Oregon Investment Council

July 28, 2010 - 9:00 AM

PERS Headquarters
11410 S.W. 68th Parkway
Tigard, OR 97223

Oregon Investment Council

Harry Demorest
Chair

Office of The State Treasurer

Ted Wheeler
State Treasurer

Ronald Schmitz
Chief Investment Officer

OREGON INVESTMENT COUNCIL

2010 Meeting Schedule

Meetings Begin at 9:00 am
at
PERS Headquarters Building
11410 SW 68th Parkway
Tigard, OR 97223

January 27, 2010

February 24, 2010

April 28, 2010

May 26, 2010

July 28, 2010

September 29, 2010

October 27, 2010

December 1, 2010

OREGON INVESTMENT COUNCIL

Agenda

July 28, 2010
9:00 AM

PERS Headquarters
11410 S.W. 68th Parkway
Tigard, Oregon

Time	A. Action Items	Presenter	Tab
9:00-9:05	**1. Review & Approval of Minutes** May 26, 2010 Regular Meeting	**Ron Schmitz** *Chief Investment Officer*	**1**
9:05-9:50	**2. Blackstone Capital Partners LP, VI**	**Jay Fewel** *Senior Investment Officer* **Tony James** *President & COO* **Ken Whitney** *Senior Managing Director*	**2**
9:50-10:45	**3. Annual OPERF Real Estate Review**	**Brad Child** *Senior Investment Officer* **Nori Lietz** *Partners Group*	**3**
10:45-11:00	**----------BREAK----------**		
11:00-11:45	**4. Angelo Gordon Pan Asia Real Estate Fund II** *OPERF Real Estate*	**Brad Child** **Nori Lietz** **Keith Barket** *Senior Managing Director* **Aliana Spungen** *Managing Director*	**4**
11:45-11:55	**5. Higher Education Pooled Endowment Fund** *Asset Allocation Recommendation*	**Mike Mueller** *Deputy Chief Investment Officer* ***John Meier*** *Strategic Investment Solutions*	**5**
11:55-12:00	**6. OIC Policy Updates**	**Mike Mueller**	**6**

Harry Demorest Chair	Keith Larson Vice-Chair	Ted Wheeler State Treasurer	Katy Durant Member	Richard Solomon Member	Paul Cleary PERS Director (Ex-officio)

B. Information Items

12:00-12:20	**7. Annual Proxy Voting Update** *Glass Lewis & Co.*	**Jennifer Peet** *Contracts & Corporate Governance Officer* **Bob McCormick** *Chief Policy Officer* **Jeff Thompson** *Director of Business Development*	**7**
12:20-12:35	**8. Annual Audit Update** *OST Internal Audit*	**Andrea Belz** *Chief Audit Executive*	**8**
12:35-12:40	**9. Asset Allocations & NAV Updates** a. Oregon Public Employees Retirement Fund b. SAIF Corporation c. Common School Fund d. HIED Pooled Endowment Fund	**Ron Schmitz**	**9**
	10. Calendar—Future Agenda Items	**Ron Schmitz**	**10**
	11. Other Items	**Council** **Staff** **Consultants**	

C. Public Comment Invited

15 Minutes

Harry Demorest, Chair
Keith Larson, Vice-Chair
Ted Wheeler, State Treasurer
Katy Durant, Member
Richard Solomon, Member
Paul Cleary, PERS Director (Ex-officio)

TAB 1 – REVIEW & APPROVAL OF MINUTES

May 26, 2010 Regular Meeting

RONALD D. SCHMITZ
CHIEF INVESTMENT OFFICER
INVESTMENT DIVISION

PHONE 503-378-4111
FAX 503-378-6772

STATE OF OREGON
OFFICE OF THE STATE TREASURER
350 WINTER STREET NE, SUITE 100
SALEM, OREGON 97301-3896

OREGON INVESTMENT COUNCIL
MAY 26, 2010
MEETING MINUTES

Members Present:	Paul Cleary, Harry Demorest, Katy Durant, Keith Larson, Dick Solomon
Member Absent:	Treasurer Ted Wheeler
Guest:	James Dalton, PERS Board Chair
Staff Present:	Andrea Belz, Darren Bond, Brad Child, Jay Fewel, Sam Green, Norma Harvey, John Hershey, Brooks Hogle, Julie Jackson, Robert Johnson, Jeff Keto, Perrin Lim, Tom Lofton, Ben Mahon, Mike Mueller, Kevin Nordhill, Jen Peet, Jo Recht, Tom Rinehart, Ron Schmitz, James Sinks
Consultants Present:	Allan Emkin and Mike Moy (PCA), Mike Beasley, Lou Kingsland, and John Meier (SIS), David Fann and Sundeep Rana (PCG)
Legal Counsel Present:	Dee Carlson, Oregon Department of Justice Fred Boss, Oregon Department of Justice

The OIC meeting was called to order at 9:00 am by Harry Demorest, Chair.

Chair Harry Demorest read a statement (attached) in honor of the legacy of past Treasurer Ben Westlund and the many accomplishments he made for Oregonians.

I. 9:00 a.m.: Review and Approval of Minutes

MOTION: Mr. Demorest brought approval of the April 28, 2010 OIC minutes to the table. Mr. Solomon moved to approve the minutes. The motion was seconded by Ms. Durant and passed by a vote of 4/0 (Treasurer Wheeler was not present for the vote).

II. 9:05 a.m.: Litigation Update

Fred Boss, Chief Counsel, Civil Enforcement from the Oregon Department of Justice provided an update on current litigation.

III. 9:10 a.m.: Securities Lending Cash Management

Mike Mueller, Deputy Chief Investment Officer introduced Steve Meier, Executive Vice President and Global Cash CIO with State Street Bank and Johnson Shum, Vice President with State Street Global Advisors. Mr. Meier and Mr. Shum made a presentation on the cash collateral reinvestment pools managed by State Street Global Advisors, for the securities lending programs.

During the February 2010 annual review of the securities lending program with State Street Bank, the OIC requested a discussion dedicated to the reinvestment of the cash collateral. Mr. Meier discussed the firm's credit research capabilities and investment philosophy, as it relates to cash management.

There was a brief question and answer period following the presentation.

ACTION: The Council asked staff to look into a separately managed account and if/how this could be implemented. Council supports this and Mr. Mueller was directed to look into how this can be achieved and to provide an update at a subsequent meeting.

IV. 10:00 a.m.: Policy Implementation Overlay

Mr. Mueller introduced Greg Nordquist, Senior Portfolio Manager and Sylvia Perek, Portfolio Manager with Russell Investments. Mr. Nordquist provided the Council with an update on the OPERF Policy Implementation Overlay program provided by Russell Securities. This presentation was informational only.

In September 2005, the OIC retained Russell Securities to implement a more thoughtful overlay program that does more than blindly "equitize" excess manager cash. Through this daily effort, Russell monitors excess manager cash, cash held by the fund to meet benefit payments, and the current allocation of the fund to the OIC established strategic asset allocation targets. They then trade equity and fixed income futures to better align the fund's overall asset allocation. The OIC receives a monthly update on the overlay exposures in the asset allocation portion of the monthly agenda materials.

As of March month end, OPERF has $24 million in fixed income contracts and $1.084 billion in global equity contracts, for a total notional exposure of $1.1 billion.

Last February, Russell Securities provided the OIC a presentation on the mechanics of the program, and the performance to date. Today's presentation was an update on the program.

There was a brief question and answer session after the presentation.

V. 10:35 a.m.: OPERF Asset Liability Study (Joint Meeting with OPERS Board)

Mike Beasley, John Meier, and Lou Kingsland from Strategic Investment Solutions (SIS) gave an update on the ongoing Asset/Liability study they are conducting. James Dalton, Chair of the PERS Board was part of the discussion.

July Presentation Goals:

- Refine ALM Analyses as necessary
- Refine Potential Asset Allocation Policy
    - New Asset Classes or Implementation (Opportunity Portfolio, Alternatives Portfolio, TIPS, EMD, etc.)
- Adopt New Asset Allocation Policy

Summary-Next Steps:

- Ultimate Net Cost does not suggest taking less risk.
- Liquidity is not a problem.
    - IAP is the wild card.
- Refine ALM analyses as necessary.
- Refine asset mixes while reflecting OIC risk/return preferences.
- June/July – Share interim written correspondence, present final results on July 28, 2010.

After the presentation there was discussion among the Board, staff, and SIS. Staff suggested the adoption of a strategic target for an Alternatives Portfolio-keeping the existing tactical strategy within the Opportunities Portfolio from a zero percent target up to a three percent target, as opportunities present themselves.

After listening to the information from SIS and having discussions it was decided that there will be no change in the current policy at this time.

VI. 12:00 p.m.: Asset Allocation and NAV Updates

Mr. Schmitz reviewed the Asset Allocations and NAV's for the period ended April 30, 2010. All asset classes are within their allocation ranges.

VII. 12:02 p.m.: Calendar – Future Agenda Items

Mr. Schmitz highlighted future agenda topics. Topics to be covered in the July meeting are Real Estate Annual Review, Proxy Voting Update, and Annual Audit Update.

VIII. 12:04 p.m.: Other Business

There was no other business discussed.

12:05 p.m.: Public Comments

There were no public comments.

The meeting adjourned at 12:05 p.m.

Respectfully submitted,

Julie Jackson
Executive Support Specialist

Friends, colleagues…

I would like to read into the record a few words about our late Treasurer Ben Westlund. He was a strong voice both on this panel… and for it. He somehow managed to leave a legacy of both prudence and activism in the Treasurer's Office.

He was Treasurer for only 14 months before he died tragically of lung cancer in March.

But Ben made an indelible mark, and his tireless efforts as Treasurer and as a longtime legislator touched Oregonians deeply.

Ben was a classic entrepreneur. He helped start a mine for kitty litter in Eastern Oregon, and then got into ranching and then made a mint selling what you could call "liquid assets" (also known as cattle genetics or bull sperm). He used to joke that you could learn a lot about how to be Treasurer from the open range: A bull market is a good thing, he'd say. Be wary of predatory types. And always, you also have to watch where you step.

As Treasurer, Ben led the effort to stabilize and strengthen the Oregon 529 College Savings Program, and to win families a settlement for mismanagement of their accounts by Oppenheimer. He helped this council put Oregon in the spotlight nationally as an active limited partner.

But while he was a relative newcomer among Treasurers, he was an old friend for Oregonians.

He was the epitome of non partisan, or multipartisan, depending how you looked at it. He was a Republican and then an Independent and then a Democrat. But asked to describe him, most folks would say this: He was an Oregonian, and a damn good one.

And Ben looked out for what made Oregon special. In his 12 years in the Legislature, he created the Oregon Cultural Trust and then saved it from the budget ax. He created the Public Safety Memorial Fund and led the effort to save the Metolius River from destination resort development. He helped create the Rainy Day Fund that is responsible for protecting the state's credit rating.

And after first being diagnosed with lung cancer in 2005, he became a tireless advocate for expanding access to health care.

He was a family man -- a married father of two. He had the kind of welcoming personality that made it almost impossible dislike him. He was an inspiration to many.

He was 60, and he died much, much too soon.

This council lost an ally and a champion, and Oregon lost a friend and a leader. We all miss him.

Ben used to say this all the time, and it seems appropriate: Down the trail.

Down the trail, Ben.

TAB 2 – BLACKSTONE CAPITAL PARTNERS LP, VI

Blackstone Capital Partners VI, L.P.

Purpose

Staff is recommending a commitment of $200 million to Blackstone Capital Partners VI, L.P., ("the Fund") a $12.0 billion target fund pursuing a generalist, value-oriented buyout strategy. Fund VI will be a continuation of the successful strategy employed in prior Blackstone Capital Partners funds, focusing on building a portfolio of 25-40 companies diversified across transaction structures, geographic locations, and sector allocations.

Background

Founded in 1985 by Pete Peterson and Stephen Schwarzman, Blackstone has developed into a market leading, global alternative asset manager with business lines including: private equity funds, real estate opportunity funds, funds-of-hedge-funds, credit oriented funds, collateralized loan obligation vehicles, and closed-end mutual funds. Over 700 investment and advisory professionals, including 107 senior managing directors, manage approximately $100 billion of third-party capital from 15 global offices. In June 2007, the Firm completed an initial public offering on the New York Stock Exchange, and trades under the symbol "BX".

Depending on market conditions and opportunities, the Fund may invest via a variety of transaction structures, including traditional buyouts, corporate partnerships, platform buildups, strategic minority stakes, growth equity, and distressed investments. Typical investment sizes will be between $300 million and $800 million, with the exception of growth equity investments which will usually be smaller. The Fund will continue Blackstone's focus on building post-acquisition value through earnings growth, operational improvements, and cost savings via aggregated procurement strategies.

Blackstone has compiled an impressive track record in its five prior generalist funds. As of December 31, 2009 the performance of these funds is as follows:

- BCP I, a 1988 vintage fund, had a net IRR of 18.9 percent (first quartile), and a net total value multiple of 1.85x.
- BCP II, a 1993 vintage fund, had a net IRR of 31.7 percent (first quartile), and a net total value multiple of 2.09x.
- BCP III, a 1997 vintage fund, had a net IRR of 12.5 percent (first quartile), and a net total value multiple of 1.67x.
- BCP IV, a 2003 vintage fund, had a net IRR of 40.4 percent (first quartile), and a net total value multiple of 2.10x.
- BCP V, a 2006 vintage fund, had a net IRR of -15.4 percent (Fourth quartile), and a net total value multiple of .73x. It should be noted that the performance of this fund is too early to be meaningful, and the fund's progress to date is in line with other large-cap buyout funds invested during the 2006-2008 period.

OPERF has not committed to prior Blackstone funds, and a commitment to Fund VI would commence a new manager relationship. Staff believes that Blackstone has developed into a durable, institutionalized organization that will stand the test of time, and has demonstrated a proven formula for building value over a long period of time, and during multiple market cycles. In addition to Blackstone's appeal on a stand-alone basis, this recommendation is also based on a desire to restructure OPERF's large corporate finance manager pool. Adding BCP VI would provide OPERF needed portfolio diversification in the large corporate finance subsector, and along with a contemplated reduction in the size of the next commitment to KKR, would reduce OPERF's single-manager concentration risk (KKR).

A new commitment will be allocated 100 percent to the Corporate Finance subsector. As of March 31, 2010, OPERF's allocation to Corporate Finance is targeted at 65-85 percent, with a current fair market value plus unfunded commitments exposure totaling 72 percent.

Recommendation

Staff recommends that the OIC authorize a $200 million commitment to Blackstone Capital Partners VI, L.P., subject to the satisfactory negotiation of terms and conditions, and completion of requisite legal documents by DOJ legal counsel working in concert with OST staff.

MEMORANDUM

TO: Oregon Public Employees' Retirement Fund ("OPERF")

FROM: PCG Asset Management LLC ("PCG AM")

DATE: 6/2/2010

RE: Blackstone Capital Partners VI, L.P. ("the Fund")

Strategy:

The Blackstone Group ("Blackstone," the "Firm" or the "General Partner"), a global alternative asset manager listed on the New York Stock Exchange (ticker symbol "BX"), is sponsoring Blackstone Capital Partners VI, L.P. ("BCP VI," the "Partnership" or the "Fund") to pursue a broad range of equity and equity-related investments. Following the multi-dimensional, value-oriented investment strategy implemented across the General Partner's five prior private equity funds, Blackstone will continue to utilize a generalist approach to develop a portfolio with a diverse mix of transaction structures, geographic locations, and sector allocations.

The General Partner is seeking to make investments requiring $300 million to $800 million or more of equity capital depending on geographic location and investment type. Given the proposed commitment sizes and the targeted overall fund size of approximately $12 billion, Blackstone expects to acquire between 10 to 15 portfolio companies on an annual basis and 25 to 40 companies in aggregate across BCP VI.

Blackstone is in the later stages of raising capital for BCP VI. To date, the General Partner has secured $8.8 billion through a series of dry closings beginning in July 2008. A final close is expected on June 30th, 2010. The General Partner has stated that it will make a capital commitment equal to the sum of (i) $500 million and (ii) 5% of the capital commitments in excess of $10 billion, up to $750 million in aggregate. Through a side-by-side co-investment program, Blackstone and its professionals may also commit up to 7.5% of the amount of equity in each investment consummated through the Fund, although this amount may vary from year to year.

Please see attached investment memorandum for further detail on the investment opportunity.

Allocation:

A new commitment to the Fund would be allocated 100% to the Corporate Finance investment sub-sector. As of December 31, 2009 OPERF's allocation to Corporate Finance is listed in the table below. It is important to note that since allocation is based on fair market value, a commitment to the Fund would not have an immediate impact on OPERF's current portfolio allocation. A commitment to the Fund is complementary to OPERF's existing fund commitments and provides the overall portfolio with a further degree of diversification.

As of December 31, 2009	Target	FMV	FMV + Unfunded
Corporate Finance	65-85%	76%	73%

Conclusion:

The Fund offers OPERF an opportunity to participate in a differentiated private equity investment. PCG AM's review of the General Partner and the proposed Fund indicates that the potential returns available justify the risks associated with an investment in the Fund. PCG AM recommends that OPERF consider a commitment of $200 million to the Fund. PCG AM 's recommendation is contingent upon the following:

(1) Satisfactory negotiation or clarification of certain terms of the investment;

(2) Satisfactory completion of legal documents;

(3) Satisfactory continuation and finalization of due diligence;

(4) No material changes to the investment opportunity as presented; and

(5) Confidentiality maintained regarding the commitment of OPERF to the Partnership until such time as all the preceding conditions are met.

TAB 3 – ANNUAL OPERF REAL ESTATE REVIEW

OPERF Real Estate Portfolio 2010 Staff Review

Background:
The past five years have seen "the best of times and the worst of times" for the global economy and for real estate investing. As we head into the next decade, it is timely to look at OPERF's real estate portfolio: 1) regarding its ability to provide for the needs of the PERS account and 2) regarding how it is structured, both offensively and defensively, to profit from the global economy that we expect.

The OPERF Mission is:
To invest the PERS assets to provide and protect the pension benefits of Oregon state employees. The PERS assets are augmented by monthly employer/employee contributions, investment income and growth of investment assets. Lack of income or investment growth will increase the need for employer/employee contributions in the short term, impacting the state budget and indirectly increasing state taxpayer burden. Extreme financial losses incurred by the OPERF account may require direct state funding to cover PERS benefit obligations.

OPERF Goals:
To achieve its mission, the OPERF portfolio attempts to provide PERS with the following: (1) a long term total return of 8% (20 year "Actuarial Discount Rate"), (2) protection from catastrophic loss in portfolio value through investment diversification and fiduciary controls and (3) sufficient liquidity for annual PERS operations.

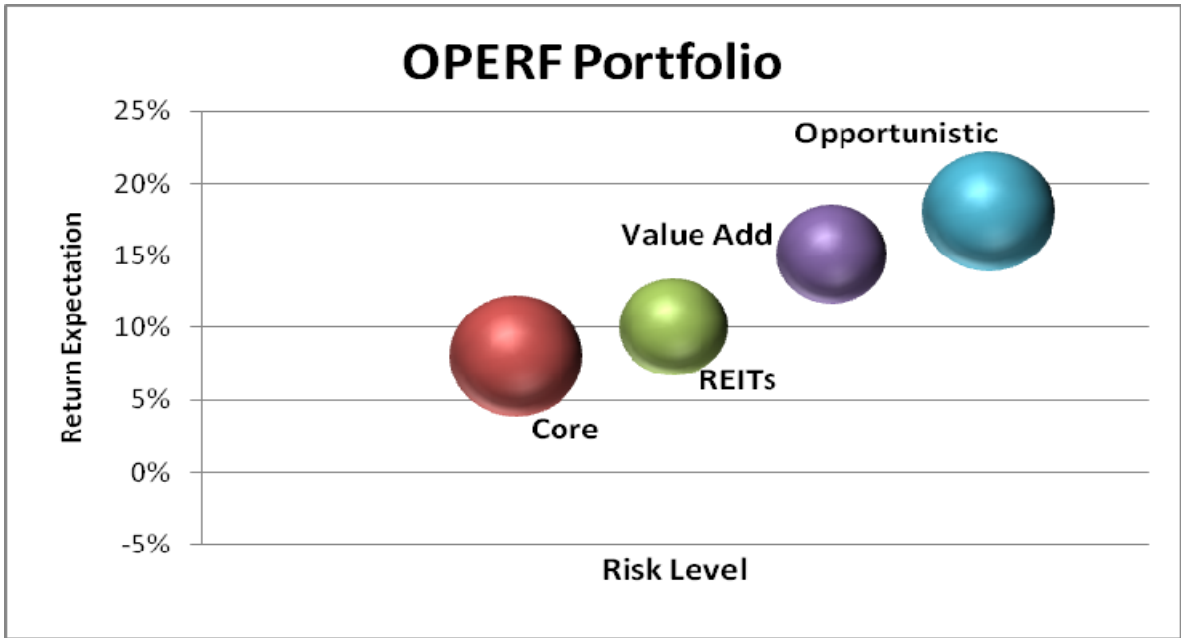
OPERF Structure:
To achieve its goals, the OPERF portfolio is structured with the following target allocation: Fixed Income 27%; Public Equities 46%; Private Equity 16% and Real Estate 11%. Liquidity needs are provided primarily by the Fixed Income and Public Equity accounts. The Real Estate and Private Equity accounts are focused on achieving long term returns above the OPERF 8% total return target and are less concerned about short term liquidity.

OPERF Real Estate Portfolio Structure:
Historically, the OIC considered Real Estate to be lower on the risk scale than Public Equities. At that time, the OPERF real estate portfolio was allocated 50% to domestic core real estate (with 40% maximum leverage). The core allocation offered good cash flow with the opportunity for long term appreciation, but with reduced liquidity. An additional 20% was allocated to a domestic Public REIT portfolio. REIT's are considered a surrogate for core real estate, generally holding well managed, commercial quality properties, with low levels of leverage. REITs provide a high level of liquidity but as a result show a higher level of pricing volatility. One OPERF REIT account targeted only the ownership of Regional Shopping Centers, an asset type that was difficult to acquire directly in OPERF's core allocation. Another account held only preferred REIT shares with a primary focus on income production. Thus,

REITs can provide tactical as well as strategic application. The remaining 30% of OPERF's real estate allocation pursued closed-end private equity real estate funds with a variety of "Opportunistic" strategies. These funds were very illiquid, generally with a ten-year life. They had a wide range of real estate strategies and permitted the use of ample leverage. Most funds create performance incentive by sharing fund profits with the manager (typically over a preferred return to the investors of 8% or more). Initially, these funds were OPERF's only exposure to global real estate markets outside the U.S.

In the past five years, OPERF's Core real estate allocation was reduced to 30% (while allowing debt levels of up to 50%). The remaining 20% of the Core real estate portfolio was re-allocated to "Value-added" real estate strategies that could acquire higher risk investments (when compared to Core) and through active management create core-like portfolios. Executed since 2007 as a defensive strategy against cap rate expansion being experienced in core markets, the Value-added funds have had a difficult time with eroding fundamentals and a disappearing debt market. Most have retained sufficient "dry powder" unfunded commitments to weather the storm. Given more time and a benevolent economy, the active management employed by Value-added funds should help them to perform well.

Future Value-added funds may pursue non-core property types such as: student housing, senior housing, medical office and public storage as well as ex-US core real estate that we would consider Value-added, due to a level of political and currency risk. These Value-added funds are expected to have risks, returns and leverage levels that fall between the Core real estate portfolio and the Opportunistic portfolio. They add an element of diversification to the portfolio which should help stabilize returns.



As international real estate markets have matured, OPERF's real estate portfolio has increased its global exposure. Currently, about one-third of the real estate portfolio's value is ex-US, primarily in the REIT

portfolios and the Opportunistic closed-end funds. Real estate investment performance is dramatically impacted by its local economic and demographic trends. Having a global portfolio permits a broader selection opportunity on the buy-side and offers a diversified return performance when holding or selling.

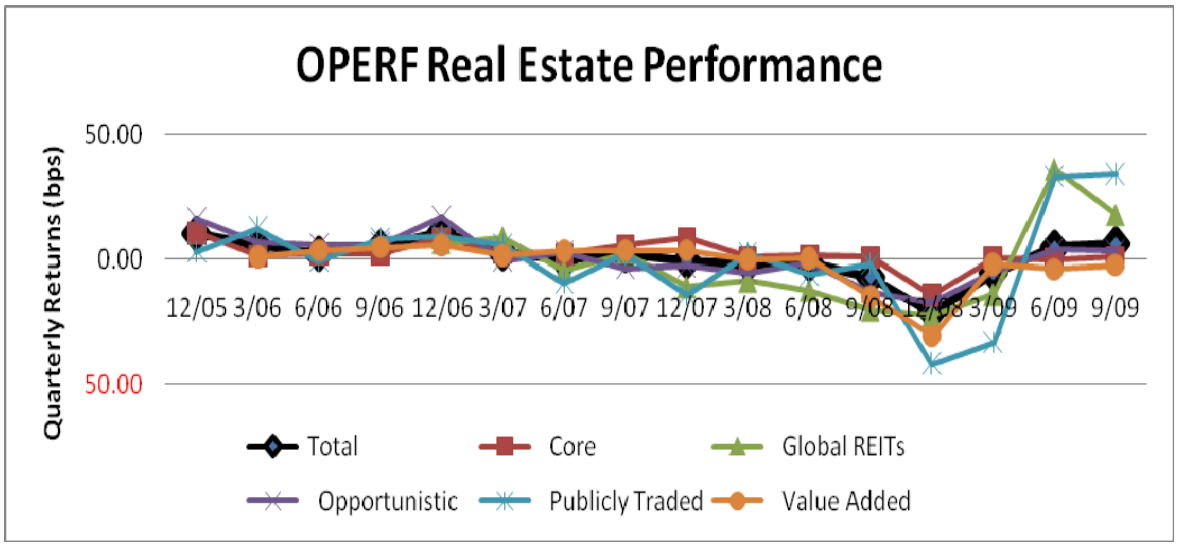
OPERF Real Estate Status 2009 Year-End:

2008 and 2009 will be remembered as a period of real estate re-pricing, debt re-structuring and portfolio re-evaluation. OPERF's portfolio is no exception. The 3-year annual real estate portfolio return at the end of 2007 was **+20.86%**. The 3-year annual real estate return at December 31, 2009 was **-11.02%.** During the past two years, REITs had the most dramatic swings in valuations (with a severe decline in value followed by a rapid recovery). OPERF rebalanced the REIT portfolio in mid-2009 to bring the portfolio into compliance with OIC policy. We invested $300 million at a low point in the pricing cycle and benefited from the subsequent market rebound. In May 2010, after the rebound moved the portfolio above OIC policy limits, we sold $300 million of the REIT portfolio after making a 40+% return. While the REIT portfolio has volatile pricing, it is more liquid than the rest of the real estate portfolio.

The OPERF Core portfolio consists of institutional quality office, retail, industrial, and apartment investments. 70% of the Core portfolio is managed in separate accounts for OPERF by four managers (one for each property type). The remainder is split between an open-end core real estate account with RREEF and a separate account for real estate debt with Guggenheim. OIC Policy targets the following Core portfolio diversification: office at 30%, retail and apartment at 25% each and industrial at 20%. At year-end 2009, the Core portfolio was distributed: office 28%, retail 28%, apartment 17%, industrial 20% and "other" 7%. OIC Policy targets core debt maximum level at 50% loan to value. The aggregate debt level for the core portfolio at year-end was 23% primarily due to holdings with RREEF (18% LTV) and Guggenheim (no leverage). Most of OPERF's separate account holdings were levered at 50% prior to the financial crisis but LTV's have increased up to 71% as property values have dropped. While the accounts are not in jeopardy for debt service coverage or margin calls, they have had to add equity occasionally as loans have matured. The OPERF Core portfolio held up well, defensively, given its low level of debt but has shared the drop in market values and will likely see more declines in 2010 due to a weak economy which has reduced demand for space. Improving cash flows and increasing valuations should occur over the next three to five years as real estate fundamentals and debt markets stabilize. During 2010 we expect the direct Core portfolio to produce a 9+% income return on 12/31/09 net asset values.

The Opportunistic and Value-added parts of OPERF's real estate portfolio see a mix of problems and opportunities. Those that invested in early 2008, and before, are struggling with value reductions and debt maturities. Delayed realizations at reduced pricing levels will mean that just returning capital and producing a positive IRR will be a good outcome. Later vintage funds that held on to their capital commitments will find the current buying environment beneficial for excellent returns in the future (in spite of and because of the decimated debt market).

In total, real estate represented about 9% of the total OPERF portfolio (target 11% of OPERF) at year-end 2009. The real estate portfolio's actual distribution at December 31, 2009 was: Core 28% (target 30%); Value-added 9% (target 20%); Opportunistic 38% (target 30%) and REITs 25% (target 20%). This diversification was most beneficial in recent years with Core returns holding up at the end of 2008 when REIT values fell and the reverse in 2009 when REIT values rose as Core values fell.



The OPERF real estate portfolio is diversified both geographically and by risk/return strategies. The following chart shows this breakout of portfolio Net Asset Values plus unfunded commitments. REITs are included in the core allocations. Of the $2.875 billion commitments approved in 2007 and 2008, over 50% have remained uncalled. Managers investing in distressed or discounted real estate debt, such as Lone Star and Guggenheim, have been active. Managers of equity real estate strategies have been keeping "Dry Powder" offensively (waiting for deal flow at distressed prices) or defensively (to support existing portfolio capital needs). OPERF has been well served by its managers who prudently avoided investing their commitments at the top of the market. They are well positioned to weather the down-turn and prepared to invest as the market improves. The portfolio is diversified across the U.S. with heavier concentrations in the East Coast and West Coast population centers. As noted previously about one third of the OPERF real estate investments are located in Europe and Asia with slight over-weighting to Europe.

December 2009 NAV plus Unfunded Commitments

	Core + REITs	Value-Add	Opportunistic	Total by Location
Ex-US (Non-U.S. only)	**$253**	**$100**	**$519**	**$872 (13%)**
Global (includes U.S.)	**$81**	**$0**	**$2,015**	**$2,096 (30%)**
Domestic (U.S. only)	**$2,807**	**$1,058**	**$95**	**$3,960 (57%)**
Total by Strategy	**$3,141 (45%)**	**$1,158 (17%)**	**$2,629 (38%)**	**$6,928**

2010 Economic and Real Estate Environment:

Like all downturns in the economy, we can expect a recovery over time. How will this one unfold and how can the OPERF real estate portfolio benefit most? Given the generally illiquid and long term hold nature of the investment, a 3-5 year view is appropriate. A shorter period will not allow time for new strategic applications to take hold. A longer view is really beyond our capabilities to project. Consensus appears to be a bumpy ride for years 1-3 with a gradual recovery by years 3-5. The early years should provide slow GDP growth of less than 3% (2.3% for the next decade, per Woody Brock), weak employment recovery, and low consumer confidence resulting in poor fundamentals for real estate across the board. Proforma rents and occupancies are both expected to remain depressed. CBRE predicts that it will take until 2014 for job growth to absorb current vacant space. Prices are still dropping but should bottom out in 2011 (per PCA Real Estate Advisors) but go nowhere until the debt markets recover. Real estate transaction volume in 2009 for NCREIF properties went from 17 in 1Q09 to 38 in 2Q09 to 80 in 3Q09. However, the market is still finding a bottom. Some sales are from distressed owners driven by financial pressures and "opportunistic" buyers looking for a deal rather than "a willing seller and willing buyer" as would be the case in a more stabilized market. Cap rates on these deals are in the 7%-8% range rather than the 4%-5% range experienced at the peak of the market. A few are

trophy properties in core markets yielding multiple bids at very low cap rates. At mid-year 2010, we see a few transactions at either end of the spectrum but none in the middle. Barring a "double-dip" in the economy or a relapse in the debt markets, a long, gradual real estate recovery should be underway. Longer term, inflation may become an issue. This may be the unintended result of recent government intervention to preserve the U.S. financial system. In general, inflation has helped real estate values increase once supply and demand are in balance.

Globally, demographics favor China, India and Mexico with young, growing populations when compared with aging Japan and Europe. The "BIC" markets (BRIC less Russia) of Brazil, India and China give the appearance of "emerging market" growth with scale plus some political stability. Appearances may be deceiving and "your results may vary".

The "Where To" and "How to" Invest in Real Estate Questions for OPERF:

We know where we are and where we have been but if we don't ask where we are going, it's hard to pick a path. What does the OPERF portfolio want real estate investments to provide? How should the real estate portfolio be positioned to complement the rest of the OPERF portfolio? To do this, staff reviewed the existing real estate portfolio elements to determine how they met OPERF goals in the recent good times and bad.

According to the OIC's Investment Objectives and Policy Framework for OPERF, the following goal has been set for the real estate portfolio: Real estate investments are being managed with the objective of earning at least 75 basis points in annualized net excess returns above the *NCREIF Index* over moving five-year periods. From 2005 to 2007, the five-year returns for OPERF's real estate portfolio exceeded NCREIF by more than 650 basis points each year. For 2008 and 2009, OPERF returns lagged NCREIF by 205 and 112 basis points, respectively. The portfolio structure was well rewarded in the "good years" and not penalized too severely in the "bad years".

Income vs. Appreciation

Currently, the real estate portfolio is weighted at the mid to upper end of the risk-return spectrum for pension fund products, in a desire to increase total returns. Fundamentally, we are saying that there is a benefit for OPERF to seek value appreciation through asset growth and the inflation hedge features provided by real estate (rent growth for core investments and financial engineering and market timing for Value-added and Opportunistic funds) foregoing current income. Should OPERF reshape the portfolio with more debt products producing interest returns but no growth (such as first mortgages) or preferred equity real estate securities to reduce risk even if it is at a cost of reduced total return?

Staff recommendation: ***The next five years should be a period of recovery for real estate. While base returns may be more assured by becoming more conservative, we would preclude much of the expected upside. If we acknowledge that appreciation in value is an objective for the real estate portfolio, then we must factor sufficient time for rents to grow and strategies to mature.***

Risk vs. Return

Increasing core real estate or investing in first mortgages could be a lower risk option but at a cost of lower returns (assuming no repeat of the Black Swan financial crisis). At December 2009, the 5-year returns were **2.4%** for Core and **9.3%** for Opportunistic. At December 2007, the 5-year returns were **18%** for Core and **27%** for Opportunistic showing, that opportunistic strategies can work in both up and down markets. The quarterly performance chart (above on page 4) indicated a consistent return pattern with REITs holdings, not Opportunistic funds, showing the greatest return volatility in recent years. Opportunistic funds have held up relatively well given the recent market turmoil. Should OPERF retreat from seeking higher returns from opportunistic real estate strategies to reduce risk?

Staff recommendation: ***In all, OPERF has been fairly rewarded for the risk it has taken. A period of economic recovery should provide conditions that will benefit Opportunistic fund strategies. Value-added strategies worked well in a heated market, unlikely to be seen again for a number of years. This sub-sector of the portfolio should be reduced from 20% to 15% of the real estate portfolio. The re-allocation should be returned to core strategies (either public or private) or allocated to core real estate in mature Non-US markets such as London, Paris, Hong Kong and Tokyo, to provide additional diversification.***

Capital Loss vs. Opportunity Loss

OPERF's real estate capital losses have come in two forms: recoverable and unrecoverable. Just as the REIT market declined and recovered, most of OPERF's private real estate will have value write-downs that should, in time, recover. OPERF's unrecoverable losses come primarily from debt issues caused by margin calls or debt maturities. While OPERF's Core properties dropped in value, no properties were lost to margin calls or maturities. OPERF's Value-Added and Opportunistic Funds have generally had success in minimizing major losses in dealing with this issue. A few have looked at future prospects for a property and handed the keys to the lenders because that was the best decision for the fund's overall return. Two prime examples that were severe were a levered debt fund and a large residential development. The debt fund lost most of its assets to its lenders, based on margin calls that could not be met. While the underlying loan assets were current, their values had dropped below the margin levels. The manager had reserves for "normal" real estate value volatility but was hit by the 100 year storm. A separate account, with the same manager and similar debt products, is up 12.5% with an $86 million profit, since inception in May 2008. The distress in the residential markets over the past few years has caused land values to plummet. The investment manager and the lender are trying to determine the best course of action for both to be made whole. Our underwriting stressed the proforma numbers by extending sale timing by 50% and reducing prices 10%, but it wasn't enough. If negotiations succeed, losses will be minimized. In both cases, the loss or potential loss occasioned by the economic down-turn was worse than had been underwritten, when the deal was approved. Even with the recent financial crisis, OPERF's 5-year total returns at 12/31/09 for its opportunistic real estate investments held at 9.3%. Should OPERF retreat from seeking higher returns from opportunistic real estate strategies to avoid capital losses?

Staff recommendation: ***Continued due diligence and risk management are necessary but if we attempt to remove all risk, we will also remove the chance for superior returns. Manager selection is critical to both deal underwriting and problem workouts so that capital losses will be minimized.***

Global Investing

Real estate truly is a local investment (location, location, location…). The benefits of investing locally extend outside the U.S. borders. OPERF's global (Ex-U.S.) exposure is about 30% to 33% of total net asset value. This has allowed for diversification and exposure to emerging markets where growth is more likely than in U.S., Japan and Europe. It also has allowed OPERF to participate in recovery of distressed markets outside our borders with global investment managers such as Fortress and Lone Star. This exposure adds several areas of risk: political risk (e.g., tax law changes, property being taken through nationalization and country rule of law risk), market and partner due diligence risk (how best to do business there), currency risk, and a myriad of other legal structuring issues. The good news is that between DOJ, our SAAGs and the GP's legal teams, the legal issues seem to be well handled. Both our consultants and a variety of GPs seem to be well equipped (and experienced) to handle the due diligence required of these opportunities. OPERF's past performance has been aided by the addition of global investments in its portfolio. 19 OPERF real estate accounts had returns greater than 10% during 2009. 16 of these 19 accounts held some or all of their investments outside the U.S. Should OPERF continue investing globally or retreat to within U.S. borders?

Staff Recommendation: ***Modern transportation and communications have "flattened the world." OPERF's top ten performing opportunity funds for 2009 all held international investments. While the risk of capital loss may be increased by venturing outside our borders, the opportunity loss for not doing so is substantial enough that we should not back off our current exposure.***

Operational Controls and Staffing

Limited Partnerships, by definition, allow "limited" involvement by the LP investor. Managed REIT accounts trade daily but have no OPERF staff input on transactions or portfolio direction. In both cases, staff selects or creates the investment mandate and then monitors the manager's execution. Direct real estate separate accounts move at glacial speed, requiring limited day to day attention. OPERF staff is consulted on major issues such as acquisition and sales and does review and approve annual capital and operating budgets for the direct portfolios. OPERF currently has about 75 real estate investment accounts with about 40 managers requiring attention of two OPERF investment managers. In general, State Street/Private Edge reporting, GP Quarterly reporting, Treasury Investment Accounting and OPERF's Real Estate consultant all add up to adequate oversight. In the past year, investment problems have taken substantial staff time working with both our general partners and other limited partners.

Some limited partners are encouraging the formation of "club deals" (a GP and one to three LPs). In these club deals, the LPs would have more control over the investment vehicle and be involved in some major decisions similar to OPERF's involvement in its direct separate accounts. LPs like the control that a club offers. GPs like dealing with a small number of like-minded investors. It is likely that OPERF could be 33% or more of the capital commitments of these investment vehicles. Given that the portfolio is larger

than in the past (11% of OPERF vs 8%), more complex than in the past (more Global) and requiring more LP involvement than in the past, it is likely that larger investment commitments (minimum $100 million) will be required.

Very large real estate investments may present areas of concern such as, manager qualifications (can a replacement be found?), ability to exit (i.e. large property liquidity) and concentration risks. More specialized staff may be required and more delegated approval authority from the OIC may be needed in the future to allow us to be more active partners with such deals. Should OPERF pursue large "club deals" and separate accounts that require greater staff involvement, more LP decision control and a higher percent ownership by OPERF than typical LP funds in the past?

Staff Recommendation: ***As the OPERF portfolio approaches $60 billion, the real estate portfolio will approach $6.6 billion. By necessity, more real estate commitments will need to be in the $500 million range. New managers and real estate platforms will need to be underwritten to provide for these investments. If the "club deal" concept takes hold, some of the best GPs may limit their LP groups to a few, major investors. OPERF will benefit from the additional control and the closer working relationship between LP and GP in these structures. State budget constraints have lead to a hiring freeze, currently. However, over time, OPERF should increase staff to facilitate these larger, hands-on deals.***

2010 OPERF Real Estate Portfolio Staff Summary:

As noted, if total OPERF value is $60 Billion, then the 11% target Real Estate will be $6.6 billion. Current real estate NAV (12/31/09) is $5.4 billion with unfunded commitments of $1.8 billion. If current commitments are drawn down by 50%, OPERF will be about $0.4 billion below its NAV target. This shortfall can be accepted as part of the normal "range" or can be rebalanced in the short term by acquiring REIT shares.

The use of leverage should also be monitored. OPERF's core portfolio limit of 50% LTV seems to have served us well in the past turmoil. REITs debt is self monitored by the market. The closed-end funds use debt that is available. If we have concerns about OPERF's debt levels, we can attempt to pursue deals with more controlled debt parameters. ***The appropriate amount of debt varies from time to time so, other than Core, OPERF needs to be flexible and leave the burden of leverage use to the GP as it has in the past.***

2010 Core Real Estate Strategy: Managers with active asset management capabilities will continue to be needed to work through the weak real estate fundamentals over the next couple of years. Staff will continue to monitor the existing manager teams and take action should their performance fail. Selective acquisitions of high quality properties should be encouraged if cap rates become elevated by historic standards and prices are below replacement cost. Focus on strong current cash flow and appreciation will follow. ***No major changes from current strategy.***

2010 REIT Portfolio Strategy:

Reconfigure management teams for more stream line operation. Rebalance by adding to the portfolio late in year if a down-turn is caused by real estate fundamental softness. ***No major changes from current strategy.***

2010 Value-Add Real Estate Strategy: OPERF's move to Value-add in January 2006 had two motivations. One goal was diversification to make room in the portfolio allocation for real estate holdings that were not defined as "Core" (i.e. Class "A" office, neighborhood retail, industrial warehouses or apartment buildings). Thus, student housing or public storage might be good investments but were not traditional core. Use of additional leverage (loan-to-value of up to 70% for Value-added funds vs. Core funds at 50% max) was allowed. The Value-add sector provided an allocation for these investments. The second goal was to acquire more risky (generally vacant) office, industrial, retail or apartments and turn them into "core" investment through active management and generate higher yields that the then "over-heated" market allowed. This was, in essence, a market timing strategy. In hindsight, the second strategy was ill-timed. The 2007/2008 vintage ran into a buzz saw of weakening fundamentals and a debt market in disarray. ***Looking forward, we should consider a reduction of Value-add sector from 20% to 15% to be used alternative real estate types (student housing, medical office, etc). The amount reduced should go to core investments primarily for global (ex-U.S.) core real estate investments.***

2010 Opportunistic Real Estate Strategy: Alignment of interest, fair fees, and LP controls (governance) will need to be addressed in the next round of investments. Strategically, we will continue to be opportunistic in looking for returns. As always, this will be both distressed markets and growth markets. ***No major changes from current strategy.***

OPERF Real Estate
2009 Review &
2010 Overview

2009 - 2010 Real Markets Estate

- Falling Fundamentals (occupancies & rents)
- Falling Values (Bottoming?)
- Debt Restructuring (but low interest cost)
- Few Trades
- Few New Building Starts

- REIT rebound anticipating a turn?
- Lots of Uncertainty

2009 OIC Policy Issues

- 1. Non-Mandate Investments
- 2. Leverage Limits
  - RE Portfolio 60% - actual 62.6%
- 3. REIT Portfolio Rebalancing
- 4. Portfolio Balance (Value-Added)
- 5. CORE Balance (Apartments)

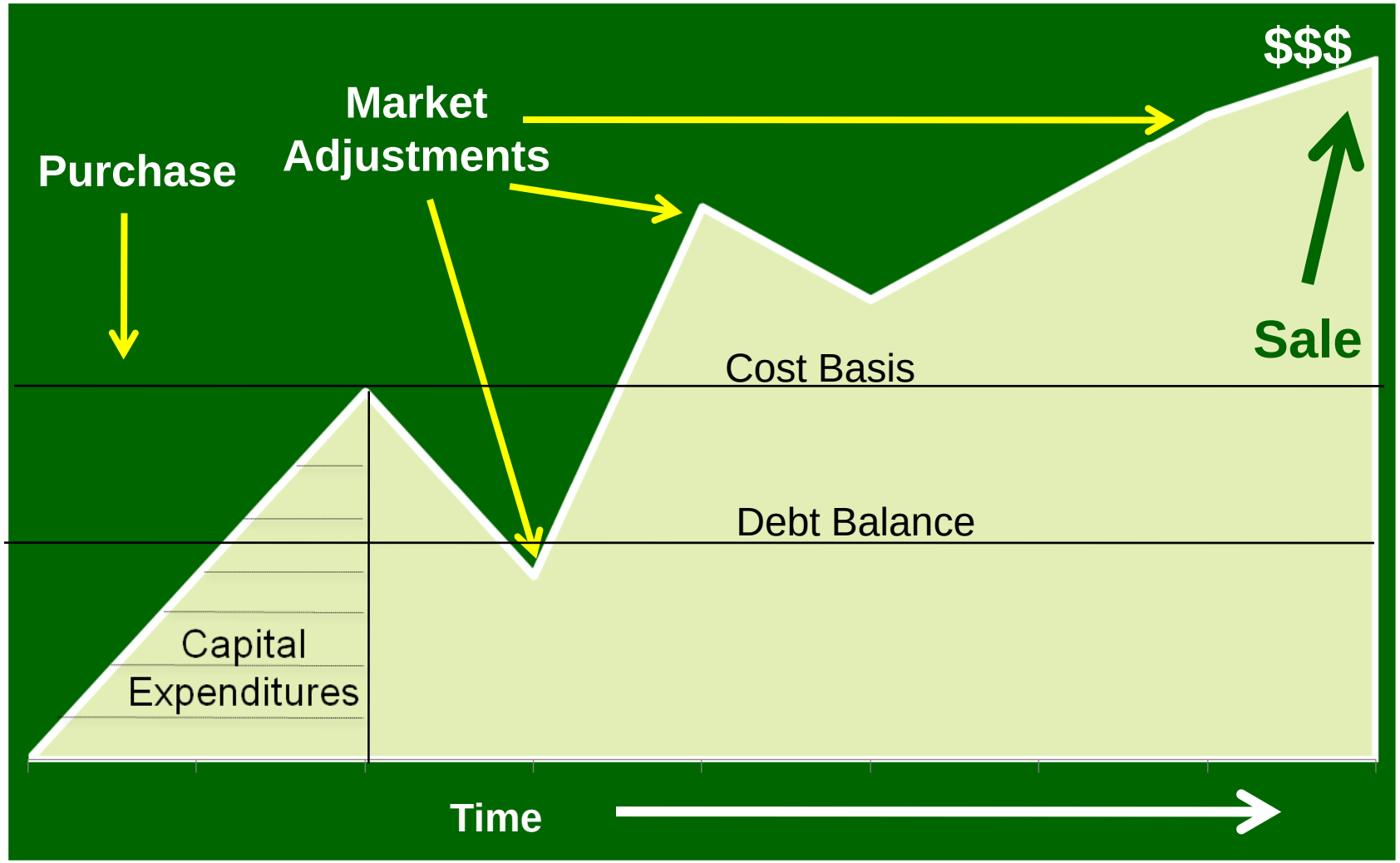
Non-Mandate Program

- **No New Acquisitions in 2009**
- **No Properties Declined for Conflict with Core**
- **Existing Non-mandate Investments 12/31/09**
  - **Lincoln Office** **$8.8 million NAV**
  - **Regency Retail** **$50.0 million NAV**

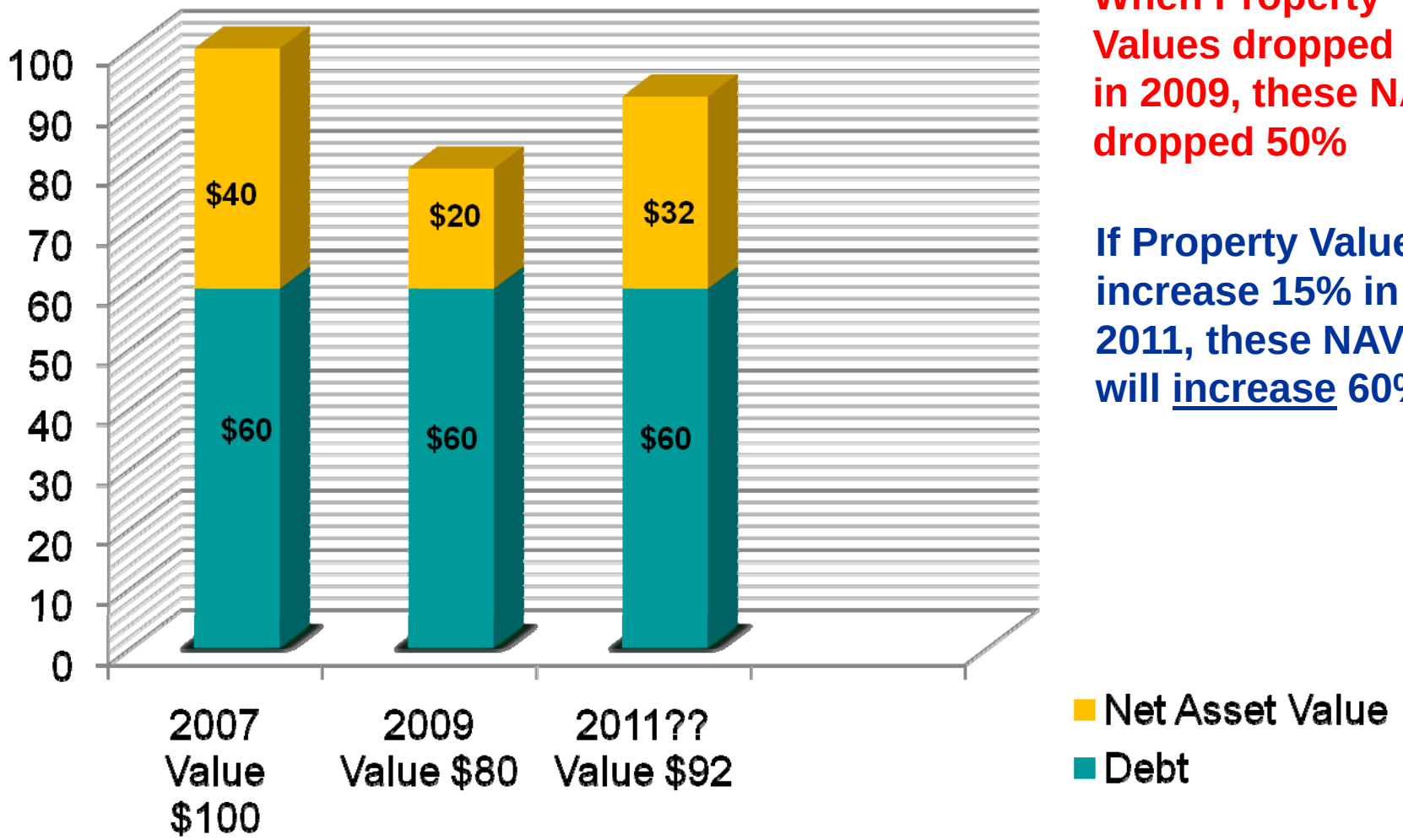
Leverage Limits

- OIC Loan-to-Value (LTV) Mandate
  - RE Portfolio Target LTV 60% -12/31/09 actual 63%
  - CORE Direct Target LTV 50% -12/31/09 actual 23%
    - Apartments 71% Industrial 61%
    - Retail 59% Office 59%
  - In part, an appraisal issue

Real Estate Asset Values (all is not lost)



Debt – the two edged sword



When Property Values dropped 20% in 2009, these NAV's dropped 50%

If Property Values increase 15% in 2011, these NAV's will <u>increase</u> 60%

Direct CORE Occupancy

Occupancy	12/31/08	6/30/09	6/30/10
Office	92.8%	92.3%	90.7%
Industrial	92.6%	92.1%	91.0%
Residential	96.0%	97.9%	97.6%
Retail	94.0%	93.0%	92.1%

- Projected 2010 cash flow returns > 9% on 12/31/09 NAV

Leverage Limits

- Staff recommends waiting for property values to rebound which will reduce the Loan to Value ratios.
  - The portfolio has no maturity or margin-call issues
  - No debt coverage issues
  - There would be a cost to Rebalance
  - Currently a low interest rate environment

Portfolio Balance 12/31/09

- 9% of OPERF Total Value vs Target 11%
  - CORE 28% of Real Estate vs Target 30%
  - REITs 25% of Real Estate vs Target 20%
  - Value Added 9% of RE vs Target 20%
  - Opportunistic 38% of RE vs Target 30%
  - Unfunded Commitments = $1.87 Billion

2009 & 2010
Fund Commitment Activity

- **2009 Fund Commitments**
  - Lone Star RE II $ 300,000,000
  - Lone Star VII $ 100,000,000
  - 3 Follow-on Commitments $ 22,000,000
  - Total 2009 Commitments $ 422,000,000

- **2010 Fund Commitments**
  - Vornado $ 100,000,000
  - Total 2008 Commitments $ 100,000,000

2010 Real Estate – 11%Target

$6.6 Billion Assuming OPERF at $60Billion

		Targets *	Actual NAV plus Unfunded 6/2010	Additional Needed Commitments
Core	30%	$1.980 B	$1,827 B	**$153 M**
REITs	20%	$1.320 B	$0.918 B	**$402 M**
Value Added*	20%	$1,650 B	$0.982 B	**$668 M**
Opportunistic*	30%	$2,970 B	$3.216 B	**-246 M**
Total Real Estate		$7,920 B	$6.943 B	**$977 M**

* Add buffer for standing unfunded commitments and harvested NAV

Unfunded Commitments – Dry Powder

- Held for Better Buying Opportunities
  - Prudently Patient Managers
- Held Defensively
  - For Capital Needs and Debt Buy-down
- Some will not be called as investment periods end.

REIT Portfolio Rebalancing

March 2009 - REIT holdings were <u>underweight</u>

9% of Real Estate Portfolio vs Target 20%

REIT Allocation Increased by $300 Million

$200 M to LaSalle + $100 M to Morgan Stanley in May 2009

March 2010 - REIT holdings were <u>overweight</u>

27% of Real Estate Portfolio vs Target 20%

US Allocation decreased $300 Million

$300 Million from La Salle in May 2010

What to Expect in 2010-11?

- **Core Real Estate**
  - **Net Incomes soft but stabilizing**
  - **Pricing and Deal Flow slowly improving**

- **REITs**
  - **Domestic Prices will hinge on private real estate pricing**
  - **We still expect Global REIT investments to provide Diversification and Growth, particularly in Asia**

- **Value Add & Opportunity Funds**
  - **Looking for Distressed Sellers and Distressed Property**
  - **Still working through the Pain**

OPERF Portfolio Structure Issues

- Target Income or Appreciation?
- Accept Risk for Higher Return or avoid it?
- Diversify Globally or avoid the risk?
- Pursue Fewer but Larger Commitments and Deals?

TAB 4 – ANGELO GORDON PAN ASIA REAL ESTATE FUND II

Angelo Gordon

AG Asia Realty Fund II, L.P.

Purpose:
Staff recommends a commitment of $100 million be made to AG Asia Realty Fund II, L.P., a pan-Asian real estate investment partnership sponsored by Angelo, Gordon and Co. The fund will seek investments in growth markets and recovering distressed markets through-out Asia. The opportunistic fund will seek net IRR returns of 20% using development and property repositioning strategies.

Background:
Angelo, Gordon & Co. is forming AG Asia Realty Fund II, L.P. to pursue an opportunistic real estate investment strategy primarily in mainland China, South Korea and Japan. They anticipate making 25 to 30 investments (ranging from $25 million to $100 million of equity) across different property sectors including: residential development, retail, office, industrial, multifamily and hotel. The fund intends to focus on acquisitions, particularly in Japan and South Korea, of distressed or sub-performing assets resulting from owner liquidity issues and inability to obtain debt financing, as well as opportunistic development strategies, particularly in China.

Angelo, Gordon is targeting capital commitments of approximately $550-650 million for the fund, following their $526 million AG Asia Realty Fund I. Fund I is now fully-invested and is projected to return an approximate 13% net IRR to investors and a 1.5x equity multiple. While this is lower than their initial target return of 20% net IRR, it is competitive when compared to fund level returns of other pan-Asia real estate strategies of the same vintage years as the Fund I investments were made. Fund II is targeting a net IRR of 20% to investors.

Angelo, Gordon & Co. was founded in 1988 by John Angelo and Michael Gordon. A privately-held registered investment advisor headquartered in New York City, Angelo, Gordon's specializes in alternative, or non-traditional, investments with significant experience in fixed income, private equity, real estate and hedging/arbitrage strategies. Currently managing approximately $23 billion in AUM, the firm employs over two hundred personnel globally with seven offices, three of which are in Asia. It began investing in U.S. commercial real estate in 1993. Their first Asian real estate investments began in 2005 and to-date they have invested over $800 million in 29 transactions, 16 of which were in Fund I. The AG Asia real estate team has 16 investment professionals with offices in New York (2); China (8); Korea (4) and Japan (2).

Issues for Consideration:
An investment in AG Asia Realty Fund II will continue to diversify OPERF's global real estate portfolio and provide additional exposure to the Asian emerging markets. As of December 31, 2009, the real estate portfolio had an approximate 12% exposure to Asia. Given the current fundamentals in the domestic and European real estate markets, as well as the projected growth for the emerging Asian markets,

employing a pan-Asian investment strategy provides OPERF additional geographic diversification and opportunistic target returns on a risk adjusted basis. OPERF's real estate Opportunistic portfolio has a target allocation of 30 percent of the real estate portfolio, with an allocation range of 20-40 percent. At year-end 2009, the Opportunistic portfolio was 38% of total OPERF real estate holdings. PCA's current pacing study indicates the Opportunistic portfolio dropping to 33% by year end 2010.

Angelo, Gordon's investment platform in Japan is relatively new. The head of their Japan office previously was responsible for a $1.5 billion real estate investment portfolio for RREEF. He worked at RREEF for 11 years and was a founding member of RREEF's Japanese platform.

Asian investment has political and currency risk not associated with domestic investing. Country and property type diversification targeted by the AG Asia Fund should soften the impact of these risks.

OIC's consultant, PCA Real Estate, Inc., has expressed concern that the mandate for AG Asia Realty Fund II includes the ability to use commitments to tactically acquire public real estate securities. They recommend limiting such acquisitions to less than 20% of the commitments. OST Staff concurs and is negotiating for this limitation.

Recommendation:
OST Staff and PCA Real Estate Advisors recommend a $100 million commitment to AG Asia Realty Fund II, L.P. OST Staff recommends that OPERF's commitment be no more than 20% of total AG Asia Realty Fund II commitments. It appears that the fund will raise more than $500 million. Staff recommends, however, that if total commitments to the fund are less than $500 million that OPERF's commitment be reduced to 20% of the total raised. Said commitment is subject to the satisfactory negotiation of the requisite legal documents by legal counsel working in concert with OST Staff and Department of Justice.

ANGELO, GORDON & CO.

AG Asia Realty Fund II, L.P.

presentation for

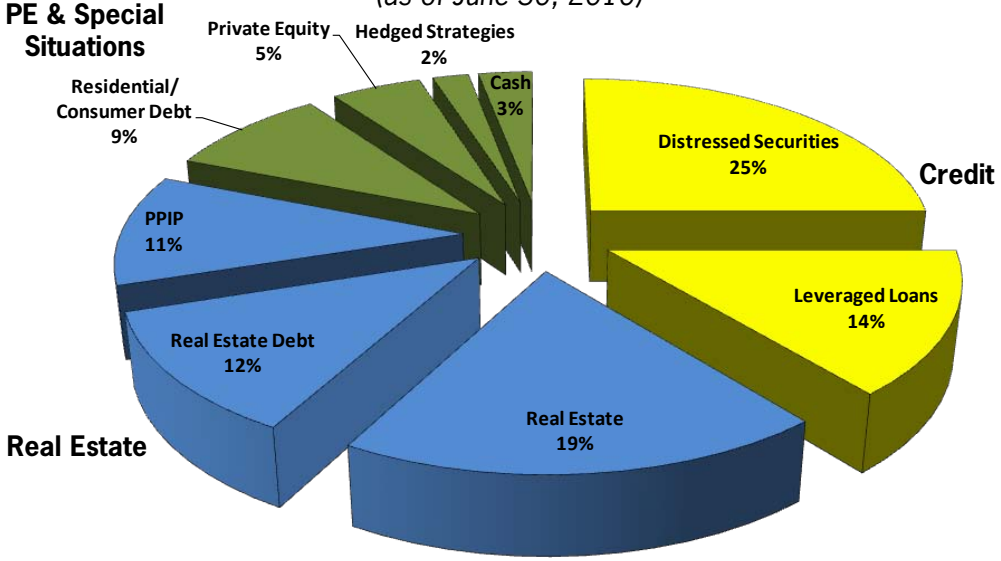
This document does not constitute an offer for sale of interests in AG Asia Realty Fund II, L.P. Such an offer may be made only by means of the Private Placement Memorandum of the Fund and will be made exclusively to investors satisfying the applicable eligibility criteria.

AG Overview

- Founded in 1988; privately held
- Leader in alternative investments focusing on absolute return strategies
- 206 staff members
  - 86 investment professionals
  - 54 accounting and operations professionals (22 CPAs)
  - 3 risk managers; 5 legal/compliance officers
  - 20 client service professionals
- Headquarters in New York with associated offices globally

$23 Billion in Assets Under Management

(as of June 30, 2010)



AG Commercial Real Estate Group

40 real estate investment professionals plus 25 support staff

Keith Barket
Global Head of AG Real Estate

Real Estate Debt

Andrew Solomon
Portfolio Manager

3 Add'l Investment Professionals

Real Estate Private Equity

US/London

Adam Schwartz
United States

13 Add'l Investment Professionals

Asia

Wilson Leung
China

Steven Cha
Korea/Japan

12 Add'l Investment Professionals

Net Lease Real Estate

Gordon Whiting
Portfolio Manager

5 Add'l Investment Professionals

US Real Estate Experience

Results

- Over $3.5 billion equity invested in over 230 transactions since 1993
- More than 70% of transactions realized
- 21% gross IRR on realized transactions
- Results achieved using average of 55-60% leverage

Competitive Advantages

- Over 35 active local operating partners without conflicts
- Seasoned team with operating experience
- Proven ability to navigate cycles (e.g., housing, land, hotels)

Asia Real Estate Experience

AG &Co

Results

- Invested approximately $800 million of equity in 29 deals since 2005
- Early deals meeting expectations (eight full realizations, four partial sales, several refinancings)
- Projected high teens gross IRR with 40% leverage

Competitive Advantages

- One of the most active Western investors in China and South Korea
- Experienced local AG real estate team throughout Asia
- Proven ability to exploit opportunities and avoid pitfalls
- Avoided:
  - Japan and Singapore real estate bubbles
  - Housing in China's primary cities (pre-correction)
  - Competitive land auctions
  - Traditional office
  - Korea housing

AG Asia Realty Fund I – Fund Status

- Inception: 2006
- Fund size: $526 million
- Capital called: 94%
- Capital distributed: 24.25%
- Leverage: 30% (est.)
- Projected gross IRR: 18%
- Investment status: Purchased 16 assets; fully invested

Asia Real Estate Strategy

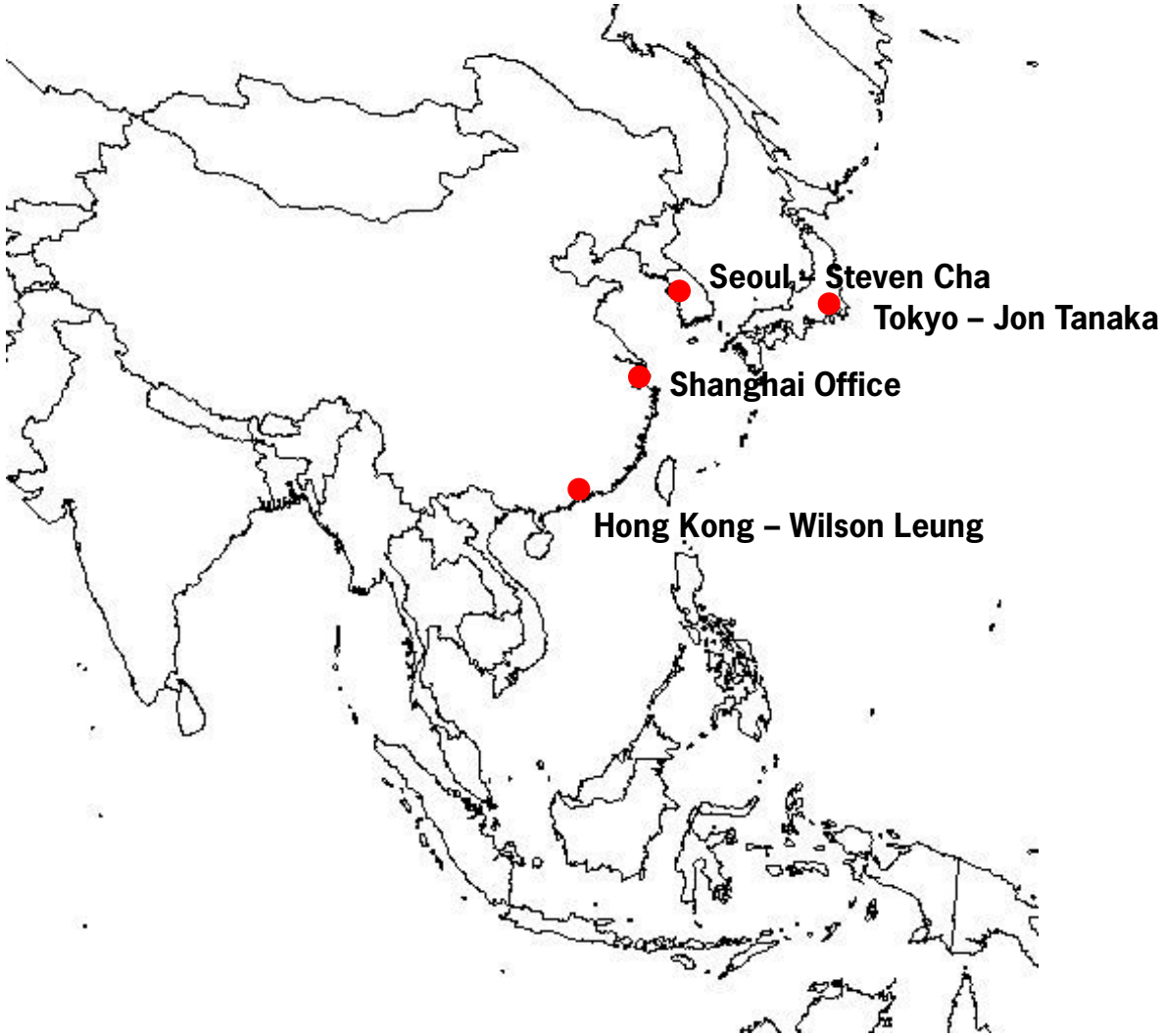
AG &Co

Capitalize on value-added turnaround and development opportunities primarily created through the lack of real estate expertise and illiquidity in many Asian markets.

- **Target returns:** 20% net
- **Holding period:** Typically 3-5 years
- **Expected leverage:** 50%

Angelo, Gordon Asia Real Estate Team

14 Investment Professionals
5 Support Staff



Typical AG/Operating Partner Model

Joint venture partnership with local operating partners

- AG provides majority capital and has control
- Capital is pari passu
- Operator manages day-to-day activities for a negotiated fee

AG has full control, including:

- All decisions (not just major decisions)
- Bank accounts and project company CFO
- Legal, environmental, ERISA, insurance, tax specialists
- Approves budgets, leasing, financing, capital expenditures, sales

Advantages

- Alignment of interests
  - AG takes no additional fees
  - AG is not driven by staffing concerns and can be nimble
- Vast off-market deal flow
- Best in class operators

Typical Categories of Deal Flow

AG &Co

Capital constrained sellers

- Tremendous liquidity issues in most of Asia due to lack of debt financing and immature capital markets
- Inexperienced owners lack capital to complete projects
- Motivated corporate and government sellers
- Significant increase in non-performing loans in Korea and Japan

Poorly managed assets

- New entrepreneurs with little experience
- Few assets have been repositioned
- Government-to-private ownership

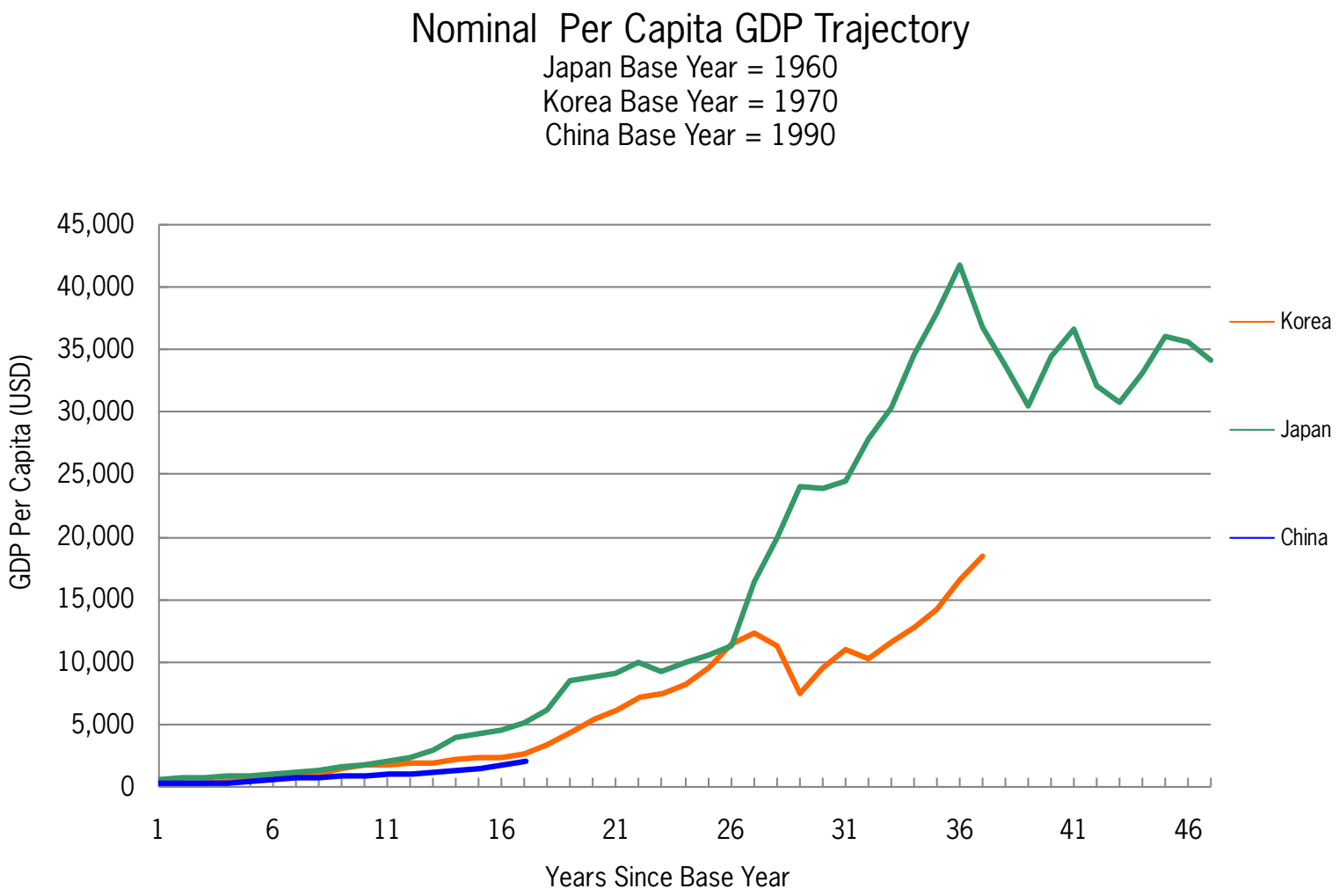
Growth-related development opportunities

- Migration to urban areas creating huge residential need
- Growth in economy creating need for distribution and retail product
- Globalization and growing service sector are creating office growth

The Case for Asia

- Importance of developing countries
  - US and Europe GDP growth will lag the rest of the world
  - As investors search for higher yield, they will encounter greater risk
- Asia offers among the best risk/return opportunities in the world
  - The Asia success story has been demonstrated by Japan, South Korea, Singapore, Hong Kong and Taiwan
- Talented managers in Asia should be able to outperform the indexes and western economies in all market cycles

The Case for Asia



Source: World Bank - adjusted to current currency , World Development Indicators database and www.earthtrends.wri.org

Market Opportunity – China

AG &Co

Growth – following same path as Japan, South Korea, Singapore

- 30 years of virtually uninterrupted growth of 10% per annum
- Tremendous investment in infrastructure

Unprecedented real estate needs

- Estimated need for 17 million new residential units per year
- Rapidly rising middle class will support retail and leisure
- Industrial sector growing quickly

Current outlook is positive

- Volatile stock market has limited IPO and public equity raises
- Significant stimulus package enacted
- Healthy profit margins on real estate deals
- Underleveraged economy

Market Opportunity – Japan

Global credit crisis affecting Japan

- Rising defaults
- Lack of leverage has reduced competition
- Prices down 30-40% since peak
- Expect corporate and public sectors to shed excess real estate

Public real estate companies undervalued

- Shareholder activism increasing
- Expect restructurings and real estate property sales

Fundamentals still strong

- Tokyo office vacancy rate in mid-single digits
- Very little new supply across all sectors
- Urbanization continues to drive population growth in Tokyo

Market Opportunity – South Korea

AG &Co

Credit crisis impacting Korea

- Cap rates have risen by 100 bps
- Increase in non-performing loans
- Housing prices down by 20%+

Few real estate private equity players

- Need for entrepreneurial private equity real estate capital
- Credit crisis has reduced availability of financing
- All foreign players affiliated with banks are exiting Korea

Strong fundamentals

- Low vacancies and limited new supply
- Office and retail rents are low compared to Asian neighbors
- GDP growth will continue to outpace world average
- Should benefit from trade with China, its largest export market

Sample Asia Transactions

Asia Transaction

Dalian Star Sea Project

3,100,000 sq. ft. mixed-use development in Dalian, China

Details of Purchase

Purchased from:	Insolvent developer
Purchase date:	February 2007

Fundamental strengths:

- Desirable, wealthy city in northeast China
- High-end residential neighborhood
- Low land basis with construction permits and plans in place
- No new land supply in immediate vicinity

Investment opportunity:

- Previous owner ran into financial difficulty
- Outstanding liabilities resolved by our partner prior to our investment

Turnaround plan:

- Pre-sell Phase I residential units to individual buyers during construction period
- Evaluate Phase II commercial to determine whether or not to exercise AG's Put option to sell shares back to operating partner

Results

Sale date:	March 2010
Invested equity:	$52.0 million
Net profit:	$41.7 million
Realized gross IRR/multiple:	**21.9%/1.8x**

Asia Transaction

Chengdu Logistics Facility

357,000 sq. ft. warehouse and office development in Chengdu, China

Status as of June 2010

- Three of the four facilities completed
- Completed buildings are 70% leased to the Customs and Inspections Authority
- In final lease negotiation for remainder of space

Details of Purchase

Purchased from:	Government land sale
Purchase date:	March 2007

Fundamental strengths:

- Chengdu is one of two major cities located in the western half of China
- Site is located in the Chengdu Airport Logistics Zone, an important logistics hub in China
- Obtained letters of intent with potential tenants prior to land purchase
- Strong tenant interest from local Customs and Inspection Authority, which would generate demand from other logistics tenants looking to locate near this critical government agency

Investment opportunity:

- Area around airport largely undeveloped
- Local government seeking experienced logistics operators/developers

Turnaround plan:

- Lease buildings to logistical users
- Build the facility and sell once fully stabilized

Projected Economics

All-in costs:	$18.0 million
Projected stabilized NOI:	$3.1 million
Projected gross IRR/multiple:	30.3%/2.2x

Asia Transaction

Project Seoso

107,000 sq. ft. office in Seoul CBD, Korea

Status as of June 2010

- In negotiations with the owner of adjacent parcel to purchase additional land parcels
- In discussions with Standard Chartered to secure development/construction loans
- Considering an early exit to local investors and discussing sales structure and terms

Details of Purchase

Purchased from:	Insurance company user
Purchase date:	July 2008

Fundamental strengths:

- Located in prime area of downtown Seoul
- Current utilized FAR is 400% while zoning permits up to 1,000%
- Purchased land at 30% discount to comparable sites

Investment opportunity:

- Owner motivated to sell quickly
- Previous owner was not an experienced real estate operator and did not seek highest and best use of site
- Vacant sites of this size are exceptionally rare in prime office locations in central Seoul

Turnaround plan:

- Demolish existing structure
- Assemble adjacent land parcels
- Develop and lease new class A office property

Projected Economics

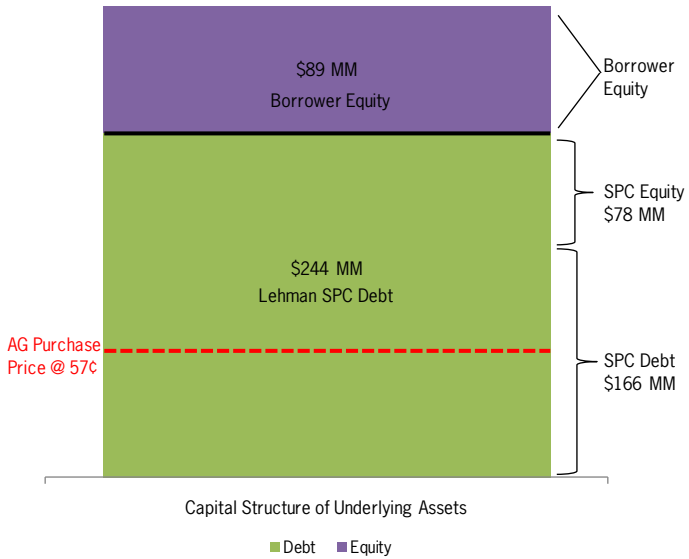
All-in costs:	$143 million (includes expansion)
Cost PSF:	$410
Sales price PSF*:	$565
Projected gross IRR/multiple*:	24.1%/2.8x

* Includes foreign currency hedge

Asia Transaction

Lehman Legacy Portfolio

Distressed real estate loan in Korea



Note: In the above chart, miscellaneous non-Lehman debt is excluded. Also, all amounts are based on the exchange rate at acquisition.

Status as of June 2010

- Court declared SPC bankrupt and court liquidator was appointed in Nov'09
- Court liquidator closed on sale of one of the underlying assets and signed SPA to sell another underlying asset in 2Q'10
- To date, we recovered 28.6% of our purchase price
- Expect to recover 100% of purchase price by year-end, ahead of our projections

Details of Purchase

Purchased from: Australia New Zealand Bank ("ANZ")

Purchase date: June 2009

Fundamental strengths:

- Lehman Brothers made 12 senior/mezz real estate loans in Korea through an SPC with $244 million
- SPC was capitalized with 32% Lehman equity and 68% senior loans. Senior lenders were ANZ, Standard Chartered and Lehman. ANZ portion was $62.4mm, or 37% of total senior loans. Lehman NY guaranteed senior loans
- Although assets performed, SPC went into bankruptcy triggered by Lehman NY bankruptcy

Investment opportunity:

- Purchased ANZ loans at 57% of OPB. ANZ sold loans due to limited understanding of underlying real estate and bankruptcy process

Turnaround plan:

- Negotiate with Lehman and other creditors to agree on a private workout plan
- Private workout plan may involve (i) write-down of Lehman's loan and equity in the SPC and (ii) taking direct control of the underlying assets
- Lehman is highly incentivized to cooperate

Projected Economics

All-in costs:	$38.3 million
Original principal balance:	$67.4 million
Projected recovery value*:	$64.9 million
Projected gross IRR/multiple*:	30%+/1.7x

* Includes foreign currency hedge

Asia Transaction

Hwasung Logistics

5.4 million sq. ft. of land suitable for industrial/logistics facilities

Details of Purchase

Purchased from: Korean/Japanese investor

Purchase date: December 2006

Fundamental strengths:

- Low cost basis in land
- Large site that is difficult to assemble in a comparable location
- Strategic location 35 kilometers south of Seoul and located on primary north/south highway
- Partnered with CJ Group, a major consumer goods and logistics user (CJ committed to buy 35% of site). CJ Group is affiliated with the Samsung Group

Investment opportunity:

- Prior owner unsuccessful in assembling enough land for golf course development
- Seller needed to sell before 2007 for tax reasons

Turnaround plan:

- Re-zone to large scale logistics use
- Complete horizontal improvements
- Sell pads to end users

Results

Sale date: November 2009

Invested equity: $29.1 million

Net profit*: $19.1 million

Realized gross IRR/multiple*: 20.8%/1.7x

* Includes foreign currency hedge

Summary of Terms

- **Term:** 4 year investment period following initial closing; 4 year liquidation period; option to extend up to two additional one year periods

- **Management Fees:**
  - Below $50mm — 1.75% of committed capital during investment period; 1.75% of net funded capital thereafter
  - $50-99mm — 1.25% of committed capital during investment period; 1.75% of net funded capital thereafter
  - $100mm+ — 1.00% of committed capital during investment period; 1.50% of net funded capital thereafter

- **Incentive Distributions:** 20% to Angelo, Gordon, subject to a 10% compounded preferred return and a 50% catch-up

- **AG Commitment:** $15 million

PLEASE REFER TO THE CONFIDENTIAL INFORMATION MEMORANDUM FOR A COMPLETE DESCRIPTION OF TERMS.

Contact Information

Aliana Spungen
Angelo, Gordon & Co.
245 Park Avenue, 26th Floor
New York, NY 10167
Telephone: (212) 692-8267
Facsimile: (212) 867-9328
Email: aspungen@angelogordon.com

TAB 5 – HIGHER EDUCATION POOLED ENDOWMENT FUND

Oregon Investment Council
Higher Education Pooled Endowment Fund
Asset Allocation Study

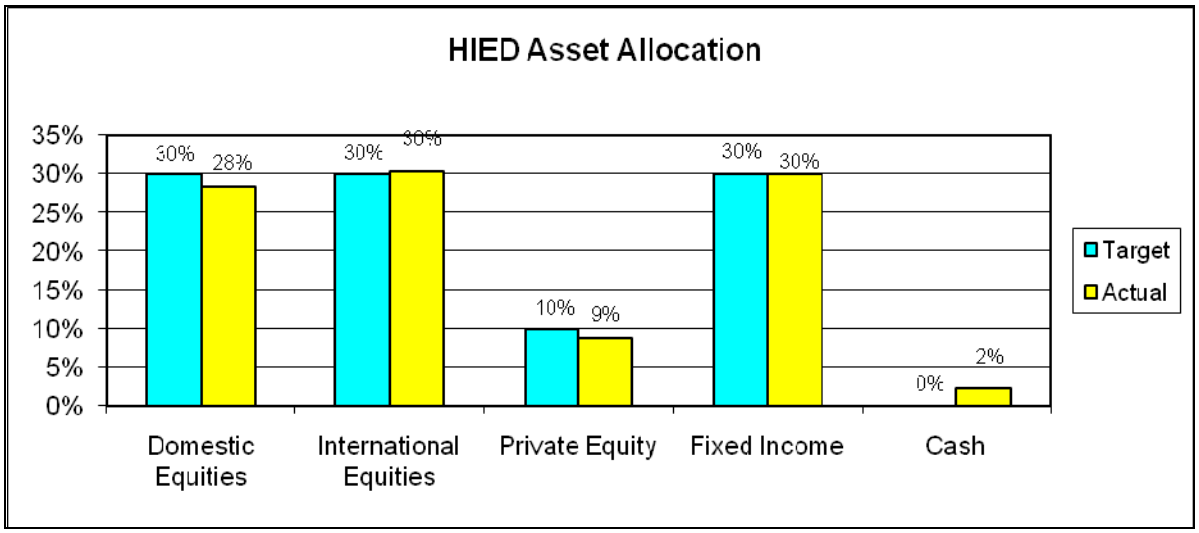
Purpose
To seek OIC approval for a proposed change in the asset allocation for the Higher Education Pooled Endowment Fund.

Discussion
As reported to the OIC in December of last year, the HIED Board commenced with an asset/liability study in 2010, which resulted in proposed changes, approved by the HIED Board at their meeting on July 9, 2010.

Background
Staff and SIS have been working with Oregon University System (OUS) staff to revisit the Pooled Endowment Fund's asset allocation, at the request of the HIED Board.

Current asset allocation:

HIED	Policy	Target	$ Thousands	Actual
Domestic Equities	25-35%	30%	$17,136	28.4%
International Equities	25-35%	30%	18,314	30.4%
Private Equity	0-10%	10%	5,274	8.8%
Total Equity	**65-75%**	**70%**	**40,724**	**67.6%**
Fixed Income	**25-35%**	**30%**	**18,120**	**30.1%**
Cash	**0-3%**	**0%**	**1,404**	**2.3%**
TOTAL HIED			**$60,248**	**100.0%**



The HIED board is has focused on defining fund assets in three broad categories:

1. Growth Assets
2. Inflation Hedging Assets
3. Diversifying Assets

Based on this rubric, SIS and staff presented the following recommendation to the HIED Board (see attached for further details):

Asset Group	Current Target	New Target	New Range
Growth Assets	67%	60%	50-75%
Inflation Hedging Assets	3%	15%	7-20%
Diversifying Assets	30%	25%	20-30%

Staff and SIS plan to return to the HIED Board and the OIC in September with proposed policy changes and an implementation plan. Part of the analysis to be provided will be an assessment of the cost-effectiveness of implementing the "hard asset" allocation.

Recommendation
Accept the proposed change in asset allocation for the HIED Pooled Endowment Fund, subject to revised policies and an implementation plan being presented to the OIC in September.

HIGHER EDUCATION ENDOWMENT FUND

ASSET ALLOCATION RECOMMENDATION

July, 2010

STRATEGIC INVESTMENT SOLUTIONS, INC.

333 Bush Street, Suite 2000
San Francisco, CA 94104
(415) 362-3484

John P. Meier, CFA
Managing Director

Asset Mix Recommendation

	Current Target*	Rec. Target	Min	Max
Growth Assets	67%	60%	50%	75%
US Equity	30%	25%	20%	30%
International Equity	30%	25%	20%	30%
Private Equity*	7%	10%	0%	15%
Inflation Hedging Assets	3%	15%	7%	20%
Real Estate*	3%	5%	0%	10%
TIPS	0%	5%	0%	10%
Other Hard Assets	0%	5%	0%	10%
Diversifying Assets	30%	25%	20%	30%
Nominal Fixed Income	30%	25%	20%	30%
Cash	0%	0%	0%	3%
Expected Return	8.17%	8.33%		
Expected Std Dev	12.7%	12.7%		
Sharpe Ratio	0.408	0.421		

*Real Estate and Private Equity are currently combined within Alternative Assets

Asset Mix Transition

	Current %	Current $	$ at New Target	Delta
Growth Assets	68.5%			
US Equity	30.5%	$ 19.6	$ 16.0	$ (3.5)
International Equity	32.4%	$ 20.8	$ 16.0	$ (4.7)
Private Equity	5.6%	$ 3.6	$ 6.4	$ 2.8
Inflation Hedging Assets	2.7%			
Real Estate	2.7%	$ 1.7	$ 3.2	$ 1.5
TIPS	0.0%		$ 3.2	$ 3.2
Other Hard Assets	0.0%		$ 3.2	$ 3.2
Diversifying Assets	28.9%			
Nominal Fixed Income	28.4%	$ 18.2	$ 16.0	$ (2.2)
Cash	0.5%	$ 0.3	$ -	$ (0.3)
Total		$ 64.1	$ 64.1	

Implementation Plan

- Hire TIPS Manager
- Continue to Fill Real Estate and Private Equity Allocations through Oregon Treasury and SIS Relationships
- Seek Cost Effective implementation of “Hard Asset” Allocation
  - If not obtainable, split allocation between TIPS and Real Estate (8.2% Exp. Return, 12.5% Exp. Std. Dev., 0.415 SR)

TAB 6 – OIC POLICY UPDATES

OIC Policy Updates
July 2010

Purpose
To update an OIC Policy revision that was missed during the April 2010 update.

Discussion
4.03.01: Proposed changes resulting from a recent internal audit.

Recommendation
Approve staff proposed changes outlined above, and as reflected in the attached policy.

FUNCTION: Fixed Income Investments

ACTIVITY: Strategic Role of Fixed Income for OPERF

POLICY: Fixed income investment should comprise 22% to 32% of OPERF's total assets, subject to the specific strategic target allocations established by the OIC.

A. PROCEDURES:

PURPOSE

The purpose of these Fixed Income Investment Policies & Strategies is to define the strategic role of fixed income as an asset class within the Investment Council's general investment policies for the Oregon Employees Retirement Fund (OPERF), to set forth specific short-term and long-term policy objectives for this segment of OPERF's investment portfolio, and to outline the strategies for implementing the Investment Council's fixed income investment policies.

STRATEGIC ROLE

The purpose of fixed income investments is to provide diversification to equity securities, through lower expected return and volatility and a low correlation to equities. Fixed income investment should comprise 22% to 32% of OPERF's total assets.

B. POLICY OBJECTIVES

1. To achieve a portfolio return of 75 basis points or more above the custom policy benchmark, consisting of 90% Barclays Capital U.S. Universal and 10% Citigroup Non-U.S. World Government Bond (Hedged) Indexes, over a market cycle of three to five years on a net-of-fee basis. The portfolio is also expected to achieve top quartile peer group performance. Peer group shall consist of public and corporate funds with total assets greater than $1 billion.
2. To control portfolio risk, as measured by standard deviation of returns, to the level of the custom benchmark or less through diversification of investment approaches.

C. STRATEGIES

1. Maintain a well-diversified bond portfolio, managed to maximize total return, that reflects the overall characteristics of the custom benchmark.
2. Maintain an average bond duration level of +/-20% of the benchmark duration.

3. Invest opportunistically, using innovative investment approaches within a controlled and defined portfolio allocation.
4. Active investment managers are expected to outperform stated benchmarks on an after-fee, risk adjusted basis, over a market cycle of three to five years.
5. The Investment Council's selection of active managers will be based upon demonstrated expertise. Active managers will be selected for their demonstrated ability to add value, over a passive management alternative and within reasonable risk parameters.

D. PERMITTED HOLDINGS

The following fixed income securities, individually or in commingled vehicles, may be held outright and under resale agreement:

1. Obligations issued or guaranteed by the U.S. Federal Government, U.S. Federal agencies or U.S. government-sponsored corporations and agencies.
2. Obligations of U.S. and non-U.S. corporations such as convertible and non-convertible notes and debentures, preferred stocks, commercial paper, certificates of deposit and bankers acceptances issued by industrial, utility, finance, commercial banking or bank holding company organizations, bank loans, common stock received in connection with the restructuring of corporate debt.
3. Mortgage-backed, ~~and~~ asset-backed securities and structured securities.
4. Obligations, including the securities of emerging market issuers, denominated in U.S. dollars or foreign currencies of international agencies, supranational entities and foreign governments (or their subdivisions or agencies), as well as foreign currency exchange-related securities, warrants and forward contracts.
5. Obligations issued or guaranteed by U.S. local, city and state governments and agencies.
6. Securities defined under Rule 144A and Commercial Paper defined under Section 4(2) of the Securities Act of 1933.
7. Yankee Bonds (dollar denominated sovereign and corporate debt).

~~7.~~8. Derivatives including futures, swaps and options contracts.

~~8.~~9. Securities eligible for the Short-Term Investment Fund (OSTF).

E. DIVERSIFICATION:

The portfolio should be adequately diversified to minimize various risks. The following specific limitations reflect, in part, the OIC's current investment philosophy regarding diversification:

1. Obligations issued or guaranteed by the US government, US agencies or government sponsored enterprises are eligible, without limit.

2. Obligations of other national governments are limited to 10% per issuer.
3. Private mortgage-backed and asset-backed securities are limited to 10% per issuer, unless the collateral is credit-independent of the issuer and the security's credit enhancement is generated internally, in which case the limit is 25% per issuer.
4. Obligations of other issuers are subject to a 3% per issuer limit excluding investments in commingled vehicles.
5. Not more than 25~~15~~% of the portfolio may be invested in non-dollar denominated securities.
6. Not more than 10% of the portfolio may be invested in Emerging Market Debt (dollar and non-dollar denominated) rated below investment grade.
7. Not more than ~~30~~35% of the portfolio will be below investment grade (below Baa3/BBB-). ~~The minimum aggregate credit quality shall be A+, as measured by the weighted average of the portfolio.~~
~~7.~~8. No more than 5% of the portfolio will be invested in original futures or swaps margin and option premiums, exclusive of any in-the-money portion of the premiums. Short (sold) options positions will generally be hedged with cash, cash equivalents, current portfolio security holdings, or other options or future positions.

F. ABSOLUTE RESTRICTIONS:

Investments in the following are prohibited:

1. Short sales of securities.~~;~~
2. Margin purchases or other use of lending or borrowing money or leverage to create positions greater than 100% of the market value of assets under management.~~;~~
3. Commodities or common stocks,~~; and~~ unless common stock shares are received due to a restructuring, then shares will be liquidated at the manager's discretion.
4. Securities of the existing investment manager, its parents, custodians or subsidiaries.

SAMPLE FORMS, DOCUMENTS, OR REPORTS:

None

TAB 7 – ANNUAL PROXY VOTING UPDATE

2010 Proxy Voting Summary and Current Issues

Purpose
To provide a summary of the votes Glass, Lewis and Co. cast on the OIC's behalf for the period January 1 to June 30, 2010, and to provide a review of the recent proxy voting season and current issues.

Background
At the September 27, 2006 OIC meeting, the Council voted to retain Glass, Lewis and Co. as its proxy voting agent, and to follow Glass Lewis' standard Proxy Paper Policy Guidelines. Glass Lewis replaced Institutional Shareholder Services (ISS), initially retained by the OIC in 2003 (the same year Glass Lewis was founded). Glass Lewis describes their proxy voting service as follows:

- The research is fully independent and objective; we are not in the business of providing consulting services to public companies and can therefore focus solely on the best interests of investors;
- The focus of the research is the economic and financial consequences of voting and therefore on improving medium- to long-term value and mitigating risk at public companies;
- Our approach to corporate governance is to look at each company individually and determine what is in the best interests of the shareholders of each particular company; we do not believe there is one answer that applies to every company;
- The research team is highly professional, with more than 70% of our research analysts holding graduate degrees in fields relevant to our research;
- Our research analysts are available to clients for questions or assistance on specific companies or meetings or for general corporate governance topics;
- We have a global presence, with research offices in Asia, Australia, North America and Europe; and
- Our research on proxies covers more than just corporate governance -- we analyze accounting, executive compensation, compliance with regulation and law, risks and risk disclosure, litigation and other matters that reflect on the quality of board oversight and company transparency.

The information for this presentation relates generally to Glass Lewis' standard proxy voting policy. A summary of their Guidelines is available upon request.

Information
This report includes a comprehensive summary of the votes Glass Lewis cast on the OIC's behalf for the 2010 proxy season, January 1st through June 30th, 2010. This report is included in accordance with OIC policy 4.05.06 (attached) that requires "Treasury staff [to] provide a . . . proxy voting summary to the OIC."

Staff Recommendation
None. Information only.

Proxy Voting Report

Ballot Status Summary

Number of Meetings	
	3822
Number of Ballots	
	7281
Confirmed	**% Of All Ballots**
6883	94.5%
Validated	**% Of All Ballots**
33	0.5%
Sent Ballots	**% Of All Ballots**
6	0.1%
Unsent Ballots	**% Of All Ballots**
11	0.2%
Take No Action	**% Of All Ballots**
530	7.3%
No Vote Cast	**% Of All Ballots**
345	4.7%

Vote Against Management (VAM) Summary

Number of Meetings	Number of Proposals
3822	43338
Number of Countries (Country of Origin)	**Number of Countries (Country of Trade)**
58	57
Number of Meetings With VAM	**% of All Meetings Voted**
2353	70.1%
Number of Proposals With VAM	**% of All Proposals Voted**
5553	16.4%
Number of Meetings With Votes For Mgmt	**% of All Meetings Voted**
3318	98.9%
Number of Proposals With Votes For Mgmt	**% of All Proposals Voted**
28333	83.4%
Number of Abstain Votes	**% of All Proposals Voted**
848	2.5%

Votes Against Policy (VAP) Summary

Number of Meetings	Number of Proposals
3822	43338
Number of Countries (Country of Origin)	**Number of Countries (Country of Trade)**
58	57
Number of Meetings With VAP	**% of All Meetings Voted**
15	0.4%
Number of Proposals With VAP	**% of All Proposals Voted**
32	0.1%
Number of Meetings With Votes For Policy	**% of All Meetings Voted**
3347	99.8%
Number of Proposals With Votes For Policy	**% of All Proposals Voted**
33886	99.8%
Number of Abstain Votes	**% of All Proposals Voted**
848	2.5%
Number of No Votes Cast	**% of All Proposals Voted**
4153	12.2%
Number of Proposals with Votes with GL	**% of All Proposals Voted**
33917	99.9%

Proposal Summary

Number of Meetings: 3822

Number of Mgmt Proposals: 37472

Number of Shareholder Proposals: 615

Mgmt Proposals Voted FOR	% of All Mgmt Proposals
27923	74.5%
Mgmt Proposals Voted Against/Withold	**% of All Mgmt Proposals**
4577	12.2%
Mgmt Proposals Voted Abstain	**% of All Mgmt Proposals**
848	2.3%
Mgmt Proposals With No Votes Cast	**% of All Mgmt Proposals**
4141	11.1%

ShrHldr Proposal Voted FOR	% of All ShrHldr Proposals
241	39.2%
ShrHldr Proposals Voted Against/Withold	**% of All ShrHldr Proposals**
361	58.7%
ShrHldr Proposals Voted Abstain	**% of All ShrHldr Proposals**
0	NA
ShrHldr Proposals With No Votes Cast	**% of All ShrHldr Proposals**
12	2.0%

TAB 8 – ANNUAL AUDIT UPDATE

Office of the State Treasurer
Audits Update

Purpose
To provide the Oregon Investment Council with an update of the investment-related audit engagements completed by OST's Internal Audit Services during the past year.

Background
Oregon Revised Statute (ORS) 293.776 states "The Oregon Investment Council shall provide for an examination and audit of the investment funds investment program, and for submission to the council of a report based on the examination and audit, at least once every four years and at other times as the council may require. The examination and audit, and the report based thereon, shall include an evaluation of current investment funds investment policies and practices and of specific investments of the investment funds in relation to the objective set forth in ORS 293.721, the standard set forth in ORS 293.726 and other criteria as may be appropriate, and recommendations relating to the investment funds investment policies and practices and to specific investments of the investment funds as are considered necessary or desirable. The council shall make copies of the report or a summary thereof available for distribution to interested persons."

Investment Policy 04.01.12 addresses this requirement as follows:

> <u>On an annual basis:</u>
> The Office of the State Treasurer's Internal Audit Services will perform an audit of the internal control structure over one of the major asset classes (i.e., Real Estate, Fixed Income, Public Equities, Private Equities, Opportunity Portfolio, or Short-term Investments) for each year ended June 30. The audit shall be performed in accordance with professional auditor's standards approved by OST's Audit Committee.
>
> <u>At least once every four years:</u>
> The Office of the State Treasurer (OST) will obtain the services of a qualified consultant to perform a procedural (operational) review of the investment portfolio (or area) and its practices as compared and contrasted to the investment portfolio practices of similarly managed investments in the private and public sectors.

Annual Internal Control Audits
Beginning with fiscal year 1993, OST began a process of annually reviewing the internal controls of one of the major assets classes. The reviews performed to date are summarized below:

Year Ended	Area	Firm
June-1993	Equities	KPMG
June-1994	Real Estate	KPMG
June-1995	OSTF	KPMG
June-1996	Fixed Income	KPMG
June-1997	Alternative Equities	KPMG

June-1998	Equities	Deloitte & Touche
June-1999	Real Estate	Deloitte & Touche
June-2000	OSTF	Deloitte & Touche
June-2001	Fixed Income	Deloitte & Touche
June-2002	Alternative Equities	Deloitte & Touche
June-2003	Public Equities	Internal Audit Services
June-2004	Real Estate	Internal Audit Services
June-2005	Short Term/Fixed Income	Internal Audit Services
June-2006	Private Equity	Internal Audit Services
June-2007	Real Estate	Internal Audit Services
June-2008	Public Equities	Internal Audit Services
June-2009	Short Term/Fixed Income	Internal Audit Services
June-2009	Opportunity Portfolio	Internal Audit Services

The Short Term & Fixed Income Portfolios Internal Controls Audit report was issued by Internal Audit Services on January 26, 2010. A total of 16 findings were identified during this engagement.

The Opportunity Portfolio Internal Controls Audit report was issued by Internal Audit Services on November 5, 2009. A total of five findings were identified during this engagement.

Other Investment-Related Audit Engagements

The Office of the Secretary of State Audits Division issued a management letter addressing their review of internal controls over financial reporting for the Oregon State Treasury for the year ended June 30, 2009, on February 23, 2010. OST staff have resolved the prior audit finding noted within this letter, and expect to complete work for the current audit finding by the end of the calendar year.

Recommendation

None

TAB 9 – ASSET ALLOCATIONS & NAV UPDATES

Asset Allocations at June 30, 2010

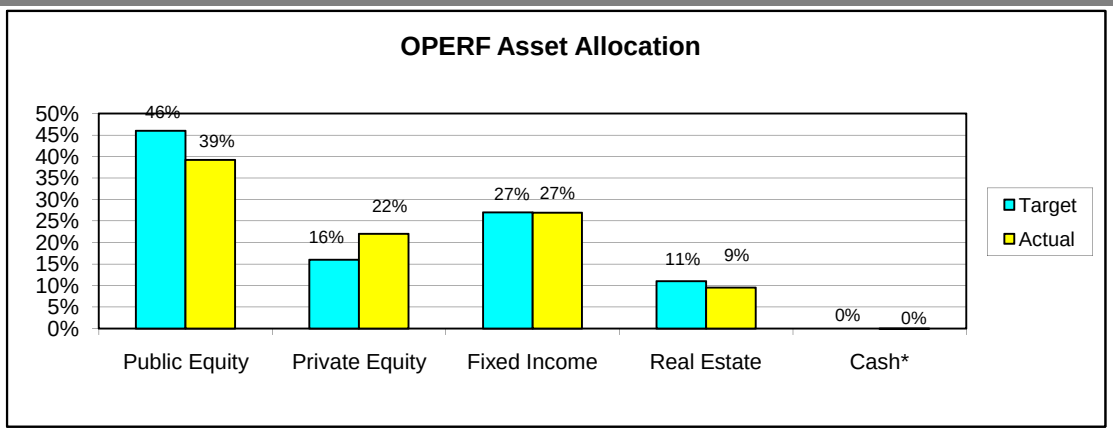
OPERF	Policy	Target	Regular Account $ Thousands	Pre-Overlay	Overlay	Net Position	Actual	Variable Fund $ Thousands	Total Fund $ Thousands
Public Equity	41-51%	46%	18,896,644	37.7%	771,089	19,667,733	39.2%	809,303	20,477,036
Private Equity	12-20%	16%	11,066,890	22.1%		11,066,890	22.1%		11,066,890
Total Equity	**57-67%**	**62%**	**29,963,534**	**59.7%**	**771,089**	**30,734,623**	**61.3%**		**31,543,926**
Opportunity Portfolio			1,138,791	2.3%		1,138,791	2.3%		1,138,791
Fixed Income	**22-32%**	**27%**	**13,267,529**	26.5%	**251,470**	**13,518,999**	27.0%		**13,518,999**
Real Estate	**8-14%**	**11%**	**4,765,053**	9.5%		**4,765,053**	9.5%		**4,765,053**
Cash*	**0-3%**	**0%**	**1,025,775**	2.0%	**(1,022,559)**	**3,216**	0.0%	8,531	**11,747**
TOTAL OPERF		**100%**	**$ 50,160,682**	**100.0%**	**$ -**	**$ 50,160,682**	**100.0%**	**$ 817,834**	**$ 50,978,516**

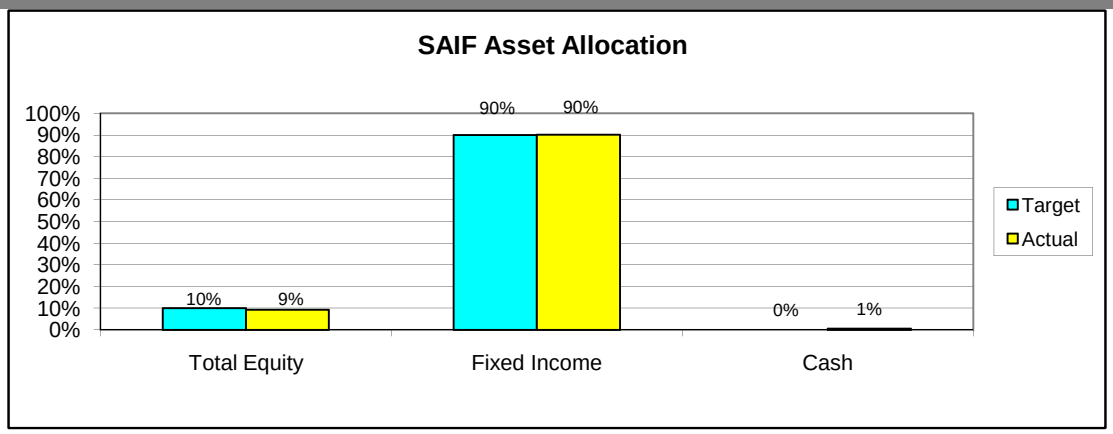
*Includes cash held in the policy implementation overlay program.

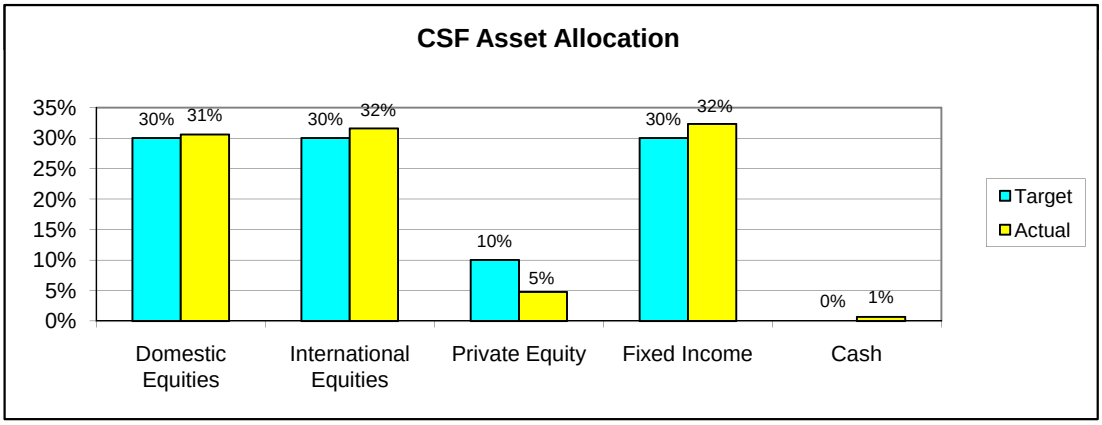
SAIF	Policy	Target	$ Thousands	Actual
Total Equity	**7-13%**	**10.0%**	**373,873**	**9.2%**
Fixed Income	**87-93%**	**90.0%**	**3,644,140**	**90.1%**
Cash	**0-3%**	**0%**	**26,171**	**0.6%**
TOTAL SAIF		**100%**	**$4,044,184**	**100.0%**

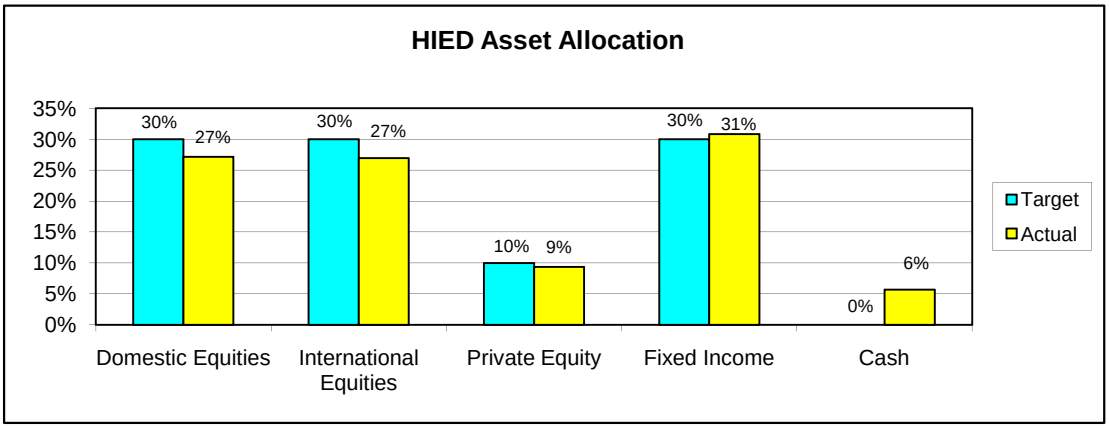
CSF	Policy	Target	$ Thousands	Actual
Domestic Equities	25-35%	30%	$281,017	30.6%
International Equities	25-35%	30%	290,189	31.6%
Private Equity	0-12%	10%	43,899	4.8%
Total Equity	**65-75%**	**70%**	**615,105**	**67.0%**
Fixed Income	**25-35%**	**30%**	**296,867**	**32.3%**
Cash	**0-3%**	**0%**	**6,263**	**0.7%**
TOTAL CSF			**$918,235**	**100.0%**

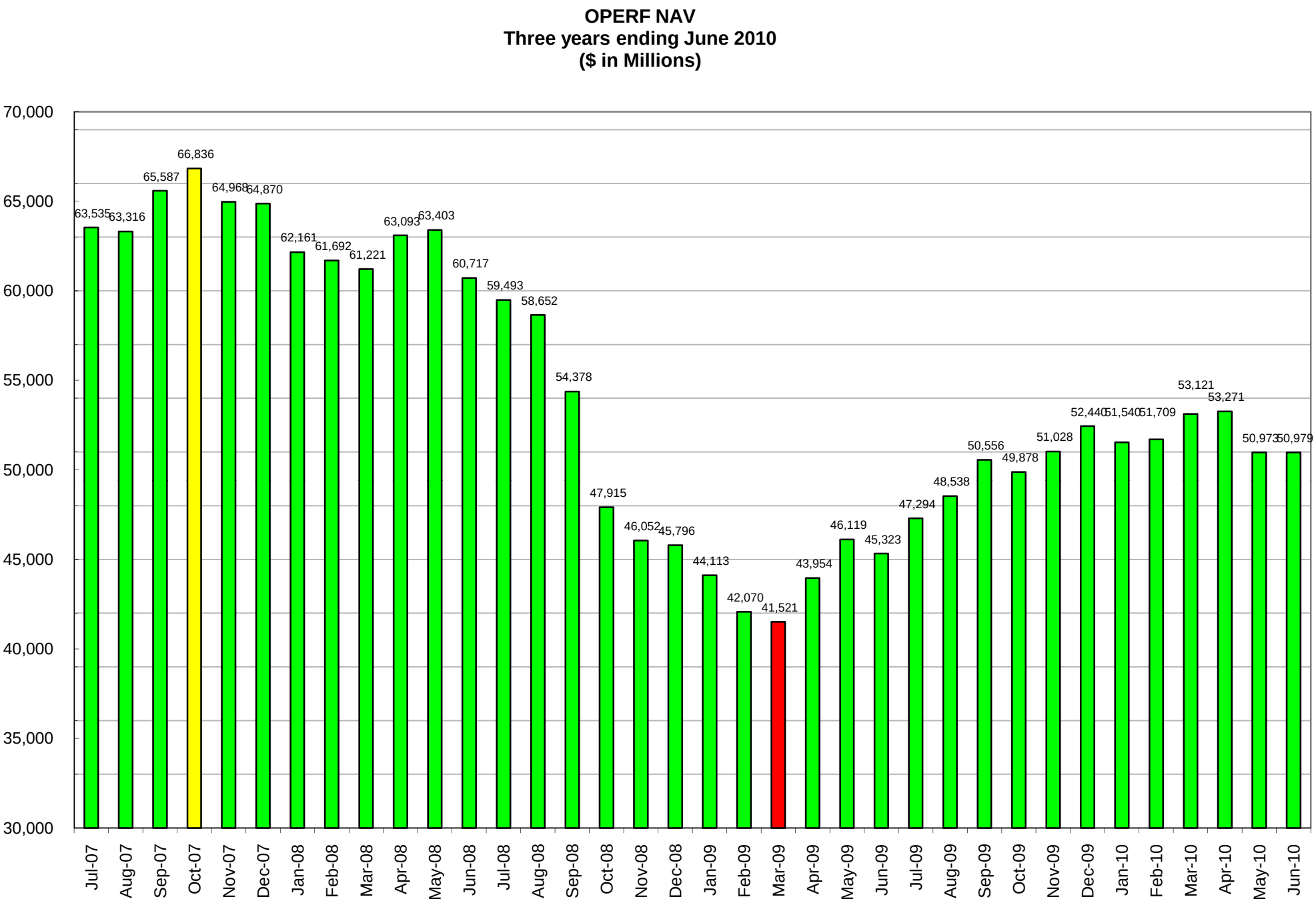
HIED	Policy	Target	$ Thousands	Actual
Domestic Equities	25-35%	30%	$16,217	27.2%
International Equities	25-35%	30%	16,098	27.0%
Private Equity	0-10%	10%	5,598	9.4%
Total Equity	**65-75%**	**70%**	**37,913**	**63.5%**
Fixed Income	**25-35%**	**30%**	**18,387**	**30.8%**
Cash	**0-3%**	**0%**	**3,410**	**5.7%**
TOTAL HIED			**$59,710**	**100.0%**

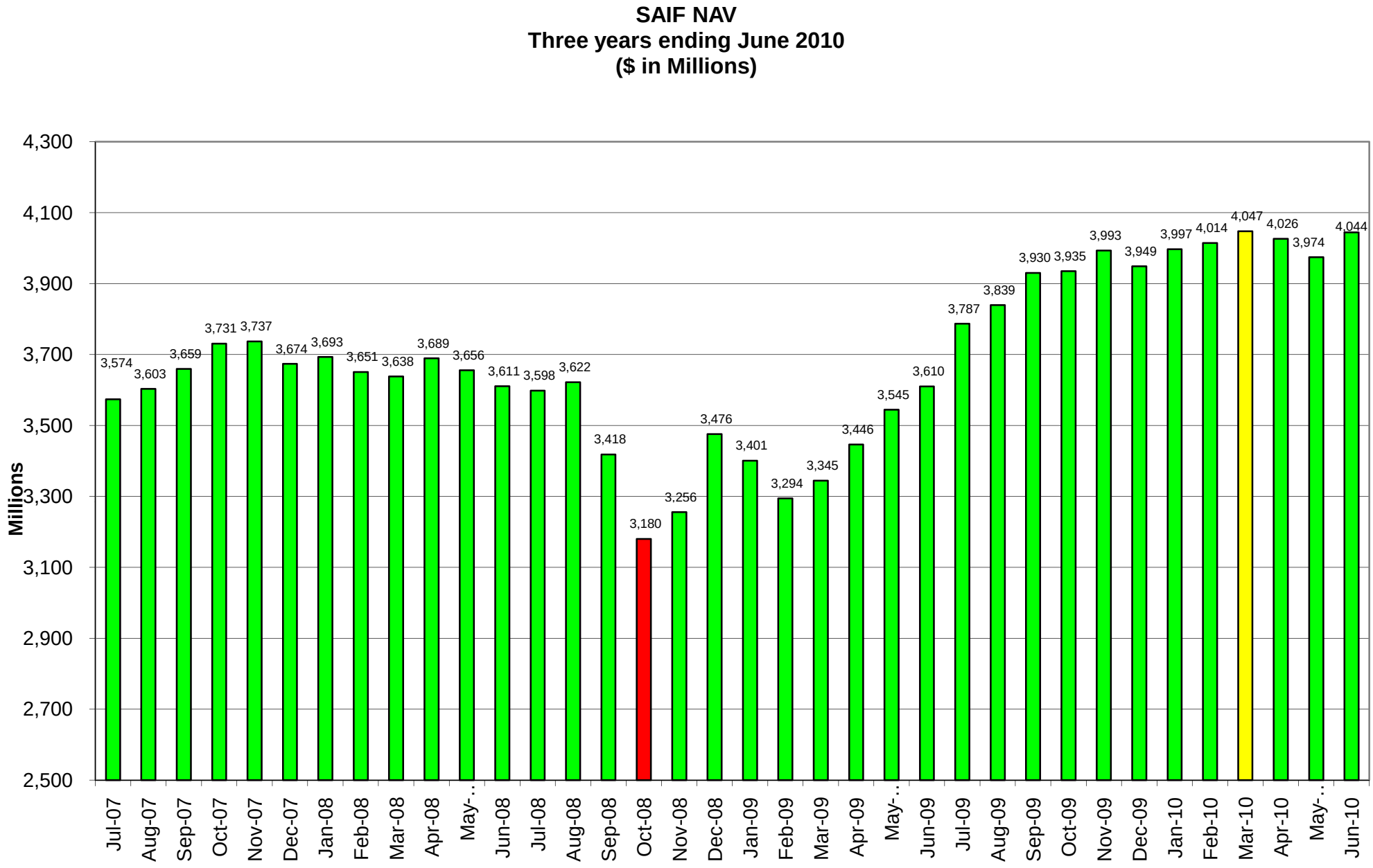

OPERF Asset Allocation
50%
45%
40%
35%
30%
25%
20%
15%
10%
5%
0%
46%
39%
16%
22%
27%
27%
11%
9%
0%
0%
Public Equity
Private Equity
Fixed Income
Real Estate
Cash*
Target
Actual

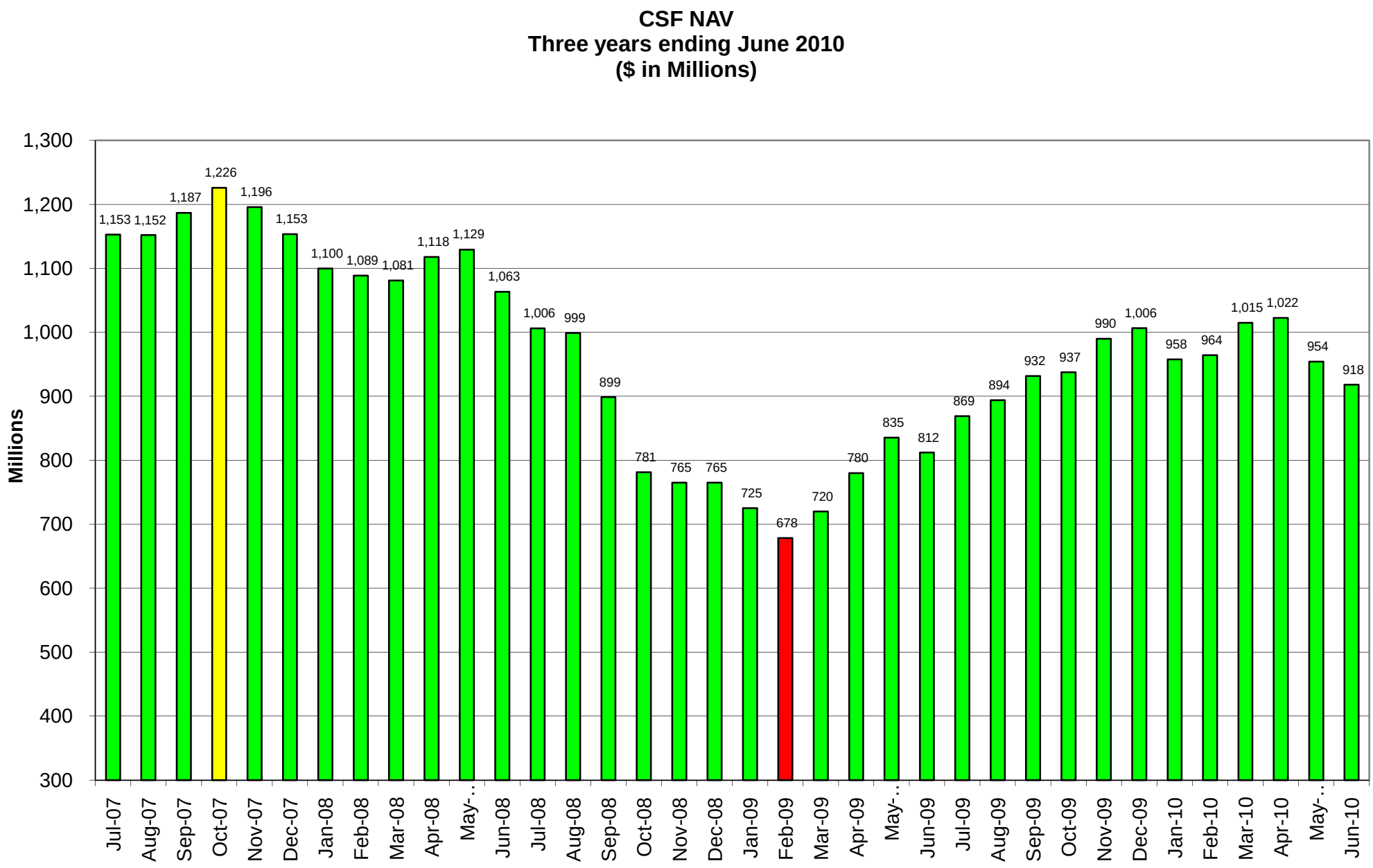

SAIF Asset Allocation
100%
90%
80%
70%
60%
50%
40%
30%
20%
10%
0%
10%
9%
90%
90%
0%
1%
Total Equity
Fixed Income
Cash
Target
Actual


CSF Asset Allocation
35%
30%
25%
20%
15%
10%
5%
0%
30%
31%
30%
32%
10%
5%
30%
32%
0%
1%
Domestic Equities
International Equities
Private Equity
Fixed Income
Cash
Target
Actual


HIED Asset Allocation
35%
30%
25%
20%
15%
10%
5%
0%
30%
27%
30%
27%
10%
9%
30%
31%
0%
6%
Domestic Equities
International Equities
Private Equity
Fixed Income
Cash
Target
Actual


OPERF NAV
Three years ending June 2010
($ in Millions)
70,000
65,000
60,000
55,000
50,000
45,000
40,000
35,000
30,000
63,535
63,316
65,587
66,836
64,968
64,870
62,161
61,692
61,221
63,093
63,403
60,717
59,493
58,652
54,378
47,915
46,052
45,796
44,113
42,070
41,521
43,954
46,119
45,323
47,294
48,538
50,556
49,878
51,028
52,440
51,540
51,709
53,121
53,271
50,973
50,979
Jul-07
Aug-07
Sep-07
Oct-07
Nov-07
Dec-07
Jan-08
Feb-08
Mar-08
Apr-08
May-08
Jun-08
Jul-08
Aug-08
Sep-08
Oct-08
Nov-08
Dec-08
Jan-09
Feb-09
Mar-09
Apr-09
May-09
Jun-09
Jul-09
Aug-09
Sep-09
Oct-09
Nov-09
Dec-09
Jan-10
Feb-10
Mar-10
Apr-10
May-10
Jun-10


SAIF NAV
Three years ending June 2010
($ in Millions)
Millions
4,300
4,100
3,900
3,700
3,500
3,300
3,100
2,900
2,700
2,500
3,574
3,603
3,659
3,731
3,737
3,674
3,693
3,651
3,638
3,689
3,656
3,611
3,598
3,622
3,418
3,180
3,256
3,476
3,401
3,294
3,345
3,446
3,545
3,610
3,787
3,839
3,930
3,935
3,993
3,949
3,997
4,014
4,047
4,026
3,974
4,044
Jul-07
Aug-07
Sep-07
Oct-07
Nov-07
Dec-07
Jan-08
Feb-08
Mar-08
Apr-08
May-...
Jun-08
Jul-08
Aug-08
Sep-08
Oct-08
Nov-08
Dec-08
Jan-09
Feb-09
Mar-09
Apr-09
May-...
Jun-09
Jul-09
Aug-09
Sep-09
Oct-09
Nov-09
Dec-09
Jan-10
Feb-10
Mar-10
Apr-10
May-...
Jun-10


CSF NAV
Three years ending June 2010
($ in Millions)
Millions
1,300
1,200
1,100
1,000
900
800
700
600
500
400
300
1,153
1,152
1,187
1,226
1,196
1,153
1,100
1,089
1,081
1,118
1,129
1,063
1,006
999
899
781
765
765
725
678
720
780
835
812
869
894
932
937
990
1,006
958
964
1,015
1,022
954
918
Jul-07
Aug-07
Sep-07
Oct-07
Nov-07
Dec-07
Jan-08
Feb-08
Mar-08
Apr-08
May-...
Jun-08
Jul-08
Aug-08
Sep-08
Oct-08
Nov-08
Dec-08
Jan-09
Feb-09
Mar-09
Apr-09
May-...
Jun-09
Jul-09
Aug-09
Sep-09
Oct-09
Nov-09
Dec-09
Jan-10
Feb-10
Mar-10
Apr-10
May-...
Jun-10

TAB 10 – CALENDAR – FUTURE AGENDA ITEMS

2010 OIC Forward Agenda Topics

September 29:	CEM Annual Review CSF Annual Review Passive/Active Analysis & OPERF Equity Attribution
October 27:	OPERF Opportunity Portfolio Annual Plan General Consultant Review
December 1:	OPERF 3rd Quarter Performance Review HIED Annual Review