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**Quarter Ended March 31, 2014 DC Plan
Quarterly Performance Meetings**
April 24, 2014
Retirement Fund Conference Room

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David M. O'Brien, Trustee

Staff Present:

Paula M. Blas, Director
Diana T. Bernardo, Controller

Other Present:

Terry Dennison, Mercer Investment Consulting Inc.
Doris Flores-Brooks, Office of Public Accountability
John Borne, Great West
Alice Tajeron, Great West

Economic & Capital Market Environment
DC Plan Performance
GWRS Annual Review

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Economic & Capital Market Environment

Terry Dennison: We'll start with the discussion of the economy. It's always I start with the world, then we'll talk a little about what the markets are discounting because the way the markets work is they tend to first of all try to think about what they expect that's going to happen and that's call discounting and then they react to what actually does happen and that's why you tend to see when news happen it reacts if the news is not what they expected because they build into the pricing their expectations and if the expected happens typically there's very little reaction in the market or when the unexpected happens then you get the big change. And clearly last year we had a risk version that we saw in the global financial crisis continue to evaporate is the Global Central Bank continues to put tremendous liquidity into the market and we saw the security prices pretty much generally raise dramatically. And we saw high equity prices, tight credit spreads, low interest rates, low in pride volatility and very benign conditions and it hasn't changed that much this year. But we have seen a flattening in equity prices if you remember last year we saw the equity prices in the US up about 30% we have not seen that this year because there are some cautionary notes, you are seeing slower discounted future growth.

The census that probably we're not going to see the same kind of growth we've seen in 2012-2013 going into 2014 and perhaps into 2015 the equity returns are likely not to be as strong as we've seen going forward and particularly in the emerging world where a lot of growth was expected, we're now seeing substantially lower discounted future growth going forward. And you can see that particularly in commodity prices, commodity prices are particularly sensitive to expected demand from the emerging markets. Emerging Markets are the great consumers of commodities things like copper, iron ore because they're building things. If you travel all in the emerging world you see they're just building stuff like mad and consuming great quantity of basic materials and as soon as the demands slows the other consumption of these basic materials drops dramatically. Countries and companies that are big suppliers and producers of these suffer dramatically and also we've seen as liquidity has dried up particularly dollar liquidity the Federal Reserve have been slowing their bond purchases, the slowing of QE3 and dollar liquidity has been slowing inward for investment into the emerging countries has slowed dramatically and we're going to talk a lot about that because that's one of the major threats we're now seeing particularly to a number of emerging countries and to a degree the biggest emerging market of them all into China.

I am going to talk about China particularly because from a global perspective there's really only two countries that matter, its China and the US, the rest of the world really doesn't matter from a global perspective. Doris Flores-Brooks: Not even India. Terry Dennison: Not even India, frankly not even Europe. Incidentally most of you know I spent the last two weeks in India which is a fascinating place I could tell you stories I have not been there before, the closest I have been is to Singapore a number of times but India is a very interesting place. Just like the US except all those people are small and have black hair just like the US. China is potentially the trigger of some very difficult things. China is slowing dramatically and you can see it in the slowing of growth there, the currency is losing value. The Chinese government has been slowly increasing the value of Yuan which is a managed currency partly to avoid issues with the US historically they maintained a

very much of a mercantile list currency strategy, they began keeping currency cheap versus trading partners particularly the US dollars to favor their exports. This obviously irritated the US and Congress has periodically threatened sanction against Chinese imports and basically they stayed just ahead of the sanctions and have basically been increasing the value of the Yuan a couple of percent a year and literally the Yuan has fallen about 3% since January a clear break from their past practice and had the biggest one week fall in 20 years and this has triggered a lot of issues because one of the long standing trade in the market is a carried trade in the Yuan because the government has been managing it, it made a very interesting trade you could borrow dollars cheap because they were very inexpensively priced by Berman Bee Yuan and basically just get a risk less transaction. Now the problem is that all of a sudden reversed, you lost money on that trade and since a lot of people were doing that with borrowed money now all of a sudden there was a lot of losses flowing through the system and that cause a fire sale of Hong Kong properties as Chinese investors were desperate to raise cash. Some Chinese properties in Hong Kong were cut in price 20% to get quick sale because of a necessity to raise cash this produced liquidity squeeze in Mainland, China led to a clasp to couple of property companies one a not going to attempt of the Chinese name a real estate company with 570 million US dollars in debts failed obviously the Chinese have a lot of money and they can deal with this, they have a lot of money but they do not have an infinite amount of money and will get in the scale of some of these debts that they have. This is also potentially raising issues with the banks because the banks have been big lenders to Chinese property companies particularly European banks the UK banks through Hong Kong and other Europeans banks have been big lenders not in Yuan but in European currency and in dollars to Chinese corporations so there's a real threat to the global banking system taking place there with what's going on in China. The Chinese companies borrowed about 1.1 trillion US dollars in the Hong Kong markets. I mentioned a quarter in UK banks and a number of major global banks now have raised flags saying that this represents a very serious issue to the global banking systems. Morgan Stanley has raised the issue that China may be approaching a Minskee moment and I'll explain what a Minskee moment is. It's a phrase that's surfaced with the US global financial crisis, basically this is where a credit bubble collapses of its own weight. What happens is that the credit growth is no longer sustainable what's happening now is it takes about four Yuan of debt to produce one Yuan of GDP growth. As late as the middle 2000 one Yuan of debt produced one Yuan of GDP growth. So, what's happening now is the economy is becoming so indebted that it takes so much more debt to produce a dollar of growth that eventually becomes unsustainable. The Minskee refers to an economist who's largely ignored until the global financial crisis who identified that there are three (3) phases of crisis. Phase 1 is where people are able to pay and I'll use household mortgages as an example although it could be used in any sort of contacts where people can pay a mortgage, principal and interest, so basically pay a mortgage both the principal and interest. And the second phase is they can pay the principal but not pay the interest. And the third phase is where they can pay neither the principal nor the interest and that's the Minskee moment because that's when literally the whole cycle collapses and effectively what you have is a Ponce' scheme and the Morgan Stanley comment is effectively saying that Chinese credit bubble has now arrived at basically being a Ponce scheme where they now need so much money flowing in to be able to sustain the credit. In fact they actually characterized it as a Ponce scheme, the Ponce finance dominates the China economy at

this stage a question of when and how the system current instability resolves itself that's a quote from Morgan Stanley.

Wilfred Leon Guerrero: This money that the banks have is mostly US or European. Terry Dennison: Mostly European banks, the US banks have largely stayed away. The problem is because Hong Kong is always been the gateway to China and the big European and particularly UK banks have always been based in Hong Kong, ShunHun, and Shanghi banking corporation started there. So a lot of the banks saw big business there and the three banks I've mentioned Citicorp basically put out an alert saying that the Chinese carried trade is now become dangerous and the flood of hot money into China is at risk of sudden reversal that Citigroup characterized it as a second phase of the tapered tantrum. People are now spending a lot of time with thesaurus finding clever ways to characterize these things. David O'Brien: The debt is unsecured, sovereign secured? Terry Dennison: Most of this debt is actually to corporations. The Chinese government has plenty of money that's not the issue. The problem is a lot of this debt is to corporations either government sponsored or private and it's not in Yuan, it's in dollars they're big borrowers in foreign currencies so they've been borrowing in dollars.

Doris Flores-Brooks: So, is this debt like Japan where it's more contained. So, if China has its fall out, will the rest of the world follow too? Terry Dennison: These are debts that are owed to foreign banks. Doris Flores-Brooks: But you said the US was not as large. Terry Dennison: They're US dollars but they're not owed necessarily to US financial institutions. One of the quotes here they argued that Chinese credit boom has become a function of external dollar funding mostly through off shore lending in Hong Kong and Singapore to circumvent internal curves. It is a side effect of super loose policy the Fed which the Chinese have been unable to control. Basically, the Chinese banking system the people's bank of China tightly controls credit growth. So in order to get credit for the enormous infrastructure that you see there, the tremendous growth of building, cities, railroads, all of this infrastructure growth they can't get funding from the peoples bank of China so they get bank growth from the informal banking system and a lot of this is through either trust products or lending from foreign banks often in dollars and that's where the threat is.

David O'Brien: I know this is a detailed question, but do you know the percent secured to the loan or how much the percentage secured of this loan of the 1.1 trillion valued the loan? Terry Dennison: My guess is the security is the project themselves, the empty buildings this is largely unsecured, you have all these empty buildings. So, that's why we're talking about this here is the risk to global financial system is basically with the same situation a much smaller degree exist to a number of other emerging market countries it's the contagion risk from Turkey, Brazil, to some degree Russia. Forgetting that you have political issue but just from the financial issue there's a number of emerging market countries with Argentina representing a risk of global financial system.

David O'Brien: Yeah, what's running through my mind obviously is how it plays out and we don't have any history on the Chinese bank and Chinese government how we might handle it appears the property guys just kind of disappear and there's a global response. Terry Dennison: The Chinese government these are very, very clever people the question is they're walking a tight rope, there's very little experience, very little prior practice, they're

very smart, they have a lot of money the question is, are they going to be able to handle it? Global central banks are very conscious of this as well as the World Bank, the International monetary fund, the Bank for international settlement everybody's aware of this it's not a big secret. The question is, are they going to be able to cool it down without it blowing up? David O'Brien: Didn't the Euro banks just go through a recapitalization?

Terry Dennison: Well they're running the stress test and in unlike the prior stress test which were a joke. Now they're running real stress test and the concern is that there now some of the big commerce banks particularly in Germany are likely to fail. David O'Brien: Fail the test. Terry Dennison: Fail the test, because unlike the first test which were kind of softball, these aren't. In fact Citibank has failed ours, they've got over leverage and they failed ours. David O'Brien: So are they mandatory. Terry Dennison: They're going to have to raise all the capital. David O'Brien: It's mandatory. Terry Dennison: Mandatory. This time they're playing hard ball with us and I think you're going to see a lot of capital raising and a great deal of restriction on things like dividends and pay outs and the like because there's realization at the banking system is going to be very stretched. A lot of the global banks that have made a lot of loans to a lot of these countries and not just the countries, it's not the country China that's the issue, because China borrows in its own currency and of course they can print plus they have tremendous foreign currency reserve. The issue is government sponsored corporation, the provinces and private corporations that have borrowed principally in dollars and principally from foreign banks those are the issues. The question is, is the government going to bail them out and can the government bail out? Are these debts too big? David O'Brien: How would they bail them out because given that the primary US dollars holdings are the US treasury and US bonds. Terry Dennison: If they have to sell those now, there's going to be a spike in interest rate.

David O'Brien: Not only that you have two things going on at once a fling on the global side to save investment allied US treasury and bonds at the same time you have Chinese selling US treasury and bonds to recapitalize their banks. Terry Dennison: And the question is, sell them to who? James Duenas: So that leads to the valuation of the dollar? David O'Brien: Not necessarily but it's just interesting if Terry is positioning this as a big threat the question is how do you think your way through it? Doris Flores-Brooks: Can I deviate for a little bit, I remember two years ago we were talking about the demise of the European Union with Greece and everything that seems to have kind of like worked its way around. Terry Dennison: It'll be back. Doris Flores-Brooks: It'll be back because right now you don't hear much about it. So, Greece is gone away, now it's China. Terry Dennison: Basically the issue is frankly Europe is a side show. Remember back during global financial crisis we talked about systemically important banks we're now talking about systemically important countries. Europe actually is not systemically important and Europe could go down the drain and it really wouldn't be important. China is important systemically now we're talking really big chips because of the amount of money involved.

Terry Dennison: Let's talk about the US. The US is actually is doing a little better, now a little better on a relative basis we're now about 65 months into our so called recovery. Doris Flores-Brooks: This is a long one by standard. Terry Dennison: Post World War II economic recoveries this is getting a little long enthused. This is about the average length of a Post World War II recovery. It's also about the weakest of the Post World War II recovery particularly given the depth from which we are recovering. Historically if this were

a normal recovery we would probably be looking at the beginning of a slow down but the reality is everything is now so managed that I'm not sure if we will have another slow down. Although, we are seeing a bit of slowing in terms of retail sales things are still not looking very good, the public unemployment number seems to be declining but we're not seeing big improvement in hours worked, we're not seeing a big improvement in disposal income, we're not seeing a big improvement in basically standards of living, we are seeing a bunch of improvement in statistics if you ask people how happy they are they're not seeing a great improvement in happiness.

But the US is doing better than just about anywhere else. The Federal Reserve is beginning to try to normalize and of course the Federal Reserve impacts the rest of the world and this is actually the slow down. I mentioned that the Fed is beginning to taper its bond purchases, it's now beginning to adjust the rate of those bond purchases somewhat this is causing some anxiety just about every economic entity outside the US has become anxious about the rate in which they're doing it. In fact they're doing it at all because the reduction in US dollar liquidity is beginning to put great stress on emerging markets that are dependent on dollar liquidity basically all the rest of the world has now become addicted to easy US dollar money. However, they clearly pointed out the sign on the door is US Federal Reserve and US Federal Reserve thinks this is the right thing to do for the US and despite everybody saying would you please not do it, they're going to continue to do it. There's been a lot of speculation about how this is going to play out. I think the best thinking we've seen and we're looking for a lot of different sources I read about 20 economic bloggs a day. I read about 10 newspapers and about 20 economic bloggs everyday.

The sense is that one thing they have done is they're trying to provide forward guidance, they become a lot less clear as to what that guidance is based on and now it's become a lot more vague because the trouble is 6½% unemployment because if you have to look at participation you've now got workforce participation is becoming a fuzzy number, as the baby boomer head into retirement, you have a lot of people on disability, it's now not obvious what does 6½% unemployment mean, it doesn't mean same thing that it meant 10 or 20 years ago. But, the sense is they just can't keep growing the monetary base, obviously some of the bonds they've been buying are maturing they're not just adding 80 billion dollars or 70 billion or 60 billion dollars a month to the monetary base because some of these bonds are maturing but the reality is the Fed balance sheet is getting bigger and bigger and at some point they're going to have to say that this is going to become a problem, they're going to have unwind it and unwinding it will become extremely negative for economic growth.

It's been very simulative to do it, to withdraw it or to reverse it becomes very depressive and that would become very negative for the economist they don't want the problem to get bigger because when they unwind it, it's going to be very negative. So the question is, how long is it going to take for the QE withdrawal to reach zero and when are the rates going to start to rise? The question then is, when does Ms. Yellen's view of interest rates start to become a factor? She is believed to be somewhat more of an inflation dove than Dr. Bernanky. That she is much more a believer that a little inflation is not bad but the problem right now world-wide its not inflation but deflation will get to this in Europe. Europe now, there are 8 Euro countries that actually have deflation which is extremely

bad because deflation actually produces a very evil economic effect because that makes it extremely difficult for indebted countries to ever get out of debt because then in effect real interest rates become extremely high. Because if you have negative inflation you have deflation real interest rate becomes extremely high and the debt burden just grows and grows that's what you had in the US in the 1930's. Any debt actually grows very rapidly you can never get out of debt, you just get on this debt treadmill and that's what you got in the Southern Europe countries and now just about every country other than Germany is either in deflation or just about neutral inflation. Gerard Cruz: Every country? Terry Dennison: Just about, I'll give you the list before we get to Europe.

Terry Dennison: The only country that's well clear is UK and because they have their own QE program. And the problem is the ECB because of dark mutterings from the Germans will not go there at least they haven't historically gone there, now they're making noises they may have to. But, the reality is even in the US inflation which the economist like to think around 2% is now running low below 2%. So realistically the economy could frankly use a dose of inflation but realistically you're probably going to see rate start to rise not because of demand pushing rates up but because the economist say we need inflation to avoid the evils of deflation that you're going to see effectively. What you saw in Japan that's basically the government induce inflation simply to avoid the evils of deflation because that's what you've seen in Japan for 20 years. Wilfred Leon Guerrero: So when is it going to happen? Terry Dennison: The best thinking we see is beginning of 2015 which is only 8 months away. That the reality is that the concern that you could be entering a long period of Japanese style stagnation is going to be so concerning that you could start to see rates rise and the sense is that the economy is strong enough and we've done so much in a way of deleveraging. I mean corporations have deleveraged, households have deleveraged, rising interest rates is bad if you're heavily indebted. Well, Corporations have delevered, individuals have delevered, governments less so and the big government can still print money so the reality is you can raise interest rates without strangling the economy.

The tool of raising interest rates and what it used to do is they used to use it to cool the economy because if you raise interest rates, interest expense went up, profits went down and that slowed the economy. But if you don't have a lot of debt you can raise that dial, it causes inflation to go up but it doesn't have the same slow down in growth because it's not being applied to as much debt that's the advantage of the good deleveraging we've had in the US. And that doesn't work as well in Europe because they haven't had the same kind of deleveraging in fact they've had more leveraging particularly at the Government level the debts in Europe had been going up, they haven't had deleveraging. They hadn't written anything off, the governments and individuals if you look at some of the debts statistics in the individual level in countries like the Netherlands, in Finland the individual indebtedness is gigantic. And if they raise interest rates there, you would start to see people really hurt but here you could raise rates, you could see rates go up a couple of percent and wouldn't slow growth dramatically because we've really cut back on the amount of debt in the system. Doris Flores-Brooks: Wouldn't that effect housing in the US? Terry Dennison: Yeah, a little bit.

David O'Brien: How about Corporate investment? Terry Dennison: Corporations have really cleaned up their balance sheet a little bit, may have cleaned up a lot. I am not going

say there's no effect but it's not going to slow down the economy, it's a trade off. I think the concern of avoiding the Japanese style deflationary trap is going to cause them to say let's have a little inflation plus I think you got Dr. Yellens believe that a little inflation is going to be helpful. So you're going to see a move to actually start to raise rates sooner than you think because of an issue of let's have some inflation because it's good for the economy. Doris Flores-Brooks: When you say sooner than we think, what is sooner? Terry Dennison: I say the beginning of 2015. David O'Brien: So you are going to talk about how this plays out in stocks and bond markets. Terry Dennison: Clearly bond markets are not going to be healthy I mean clearly mechanically bond prices go down when interest rate goes up. The effects of stocks is not mechanical, bond prices is mechanical because it's changing the yield to maturity. Stocks to some degree remember I said you're talking about what's priced into the market, what's been discounted I think you're beginning to see the market start to discount some of this in. In fact that might be why you are not seeing quite the dual market that you saw before.

Gerard Cruz: I think if the rising interest rate worked it's because of the price because of its forwarded announcements not so much because of the fact that inflation is going to start to appear and this is because I would think that the more money chasing goods would cause inflation. The more money chasing goods is a result of lower interest rate not necessarily higher, so going up in interest rate causing inflation is a little kind of intuitive. Rising interest rate announcing it a year before and pricing it into the market and having it successful would cause the inflation.

Terry Dennison: I don't think this is going to be scarce city of goods causing price rises. I think this is going to be purely interest affect. There's a surplus of just about anything you could imagine. There's a surplus of labor, a surplus of goods, commodity prices are down, I don't think its commodity price inflation, I think it's a price of money inflation. Gerard Cruz: Yeah, but the price of money is higher, then it would make more sense for investors to just keep it invested rather than to spend it. David O'Brien: Well stock markets kind of the hedge against inflation in a way and you get rotation out of bonds. Gerard Cruz: I think people get hurt in bonds. Terry Dennison: We get killed at bonds particularly in sovereign but everybody knows, I mean everybody is out of sovereigns, nobody's owns treasury or any kind of sovereigns. Gerard Cruz: If you are, you're just crazy. David O'Brien: Unless you're playing to safety unless you're a good China believer, the China disaster believer. Gerard Cruz: But even that is one of those too big to fail scenario where you just can't allow China to blow up. David O'Brien: It's the 12 month shock. Terry Dennison: But if you've got to own bonds, be short, shorten your duration you don't want to be 30 year. What you are going to see if it's the long end it's going to be impacted the most of all, so you're not going to have a parallel shift and a yield curve because the yield curve not going to be a parallel shift because the bottom end is still going to be controlled by the Fed so it's going to be a whip at the long end, not parallel shift. David O'Brien: But of course it's the opposite of what's happening on the yield curve today. Terry Dennison: Yeah. Gerard Cruz: Just real quickly on China again, you mentioned there's a lot of foreign debt. Terry Dennison: Dollar debt. Gerard Cruz: Foreign dollar debt, foreign banks not with US banks. Terry Dennison: Typically not US, what we're seeing is not a lot of it in US banks there's going to be some, Citibank going to be over there, Chase is going to be over there.

Gerard Cruz: They're buying large though, they're European banks. Terry Dennison: Mostly European banks. Gerard Cruz: So, with the European central bank instituting that similar act in purchase program that at some point it's going to mature as well and if Europe then is not a player in this whole scenario meaning that if they went South it won't make a difference if China fails and brings down Europe, would they have a systemic impact? Terry Dennison: Let's be careful, let's not get too carried away with the language. China is not going to fail, the country is not going to fail it's going to be the credit bubble in the Chinese economy particularly these highly leverage, the wealth management products, the trust product, these loans to the developers, all of that. Gerard Cruz: Agreed. So, one of my question is over riding basically, then. Is this a China corporate problem? Terry Dennison: It's a China corporate problem. Gerard Cruz: So not the China government. Terry Dennison: The Government has plenty of money and they can print their own. Gerard Cruz: Okay, so it would be an asset adjustment issue not necessarily a fundamental systemic, China goes away as a second largest in the country.

Terry Dennison: China is going to spend some of its reserves just like it has already. China has spent several hundred billion already to deal with some of these early failures to try to reassure the market. Somebody once said several years ago couple hundred billion here, couple hundred billion there, after awhile you're talking real money. Gerard Cruz: Would it be better if they just floated their currency and let it adjust for itself. Terry Dennison: The problem is that it's going to be an issue with their whole mercantile economic structure I mean it's a managed currency. Gerard Cruz: But everybody knows that. David O'Brien: And it exasperates their problem because all their loans are in US dollars and so you let the currency float assuming that the immediate effect is something similar to the 3% drop you've got now, what does that do with the credit bubble crisis? Gerard Cruz: It just exasperates it, but does market to market which causes the European banks to address the issue today rather than kicking it down the road which is what they did with Brazil and all those other countries which is why nothing has been solved which is prolonging the issue which I think the euro currency and the euro countries.

Terry Dennison: I think if you look at the behavior at the Chinese leadership they're exceedingly conservative, they're exceedingly cautious. They're going to move very cautiously in a very measured fashion they're not going to do anything radical, they're not going to do anything bold, they're going to be very cautious and they're going to be very careful. I think frankly at the end of the day I trust them more than I trust most people. They got the long view they're not going to do something stupid, if you look at their background and this is not the post mild generation, a bunch of goof balls these people are mostly western educated. This is a pretty sharp bunch of people that's running this country, if you look seriously at their background and read their resumes they're not just a bunch of faceless guys in ill fitting suits you really look into their background these are the kind of folks you wish they're running your country, I think they'll be okay.

Gerard Cruz: I have a bigger question with Emerging market because it's an asset class in both DC and on the other plan we are pretty heavily weighted-in, do you think that problem with emerging market is a cyclical one? Terry Dennison: To some degree it's cyclical, the reality is that the long term story is still sound, the growth potential is still there but like a lot of stories it can get ahead of itself that it can get over sold and the stocks get over bought if you get the distinction. The demographic story makes a lot of

sense the economies are younger they're growing from a smaller base. They tend to actually have less debt if you look at the actual indebtedness of these countries they have less debt than the developed world does. They tend not to have as much in the way of liabilities maybe they should, they typically don't have social security systems, they cannot have health care system, maybe they should but they don't. The reality is that their economic balance sheets look better than developed worlds do, their health care isn't as good and their living standards aren't as good but the reality from a financial perspective they're probably are in better shape.

The reality is that they're growing from a smaller base they can grow faster, they're younger, their demographic picture, their demographic wedge looks better but the reality is that at some point there expensive that you still have to look at price. Anything is a good deal if you can get a cheap enough price well they're pretty richly priced now, that store has been in the market for 10 or 15 years it's been bid up and maybe it just got little to rich. The emerging market story is still there it's not as good as it was 15 years ago certainly not as good as it was 25 years ago, the problem is it's gotten a little rich, it's a little over priced and there's going to be some adjustment.

Wilfred Leon Guerrero: Tell us what's happening in Japan? Terry Dennison: Let go to Japan. Japan after seemingly endless efforts to try to do something about their economy tried something kind of bold. My headline here is Japan shift towards a beautiful deleveraging monetary policy is showing some signs of working. Their problem of course is that they had 20 years of effectively a deflationary trap prices have been following for 20 years, the economy has been contracting from a hugely over inflated base, if you look at where they were in 1989 it was hugely over inflated. And they have a huge debt problem, now they owe debt to themselves they can't really go broke as a country because they owe the debt to themselves. And after an enormous amount of fiddling around of trying things they finally decided at the end of the day let's just print a lot money and it finally worked, they drove down the value of the yen that stimulated imports it certainly had a positive impact on the stock market, it did stimulate corporate profits largely because as an exporter the fallen exchange rate simply cost their revenues and foreign currency will be revalued to their base currency it will be worth more, so it clearly benefited that.

They did not significantly increase their corporate spending or hiring, it basically just flowed through as profits, it did increase household confidence they did lower their savings rate and did increase their spending a bit. It did cause a little bit of an expansion, it hasn't really cost them to be a lot more competitive and it hasn't really cost them to do a lot of increased fixed investment they haven't really invested a lot of the money the corporations basically just pocketed. They got somewhat higher inflation rate and the services has moved from deflation to inflation. Also, starting in April they had a negative fiscal change they've increased the value rider tax which was sort of an odd move I guess they needed the money because the government is now spending more and of course it has exactly a negative effect that's a depressant and now basically that's going to put downward pressure on growth.

So, they had a growth spurt because businesses saw improvement in profits because they've been now translating their foreign revenue which is substantially in an export based economy into lower valued yen so they were getting big improvement, increased in

spending at the consumer level but now VRT is higher, so everything is slowing down again, so will have to see if it continues to improve. But I think the decision which was probably necessary given that they don't have a lot of latitude on the debt side probably most indebted develop country in the world. But, the reality is that they felt they needed to increase the value rider tax but I think from a strictly economic perspective that was a poor move on the fiscal side, we'll have to see. Wilfred Leon Guerrero: What I like to know, are they still going to do some traveling?

David O'Brien: The question is, does that consumption tax apply to travel packages as well? Terry Dennison: I would assume as a value added tax it would only be on things purchased in Japan. David O'Brien: If they purchased the travel packages in Japan. Terry Dennison: I would assume if they're buying a package deal in Japan that it would be increased there, now of course it's also more expensive for them to come because when they translate their yen into dollars. David O'Brien: Well you got 3 effects, the consumption tax, lowered value yen and less disposal income because of the consumption tax effect on other things you buy, that's all negative for us. Terry Dennison: Now, they're feeling a little wealthier but the reality is that they're wealthier perhaps in Japanese terms but not wealthier when they come here, so that's not positive when they come here.

Doris Flores-Brooks: And there is a slowing down already, but fortunately Korea is picking it up a little bit more. David O'Brien: Dollar pressure on the yen, continue? Terry Dennison: Well they've seen this works and after 20 years of trying everything else under the sun including gift certificates for everybody in the country that didn't work I think they'll keep doing it. It's only working for 20 years I think they'll keep trying to do it. They have the right kind of economy for it to work if you are an export driven economy lowering the value of your currency. Now, the other thing is to some degree they do compete against China for exports with the Yuan dropping in value they're going to have some kind of competitive devaluation or they're going to start to lose high value exports against export markets against the Chinese. Gerard Cruz: Everybody's devalued that's this whole race. Terry Dennison: But you are going to have a competitive race to the bottom devaluation so they're going to have to devalue to some degree on a competitive basis. So, you're going to have a round of competitive devaluation in Asia. Gerard Cruz: That's amazing because everybody's racing to the bottom including the US for awhile it started with the US everybody thought it would work. Terry Dennison: You can see the damage that it's doing, the one that is suffering is Euro. I mean the Euro is soaring verses other currency and it's just killing particularly the Southern European countries because at this point their exports are not completely priced out of the global markets. Gerard Cruz: Because they still want to retire at 55. Terry Dennison: Well who wants to work 35 hours and other stuff? I've got more but do you want me to do it or switch over? David O'Brien: I want you to talk about the fixed income market, the magical fixed income market.

Terry Dennison: The problem with the fixed income market is it's completely driven by what the Fed wants it to do and it's partly political and again we're heading in to an election year, it's partly political and partly in response to what other governments do. At this point I think you're going to see a continued pressure on the dollar and I think you're going to see rates start to rise. Gerard Cruz: As an investor then, how do you diversify out of that, what asset classes? David O'Brien: That's such a great question because for a

long time we've been talking about we got all our DC contributors and you got on the DB side our investments are huge the bond market, so it's a great question.

Terry Dennison: Well, realistically at the end of the day there are only 2 kinds of investments. They are interest rate sensitive investments where you are basically some form of a lender and there are equity kinds of investment where you are some kind of an owner. That's really the only kinds of things you can invest in and if you are some kind of a lender you have interest rate risk. Now they come in various flavors because you can lend money to all kinds of people, all kinds of places, all kinds of terms. You can lend money to people outside the US in different kinds of currencies, you can lend money to risky borrowers, you can lend money to safe borrowers, you can lend money to short and long term, variable term, but that's the only kind of things you can invest in. You can either lend money or you can own things. So you really have to decide what proportions of your investments you're going to own in the DB plan or what kinds of options are you going to provide your investors in the DC plan. If you strip it all down you can give it all kinds of fancy names, offer all kinds of fancy options that is literally the only things you can offer people, even if you have commodities, even if you let them buy gold, you'll own it. A mortgage REIT is lending money and equity REIT owns real estate, same thing.

David O'Brien: One of the reasons I ask this from the DC side is obviously we have a ton of the member's money in these target date funds. The target date funds conservatively on the retirement 20/20 fund which is where I think the bulk of the money is and those people are in those funds in a lot of interest rate sensitive investments but they don't see that way, they see it as being in a conservative target date fund. That's my issue and I think that's what Gerry's getting at, what is this message and how do we educate people? How do we inform people? These people are out there own their own they're not talking to you.

Terry Dennison: Well that's the dilemma as an investor because in a sense you are trying to mix two concepts because as I said there are two sorts of things you can invest in, you can either be a lender or an owner. But there's another way of looking at things, you can either take more risk or take less risk the problem is that being an owner is generally more risky, than being a lender. There are very few low risk ownership opportunities that are simply the nature of the ownership equation. There are very few things you can own that provide lower risk than being a lender because there are things that you can lend that are very low risk, you can lend for a very short time frame to very safe borrowers. So if you have a near horizon target date fund the options that you can provide to somebody who wants to be conservative which is the theory for a near target date fund are inevitably going to be more skewed toward the lender type of investment. Because there are very few low risk ownership opportunities, I wish I can pull out of my magic hat low risk ownership opportunities but I can't think of any. What can I think of that you could own that's low risk?

David O'Brien: Below inflationary environment catch. Wilfred Leon Guerrero: Dave, do you want Alice to tell the participants that the interest rate is going to go up, get out and buy. David O'Brien: I want us to think through how we send messages or how we offer products to the DC members who are out there on their own. Terry Dennison: You want to be very careful about sending messages. Gerard Cruz: You want to at least help

calibrate their expectations to what has become a different reality in the market because after that discussion you just had in my mind has turned to just the realization, I don't know necessarily equities are the riskier asset class and traditionally absolutely but for the last due diligence go arounds at least when you're here and our DB consultants here, we're hearing that fixed income is a riskier asset only because the likelihood of the interest rates going up and therefore value is coming down is much higher. Terry Dennison: Depends on your time horizon. Gerard Cruz: Okay. Terry Dennison: That's the third factor.

Gerard Cruz: Agree, but certainly there are different variables but if you look at the surprises in the market, chances are for fixed income the surprises are going to be to the downside as it was in May, interest rates are just simply going to go up there is just more risk there and so knowing that and hearing that I think we need to either positioned expectations so that our members understand it or at a minimum create some new menu of items to help diversify.

Doris Flores-Brooks: Part of this also is education and I keep on telling my employees you owe it to yourself to get educated so that you could evaluate. Wilfred Leon Guerrero: The thing I'm trying to point out is that the Board learned about this stuff, how do we communicate to the participants? Gerard Cruz: I mean its good education we are but 7 people looking out for over 8,000, so we need to move that message now. Doris Flores-Brooks: They need an annuity whether social security or something because just the path alone is not enough. Gerard Cruz: I agree. Doris Flores-Brooks: Really they have to have some kind of annuity, just to rely on this alone they're going to be destitute. David O'Brien: Gerry phrased it pretty well, do you have a response to what Gerry asked, Terry?

Terry Dennison: You had mentioned the 20/20 fund, the 20/20 fund of the top probably Alice knows of the back, it's probably 40% equities or maybe even close to 50% equities. I mean the reality is all of these are a blend even a 20/10 fund is probably 30% equities. The reality is all of these funds have some element of risk to them. Gerard Cruz: I think we all accept that but maybe it's just a period in time issue, maybe just this period in time fixed income is just popping up as having a higher than normal risk because of the artificial low interest rate environment that we've been in for so long. So therefore, how do you then position a portfolio knowing that?

David O'Brien: Can I just rephrase the same thing because as you said you have a way of cutting across that's exactly right, you have a lot of people who believe you have the baby boom generation maturing very quickly including several people here. So, my restatement of Gerry's issue which I absolutely agree with is that you have a lot of people who believe they are moving assets toward conservative safe funds. Where in fact if I hear you correctly they're not and I think this is Gerry's point, there's this message out there because we're defaulting many of them in these funds, so I think that view, that cut of it is a hugely important question for the DC members.

Terry Dennison: I just want to give Gerry a thought just to validate what he's saying. In financial theory there's a concept called a risk free rate of return and it's important, it's more of a theoretical concept a risk free rate of return is defined to be the rate of return that has no risk at all and all other rates of return are calculated from it, and we've given

some thought to what Mercer's view of what the risk rate of return should be and the US is generally considered to be US treasuries. We actually think the risk free rate of return should be a blend of the equity returns of global companies like Seaman's, Nestle, General Electric and global companies that make things that are never going to go out of existence that aren't dependent on government actions and step away from being fixed income but literally equity returns from transnational global companies that manufacture things that aren't financial, aren't utilities that make things that global consumers around the world buy. I think people are actually beginning to think in those terms that considering the risk free rate to be your local government short term interest rate is probably out day of thinking the risk free rate really ought to be something that really reflects, something more like what I just talked about. David O'Brien: Large cap core fund. Terry Dennison: Yeah, that's not inconsistent with what you're thinking. Gerard Cruz: What their borrowing rate would be. Terry Dennison: Yeah, that's really what the risk free rate is.

James Duenas: But, technically it's all cyclical. David O'Brien: Yeah, but it's going to play out over a number of years I think that's Terry's point, it's starting to happen in 15 in his view but it will continue through, it'll take a long time. Gerard Cruz: I think that thought is more relevant today while they're considering whether or not the US should be the reserve currency of the world that being the case you would need to find then what is your real risk rate.

Wilfred Leon Guerrero: You still have not addressed our question of what should the Board do knowing or expecting that this is going to occur? Terry Dennison: You can only offer things that the market provides you to offer. Gerard Cruz: Should we be looking at other asset classes? That being the case. Wilfred Leon Guerrero: No, let's talk about this getting to the participant. Terry Dennison: You don't want to give investment advice. You can only provide things that people can buy, you can't offer things that aren't in the market place, you can't offer some hypothetical product that is some idealized pure risk less or risk product, and you can only offer equity funds or blended balance funds or target date funds. David O'Brien: But we don't offer funds. Terry Dennison: Yes. Yes you should educate people but people need to want to be educated, if people don't go to the sessions, if people don't want to go to the effort to learn about it, you can't make them do it.

David O'Brien: But we are defaulting them into certain funds. Terry Dennison: Well you are defaulting them into the most logical fund. Before you join the Board I made my sometimes whimsical over the point comment that the target date fund is the best option for the 80% of the people who realize they don't know anything about investment and for the 20% of the people who think they do and are wrong. David O'Brien: You said that when I join the Board what was your statement, there was 1%. Terry Dennison: Whatever the proportions are, the comment stands.

Gerard Cruz: Are you finding that these target date funds are making their own adjustment in their portfolio to account for some of the changes that we've been talking about. Terry Dennison: No, they are not doing tactical asset allocation, they have a mechanical glide path. We got somebody here who's running one, are you doing tactical asset allocation? John Borne: Our managed account is, Ibbotson, however their target date funds as you said they're typically, they have a mandate they have to stick to a

certain percentage of bonds they may look to cut duration on some of those bonds theoretically. Gerard Cruz: So you could then in theory have a bond portfolio in the target date funds that have a duration that looks closer to the shorter end. John Borne: You could but like Terry said there's only so many investments out there and everybody is looking for those types of bonds if the prices are low. It's not a great time to be a bond investor but there's not a lot of alternative out there people use to think real estate is alternative to bonds and then it crashed, that theory went out the window. Gerard Cruz: So just constantly need an education, just readjusting expectations but it's just what I am feeling is there's a train coming, the lights are on and you see it and we are just going to. Wilfred Leon Guerrero: Maybe John can tell us what they're going to do? Gerard Cruz: Yeah, what are you going to do John?

John Borne: We are mapping everyone to Secure Foundation and they're going to have a guarantee, so if the bonds drop significantly they still have the guaranteed pay out that's one thing the Board is doing. You could think of this I don't know how many of you are parents and had to look for a new car for your teenager and you would research and find out which car is the safest what's the impact rating, does it have airbags, and you look at the gas mileage, what's the trade in value all the things you require to look for in a car, and that's what you all do here monthly, quarterly when you look at the funds and the plans you put together a good plan for a car for your kids but the problem is some of the kids get in the car and find out it's a stick shift and a lot of people don't know how to drive a stick shift some people think they know how to drive a stick shift some people will always lack the coordination put one foot down and pick the other one up at the same time and so I think that's where a good selection of target date funds or management account would come in and have someone do all that driving for them.

Terry Dennison: Nothing is going to correct not putting in enough money and not starting early enough. Doris Flores-Brooks: Right, well starting early enough is already a little too late on that one, so it's more the money. Gerard Cruz: As we all know that it's so much easier said than done. Doris Flores-Brooks: That's why I'm going back to annuity, annuity. Gerard Cruz: I'm with you on that one. David O'Brien: And it's not reflective of our participants either. Doris Flores-Brooks: Because if we just rely on that, people will not survive. David O'Brien: You know our participants have not gone in early we can see it in their balances. Gerard Cruz: And they have not put in enough. David O'Brien: And that's our role. Doris Flores-Brooks: We need to get them into Social Security. David O'Brien: Social Security, that's what you want. Doris Flores-Brooks: Something. Paula Blas: Something. Doris Flores-Brooks: 55% Social Security, 45%. Gerard Cruz: But doesn't take care of those that are in the plan today, we just have to come to that realization. Doris Flores-Brooks: We have to start now. Gerard Cruz: I agree, but those that have been in the plan since day one 20 years or 17, 19 years that group is the one that is looking at destitute sooner than those who start tomorrow because those who start tomorrow will benefit from social security, absolutely. Doris Flores-Brooks: My office is the classic example, I have 10 people who are barely 30 in my office and then a few others are 34, the average age in my office if you take me out of the equation is probably around 30 in my office and they are doing the 5%, a handful are doing the 457, because once a year I talk to them about.

David O'Brien: I tell you the average age at UOG is not 30, the average age at UOG are in the 50-70. Doris Flores-Brooks: You're different. Wilfred Leon Guerrero: So, what would you like to see in your office, you want everybody on Social Security. Paula Blas: Something. Doris Flores-Brooks: For those 30 year olds, Social Security. The last time I heard you do all the mechanics I said okay. I'll tell you my biggest fear about having a modified DB Plan – Hybrid, again the unfunded liability we can't control and look at our 1.49 billion now, down the future that's going to eventually be another unfunded that's my biggest fear on why I am hesitant that's the conservative because we cannot afford again another 1.5 billion that's why I'm still leaning more to Social Security.

Wilfred Leon Guerrero: When you say Social Security, you're just talking about putting everybody on Social Security. Doris Flores-Brooks: No, they need Social Security but then to make the government contribute. David O'Brien: Social Security, plus. Doris Flores-Brooks: It always had to be Social Security, plus. Wilfred Leon Guerrero: So, what's the plus? Doris Flores-Brooks: What you have now. James Duenas: But is the Government willing to spend more. Doris Flores-Brooks: That's why I said after seeing your numbers I was willing too, but my biggest fear is another unfunded liability for the long term for GovGuam that's my biggest fear because then the legislature then will continue to tinker and tinker and you're stuck, that's my biggest fear. I'm saying an annuity they need a paycheck everybody needs to have a paycheck not rely on the funds. David O'Brien: Including the transition folks that was Gerry's point and maybe that the transition folks are in a whole different thing. Doris Flores-Brooks: Yes, but again where do you draw the line who's the guy that made it to it and then the one just below, the one who is one month short right you're always going to have that inequity. Oh, I just made it just like going to school because of what year you were born, you're in you start now, you start next year. I know we've been talking about it and part of it is that selling that comprehensive, do something now for them, do something for all my 30 year olds.

Wilfred Leon Guerrero: I got to tell you we're tired of talking about it we want to take it out of here and send it down to the Legislature. Doris Flores-Brooks: That's my biggest fear. Gerard Cruz: You know the irony is that's everybody's biggest fear the challenges to get anybody to agree on the route to not get us there, the longer we wait the more we have the plan design, the closer we get to that reality. Doris Flores-Brooks: You offer and let people decide Social Security versus the hybrid or if they want to do both then you let them pay the government share if they do both, do one or the other but if you want to do both they have to kick it in themselves with the option to choose. David O'Brien: The buffet plan. Gerard Cruz: You can offer all of that but all of that comes at some administrative cost as well. Doris Flores-Brooks: Social Security does not come at administrative cost that cost is not on your thing. It's on the government to write the check but as far the administration everything else, it's there. Gerard Cruz: Because even the DC is managed by third party has some cost. Doris Flores-Brooks: I have the youngest office I think and I am the only one in the DB, I'm the lone ranger, these kids are younger than my son. Wilfred Leon Guerrero: Okay, let's talk about the performance.

DC Plan Performance

Terry Dennison: Let's get to the bound book going to go through this quickly but there are a couple of decisions here, go to page 11 again some of this is formality looking at the Theoretical Return and Risk Chart and we do have options really pretty much all along the risk return spectrum providing our participants funds to allow them to create portfolios to suit their individual needs.

Looking at page 12, while certainly first quarter returns weren't as luscious as we did see in 4th quarter last year we funded gross of to 2.6%, 401A up to \$368 million, 457 up to \$36.2 million. Page 13, let me go quickly to the observations on the Dreyfus/Standish Global Fixed Income if you remember last quarter we had a discussion of what happened with the proxy vote. We don't know what happened with the proxy vote. We did not hear back from Standish what actually was the result whether the proposed actions were approved or not, so at this point the Fund continues to do well so I think this is going to have to be a carryover we're going to have to find out from Standish, I actually went on the website to see if they reported anything. So, I think we're going to figure out how to find out. David O'Brien: Isn't there an analyst, they must have an analyst, right, somewhere. Terry Dennison: But I was actually hoping is if Great West had some way since Great West turned in our vote was their some way to find out what the result was of the vote. Alice Tajeron: I think the Board had a concern in regards to material changes and we did reach out and there wasn't anything that was reported. David O'Brien: There was two parts, one was the vote itself because that changes their ability to do other things and then I think John's point in the discussion was until we see what happens to their actual performance through the Ibbotson analysis we don't know if they even care that they got the new. John Borne: Our advice assets group has reported no significant change. Terry Dennison: I don't expect them to go running off and going crazy with this I'm just curious to see did the vote pass but until we find out at this point it would be steady as we go. There is one action item we're going to proposed on page 14, you now are eligible to move to a slightly lower cost share class with Vanguard S&P 500 Index Fund to go to a share class that's 4 bps rather than 5 the Institutional share class they're re-designating it in October the Signal share class, the Admiral share class but you will be able to go to the Institutional share class this would be something that Great West would do for you.

The one that is somewhat significant is on page 15, Baron Asset this is the one that goes on and off. Baron is a Small Cap Fund and one of the issues with Small Cap fund is how big it is. Small Cap funds by their nature become problematic if the assets grow large and the issue is that small cap funds by their nature invest in smaller companies and if they become large and right now it's up to 5.7. The problem with that is either they're buying bigger stocks or buying more stocks neither one of those is particularly good because of one case it's no longer really small cap for example, the average market cap is now up to 4.4 billion which is getting mid capish and the idea behind small cap is these are companies that are in the 2 billion, maybe 2½ billion in the market cap. 4.4 is getting into the Mid Cap space which should be about 2½ to 10 and the theory in Small Cap is these are companies that are rapidly growing and are less recognized by the market less followed not as many analyst. So this is no longer quite the Small Cap fund or they're getting to be holding a lot more names so this is an issue and we'll take a look at the performance in a

bit, so I think we're going to recommend putting them on watch again partly for performance but now also for style. At this point I don't think we recommend search, although if you want us to do a search as a standby it would be fine with us just in case if we wanted to next quarter have the option. David O'Brien: Are Champlain and Baron in the same space. Terry Dennison: No, they're in different spaces. David O'Brien: I mean they're different styles, I accept that.

Terry Dennison: Yeah, but I think this one belongs on watch, so I would say put it on watch we can either do a search just to have something in our back pocket or not. The Thornburg we had asked because the new fund which is the Transamerica fund that's managed by Thompson Siegel and Walmsley does not have revenue sharing we had talked about imputing a revenue share and Great West upon your request did a performance calculation and you actually have excess revenue. And the question is you can replicate the revenue you gotten from Thornburg or you could actually just reduce the take and reduce the bite that the participants are paying, you have excess revenue. Now the reason that you might want to preserve the excess revenue and this is a judgment call on your behalf I don't know the mechanics and to some degree I'll defer to the Director because I don't know what you do with the excess revenue maybe you have a use for the excess revenue. David O'Brien: Can you give me more of a background, how does the excess revenue get created? Terry Dennison: You are collecting more expense ratio than Great West needs to operate the Fund. So, I don't know if there's aspect to the commercial deal you have with Great West that I do not totally understand, so can I defer to the Director. Paula Blas: Diane that's the 12B-1 excess revenue use for admin expenses. Diana Bernardo: Those money are used along with forfeitures to pay for administrative expenses. Terry Dennison: So, your choice is to just to keep the money the same chart that you had in Thornburg or reduce it. Paula Blas: We're going to have to look at how it affects the overall because just this fund is in excess. Terry Dennison: Yeah, that's the reason I didn't have enough information. Wilfred Leon Guerrero: How much money are we talking about? Paula Blas: We have a spreadsheet on it. Diana Bernardo: She reran this and just gave this to us. John Borne: I think if the impact was minimal it's because of the assets.

Terry Dennison: Thornburg provided revenue, Transamerica does not, so we were going to add a synthetic charge to replicate the revenue share and we were losing the question, is how much? We could get full amount that we were formerly getting from Thornburg but that actually is apparently in excessive need and the question is do we take the amount getting for even though it's an excessive need or do we just take what we need, because I don't fully understand the complete commercial deal you have with Great West. Fiduciary perspective you don't want to take more than you need, except the Fund has to fully support itself so there's the question.

Paula Blas: So, without it are we able to meet expenses, Diane. Diana Bernardo: So far we're able to, we still have monies in the forfeiture account but you know a few years down the line we may need to find additional source of funding. John Borne: Just to throw this out there, this is a discussion a lot of plans are having now there's a number of different rate needs for participant revenue sharing, but one thing you could do is go in a direction where you eliminate all revenue sharing for the funds and go to the lower share class and we can put on an explicit charge, that way everybody in the plan pays the exact same thing no matter what investment there in. David O'Brien: Yeah, you're not cross

subsidizing. Diana Bernardo: We used to have that. Paula Blas: Yeah, there used to be a participant charge, member charge across the board. Gerard Cruz: But, we had that participant charge in addition to the revenue sharing.

Terry Dennison: Along that same line though I don't think even if you could get away with charging nothing you should let people who invest in this fund pay nothing because then you have a free ride aspect of this. You might want to put something on this even though you don't need the money just to avoid the free riding aspect of it. But this decision needs to be made before we can implement this, so if Thornburg continues to do very poorly, then we want to make this decision so that we can get rid of Thornburg and get our Thompson Siegel and Walmsley funded. Wilfred Leon Guerrero: What do you think we should do? Terry Dennison: I think you should just from a Fiduciary perspective charge 10-15, some number so that you avoid the free riding situation and prolong the circumstance where you don't run out of money, but I don't think charging the full 35 basis points would necessarily be the right the thing to do either, the number you pick is kind of arbitrary. Diana Bernardo: Or you mean if we're going with these items and charging the participants. Terry Dennison: No, I would say just throwing in Thornburg the other is a much more a cosmic decision I would just pick a number for Thornburg like 15, 20, some number like that, not 35. Doris Flores-Brooks: Split the difference. Terry Dennison: I don't think zero is right even if you don't need the money because you have the free riding issue anybody who invests in the new fund is contributing nothing to the operation of the Fund. Gerard Cruz: So it's arbitrary. Terry Dennison: It is arbitrary. Gerard Cruz: Okay, so just half of 35. Terry Dennison: 15 or 20.

Paula Blas: Terry is not recommending 35 because it provides excess revenue so he's saying 15, it keeps it at a flat. Wilfred Leon Guerrero: So, what do you want Director? Paula Blas: I need to find out because 5% could be a big difference. John Borne: The other thing is I'm fairly certain they're not on here because they're not providing any revenue either as the Vanguard funds. So, would you want to implement the same practice for those funds, too? Gerard Cruz: Vanguard is the stable value. John Borne: Vanguard 500 Index and Vanguard Windsor it's close to 5 million in both of those funds.

Terry Dennison: You obviously have a better view but historically I think the people invested in the Index funds expect to get Index returns I think the Active funds I would draw a distinction between the Active funds, I think the Active funds should pay, the Index funds should get a free ride, I know it's inequitable. John Borne: The concern there is what if the whole plan decides to go Index then no one to pay the cost of our plans. Terry Dennison: I know but then we have to think about it again obviously it's committees choice but I would limit at this point to just the discussion of what to do with the Thornburg. David O'Brien: But we know what percents in the Index Fund, do you have that in your report? Paula Blas: It's about 5 million. John Borne: Excuse me that was only for the 457, there's another 25 million in the 401A. Sorry, it's about 25 million total, combined for both plans. David O'Brien: So about 8-10%. Wilfred Leon Guerrero: Okay, so before our official Investment Committee Meeting the Director and Controller are going to get together to come up with a number. Gerard Cruz: Between 19 and 21 make it easy for you. Wilfred Leon Guerrero: Anything else, Terry. Terry Dennison: No. Doris Flores-Brooks: How did they do? Terry Dennison: Everybody else did well, those are the comments.

David O'Brien: Given your comments are there other funds that you suggest play the ear issues that we would consider the gaps not what we have. Terry Dennison: Realistically we are seeing some interest at this point in diversified inflation funds but I think it's early, these are funds that invest in things like commodities, tips and stuff like but I think it's early for that, there will be plenty of time to think about diversified inflation funds. I think at some point we might start to see availability of funds that contain some kind of alternatives. David O'Brien: That was my question something that has MLP, something that has shorts.

Terry Dennison: The problem with that is daily valuation and daily transfer billing that's the reason that you don't see it. How do you value it by 4:00 in the afternoon everyday New York time? David O'Brien: And that's a requirement. Terry Dennison: That's why you don't see private equity hedge funds all the other good stuff that is a real true diversifier that's why all these funds have huge amount of equity risk premium because they're all made of stuff that's full of equity risk premium the only thing you can get that is priceable everyday.

Doris Flores-Brooks: Could I just ask a question. Going back to page 27, I see all these Red X's in the Black Rock where the vast majority of the portfolios are, what are we going to do? Because on page 12. Terry Dennison: If you look at the detail on page 30, we talked about this last time, the trouble with the X's is if you miss by a tiny amount you get the X. First of all, interestingly the Black Rock is really starting to improve and even where they missed, they're missing actually by tiny amounts. So, if you actually look at the numbers for example the 20/20 funds for 3 years they were 6.8, the index was 7.0 for 5 years, 13.0 the index was 13.5, they missed a little bit. Doris Flores-Brooks: Look at the Great West below, although it's a newer fund. Terry Dennison: Realistically, what we're seeing is they significantly narrowed the gap. They were much worse and actually they started to turn up if you look at the 1 quarter doesn't even improve but all of a sudden you can tell they did very poorly when the market was up a lot. Market has no longer up a lot and look at how all of them for three months are doing much better. So, they definitely were hurt when the market was doing great and when the market is not doing great significant improvement, but the reason we've not pull the trigger on these guys is and in fact if you look at them for one year they're pretty much positive across the board for one year and narrowed it pretty substantially for three years. Doris Flores-Brooks: Because that's where 80% of the money is. Terry Dennison: Yeah, because we basically defaulted everybody there, now we watch that one. Wilfred Leon Guerrero: Okay, let's take a break.

GWRS – Annual Review

John Borne: On what we did last year, we also hear some references through ERISA, we would like to follow that ERISA model as a best practice even though as a government plan you are not required to. Turn to tab 1, the first section is a little bit of a review about Great West because within ERISA it also requires that your plan provider make sure they have experience in offering these types of plans and also have references that check out with these types of plans as well.

So, on page 2 you'll see Great West financial strength and we're proud of the fact that we're really conservatively run and even in the great recession in 2008 Great West stood alone as the only North American insurance company to not received one down grade during that whole financial crisis, so we maintained a strong rating and we're going to keep our conservative approach. In terms of this year we've already been pretty busy, Great West has been in the news a couple of times this year. One was with our parent company Great West Life Co they actually owned Platinum investments. So, Platinum was a sister company of ours for a long time and we actually merged retirement business, so Great West has taken over all the Platinum business as well there technology of bringing into the fold and in about 2-3 weeks ago we announced the acquisition of all JP Morgan's retirement plan business as well. So, those 2 acquisitions are actually going to move us in to firms spot at number 2 overall retirement plan provider and in terms of government were number 1 by a long shot, we just picked up our 21st state this year as well with the state of West Virginia. A lot going on at Great West an exciting time to be there as well.

Page 4, you can see these are our government plans throughout the United States you can see this is an old map with 20 plans state relationship but each number within that state is how many government plans we have within that state as well. You see the two plans in Guam. Joe San Agustin: How come we're so close to California? John Borne: Guam is now located right off the coast.

Page 6, you see our mission statement it really holds our pre-core value partnership and providing commitment and that really goes to our approach to everything whether it's the administration of the plan or the services or products we offer to your participants we believe that these 3 things fit into everything we do as well.

Page 7, we'll show you your plans specifically as well as industry best practices and trends. So, we'll show you whether your plan if it has a yes you are already implementing that service, if it has no it will be something to consider, so you have most of our services only no on auto enrollment which we'll talk about it later, auto increase. Self directed brokerage unless you have participants begging you for it, I would suggest stay away from it. And then DC integration and this is something we can do, we've really developed a robust technology system where we can actually take feeds from defined benefit plans and incorporate that into our website so when our participants pull up their deferred comp stage they'll get an estimate of what they're going to have with their DB and then you can see their overall retirement picture. And with that information we can actually report back to you as a plan sponsor as long as we have salary information as well we can tell you as a percentage what population of your people are on track to replace at least 80% of their income in retirement. So, the more data you can give us, the more reporting we'll be able to do for you as well.

Page 8, the payroll data interchange that's basically what I was referencing. Online deferral changes that's something we can implement as well if you are interested. Page 9, this is a study we commissioned through Boston College Center for Retirement research and it's really focus on the public sector, you see a lot of news people attacking public pension saying they're too rich but with this study found out through Boston college is that in actuality most public sector participants only retire between 48-57% of their salary. So, all those things in the news about 80% most people don't achieve that,

according to this study in this chart 70% of the people replaced between 57% or lower of their income in retirement and only 30% actually got up to 72%. So, this tells us a couple of things through the studies that a lot of public sector workers come to the public sector later in life or people are not staying in the public sector their whole career so in case if you're not staying in 25-30 years you're not going to get that full DB benefit and that's really what the study concluded.

So, four things to consider to having a successful retirement plan, first you have market risk which we talked about today, as well. Inflation risk and the sequence of return risks and that's really the return they get pretty much closer to retirement age. So you have a down market right before they retire or right after they retire that really affects the participant's retirement readiness. And the longevity risks which was mentioned today as well and with those four risks in mind we developed our sweeter products which we call our RetireBright Solutions which is actually a trademark. And that has book end products that are geared toward the participant and as well as reports that are geared towards the plan sponsoring helping you cipher all that information. So, we have our Guaranteed Lifetime income product that's the Secured Foundation, our Great West Target Date funds, our Managed Account Advisory services as well as our Retirement Income Control Panel and that's the tool where we can integrate DB information for you as well. David O'Brien: So we have access to all these things. John Borne: Correct. Page 12, just talks about ERISA and qualified default investment alternatives so this is the QDIA section and in the past a lot of plans defaulted people in the stable value just because.

Respectfully Submitted:


Rena Cruz/Marilyn Aguon
Recording Secretary

Affirmed:


WILFRED P. LEON GUERRERO, Ed.D.
Investment Committee Chairman

