

Legislative Update

Presented by
Kim Rhead, MERS Legislative Outreach Director

BUILDING
RETIREMENT
SUCCESS
TOGETHER



1996: HB 6229 / PA 487 of 1996

1996: HB 6229 /
PA 487 of 1996

Market Conditions
in 2008 – 2009

EVIP: HB 4328 /
PA 59 of 2013

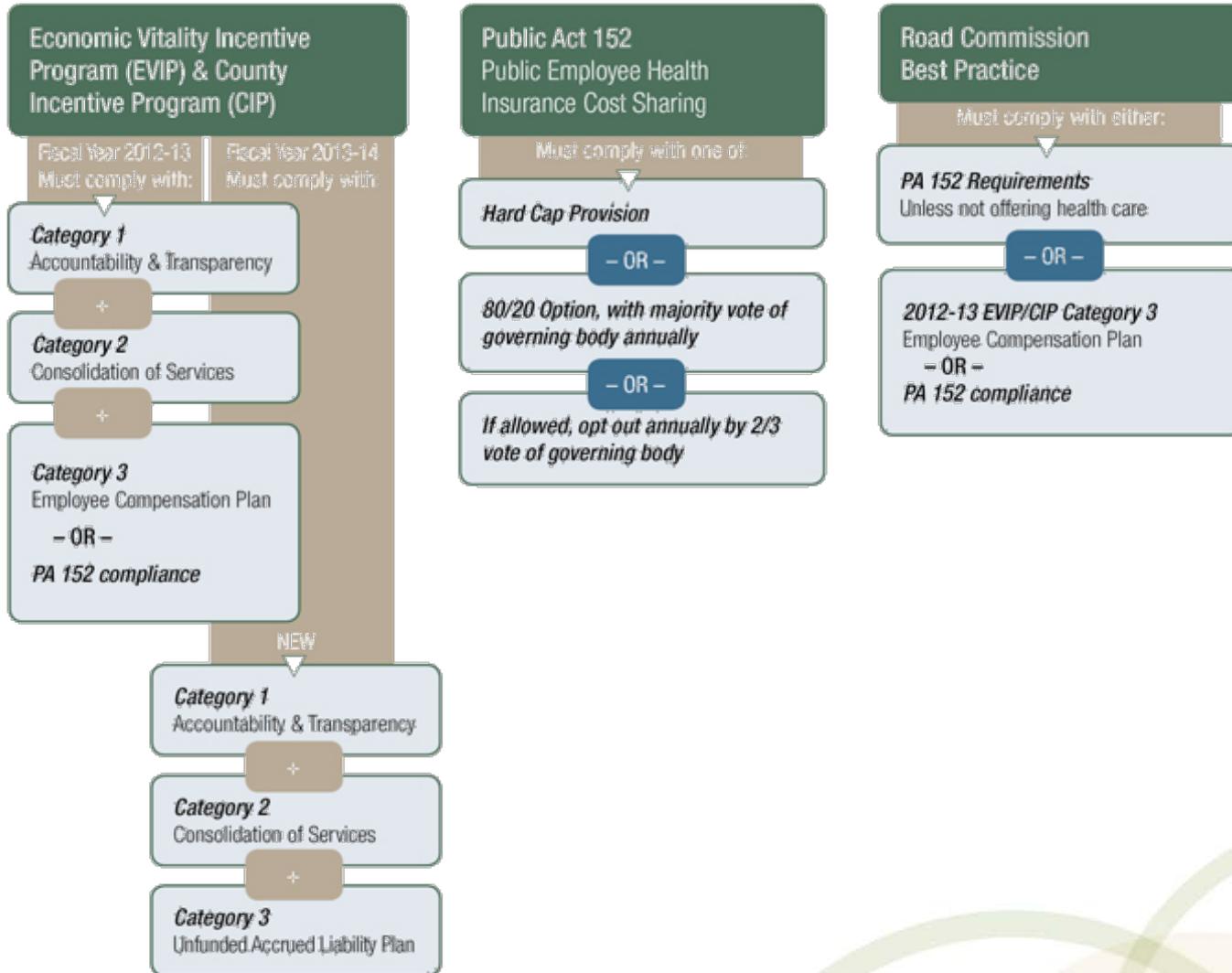
Road Commission
Best Practice

HB 5301 / PA 466 of 2012
HB 5302 / PA 506 of 2012
HB 5313 / PA 507 of 2012

Unfunded Accrued
Liabilities
SB 1129 / PA 329
of 2012

Publicly Funded Health
Insurance Contribution
SB 7 / PA 152 of 2011

Compliance



Liability Bonding Bill

- Allows municipality to issue a municipal security to pay all or part of the costs of the unfunded pension liability or OPEB liability
- Existing Defined Benefits Plans must be closed to new hires
- Available only through December 2014
- Several requirements established that need to be met to bond for unfunded accrued liability

Partnering with You

- Working collaboratively with MML to assist you with EVIP Category 3 compliance
- Recent bill introduced to clarify treatment of MERS HCSP regarding PA 152
- Regional Teams available to assist you with managing/reducing your pension and OPEB liabilities



Municipal Employees' Retirement System

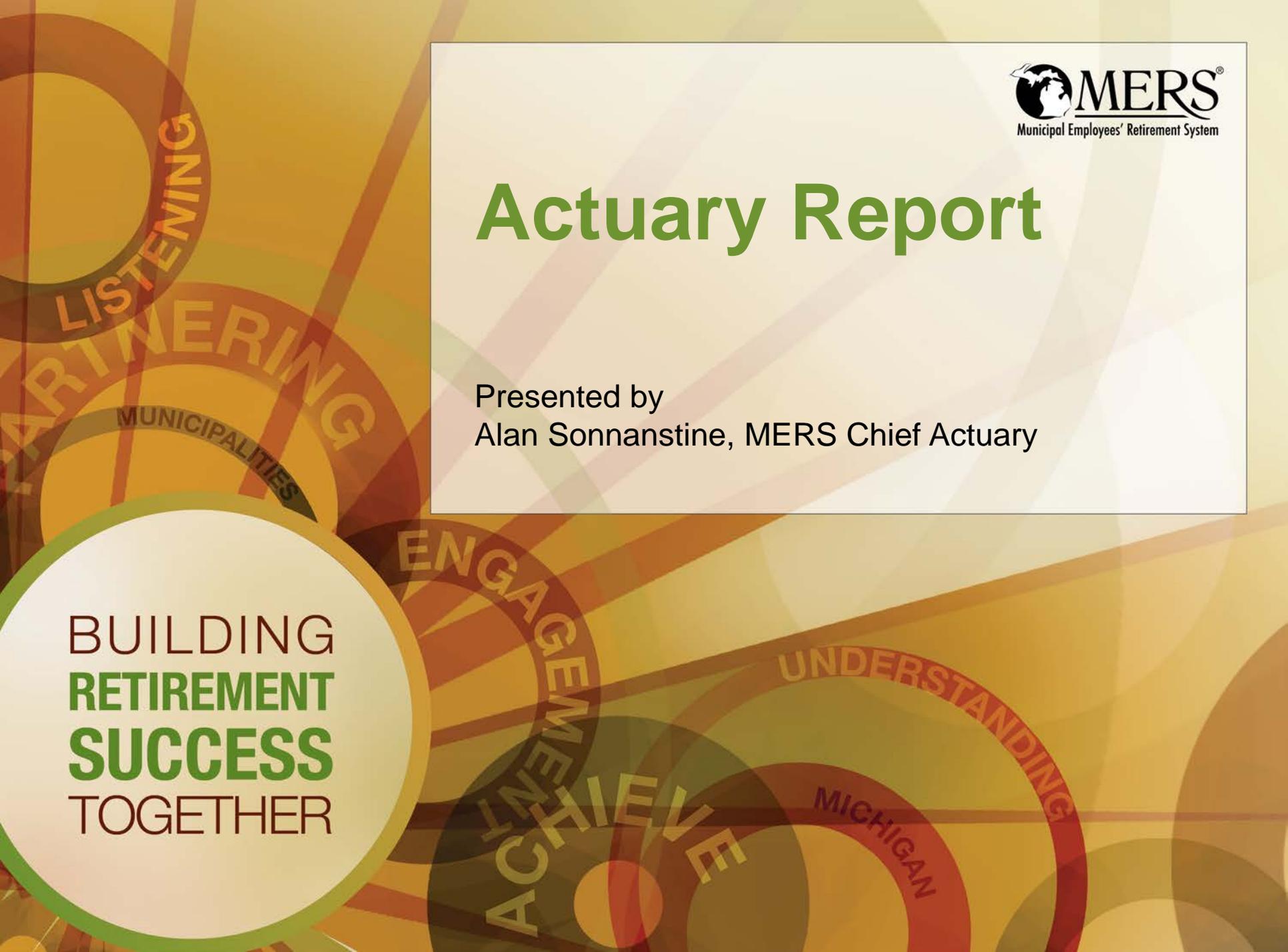
BUILDING
RETIREMENT
SUCCESS
TOGETHER



Actuary Report

Presented by
Alan Sonnanstine, MERS Chief Actuary

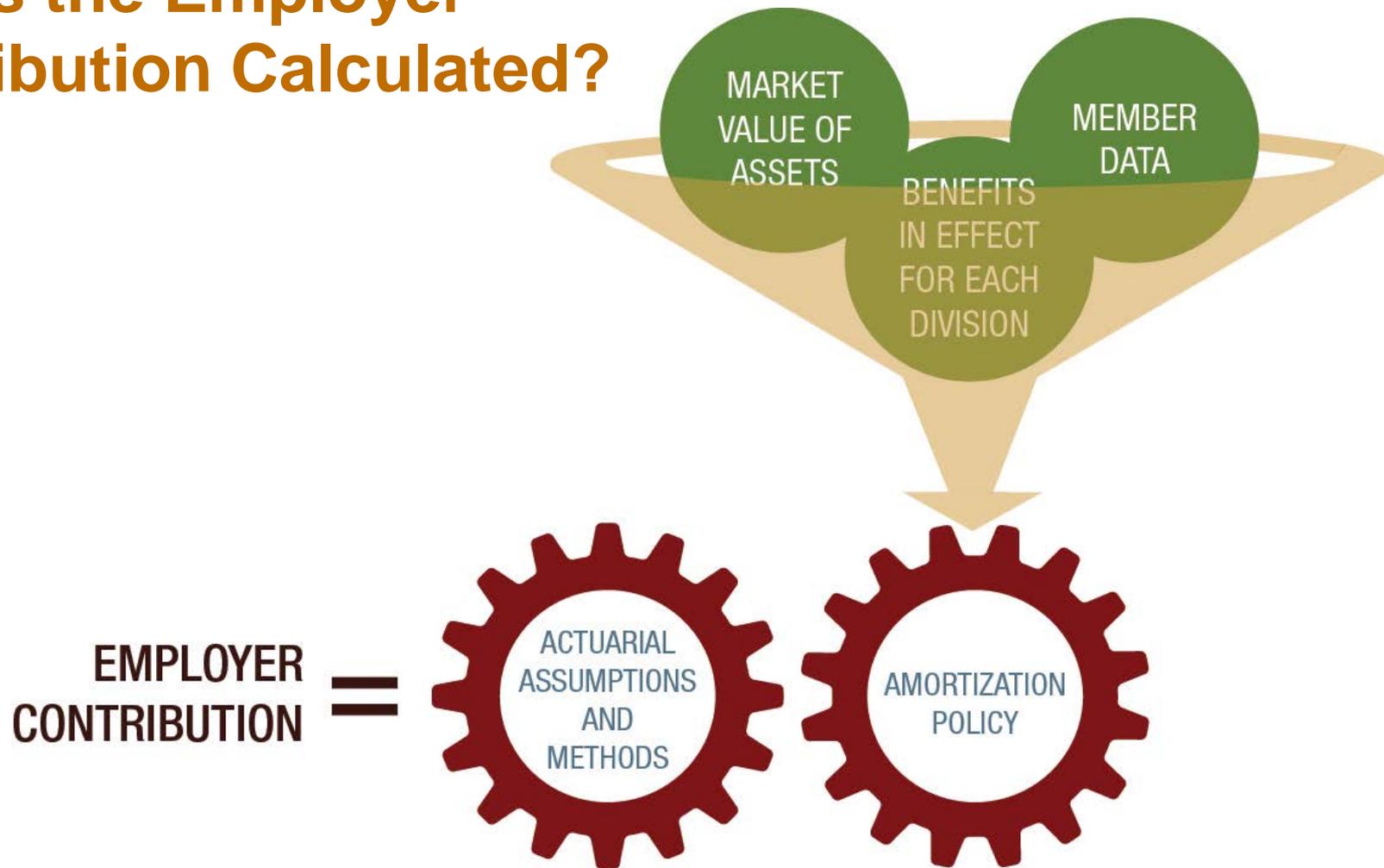
BUILDING
RETIREMENT
SUCCESS
TOGETHER



Annual Actuarial Valuation

- An important tool to help you budget for your municipality's retirement benefits, with information specific to your municipality's retirement plan
 - As a multiple-employer plan, MERS establishes a separate trust for each municipality
 - Each entity is responsible for the employer contributions needed to provide benefits for its employees and former employees
- Provides to you as a snapshot of your MERS Defined Benefit Plan as of December 31 each year
- Provides insight to your plan's liabilities, funding levels, contributions for both the employer and employee, and important GASB Information
- The information in the report will provide you contribution rates for each division for your following fiscal year
 - If you are reviewing the valuation for December 31, 2012, the rates go into effect the first day of your fiscal year in 2014
 - Rates are designed to be level as a percentage of payroll for open division

How is the Employer Contribution Calculated?

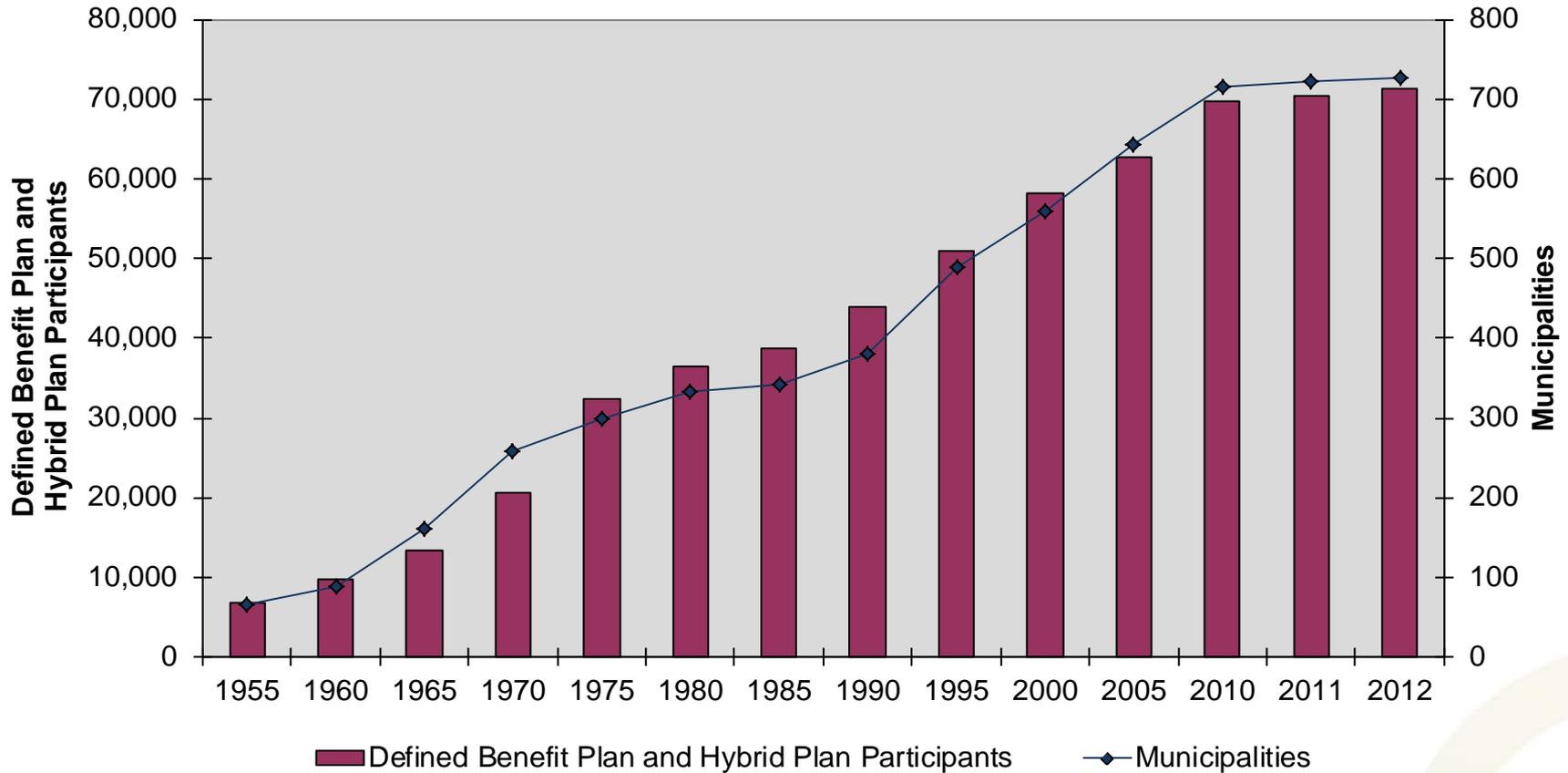


Actuarial Assumptions and Methods established by the Retirement Board

Assumption and Method Changes

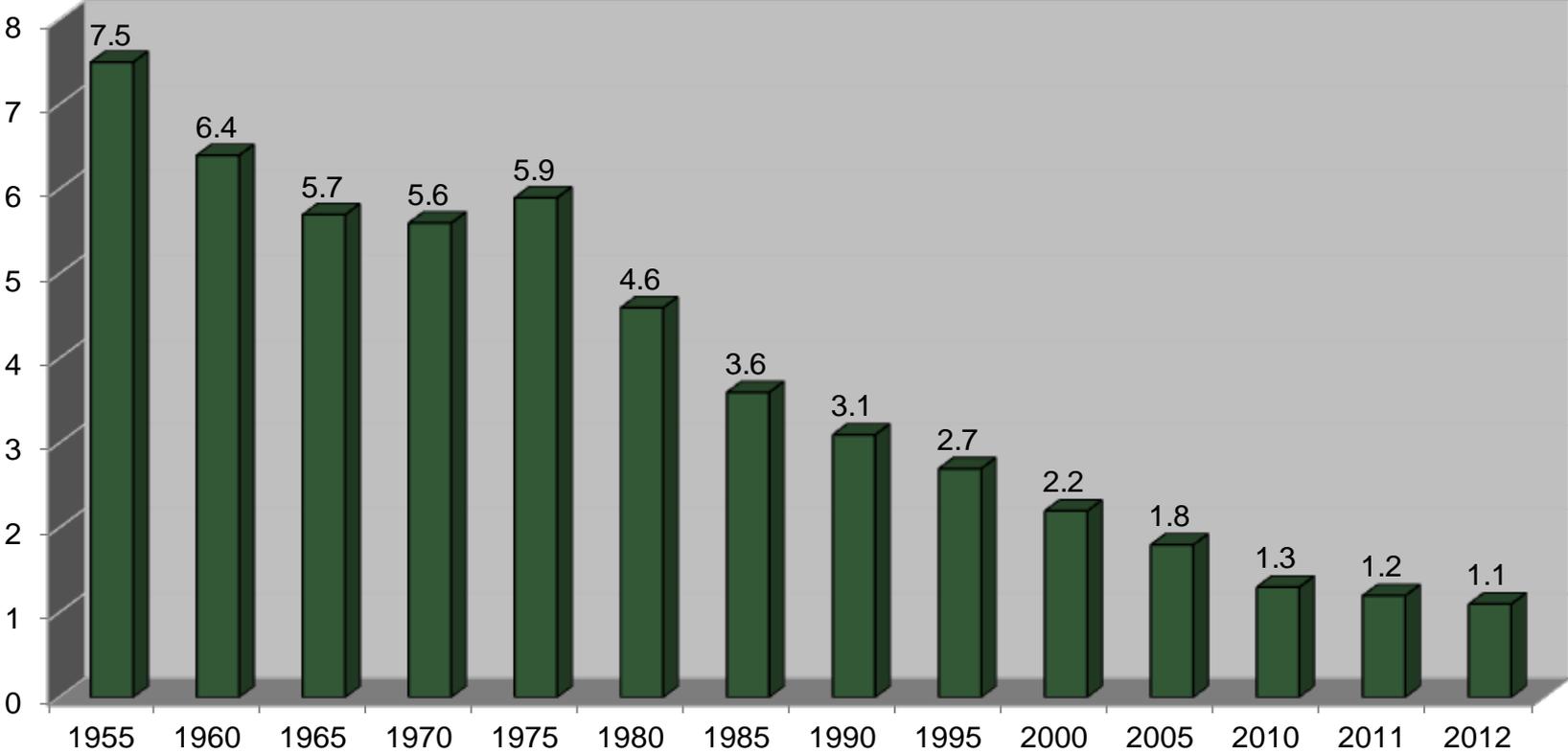
- Reduction in the 2015 and 2016 wage inflation assumption, to better reflect near-term economic conditions in Michigan
- Increase in the minimum funding requirements for poorly funded closed divisions

MERS Continues to Grow



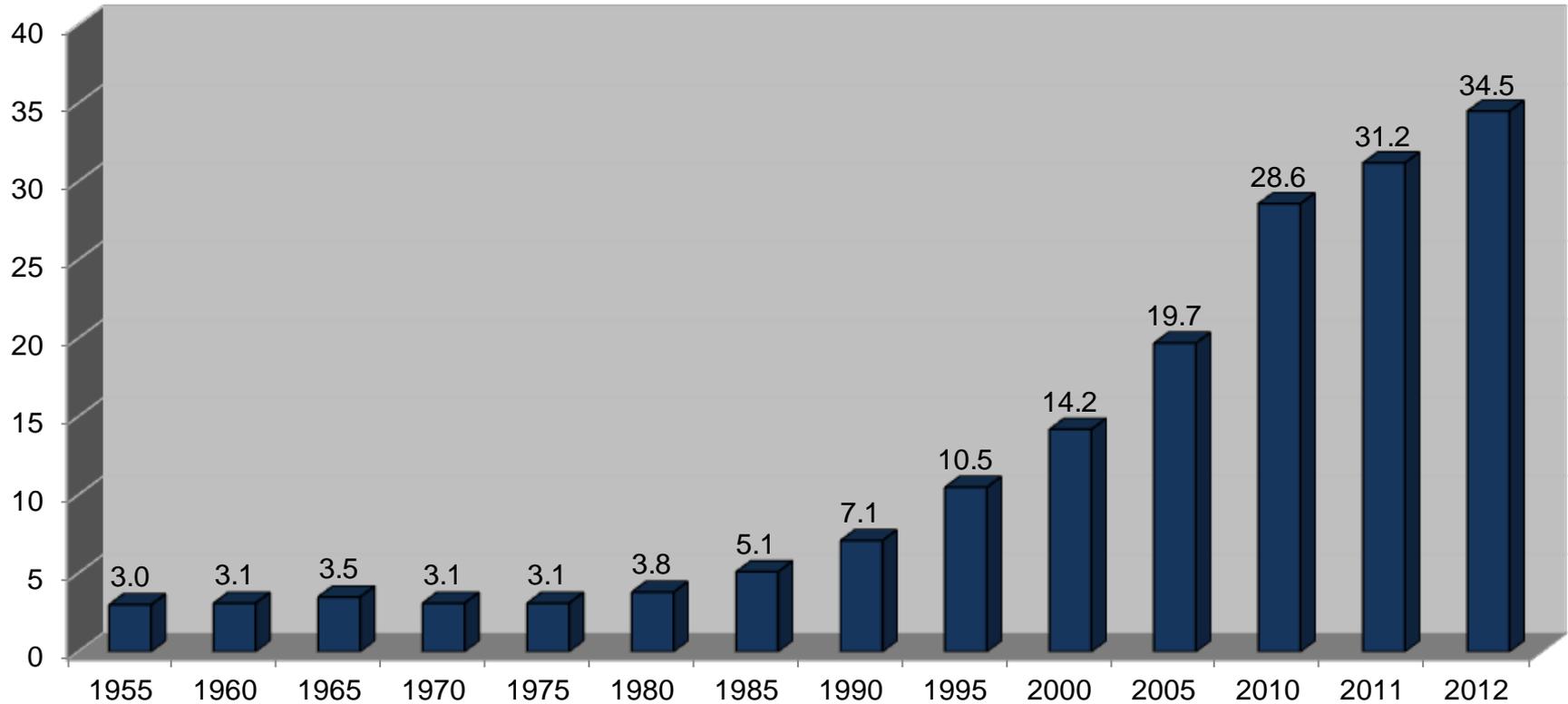
MERS Becoming More Mature

Active Members Per Pension Recipient



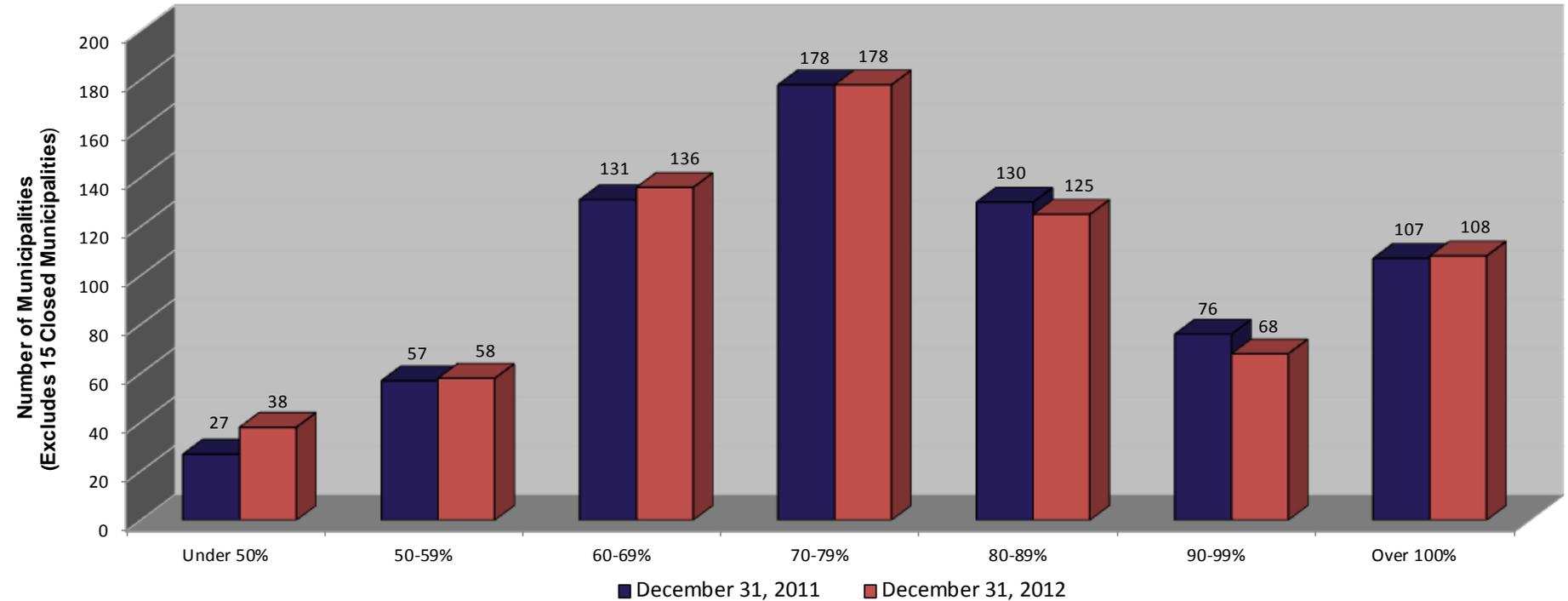
MERS Becoming More Mature

Benefits as a Percent of Pay



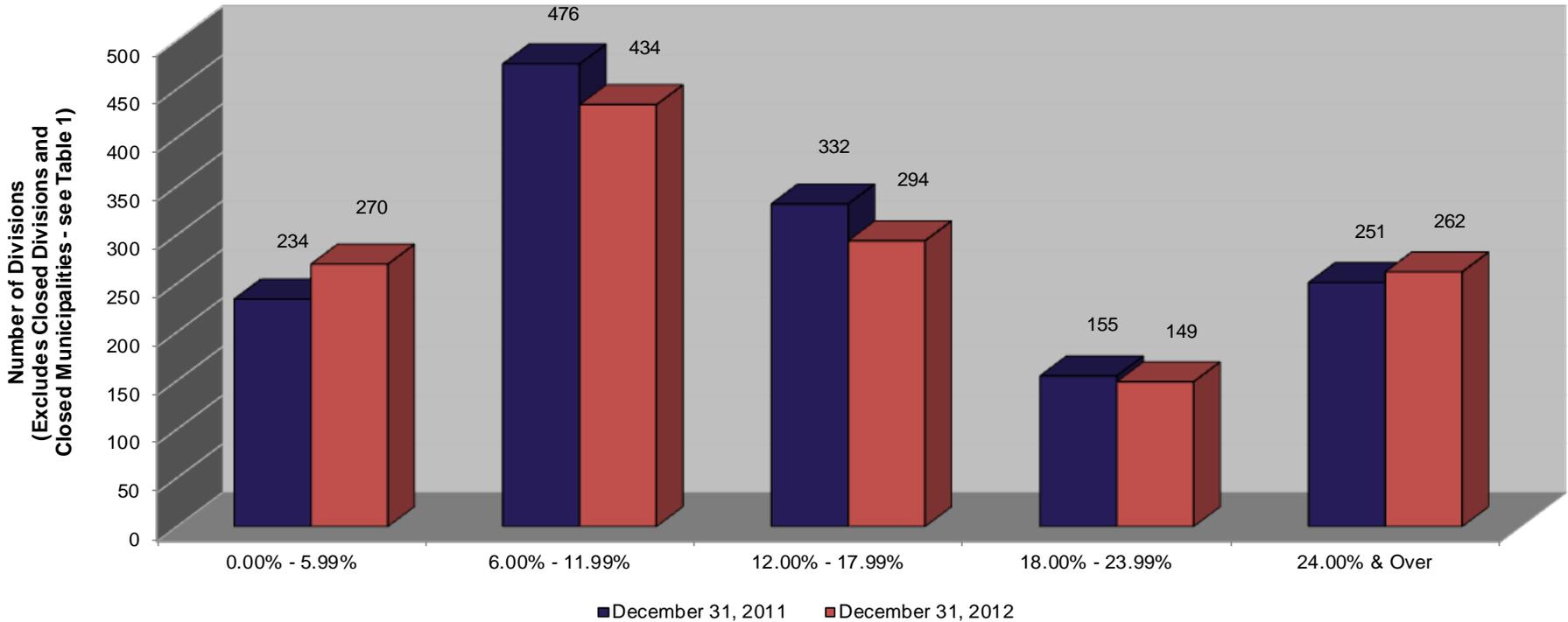
Distribution of Funded Percentages

2011 and 2012 Valuations



67% of all municipalities in MERS are funded at 70% or higher. 15% of all municipalities are funded at 100% or more. The average funded percentage is 80% in 2012 and 81% in 2011.

Distribution of Contribution Rates



The average employer contribution rate (for divisions open to new hires) is 15.14% in the 2012 valuations, and 14.35% in the 2011 valuations. Employer contribution rates vary between divisions as a result of differences in demographics, benefit provisions, and cost-sharing arrangements.

2012 Actuarial Valuation Results

- Every MERS employer stands on its own
- Average funded percentage of employers decreased slightly
 - Normal increase from amortization schedule (+1%)
 - Assumption changes (+1%)
 - Offset by 2008 market loss (-2%)
 - Other experience: retirement, mortality, disability, new benefits, etc. (-1%)
- On average, employer contributions increased by around 9 cents on the dollar, in order to head back toward 100% funded
 - Increases due to the financial markets (2008 market loss)
 - Increases due to amortization policy
 - Decreases due to assumption changes
 - Decreases or increases due to changes in active member pays
 - Other changes due to changes in benefit provisions and other experience
- **Most MERS employers remain in a very strong financial condition**

Comments on the Financial Markets

- Dramatic price declines in 2008
- Average 10+% annual market returns in 2009-2012
- Still plan to meet the average 8% investment return assumption (30 year return is 9.3%, even with 2008 in the average)
- 10-year asset smoothing reduces volatility in the required employer contribution and funded percentage
- 12/31/2012 smoothed assets equal 114% of market value
 - Need future market returns in excess of the 8% assumption, to make up for 2008 experience
 - Otherwise, employer contributions will have to gradually increase over the next 5 years
- Policies ensure that any contribution changes are incremental as opposed to steep

What Does the Future Hold?

- MERS will remain in a very strong financial position
 - For employers that have regularly remitted the required contributions, all benefits will be paid
 - Most MERS employers have assets equal to many times their current benefit payout
- A better than 8% market return is needed to avoid increases in average employer contributions (to make up for 2008)
- Small divisions will continue to have more volatile actuarial valuation results
- Closed divisions will continue to experience increases in required employer contributions of about 5-10% annually, until full funding is reached
- MERS will continue to mature
 - More retirees and higher benefit payout
 - Gradually declining employer contributions (once market losses are made up)
 - Normal for a prefunded retirement plan like MERS



Municipal Employees' Retirement System

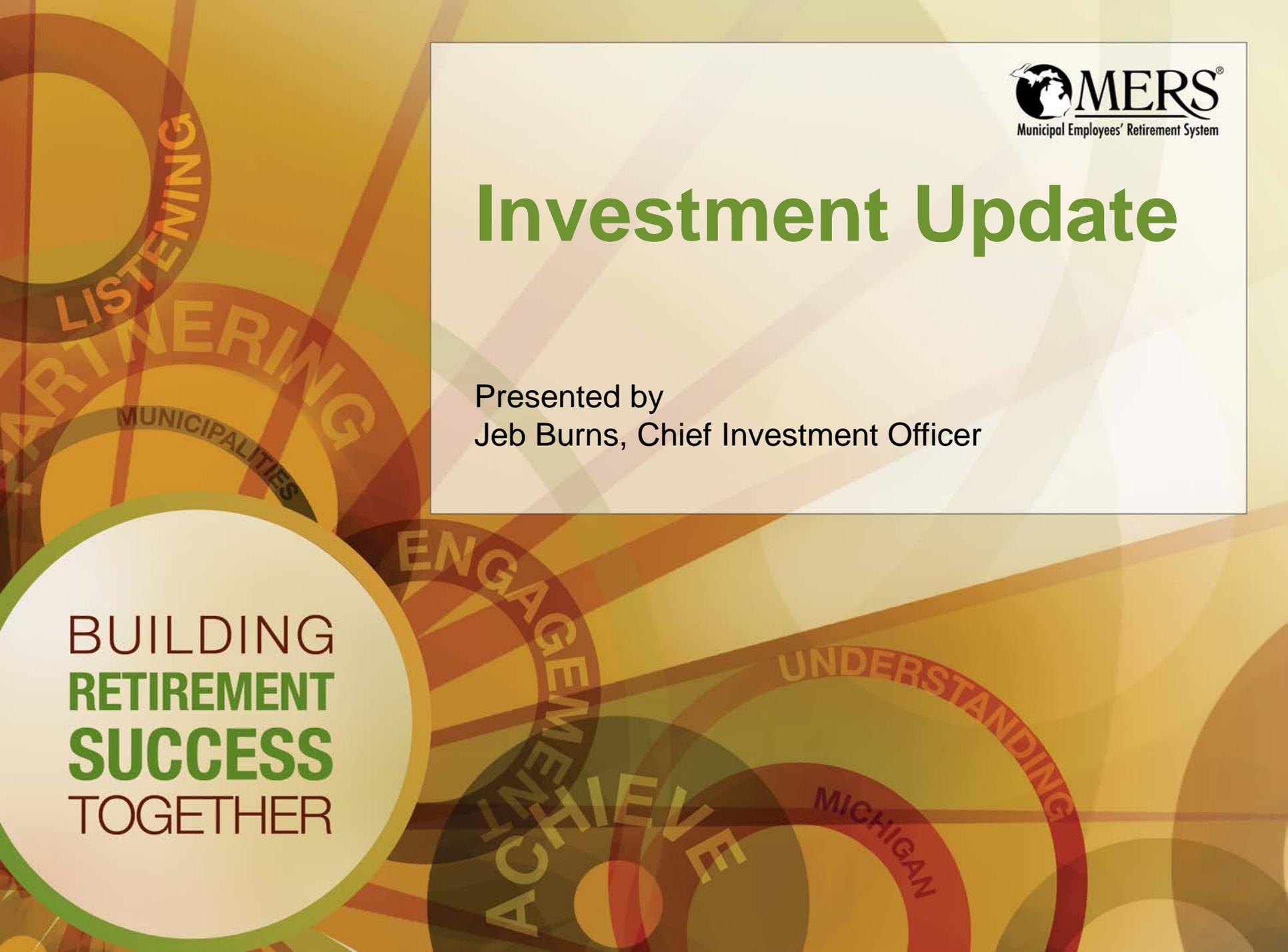
BUILDING
RETIREMENT
SUCCESS
TOGETHER



Investment Update

Presented by
Jeb Burns, Chief Investment Officer

BUILDING
RETIREMENT
SUCCESS
TOGETHER



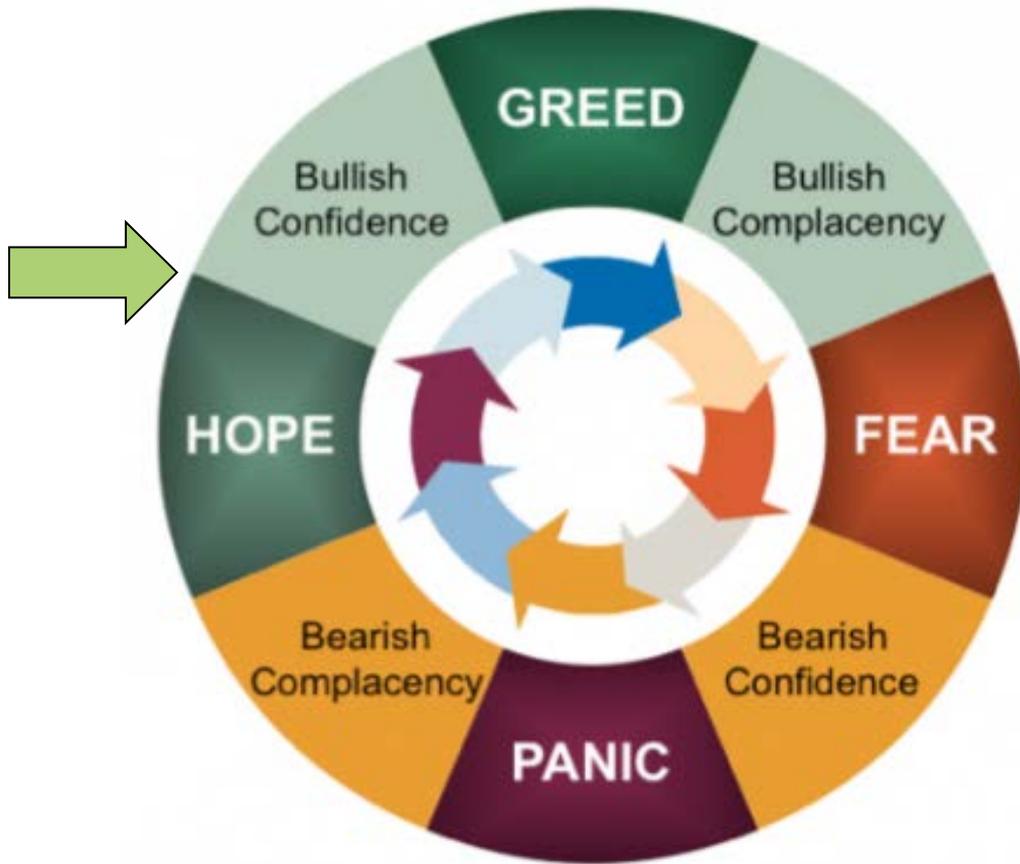
Current Economic Environment

- Global growth expected to accelerate into 2014 as Europe strengthens
 - Eurozone recession ended this year
 - Expected to remain below trend as deleveraging continues
 - Expect moderating yet stable growth in China
- World inflation subdued amid excess capacity and stable commodity prices
 - Political unrest in oil producing countries may result in supply disruption and higher prices

Current Economic Environment

- US housing market recovery expected to be accretive to economic growth
 - Home prices nationwide have risen for 18 consecutive months
- US fiscal policy expected to affect growth and increase uncertainty in markets
- FED expected to continue unprecedented monetary stimulus into 2014
 - Withdrawal of stimulus likely to increase volatility in global markets

Investment Life Cycle



Complacent

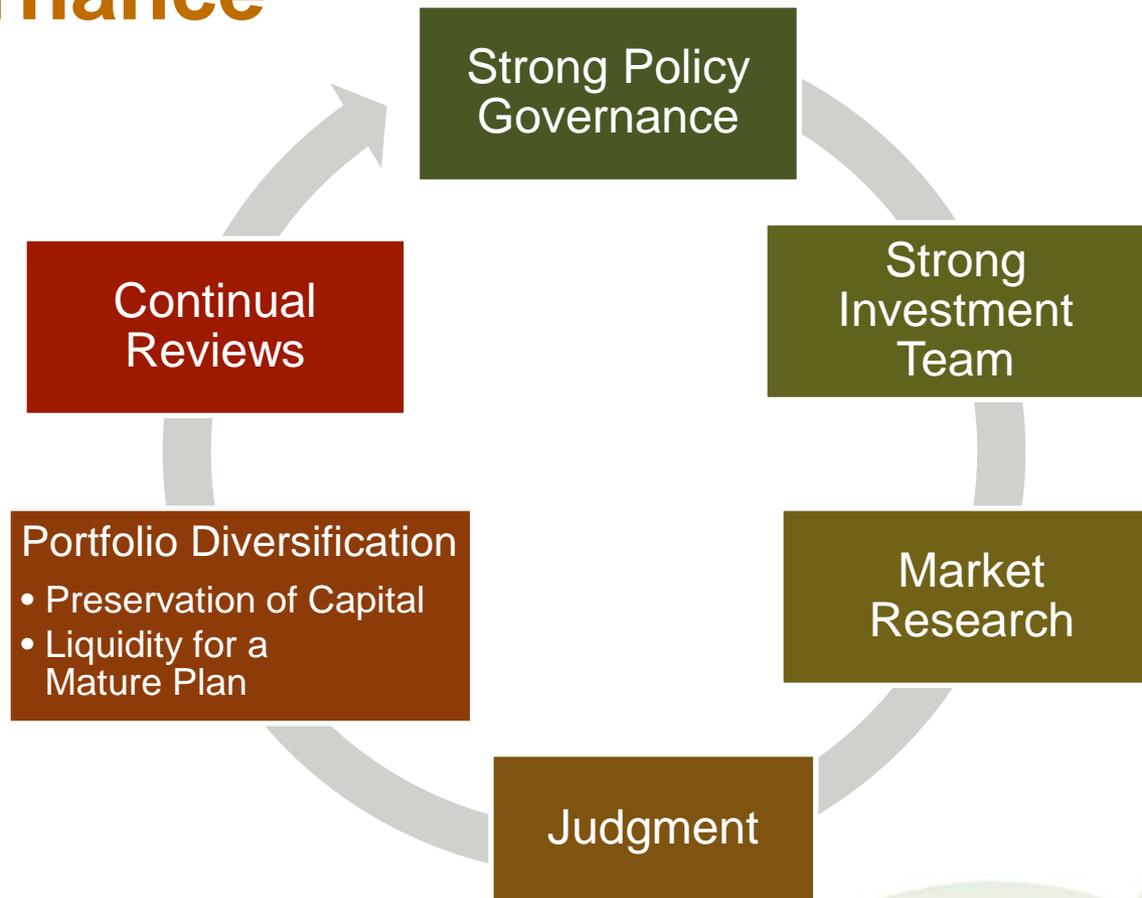
Concerned

Capitulate

Barclays

Contributed by Jordan Kotick, Head of Technical Strategy of Barclays

Disciplined Investors Prepare for Unexpected by Using Best in Class Governance





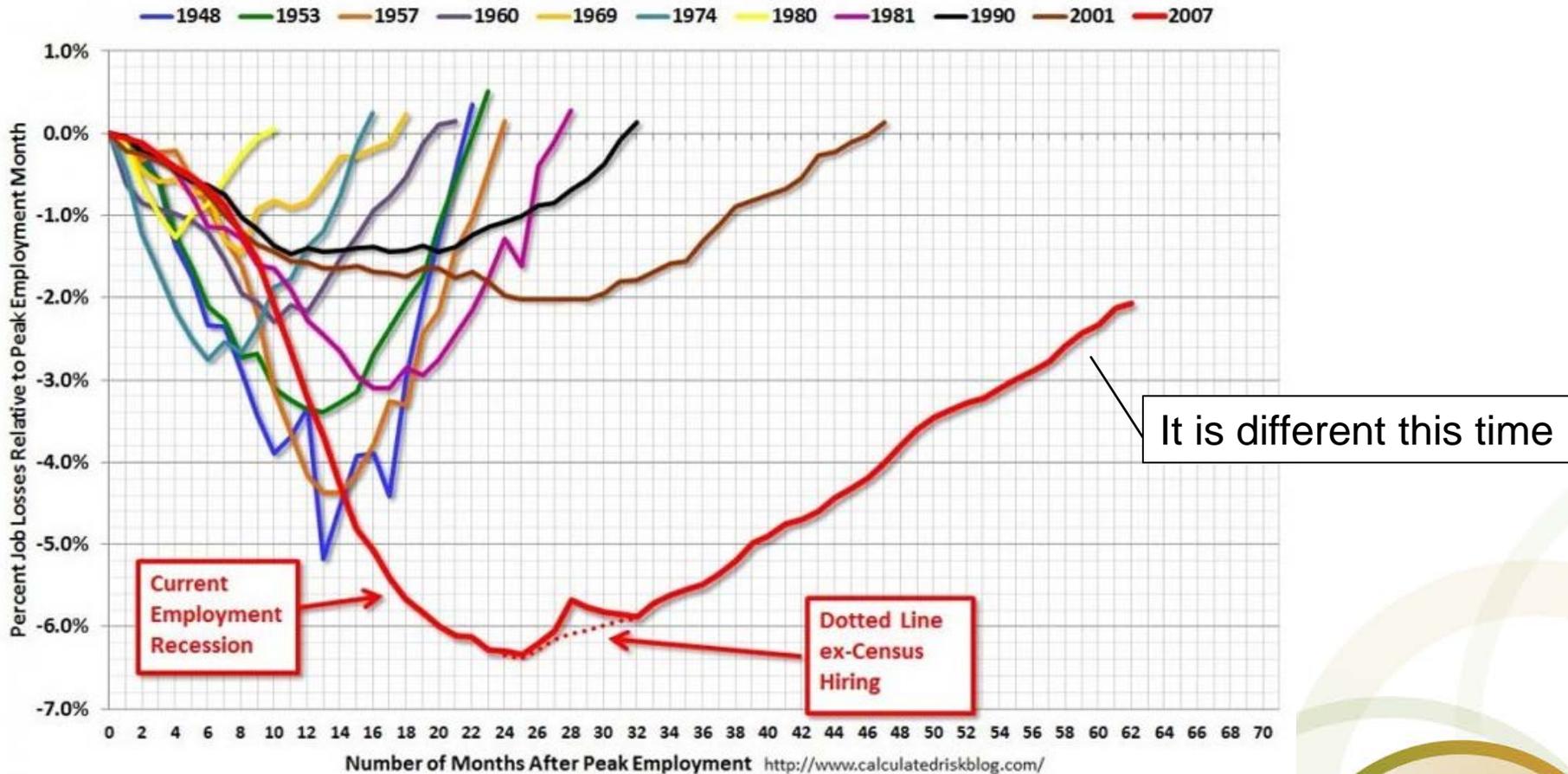
Economic Environment

Performance vs. Fear



It Really Was That Bad!

Percent Job Losses in Post WWII Recessions



1 Year Chart of the 10 Year Treasury Yield



5 Year Chart of 10 Year US Treasury Yield



Interest Rates and the Fed



Policy Response to Unemployment

— Unemployment — Unemployment U6 — 10 Year Treasury



Single Family Housing Starts and Unemployment

Single Family Housing Starts and the Unemployment Rate

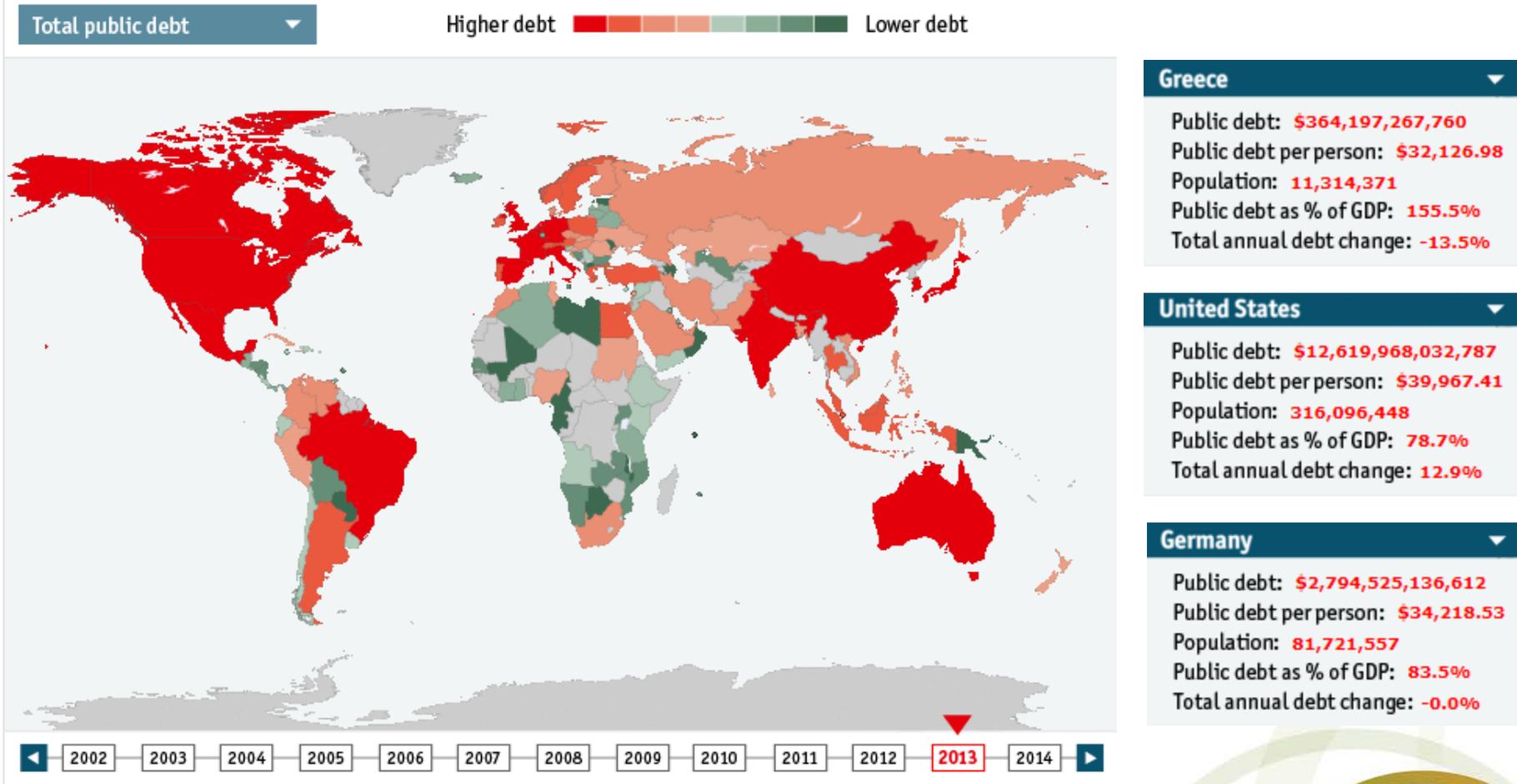
Recession One Unit Structures Unemployment Rate (Inverted)



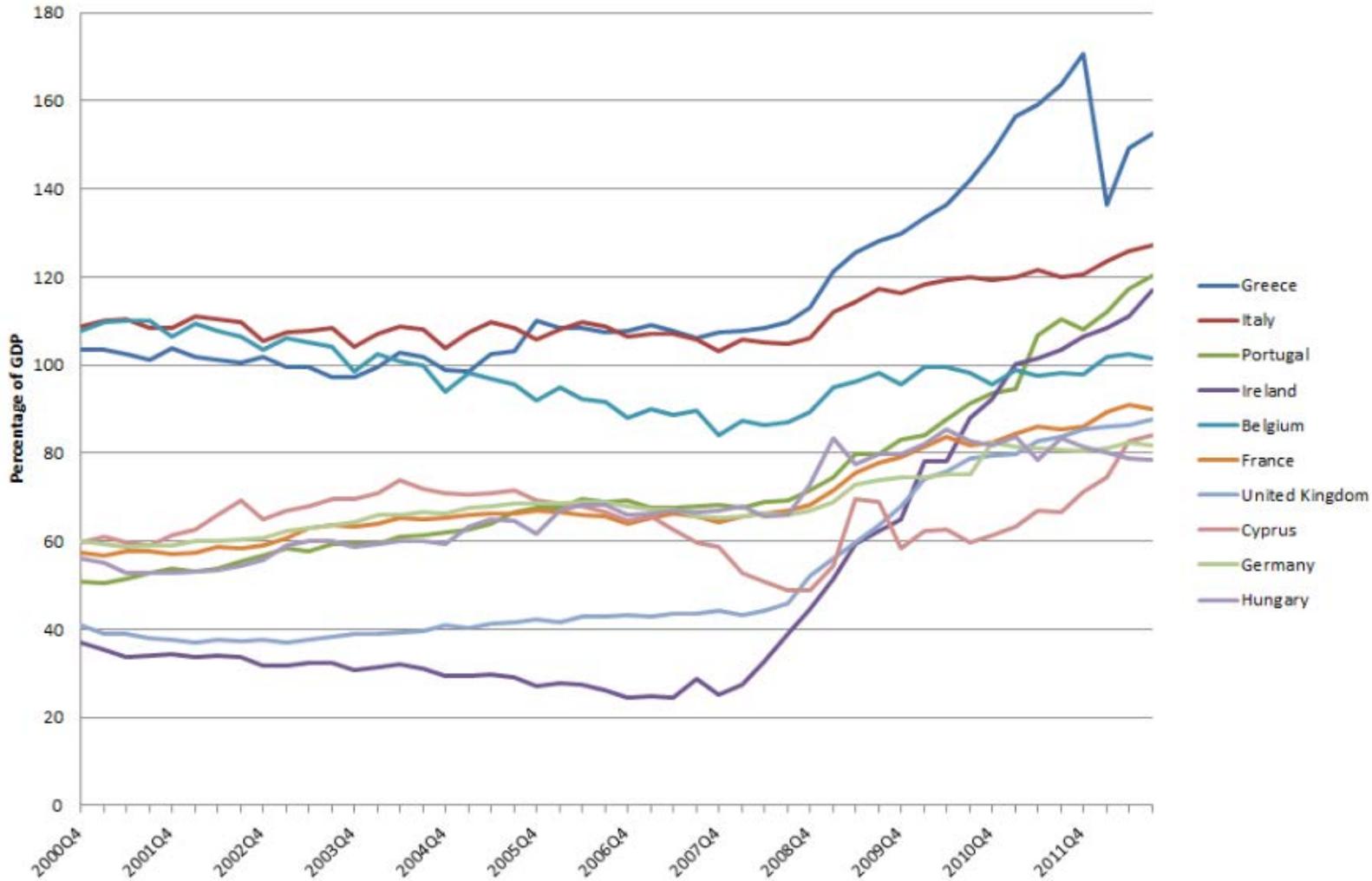
<http://www.calculatedriskblog.com/>

“More Better”

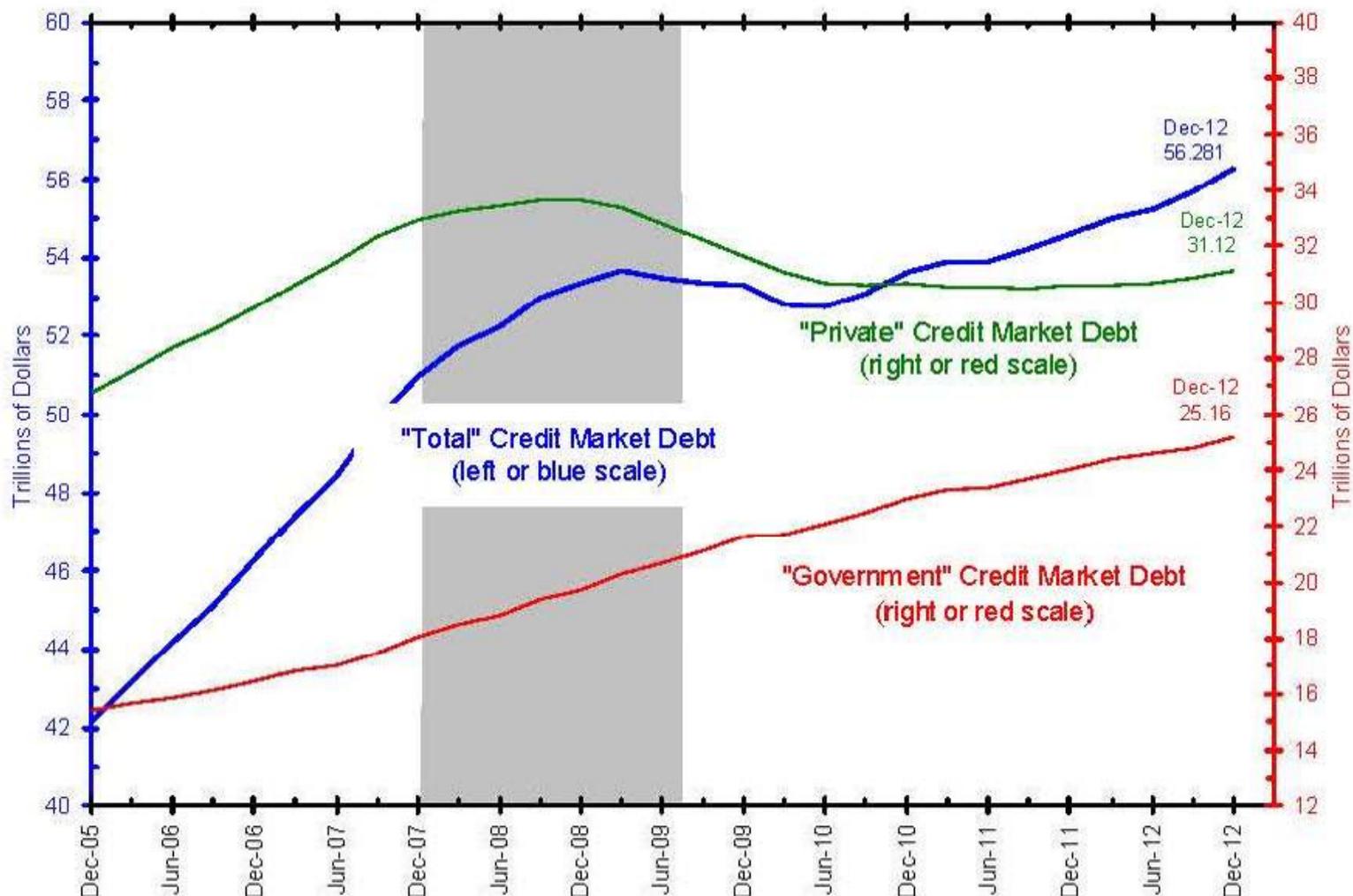
Global Debt Levels



Top Ten Countries Deleveraging



What Deleveraging?



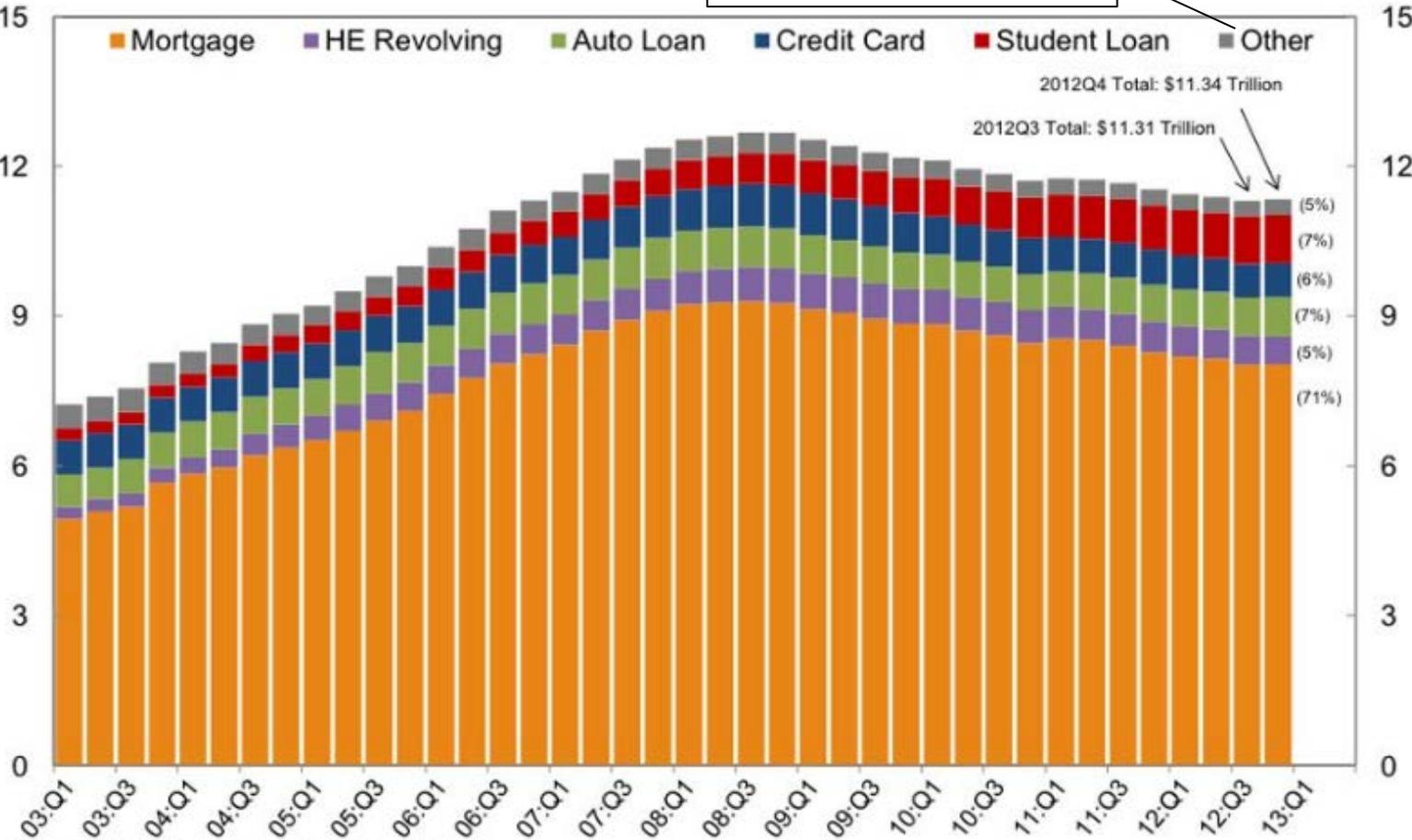
Source: Bianco Research (via The Big Picture)

Consumer Debt Decrease In Q1 '13

Trillions of Dollars

Trillions of Dollars

The next problem?



Source: FRBNY Consumer Credit Panel/Equifax



MERS Roles and Responsibilities

MERS Retirement Board

- Acts as sole fiduciary and sets general investment policy

Investment Committee

- Serve as the Board's investment policy development arm
- Approves recommendations to hire and fire core mandate managers

Portfolio Review Committee

- Internal decision making group
- Makes recommendations to Investment Committee

Office of Investments

- Responsible for day to day investment management activities



Defined Benefit Portfolio Overview

MERS Long-Term Objectives

MERS Defined Benefit Investment Objectives

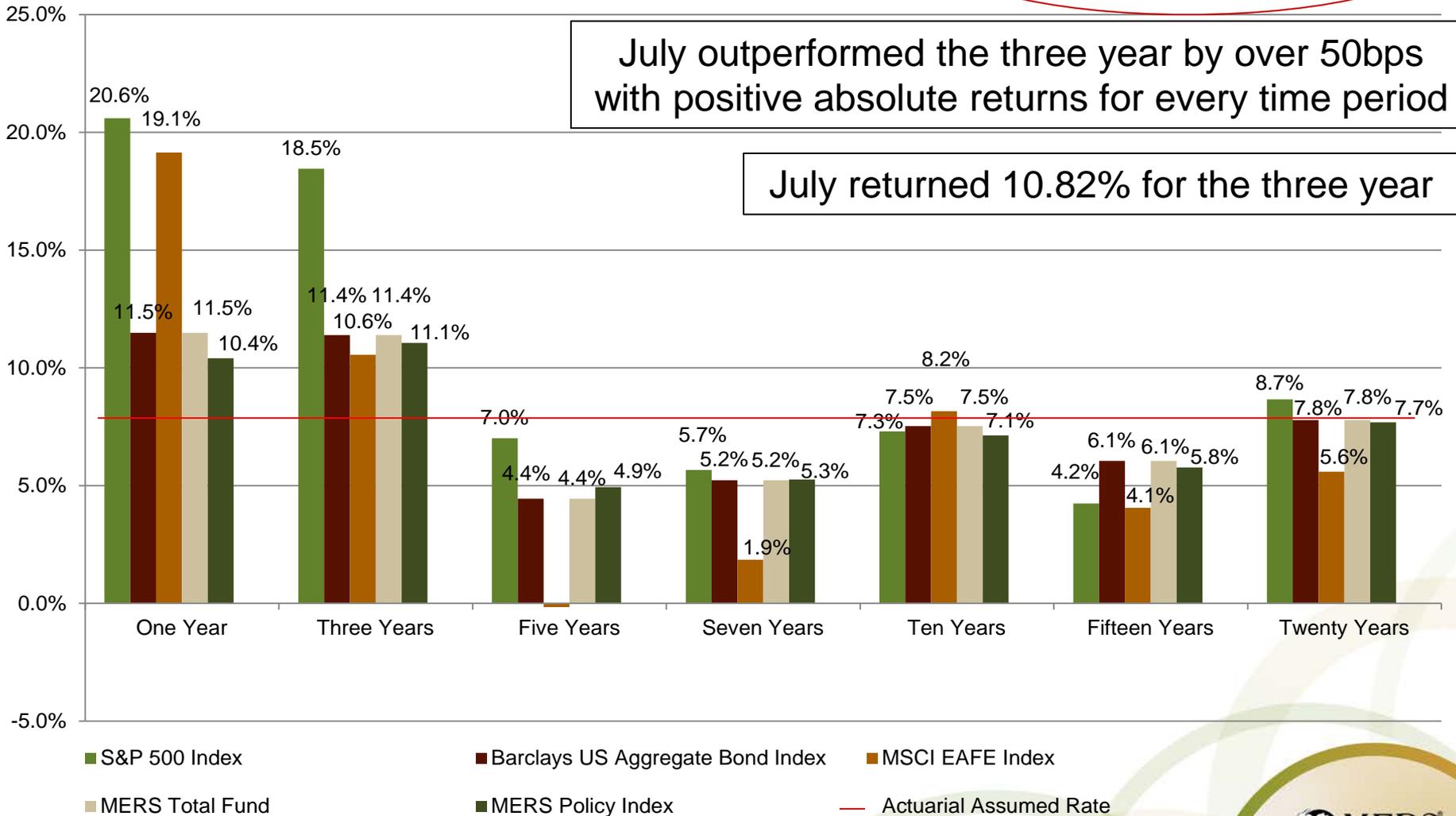
Investment Rate Assumption	8% Return
Strategy	Preserve Capital
Real Rate of Return	Consumer Price Index (CPI) + 3.5%

Historical CPI

As of 9/17/13	1.5%
As of 9/14/12	1.7%
As of 9/15/11	3.8%

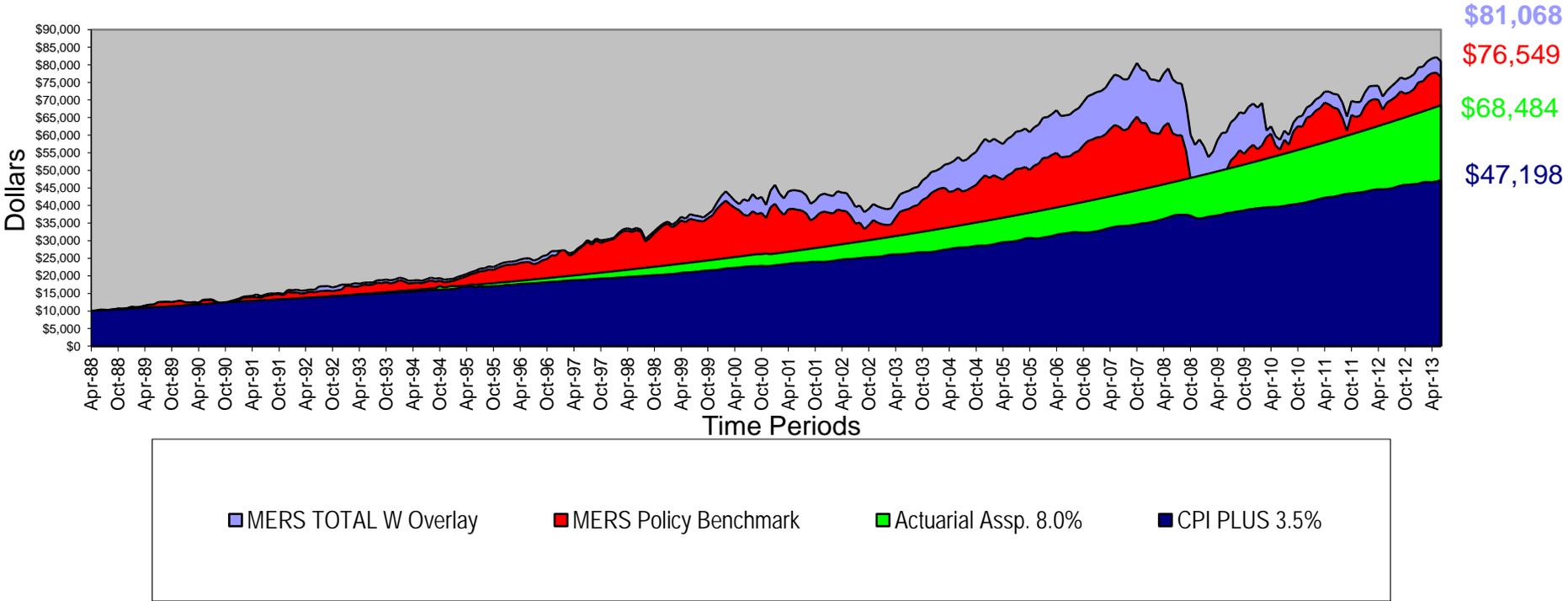
Investment Results

As of 6/30/13,
25 year return: 8.55%

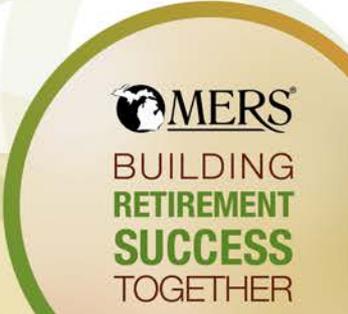


As of June 30, 2013

Growth of \$10,000



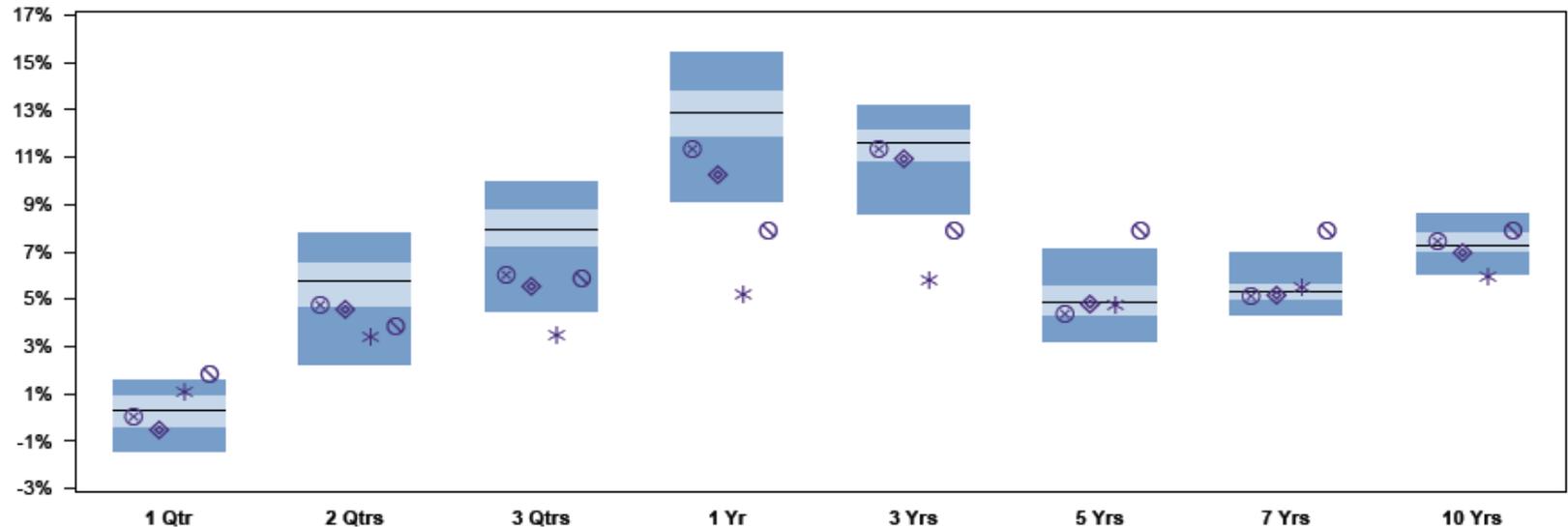
As of June 30, 2013



Management Objectives

- Enhance the portfolio's performance and efficiency
- Maintain above median peer rankings for three, five, and ten year time periods
- Integrate and develop industry best practices into MERS portfolio management model
- Outperform Policy Benchmark for the three year period Net of Fees

Peer Comparison



	1 Qtr	2 Qtrs	3 Qtrs	1 Yr	3 Yrs	5 Yrs	7 Yrs	10 Yrs
5th Percentile	1.60	7.79	9.93	15.44	13.16	7.12	6.93	8.65
25th Percentile	0.94	6.56	8.82	13.86	12.21	5.64	5.70	7.85
50th Percentile	0.27	5.73	7.92	12.86	11.63	4.87	5.35	7.29
75th Percentile	-0.43	4.65	7.17	11.83	10.79	4.24	4.93	6.94
95th Percentile	-1.43	2.24	4.47	9.15	8.61	3.19	4.34	6.10
No. of Obs	67	65	65	65	64	64	63	58
⊗ MERS TOTAL PLAN With O	0.10 56	4.87 70	6.10 85	11.47 81	11.41 55	4.46 69	5.23 58	7.53 39
⊠ Mers Total Plan Custom BM	-0.36 74	4.71 73	5.66 91	10.41 93	11.06 68	4.93 50	5.26 58	7.13 63
* CPI + 3.5% Annually	1.18 15	3.46 87	3.54 97	5.31 100	5.90 100	4.85 51	5.60 32	6.01 96
⊙ Actuarial Rate 8%	1.94 5	3.92 85	5.94 87	8.00 97	8.00 97	8.00 2	8.00 2	8.00 17

MERS External Investment Managers

Fixed Income



First International
Advisors, LLC



OAK STREET *Real Estate Capital*

Stone Harbor
Investment Partners



Domestic & International Equity Management



Alternative Asset Management

The Townsend Group[®]



Australian Pastoral Funds Management

THE CARLYLE GROUP

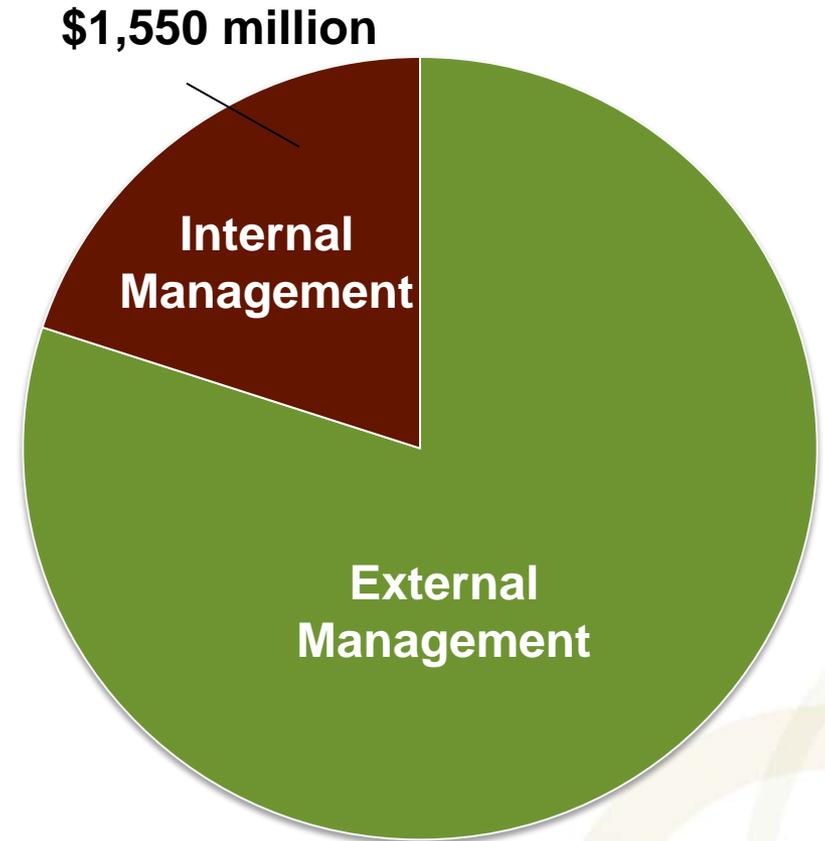
GLOBAL ALTERNATIVE ASSET MANAGEMENT



CenterSquare
INVESTMENT MANAGEMENT

MERS Internal Asset Management

- Domestic Equity Indices
 - S&P 500 Index (Large Cap)
 - S&P 400 Index (Mid Cap)
 - S&P 600 Index (Small Cap) - 2014
- Domestic Equity Active Management
 - Micro Cap
- Short-term Fixed Income Portfolios
 - Dedicated Cash
 - Commodities
- Tactical Cash Management



As of June 30, 2013

Cost-Effective Investment Management Fees

Total Portfolio*	21.54 bps
<u>Portfolio Income**</u>	<u>6.10 bps</u>
Net Portfolio Expense	15.44 bps

bps = Basis Points or 0.01% 100 bps is equal to 1%.

* *Total Portfolio expenses paid from cash (Annualized)*

** *Portfolio Income = Securities Lending and Commission Recapture*

As of June 30, 2013



Participant Directed Account Overview

MERS Program Asset Totals

Defined Benefit Plan	\$7.0B
Defined Contribution Plan	\$ 421.2 M
Retiree Health Funding Vehicle	\$ 436.0 M
Health Care Savings Program	\$ 74.4 M
Investment Services Program	\$ 8.6 M
457 Supplemental Savings Program	\$ 9.7 M
Total	\$ 7,949.9 B

As of June 30, 2013

MERS Investment Menu

- Historically, participants have had to make a lot of complex decisions in a self-directed plan
- MERS sought to improve participant outcomes by developing a strategic and streamlined investment menu
- The MERS Investment Menu has a concentrated list of options to provide quality over quantity, following industry best practices
 - Options are grouped into four logical “sleeves” that participants can identify with, which assists in simplified decision making

MERS Retirement Strategies

- Default fund for the MERS Defined Contribution Plan
- Nearly half of participants are in the MERS Retirement Strategies funds (47.6%)

Benefits of MERS Investment Menu

- MERS is the fiduciary, meaning we have an obligation to place the participant's interest first in making any decisions about the plan
- The MERS Retirement Board and the MERS Office of Investments:
 - Actively monitors and select the fund lineup and investment managers
 - Ensures quality investment options are offered
 - Negotiates fees that individuals would not be able to negotiate on their own



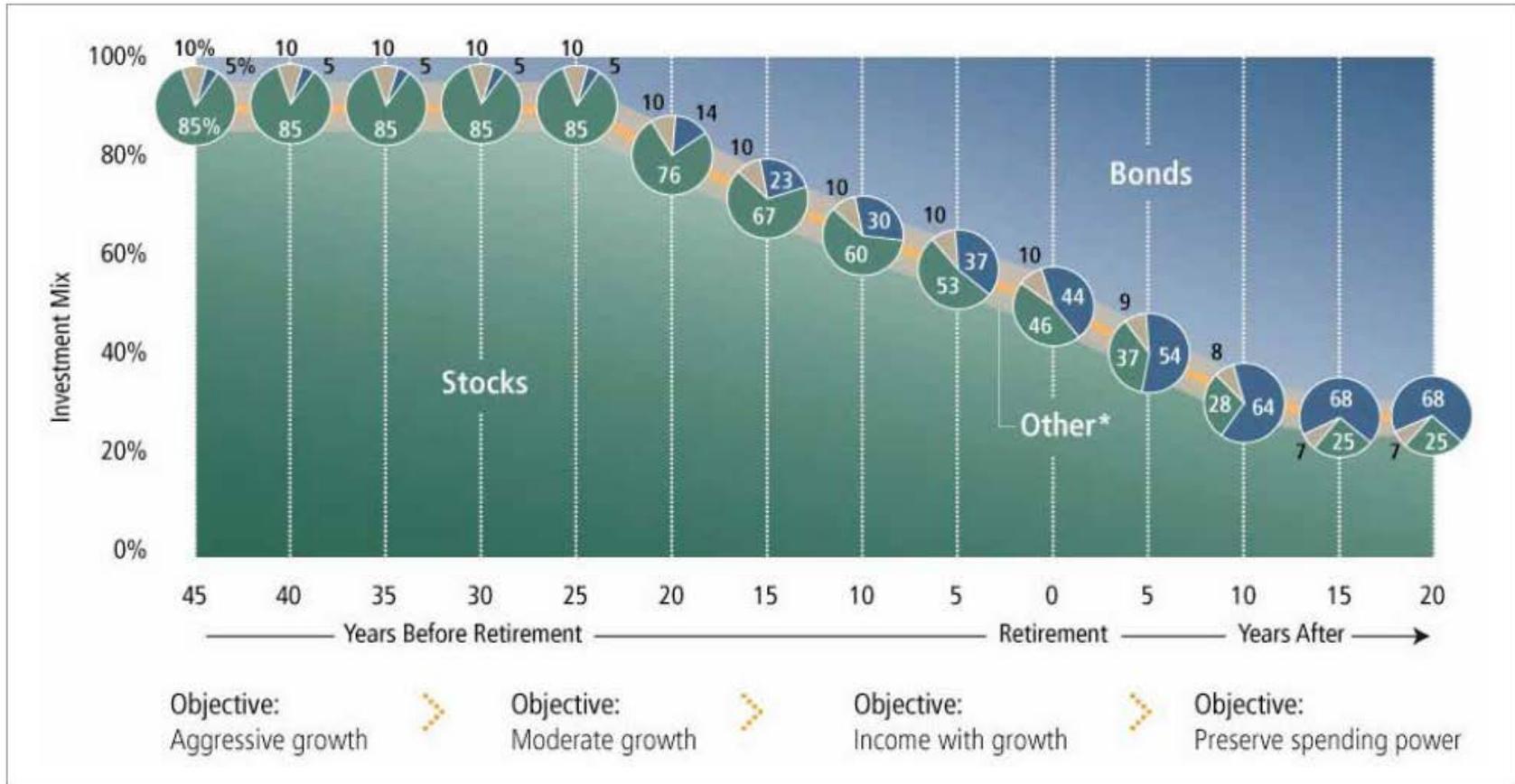
Retirement Strategies

Target Date Funds

For those who want a simplified way to invest

- Complete diversified investment fund
- Assets change from aggressive to conservative as participant approaches selected retirement age and through retirement
- Default investment selection, based on projected retirement age 60

How the Glide Path Works



*Other includes Global Real Estate Investment Trusts (REITs) and Commodities



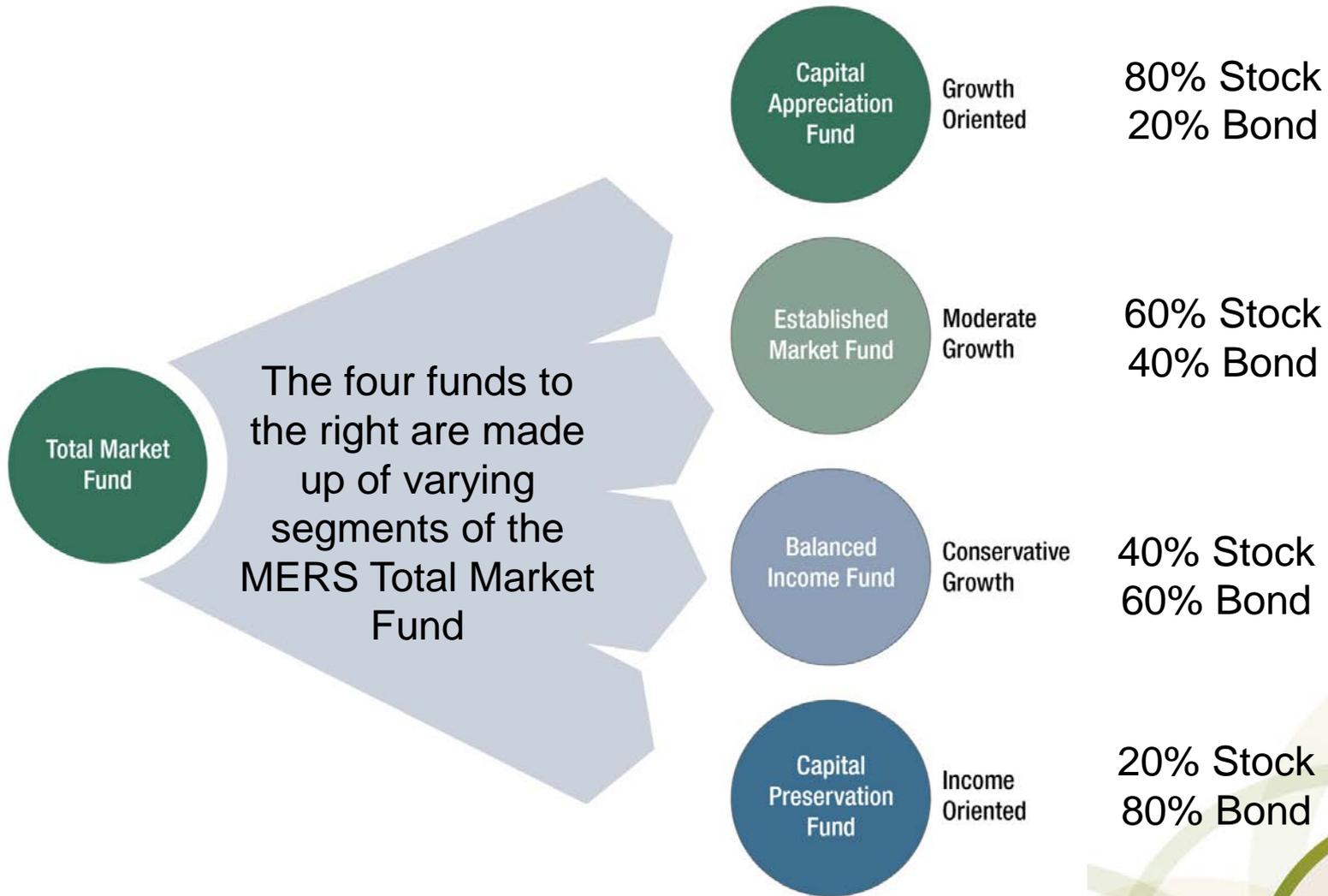
Diversified Portfolios

MERS-managed portfolios

For those who want a fully diversified, professionally managed portfolio they are in charge of changing

- Professionally managed by MERS
- Customized to participant's risk preferences
- Each have target allocation mix rebalanced (or readjusted) quarterly

How Diversified Portfolios Work



3

Expanded Funds

Building and fine-tuning your own portfolio

For the investor who knows their goals, risk tolerance and time horizon and wants to build or add to their current portfolio

- Gives experienced investors a variety of funds to select from
- Can be a great addition to the other categories and help to further diversify investment portfolio and fine-tune strategy
- MERS actively monitors the selection of funds to ensure quality

4

Self-Directed Brokerage Window

More choices for experienced investors

For the experienced investor who wants access to even more options

- Gives access to over 1,000 additional investments:
 - Individual securities
 - Mutual funds in a variety of share classes
- Certain restrictions apply

Benefits of MERS

- MERS takes on fiduciary responsibility
 - We proactively maintain the IRS qualified status of plan
- We actively manage the investment menu to ensure quality funds are offered to participants
- Fees
 - One of the greatest benefits provided by MERS is our ability to pool assets
 - We follow the Department of Labor fee disclosure rules

Selection and Monitoring of Menu Options

- Performance exceeding 50th percentile of peers over last three years
- Institutional share class availability
- Morningstar rating of three stars or higher
- Expense ratio better than peer average
- Stability of the investment team
- Reputation of the fund company
- Outside mutual funds must meet above objectives

Contact Us

MUNICIPAL EMPLOYEES' RETIREMENT SYSTEM

1134 Municipal Way

Lansing, MI 48917

800.767.2308

Fax: 517.703.9707

www.mersofmich.com

www.mymers.mersofmich.com

This presentation contains a summary description of MERS benefits, policies or procedures. MERS has made every effort to ensure that the information provided is accurate and up to date. Where the publication conflicts with the relevant Plan Document, the Plan Document controls.



Municipal Employees' Retirement System

BUILDING
RETIREMENT
SUCCESS
TOGETHER

