ALASKA PERMANENT FUND CORPORATION
Board of Trustees Meeting
May 19-20, 2015

Location of Meeting:
Sheraton Anchorage Hotel
The Summit – 15th Floor
401 East 6th Avenue
Anchorage, AK 99501

SUMMARY MINUTES

Trustees Present:	William G. Moran, Chair Carl Brady, Vice Chair Larry Cash, Trustee Gary Dalton, Trustee Larry Hartig, Trustee Randall Hoffbeck, Trustee
Staff Present:	Jay Willoughby Valerie Mertz Chris Poag Laura Achée Robin Strader Rose Duran Valeria Martinez Jim Parise David Fallace Marcus Frampton Fawad Razzaque Steve Moseley Kathy Thatcher Brian Duncan
Advisors Present:	Jerrold Mitchell
Invited Participants and Others Present:	Gregory Allen, Callan Associates Inc. Steven Center, Callan Associates Inc. Loren Crawford, Petroleum Economist Tim Harper, Petroleum Economist John Tichotsky, SOA Chief Petroleum Economist Joe Beedle, Northrim Bank Daniel Summers, *Alaska Journal of Commerce* reporter

TUESDAY, MAY 19, 2015

CALL TO ORDER

CHAIR MORAN called the meeting to order at 8:30 a.m.

ROLL CALL

TRUSTEES MORAN, BRADY, CASH, DALTON, HARTIG and HOFFBECK were present to form a quorum.

APPROVAL OF AGENDA

There were no objections raised to the meeting agenda as presented.

APPROVAL OF MINUTES (February 25-26, 2015)

TRUSTEE DALTON moved and TRUSTEE HARTIG seconded the approval of the February minutes. The minutes were approved without objection.

SCHEDULED APPEARANCES AND PUBLIC PARTICIPATION

None were scheduled and no members of the public offered comment.

EXECUTIVE DIRECTOR'S REPORTS

In the absence of Executive Director MIKE BURNS, Chief Investment Officer JAY WILLOUGHBY offered brief commentary on his behalf. First quarter CY performance results were good; the Fund is up 2.75%. This may drop somewhat in the second quarter due to a dip in prices for Juno Therapeutics. In terms of cash flow, the Fund is tracking closely to a dividend similar to last year's, perhaps a bit higher.

MR. WILLOUGHBY went on to report that the Legislature is still in session, as they have not yet passed the FY16 state budget. While the Corporation's request for four new positions has been approved, the request for annual merit-based increases for staff was not approved. Yesterday, an email from the Governor was sent out to all State employees about potential layoffs slated for July 1st in the event that the Legislature does not pass a fully funded budget. This is a difficult time in the state of Alaska; hopefully the Permanent Fund will be allowed to continue to meet its capital calls.

RISK DASHBOARD

[A copy of the slides for this presentation is on file at the APFC offices.]

Director of Risk Management VALERIA MARTINEZ provided a summary of highlights from Fund performance over the last quarter. While many areas in asset allocation remained essentially unchanged, there were changes in special opportunities due to the funding of new strategies, and the overweight to company exposure continued. The Fund's risk exposures continued to be more conservative than the risk benchmark; most asset categories are less risky than the benchmark, although special opportunities and real assets are taking more risk than the benchmark.

The highest tracking error can be found in the corporate portfolio, due to an allocation to intermediate corporate bonds that is a mismatch with the index duration.

The Fund's total performance results were very positive for all periods, outperforming all performance and risk benchmarks. For the quarter, the Fund is up 2.75% vs. 2.16% for the risk benchmark and 1.26% for the performance benchmark.

Private equity is below target at 5.5%, although staff added $220M in new commitments this quarter which have not yet been called. Real assets (real estate, infrastructure and TIPS) remained essentially unchanged. A $300M commitment was added to Bridgewater under the absolute return line.

MS. MARTINEZ pointed out that the top three holdings in the Fund portfolio were special opportunities initiatives – Juno Therapeutics, American Homes 4 Rent and Riverstone.

MS. MARTINEZ noted that while there is no leverage at the Fund level, there is embedded leverage in some strategies in the portfolio. Gross exposure is calculated using the absolute value of long plus short positions, while net exposure is represented as the value of long minus short positions. Staff does not have complete visibility into leverage levels at portfolio companies of the underlying private equity and infrastructure managers. Therefore, these leverage levels are staff estimates based on guidance from managers.

There has been relatively little change in the Fund's asset allocation when comparing the current allocation to one year ago. Public equity exposure has been reduced, although there is now more exposure to private equity and corporate bonds.

All investments in the ECIO portfolios are liquid. While changes in the Goldman Sachs portfolio are relatively small, both AQR and Bridgewater, as risk parity managers, tend to have more equities and more corporates and to hold fewer government bonds.

MS. MARTINEZ stated that the Fund has had a good year in terms of performance. As of March 31, 2014, the Fund stood at $50.8B. Twelve months later, the Fund total is $54.3B.

Current allocation to the company exposure bucket is 59.2%, which is overweight the target of 55%. This portfolio did well for the quarter, outperforming the benchmark by 2.61% to 2.48%. While it underperformed for the year, it outperformed for the 3-year period.

The real assets allocation is 16.3%, under the target of 19%. While it underperformed for the one-year period, it outperformed for the quarter and the 3-year return. This bucket includes real estate, infrastructure and TIPS.

For special opportunities, the target is 20% and actual allocation stands at 18.5%. All time periods significantly outperformed the benchmark, due in large measure to the returns from Juno Therapeutics.

The one-year contribution to Fund return vs. the strategic risk benchmark was positive for all portfolios with a total return of 8.55%, as compared to the benchmark return of 6.82%. Much of the contribution to the outperformance came from special opportunities, company exposure and real assets, followed by cash and interest rates.

Board Investment Advisor JERROLD MITCHELL commented that these are excellent numbers; APFC is ahead in every category. He encouraged staff to keep up their good work.

CHAIR MORAN called a BREAK at 9:30 a.m. The meeting resumed at 9:58 a.m.

ASSET CLASS UPDATES

[A copy of the slides for these presentations is on file at the APFC offices.]

Public Equities Update:

Director of Public Equities FAWAD RAZZAQUE reviewed performance for the third quarter, noting that public equities returned 2.88%, outperforming the benchmark by 30 bps. However, for the FYTD, public equities are underperforming by just over 100 bps. One of the main reasons for this is the strategic allocation, which has an underweight to U.S. equities. Conversely, the underweight to U.S. equities contributed to the 3rd quarter outperformance, as did active managers. Quasi-passive managers, due to their value exposures, underperformed and detracted from the overall performance.

Third quarter performance was driven by overall market direction, headed up by non-U.S. equities, small cap stocks and growth sectors, and by the strategic allocation which underweighted U.S. equities. Growth stocks outperformed value sectors across the board, and small caps outperformed large caps in all markets. Country performance was led by Japan, Europe and emerging markets, while the U.S. lagged.

All of the global equity managers in the portfolio – AQR, Lazard and McKinley – substantially outperformed the benchmark, and each had an overweight to growth.

MR. RAZZAQUE outlined the three points to the Fund's allocation framework for public equities:

- Strategic – long term secular theme, more than 5 years;
- Tactical – short-to-intermediate term, one to two years; and
- Fund manager – conviction level, performance cycle

The strategic (long-term) allocation is based upon favorable trends in demographics and investment (population, wealth, consumerism and infrastructure); share of the world economy (long-term GDP growth potential); share of the world capital markets; and investability.

The tactical allocation (reversion to the mean) shows significant divergence in valuation, performance, fundamentals, and macroeconomics.

MR. RAZZAQUE noted that U.S. equities have delivered positive returns in each of the last six calendar years. While fundamentals have improved significantly, so has the valuation. By contrast, non-U.S. developed markets equities have delivered mixed returns and have underperformed U.S. equities over the past six years. Since 2010, emerging markets equities have delivered negative absolute returns on a cumulative basis, and profit margins have been declining.

Real Estate Update:

ROSE DURAN, Director of Real Estate Investments, provided an update on the current status of the commercial real estate markets. The U.S. economy has delivered steady GDP growth, with much progress to be seen in commercial markets. Vacancy rates have declined below long-term averages, although the office sector is trailing. NCREIF 4th quarter rolling NOI growth came in at a very impressive 6%. While the office sector is still in the recovery phase, all other property types are in the expansion phase, with multi-family nearly ready for the hyper-supply phase.

While long-term spreads have been at 280 bps, today spreads are at 350 bps. Real estate continues to be fairly priced, and staff would expect to see very little cap rate compression going forward.

MS. DURAN continued that the Permanent Fund has $200M of real estate in the market pipeline today, representing five properties. While a couple of the properties have not performed well, staff is also selling two solid performers, although they are not expected to outperform their benchmarks in the future. Given today’s real estate market, it makes sense to cycle out of these assets at this time.

There are two acquisitions in the pipeline. One is a very large European retail property, being acquired in a 50/50 partnership with Immotion, the firm which partnered with the APFC on two other international assets. The other acquisition would represent the Fund’s first medical office property, the Texas Medical Center in Houston, TX. Both acquisitions will probably close in the next fiscal year.

Wrapping up, MS. DURAN informed the Board that the Tysons project was now fully delivered. The Hotel opened on April 15, and the Vita Apartments are now 25% leased. She offered kudos to MIKE BURNS for his commitment, support and resolve in accomplishing all the elements of this huge development deal.

Fixed Income Update:

Director of Fixed Income Investments JIM PARISE stated that third quarter performance was mixed across all portfolios. One-year numbers were good, with outperformance noted in five of the seven portfolios internally managed.

The internal aggregate portfolio maintains a slight duration short, with an overweight to spread product (corporate bonds) and underweight to mortgage-backed securities.

The internal corporate bond portfolio is a $3B portfolio representing 200+ positions with 150+ issuers. It continues to perform very well, outperforming during all time periods, including +130 bps over the one-year timeframe.

The internal intermediate corporate bonds portfolio has not performed as well, underperforming by 50bps for the last quarter and YTD. CDX, the credit default swaps exchange, is used as a liquidity tool, with cash as the unofficial internal benchmark. This provides exposure to the corporate bond market in an extremely liquid format.

The internal mortgage-backed securities (MBS) portfolio, managed by CHRIS CUMMINS, has outperformed over all periods. He does an excellent job of security selection; it is very difficult to achieve consistent outperformance.

The TIPS portfolio, managed by MASHA SKURATOVSKAYA, has also done extremely well. She is excellent at finding places on the curve that are technically "cheap".

The CMBS portfolio has produced somewhat mixed results. It has always had – and probably always will have – an ultra high quality tilt. When those securities perform well, so does the portfolio. Staff can generally keep up with the index in bad times, and outperform in good times.

The internal global government bond portfolio has also done well over time. MS. SKURATOVSKAYA employs a great process that has worked very successfully.

A review of the Fund's external fixed income managers shows mixed results over different time periods.

Special Opportunities Update:

Director of Special Opportunities, DAVE FALLACE, reported that during the past quarter, APFC had invested in two new funds – Blackstone's Senfina Fund (a multi-strategy fund) and the Bridgewater Optimal Portfolio Fund (a hybrid of risk parity framework and the all-weather fund).

In follow-up to the last Board meeting, MR. FALLACE noted that staff planned to move the external CIO managers into the absolute return mandate, and those investment policy changes to the hedge fund program would be reviewed during tomorrow's session.

Regarding the Emerging Markets Multi-Asset portfolio, MR. FALLACE stated that the PIMCO - EMAF had outperformed, and the Capital Group – ETOP had underperformed their respective benchmarks for the quarter. Since inception, both managers have significantly underperformed their return objectives.

In the real return (ECIO) program, AQR underperformed for the quarter, but has done well overall in other time periods; Bridgewater significantly outperformed for the quarter (largely due to currency bets they made) and overall; and Goldman Sachs outperformed for the quarter, although it is the only manager who has underperformed since inception.

It is still early days yet for the private CIO program. It may take another two years to assess how well Carlyle and Apollo have performed.

MR. FALLACE wrapped up with a review of the true special opportunities portfolio, including Blackstone, which has acquired stakes in two hedge funds – Solus and Senate, and Riverstone, Oaktree EMOF, Dyal, and Arch VIII. Other ventures in the portfolio include American Homes 4 Rent II, and two life sciences ventures, Juno Therapeutics and Denali Therapeutics. Juno has proven to be a huge success story. Denali is a pharmaceutical company committed to discovering and developing breakthrough therapies for neurodegenerative diseases, such as Alzheimer's, Parkinson's and ALS.

Private Markets Update:

Director of Private Markets MARCUS FRAMPTON offered a snapshot of the quarterly update. At quarter-end, private equity stood at $2.9B, with a 2.7% return against the benchmark of 3.1%. Infrastructure had a 1.3% return, as compared to the benchmark of -2.8%. Currently, staff has committed $125M of the $400M FY15 target in infrastructure. This reflects the desire to not commit too much money in a hot market and to wait for the right opportunities. While the deal market today moves pretty fast, staff has put a thorough due diligence process in place in order to evaluate opportunities.

CHAIR MORAN called a BREAK for lunch at 12:04 p.m. The meeting resumed at 1:08 p.m.

Senior Portfolio Manager STEVE MOSELEY reminded the Trustees that historically, the Permanent Fund had outsourced all private equity decision-making through two gatekeepers. A year ago, staff made a change to this arrangement, increasing the level of oversight and control. Early results are promising – staff has negotiated better terms with some managers and gained access to previously inaccessible funds.

On the fund commitment front this year, staff will have committed $800M to 19 funds by fiscal year-end. Half of the dollars were committed by Pathway and half by staff.

On the co-investment side, MR. MOSELEY commented that staff had invested $151M in 13 companies YTD. By June 30, there will be another 8 deals, driven primarily by BlackRock's deal velocity.

Currently, the geography sector in private equity shows just 4% exposure to Asia, as compared to 78% U.S. In the industry sector, 36% resides in IT. The current private equity target allocation for the Fund stands at 6%.

Transitioning to the private credit portfolio review, MR. FRAMPTON noted that there was a $100M allocation to commit last year, which was the first time since 2011 that staff had made a new commitment to private credit. Today, private credit represents 2.2% of the Fund versus a target of 2%. In the last 12 months, the Fund has received back about

$2 for every dollar sent out in a capital call, so the portfolio is above target, but moving down.

PRIVATE INVESTMENTS FY 2016 ALLOCATION

[A copy of the slides for this presentation is on file at the APFC offices.]
MR. FRAMPTON began with a look back at the Infrastructure program, which was started in 2007 with commitments to two global managers – Citigroup (global core infrastructure) and GIP (core-plus). More recently, since 2013, staff has taken a slightly different approach with smaller, more targeted commitments. The ultimate goal of the program is to reach the 4% target.

Staff funded listed infrastructure for the first time in 2014, which has raised the program allocation to between 2.6% and 2.7%. So far in FY15, staff has committed $125M out of $400M, which could rise to $200M if a potential deal closes. For the past three years, the program has had a $400M target, and staff made the decision not to deploy that amount.

MR. FRAMPTON's expectation is that by committing $400M a year, the program would reach its 4% target by 2019. The biggest variable, which cannot be projected, is overall Fund growth. Staff recommends to the Board that they approve a $400M infrastructure target, with the flexibility for staff to look at funds and co-investments (to be capped at $200M), as well as the flexibility to allocate between $0 and $600M, depending on the opportunities available in the market.

Regarding the Private Equity commitment, MR. MOSELEY stated that his modeling was based on the understanding that a 6% allocation is the right target, and he has designed a path to achieve that. The 6% target still provides staff some flexibility around the bands that have been set over time with regards to the green/yellow/red zones.

Staff is requesting approval for $900M authorization for FY16 private equity, with a $200M band around it, divided between co-investments (up to 25% of total) and fund commitments, depending on comparative value.

Moving on to the Private Credit FY16 request, MR. FRAMPTON stated that the bulk of the program is contained in the $716M CCOPs commitment made in 2011, which is an evergreen vehicle. Overall today, private credit is 2.2% and CCOPs is 1.8%. There has not been much in terms of ongoing private credit activity, but it is beneficial to keep some "dry powder" available for future commitments. Staff would recommend up to $100M allocation to private credit if opportunities arise.

> **MOTION**: TRUSTEE HOFFBECK moved that the Board give staff the authority to commit up to $100M to Private Credit for FYF16, subject to the following: staff may under-commit depending on the quality of opportunities reviewed and the results of due diligence; and staff may ultimately elect to commit $0 in FY16 in order to preserve "dry powder".

TRUSTEE DALTON seconded the motion. Following a roll call vote, the MOTION was UNANIMOUSLY APPROVED.

MR. WILLOUGHBY introduced the Private Equity suggested recommendation.

MOTION: TRUSTEE DALTON moved that the Board approve a $900M target allocation to Private Equity for FY16, with the allocation to be divided between co-investments (up to 25% of the total) and fund commitments, depending on comparative value; and the flexibility to increase the allocation to $1.1B if market opportunities are compelling or to decrease to $700M if opportunities are scarce.

TRUSTEE CASH seconded the motion. Following a roll call vote, the MOTION was UNANIMOUSLY APPROVED.

MR. WILLOUGHBY then reviewed the suggested recommendation for the Infrastructure program.

MOTION: TRUSTEE BRADY moved that the Board approve a $400M allocation to infrastructure for FY16, which may be split between co-investments and infrastructure funds, depending on opportunities presented, and to provide staff with additional flexibility wherein the allocation may be increased to $600M or decreased to as low as $0 depending on the market opportunities that may arise.

TRUSTEE HARTIG seconded the motion. Following a roll call vote, the MOTION was UNANIMOUSLY APPROVED.

CHAIR MORAN called a brief BREAK at 2:10 p.m. The meeting resumed at 2:20 p.m.

APFC BUDGET

[A copy of the slides for this presentation is on file at the APFC offices.]

FY15 Budget Projections

LAURA ACHEE, Director of Communications and Administration, and KATHY THATCHER, Administrative Officer, reviewed highlights of the FY15 year-end budget projections. Staff is required, by resolution, to review the present year budget as well as the budget for the upcoming fiscal year with the Board at its spring meeting.

MS. THATCHER reminded the Board that there are two appropriations to the APFC budget – one for Corporate Operations and one for Manager and Custody Fees. The Corporate Operations budget had a $12.2M appropriation for FY15, and staff is projecting expenditures of $11.9M by year end, leaving a surplus of approximately $268K. There are five line items under this appropriation: Personal Services, Travel, Contractual Services, Commodities and Equipment.

The Personal Services budget for FY15 was $7.3M, which is a $503K higher expected expenditure than in FY14. This can be accounted for by the 5% geographic differential and 1% COLA applied to base salaries on July 1, 2014. There was also much lower position vacancy this year in comparison to FY14. Staff is projecting a shortfall of $221K in Personal Services by year end.

Under the Travel budget, this year's authorization was $430K, of which $260K will be expended, leaving an expected surplus authorization of $170K. There were 11% fewer trips taken by staff this year, with no international travel booked.

MS. THATCHER continued that staff expects to expend about 93% of its $4.3M authorization in Contractual Services, ending the year with $307K surplus. Some of this surplus would be utilized in reconfiguring current APFC office space to accommodate the addition of four new employees (three in investments and one in finance) authorized in the FY16 budget. Cost estimate for this project is approximately $100K, not including furniture and equipment for the new personnel.

The Training/Education budget has been $54K overspent, primarily because of the corporate membership to the International Forum of Sovereign Wealth Funds (IFSWF). The Commodities budget will likely end the year with a $32K surplus, while the Equipment line will show a $20K shortfall, due to expenditures for a server room A/C unit, replacement of firewalls and a new audio system for Board of Trustees meetings.

Overall, MS. THATCHER is projecting a total expenditure of $12M in the FY15 Operations budget, with a surplus authorization of $268K. There will likely be shortfalls in Personal Services and Equipment, which can be covered by funding found in Travel, Contractual Services and Commodities.

> **MOTION:** TRUSTEE DALTON moved that the Trustees approve the transfer of funds into the Personal Services line to cover the estimated $221K shortfall in FY15 – specifically, to transfer $100K from Travel and the balance needed (estimated at $121K) from Contractual Services.
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> TRUSTEE HARTIG seconded the motion. Following a roll call vote, the MOTION was UNANIMOUSLY APPROVED.
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> **MOTION:** TRUSTEE CASH moved that the Trustees approve the transfer of the necessary amount (estimated at $20K) from the Commodities line to cover the projected FY15 shortfall in the Equipment line.
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> TRUSTEE DALTON seconded the motion. Following a roll call vote, the MOTION was UNANIMOUSLY APPROVED.

MS. THATCHER moved into a review of the appropriation for the Manager and Custody Fees budget. The FY15 authorization was for $138.6M; staff projects total expenditure of $94.2 M, ending the year with a surplus authorization of $44.4M. Since this funding comes from corporate receipts, any unused funding simply stays in the Permanent Fund.

The third-party fiduciary fees line has a small increase over FY14, due to increased legal work engendered by expansion of investments in alternative assets. In FY15, the Corporation increased the budget allocation in this category significantly to allow flexibility in moving forward and to grow alternative asset types.

MS. THATCHER summarized that, since the Manager and Custody Fees budget will end the year with a surplus authorization, no action is required by the Board.

FY16 Budget Approval
MS. ACHEE stated that this was the first time she had presented a budget to the Board in which the Legislature had not yet wrapped up their discussions on funding for FY16. Although the APFC is fully funded for FY16 under the Governor's suggested budget, the fact remains that the budget is still in play and the Legislature is still meeting in special session. That said, she is quite certain that the Corporation's budget for FY16 will be approved. The only item in the budget that the Trustees had approved last fall that raised concerns was the issue of annual merit increases for staff. Everything else in the budget was approved by Governor Parnell and Governor Walker, as well as by the Legislature.

With regard to merit increases, while the Legislature understands that the Permanent Fund does not impact the General Fund or the budget deficit situation, the legislators felt it was only fair to hold the APFC to the same standard as other state agencies, which have had to take budget cuts and proposed staff layoffs.

The Corporation has received approval to add the four new requested positions: a real estate investment officer to work with MS. DURAN, a private assets analyst for MR. MOSELEY and MR. FRAMPTON, a special opportunities investment officer to work with MR. FALLACE, and another accountant for Finance.

In addition, MS. ACHEE mentioned that the Legislature approved the transfer of $2.5M in investment management costs from the Operations budget to the Investment Management Fees budget, and had approved small increments for IT, manager searches, financial network software, and investment-related legal fees.

Summarizing the FY16 budget, MS. ACHEE stated that staff expects approval for a Corporate Operations budget of $10.7M, with Personal Services pegged at $8M. Staff also projects $151M for Investment Management Fees, including $138M for Investment Manager Fees, and Custody Fees of $1.3M to the Bank of New York Mellon.

MS. ACHEE reiterated that she fully expected that the Legislature would ultimately approve the FY16 budget as presented to the Board, but pledged that if there were moderate-to-significant differences in the final passed version of the budget, that she would work with the Board Chair to call a special session so that the Trustees could vote again on the final approved budget – or present the final approved budget to the Board at its September annual meeting – whichever was most appropriate.

> **MOTION**: TRUSTEE DALTON moved that the Board authorize the Executive Director to expend the draft legislative authorizations as shown in the FY16 budget presentation. If the final budget negotiations produce a different outcome, the Board authorizes the Executive Director to expend the legislative authorizations contained in the bill signed by the Governor.
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> *(MS. ACHEE clarified that the second line of the suggested motion language shown above anticipates an outcome in which the merit-based increases or small COLA increases for staff are added back into the budget; in other words, a de minimis change to the budget).*
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> TRUSTEE HARTIG seconded the motion. Following a roll call vote, the MOTION was UNANIMOUSLY APPROVED.

BOARD MEETING RECESS FOR THE DAY

CHAIR MORAN recessed the meeting for the day at 2:50 p.m.

WEDNESDAY, MAY 20, 2015

CHAIR MORAN reconvened the meeting at 9:30 a.m.

APFC INVESTMENT POLICY CHANGES

[A copy of the slides for this presentation is on file at the APFC offices.]

MR. WILLOUGHBY stated that the purpose of this first discussion was to recommend two changes to the APFC Investment Policy, both designed to inject flexibility and reduce program costs.

Infrastructure and Other Real Assets Guidelines

MR. WILLOUGHBY said that the current Policy limits the infrastructure program to funds and core assets, which would eliminate such long-lived assets as timber and farmland from consideration. What staff is hoping to do is broaden the scope of the program to open it up to other real assets.

General Counsel CHRIS POAG noted that the first change was to broaden the infrastructure mandate to include infrastructure "and other real assets" – timberlands, agricultural farmlands, leasable hard assets and any other tangible or intangible assets that possess similar portfolio characteristics as those envisioned for infrastructure. The idea is to make the definition more open-ended in order to allow flexibility in future searches.

The other, more substantive change is that when the program was first envisioned, it was assumed that infrastructure would generate an annual, high level of income. However, that has not proven to be the case, so staff is removing that language from the Policy.

MR. FRAMPTON continued that there are thirty underlying assets in the private infrastructure portfolio, with an NAV of approximately $1B. These underlying assets are income-producing assets, such as ports, airports, toll roads and power generation facilities. The managers are primarily financing these with debt at the project level, and the cash flow from the majority of these assets is used to de-lever. As a result, the Fund does not receive a quarterly coupon of 4-5% yield on the NAV, and therefore, MR. FRAMPTON stated that he was not comfortable having the income language stated as a part of the Policy.

MR. FRAMPTON went on to say that staff was not prepared at this time to make a commitment to timber; he wanted to illustrate for the Board an example of a "real asset" that was long-term in nature, has a history of inflation-linked returns and follows a different cycle than infrastructure. The goal is to broaden the definition of "other real assets" in the Policy in order to provide more flexibility to staff.

MR. FRAMPTON also pointed out that staff was not planning to change the benchmark, (the FTSE Infrastructure Index), as it creates the accountability that will hold staff to meeting the program objectives as they are currently expressed.

Absolute Return Mandate Guidelines

MR. WILLOUGHBY noted that this next suggested change concerns the merger of the ECIO portfolio (real return mandate) with the absolute return portfolio. The three managers currently in the ECIO program – AQR, Bridgewater and Goldman Sachs – would merge into the hedge fund program, increasing the hedge fund allocation to 10% of the overall Fund. Goldman Sachs would become an internally managed allocation to the hedge fund program, which would help to reduce costs and lower the overall expense ratio. The program is currently over-diversified, and the Fund is paying full fees to all of these managers, since the allocation to any single underlying manager is not a large one.

MR. WILLOUGHBY continued that there would be no real changes to the structure of the program to start with; everything will continue to function as it does currently.

MR. POAG stated that this particular mandate is structured for fund-of-funds, so the largest change being contemplated is to broaden the policy so it can accommodate direct hedge fund holding as well as a fund-of-fund (FOF) manager holding. Approving this change would allow staff to have both direct and FOF holdings, and to allow different reporting requirements, since each one reports slightly differently.

The second change is to fine-tune the investment objective, with the goal of achieving a single rate of return, the same as the overall Fund's rate of return objective – 5% over LIBOR. The goal is essentially to mimic the returns of the Fund, but with less correlation and less volatility. The correlation measurement will be to the Fund; in other words, staff will report to the Board the correlation of this asset class to the overall Fund.

The third change is to the diversification of the asset class; through the evolutionary process, the mandate has arguably become over-diversified, with approximately 319 underlying hedge fund holdings in about 120 core funds. What staff has found is that when a larger and more concentrated investment is made, there are different and better economics at work – such as reduced fees, revenue sharing, etc.

MR. POAG stated that the Policy would still mandate the use of a limited liability entity. The investment objective would change to a single rate of return of 5% over LIBOR and a single volatility measure of 12%, and would add the correlation measurement, which doesn't currently exist.

The new Policy would permit the limited liability entity to be structured in four different ways: a portfolio of directly invested hedge fund investments; a fund-of-one directly held by the Fund; the traditional FOF structure, externally managed; and limited liability interests in individual hedge funds.

Very little change is contemplated in terms of risk management. Externally managed funds would eliminate over-diversification by holding a maximum of 10 funds (as opposed to the current policy, which requires holding a minimum of 20 funds).

MR. POAG added that there is no change in the Policy with regard to leverage risk or liquidity. There will be some modification to counterparty risk, wherein managers who plan to engage in derivative transactions will provide staff with a risk control plan to mitigate those risks.

MR. WILLOUGHBY commented that there will be no change to the broader reporting benchmarks, since the funds will all remain within the special opportunities risk bucket. MR. ALLEN noted that from Callan's standpoint, the reporting structure will be different.

CHAIR MORAN inquired as to whether staff could estimate how much less the Fund would pay out in fees and administrative costs under this scenario. MR. WILLOUGHBY replied that at first, the current fee structure would be unlikely to change. Over the course of time, the fees could change substantially – as much as between 10-20% cost savings on what the underlying managers are making.

CHAIR MORAN asked what impact these changes might have on Finance staff. MS. MERTZ responded that currently there are two functions in Finance that relate to all asset classes – accounting for the assets and tracking compliance. Accounting for absolute return is relatively straightforward. The time-consuming factor is compliance, which is driven by current regulations, the Investment Policy, and the individual Investment Management Agreements. With regard to the current policy and the FOFs held now, two of the funds are not problematic, while the third requires a lot of due diligence due to the number of underlying funds. Concerning the changes being contemplated, the biggest impact on Finance would be caused by the sheer number of underlying funds – not whether they are internally or externally managed.

MOTION: TRUSTEE DALTON moved that the Board approve the amendment of the Investment Policy statement to broaden the Infrastructure mandate to include infrastructure "and other real assets".

TRUSTEE BRADY seconded the motion.

Following a roll call vote, the MOTION was UNANIMOUSLY APPROVED.

Before moving onto the absolute return vote, MR. POAG recommended that the Trustees permit staff to remain in noncompliance with the new mandate in order to allow time for prudent adjustments as underlying funds are winnowed down to a maximum of ten (from the current minimum of twenty). This keeps the pressure on staff to make the changes as market timing allows. Regular reporting to the Board on progress made by staff would also be required.

TRUSTEE HOFFBECK agreed that this would be a good plan; he does not want to see artificial deadlines put in place.

MOTION: TRUSTEE DALTON moved the following changes to the Absolute Return and Real Return mandate:

- Dismantle the Real Return program and transfer these assets into the Absolute Return program;
- Modernize those components of the Absolute Return policy that have evolved;
- Enhance the efficiency and level of alpha generated by the Absolute Return program by eliminating the over-diversification, and authorizing the Fund to make a smaller number of more concentrated Absolute Return investments.

TRUSTEE BRADY seconded the motion.

Following a roll call vote, the MOTION was UNANIMOUSLY APPROVED.

CHAIR MORAN called a break at 10:40 a.m. The meeting resumed at 10:50 a.m.

PERFORMANCE MEASUREMENT – Callan Associates Inc.

[A copy of the slides for this presentation is on file at the APFC offices.]

MR. ALLEN opened by stating that while staff does a great job of discussing the various asset classes and risk dashboard, Callan's role is to put the Permanent Fund's performance in context with how other large funds are performing – and this is a good quarter to talk about relative performance.

Taking a look at the capital markets, MR. CENTER observed that last quarter was a good one for the equity markets, especially for non-U.S. equities and small caps. It has been a bull market for the equity space.

Emerging markets were up 2.3%, while U.S. markets were up just under 2%. The U.S. market continues to be the strongest performer over the last 5 years; the Russell 3000 is up just under 15%.

In the private equity space, it was a very strong quarter for fund closures, with 147 new funds raising about $56B in new assets, outpacing the first quarter of last year. However, fewer new partnerships were formed. Larger dollar value and a smaller number of partnerships points to the return of institutional investors to investing in larger deals. Buyouts continued to be the biggest fundraiser within the new issue space. Private equity performance, as compared to the public space, has lagged; however, in looking at long-term performance over 10+ years, private equity continues to outperform the public equity space.

Moving on to a discussion of the Total Fund asset allocation and performance, MR. CENTER stated that the Fund is currently invested 40% in public equities, 23% in fixed income and 37% in alternatives, which covers real estate, private equity, infrastructure, absolute return, true special opportunities, distressed debt and mezzanine debt.

Last quarter, the Fund returned 2.8%, outpacing all of its benchmarks, and this held true over the last twelve months as well.

The APFC public equity allocation is divided 42% in U.S. equities and 58% in non-U.S. equities. Performance in the last quarter was quite strong at 2.9%, versus 2.6% for the benchmark.

Regarding the fixed income allocation, MR. CENTER noted that 85% of the portfolio is managed internally by APFC staff, including allocations to TIPS and non-U.S. bonds. The portfolio has performed very well over time relative to the benchmark. All of the internally managed portfolios have been performing in line or slightly ahead of their benchmarks during near-term periods.

Discussing the alternatives allocation, MR. CENTER commented that 63% of the real estate portfolio is invested in direct real estate, with 5% invested internationally through CBRE Europe and LaSalle UK. Another 19% is invested in REITs, and includes AEW Global and American Homes 4 Rent. Near-term performance has slightly lagged the benchmark due to the non-U.S. allocation, but ranks very favorably over the long term.

The absolute return portfolio has beaten its LIBOR+4% benchmark over the last quarter, two-, three-, and five-year periods, and ranks above median for all time periods of five years and beyond. It compares well to its peer group and benchmarks over time.

The private equity structure is well-diversified by strategy and geography; there are no concerns at this point.

TRUSTEE BRADY asked for an update on the status of American Homes 4Rent, I and II. MR. ALLEN replied that AH4R I is now publicly traded, and is considered a somewhat weak stock. He said that he did not know the long-term plan for AH4R I, but now that it is public, the stock is subject to the vagaries of the public markets.

Regarding AH4R II, MR. WILLOUGHBY noted that it is the follow-on program to the original American Homes 4 Rent deal, designed to buy homes valued at $500K or higher. APFC agreed to fund 80% of $200M; AH4R agreed to fund the other 20%. To date, APFC has invested about $80M. The opportunity is not developing as fast as originally anticipated, which is why a decision was made to invest in homes for as little as $250K on half of this portfolio. The likely disposition strategy is that the homes will be sold one at a time, after 2-3 years. While the acquisitions have been attractive, it has been slow going. Overall, MR. WILLOUGHBY believes it will be a good investment for the Fund.

In his closing remarks, MR. CENTER summarized that Permanent Fund performance had been quite strong over the last quarter and the last 12 months. Longer-term performance, while it may lag some of its peers, is in line with the overall investment strategy for the Fund over time.

Callan is currently working on some projects with Fund staff, including evaluating a public equity strategy for MR. RAZZAQUE, working with MR. FRAMPTON on identifying some potential timber investments, and streamlining Callan's performance reporting process with the Accounting staff.

MR. WILLOUGHBY asked whether Callan could offer any suggestions to improve reporting or if they saw any significant areas of exposure in the Fund.

MR. ALLEN responded that the board asset class target is a much better fit with their reporting, and Callan would begin to use it as a benchmark and frame of reference starting with the September board meeting.

In terms of exposure risk and volatility, MR. ALLEN pointed out the large allocation to emerging markets, and the significant exposure in the Fund to two individual stocks, Juno Therapeutics and AH4R. As a biotech stock, Juno is pretty volatile, and has the potential to singlehandedly affect performance relative to the benchmark.

MR. WILLOUGHBY followed up by asking how important the day-to-day volatility of Juno Therapeutics was over any given time period, when weighed against the longer-term expectation of Juno being a better prospect/investment?

MR. ALLEN commented that some public funds would be concerned about it from a headline risk perspective. Callan's clients tend to be more on the risk-adverse side and less likely to take big positions in individual stocks.

MR. WILLOUGHBY noted, for the record, that staff has retained Crestline to continue providing counsel on Juno, and CS Capital provides counsel on AH4R.

CHAIR MORAN called a break for lunch at 11:40 a.m. The meeting resumed at 12:40 p.m.

INVESTMENT ADVISOR COMMENTS

MR. MITCHELL commented that he often came across articles and other writings that could be of interest to the Trustees, and offered the following "food for thought" for their consideration.

First were a couple of book reviews he had seen recently in the *Wall Street Journal* and *The Economist*, regarding a book entitled "Misbehaving: The Making of Behavioral Economics", authored by Richard Thaler. His argument is that much of macro-economic theory (such as money supply, etc.) and much of finance theory (such as the efficient market hypothesis) are wrong, because they are based on the idea that human behavior is rational, and that humans always make the best and most logical decisions. Thaler's research shows that this is not true: people do not always make the best choices, because they are biased; they are human. This rationality, which is assumed by economic theorists and by those who devise complex investment models, is not true in the real world. While this does not mean the Permanent Fund should change the way it operates, MR. MITCHELL suggested that when listening to a manager or consultant explain how rational their investment process is, just consider the thought: what if we are not rational?

Secondly, MR. MITCHELL mentioned an article he read in the May 18th issue of *New Yorker Magazine,* which reviewed the reasons for the flash crash in the 2010 stock market. Recently, the FBI has accused a 36-year-old private investor, living in London, of causing the flash crash. The article pointed out that on a day-to-day basis, public equity market prices are determined more by computer algorithms than by human judgment. In a way, the stock market has become "self-reflexive", meaning that 60-70% of the changes in stock prices are driven not by fundamentals or any new information, but rather from self-generated activity – one computer trading against another computer. In other words, the markets are moving themselves – we are not moving the markets.

EXECUTIVE SESSION

MOTION: TRUSTEE BRADY moved, per Alaska Statute 44.62.310(c)(1), pertaining to the open meetings act, that the Board of Trustees convene in executive session to discuss a financial matter. This topic falls under subsection (1) of that statute, as "matters, the immediate knowledge of which would clearly have an adverse effect upon the finances of the public entity."

In addition, per Alaska Statute 44.62.310(c)(1), pertaining to the open meetings act, TRUSTEE BRADY moved that the Board of Trustees convene in executive session to discuss a personnel matter. This topic falls under subsection (2) of that statute, as "subjects that tend to prejudice the reputation and character of any person, provided that person may request a public discussion."

TRUSTEE HOFFBECK seconded the motion. Following a roll call vote, the MOTION was UNANIMOUSLY APPROVED.

Executive Session convened at 12:51 pm and ended at 1:45 p.m.

CHAIR MORAN announced that while in Executive Session, the Board considered only the matters mentioned in the motion and took no action.

TRUSTEE COMMENTS / FUTURE AGENDA ITEMS / OTHER MATTERS

TRUSTEE HOFFBECK stated that he would bring a letter to the Board of Trustees with a request to put together a workshop on the idea of using leverage as a method of generating additional income for the Fund, for the purposes of general government operations. CHAIR MORAN responded that once he received the letter, he would work with the staff to determine how much time would be needed to accumulate enough information to make a workshop worthwhile and then schedule accordingly.

CHAIR MORAN also commented that he hoped the good news in the Fund continues, and that he was very impressed with the progress being made in the portfolio. He commended MR. WILLOUGHBY and his staff for their outstanding work.

ADJOURNMENT

There being no further business, CHAIR MORAN adjourned the meeting at 1:50 p.m.

APPROVAL OF MINUTES

/s/William G. Moran, Chair

September 30, 2015