

July 2014



PENSION RESERVES
INVESTMENT
MANAGEMENT BOARD

PRIM Board Update

Massachusetts Pension Reserves Investment Management Board

Global Markets Snapshot for July 2014

Most equities lost ground in July, mostly on the last day of the month, as Gross Domestic Product (GDP) strengthened (good news is bad news). Small Caps sold off -6% in July, Large Caps fell 1.4%. The Small Cap selloff was due to high valuations, muted earnings growth, and expectations for higher interest rates (small caps are most sensitive to interest rates). The VIX (an index that measures market volatility) was at 17.0 vs. 11.4 last month and 20.2 over five years. Higher-dividend sectors (Utilities, Health Care, Telecom) outperformed calendar-year-to-date (CYTD) as a fall in interest rates supported investors' search for yield. Developed markets have outperformed emerging longer term, but Emerging Markets Equities (EME) picked up steam in May and July, outperforming CYTD: EME +8.4% vs. S&P 500 +5.7%. Russia tensions escalated as the Malaysian airplane was shot down in Ukraine, and US & European Union (EU) imposed economic sanctions on Russia (Russian equities -8% in July and -13% CYTD; Russian ruble depreciated -5% in July and -8% CYTD). Chinese equities (20% of EME Index) were up 8% in July on positive economic news, a cut to banks' reserve rate requirement, optimism the government will achieve its economic growth target for this year (7% - 7.5% GDP growth), and general economic reforms. The market continues to be surprised with Treasury strength. The yield curve flattened in July (30-year yields fell 4 basis points (bps) to 3.32%, 10-year yields rose 3 bps to 2.56%). The yield curve also flattened CYTD with the long end falling and the short end rising: 30 year yields are 66 bps lower than 12/31/13; 10-year yields are 48 bps lower than 12/31/13; and 2-year yields are 14 bps **higher** than 12/31/13 as market price in a faster or sooner Fed rate hike. 20+ Year STRIPS Index: +23.2% CYTD, +1.4% in July, and +9.3% since PRIM's initial funding in April 2014. Investor demand for long Treasuries is driven by: lower sensitivity in long end to central bank policy, liability-driven investing (corporate pension plans), and STRIPS issuance increasing. Credit spreads remain tight. High Yield (HY) sold off -1.3% in July, while Investment Grade (IG) Credit was flat - general yield grabbing trade reversal. HY - IG spread widened from 257 bps to 309 bps. Investment grade credit was 95bps over US Treasuries (UST) vs. 132 bps one year ago and 174 10-year average). HY credit was 404 bps over UST (vs. 471 bps one year ago and 562 bps over a 10-year average). Bank loans were 443 bps over UST (vs. 499 bps on a 10-year average).

Market Recap – July 31, 2014

Global Equity Markets

U.S. Equities:

Index	Month	CYTD	1-Year
S&P 500	-1.38%	5.66%	16.94%
Dow Jones Industrials	-1.44%	1.20%	9.39%
NASDAQ (Price Change)	-0.87%	4.63%	20.50%
Russell 2500	-4.92%	0.74%	12.08%

International Equities:

Index	Month	CYTD	1-Year
Custom World IMI Ex-US	-1.87%	3.48%	15.91%
MSCI Emerging Mkts. IMI	1.92%	8.47%	15.35%

Fixed Income

Index	Month	CYTD	1-Year
Barclays Aggregate	-0.25%	3.66%	3.97%
ML High Yield Master II	-1.32%	4.24%	8.28%

Real Estate

NCREIF 1-Qtr Lag Private	0.00%	5.34%	11.18%
FTSE EPRA NAREIT Global	0.33%	12.48%	13.27%

Hedge Funds

Index	Month	CYTD	1-Year
HFRI Fund of Funds	-0.59%	1.44%	5.85%

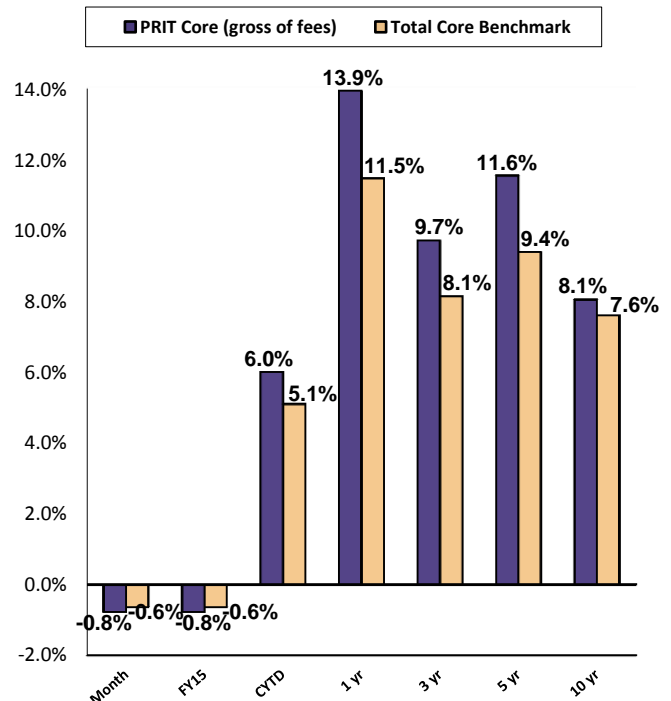
PRIT FUND ASSETS: \$60,301,895,000

PRIT Core Fund Recap – July 31, 2014

Portfolio	Month	CYTD	1-Year
PRIT Core Total	-0.78%	6.01%	13.94%
U.S. Equity	-2.13%	4.43%	15.95%
International Equity	-1.89%	3.70%	16.16%
Emerging Markets Equity	1.35%	7.30%	14.50%
Core Fixed Income	0.35%	5.73%	5.84%
Public Value Added FI*	-0.69%	4.89%	5.87%
Total Value Added FI**	-0.59%	5.93%	8.69%
Private Equity	-0.63%	12.82%	25.76%
Core Real Estate	0.40%	8.04%	13.12%
Timber/Natural Resources	-1.06%	4.69%	11.08%
Hedge Funds (net of fees)	-0.52%	3.97%	9.20%

Returns are gross of fees unless otherwise noted. Timber/Natural Resources and Total Value-Added Fixed Income sleeves are currently not available through Segmentation; however, the *Public Value Added Fixed Income sleeve is available as of April 1, 2013. **Total Value-Added FI includes return of Public Value-Added FI. Private Equity is available to Segmented Systems through the Vintage Year Program.

PRIT Core Fund as of 7/31/2014



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