

LFC HEARING BRIEF

BACKGROUND INFORMATION

AGENCIES: SIC, PERA, ERB

DATE: April 22, 2008

PURPOSE OF HEARING:
**Polices and Procedures
Relating to Alternative
Investments**

WITNESS: Allan Martin,
New England Pension
Consultants (NEPC); Steve
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Lewis, State Treasurer;
Gary Bland, State
Investment Officer; Robert
Gish, PERA Investment
Officer; Robert Jacksha,
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OUTCOME:
**Assessment of Investment
Agency Due Diligence**

***Alternative investments
are designed to have a
low correlation with
traditional equity and
fixed income
investments. This lowers
the volatility and
increases the long term
return.***

Recent Wall Street woes -- including the demise of the hedge fund giant, Amaranth; the sub-prime crisis with its devastating impact on such firms as Wachovia and Thornburg, leading to the collapse and buy-out of Bear-Stearns; and the continuing turmoil in credit markets with its various impacts (such as the difficulty of private equity firms to borrow money to fund deals) -- point to a dramatic shift in the capital markets at a time when the New Mexico permanent funds are diversifying out of traditional investments. The past six months have illustrated the need for continued vigilance on the part of the state's investing agencies as many "safe" investments have been exposed for undue and irresponsible risk taking. Thus, reviewing the policies and procedures the agencies have developed to mitigate risk as they deploy into other types of investments has become even more relevant and timely. Based on discussions with LFC staff, all of the investing agencies have responsible policies and procedures established with layers of monitoring to protect the state's money.

Prudent Investor Act. Since the passage of the "Prudent Investor Act" in 2005, agencies responsible for investing pension and permanent funds—State Investment Council (SIC), Public Employees Retirement Association (PERA) and Education Retirement Board (ERB)—have initiated or expanded investments in non-traditional or alternative investments in order to optimize returns and reduce risk. Principally, these investments are in hedge funds, real estate or real assets, and private equity. SIC has also made "economically targeted investments (ETI)" that invest capital in New Mexico entities. These investments, made from the severance tax permanent fund (STPF), have a competing goal of economic development in addition to return on investment. As of 12/31/07, ETI's represented 5.4 percent of the STPF portfolio. Table 1 highlights the types of alternatives currently held by the agency portfolios.

As can be seen in the Chart 1, adding alternatives improves the risk/return potential by moving the "efficient frontier" (a line depicting expected returns for various portfolio combinations of investments) upward from the traditional-only mix. For example, at a 10 percent risk level, the first line (stocks and bonds) yields about 7 percent while the line with portable alpha yields about 9 percent: same risk, higher return. This power of diversification occurs due to assets moving in different directions or degrees, often depicted in correlation charts (see Attachment A).

Alternative investments and other strategies that strive to achieve “alpha”—or non-market returns—are becoming increasingly important to pension funds because traditional assets no longer provide an investment return required to meet actuarial assumptions.

The actuarial assumption for both ERB and PERA is 8 percent. SIC has a target return of 8.5 percent.

Layers of Outside Expertise:

- General consultant
- Specialized consultant
- Fund manager
- Fund-of-funds manager
- Third party evaluations
- Outside legal counsel
- Actuary

The general consultants played an important role in developing the overall strategy for deployment into alternatives, including selecting the alternative advisors, and continue to play a key role as part of monitoring process for the entire portfolios.

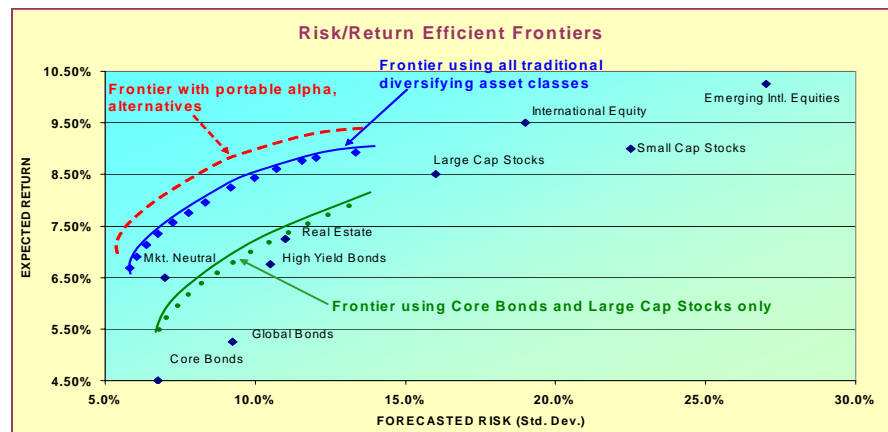
ERB has hired a separate advisor for each alternative asset class while PERA has selected one advisor to coordinate the entire alternative portfolio.

Table 1: Current Portfolios as of 12/31/07

	SIC	PERA	ERB
Large Cap Equity	x	x	x
Small/Mid Cap Equity	x	x	x
International Equity - Developed	x	x	x
International Equity - Emerging	x	x	x
Core Fixed Income	x	x	x
High Yield Fixed Income		x	x
Credit and Structured Finance	x		
Alternatives { Private Equity	x	x	x
Hedge Funds	x	x	x
Real Estate, Real Assets	x	x	x
Economically Targeted Investments	x		

However, while providing a potential for higher returns, these new asset classes introduce new risks because many alternative investments are not subject to the same scrutiny and regulations that govern traditional equity and fixed income investments. In addition, alternative investments involve unique tracking issues, including lagged reporting, valuation, and proper benchmarking. Rebalancing can also pose a challenge because of the constraints posed by varying degrees of liquidity and entrance restraints. Thus, as the alternative portfolios grow, knowing how—and how well—the agencies choose, monitor and adjust these investments to mitigate risk becomes critical for adequate oversight.

Chart 1



BEST PRACTICES TO REDUCE RISK

How the agencies approach and execute their alternative programs can be assessed against best practices that have been identified by the

**ERB's
Consultant/Advisor
Selection**

Staff:

- Draft, issue and administer RFP
- Provide information and analysis to Investment Committee
- Execute contracts

Investment Committee:

- Review information provided by staff and potential service providers, usually including in-person presentations
- Select service providers by committee vote
- Make recommendation to the Board

Board

- Review and vote on Investment Committee recommendation

Steps to implementing the alternative assets strategy:

- Portfolio building and asset allocation
- Portfolio reconfiguration
- Identifying potential investments
- Due diligence
- Negotiation
- Performance monitoring
- Risk monitoring
- Termination/exit as necessary and feasible

industry. Overall, the agencies appear to be effectively developing their alternative platforms, as the following examples indicate. A few weaknesses are also noted.

Expertise. First and foremost is obtaining the expertise necessary to navigate this new territory, which includes hiring outside consultants as well as building staff for analysis, accounting and monitoring. Table 2 identifies the outside consultants for each agency. Appendix B provides additional information on the alternative consultants, which portray an impressive array of knowledge and experience in the arena.

While the alternative consultant(s) take the lead regarding alternatives, the general consultant will often “weigh-in” on strategies, providing another voice in the decision making and monitoring processes. As an example, PERA’s general consultant (RVKhuns) took a strong position in favor of a fund of fund approach (a fund that manages a portfolio of hedge funds) for investing in hedge funds in opposition to Cliffwater’s direct approach. The extended debate provided a unique opportunity for the PERA board to be more knowledgeable regarding its actions.

Table 2 – Investment Advisors

Agency	Consultant	Asset Class
ERB	NEPC	General Consultant
	NEPC	Hedge Funds
	Aldus	Private Equity
	ORG	Real Estate & Real Assets
	Courtland	Infrastructure
PERA	RVKhuns	General Consultant
	Cliffwater	All Alternatives
SIC	NEPC	General Consultant
	NEPC	Hedge Funds
	Aldus	Private Equity – National Program
	Sun Mountain Capital	NM Private Equity
	Courtland	Real estate

All agencies follow a similar advisor selection process as noted for ERB in the sidebar, starting with a Request for Proposal (RFP) initiated by staff, followed by a thorough vetting process by the agency’s Investment Committee, and finalized by Board approval. Providing entrée into the best opportunities is the primary value an alternative consultant brings, although the agencies do not rely solely on the advisors to source deals. The agencies report satisfaction with their alternative consultants.

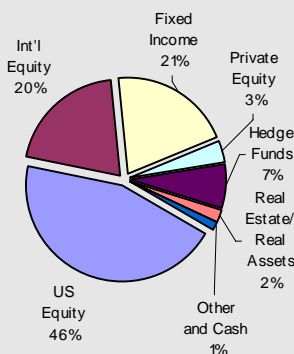
Survey of public plans:

- 25 responded
- 9 have formal education policy
- 6 have mandatory educational requirements
- 1 has a mandatory certification program

Source: Governing October 2007

Subjecting the investing agencies to the Prudent Investor Act eliminated the need for a “legal list.” a menu of allowable investment options. Now all agencies can invest in virtually any asset so long as it meets the prudent investor standard and fits the agency’s policies. This shift from traditional assets naturally increased the required sophistication of those responsible for choosing investments and advisors, monitoring portfolios, and assessing risks.

**Allocation of State of
New Mexico
Combined Funds**



The investment committees also greatly rely on investment staff for expertise. However, as the alternative investments have ramped up, so has the workload, stretching current resources thin. Both ERB and PERA have requested and received additional staff but SIC admits that the agency missed its opportunity to add needed staff for FY09. Agency staff is listed as part of Appendix B.

Finally, PERA and ERB are also striving to develop expertise on their boards through regular presentations and annual retreats that focus on investments. Attending conferences is also encouraged; a sample of PERA’s approved conference list is included as Appendix C. ERB and SIC can benefit from having common board members that “cross-pollinate” expertise. Gary Bland, State Investment Officer for SIC, is also on the ERB board as a governor-appointee while State Treasurer James Lewis sits on all three boards. However, importing investment decisions from one agency to another can also present a weakness, as the losses incurred from collateralized debt obligations (CDO’s) for SIC and ERB demonstrate. It may also represent a reduction in diversification across all state funds. Finally, recent governance reforms in other states to require annual certifications for board members or minimum requirements have not been adopted in New Mexico.

Asset Allocation--Portfolio. Each agency has developed a policy for asset allocation, an established mix of investments within specified ranges. Long acknowledged as the single most important decision made by those who oversee the funds, asset allocation yields higher returns and/or lower risks through diversification as seen by the efficient frontier model presented above. The recent modification to this theme, which has become a best practice developed first by large endowment funds and later through the larger public pension plans, has been broadening the concept of diversification by broadening the types of assets included in portfolios that are more or less uncorrelated. This concept of “inoculating” portfolios to withstand all types of market events through increased diversification supersedes the prior practice of tactical allocation policy – or defensive positioning by underweighting an asset class – which PERA took for equities during the 2000-2002 market downturn to preserve capital.

All agencies are pursuing this best practice of greater diversification due to the Prudent Investor Act; the problem is that it takes time to implement. SIC has had alternatives, such as private equity and hedge funds, on its “legal list,” the allowable investments prior to the Prudent Investor Act, and so has a longer history with some asset classes. PERA and ERB were only recently allowed to invest according to the Prudent Investor Act and it took almost a year for the

Asset Allocation

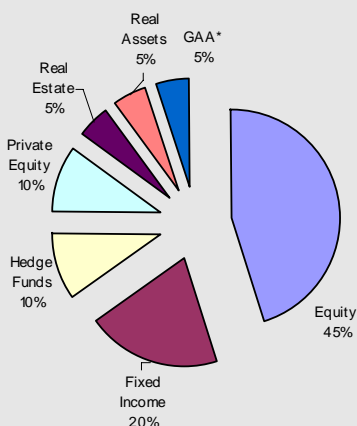
- Annual Asset Allocation Study using expected asset returns and risk, as measured by standard deviation (see sample in Appendix D).
- Asset-Liability studies periodically performed to assess appropriateness of current asset allocation relative to the expected progress of liabilities and cash flows

Independent Sources of Information – A Best Practice

ERB and PERA Boards receive independent sources of information from:

- External auditor
- Investment consultant
- Actuary

ERB Asset Allocation 35% Alternatives



*Global Asset Allocation

Source: ERB

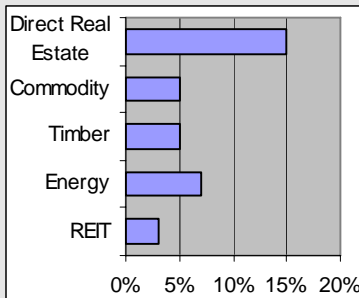
agencies to plan their strategies. Thus, both agencies are caught in an awkward “ramp-up” phase that fails to fully capture the effect of adding alternatives.

The current volatile market environment has highlighted the need for diversification of assets. SIC has a more mature asset allocation and so weathered the financial market storm to some extent, but because ERB and PERA do not have full deployment into alternatives, they faced the full brunt of the equities decline. SIC has also initiated a defensive strategy to preserve capital allocated to the domestic equity class using derivatives, described more fully in the last section of the brief. Neither ERB nor PERA is being encouraged by their consultants to employ a similar defensive strategy during this market correction.

Table 3 details the asset allocations for each agency as of December 31, 2007. ERB and PERA targets for the private equity and real estate/real assets are transitional because of the long deployment period for some assets, particularly private equity and real assets or real estate. These targets will be adjusted upward as the agencies progress in these programs to match the long term targets of 15 percent for PERA and 35 percent for ERB. Just how powerful asset allocation becomes over the long term was illustrated by a study recently performed by PERA’s general consultant that showed if PERA had been fully invested in its alternative mandates since January 2003 (the same as their top performing peers), five-year performance would have improved by a hypothetical 245 basis points.

SIC has recently increased the targets to alternatives. Legislation passed in 2007 increased the cap on private equity investments in New Mexico from 6 percent to 9 percent for the Severance Tax Permanent Fund (STPF). The council also recently raised the target allocation for STPF and the land grant permanent fund (LGPF) to hedge funds to 15 percent. This will raise the allocation to alternatives for STPF to over 30 percent and for LGPF to 24 percent. Table 3 below does not reflect these new targets.

Cliffwater's Real Asset Sample Allocation



Source: May 2006 PERA Retreat

Pension Reform in U.S.

- Ohio: increased education and training of board members
- Arizona: clarified the roles and reduced the diverse responsibilities placed on the board
- Maryland: requires all board members to receive at least 8 hours of investment and fiduciary training annually
- Illinois: adopted restrictions and disclosure requirements to prevent kickbacks
- San Diego: replaced some positions designated for active and retired employees with individuals with financial expertise
- California: halted business dealings with two investment firms that had made sizeable contributions to the governor and other elected officials and limited contributions to \$5,000

Source: *Governing*, October 2007

Table 3
Fund Asset Allocation Detail, Quarter Ending December 31, 2007

	ERB*		PERA		LGPF		STPF	
	Actual	Target	Actual	Target**	Actual	Target	Actual	Target
Total US Equity	37.6%	40.0%	41.5%	40.0%	52.2%	53.0%	52.0%	53.0%
International Equity	20.9%	20.0%	28.6%	25.0%	12.2%	10.0%	13.8%	10.0%
Total Fixed Income	27.5%	29.0%	25.1%	32.0%	16.3%	18.0%	4.9%	11.0%
Total Alternatives	12.8%	11.0%	4.5%	3.0%	19.1%	19.0%	29.3%	26.0%
Private Equity	0.5%	1.0%	0.4%		6.4%	6.0%	10.5%	12.0%
Hedge Funds	8.3%	5.0%	3.9%		9.6%	10.0%	9.5%	10.0%
Real Estate/Real Assets	4.0%	5.0%	0.2%		3.1%	3.0%	3.8%	3.0%
Economically Targeted Investments	0.0%	0.0%	0.0%	0.0%	-	0.0%	5.4%	0.0%
Cash Equivalents	1.2%	0.0%	0.8%	0.0%	0.2%	0.0%	0.2%	0.0%
Total Fund %	100%	100%	100%	100%	100%	100%	100%	100%

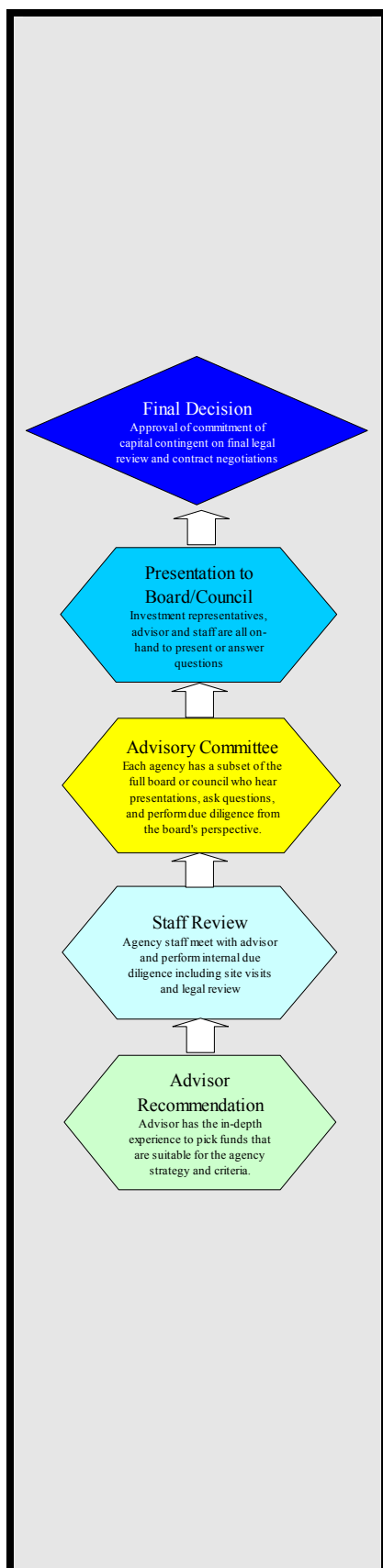
*ERB is adopting a new asset allocation mix that will raise the commitment to alternatives to 35% and correspondingly reduce equity and fixed income asset classes. See [Current Issues](#) section for more detail.

**Due to the long implementation period for some alternatives, both PERA and ERB targets for some alternatives will be increased over time to match the long term targets.

Each agency reviews its asset allocation policy annually and makes adjustments based on market expectations to maximize returns along the efficient frontier, given risk tolerance and policy or statutory constraints. For example, beginning in 2005, PERA moved from a 35 percent fixed income policy to a portfolio overweighting international equities. After the passage of the Prudent Investor Act, both ERB and PERA developed new asset allocations totaling 15 percent to the alternative asset classes. More recently, ERB has moved its long term alternative target to 35 percent as shown in the sidebar. This asset allocation is expected to bring a 8.49 percent long term return with lower expected risk than the current portfolio mix, as shown as Mix A in Appendix D.

Asset Allocation—Alternatives. Diversifying within each alternative class is also essential to optimize the risk/return ratio. Each asset class is characterized by specific diversifying elements, such as by vintage year and type for private equity. All agencies are following this best practice, exemplified by PERA's hedge fund (or absolute return) portfolio presented as Appendix E. In addition, all agencies have established work plans that deploy assets in a pre-planned way to ensure adherence to the portfolio reconfiguration designed by the alternative advisors and staff. A sample SIC work plan from Aldus Equities is included as Appendix F. Finally, SIC employs a "completion fund" in its hedge fund portfolio that allows the agency to make adjustments if it finds too much of an exposure concentrated in its other hedge funds, allowing it to diversify away from that exposure.

Investment Selection. Investing in alternative assets is very labor intensive; all agencies reported that this minority portion of their



portfolios is requiring the majority of their time. As the flowchart in the sidebar indicates, investment selection goes far beyond choosing a manager for a traditional investment, which becomes essentially a matter of issuing a RFP and evaluating responses.

For private equity, the starting point is with the investment advisor—Aldus for ERB and SIC, Cliffwater for PERA—who has the range of experience and expertise to vet different funds. The advisor knows two important things: the agency's strategy and the allocation targets. In this case the allocation targets would be within an asset class. For example, within private equity, there are venture capital funds, leveraged buyout funds, and distressed asset funds, to name just a few; each agency will look to diversify inside the asset class. The advisor knows the current allocation and will not recommend funds that do not fit into the plan.

The second step is staff review. The staff meets frequently with the investment advisor and considers recommendations. In some cases, the staff will know about a fund and ask for the advisor's analysis or opinion. The amount of staff time required for fully assessing assets like private equity funds is considerably more than is required for traditional asset managers like domestic equity. Since the investment is long term and the fees begin right away, the staff has to be comfortable with the managers, the experience, past funds' performance, the strategy of the fund, and the legal considerations as well as the fees and potential return. The staff must visit the headquarters and meet all of the principals, and the general counsel has to oversee the legal review of what ends up being hundreds of pages of contract language. PERA also reports that their general investment advisor will, if requested, assess the prospective investment fund.

Following the staff review, the fund will come before the advisory committee. Each agency has an advisory committee with different compositions and roles. See appendix B for the details for each agency. The advisory or investment committee will hear presentations from the advisor and representatives from the fund being considered. Agency staff is also on hand to answer any questions from the staff point of view and often presents a staff memo recommending or not recommending the investment, and why. (See Appendix G for a recent PERA memo.) The investment committee will then recommend the investment to the full board/council if it conforms with the agency's guidelines and strategy and the committee is satisfied with the presentation.

Both ERB and SIC report that 85%-90% their hedge funds are “marked to the market” daily.

Hedge Fund Reporting for PERA:

- *Weekly estimates*
- *Monthly reports on the 5th or 6th business day*
- *Public reporting lagged 1 month to protect strategies*
- *3rd party pricing*

How ERB increases its monitoring capacity to “touch the data” for limited partnerships:

- Sit on advisory boards
- Quarterly conference with general partner
- Watch money deployment-question if drawdown is not proceeding
- Watch cash flow
- Annual write-ups on portfolio
- Regular reviews with advisor
- Review annual audit

Examples of Private Equity Investments

- ***Eclipse Aviation is one of SIC’s investments that looks like it has the potential for high return.***
- ***TCI Medical has shut down, evaporating over \$7 million in SIC investments.***

The full board/council makes the final decision after hearing from the advisory committee, the staff, and the investment advisor. The representatives may or may not make a presentation. The decision to commit funds is always contingent on legal review and final contract negotiations. Once the details have been worked out, the approved fund can begin drawing money out and charging management fees.

Due Diligence. Completing the extensive due diligence for a potential deal is the most important function an alternative advisor performs, particularly in the less liquid investments. While confidential, LFC staff has reviewed due diligence reports from each of the consultants and has found them to be comprehensive, covering weaknesses as well as strengths and clearly specifying how the investment fits into the overall strategy of diversification within the asset class. Aldus reports, in particular, review these issues extensively in a user-friendly format. Appendix H outlines the items Aldus looks at and reports on when making a recommendation.

Oversight. Last year, the Public Finance Management Group (PFM Group) completed a review of tracking alternative investments and concluded that the state uses an acceptable methodology for valuing real estate. It underscored the following for other investment types:

- The importance of having specialized consultants for hedge funds, due to this investment’s complex nature.
- That decreased transparency of fees and practices, as well as documented fraudulent activity, makes due diligence a critical aspect of oversight.
- Using appropriate benchmarks, while difficult, is essential for tracking performance.

The report concluded, “While riskier, less transparent, and less liquid than more traditional asset classes, alternative investments can offer pension funds higher returns when handled with care.”

Monitoring. Alternatives are less transparent than publicly traded investments because there is no published information on most of the funds. Oversight is very difficult even for the agency which has access to confidential information. There is a spectrum of transparency beginning with hedge funds, which can report credible market values with high frequency, to private equity funds – particularly venture capital – where the real value may never be known until there is an exit (sale or going public).

All of the agencies reported to LFC that they are able to get reliable information about the valuation of their hedge funds on a monthly basis and that there is third party valuation every quarter. Annual

“It appears that Investment staff is doing what it can to keep up to date with market valuations...Since these assets are not reported on any exchange, actual values for these alternative investments cannot really be determined exactly until the assets are sold sometime in the future.”

-- PERA Internal Audit of Alternative Investment Transactions #08-03-11-301-001

Cliffwater maintains that hedge funds are not as liquid as many believe but allocations can be changed much easier than for private equity and real estate.

audits are also performed. While not a daily indication like a publicly traded stock, the reporting is sufficient to know the trends and carefully watch the funds' performance. As Deputy State Investment Officer Adam Levine reported to LFC staff, valuation is sometimes meaningless if you have a long-term strategy: the value today is really only relevant if you need to sell it *today*.

For real estate and real assets, there is a highly evolved appraisal industry that can independently evaluate investments. All of the investments are subject to third party review and valuation and reporting is quarterly. These tend to be much longer term investments than hedge funds so swings in valuation due to the marketplace may not accurately value a specific investment.

Finally, private equity funds are the hardest to value with any frequency and any valuation is necessarily going to be arbitrary. This is less true for funds that purchase existing companies where there is track record and history but even then the fund is purchasing the company because its managers think they can substantially add value and so valuation based on the appraisal of the existing company will be underestimated. The value of an investment in a company is only realized when (a) the company fails and is liquidated or (b) the company is sold or taken public and the investors receive compensation. In (a), whatever the last valuation was, the current value may be near zero, depending on the value of assets sold in liquidation. In (b), the value could be significantly higher than any cost-based valuation. FASB 157 expanded the generally accepted accounting principles for reporting fair value for private equity, which may increase “data points” but the agencies conclude will remain inconclusive until the position is closed out.

Portfolio Adjustments and Termination/Exit Strategy. It is important for the agencies to have a clear termination or exit strategy in mind for each investment. All three agencies indicated a long term vision, or “wait and hold” strategy, for the investments most likely packaged as limited partnerships. In this regard, the upfront due diligence and selection process take on a whole new dimension of importance.

However, the agencies also cautioned that they monitor the investments for any red flags that would trigger, at the very least, a discussion with the general partners or fund manager. One such indication would be if the drawdown of the commitment appears to be lagging. Changes in management or “strategy drift” as well as poor performance are also closely monitored by staff and the consultants.

SIC is implementing a new risk program that will help optimize its portfolio in changing environments.

SIC has also started a hedge program on domestic equities using derivatives to protect against downside risk.

Put: the right to “sell” the index

Call: the right to “buy” the index

It was a lagging performance and an unreported change in management that led ERB to exit its investment in one of its hedge funds only after a few months. Generally, traditional managers are terminated under a longer-term policy, such as a PERA’s “watch list” where equity managers have to meet a three year underperformance. A termination policy for alternatives was not explicitly presented by any of the agencies; rather, the selection and monitoring process appear paramount and the agencies appear to rely on the advisors’ role as gatekeeper.

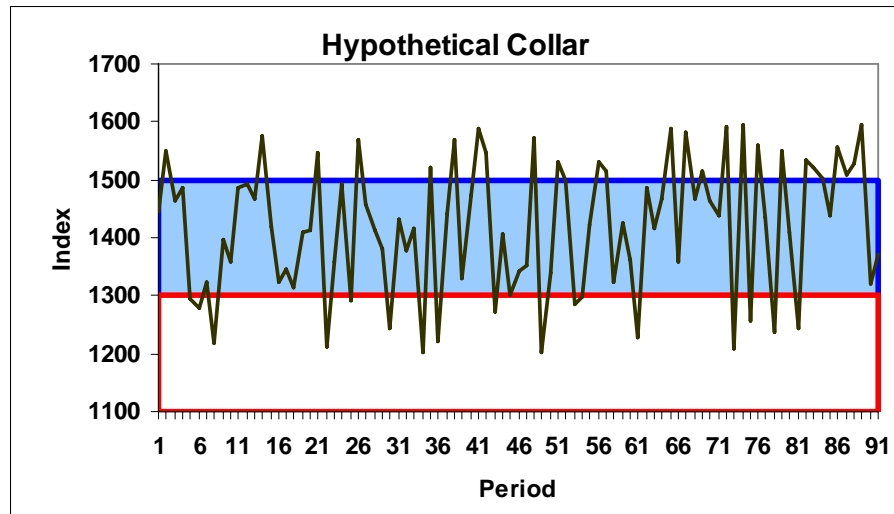
ADDITIONAL RISK MITIGATION STRATEGIES

The previous discussion has focused on ways to mitigate risk by diversifying, selecting managers, and adopting policies and procedures to make deliberative decisions. SIC has adopted two additional strategies to assess and mitigate risk. First, the agency is developing in-house expertise on “risk management,” a discipline that assesses the risk of the entire portfolio to internal and external factors. For example, in most cases investors look at the portfolio from the correlation matrix point of view and make decisions about diversification (the efficient frontier). This is addressing risk by looking for asymmetric return in diverse asset classes. What about the risk of inflation on the entire portfolio? Or an inverted yield curve? These types of macro issues are only indirectly addressed using the standard correlation matrix.

SIC is subscribing to a new modeling tool called Measurisk© that allows their entire portfolio to be loaded into a system where they can perform various scenarios to determine the appropriate asset allocation in changing economic environments. The agency is one of Measurisk’s first institutional clients, although they’ve provided risk tools for hedge fund managers for some time.

Derivatives. The second measure SIC has adopted is the use of hedge derivatives. At this point, SIC purchases puts and calls on the Standard and Poor’s 500 index to reduce the exposure to the broad domestic equity market volatility. As the program matures, SIC will consider hedging other asset classes to reduce exposure to volatility. The puts and calls create a range, or “collar,” of acceptable volatility. In the example below, a collar is purchased for a hypothetical index with a put at 1300 and a call at 1500.

SIC has instituted a “standard of care” clause in its legal investment documents that the agency hopes will become the industry standard to hold alternative investment firms to a higher standard for fiduciary responsibility and reporting commitments to investors.



The collar is set to minimize or eliminate the cost of purchasing the options. Since you buy a put as insurance and sell a call, there are two levels where the net effect is zero cost. The example shows that volatility is constrained to a range and so the investment does not receive the full benefit when the index goes above 1500 but it doesn't lose when the index declines below 1300. This is referred to “giving up the upside to protect the downside.” SIO Bland reports that the fund balance of SIC managed funds would be roughly \$1 billion higher if they had options in place last year when they planned to have a manager selected. However, negotiations took longer than expected and it took several months to finalize the current derivatives manager, First Quadrant. SIC has also updated its policy on the use of derivatives to make explicit that derivatives are only used to hedge risk and not for any speculative purpose.

QUESTIONS

What tools are available to the public, including the legislature, to monitor the investment agencies?

How do the agencies insure they are gaining access to the top fund managers?

How do board members process recommendations so that any misinformation is not acted upon?

Has an advisor recommended an investment that was not approved by staff? If so, why not and what was the outcome?

How does the past performance of the alternative investments hold up for future expectations?

How does the current economic environment affect the investment plans in real estate and private equity?

How does the lag time associated with valuing the new alternative classes affect reporting and the oversight function of the respective agency boards?

Does a policy exist for a termination report, similar to a procurement report?

There was an ad-hoc investment group made up of the three investing agencies. One of the recommendations was reporting on third party fees for asset managers. Has this been incorporated into the investment policy?

What steps does each agency take to reduce impacts from conflicts of interest?

NF:MA/bb

Appendix A

NEPC 2007 Asset Correlation Forecasts

	Large Cap Equities	Small/Mid Cap Equities	Int'l Equities	Int'l Small Cap Equities	Emerging Int'l Equities	Core Bonds	High-Yield Bonds	Bank Debt	EMD	Hedge Funds Cons	Private Equity	Real Estate	Real Assets	Infrastructure	GAA
Large Cap Equities	1.0000	0.8000	0.6000	0.4500	0.4000	0.2000	0.5000	0.6000	0.5000	0.2000	0.7500	0.0000	-0.2000	0.1500	0.0000
Small Cap Equities	0.8000	1.0000	0.5500	0.4500	0.4000	0.0000	0.6000	0.6000	0.5000	0.2000	0.8500	-0.0500	-0.2000	-0.1000	0.0000
Int'l Equities	0.6000	0.5500	1.0000	0.9000	0.5500	0.0000	0.3500	0.5000	0.5000	0.0500	0.5000	0.1000	0.3500	-0.2000	0.0000
Int'l Small Cap Equities	0.4500	0.4500	0.9000	1.0000	0.5000	0.0000	0.3000	0.5000	0.5000	0.0000	0.6000	0.0000	0.4000	-0.1000	-0.1000
Emerging Int'l Equities	0.4000	0.4000	0.5500	0.5000	1.0000	-0.2000	0.4000	0.4000	0.6000	0.0000	0.2500	-0.1000	0.2500	-0.1000	-0.1000
Core Bonds	0.2000	0.0000	0.0000	0.0000	-0.2000	1.0000	0.5000	-0.3000	0.0000	0.3500	0.1500	-0.1000	-0.1000	0.2500	0.7500
High-Yield Bonds	0.5000	0.6000	0.3500	0.3000	0.4000	0.5000	1.0000	0.6000	0.5000	0.3000	0.6000	-0.1000	-0.2000	-0.1000	0.3000
Bank Debt	0.6000	0.6000	0.5000	0.5000	0.4000	-0.3000	0.6000	1.0000	0.5000	0.4000	0.5000	0.1000	-0.1000	0.5000	-0.1500
EMD	0.5000	0.5000	0.5000	0.5000	0.6000	0.0000	0.5000	0.5000	1.0000	0.0000	0.2500	0.0000	0.1500	0.3500	0.1000
Hedge Funds	0.2000	0.2000	0.0500	0.0000	0.0000	0.3500	0.3000	0.4000	0.0000	1.0000	0.1000	-0.1000	0.1500	0.5000	0.4000
Private Equity	0.7500	0.8500	0.5000	0.6000	0.2500	0.1500	0.6000	0.5000	0.2500	0.1000	1.0000	0.0000	0.3000	-0.1000	0.0000
Real Estate	0.0000	-0.0500	0.1000	0.0000	-0.1000	-0.1000	-0.1000	0.1000	0.0000	-0.1000	0.0000	1.0000	0.0500	0.4000	-0.1000
Real Assets	-0.2000	-0.2000	0.3500	0.4000	0.2500	-0.1000	-0.2000	-0.1000	0.1500	0.1500	0.3000	0.0500	1.0000	0.0500	0.3000
Infrastructure	0.1500	-0.1000	-0.2000	-0.1000	-0.1000	0.2500	-0.1000	0.5000	0.3500	0.5000	-0.1000	0.4000	0.0500	1.0000	0.0000
GAA	0.0000	0.0000	0.0000	-0.1000	-0.1000	0.7500	0.3000	-0.1500	0.1000	0.4000	0.0000	-0.1000	0.3000	0.0000	1.0000

- **No changes in 2007**
- **In 2006, revised moderate hedge fund correlations (up to equity, down to bonds)**
- **In 2006, revised conservative hedge fund correlations (down to equity, up to bonds)**
- **In 2003 and 2004, raised the domestic/international equity correlations (from 0.45 to 0.60)**
- **In 2005, lowered the stock/bond correlations**

APPENDIX B
AGENCY INVESTMENT ADVISORS, COMMITTEE COMPOSITION AND STAFF

Educational Retirement Board (ERB)

Advisors

Aldus Equity Partners: Private Equity

Contact: Saul Meyer, Partner

Aldus Equity is a boutique alternative investment management and advisory firm specializing in private equity. The firm's expertise includes domestic private equity, mezzanine finance, domestic real estate, European private equity, secondaries, and special situation funds. The firm is primarily employee-owned with Deutsche Bank recently taking a minority interest. The Aldus partners have invested in excess of \$5 billion into over 80 private equity funds since 1998. Currently, the firm manages and advises in excess of \$1 billion of assets for some of the largest and most reputable institutional private equity limited partners in the country. The company is located in Dallas, Texas.

<http://www.aldusequity.com/>

Courtland: Infrastructure

Contact: Steve Novick, Partner

Since inception in July 1995, Courtland has provided clients with a full range of consulting services including strategic and investment planning, market review, research, benchmarking, real estate operating company evaluations, performance measurement and analysis, manager/partner selection, investment evaluation and manager/partner fee structuring. Courtland has advised and assisted public, corporate, endowment and Taft-Hartley pension plans in the positioning of portfolios representing over \$25 billion in real estate and infrastructure investments. Their investment strategies include core, value-added, and opportunistic infrastructure and real estate investments in domestic and international markets. Services have included comprehensive portfolio monitoring and reporting services.

Michael Humphrey and Steven Novick are the two Principals of Courtland. Together Messrs. Humphrey and Novick oversee all of Courtland's underwriting and investment related activities as joint participants in an investment review process that requires their unanimous support. As directors, Ben Blakney and Joe Cook support the principals with respect to firm policies and corporate direction. In aggregate, Messrs. Humphrey, Novick, Blakney and Cook have over 100 years of financial service industry experience.

<http://www.courtland.com/>

New England Pension Consultants (NEPC): Hedge funds and General Consultant

Contact: Allan Martin, Partner

NEPC, LLC, formerly New England Pension Consultants, is one of the country's leading investment consulting firms, currently servicing 266 retainer clients with \$300 billion in assets. Headquartered in Cambridge, Massachusetts, NEPC has been providing institutional consulting services as its sole line of business since 1986. Today, the firm has locations in Detroit, San Francisco, Las Vegas, Cincinnati and Charlotte. NEPC's clients currently have invested capital of \$13.3 billion in hedge funds of funds and \$5.3 billion invested capital in single/multi-strategy funds.

<http://www.nepc.com/>

APPENDIX B

AGENCY INVESTMENT ADVISORS, COMMITTEE COMPOSITION AND STAFF

ORG: Real Estate Consulting including timber, farmland and mitigation banking

Representative: Steve Gruber, Partner

ORG Portfolio Management LLC provides advisory services to institutional investors for global real estate, natural resources and infrastructure investments. In addition to ERB, ORG's clients include CalPERS, CalSTRS, New York Common Retirement Fund, and more than six other respected institutional investors. ORG specializes in strategy development, discretionary and non-discretionary portfolio management, manager due diligence, manager selection and monitoring, performance measurement and special projects. ORG professionals have over 80 years of institutional real estate and real asset experience exclusively representing investors in the development and implementation of global real estate, natural resource and infrastructure investment strategy. ORG Portfolio Management LLC is a Registered Investment Adviser under the Investment Adviser Act of 1940. ORG Real Property has offices in Cleveland, Ohio and Portland, Oregon.

<http://www.orgrealproperty.com/>

To Be Determined: ERB will be executing a RFP soon for its Global Asset Allocations (GAA) advisor.

Outside Legal Counsel

Foster Pepper: Legal, specializing in alternative investments. Other clients include several large public pension funds.

Contact: Bob Perez

Staff

Bob Jacksha, Chief Investment Officer – oversight of all investment areas

Steve Neel - Private Equity/Hedge Funds/Commodities

Mark Canavan – Real Estate and related Real Assets (Timber, Farmland, Mitigation Banking, Infrastructure)/Commodities

LeAnne Larranaga-Ruffy – Public Securities Managers/Internal Index Funds

Selma Arnold – Investment Operations and Reporting

ERB Trustees

Bruce Malott, Chairperson -- Governor Appointee; CPA, CFP, CFA; Managing Principal, Meyners + Company

Mary Lou Cameron, Vice Chairperson – elected member representing National Education Association of New Mexico; Literacy Specialist and Associate Superintendent in Deming Public Schools 1976-present

Gary Bland, Secretary – Governor Appointee; State Investment Officer

Veronica Garcia, Ex-officio; Secretary of Department of Public Education

James Lewis, Ex-officio; State Treasurer

Russell Goff – representing New Mexico Association of Educational Retirees; retired from public education in 2001 as principal of Eldorado High School

Pauline H. Turner, Ph.D – elected to represent New Mexico Conference of the American Association of University Professors; Professor Emerita at UNM

APPENDIX B

AGENCY INVESTMENT ADVISORS, COMMITTEE COMPOSITION AND STAFF

ERB Investment Committee Composition The Board Chair and Executive Director are ex-officio members and two other Board members are chosen annually by the Board. All are voting members. The membership of the Investment Committee also composes the Private Equity and Real Estate Investment Committee. One or more of these committees meet monthly, although the Board meets bi-monthly. Current membership:

Bruce Malott, Board Chair (ex-officio)
Jan Goodwin, Executive Director (ex-officio)
Gary Bland, State Investment Officer
James Lewis, State Treasurer

Public Employee Retirement Association

Advisors

Cliffwater, LLC: All Alternatives

Contacts: Steve Nesbitt, CEO; Jamie Feidler, Director

Cliffwater, LLC was founded in 2004 by four senior investment consultants who have a combined 60 years experience to focus on alternative investments for institutional clients. The firm currently advises 19 retainer clients with over \$100 billion in total assets and \$15 billion in alternative assets. Clients include several endowments and retirement plans, such as the foundation of Ohio State University, the State of New Jersey and the Texas County & District Retirement System. Cliffwater now has 27 employees with offices in Marina del Rey, California and New York. Steve Nesbitt was formerly head of consulting at Wilshire Associates for 15 years.

www.cliffwater.com

R.V.Kuhns & Associates, Inc.: General Consultant

Contacts: Russell Kuhns, Chairman; Jim Voytko, CFA, Co-President; Marcia Beard, CFA, Senior Consultant

R.V. Kuhns & Associates, Inc. provides strategic investment consulting services to institutional investors. Since 1985, R.V. Kuhns & Associates has offered its clients world-class investment advice based on cornerstones of integrity, capability, and client service. The firm is headquartered in Portland, Oregon, with regional service centers in Seattle and New York City. The firm derives 100% of its revenues from investment consulting services, its only line of business. The firm's consulting team delivers a wide array of expertise in areas of financial and investment management for its clients. The firm is independently owned by thirteen employee principals. Russell V. Kuhns is the Chairman, founder, and majority stockholder.

Outside Legal Counsel

Morgan, Lewis & Bockius, LLP
Paul Hastings, Janofsky & Walker, LLP
Kirkpatrick & Lockhart Preston Gates Ellis, LLP

NM PERA Internal Legal Counsel

Susan Pittard, General Counsel
Chris Bulman, Assistant General Counsel

APPENDIX B
AGENCY INVESTMENT ADVISORS, COMMITTEE COMPOSITION AND STAFF

NM PERA Internal Investment Staff

Terry Slattery, Executive Secretary

Robert E. Gish, Director of Investments, overall responsibility for advising and reporting to the Executive Secretary and board and implementing board policy

Dominic Garcia, Deputy Director of Investments, provides backup assistance to the Director of Investments and as Portfolio Management for Real Estate, is responsible for monitoring the external managers hired to make real estate investments

Julian Baca, Portfolio Management U.S. and non-U.S. equities and Private Equity, responsibility for monitoring all investment managers, including private equity

Jason Goeller, Portfolio Management for fixed-income, Securities Lending, Currencies and Hedge Funds, responsibility for monitoring all of these investment activities conducted by external investment managers

Sandy Perez, Investment Officer responsible for custodian accounting records and Alternative Investment Accounting files.

Debbie O'Dell, Investment Officer responsible for manager fees, daily, monthly and quarterly internal analyses and Board reports

PERA Board (All elected positions except two ex-officio)

Victor A. Montoya, Board Chairman-- Retiree Member, Santa Fe County Treasurer's Office

Cynthia Borrego, Vice Chair -- Municipal Member, Albuquerque Metropolitan Redevelopment Agency

James B. Lewis, State Treasurer, Ex-Officio Member

Mary Herrera, Secretary of State, Ex-Officio Member

Oscar Arevalo -- State Member, Administrative Office of the Courts

David Baca -- County Member, Risk Management Director, Bernalillo County

Susan Biernacki—Municipal Member, Albuquerque Legal Department

Patricia French-- Municipal Member, City of Albuquerque Police Department

Nancy Hewitt – State Member, NM Public Defender Department

Annette Martinez-Varela – State Member, 13th Judicial District Attorney's Office

Loretta Naranjo-Lopez – Retiree Member

Francis Page – State Member, Corrections Department

Investment Committee Composition The Board President appoints the committee members, which are all voting members of the committee. Other board members that regularly attend the monthly meeting are nonvoting. This committee meets monthly and includes the following Board members:

David Baca, Chair

Susan Biernacki, Vice Chair

Cynthia Borrego

Patricia French

James Lewis

Victor Montoya

Related Documents: *New Mexico PERA Alternative Investments Internal Operations and Procedures*

APPENDIX B
AGENCY INVESTMENT ADVISORS, COMMITTEE COMPOSITION AND STAFF

State Investment Council

Advisors

Aldus Equity: Private Equity (See description under Educational Retirement Board.)

Contact: Saul Meyer, Partner

Courtland Partners: Real Estate (See additional description under ERB.)

Contact: Steve Novick, Partner

Courtland offers its clients research in the following areas: Market Economics - Property Market, Submarket, Peer Group Analysis: In-depth market research for use in valuation, due diligence, acquisition and disposition decisions. Market Cycle Research: Quarterly analysis and future estimates for 66 major metropolitan markets and 60 secondary markets in the four major property types. Diversification Analysis: Yearly geographic, economic, supply side and cycle analysis. Trend Research: Yearly analysis of property type trend changes.

New England Pension Consultants: General Advisor and Absolute Return (Hedge funds) (See description under Educational Retirement Board.)

Contact: Allan Martin

Sun Mountain Capital: New Mexico Private Equity

Contact: Brian Birk, Principal

Sun Mountain Capital is an investment partnership formed by senior private equity professionals based in Santa Fe, New Mexico. The firm's professionals have a depth of experience in private equity that dates back to 1981 and have an extensive track record of creating value through fund advisory activities and direct investments in promising SIC companies. Prior experience for the principals include employment at Credit Suisse First Boston, Morgan Stanley, Brentwood Associates, Fort Washington Investment Advisors, GE Capital, Kline Hawkes, and The Boston Consulting Group, among other top tier firms. As a private equity advisor to pension plans and other program sponsors, Sun Mountain develops customized private equity programs.

www.sunmountaincapital.com/

Weissmann Wolff: Film

Contact: Peter Dekom, Film Advisor

Peter J. Dekom is "of counsel" with Weissmann Wolff's entertainment department and was formerly a partner in the firm of Bloom, Dekom, Hergott and Cook. Mr. Dekom's clients have included such Hollywood notables as George Lucas, Keenen Ivory Wayans, John Travolta, Ron Howard, Rob Reiner, Andy Davis, Robert Towne and Larry Gordon among many others, as well as corporate clients such as Sears, Roebuck and Co., Pacific Telesis and Japan Victor Corporation (JVC). He has been listed in Forbes among the top 100 lawyers in the United States and in Premiere as one of the 50 most powerful people in Hollywood. Mr. Dekom has been a management consultant and entrepreneur in the fields of entertainment, Internet, and telecommunications. As a consultant to the state of New Mexico, he is and was instrumental in creating, writing and implementing legislation to encourage film and television production in the state.

www.weissmannwolff.com

APPENDIX B
AGENCY INVESTMENT ADVISORS, COMMITTEE COMPOSITION AND STAFF

SIC, continued

Outside Legal Counsel

Brownstein Hyatt Farber & Shreck (Private Equity) Albuquerque/Denver
Weissmann Wolff Bergman Coleman Grodin & Evall (Film) Los Angeles
Paul Hastings (Credit/Structured Finance) San Francisco
Squire Sanders & Dempsey (Real Estate) Cleveland
Baker & Hostetler (Real Estate) Los Angeles

Investment Staff

Senior Investment Staff:

Gary Bland, State Investment Officer

Adam Levine, Sr. Deputy State Investment Officer; All Alternatives, incl. Absolute Return (Fund of Hedge Funds), Private Equity, Real Estate, ETIs and Derivatives strategies

Michael Custer, Deputy State Investment Officer; Public Equities

Kay Chippeaux, Deputy State Investment Officer; Fixed Income, Credit & Structured Finance

Public Equities

Todd Frybarger, Sr. Portfolio Manager

Robin West, Sr. Portfolio Manager

David Lee, Portfolio Manager

Bart Stucky, Portfolio Manager

Paul Heine, Equity Trader

Starla Bennett, Asst. Equity Portfolio Manager

Fixed Income

Connie Lee, Manager

Rose Struck, Manager

Alternative Investments

Scott Smith, Director Real Estate

Greg Kulka, Director Private Equity, Film, Economically Targeted Investments

Lori Romero, Financial Analyst (PE, Film)

Legal Staff

Bryan Otero, General Counsel

Rosalyn Nguyen, Asst. General Counsel

Michelle Ortega, Paralegal

Administrative Services/Accounting

Rick Scroggins, CFO/ASD Director

Pam Hamilton, Accountant

Cyndy Lynch, Investment Accounting Manager

Angela Romero, Financial Analyst

Nicole Gallegos, Financial Analyst

Kelley Koehler, Financial Analyst

Mary Martinez, Financial Analyst

APPENDIX B
AGENCY INVESTMENT ADVISORS, COMMITTEE COMPOSITION AND STAFF

New Mexico State Investment Council

Governor Bill Richardson

Gary Bland, State Investment Officer

Patrick Lyons, State Land Commissioner

James Lewis, State Treasurer

Katherine Miller, DFA Secretary

David Harris, Public Member; CFO University of New Mexico

Andrew Davis, Public Member; Portfolio Manager, Davis Funds

Paul Blanchard, Public Member; CEO Downs at Albuquerque

Jim Rutt, Public Member; Former CEO of Network Solutions, Investor

Private Equity Investment Advisor Committee

Gary Bland

Andrew Davis

Tom Bonafair; CEO Bonafair Management Group, Pella Windows & Doors Distributor

Willie Giron; Retired, Founder Bank of Belen

Bill Enloe; Chairman & CEO Los Alamos National Bank

Internal SIC Committees

Investment Committee (all voting):

Gary Bland

Adam Levine

Michael Custer

Kay Chippeaux

Real Estate Committee

Gary Bland

Adam Levine

Michael Custer

Scott Smith (Nonvoting)

Bryan Otero (Nonvoting)

APPENDIX C
Educational Conferences for PERA Board Members

DATE	Place	Sponsor	Conference	Topics	Fee	Dead line
			MAY 2008			
5/4-6	Austin, TX	Opal Financial Group	Institutional Investor Education Benefit Forum	Infrastructure investing, real estate, fixed income developments	N/A	N/A
5/6-7	San Francisco, CA	Pensions & Investments	130/30 Strategies Conference	Active extension strategies	TBD	N/A
5/6-9	Boston, MA	NYU Stern School of Business	14 th Annual Mid-sized Retirement and Pension Plan Management Conference	Fiduciary responsibility; plan fees; communication strategies	\$995	4/7
5/13-14	Chicago, IL	Pensions & Investments	130/30 Strategies Conference	Active extension strategies	TBD	N/A
5/14-15	New York, NY	International Institute for Business Information & Growth	2008 Distressed and Turnaround Investment Forum	Distressed investments in middle markets	\$1995	N/A
5/15-16	New York, NY	Financial Research Associates	Real Estate Derivatives 2008: Market Assessment, Deal Structuring and Institutional Investing	Role of derivatives in investment plans, differences between real estate derivative products	\$2095	N/A
5/16-17	New Orleans, LA	NCPERS	Trustee Educational Development Seminar	Actuarial assumptions; picking a money manager	\$350	4/24
5/18-22	New Orleans, LA	NCPERS	Annual Conference	Fiduciary responsibility; market cap and style performance cycles; emerging markets; global infrastructure	\$350	4/24
5/19-21	Washington, DC	IFEBP	Washington Legislative Update	Legislative/regulatory developments in public sector plans	N/A	N/A
5/19-22	Philadelphia, PA	IFEBP	Portfolio Concepts and Management	Manager monitoring; role of investment style; fundamentals of portfolio theory	\$3,100	4/7
5/20-21	New York, NY	Pensions & Investments	130/30 Strategies Conference	Active extension strategies	TBD	N/A

APPENDIX C
Educational Conferences for PERA Board Members

DATE	Place	Sponsor	Conference	Topics	Fee	Dead line
JUNE 2008						
6/2-4	Boca Raton, FL	IIR	Super Return Americas 2008 – Private Equity and Venture Capital Summit	Mid market transactions; globalization of cleantech, sovereign funds	\$3395	3/7
6/3-5	Miami, FL	Terrapinn Ltd.	Private Equity World Latin America 2008	N/A	N/A	N/A
6/5-7	Carlsbad, CA	IFEBP	Trustees and Administrators Institutes	Trustee educational policy; alternative investment issues	\$950	4/30
6/10-11	New York, NY	Financial Research Associates	5 th Annual Hedge Fund Structured Products Summit	Global considerations; alpha beta decomposition	\$1795	N/A
6/10-11	Chicago, IL	IFEBP	CAPPP I	Actuarials, governance, legal environment, legislative/regulatory developments	\$835	N/A
6/12-13	Chicago, IL	IFEBP	CAPPP II	Plan design, investments, administrative strategies, emerging issues	\$835	N/A
6/12-13	San Francisco, CA	Financial Research Associates	Hedge Funds 101 and 102	Hedge fund strategies, due diligence process, funds of funds	\$2095	N/A
6/11-13	New York, NY	Terrapinn Ltd.	Hedge Funds World Global Opportunities 2008	NA	N/A	N/A
6/17-18	New York, NY	Financial Research Associates	Hedge Funds 101 and 102	Hedge fund strategies, due diligence process, funds of funds	\$2095	N/A
6/23-25	San Francisco, CA	IFEBP	Hedge Funds, Real Estate and Other Alternative Investments	Asset allocation; funds of funds; private equity and venture capital	\$2,900	5/12

APPENDIX D
NM ERB Asset Allocation Choices (Mix A)



	Current Target with 2007 Assumptions	Mix A (Same Return)	Mix A' (Expected 8.5% Return)	Mix A'' (Same Risk)	Mix A''' (Same Risk w/out GAA)
Equity	58%	36%	45%	52%	52%
Large Cap	35%	19%	23%	27%	26%
Small Cap	5%	1%	2%	2%	3%
Developed Int'l Equity	15%	5%	8%	10%	10%
Developed Int'l Small Cap Equity	0%	1%	2%	3%	3%
Emerging Markets	3%	10%	10%	10%	10%
Fixed Income	27%	29%	20%	13%	18%
Core Bonds	22%	24%	15%	8%	13%
High Yield Bonds	5%	0%	0%	0%	0%
Bank Debt	0%	5%	5%	5%	5%
Alternative Assets	15%	35%	35%	35%	30%
Hedge Funds	5%	10%	10%	10%	10%
Private Equity	5%	10%	10%	10%	10%
Real Estate	5%	5%	5%	5%	5%
Real Assets	0%	5%	5%	5%	5%
Global Asset Allocation	0%	5%	5%	5%	0%
Expected Long Term Compound Return*	8.15%	8.15%	8.49%	8.73%	8.59%
Expected Risk	10.70%	8.54%	9.76%	10.68%	10.70%
Probability of return <= 0% over the next year	21.1%	15.9%	18.0%	19.4%	19.8%
Probability of return <= 0% over the next 5 years	3.7%	1.3%	2.0%	2.7%	2.9%
Probability of return <= 8% over the next year	49.3%	49.2%	47.8%	47.1%	47.6%
Probability of return <= 8% over the next 5 years	48.4%	48.2%	45.1%	43.4%	44.6%

Individual Constraints: Int'l Equity max 30%, Int'l Small Cap Equity max 10%, Emerging Mkts max 10%, Bank Debt max 5%, Emerging Markets Debt 5%, High Yield Bonds 5%, Hedge Funds max 10%, Private Equity max 10%, Real Estate max 5%, Real Assets 5%, Infrastructure 3%, & GAA 5%

Group Constraints:

Mix A: Small/Mid Cap Equities <= 0.25 x Large Cap Equities, Int'l Small Cap Equities <= 0.25 x Int'l Equities, Int'l Equities + Emerging Mkts + Int'l Small Cap Equities <= 0.8 x Large Cap Equities + 0.8 x Small Cap Equities

Source: NEPC 2007 Asset Allocation

NM PERA
Absolute Return Portfolio
Portfolio Performance Summary
Estimated as of February 29, 2008



Fund	Mkt Value ¹ \$(000)	Actual %	Returns ¹				Ann Std Dev	Sharpe Ratio	Incep. Date
			Feb	FYTD	CYTD	Incep.			
Market Neutral									
Mariner Partners, L.P.	34,361	5.6%	-1.50%	-	-2.59%	-1.83%	4.33%	-	1-Aug-07
Credit									
Canyon Value Realization Fund, L.P.	33,924	5.6%	0.38%	-	-2.75%	-3.07%	6.39%	-	1-Dec-07
Golden Tree Multi-Strategy, L.P.	28,021	4.6%	-1.65%	-6.65%	-4.07%	-6.60%	5.40%	-	1-Jun-07
Silver Point Capital Fund, L.P.	30,131	4.9%	-0.77%	-5.31%	-3.15%	0.40%	4.59%	-0.94	1-Feb-07
Distressed									
King Street Capital, L.P.	34,931	5.7%	2.22%	9.13%	3.78%	9.16%	6.96%	-	1-Jun-07
Marathon Special Opportunities Fund, L.P.	35,071	5.7%	0.10%	-	-0.02%	0.20%	0.60%	-	1-Dec-07
Event Driven									
Davidson Kempner Institutional Partners, L.P.	30,190	4.9%	-0.63%	-2.93%	-2.08%	0.63%	4.57%	-	1-Apr-07
Pendragon Lancelot II Fund	31,125	5.1%	1.10%	-	-11.07%	-11.07%	32.18%	-	1-Jan-08
York Capital Management L.P.	32,939	5.4%	2.60%	2.93%	-1.88%	2.93%	9.95%	-	1-Jul-07
Equity Long/Short									
Archipelago Partners, L.P.	32,936	5.4%	1.80%	1.67%	-2.24%	9.00%	7.32%	0.56	1-Feb-07
Ascend Partners Fund II L.P.	34,577	5.7%	2.25%	-	-1.21%	-1.21%	13.80%	-	1-Jan-08
Glenview Institutional Partners, L.P.	24,274	4.0%	-0.89%	-2.90%	-2.30%	-2.90%	6.71%	-	1-Jul-07
TPG-Axon Partners, L.P.	35,088	5.7%	6.20%	-	-1.17%	0.25%	23.05%	-	1-Dec-07
Multi-Strategy									
AG Super Fund, L.P.	34,252	5.6%	0.30%	-	-2.14%	-2.14%	6.69%	-	1-Jan-08
Black River Global Multi-Strategy Leveraged Fund	31,713	5.2%	-0.76%	-2.14%	0.46%	-0.90%	5.07%	-	1-May-07
Farallon Capital Institutional Partners, L.P.	31,472	5.2%	-0.03%	-2.33%	-3.73%	4.19%	6.33%	-0.08	1-Jan-07
OZ Domestic Partners II, L.P.	31,820	5.2%	1.05%	0.25%	-0.80%	6.07%	4.71%	0.26	1-Mar-07
Satellite Fund II, L.P.	29,419	4.8%	-0.70%	-5.62%	-6.59%	-1.94%	8.48%	-	1-Apr-07
Stark Investments L.P.	34,229	5.6%	2.26%	-	-0.25%	-2.20%	8.14%	-	1-Sep-07
NM PERA Absolute Return Portfolio	610,473	100.0%	0.76%	-1.76%	-2.30%	5.29%	5.07%	0.09	1-Jan-07
Hedge Fund Indices									
Labor + 4%			0.58%	5.66%	1.18%	8.97%	0.21%	-	1-Jan-07
HFRI Fund of Funds Composite Index			1.80%	1.03%	-1.18%	7.62%	5.98%	0.45	1-Jan-07
HFRI Fund Weighted Composite Index			2.54%	2.57%	0.22%	8.69%	5.88%	0.63	1-Jan-07
Market Indices									
3 Month Labor Rate			0.25%	3.07%	0.51%	4.95%	0.23%	-	1-Jan-07
Lehman Aggregate Bond Index			0.14%	7.87%	1.82%	7.59%	2.68%	0.94	1-Jan-07
Lehman High Yield Credit Bond Index			-1.36%	-3.61%	-2.67%	-0.72%	5.98%	-0.90	1-Jan-07
S&P 500 TR			-3.25%	-10.30%	-9.05%	-3.49%	11.12%	-0.70	1-Jan-07
MSCI EAFE - Net			1.43%	-7.58%	-7.94%	2.00%	12.95%	-0.16	1-Jan-07
MSCI EMF (Emerging Markets Free) - Net			7.38%	11.44%	-6.02%	26.04%	22.73%	0.92	1-Jan-07
Wilshire REIT Index			-3.77%	-18.03%	-4.23%	-20.17%	18.35%	-1.39	1-Jan-07

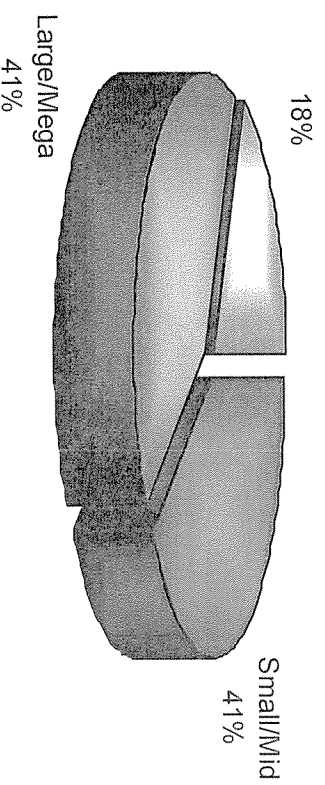
¹ Most recent month returns are based on manager estimates; prior months use final market values except Farallon, for which the two most recent month returns are based on manager estimates.

Hedge Fund Research, Inc. ("HFR") is the source and owner of the HFR data contained or reflected in this report and all trademarks related thereto.

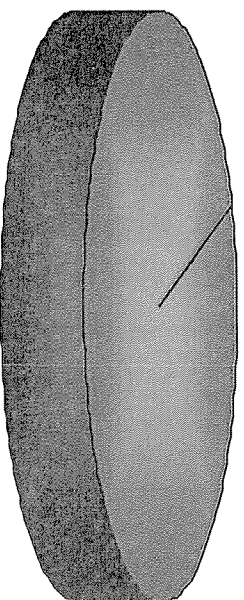
Our due diligence and reporting rely upon the accuracy and completeness of financial and other information publicly available or provided to us by the fund manager, its professional staff, and through other references we have contacted. We have not conducted an independent verification of the information provided other than as described in this report. Our conclusions do not reflect an audit of the investment or a legal review of the documentation. The information contained herein is confidential commercial or financial information, the disclosure of which would cause substantial competitive harm to Cliffwater LLC, or the person or entity from whom the information was obtained.

CURRENT SUBSECTOR ALLOCATION PLAN

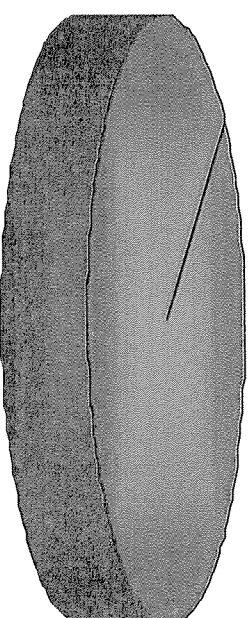
BUYOUT



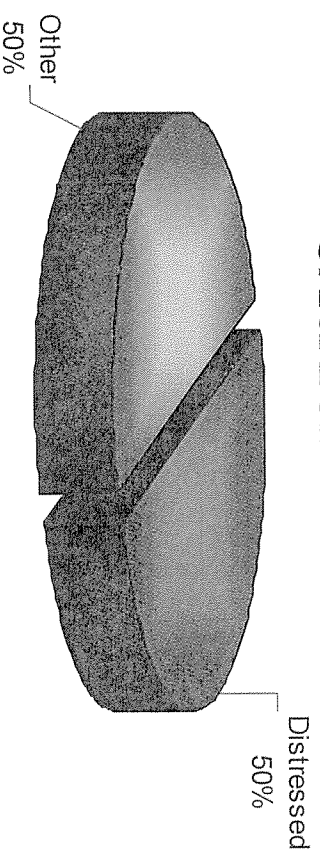
MEZZANINE



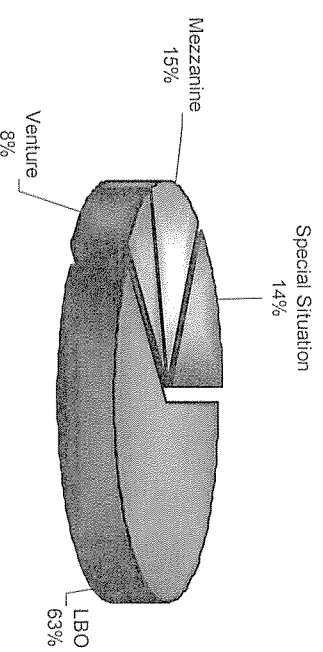
VENTURE CAPITAL



SPECIAL SITUATION

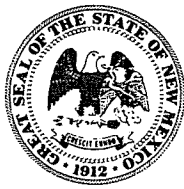


TOTAL



DETAILED POTENTIAL PLAN

2008 GAME PLAN				
Total Annual Commitment		\$355		
(\$ Millions)	commitment amount	subsector %		
		1	2	3
LBO	\$220	62%		
<i>Domestic</i>			82%	
small/mid				53%
Platinum Equity Capital Partners II	\$35			
XYZ small/mid	\$30			
XYZ small/mid	\$30			
large				47%
Clayton, Dubilier & Rice Fund VIII	\$50			
Welsh, Carson, Anderson & Stowe XI	\$35			
<i>International</i>				18%
Bridgepoint Europe IV	\$40 ≈ €30			
Venture Capital	\$30	8%		
NGN Biomed Opportunity II	\$30			
Mezzanine	\$55	15%		
<i>Un-sponsored</i>				
Levine Leichtman Capital Partners IV	\$30		55%	
Falcon Mezzanine Partners III	\$25		45%	
Special Situations	\$50	14%		
<i>Distressed</i>				
Ares Distressed Securities Fund	\$25		50%	
<i>Other</i>				
Camden	\$25		50%	
Total	\$355			



REC'D APR 09 2008

PUBLIC EMPLOYEES RETIREMENT ASSOCIATION OF NEW MEXICO
PUBLIC EMPLOYEES RETIREMENT BOARD

P.O. Box 2123
Santa Fe, New Mexico 87504-2123
(505) 827-4700

VICTOR A. MONTROYA, CHAIRMAN
Retiree Member

TERRY SLATTERY, CEBS
Executive Director

Dated: April 4, 2008
To: Investment Committee
From: Bob Gish, Director of Investments
Subject: Compliance with Procurement Policy for
Alternative Investments

The investment listed below has been reviewed for compliance with the NM PERA Procurement Policy for Alternative Investments. This review is limited to information contained in the due diligence report submitted by Cliffwater LLC, NM PERA's investment consultant and gatekeeper for alternative investments. In my opinion these investments are an appropriate fit for NM PERA's long-term investment strategy for alternative assets and meet the requirements of NM PERA's Investment Policy and Investment Guidelines and Performance Measurement Standards for Alternative Investments taken as a whole. Therefore, approval of this investment is recommended.

The primary areas of focus during the review were:

- (1) the background, organization and investment experience and credentials of the key personnel,
- (2) investment strategy and processes used and
- (3) performance record

As Director of Investments, I would concur with the recommendations of Cliffwater LLC that NM PERA invest in these funds.

On matters relating to the sufficiency of any legal documents that are required, I defer to General Counsel or outside Counsel for an opinion, although NM PERA's investment division staff members have reviewed some of the applicable legal documents in cooperation with General Counsel.

APPENDIX H

INVESTMENT ADVISOR DUE DILIGENCE

The following represents the breadth of due diligence that Aldus Equities, the alternatives advisor for SIC and ERB, provides staff, the investment committee and the full board/council. Whenever an investment is proposed, Aldus provides a complete reporting on all pertinent issues.

- I. Partnership Summary: outlines all of the parameters of the proposal including
 - a. Manager
 - b. Fund size
 - c. Strategic focus
 - d. Fund type
 - e. Claw-back
 - f. Management fee
 - g. Carried interest
 - h. Geographic focus
 - i. General partner commitment
- II. History of fund manager: key elements include how long the managers have been together, how many prior funds have they assembled and how they have performed.
- III. Strategy: where in the marketplace will the fund target. “Middle Market” is a strategy of investing in only medium size companies that have substantial opportunities. “Venture” is another strategy of investing in start-ups. Other considerations are the approach to identifying companies within the target market and how the manager intends to build value.
- IV. Investment Process: how deals are sourced or identified and what is the process the manager uses to go from identifying a prospect to closing a deal, including how due diligence is conducted and who makes the final decisions.
- V. Market Opportunity: Will the fund take advantage of a real or perceived market opportunity? Is the segment ripe for investment or is it saturated?
- VI. Management Team: who are they and how long have they worked together? Who’s on the advisory board?
- VII. Exit Strategy: Identifies the manager’s strategy for getting out of investments.
- VIII. Peer Group Review: how has this manager performed relative to others in the same space in terms of internal rate of return (IRR) and investment multiple.
- IX. Key fund terms: an overview of the fees, expenses and profit distribution parameters.
- X. Team Ownership: Examines how much the principal partners are investing (which is a proxy for their commitment and dedication).
- XI. Track Record: Other funds or investment performance of the managers.
- XII. Litigation: any significant litigation pertaining to any of the managers.
- XIII. Strengths: Aldus Equities assessment of the funds strengths.
- XIV. Weaknesses: Aldus assessment of weaknesses and what are the mitigating factors.
- XV. New Mexico Compliance Analysis: an assessment of compliance with NM statutes and SIC policy
- XVI. Graphic depiction of Geographic risk, style risk and manager risk with an overall risk factor that can be used to compare similar proposal