

HAWAII EMPLOYER-UNION HEALTH BENEFITS TRUST FUND
Minutes of the Investment Committee Meeting
November 12, 2013

TRUSTEES PRESENT

Ms. Celeste Nip, Vice Chairperson

Ms. Linda Currivan Musto

Ms. Loretta Fuddy

TRUSTEES ABSENT

Mr. Dean Hirata, Chairperson

ATTORNEY

Mr. Kyle Chang, Deputy Attorney General

EUTF STAFF

Ms. Sandra Yahiro, Acting Administrator

Ms. Donna Tonaki, Assistant Administrator (TA)

Ms. Debbie Pfeffer

Mr. Bert Nishihara

Mr. Neil Rue, PCA Consultant

Ms. Kay Ceserani, PCA Consultant

Mr. Colin Bebee, PCA Consultant

OTHERS PRESENT

Melissa Kunitake, Kaiser Permanente

I. Call to Order

The meeting of the Investment Committee was called to order at 1:03 p.m. by Vice Chairperson Celeste Nip in the Hawaii Employer-Union Health Benefits Trust Fund (EUTF) Conference Room, City Financial Tower, Honolulu, Hawaii, on Tuesday, November 12, 2013.

II. Approval of Minutes –August 13, 2013

MOTION was made for the Investment Committee to approve the minutes of August 13, 2013. (Fuddy/Currivan Musto) The motion passed unanimously. (Employer Trustees-1/Employee-Beneficiary Trustees-2)

III. Report

A. Pension Consulting Alliance (PCA)

1. September 30, 2013 Performance Report

Ms. Ceserani provided an update on the excess reserve fund that started at the end of September. The account was opened during the last week of September and an investment of \$35 million was made into the Vanguard Short Term Corporate Bond Index fund. A fee of \$87,500 was reduced from the initial investment amount to pay the Funds purchase fee of 25 basis point. At the end of October, the Fund's total assets were \$35.1 million; to date the portfolio has earned back the purchase fee plus a little extra. Going forward PCA will put together a report for EUTF.

Overview by Ms. Ceserani regarding the quarterly performance report

dated September 2013. The fund has out performed the policy benchmark over 3 different time periods: quarter, 1 year, and since inception (which is about 2 ¼ years). Over the longest period EUTF is outperforming the policy benchmark by 40 basis points. Over a 1 year period it returned 9% and outperformed the policy benchmark by 60 basis points. Over the recent quarter, the fund performed in-line with to the policy benchmark. The fund has outperformed the policy benchmark but underperformed the median public fund. All of the funds are performing within expectations across all reported periods. Four of EUTF's five funds matched or exceeded their benchmarks during the quarter. Since Inception all funds matched their respective benchmarks, except for the Vanguard FTSE All World ex US Index Fund, which lagged by (20) basis points.

Ms. Yahiro asked PCA to go over their outlook. Mr. Rue reported that bond yields have changed pretty dramatically over the last few months. The yield on a typical broadly diversified bond portfolio was about 2.5% which includes corporate bonds, mortgages, government bonds, and the yield is now at 3%. When interest rates rise, the value of the bond declines if you don't hold it to maturity. Everything else pretty much remained the same. There may be some volatility in the markets post Christmas

2. Strategic Allocation Review

Ms. Yahiro explained that the reason this item is on the agenda is because of the bill that has passed the Legislature requiring mandatorily prefunding of the OPEB liability. The Board had expressed concern that the bill is moving along so this is a good time to include PCA's recommendation on how we have our line-up right now.

Mr. Colin Bebee presented PCA's presentation regarding strategic allocation. The main premise behind the presentation and the structure that PCA is recommending is to begin to prepare the EUTF to become a larger scale institutional portfolio as the portfolio increases to the \$1 billion dollar mark. He explained the 4 new asset classes proposed for the EUTF: 1) Covered calls which is an equity-like asset class where there is a long equity position. You own equities and sell call options (i.e., insurance) on those equities. 2) Global credit (fixed income) are bonds from throughout the world – lending money to global companies, 3) Commodities which are probably the most advanced asset class. The main idea is it gives EUTF additional inflation protection and secure purchasing power over time by investing in a wide range of publicly traded commodities (e.g., agricultural materials, industrial metals, precious metals, and energy-related commodities). Commodities are a main input in regard to inflation. 4) Microcap/Private Equity Proxy which essentially is very, very small companies publicly listed stocks in the United States. Most microcap companies are generally \$400 million or less in market cap and generate a certain size and liquidity risk premium. Over time they tend to generate higher returns than the larger

companies. It's a riskier class but it will improve the overall expected return over time.

PCA looked at 20 portfolios and chose 3 portfolios to consider: Portfolios #9, #11, and #13. Portfolio #9 has the same return with lower risk, Portfolio #11 has the same risk but higher return, and Portfolio #13 matches the 7% assumed rate of return with higher risk and higher return. PCA recommends Portfolio #13 because it improves the expected return at the appropriate level of risk and closely matches the 7% assumed rate of return going forward. PCA recommends a 3 phase implementation timeline based on expected contributions from the state and counties and as the fund grows to the \$1 billion mark. Phase I when it hits the \$500 million mark and introduces the covered calls class. Phase 2 = \$750 million contribution amount and Phase 3 will be implemented when the fund hits \$1 billion. Dates of implementation would vary depending on when EUTF receives the contributions. Depending on the Board's preference PCA will do various levels of education sessions. PCA will participate in the December Board meeting via conference call.

MOTION to present PCA's recommendation of Portfolio #13 to the Board. (Fuddy/Currivan Musto). The motion passed unanimously. (Employer Trustee-1/Employer-Beneficiary Trustees-2)

IV. Future Agenda Items Discussion and Next Meeting Date
Tuesday, February 11, 2014 at 1:00 p.m.

V. ADJOURNMENT

MOTION was made for the Investment Committee to adjourn the meeting at 2:33 p.m. (Currivan Musto/Fuddy). The motion passed unanimously. (Employer Trustee-1/Employer-Beneficiary Trustees-2)

Respectfully submitted,

/s/

Dean Hirata, Chairperson

APPROVED on February 11, 2014.

DOCUMENTS DISTRIBUTED:

1. Hawaii Employer-Union Health Benefits Trust Fund Quarterly Report Executive Summary by PCA September 2013. (51 pages)
2. Strategic Allocation Review – 2013 from PCA dated November 2013 (56 pages)