

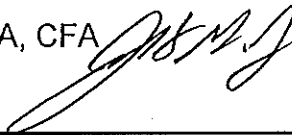
**Commonwealth of Pennsylvania
Public School Employees' Retirement System**

DATE: July 28, 2014

SUBJECT: Proposed Revisions to Exhibit E of the Investment Policy Statement, Objectives, and Guidelines

TO: Members of the Finance Committee

FROM: James H. Grossman, Jr., CPA, CFA
Chief Investment Officer



At the August 5, 2014 Finance Committee Meeting, we will request that the Committee adopt the proposed revisions to Exhibit E of the Investment Policy Statement, Objectives, and Guidelines ("IPS"). A black-lined version is included with the Finance Committee package for your review.

Exhibit E – Public Market Investment Manager Target Ranges

Subsequent to the adoption of the asset allocation plan in June by the Board, we noted that certain target ranges did not provide staff with the ability to meet the allocation targets, specifically in the risk parity allocation. We increased the permissible ranges for both the internal and external risk parity managers to be consistent with our planned allocation increase which is effective October 1, 2014. In addition, we made some other revisions which include adding the internally managed gold index portfolio as a separate commodity portfolio and eliminating the U.S. micro cap equity and the externally managed unsecured consumer credit portfolios which are not part of our current allocation.

If you have any questions regarding the changes to Exhibit E, please contact me at 717-720-4703.

Exhibit E – Public Market Investment Manager Target Ranges

All allocations to individual Investment Manager portfolios shall be subject to the limits established by the Board through the Current Target Allocation in **Exhibit C**. IOS is permitted to manage the allocation of capital to each Investment Manager portfolio within the target ranges to public market Investment Manager portfolios of the total fund noted below. The CIO shall have discretion on the timing of reducing any Investment Manager portfolio exceeding the maximum ranges approved below. However, the CIO is not permitted to allocate additional capital to those portfolios currently above the target ranges.

	<u>Target Ranges as a Percentage of the Total Fund</u>
<u>Equity Portfolios:</u>	
Public Markets U.S. Equity Portfolios	
Internally Managed S&P 500 Index	0.0% - 20.0%
Internally Managed S&P 400 Index	0.0% - 2.5%
Internally Managed S&P 600 Index	0.0% - 2.5%
U.S. Style-Oriented Small Cap Equity	0.0% - 1.0%
U.S. Micro-Cap Equity	0.0% - 0.5%
Internally Managed Synthetic Beta Replication ²	0.0% - 5.0%
Public Markets Non-U.S. Equity Portfolios	
Internally Managed MSCI ACW Index ex. U.S.	0.0% - 15.0%
Internally Managed MSCI World Small Cap Index ex. U.S.	0.0% - 2.5%
Internally Managed MSCI Emerging Markets Index	0.0% - 2.5%
Non-U.S. Equity	0.0% - 2.5%
Non-U.S. Small Cap Equity	0.0% - 1.0%
Emerging Markets Equity	0.0% - 1.0%
Internally Managed Synthetic Beta Replication ²	0.0% - 5.0%
Foreign Currency Hedge Overlay	Up to 100% of the Foreign Currency Exposure
<u>Fixed Income Portfolios:</u>	
Investment Grade Portfolios	
Internally Managed U.S. Core Fixed Income	0.0% - 5.0%
U.S. Core Plus or Non-U.S. Developed Fixed Income	0.0% - 2.0%
Internally Managed U.S. Long Treasuries ³	0.0% - 1.0%
Internally Managed Synthetic Beta Replication ²	0.0% - 5.0%
Credit-Related Portfolios	
Emerging Market Fixed Income	0.0% - 1.5%
U.S. High Yield Fixed Income	0.0% - 2.0%
Multi-Sector Fixed Income Portfolios	
Inflation Protected (TIPS) Portfolios¹	
Internally Managed U.S. TIPS	0.0% - 5.0%
U.S. and Non-U.S. TIPS	0.0% - 4.0%
Internally Managed Synthetic Beta Replication ²	0.0% - 2.0%

¹ The total TIPS portfolios may be leveraged up to 3.3 times in aggregate.

² The maximum amount of internally managed synthetic beta replication will be 911% of the total fund (excludes beta synthetically replicated within the actively managed and indexed Separate Account portfolio).

³ The U.S. Long Treasury Portfolio will be notionally funded subject to a maximum notional value of 6% of the total market value of the fund. The capital allocated to this portfolio will be for margin requirements and to settle margin variation.

Target Ranges
as a percentage
of the Total Fund

Real Asset Portfolios:

PTRES Portfolios

U.S., Non-U.S., and Global PTRES	0.0% - 1.0%
Internally Managed Synthetic Beta Replication ²	0.0% - 2.0%

Master Limited Partnership Portfolios

Externally Managed Enhanced and Full Discretion	0.0% - 1.5 2.0%
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Commodities Portfolios

Externally Managed Full Discretion and Enhanced Index Commodity	0.0% - 2.0%
Internally Managed Enhanced Commodities Index Portfolio	0.0% - 2 4.0%
Internally Managed Gold Index Portfolio	0.0% - 4.0%
Internally Managed Synthetic Beta Replication ²	0.0% - 2.0%

Risk Parity Portfolios:

Externally Managed Risk Parity Portfolios	0.0% - 2.5 4.0%
Internally Managed Optimal Liquid Beta Portfolio	0.0% - 4.0 5.0%

Absolute Return Portfolios:

0.0% - 2.0%

Short Duration Fixed Income Portfolios:

Internally Managed LIBOR-Plus Short-Term Investment Pool	0.0% - 8.0%
Externally Managed LIBOR-Plus Short-Term Investment Pool	0.0% - 5.0%
Externally Managed Short Duration Non-Agency RMBS Portfolios	0.0% - 1.0%
Externally Managed Unsecured Consumer Credit Portfolios	0.0% - 1.0%
Internally Managed Short-Term Investment Pool	No limit

PMEIM Program Portfolios	0.0% - 0.3%
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Internally Managed Synthetic Beta Replication represents market exposures in the various asset classes achieved through Derivative exposures such as futures, options, swaps, etc. IOS will synthetically achieve beta exposures to either assist in a transition from one actively managed portfolio to another or to generate alpha. It excludes synthetic beta replication within the actively managed and indexed Separate Account portfolios.

² The maximum amount of internally managed synthetic beta replication will be 911% of the total fund (excludes beta synthetically replicated within the actively managed and indexed Separate Account portfolio).