Fixed Income Overview

February 27, 2013

Fixed Income Profile
As of January 31, 2013

Allocation

- 2.5%
- 1.5%
- 0.1%
- 95.9%

Legend:
- Core Fixed
- STIF
- RMBS
- CMBS

Relative Weighting in Core Fixed

- Govt: -5.0%
- Corp: 4.0%
- Mtge: 0.1%
- Cash: 0.9%

+/- Weighting vs. Benchmark

Returns

	3 Month	1 Year	3 Year	5 Year
Core	-1.16%	4.41%	8.20%	7.74%
Non-Core	2.66%	15.22%	9.36%	
Benchmark	-1.56%	3.66%	7.97%	7.09%

Legend: Core, Non-Core, Benchmark
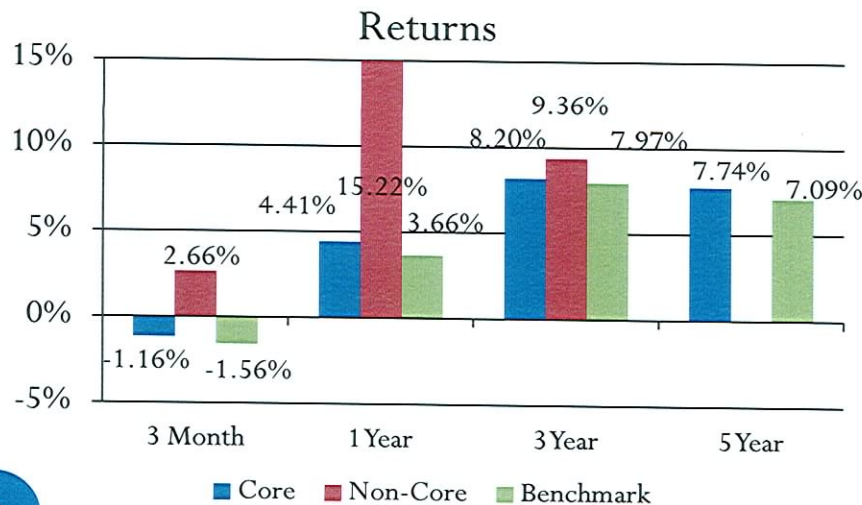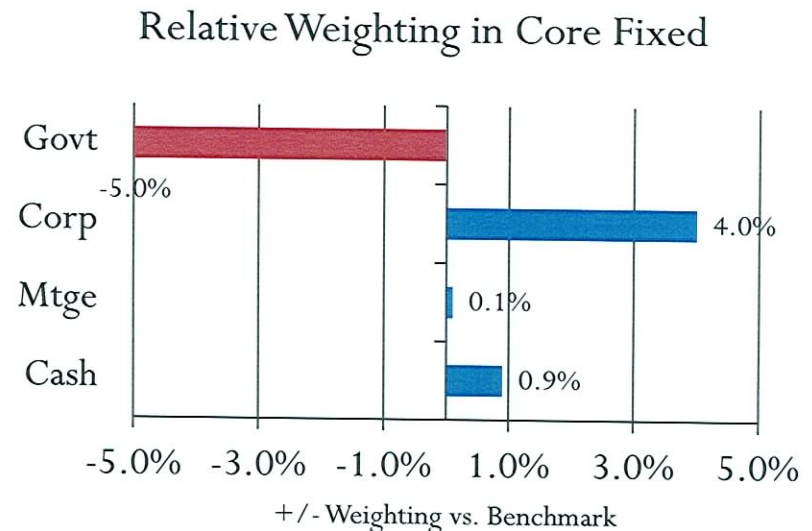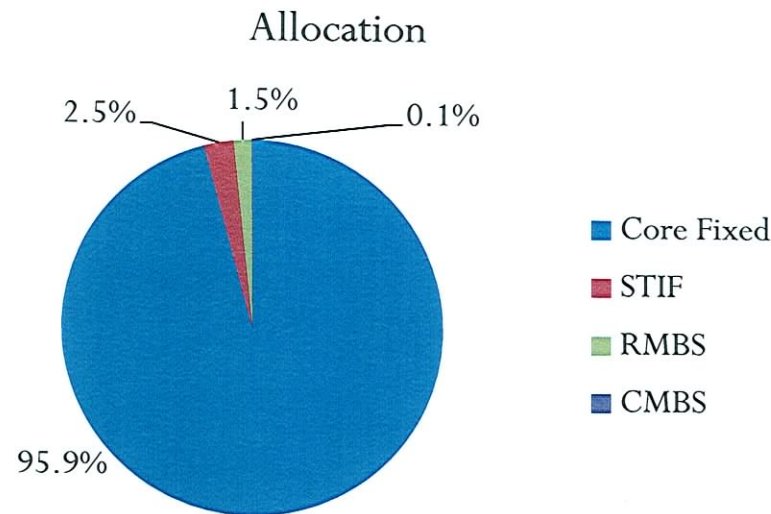
- Near term strategy in core remains focused on an overweight to corporate debt and a short relative duration position, while also exploring additional non-core allocation

- Non-core added 27bp performance to total fixed income over the last year

- Our defensive fixed income strategy outperformed by more than 50 bps during the 30bp rate increase over the last 90 days

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Treasury Yields Have Drifted Higher Off The Historical Lows

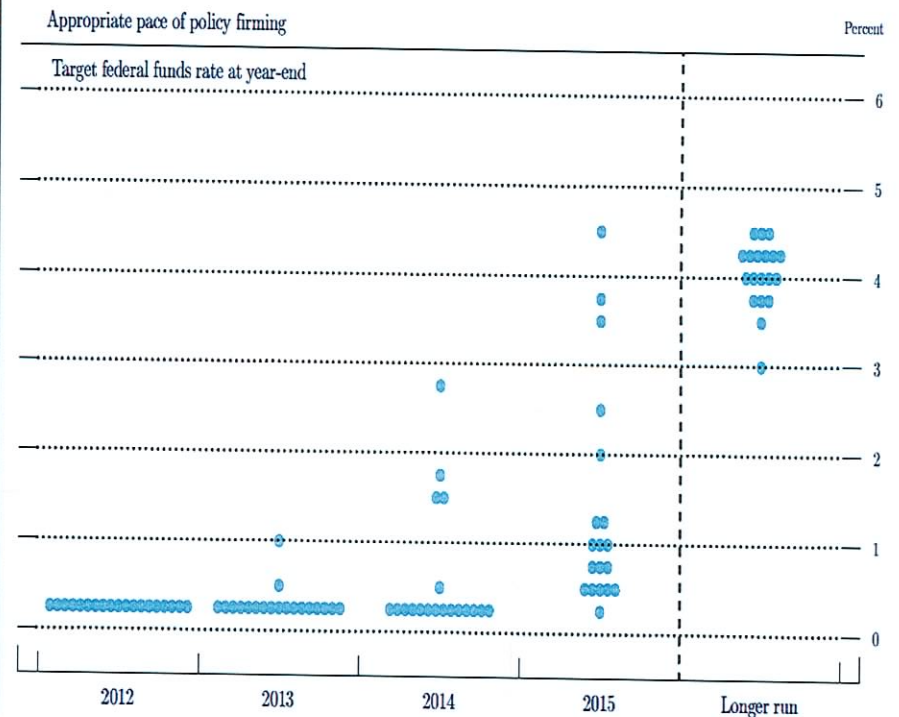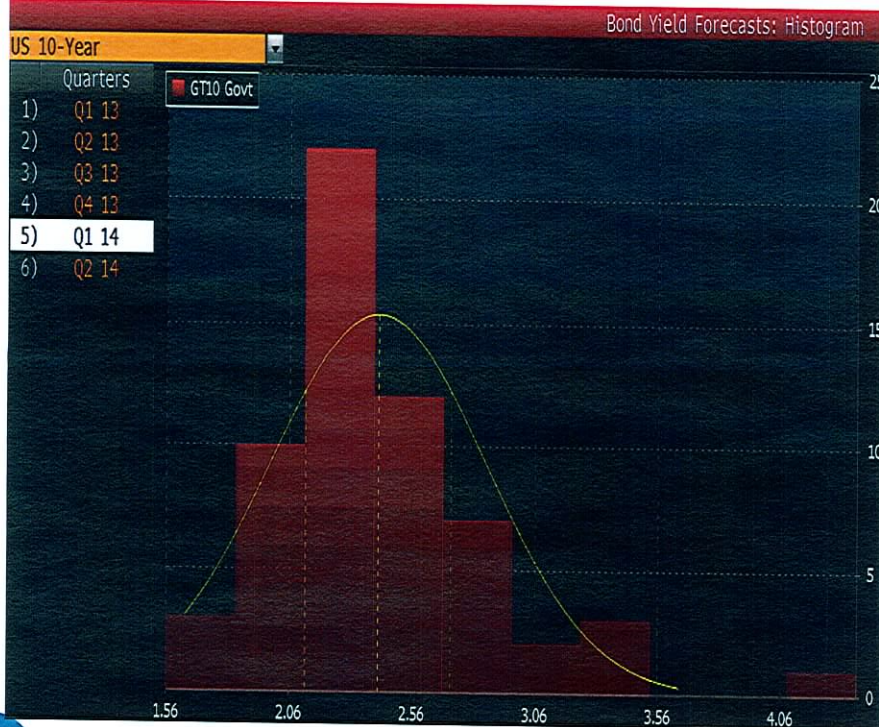# Higher Rates Still Out on the Horizon

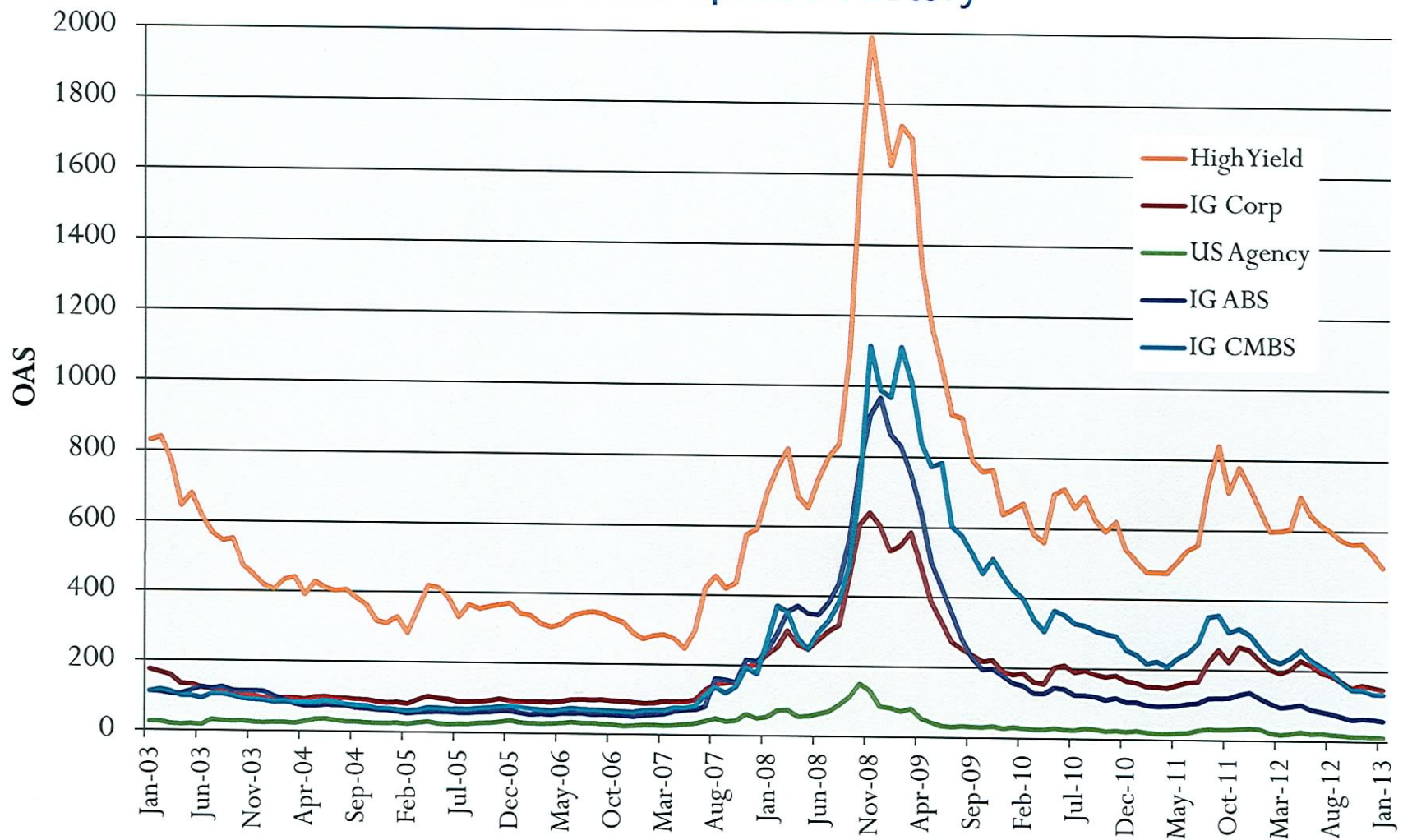95) Chart — Page 1/3 Bond Yield Forecasts

Region G7 — Spread 2 Year - 10 Year

Rate	Market Yield	Q1 13	Q2 13	Q3 13	Q4 13	Q1 14	Q2 14
United States							
1) US 30-Year	3.23	3.02	3.09	3.19	3.35	3.47	3.61
2) US 10-Year	2.02	1.86	1.96	2.07	2.24	2.43	2.58
3) US 2-Year	0.28	0.25	0.29	0.35	0.42	0.55	0.62
4) US 3-Month Libor	0.29	0.32	0.31	0.33	0.36	0.40	0.42
5) Fed Funds Target Rate	0.25	0.25	0.25	0.25	0.25	0.25	0.25
2 Year - 10 Year Spread	1.74	1.61	1.67	1.72	1.82	1.88	1.96

Bond Yield Forecasts: Histogram

US 10-Year

Quarters	GT10 Govt
1) Q1 13	
2) Q2 13	
3) Q3 13	
4) Q4 13	
5) Q1 14	
6) Q2 14	

Appropriate pace of policy firming

Target federal funds rate at year-end — Percent

SOURCE: BLOOMBERG and FEDERAL RESERVE

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Fixed Income Credit Markets
10 Year Spread History

Legend:
- High Yield
- IG Corp
- US Agency
- IG ABS
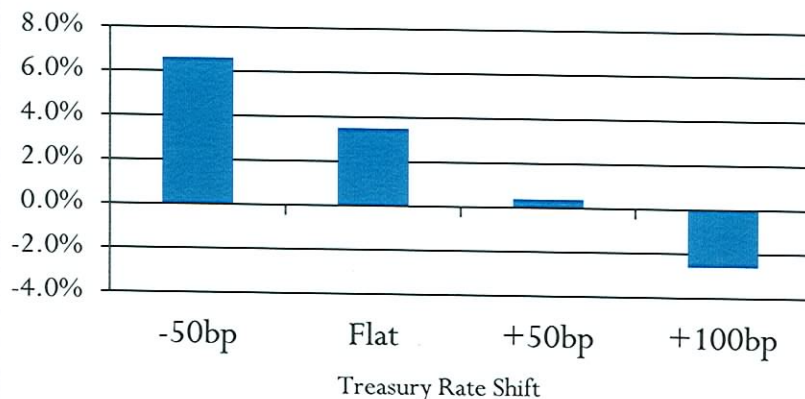- IG CMBS

Y-axis: OAS

SOURCE: BofA Merrill Lynch Bond Indices

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# Corporate Relative Value and LTIP Allocation by Sector
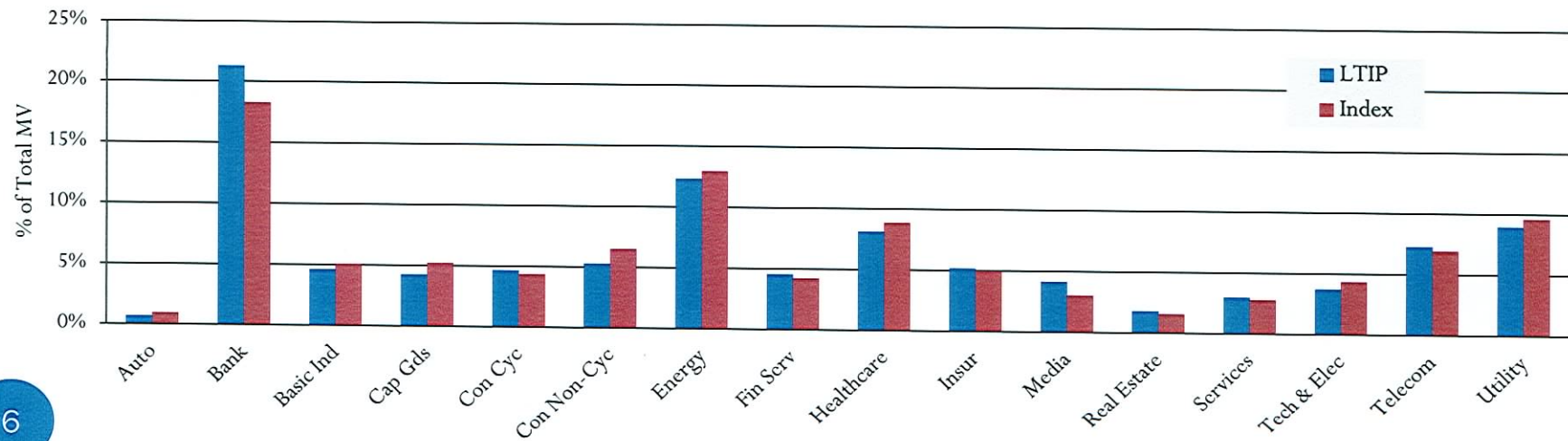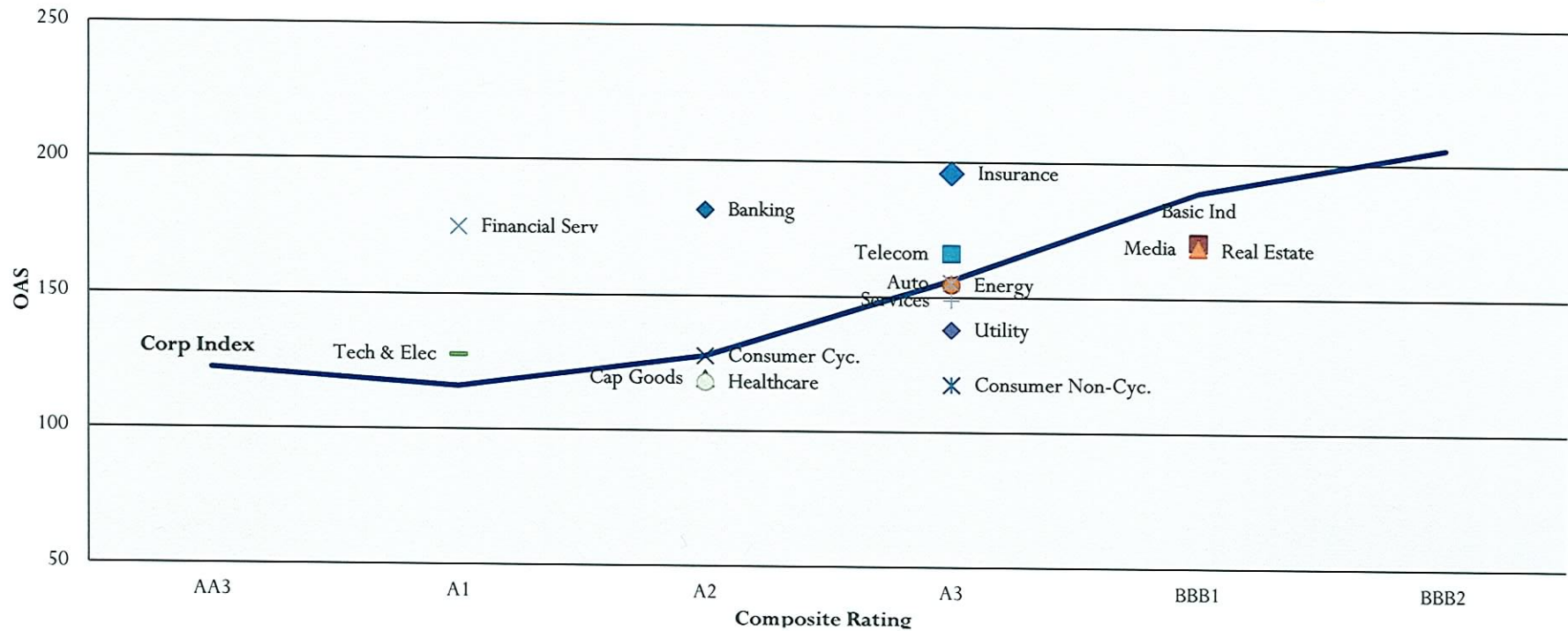
What Lies Ahead for Core Fixed Income?

### 1 Year Parallel Simulation for Core Fixed Income

- The lack of income in the current rate environment leaves fixed income returns more vulnerable to rate increases than in the past

- Inflationary pressures appear modest in the near term

- Return expectations over the next five years are 2% to 4%

- The last material backup in rates was offset by tightening corporate spreads. We have a more bearish view of the current market due to the current corporate spread levels
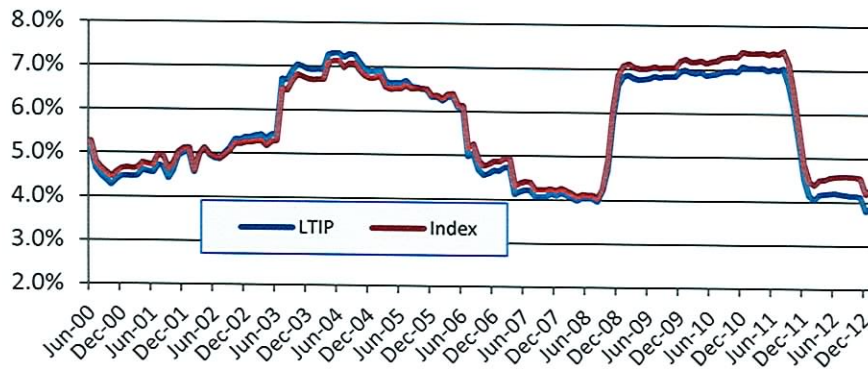
YTM versus Future 5-Year Realized Returns
1985-2012 – BOAML Domestic Master
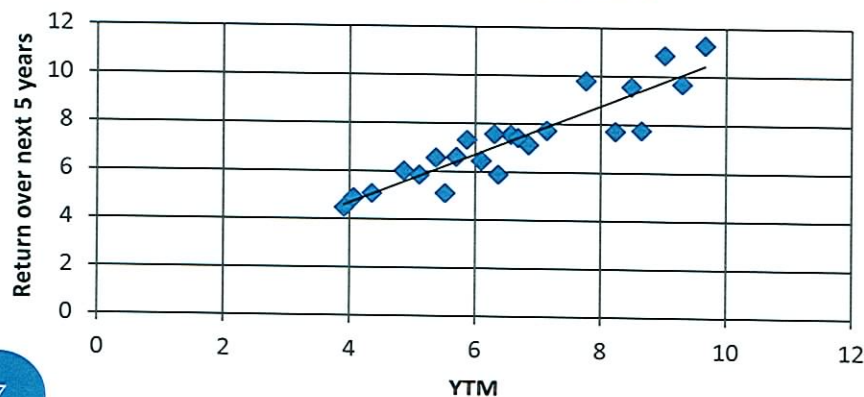
Corporate Spread History vs. US Treasury Yields
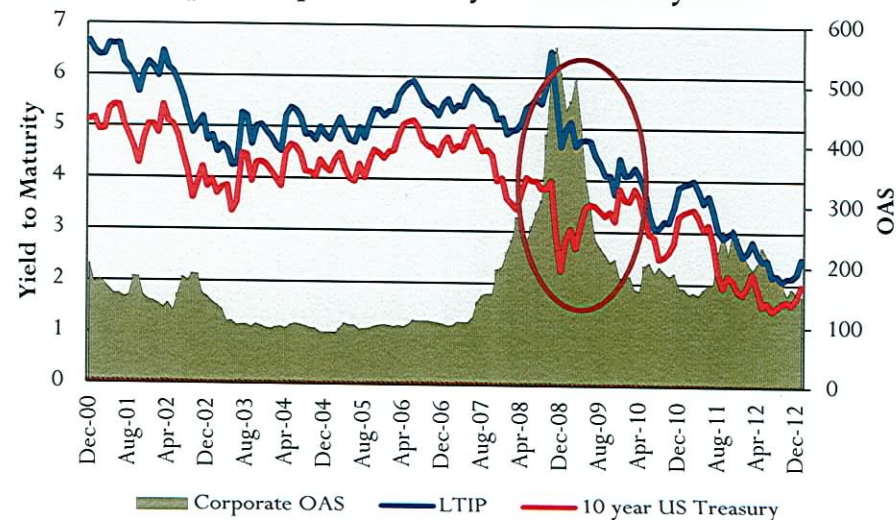
Core Fixed Income Trailing 3 Yr. Standard Deviation vs. Benchmark


Legend: LTIP, Index

## Core Fixed Income Trailing 3 Yr. Tracking Error

- Portfolio volatility remains consistent with the market

- The consistent tracking error range should allow for effective risk budgeting at the total plan level

- While core fixed income still offers significant downside protection to public equity bear markets, the costs of that protection are lower expected returns in the asset class than the past 15 years

- Fixed Income allocation is down 3% from calendar year end 2011

LTIP Performance During Recent Equity Bear Markets

August 2000 – September 2002
(Absolute Diff. 73%)

LTIP: 29%
S&P: -45%

Legend: S&P, LTIP
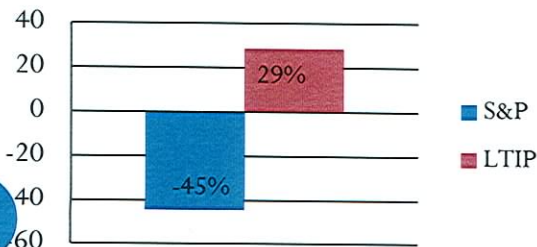
October 2007 – February 2009
(Absolute Diff. 56%)

LTIP: 5%
S&P: -51%

Legend: S&P, LTIP
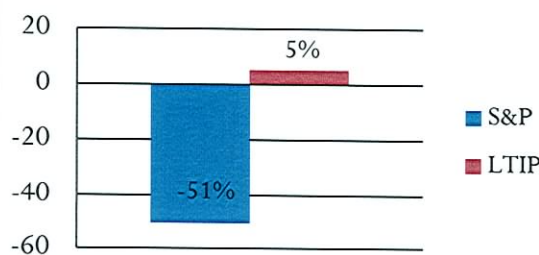
April 2011 – September 2011
(Absolute Diff. 24%)

LTIP: 8%
S&P: -16%

Legend: S&P, LTIP