today.

First in the firm on page 5, we're commercial real estate even though we do it by owning stocks. Of course we have pictures of real estate. What's terrific on this page is we really hit a benchmark this year. The public market of commercial estate is close to now a trillion dollars worth of real estate in the United States, so we went from being very small 15 years ago to a very major market for commercial real estate, you own it through the public market. What we're trying to show on this is 48 properties, all very high quality. The public market owns the highest quality real estate in America right now and they own a lot of it. These are pictures of 48, there are 22,000 properties in the public market, so our job as managers is to understand what's happening to the value of a trillion dollars worth of real estate, that's why we have such a big team. The first part that we always try to emphasize is that we're real estate investors, if we go through the stock market we're trying to figure out, what are you paying for the real estate right now and does it make sense for the risks we've seen and the big picture is commercial real estate has been rebounding very sharply in value and we think the opportunity still remains on good quality real estate on reasonable prices, but boy those prices are starting to get really high. In terms of our firm, we manage about $5.2 billion dollars, that's approximately what it was last time we spoke. We have a whole new range of products which there is some shifting going on in our asset base which I'll go over in a minute, but in terms of the big nuts and bolts, we're growing, we're owned by JP Morgan, they continue to treat us like a little boutique very, very well so the support that we get from the firm is terrific.

Maggie Ralbovsky: I have a question here, JP Morgan also has another REIT platform. Kenneth Statz: Correct. Maggie Ralbovsky: How do they deal with these 2 parallel performances? Kenneth Statz: Well it's interesting because I mentioned at the start that we're real estate investors and you can buy REITS in the public market either as a stock investor and say, what's happening to momentum, what am I paying in terms of cash flow or you can look at it from a different perspective and say, I understand it's a stock but what am I paying as a real estate investor. So when our firm was merged, when they bought our firm back in 2003 we were part of Bank One, 51 days owned by Bank One and then all of a sudden JP Morgan bought Bank One and so I don't think they bought Bank One to buy us, but at that time there was a very good decision made which in the big asset management group at JP Morgan they had a stock oriented REIT platform in the equity group and we were put in the real estate group. So the question was, should we 2 platforms, one working real estate, one working stock, would there be confusion and I don't think there's any confusion so we're 2 very different kind of platforms in process. We operate totally autonomously in Chicago with the correct oversight from compliance from legal but nobody else in JP Morgan knows what we do, they don't know what we're buying, they don't know what we're selling and so I think there's a large part of JP Morgan client base that like the fact that there's this little group in Chicago that's just dedicated towards re-investing, so our platform has actually grown very nicely, I think it's grown more than double in size since we've been a part of JP Morgan. So we are very different groups, some people like the stock approach, some people like the real estate. Maggie Ralbovsky: You don't even talk to the other group, right? Kenneth Statz: No. We see each other at conferences and we smile and that's about it.

I'm going to flip forward just to talk about some changes and to talk about our platform for a second. On page 10, to click on some of the things, we've been in great shape compliance wise, there are no issues in terms of compliance and no regulatory events. That's been true for Security Capital since inception in 1995, we're a tightly run little group in Chicago. Maggie Ralbovsky: So the London, Wale's thing has nothing to do with it? Kenneth Statz: No, it's interesting, we've really enjoyed being a part of JP Morgan, they are a terrific group and you can see how they affect us on page 10 is legal compliance and risk management. They're a terrific group, they let us do smart business things but they watch us very carefully and so it's been a tough world for compliance and legal and risk. They want to do run a tight shop and that's been working for us and we appreciate that, however, we're just a little island in Chicago and this might be small in terms of JP Morgan but it's been the largest REIT team in the business. We've had one change since we last talked, you can see in general, Tony Manno on top, Kevin Bedell and myself, we've all been with the firm, 16, 17, 18 years, that's been consistent, we make all the decisions for you and that's been great. In the analyst group where we figure out cash flow, what's going to happen to the rent and occupancy pressures of commercial real estate, we have tremendous longevity but we have a brand new analyst that replaced the Vice President, Katherine Jacobsen just came on board and that's the only personnel change we've had in years, one of our analysts went to another firm. I think if you want to check off for Security Capital is the longevity of the people working together and it's still very true but occasionally we have an analyst that goes to another competing firm so we replace that analyst. Other than that it's the same firm, the same people.

What has been happening is, just to talk about this briefly, on page 8 this is our large product line looking at REITS. You're at growth and income, growth and income is our longest running product, it's our equity. All equity means is that when commercial real estate goes up 10%, if you own the equity, you own 20% because you're levered and that's very important and so just rememeber you own the levered commercial real estate. Our whole platform we buy both the equity and the debt for investors and that part that we own equity and debt isn't growing rapidly, it's a brand new product that's actually got over a billion dollars of new money in it. The reason that's happening is people are looking at, do they want to be levered to commercial real estate all the time or do they maybe sometimes levered, sometimes de-levered by both the equity and the debt. I just want to make you aware of that because it's something unique that we do that's become very, very popular, why you're going to have lower returns with lower risks by using that, so if you think by using that and we talk about values today, you're in our premier product line, it's all in our equity, but some people are looking at the equity real estate saying, it's great when it goes up, but if it goes down we want maybe to not be so levered. That is a new product that's been doing extremely well, it's a low risk product and I just wanted to make you aware of that as you think through what I'll have to say today.

We go up and down capital structure again here in our premier product of all equity but just so you know, there are other ways of skinning the cat in terms of commercial real estate. The reason we bring this up, if you look on page 7, I'm going to be talking about 2 things today, cash flow and interest rates because that's what drives commercial real estate values, how cash flow is going and what's happening in interest rates. Commercial real estate values are really sensitive to change in interest rates. Why? Because it cost a lot of money to build and own real estate and they use that a lot to fund it. In simple terms if interest rates are going down, real estate values are going up and if interest rates are going up, the reverse happens, all of that with in terms of what's happening with cash flow. We look at that whole capital structure in real estate, clearly the equity which is your top of the capital structure, when interest rates are going down and values are going up, you get a disproportionate positive and that's what's been happening and that's great, you're making a lot of money in real estate, you've made a lot of money since you've been in the real estate market, this has been terrific and you've done well. What we're worried about right now is what happens if interest rates start moving up because if commercial real estate values start stumbling in that environment the equity will probably have more of a reaction, it might just stall for a while, but it could also have some negative implications if interest rates move faster than people expect, we could come in for a period of time unlike 20% per year interest rates are returning, are achieving, but you could have some problems with values.

Joe T. San Agustin: You say the rate of return is high? What's the rate of return? Kenneth Statz: Well your rate of return is, let's look at that... Joe T. San Agustin: You say you own so much stock, how much stock do you actually own? This is a risk so how much percent of it is a risk? Kenneth Statz: Well, if you look on page 20 and 21 and 22, right now you own $86 million dollars worth of real estate, that's as of July 31st, $86 million dollars and if you turn to page 22, you can see that you started with a relatively smaller investment back when things were very, very bad in commercial real estate. Why? Because interest rates were still higher and cash flow was going down because of the bad economy. Then you gave us a very good amount of money at the exact right time and the value of the Fund continues to go up. You've hit some distributions again and I think the distributions have been timed relatively well also. You own right now, out of $86 million dollars and it has about a 3% cash yield on that right now, a 3% dividend yield, you can see that you've done about 23.6% a year since you've been investing in commercial real estate, that's why I say this has been terrific timing. During that period of time we've had some very strong... most of your returns have been through appreciation, you've had nice healthy income but most of the returns on commercial real estate that you've achieved have been through buying it when it was very inexpensively priced and now the values have gone up dramatically.

Joe T. San Agustin: So the original investment is how much, $21 million? Gerard Cruz: No, the original was 66.5. Kenneth Statz: Right. Joe T. San Agustin: And going up to 86, is that what you're saying? Kenneth Statz: Well what you've done is you gave us your cumulative investment as $71.1 million, you've earned $7 million dollars, we've distributed to you $32 million dollars. Joe T. San Agustin: We took $32 million dollars? Kenneth Statz: Correct. You took $32 million out and you have $86.1 million left. So on $71 million dollars you made $47 million, partially you've taken part of those gains out. Joe T. San Agustin: And that $32 million there's a distribution back to... Kenneth Statz: Right. Joe T. San Agustin: What's the re-investment rate? How much have we re-invested of our earnings? We have 32 out of 47? Kenneth Statz: Right. Joe T. San Agustin: And still at the same time making a 2 digit return. 26 return, 23.3? Kenneth Statz: 23.6% return per year. Joe T. San Agustin: After taking out the $32 million dollars? Kenneth Statz: That's on the money you had with us. So you have taken $32 million back and you still have $86 million even though you started with $71.1 million. Joe T. San Agustin: And that $86 million is earning 23.6? Kenneth Statz: That's what it's earning so far. Going forward we would estimate it would probably earn 8%. Joe T. San Agustin: How much, is there a number here where we cap how much money here we're suppose to maintain so that we can re-distribute back in cash, based on what we got? Gerard Cruz: Target allocation is about 85. Joe T. San Agustin: 85 is the allocation right? Gerard Cruz: About 85.4 based on our portfolio balance. Joe T. San Agustin: Our target allocation is 86 or 85? Gerard Cruz: 85.4. We have a range, but that's mid range but we can go as high as... we can go higher. Joe T. San Agustin: But when are you going to give a hair cut? When you go up so fast... we want that cut back to... Gerard Cruz: Sure, I understand what you're saying. Paula Blas: Right now they're... Joe T. San Agustin: To our cash needs. Gerard Cruz: I don't know that securities is right for that. There are others who exceed their target allocation by a larger amount. Joe T. San Agustin: Yes, but you know what I'm getting at. You got $60 million dollars to begin with, you have gone up to that point of cumulative investment to $71 million, then you tap $47, you tap $32 million, you re-invest the difference and now you again you still went up to $86 million and your target allocation is $80 million? Gerard Cruz: $85.4 million. Joe T. San Agustin: So you're right on your target. Gerard Cruz: You're right on the cusp. Joe T. San Agustin: Basically we're right on the target. Gerard Cruz: Right.

Diana Bernardo: Mr. Chair, I just want to add in June we did take about $10 million 9 or $10 million from them and gave it to Capital or one of the other managers and I believe in 2011 we may have taken another $10 million on a re-allocation. Joe T. San Agustin: What was the earning and in the original investment how much was taken out and what the value of the investment and still earning, hopefully we're still earning 23.6%. Diana Bernardo: We started giving them money in 2009, we started with like $16 million. Gerard Cruz: 16? Diana Bernardo: Yes, we just got our, we started initially with $16 million. Joe T. San Agustin: I just want to know historical trend, as we go up at what point in time do we give them a hair cut? Diana Bernardo: Well we kind of gave them a hair cut, 2 already, we gave them, 2. we took $10 million in June and about another 10 last year. Joe T. San Agustin: So a total of about how much money? Diana Bernardo: About $20 million I'm thinking. I have to double check, it could be more than 20. I think we either took 9 or 10 this year in June, I don't recall. Joe T. San Agustin: If you made $100 million dollars and you're only taking 20, that's only 20% that's what I'm saying. Diana Bernardo: And that doesn't include the interest and dividends that we took down. Gerard Cruz: The 20 he's talking about? Diana Bernardo: No. Joe T. San Agustin: That sometimes depends on how much cash we need. Gerard Cruz: But in terms of rebalancing for the purpose of bringing them back in target, we took, since inception, we've taken down $32 million dollars. Joe T. San Agustin: Okay. Gerard Cruz: Their current market value is $86 million. Joe T. San Agustin: That is your target allocation. Gerard Cruz: That is correct. That's our target, so they're on target currently. Joe T. San Agustin: Anytime they exceed that target at a point then that's when you want that money back. Gerard Cruz: That's correct. Joe T. San Agustin: And she (Diana Bernardo) said it's only been twice since it's been taken out? Kenneth Statz: There I think has been 3 different allocations. On page 22 where you see those red... Gerard Cruz: Oh that's where we took money back? Kenneth Statz: Correct. Those were capital redemptions and that's why I thought it was important to show the relationship because number one, you started during a very volatile, very uncertain period of time for commercial real estate because of the economy. Your timing in the 4th quarter of 2009, the green is when you gave us more money and significantly increased the size of your allocation, that was superb. Joe T. San Agustin: That pays off. Kenneth Statz: That paid off a lot and commercial real estate is typical, you bought here and... Joe T. San Agustin: You usually cap it in when it goes up and then when you wait it... Kenneth Statz: I'm a farmer and there's called reaping and sowing. Joe T. San Agustin: Exactly. Kenneth Statz: You sow correctly and then you reap really, really good too. Joe T. San Agustin: I want to wait until the right time when I can harvest. Kenneth Statz: Yes. We would recommend, even though we're at current, we're going to talk to you about some strategies that we're doing we think that the very ultra low interest rate environment is supporting commercial real estate value maybe a little above what we think is the right value for commercial real estate and the reason for that is the cash flow yield, what you're getting to own it is very low today and so because of that, we're cash flow investors, we like cash flow and we like it to grow. Right now you're paying a lot for the real estate investments because things are improving slowly, because the economy is slowly improving. There's not a lot of building going on, that's terrific, but we think the primary driver of where we are paying today is that there is so few alternatives because interest rates are so low that they're probably paying in our opinion, very high prices. So we're worried, if interest rates stay low, that's okay, we think you still own commercial real estate and it's producing a very nice return. We're worried that if interest rates start moving up, people will say, gosh, I'm paying a lot for this and I have better alternatives. Joe T. San Agustin: That's what I'm saying, that's the time when you start giving them a hair cut because you have alternative investments. Gerard Cruz: Well how do you position the portfolio to address that? Kenneth Statz: Right. That's a great question. Joe T. San Agustin: That's what I'm leading up to. You're right Gerry (Cruz).

Kenneth Statz: These are all essential questions, these are great questions. Well, let's look on page 23. No we're going to talk about performance here because commercial real estate have been good, REITS have been better because you own the leverage stock of it and we've been average, in fact average pickers of stock in this last 20-24 months. Once you take our fee out you're taking a little underneath and so let's talk about, are we doing something wrong or are we looking at things in a way that we think there are some risks that are starting to position you for.

Page 23 is property type, percentages of your 70 or $86 million dollars, where is it invested right now. You can see that when we're looking at your portfolio which is the blue line, the most important thing in our research is trying to figure out by property type, do we want to be more in apartments, malls, shopping centers, hotels, where do we want to be because from research we think cash flows are going to be stronger than the market expects, that's our number one job for you. We pay have you positioned you in 2 property types, over weights in storage and multi-family because the blue is higher than the grey and the reason we do that is in this environment, occupancy rates are 96% in multi-family, 93% in storage very tight. Joe T. San Agustin: Right. Kenneth Statz: Rents are going up very sharply, the market notes that. What we think is that is that if interest rates rise, the property types that still grow and grow very rapidly will have a better chance of retaining value or maintaining value than other property types where things are still very flat, they're really not improving because they're bond like and so we like multi-family and storage because the occupancies are high and Security Capital, my firm, thinks that cash flow will remain faster in growth under a wide variety of environments than the market currently expects. People think that multi-family which is very strong, that people are going to leave apartments and buy homes now. We think some will but there is no occupancy, occupancies are so high that the 25-30 year old people that rent in the United States, they still tend to think to rent versus buy for a very simple reason. It's not that home values are going up, you can't get a mortgage. Joe T. San Agustin: Interest rates are too high? Kenneth Statz: No, you have to have more money saved. They went back to the beginning. They said, you know what, you have to have a down payment. Joe T. San Agustin: They raised the 75 down payment. Kenneth Statz: How much you can finance. Joe T. San Agustin: In other words how much you can get a house for 60% down, it's now a minimum of 80 to 75. Kenneth Statz: Well, they use to do it... Gerard Cruz: You can do a 97%. Paula Blas: You mean finance? Kenneth Statz: And there was a period of time where you didn't need verification or any money down, so it's pretty simple for the United States. We've been really good at multi-family cash flow and we just think that we want to own that for number one reason is it's good, we think it means good under a wide variety of things.

Storage in the United States is the same thing. The storage market thing where people have too much stuff, has been terrific, there has been no building going on in storage and occupancies are so high and rents have been sky rocketing, so we've been liking that business a lot. Joe T. San Agustin: Storage? Gerard Cruz: Public Storage. Kenneth Statz: Too much stuff and here's the rule, Americans are going to have less stuff before that's a terrific business, we think that's a fair bet. People just continue to have their stuff and it's simple, our business is not hard, there is no building.

Now I'm going to talk about another part about why we like multi-family and storage, their financing, we want to own commercial real estate that has very long debit attach to it because if interest rates go up, their values will be maintained. Public storage which you own a lot of, doesn't have any debt. What they have are perpetual preferreds that they finance but they never have to pay them back, so they're paying 5.5% for interest against their debt right now, they've never had such low interest rates. If interest rates go up, those perpetual preferreds financings go down in value and the value is transferred over to your equity. Joe T. San Agustin: It's paid off. Kenneth Statz: It's wonderful. This is a machine that works well today, it's a wonderful machine in rising interest rates. So why do we own so much public storage? We like it and with this interest rate environment, we like it more in a rising interest rate environment and by a rising interest rate environment this is the key question we have, because we don't know where interest rates are going to go, we don't know. What we know is the current 1.8% treasury market which has never been achieved before, 1.5, 1.6, 1.7, it's amazing, that's a haven status of treasuries, that's because people are so afraid of everything else, that's not a good reason to take risk. Interest rates are low because people are afraid of the environment, so we want to be very conservative and say, let's stick where things are really working well and their balance sheets are very conservative. Now this works if 2 things happen. One thing is if they actually grow like we say they would and 2, interest rates go up. So why is our performance just mediocre? It's because neither of those things have happened yet.
(End of presentation on Security Capital)

2:00pm-2:45pm Cornerstone

Scott Westphal, CPA, CFA, Managing Director & U.S. Portfolio Manager - Cornerstone: Thank you for having me here. I've got a book which you were all provided a copy of. I got a lot to cover here. If there are some area that you want me to dive more deeply into, please speak up and let me know and I will be happy to do so, but absent that I am just going to go through the book. Maggie Ralbovsky: We do want to hear about the update on the organization. Scott Westphal: We are going to cover that right away and we're gonna hit that front and center. If you turn to Page 5 you'll see, this is just sort of an update on Cornerstone, as part of the Mass Mutual Organization. We now are about $36.2 Billion. As we told you previously we merged in the real estate finance into Cornerstone. That increases the size of it pretty dramatically. We now service four quadroons of the real estate world. We do public and private debt. We do private and public equity. Obviously, this is a public equity investment that we manage for you. If you go to the next page you will see where our offices are. This has not really changed at all. Just a review of where our offices are - the headquarters of the company is in Hartford, Connecticut. The Securities Group is in Stamford, Connecticut. We are about an hour and fifteen minutes from Hartford and about forty-five minutes from New York City. The location close to New York City is important for us as far as Securities Group is concerned. This is the organizational chart that Maggie made reference to. I got a couple of things to update you with and I will be happy to take any questions on this because I realize that we haven't had any organizational changes in a long time. In fact, we have not lost any people in the Securities Group in over eight years which is a little unusual for most organizations. Normally there is some sort of turnover based on people looking for new career opportunities and that type of thing. We haven't had any changes but we got a couple of things to talk to you about now and I will be happy to take your questions. First and foremost Dave Wharmby who was supposed to accompany me on this trip was promoted to Managing Director of the Securities Group. He will be running the global part of the portfolio. I will continue to run the U.S. portfolio. And in addition to that, we had two analysts that we lost. One of them left because of a combination of family reasons and a career opportunity. Bill Pekowitz who was with us for about six and a half years, he lives in the New York area, his wife's mother is quite ill. She has a generative disorder that is causing a lot of extra care for her to be taken cared off. His wife Karen has three sisters who live in the Boston area. The decision was made to move to Boston so that she could share the burden of caring for their mother and obviously I think it is a very smart decision on their part. He was able to find an opportunity there that helped him out a lot and it is also a good opportunity for him to advance his career. So, we wish him all the best and we understand totally why he made the move, but nevertheless we lost him. Secondly, Nem Marjanovic left. He has no other opportunity right now, but he is currently working. That is really all I can say about that and that he is no longer with the organization. But, the good news is that we have been actively recruiting for a replacement analyst for about the last two and a half months. We are trying to pursue the best candidates that we can. The good news is that there is a rich field of candidates out there. We are very far along in the interview process. We should a person to replace this one position here very shortly. As soon as that person is hired, we will let you know. Are there any questions on organizational issues? Gerard Cruz: Is this your analyst bench now – six? Scott Westphal: Yes. Maggie Ralbovsky: For North America, there are two analysts right now. Scott Westphal: Right. Gerard Cruz: It has been only a couple of months since that has happened. Scott Westphal: It basically happened in July. We have been proactively recruiting people for a couple of months. We actually started interviewing some people back in May. As you know, it is a little difficult to get things done during the summer season, but we expect to have a decision made very shortly. We expect to have an offer to somebody within thirty days. We will notify you as soon as that offer is accepted and we will go from there. Gerard Cruz: Is there an impact to the managing of the portfolio or the Fund under management as a result of this? Scott Westphal: No, not really. Just to give you an indication of how deep we are, I actually covered the retail sector as an analyst more than twenty years ago and I covered it more recently than that. I actually know the retail companies probably better that anyone in the company. I jumped in there to cover those companies in the interim. The other areas – apartments and health care are being shared by the two analysts that exist here. Short term, we got it covered. In the next thirty days, we will have an analyst hired. The help is back fully. It will be a person with extremely high quality. I am very confident that we will have that person in place shortly.

Scott Westphal: If you go to Page 9, I want to give you an update of what is happening with the North America U.S. economic situation and how that impacts real estate. You will see here if you look at the Real GDP line. The interesting fact here is that we actually returned to GDP level of pre-economic crisis or pre-economic downturn. The problem we have is that we done it with less people. We are in an environment where companies more and more are doing more with less. The good news is that it creates efficiency for companies, it helps them create profits. But, the bad news is that we have 25 Million people in the United States who are either unemployed or underemployed. When you stop to think that we have a labor force with about 130 Million people, 25 Million people being underemployed is significant. My heart goes out to these people. We've got to figure out a way to get these people back to work. We need to get people in jobs that they are qualified for. It is not good enough for somebody that has a master's degree in biochemistry to be working as a waitress. It counts as a job, but it's not really what America is all about. We need to fix that and hopefully some things will happen soon to help us resolve this situation. I don't want to under estimate the problem that we have here in the United States, it's significant. In terms of the near term issues, the positives, the energy prices have fallen. Unfortunately, they've started to go back up again. Asia is both a risk and an opportunity. We'll talk a little bit more about China as we go on, but China is definitely an economy that affects so many other economies. It is also affected by both Europe and the United States in a major way. We are expecting GDP growth this year to run about 2.1%. We have a range there of 1.5% to 2.1%. My own personal forecast is a little lower than 2.1%, but our consensus of the company is 2.1% right now. We are expecting job growth to be about 1.4% which represents about 150,000 jobs per month. One of the real issues that we have to wrestle with in the United States is this fiscal cliff issue. If you are not familiar with it, basically the issue is we cut payroll taxes and we cut income taxes for the last couple of years. That has spurred additional economic growth. If we do not do something to deal with the fiscal cliff legislatively, we will have an increase in payroll taxes and an increase in income taxes. That could take an economic growth down from about 2% to about .5%. .5% growth, even though it is economic growth is so slow that a lot of economists will call that a stall speed growth. It is slow enough where economy could flame out and we could go into a recession. It is critical that we resolve the fiscal cliff issue.

Scott Westphal: If you go to Page 10, you'll see that we have had recently a better jobs growth number in July – that's the latest bar up there. One of the issues is that the three months prior to that are pretty anemic job growth numbers. One of the other issues that we have to concern ourselves with is that July is the most seasonal adjusted number in the entire year because there are a lot of auto plans and that type of thing where they are shutting down for inventories and that type of thing. So, there's a lot of seasonal adjustments that go on. You really can't put a lot of faith in that July number. You really need to see what happens over the next couple of months.

Scott Westphal: If you go to Page 11, you'll see that retail sales are holding up reasonably well, particularly luxury retail sales. Consumer confidence is down. That's generally not a pattern. If you look at the previous data here, you'll see a pretty high correlation between the two. We got a bid of a diversion going on right now. It's critical that we get a pick up on consumer confidence so that we can maintain a good level of retail sales going forward to keep our economy going. We're a service space consumption based economy and we need to keep that consumption going and the only way we can do that is create jobs and increase consumer confidence and get people out spending. Gerard Cruz: How is that working out - it's tough. Scott Westphal: We are in a tough place. I don't' want to minimize the place –

we are in the United States right now. We'll talk about Europe and Asia later on. Europe is a tougher place than the United States is. Unfortunately, Europe is a larger economy than the U.S. It's critical that Europe get its economic act back together in order to promote exports to Europe, but we'll talk about that a little more later.

Scott Westphal: On Page 12 you'll see what the job growth is in the United States. There are really two things going on here. One is that there's tech related markets like Dallas, Fort Worth, Phoenix, San Francisco, Seattle, and Raleigh. Then there's low cost markets where companies like to move to because it's lower cost for them to operate – that's Dallas, Fort Worth, Phoenix, Denver, Atlanta, and Raleigh. The higher cost markets in general had lower job growth and you'll see that as you look at the lower bars here, there are some higher cost job markets here, and those markets are suffering at some extent.

Scott Westphal: If you go to Page 13 – we'll talk about the property markets a little bit. One of the things that occurred is that we had a recovery in property prices very significant from the down turning that we had in 2009. The date of it is illustrated here is that the Moody's/RCA Commercial Property Price Index basically represents all different types of properties both lower quality and higher quality. The MIT Transaction-Based Index is really an institutional quality index. And as you can see, it's a little hard to see from the graph, but you can see that the recovery in that index has been a little sharper than some of the lower quality properties. Right now what's happening is the secondary quality properties are starting to catch up with that. We have a chart on the next page that really illustrates that to some extent.

Scott Westphal: If you look at the Page 14, you will see that the red line on the top graph is what we call the Gateway Markets. Basically the major CBD markets in the United States, you'll see that recovery property prices have recovered really significantly there. You'll see the Moody's number which includes both the Gateway Markets and the Non-Gateway Markets. You'll see the Non-Gateway Markets that are starting to recover, but they still have a ways to go. If you look at it on a property level basis in the chart in the lower part of the page, you'll see that the Apartment Markets, which is the red line here, have recovered very nicely, as have the CBD Office Markets. The CDB Office Markets, just to remind you, are the downtown office markets, like New York, Boston, and San Francisco. So you are seeing a pretty nice recovery in those markets. The Suburban Office Markets or the Non-Gateway Markets have still got a long way to go in terms of recovery. We typically refer to these as low bearer Suburban Office Markets.

Scott Westphal: If you turn to Page 15, you'll see from a strategic point of view what we like in terms of North America. We've also listed here for just your reference our views on Europe and Asia. In North America, we continue to like the Class A Malls. I know that might sound somewhat contrary given the economic environment I just laid out for you. But, the truth of the matter is the top 20% of income cords in the United States to the vast majority of retail spending -they continue to be in reasonably good shape. That is why we like the A Quality Malls in this kind of environment. The CBD office buildings as we talked about earlier are doing well. Self Storage is doing well because any time you have a situation where a lot of people are in fluxed in terms of jobs, houses or that type of thing, they need storage facilities. The demand for storage is very strong. The supply for storage is very limited. Healthcare properties, particularly private pay healthcare properties are doing well. Part of that is very limited supply and part of that is the demographic thing as the baby boomers start to age and need additional forms of healthcare living situations. In terms of Europe, Europe continues to be a major problem. One of the reasons I've mentioned in here is it could be a drag on the U.S. economy and it could also be a drag on the Asian economy. Europe has massive debt issues they need to take care off. A lot of what you hear about Europe in terms of their data auctions is really some what artificially created because a lot of the debt these counties are issuing is being bought by the regional banks and the government is essentially telling the regional banks to buy the debt. Even though in their heart, they probably don't want to buy it. You've got a situation that I think is fairly dangerous and is something that we are watching very carefully. Another problem with Europe is their huge structural problems in the labor markets. There are a number of labor markets in Europe where if you want to lay somebody off, you have to pay them for two years with benefits. In that kind of environment, with a lot of uncertainty in the economy, companies are very reluctant to hire people. Anytime you have that situation, people are either not going to be hired as full time people at all, or maybe they'll be hired as temporary type workers. Not a very desirable situation for the stability of the region, the stability of the economy. And the other problem that Europe has is that they have very high social cost in terms of their entitlement programs. These programs are not sustainable. They need to basically reel in those programs and become more realistic about the sustaining ability of the programs that they provide. In terms of Asia, the major issue is China. China right now is trying to engineer what we call a soft landing. In terms of China's economic growth, a soft landing for them would be 5-6% kind of economic growth. They are used to having growth in the 9-10% range. If they can engineer a soft landing and it generates that kind of economic growth, I think it will be a boom for the overall global economy. If their economic growth were to go below that it could be very detrimental to the United States, to Europe, and also to Australia. Australia is essentially a resource economy that relies very heavily on demand from China.

Scott Westphal: If you go to Page 16, you'll see a brief overview of the North America economic environment. We think, as I said earlier, this could be a moderate to slow GDP growth in the U.S. Major issue for the U.S. is both Asia and Europe. We see that there is probably going to be limited growth in Europe for the foreseeable future. Asia is the big question mark with particularly China. In terms of the federal reserves support for the U.S. economy, we believe that they will actually keep rates low until 2015. It hasn't been officially announced yet, but we think that ultimately that's what will be broadcasted. There's a major speech by Chairman Bernankey, Chairman of the Federal Reserve, that's going to be made in Jackson Hole, Wyoming, on Friday of this week. The world will be watching to see what he broadcast in terms of what his intentions are for monetary policy in the United States. One of the things that we think is very favorable about the real estate environment thought is that there is very limited growth in supply and virtually in all property types and we expect that limited growth to continue.

Scott Westphal: If you go to Pages 17 and 18, you'll see the Americas Strategy and the Real Estate Strategy. I am only going to spend a moment here on Americas Strategy and then go to the Real Estate Strategy because we already talked about a lot of these things. We continue to be very concerned about Europe. The consumer in Europe is extremely scared of what's happening. You have major countries like Spain and Italy where every week there are major withdrawals that come out of the Spanish banks by individuals because they are so afraid that their banking system will collapse. In that kind of environment, you can imagine that people are not going to be spending money if they are afraid that their banking system is in danger of collapsing. The other problem they have is that it is a very unstable environment in terms of the northern countries versus the southern countries. Germany and the northern European countries are basically trying to convince the southern European countries to stay with these austerity programs that have been enacted. The southern European countries are asking for flexibility. It's basically a game of who points first and unfortunately Germany basically has all the cards in their hands. It's a difficult situation, it's something we're watching very closely. As far as the U.S. is concerned, one of the major issues in the U.S. that I need to mention is that we do have an election this year. Most of the economist that we have spoken to really believe this election is a very critical step in the overall process for the United States reform its spending levels. We believe that we have to do something to reign in spending. Right now, for every dollar the federal government spends in the United States, we borrow forty-three cents. We can't go on at that level. You can imagine running a company or running a household with that kind of spending levels. You won't last very long. We got to do something to resolve it and it's critical that we act quickly.

Scott Westphal: If you go to Page 19, this is a quick view of the Europe economic environment. I'll just say a couple of things: 1) the austerity efforts that I've mentioned earlier need to be followed through on and there's a huge tog of war between the north and the south. I think we need to watch very carefully as to who wins that war. I think that will determine largely the future success of Europe.

Scott Westphal: On Page 20, as far as Asia is concerned, as I said earlier we need to engineer a soft landing. Asia is doing many things in their monetary policy to try to reignite their economy. One of the things they are fearful about particularly in China is that they don't want to ignite inflation in China because one of the things that China fears more than anything is having an uncompetitive labor force. If their labor force becomes uncompetitive and manufacturing jobs start moving from China to other parts of Asia, the China miracle could end very quickly and that's one of the things that they are trying to balance – trying to balance monetary stimulus with keeping inflation in check. It's a very difficult balancing act. Hopefully they will be successful. Joe T. San Agustin: Excuse me, you mentioned something about the employment in China moving away. Scott Westphal: They are moving away. Joe T. San Agustin: They are moving to Vietnam and other areas are picking up a lot. Scott Westphal: They are, in fact, to give you an example, there's a clothing chain in the United States called Joseph A. Bank. They may have stores here on Guam, I'm not really sure. They do a lot of their manufacturing in China. The CEO of Joseph A. Bank was on the CNBC, our main business news channel and he basically said, look I can't afford the manufacture there anymore. I'm moving out of China. They are moving to other lower cost markets like Indonesia. They are losing that part of the manufacturing process. It is also happening with other companies that manufacture higher value added items. This is not too dissimilar from what happened to Japan. When Japan first started, it started manufacturing in America, they had a lot of lower cost manufacturing going on and as time when on that manufacturing moved out of the country to other parts of Asia. Now the same thing is happening to China. They are very worried about it. That's one of the reasons why they are so concerned about increasing inflation because that will ultimately make their labor markets less competitive. Joe T. San Agustin: What about the President's policy about trying to entice manufacturing jobs back to the states by giving them some kind of an incentive whereas the Bush administration were paying them off and given the incentive to go of and manufacture in other countries. Now what Obama is doing is trying to reverse it. There is some small loop. Scott Westphal: There is. Joe T. San Agustin: Is there a movement to go back in. Scott Westphal: There is, but it's small. To give you an example, General Electric is obviously one of the largest companies in the world, they moved some manufacturing back to the United States. Part of the reason they did that though was there were quality problems in some of the countries that they moved their manufacturing to and part of the reason they did that was because they had unreliable delivery. Sometimes these manufacturing is components of larger pieces of equipment. If they can't have reliable manufacturing in terms of the quality and also reliable in terms of the delivery, it creates huge problems for the U.S. companies. Some of that is being reversed. It's a very small phenomenon right now. Hopefully it will pick up momentum. Joe T. San Agustin: Do you see that as a trend that will increase that. Scott Westphal: I think it's a small trend, but if you think of it as a sound, it's sort of a dull hum, we need to get it to a roar. When it gets to a roar, I think that will be good news. Joe T. San Agustin: It's not leaving a dent though on the employment in the states. Scott Westphal: It's making a dent, but it's really small. The reason it's small is because the cost of labor in some of the Asian markets is so low relative to the United States. Joe T. San Agustin: The costs of labor in foreign countries have dropped down because of the cost of transportation – the gas and all that stuff. That's one of the reason for the move plus the fact that the administration is offering some kind of an incentive to relocate to the states. Scott Westphal: There is some of that going on and the thing that I don't want to represent is that it's a ground swell. Joe T. San Agustin: Is there a ground swell? Scott Westphal: It's happening and one of the things that you have to realize is that the media tries to pick up on it and the media tries to present it in the best that they can. I think it's terrific, but is it the ground swell of support that we need for the 25 Million people that are unemployed or under employed in the United States. It's not going to solve those problems overnight. That's just my honest opinion based on the -merit of economists that I spend time talking to. Joe T. San Agustin: A lot of time it's just talk, talk, talk. Scott Westphal: We are in an election year and we have talk, talk, talk, and steroids.

Scott Westphal: If you turn to Page 22, we can talk about the portfolio that we currently manage for you. These are the top ten holdings we have. The holdings that are here are consistent with the discussion I had previously. Simon Property Group is the largest mall company in the world. It is a Class A mall company. We are very positive on its prospects. Ventas is by far the best healthcare company in the space. One of the things that we would like to focus on healthcare is there are two types of healthcare housing for the elderly. There's private pay and there's public pay. Public pay is Medicaid, Medicare. Private pay is like assisted living. The focus that we have right now is on the companies that concentrate on the private pay. The reason we're doing that is because we're concerned about the elections and the impact on public pay healthcare going forward. There maybe some downward pressure on reimbursements the federal government is willing to give and also state government because these programs are matching programs. It is something we need to watch very carefully. Public Storage is the largest storage company. Joe T. San Agustin: Going back - the assisted living quarters – is that picking up? There's a lot of stuff in San Francisco where assisted living quarters is still being supported by the state government like Medicare and what have you. Scott Westphal: What we call assisted living is purely a private pay housing for the elderly. Joe T. San Agustin: But they do get some subsidy from the state to a certain extent. Scott Westphal: Not usually. Normally assisted living is pure private pay. What you're talking about is what we call skilled nursing facilities. Joe T. San Agustin: No, not that one. Scott Westphal: Those are paid by Medicaid and Medicare to some extent. One of the problems with skilled nursing facilities right now is that most states have to grant you a permit to build those facilities and the states are not granting any permits. The reason they're not granting any permits is because they don't have the money in their budget to pay for the people to occupy those facilities. So rather than build new facilities and allow those facilities to fill up and then have to pay for those residents, they're just saying we're done, we are not building anymore skilled nursing facilities. It's a bid of an exaggeration, but there's definitely a pressure from the budget that is causing that to occur. Joe T. San Agustin: The assisted living quarters that I'm getting at - is there any movement, are they trying to get that going? You know our population – they're aging. More people now are working. Paula Blas: Are those privately built or owned? I know you're saying that the individuals that live there they pay for it themselves, it's not through public assistance. Scott Westphal: Right. Paula Blas: So are the facilities itself financed through credit. Scott Westphal: They're owned by companies like Ventas. The thing about it is one of the things you have to realize is that the assisted living part of the elderly housing programs that are out there it's a very small part of the overall equation. It's only for those people that could afford to do private pay. Generally speaking, these are higher quality facilities that require a higher income to enter into. Joe T. San Agustin: Are they covered by a long term care insurance. Scott Westphal: They are if people carry it. Unfortunately, the vast majority of Americans don't carry long term insurance. Antolina Leon Guerrero: Particularly those that are in that age group now. Scott Westphal: Right. Joe T. San Agustin: The state of California government do have a provision that make employees pay in for long term care insurance as part of the policy. You can buy at an early age a long term care insurance. Scott Westphal: I am now aware - the company that I work for does not provide that. Joe T. San Agustin: On Guam, they don't sell long term care insurance at all. We talked about that with Maggie Ralbovsky – about Guam Memorial Hospital at one time. Scott Westphal: You can buy it, but it's your own initiative to go out and buy it. Joe T. San Agustin: Some family care – PMC and other areas are looking into it. We have a vast population of elderly on Guam that are getting to be homeless. People are no longer taking care of them – the family. Our culture has changed – mom and pop are no longer being taken cared off - mom and pop stays in the back and nobody takes care of them because everybody works. Scott Westphal: It's hard. We lost an analyst, Bill Pekowitz, - part of the reason he left was because they don't want to put her in an elderly care facility and both Bill and his wife work so it's very difficult when both the husband and wife are working and they are trying to take care of somebody like that and that is why he moved to Boston. His wife Karen has three sisters and they're going to share that burden. It's a huge problem, not just for the United States, but for the world. Joe T. San Agustin: It's starting to be a problem in Guam. Scott Westphal: It's a big problem. Japan has got one of the oldest populations in the world. They also have one of the highest death levels in the world. So, they are not necessarily well positioned to provide that housing. Japan's debt to GDP right now is about 225% which is two or three times what the modern industrialized world is and that's a big issue. Joe T. San Agustin: We have a large number of elderly in our retirement payroll and I suggested that these people can go in the system with their annuity be used to pay towards third party doing that. We've done that way back. We sent some patients in the states and we sent insurance, but we have people here also. Paula Blas: That's by choice - that's their decision. Joe T. San Agustin: Right now they have no choice because they no place to go. These homes do not take care of them – their families can not take care of them. They are out there now living in dirty quarters and abandoned. Scott Westphal: It's a huge problem. One of the things that exaccerbates it is that you have so many married couples who have two incomes to provide for their standard of living and there isn't someone to stay at home to deal with caring for the elderly. This is sort of a generation all changed in what's going on in the world. It's a tough problem. The good news for the healthcare companies, in our investment world is that they have a lot of demand for their product. The bad news is that the most affordable part of that product, the skilled nursing homes, can only be built with permits that are granted from the state, which they're not granting. Joe T. San Agustin: Based on financial needs. Gerard Cruz: Why aren't they? Scott Westphal: Because Medicaid is a shared cost program. It is shared between the state and the federal government. The state budgets are under as much pressure as the federal government so their attitude is, you know what we love to provide housing for the elderly, but we can't afford it. Paula Blas: So why build it. Joe T. San Agustin: That's why there are survivor benefits. Scott Westphal: It's a big problem. Joe T. San Agustin: I am going to personally look into it. They have a lot of these in San Francisco. Scott Westphal: They do. Joe T. San Agustin: I'll connect with the Bank of Guam and we do have a branch in San Francisco and we do finance a lot of assisted living quarters. Gerard Cruz: There's a ton in San Francisco. Joe T. San Agustin: They're quite popular by the way. Rosalia Bordallo: The city has a lot. Scott Westphal: I am a bit over my time limit here. Joe T. San Agustin: I'm sorry I took your time. Scott Westphal: It's okay, it's an important issue, and I want to answer all your questions. I just want to make sure that we're okay time wise. Joe T. San Agustin: Okay, you got ten minutes. Scott Westphal: I just want to be respectful of your time. I appreciate the extra time I've been granted. Thank you for that.

Scott Westphal: We're on Page 23 - this shows basically a breakdown by property sector. We show it on a pie chart here. I also show a under weight and over weight compared to the Dow Jones Resi Index. This is consistent with what I talked about earlier. Maggie Ralbovsky: What's a not indexed? Scott Westphal: Not indexed - if you look down here there's an asterisk that addresses that. The asterisk should be up there. Those are essentially commercial finance companies that we made a small investment for in the firm that are in the portfolio. One of the things that we like about the commercial finance companies is that there is a dearth of financing for certain types of real estate out there. These companies are being able to take advantage of very low cost money and loaning out at some pretty attractive rates. One of the things that we really like about them is that they have a very healthy dividend yield and I know dividends are important to investors particularly the Government of Guam. These companies have dividend yields of twelve to fourteen percent. There is some risk associated with that. We are monitoring the risk very carefully. It is a very small a portfolio, but we think it is something they could add something to your returns and also to the cash flow that I know you need to pay your beneficiaries. It's a small, sort of odd index.

Scott Westphal: If you go to Page 24 – We've been asked to talk about performance. I can literally spend an hour on this page if you want me to. I know you don't want me so I'm going to touch some of the highlights. Joe T. San Agustin: You have five more minutes. Scott Westphal: We had some challenges in the portfolio. One of the things that has not worked particularly well for us is some of the retail allocation that we made earlier. We have made some steps to change that retail coverage and we expect those results to improve. In fact, they've already improved. One of the things that happened to us going from the first quarter to the second quarter if you'll notice we under performed in the second quarter by about sixty basis points is that we were in an environment in the first quarter of this year that we described as a risk-on environment. Basically, everybody thought the economy was going to grow rapidly. Everybody thought Europe's problems were going to be solved. Everyone thought China was going to be going gang busters and what happened was Europe exploded in the first part of the second quarter. We went from a risk-on environment to a risk-off environment. We lost some off of there. We have never lost off that much in a quarter for you. We have made some steps to correct it. If you look at the first month of the second quarter, July, we made up thirty basis points of that loss in the first month. We feel we are on the right track to get this corrected for you. We also feel like the changes that we made organizationally in terms of who we're hiring will also help us in addition to that. If there are any other questions I can answer for you on this, I have oodles of data, and I could answer just about any question you could throw at me. It's just a matter of how much time you would like to spend on it. Gerard Cruz: From inception you're still up. Scott Westphal: Yes. Gerard Cruz: Have you taken some money off the table on the retail. Scott Westphal: We have and one of the things we did do is we took some money off of the lower quality retail and we're concentrating on A quality retail because we think that an uncertain economic environment the upper income groups usually continue to spend. Gerard Cruz: Do you think they'll continue to spend because there's contemplation – I don't know how far it's going to go, the tax relief. There's talk about removing it altogether, there's talk about removing it for those that make in excess of a certain dollar amount. If there is some compromise made so that the tax goes into effect and get returns to what it was, 6.2 or at the two hundred fifty. Do you think that's going to impact the higher end retail sales. Scott Westphal: I think it will. It is something we're watching very carefully. One of the things that, for better or for worse, the chopping can get worse in the United States due to the line share of retail spending. Unfortunately, if you take away income from them through increasing their income tax levels, you might think you only impacted a very small portion of the economy, but you actually impacted a much larger part of it because of their spending behavior. Not only that, but those people – and this is something that you don't see in the economic data. Those people spend a tremendous amount of money on services and those numbers aren't even really being tracked. The amount of money the upper income people spend on services for their homes, for their cars, for their travel, all of that gets impacted. The idea that you can raise the income tax rate on a small percentage of the people and do virtually no damage to it – to me it's just a fantasy. It just doesn't really plan out that way and we need to get real about it. The other thing that you have to worry about though with the fiscal cliff is that there are two parts to it. There's the payroll tax and the income tax. But, the other part is the spending part. If they actually have to go through and cut the spending, then you've got a double whammy on your part. Gerard Cruz: I can't see that happening. Scott Westphal: I can't either, but here's the issue: we are building up a deficit of about $1.2 Trillion per year. If you look at the entire history of this country prior to four years ago, we built up $10 Trillion in over two hundred years in this country. We are building up over $3 Trillion a year right now. How long do you think we can keep going like that? The other thing you really have to worry about is that when you look at the component of the federal budget, that is interest on the federal debt, it's a huge part of the overall budget, but it's being artificially held down by the fact that we are financing that with short term treasuries. Gerard Cruz: I agree with all of that, but what is the biggest problem in the U.S. today in terms of trying to get the economy back to jump start it. Scott Westphal: If I were running the show, I will do a couple of things – one: we have the highest corporate income tax rate in the world. We used to have the second highest. Japan used to be the highest. Japan just cut their rate. We need to cut our rate to make it more attractive for companies to do business in the United States. The second thing it would do is there are trillions of dollars that U.S. corporations have that are sitting outside of the United States. They could come into the United States and be invested in productive labor and productive resources. That money won't come in unless they cut that tax rate. There's a fight going on in Washington between repatriating that money and lowering the tax rate. The other thing we need to do is we need to decrease the regulatory burden. Gerard Cruz: I agree with that. Scott Westphal: We've had a huge increase on regulatory burden in the United States over the last couple of years. Gerard Cruz: I agree that the cost of regulation has been high on all businesses. Joe T. Agustin: It's like tail-wagging the dog. Antolina Leon Guerrero: The dog almost drove us into the ground. Rosalia Bordallo: Had the dog had behaved properly we won't have to have some much rules. That's the problem, the dog just went wild. Gerard Cruz: So my question is what's the biggest problem in the U.S. Currently in the short side, it's basically jobs. Everybody is talking about trying to jump start the economy by growing jobs. Cutting the deficit – addressing those problems by reducing expenditures at the level that many of the politicians are trying to reduce it is not going to address that issue. Scott Westphal: Not in a short term. In a short term it will be pretty detrimental. Gerard Cruz: It's all deleveraging and consumer spending is going to get affected which is 70%. It's just not going to work in a short term. Scott Westphal: This is the balance sheet recession we're in and the good news is that corporations have deleveraged already but the individuals are still deleveraging. Gerard Cruz: We talked about that this morning and absolutely corporations have deleveraged and its helped to the extent that their balance sheets and their profitability are looking much better. Scott Westphal: The problem is that the government has levered up. Gerard Cruz: That's where the leverage went and in order for the corporations to be able to deleverage and to put themselves in a better position, somebody had to step in. If the government didn't step in back in 2008 with a lot of this stuff that they did, who knows where we would have been. If the government didn't save some of these companies and if they didn't perform to maybe one or two, I don't know where we would have been. Maybe we would have been better. There's no way to tell. Scott Westphal: It's an impossible question to answer. Gerard Cruz: Those were done just because of certain issues that were happening at the time and when the government is in a position it's in, not because of something that happened in 2008, it's something that happened in 1994 that the straw that broke the camel's back just happened in 2008 and that's when everything just started to happen. Scott Westphal: The problem, if you want to look at Europe as an example, Europe has been supporting social and entitlement programs for decades and the issues that you see rearing their ugly heads right now, is a result of decades of spending. You need to resolve the issue at the spending level. I understand your concern about the immediate impact of that. Gerard Cruz: Even in the case with Europe, what happens when you try to raise the tuition for British colleges or raise the retirement age for French government workers or try to impose some austerity measures for Greece civil service, you'll have something close to anarchy. You have people on the streets. Scott Westphal: You do, but the problem is right now is not just Germany, it's the other Northern European countries like the Netherlands were basically digging their heels and saying look we don't want to do it anymore, we've had enough. Gerard Cruz: I don't propose an answer because I don't have one, but these problems are very complex. Scott Westphal: They are. When you look at Germany, Germany is just finishing the reunification process of East and West Germany. That cost West Germany trillions of dollars. They're already frustrated from that. The idea that they will bail out countries like Greece, Spain, and Italy, where they have no keen ship with those people. Gerard Cruz: Those countries don't seem to want to do their part. Scott Westphal: They don't. What's happening in Spain and Greece right now is they're asking for additional flexibility on the austerity programs and Germany and the Netherlands are saying, guys – you either follow through or we're not going to come through with the a package. It's one of the things that we're a little scared about. It's one of the reasons that we've got portfolio positioned pretty defensibly. That's why we are where we are. Gerard Cruz: Regarding our portfolio, given those uncertainties right now, if you had the option of putting some money in cash, would that be something that you would be interested in. Some of our portfolio - taking money off the investment table and putting it in cash. Is that something that you like to do? Maggie Ralbovsky: Would you like allowance in your guidelines for cash. Scott Westphal: I think in times of uncertainty to have the flexibility to do that is not necessarily a bad idea because we could have a situation in Europe that explodes and that's something that we have to be conscious of. One of the things that is in your favor right now though is that the U.S. is widely viewed as the place you want to have your money invested in. When we have people that travel in Europe and Asia, all they want to talk about is North America. They don't want to talk about Europe. They don't even want to talk about China right now because China is in this very precarious situation that we talked about earlier. There is a fear that they could have social unrest because of inflation. They could have rising labor prices which would impair their competitiveness in the manufacturing world. There's a lot of moving pieces there that could be troublesome. Maggie Ralbovsky: If you have ten percent allowance for cash, would you want to use it right now. Scott Westphal: Not right now, but we could do it like that – we could do it in a day. We certainly want to have the flexibility. I don't think it's necessarily a bad thing. Maggie Ralbovsky: It's not something you wish for either. Antolina Leon Guerrero: It's a contingency. Scott Westphal: No, it's not, but recognizing that we live in a very uncertain world. One of the things that's causing so much unemployment in the world, including the United States, is that there's so much uncertainty with companies in terms of tax policy, regulatory policy that they're reluctant to hire. And, you have the same issue in Europe, only in Europe it's even more troublesome because once you hire someone in Europe and a lot of the countries, if you do need to terminate them, your cost of terminating them is huge relative to the U.S. Joe T. San Agustin: It discourages investing in the U.S. Scott Westphal: It does. If you're an entrepreneur - I can tell you stories about entrepreneurs who are frustrated. They're

frustrated by the uncertainty, they're frustrated by the regulatory burden, and they're frustrated by the fact that they see opportunities, but they're so afraid to pull the trigger. Joe T. San Agustin: That's the only reason why the banks have decreased lending money. Gerard Cruz: Well it's cheaper to borrow from the feds. Scott Westphal: That's a big issue right there –what you just spoke about. Maggie Ralbovsky: It's called a liquidity trap. Scott Westphal: It is. In any event, are there any other questions I could answer for anyone. Joe T. San Agustin: You're right on time. Scott Westphal: Okay, thank you so much. I really appreciate speaking with you.
(End of presentation by Cornerstone)

Respectfully submitted,	**Affirmed:**
JACKIE BLAS	**WILFRED P. LEON GUERRERO, Ed.D.**
Recording Secretary	**Investment Committee Chairman**