The Board of Pensions of the Presbyterian Church (U.S.A.)

2013 INVESTMENT REVIEW
THE BOARD OF PENSIONS BALANCED INVESTMENT PORTFOLIO

Who is in Charge?

Shakespeare, Bonhoeffer and Noble

The Balanced Investment Portfolio Returns 17.1% in 2013

Drivers of Global Investments in 2013

Wars and Politics

Cry "Havoc!" and let slip the dogs of war.
William Shakespeare, **Julius Caesar, 1599**

The past is prologue. Mark Antony fomented civil unrest in Rome following the assasination of Julius Caesar on the Ides of March, 44 BC. In 2013 the dogs of war slipped their bonds and went wild in civil wars and unrest that Mark Antony could relate to, with civilian deaths and plunder in Afghanistan, Egypt, Iran, Iraq, Israel, Libya, Ukraine, Sudan, Syria, Palestine, Thailand, Turkey, and other countries unfortunately too numerous to mention. Mark Antony was also a student of politics and would have smiled at the gridlock in the U.S. capital in 2013, with sequestration, government shutdown and a final last minute mini-bargain.

Outcome: Stock markets in the U.S., Japan and Europe ran with the bulls and ignored the dogs of war.

Pessimism/Optimism

It is more prudent to be a pessimist. It is an insurance against disappointment, and no one can say, "I told you so," which is how the prudent condemns the optimist.
Dietrich Bonhoeffer, **Letters and Papers from Prison, 1945**

Outcome: 2013 was the second year in a row that the cockeyed optimist slew Debbie Downer. We fought the wall of worry for most of 2013, but Ms. Market won out in the end.

In Charge

We are not in charge.
We are not in charge of life.
We are not in charge of much about life.
O, we can do many things,
And we are responsible for many things,
But in the final analysis,
We are not really in charge.
Dr. James Phillips Noble, **Words and Images that Seep into the Soul, 2013**

Outcome: We like to think we are masters/mistresses of the universe, in charge of everything we survey. The reality is that we are not the grand mistresses of events from mundane grocery shopping and ordering prescriptions online, to global stock markets, interest rates and the actions of the Federal Reserve in the U.S., the European Central Bank or the Bank of Japan. We must admit it. We are not really in charge. We like to think we are, that we can profit from our understanding of the direction of markets. In 2013 it was up, down and sideways in more than 50 global markets and currencies. We like to think we are, but we are not really in charge.

We are not in charge of markets. Yet there are many things we were in charge of in 2013 that benefited our Plan Members.

2013 was a good year for the Balanced Investment Portfolio. While we were not in charge of wars, politics and the direction of global markets, we were in charge of manager selection and asset allocation and we did a good job for our Plan Members.

Before we begin a detailed review of the 2013 performance of the Board of Pensions Investment Portfolio, we need to re-visit the 2012 Investment Review for our investment outlook for 2013.

2013 Investment Outlook Versus Actual Results

- **2012 Outlook:** Global investors in equity and debt markets will face challenges in 2013. There are few clearly undervalued asset classes as we enter 2013, so it should be a year for managers gifted in security selection. We believe we have retained those managers in our relationships we can be proud of.
  2013 Actual: Success. Active management added value. The Balanced Investment Portfolio outperformed passive index benchmarks for U.S. equity, international equity and fixed income.

- **2012 Outlook:** Despite strong corporate earnings and record cash levels, we believe 2013 will be a difficult year for investors in U.S. markets. Forecasting U.S. stock market returns in what should be a stock pickers market is for the foolhardy. We believe our U.S. core managers are best positioned to find superior companies in 2013.
  2013 Actual: Partial Success. While we preferred U.S. to international equity, we never expected U.S. equity returns to be 30+%. Through late summer 2013, we maintained an overweight to U.S. equity compared to the equal weights for U.S. and international equity that many strategists advocated. Unfortunately, we were underweight U.S. equities compared to the Asset Mix Policy Benchmark which contains a higher allocation to U.S. equity and no allocation to alternative investments.

- **2012 Outlook:** International developed markets will also face challenges in 2013. The potentially negative impact of new regulations on European banks in 2013 has been deferred, but there will be increased regulatory and market issues in the telecommunications and technology sectors and many governments will continue to grapple with large debt levels. We believe our managers will select the best companies, and we will not change the allocation to developed markets.
  2013 Actual: Success. Our international equity component exceeded the benchmark.

- **2012 Outlook:** We expect longer duration fixed income assets will be less attractive in 2013 as U.S. interest rates remain low for the next few years. Spreads on high yield and investment grade corporate bonds have narrowed, reducing opportunities in 2013. Selective investment in distressed debt will continue to provide attractive opportunities.
  2013 Actual: Partial Success. Our short duration portfolio and high yield bonds provided positive returns and outperformance. Any fixed income allocation in 2013 reduced total portfolio return.

- **2012 Outlook:** Emerging market stocks and bonds should provide superior long-term investment performance. However, given the volatility and strong performance of emerging market stocks and bonds over the past decade, overweighting these opportunities in global

growth must be a long-term commitment. We prefer investment in emerging markets private equity to managers in public market securities.
2013 Actual: Success. Emerging markets stocks and bonds significantly underperformed developed markets. We reduced exposure in early 2013, which benefited the portfolio.

Introduction

The Board of Pensions Balanced Investment Portfolio returns net of fees and the asset allocation on December 31, 2013, were as follows:

	2013 Return	Asset Allocation $ Millions	Asset Allocation Percent	Long-Term Strategic Asset Allocation Ranges
U.S. Equity	36.4%	$3,163	37.3	30-50%
International Equity	18.7	1,808	21.3	10-25
Fixed Income	0.0	2,499	29.5	25-45
Alternative Investments	6.7	1,008	11.9	1-20
Total	**17.1%**	**$8,478**	**100.0%**	

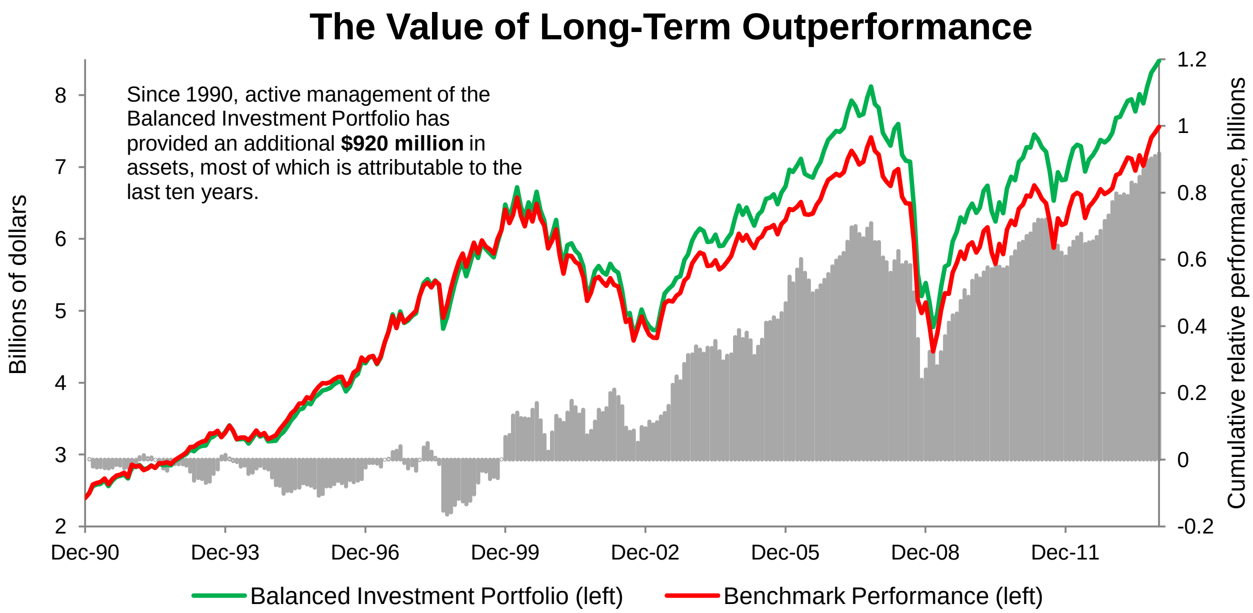
The Board of Pensions Balanced Investment Portfolio began 2013 with total assets of $7.5 billion. With strong investment performance in 2013, the market value of the Portfolio increased to $8.5 billion by December 31, 2013 after paying out $265 million in benefits payments to Plan members and their surviving spouses.

Performance of the Board of Pensions Balanced Investment Portfolio is measured against both a relative benchmark and the 7.0% long-term investment return assumption for the Pension Plan. The U.S. equity, international equity and fixed income components of the Balanced Investment Portfolio all exceeded the returns of their benchmark indices in 2013. With a return of 17.1%, the Balanced Investment Portfolio exceeded the 16.9% return of the asset mix policy benchmark and the 7.0% long-term investment return assumption for the year ended December 31, 2013.

While the Balanced Investment Portfolio had strong performance in 2013, we are long-term investors and measure performance success over longer time periods. The Balanced Investment Portfolio exceeded the return of the asset mix policy benchmark for the one, three, five, ten, fifteen and twenty years ended December 31, 2013. The Balanced Investment Portfolio also exceeded the 7.0% long-term investment return assumption for the one, three, five, ten and twenty years ended December 31, 2013.

The Value of Long-Term Outperformance: The Board of Pensions Balanced Investment Performance Versus Asset Mix Policy Benchmark Performance

As seen on the graph that follows, the actual investment performance of the Balanced Investment Portfolio compared to that of the asset mix policy benchmark has provided an additional $920 million in portfolio value since December 1990. The gray columns in the graph show the dollar value associated with the cumulative performance of the Balanced Investment Portfolio compared to its benchmark. Visually, the gray columns are the difference between the two lines at monthly intervals. Balanced Investment Portfolio outperformance has come from strong long-term performance from investment managers, active asset allocation decisions, and investments in limited partnerships. The graph also shows the sharp recovery in portfolio value from the depths of the financial crisis of 2008.



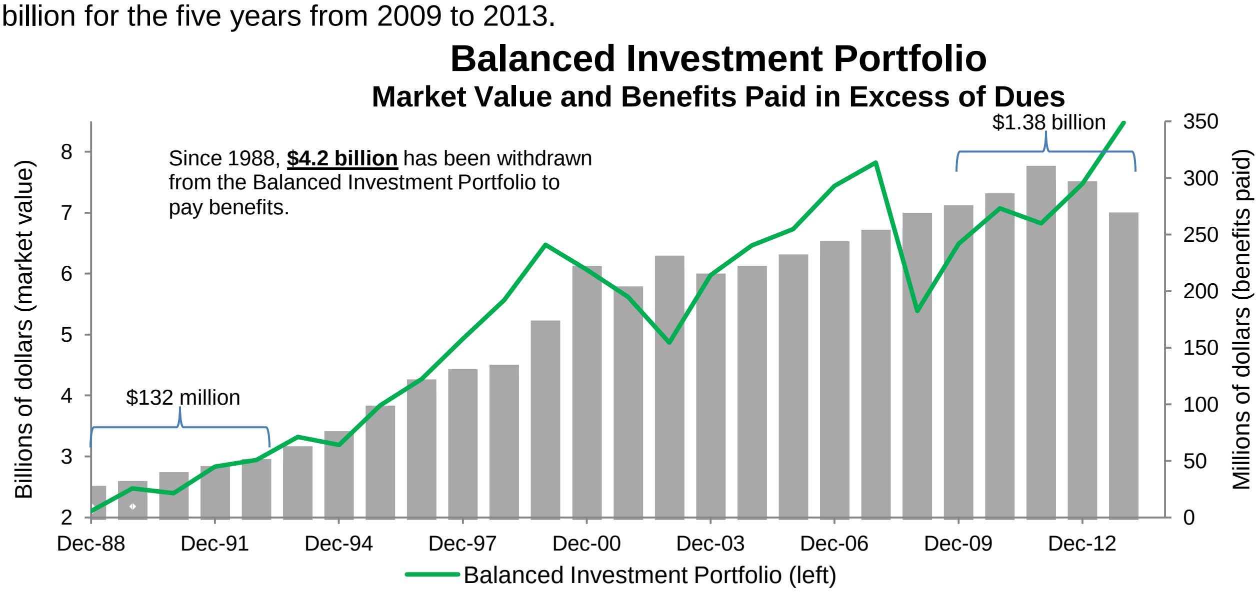
Benchmark Performance represents Asset Mix Policy Benchmark, adjusted for Balanced Investment Portfolio cash flows. Columns represent cumulative dollar impact of relative performance, shown on right hand scale.

Balanced Investment Portfolio Market Value and Cash Payments: 1988-2013

The Balanced Investment Portfolio had $2.1 billion in assets in 1988, paid out $4.2 billion in benefits to plan members and surviving spouses from 1988 through 2013, and closed the year with assets of $8.5 billion on December 31, 2013.

Benefits paid have exceeded dues received since 1988. This is not a problem and is part of the plan design. In 1988, when the Balanced Investment Portfolio was valued at $2.1 billion, the cash payment in addition to 1988 dues received was $15 million. Cash from the Balanced Investment Portfolio for benefit payments totaled $132 million for the five years from 1987 to 1991.

The Balanced Investment Portfolio was valued at $8.5 billion on December 31, 2013; additional cash for benefits payments totaled $265 million in 2013. Cash payments for benefits were $1.38 billion for the five years from 2009 to 2013.



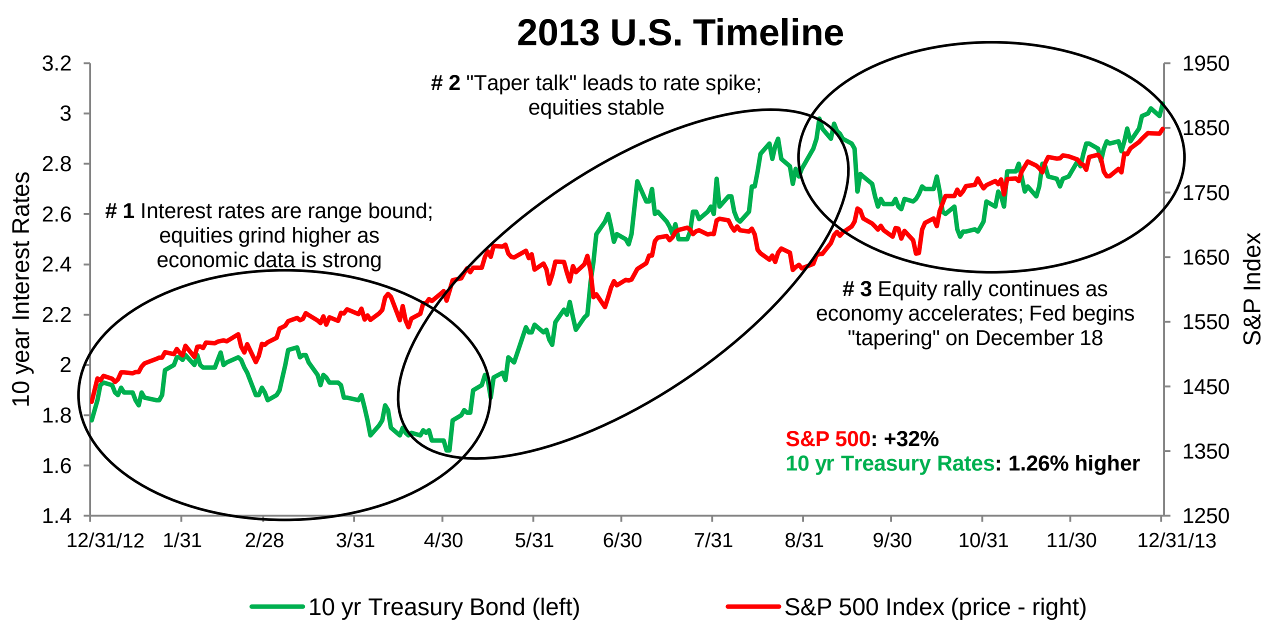
Gray bars represent benefits paid annually in excess of dues received and are shown in millions of dollars against the right scale. Timing of cash payments in December 2011, 2012 and 2013 overstates 2011 payments and understates 2013 payments. Excluding timing differences, cash payments were approximately equal 2011-2013.

An Overview of Economic and Market Events That Impacted 2013 Investment Performance

While 2013 was a less volatile year than 2012 for global equity markets, investors followed the "Risk On, Risk Off" mentality that has been evident since 2011 but updated to be "Fed On, Fed Off". The 2013 Investment Review begins with a timeline to help us remember just how our U.S. stock and bond markets were impacted by domestic and international events.

In the graph that follows, the red line (right axis) is the value of the Standard & Poor's 500 Index. The green line (left axis) is the interest rate on a 10-year U.S. Treasury bond. The interest rate on a 10-year U.S. Treasury was 1.78% on December 31, 2012. It closed on December 31, 2013 at 3.04%. With U.S. interest rates at historically low levels, the 126 basis point increase in the 10-year Treasury presented significant challenges for fixed income investors. Interest rates were very volatile and primarily impacted by comments (May 22 and June 19), inactions (September 18) and actions (December 18) of the Federal Reserve in 2013.

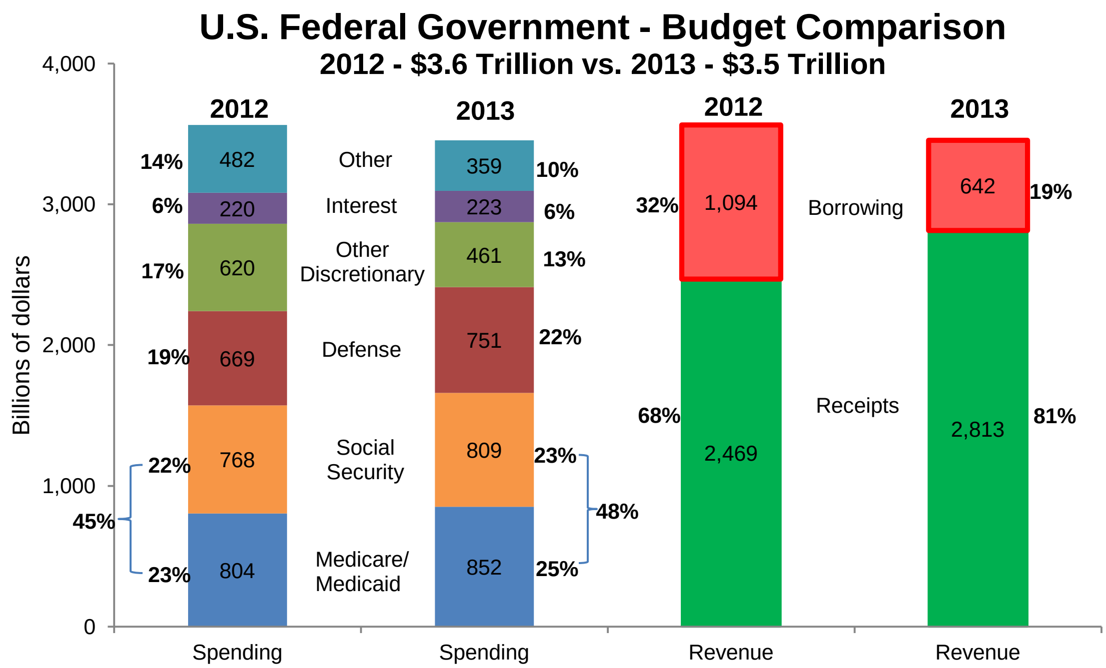
The S&P 500 began the year at 1,426, and closed the year at 1,848, a 32% increase. Stock market volatility was low in 2013, with a slow but steady market advance for U.S. stocks. The U.S. market was impacted by external factors, including concerns over the survival of the euro and the Eurozone, a slowdown in the Chinese economy, and continued instability in the Middle East. However, U.S. events including budget sequestration, the Snowden leaks of National Security Administration classified data, the shutdown of the Federal government and lack of a budget resolution had generally short-term impacts on the market advance.



Sources: Bloomberg, Federal Reserve

In Charge/Optimism

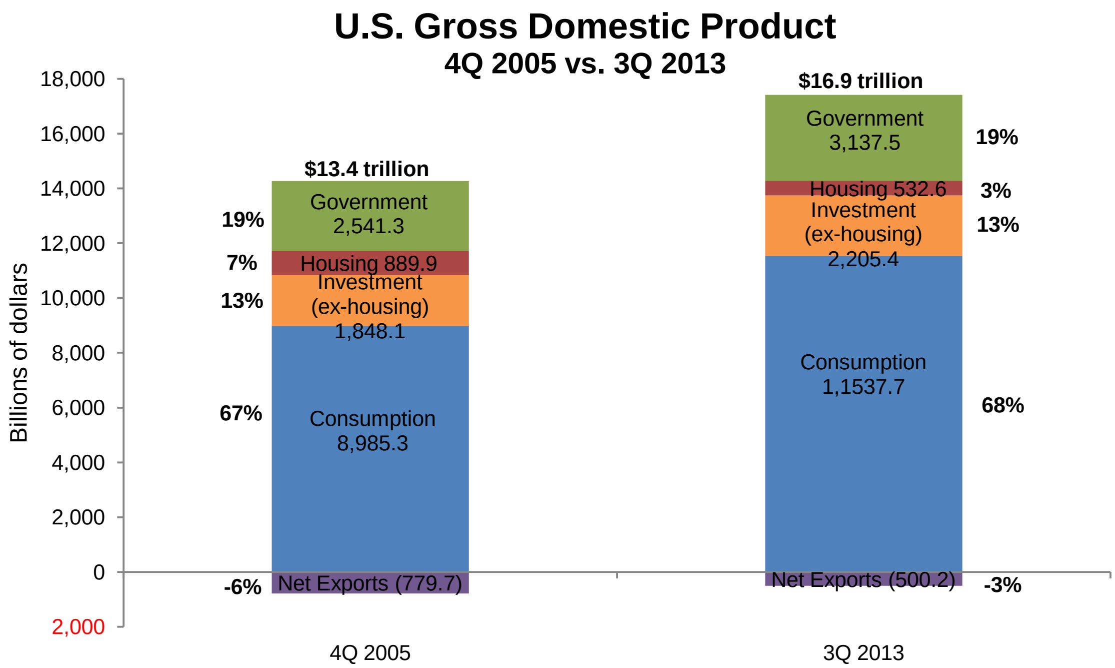
Political wrangling continued in 2013 on the size of the U.S. federal budget. When no resolution was reached and politicians refused to take charge, budget sequestration, or automatic cuts to U.S. federal government spending, went into effect on March 1, 2013. Cuts are evenly split between defense and non-defense spending, with no reduction of Social Security, Medicaid, federal pensions or veterans' benefits. As shown on the graph that follows, the 2013 budget was already $100 billion dollars lower than the 2012 budget. It is expected that sequestration will further decrease spending by over $1 trillion over the next eight years. The combination of Social Security, Medicare and Medicaid payments and defense spending accounted for 70% of federal expenditures in 2013, as compared to 64% in 2012. Revenue was in better alignment in 2013, with the ratio of receipts/borrowing moving from 68/32% in the 2012 budget to 81/19% in the 2013 budget.



Sources: U.S. Treasury, CBO, BEA, Office of Management and Budget

Optimism

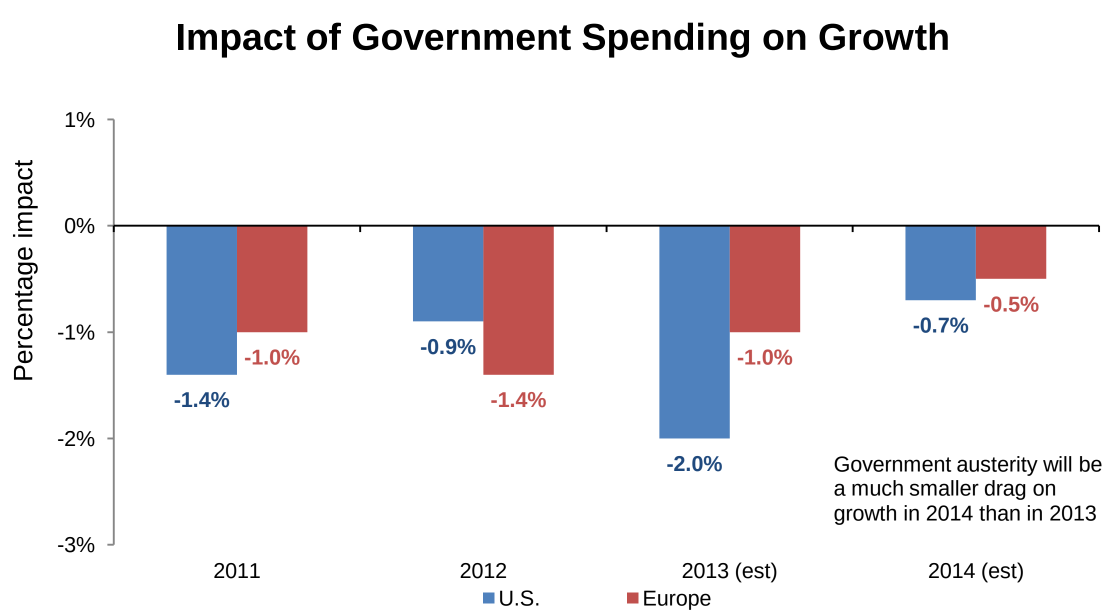
As shown on the graph that follows, U.S. GDP increased 26% from 2005 to 2013. Government remained 19% of GDP. Housing is a noticeably smaller component of the economy than it was in 2005; consumption and exports contribute more than they did in 2005.



Source: Bureau of Economic Analysis

In Charge/Optimism

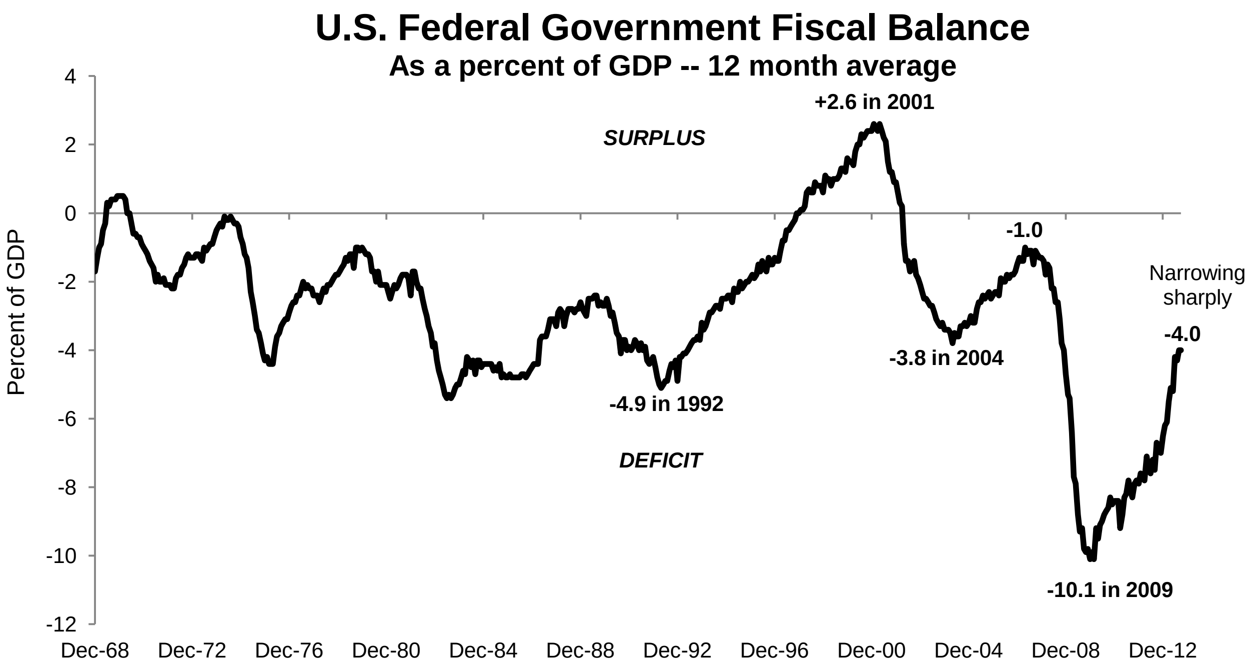
As shown on the graph that follows, government austerity programs reduced growth in the U.S. in 2011 by 1.4% in the U.S. and 1.0% in Europe. While in the U.S. the drag on growth decreased in 2012 to 0.9%, it increased in Europe due to extended austerity programs. The drag in the U.S. economy increased to a 2.0% reduction in growth in 2013 due to higher payroll tax rates, budget sequestration and closing of the Federal government in October 2013. The fading effects of these actions in both the U.S. and Europe should result in a smaller negative impact on growth in 2014 from slowing government spending.



Sources: KKR, OECD

In Charge/Optimism

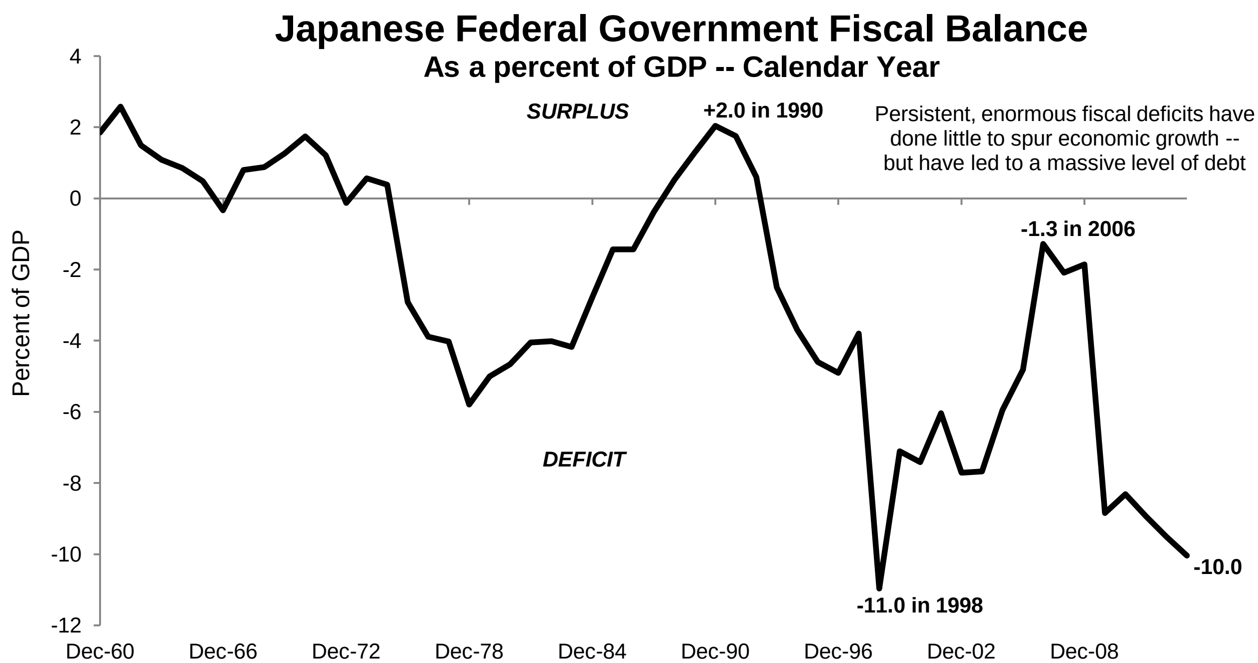
The direction and magnitude of the U.S. federal fiscal balance as a percent of GDP can be compared to that of Japan. As shown on the graph below, the U.S. experienced deficits from the 1970s through 1997. The surplus peaked at +2.6% of GDP in 2001 before sliding back into deficit status in 2002. Following the global financial crisis in 2008, the deficit peaked at 10.1%. The Federal Reserve took charge and introduced monetary policies to encourage economic growth and reduce unemployment. There is reason to be optimistic that fiscal and monetary policies remain at work to reduce the deficit from the current 4.0% of U.S. GDP.



Source: Bloomberg

In Charge?

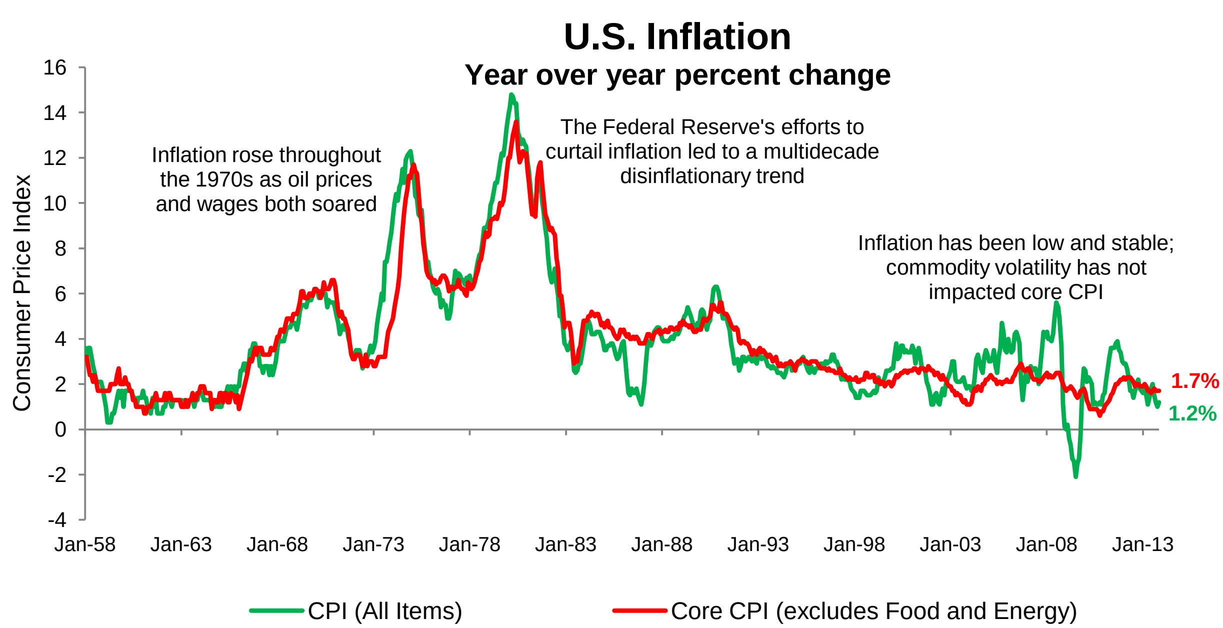
The deficit in Japan is currently at the same level as the U.S. deficit was in 2009. Japan has experienced deficits in the past and built back to a surplus position, most notably from the deficits beginning in 1972 that became surpluses from 1988 to 1992 due to strong economic growth. However, since the Japanese stock market crashed and the real estate bubble burst, the country has had 20 years of fiscal deficits. Shinzo Abe, the current Japanese prime minister, has taken charge and committed to reviving the economy and eventually reducing the deficit through his economic policies, now called Abenomics. His “three arrows” include massive fiscal stimulus, aggressive monetary easing and structural reforms to boost Japan’s competitiveness. The initial impact of Abenomics in 2013 was a dramatic weakening of the yen and a strong increase in the Japanese stock market.



Source: Bloomberg

In Charge/Optimism

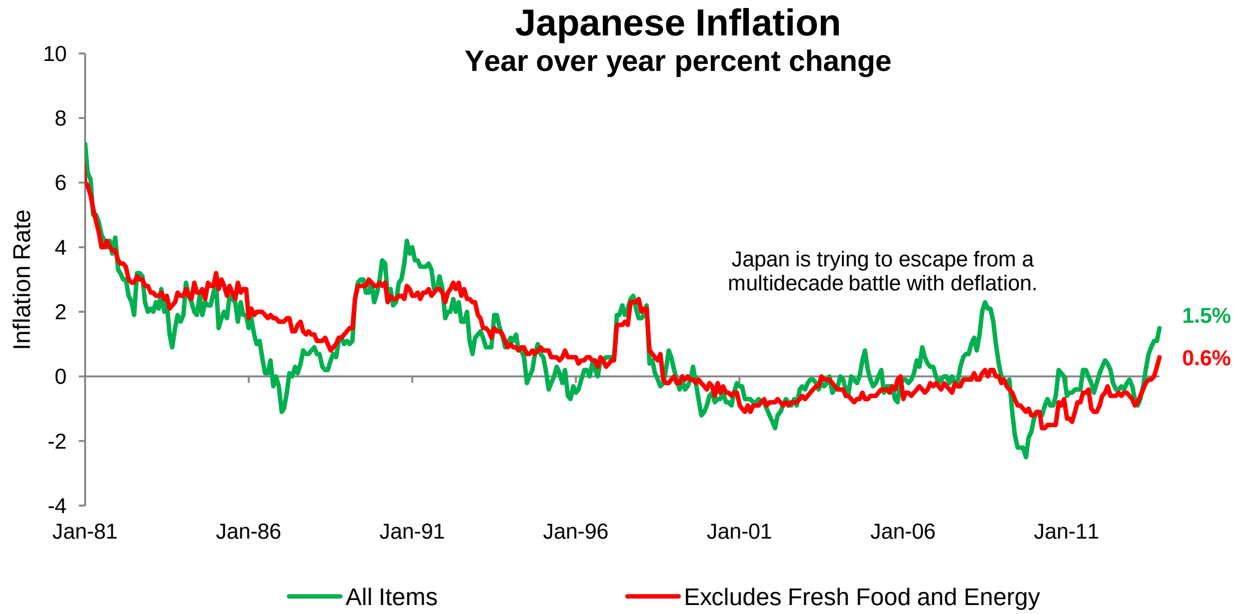
In 2008 and 2009 it was feared that the sluggish U.S. economy and high unemployment levels would lead to a deflationary spiral, similar to the Great Depression in the U.S. and Japan's multi-decade battle with deflation. The graph that follows shows that while the U.S. experienced severe inflation for a decade in the 1970s due to oil price shocks and increases in wages, the only recent period of U.S. deflation was a very brief time in 2009. Inflation has remained low in 2013 due to modest upward pressure on wages and commodity price weakness.



Source: Bloomberg

In Charge?/Pessimism

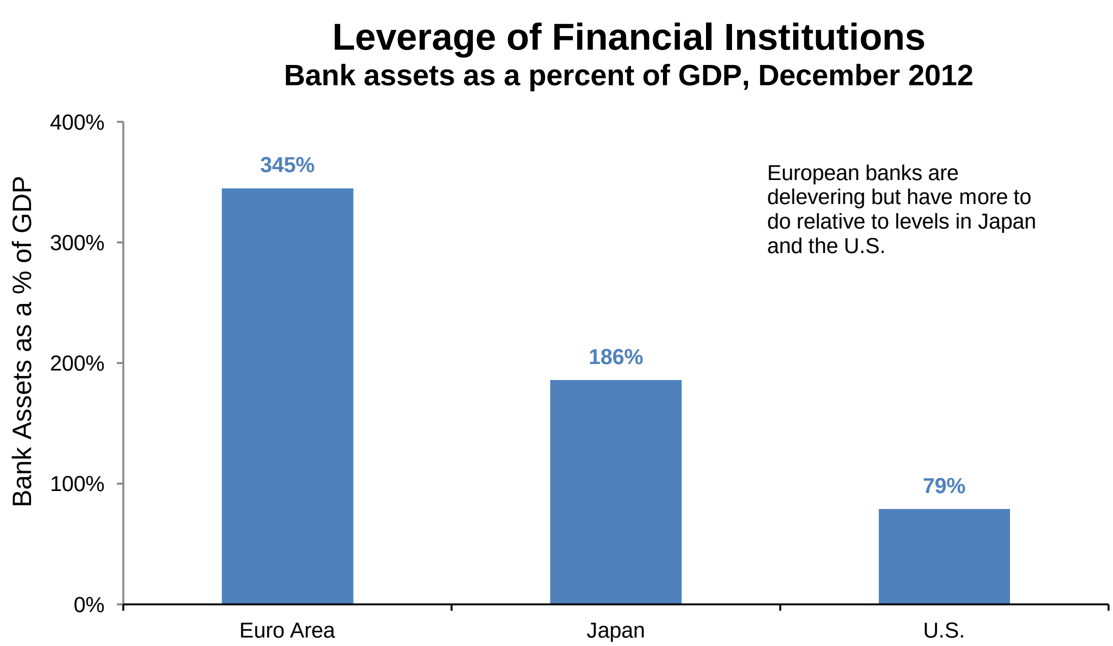
While Japan experienced inflation in the 2% to 4% range in the early 1990s, the more frequent problem was deflation, with the economy in a deflationary cycle since 1999. One of the goals of Abenomics is a 2% target level for inflation as part of an effort to encourage consumer spending and economic growth.



Source: Bloomberg

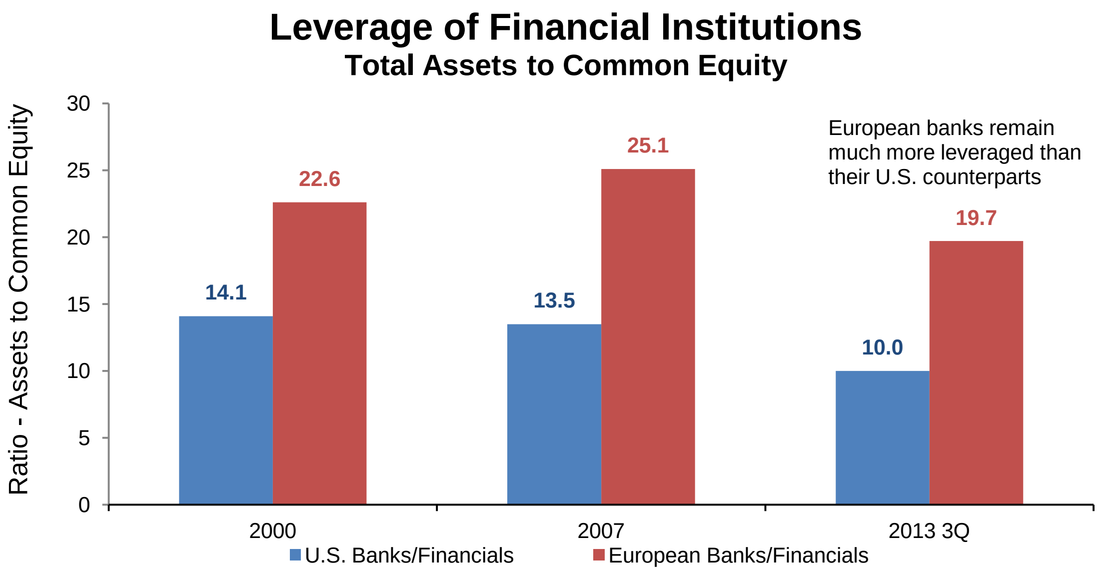
Not in Charge/In Charge

It was expected new banking rules would require European banks to sell assets and significantly delever their balance sheets in 2013. Based upon data from December 2012, European bank assets were 345% of GDP, almost four times higher than U.S. banks. However, rules were watered down in 2013 and implementation was delayed, so investment opportunities will continue in 2014 as European banks shed assets.



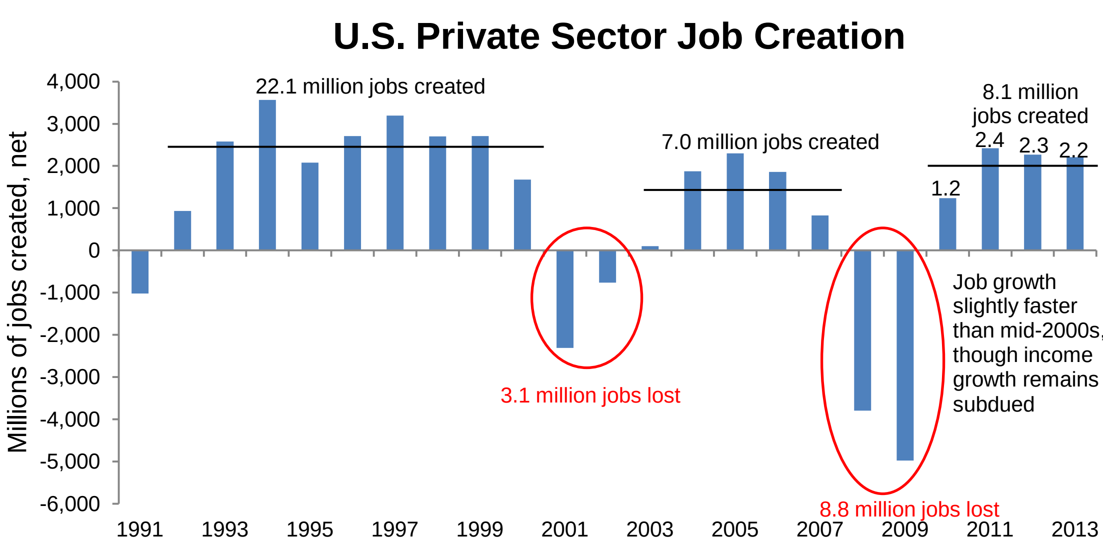
Sources: KKR, Statistical Office of the European Communities, European Central Bank, Bureau of Economic Analysis, Federal Reserve Board, Cabinet Office of Japan, Bank of Japan

Not in Charge/In Charge
Leverage of European banks and financial institutions can also be measured by the ratio of total assets to common equity. As shown on the graph that follows, in all three time periods, U.S. banks had significantly lower leverage than their European counterparts, with European banks increasing leverage in 2007 as U.S. banks were reducing it. Despite efforts to reduce leverage through asset sales and issuance of common equity, European banks were almost twice as leveraged in late 2013 as U.S. banks and financial institutions.



Sources: KKR, MSCI, S&P, FactSet, Bloomberg

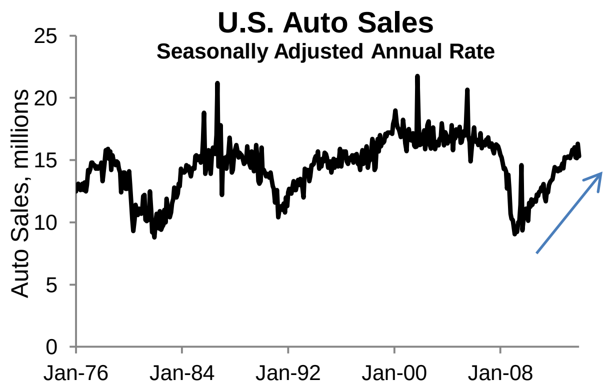
In Charge/Optimism?
In 2013 there was renewed optimism that job creation is turning in the right direction, but cumulative losses have been staggering and the number of replacement jobs and income levels may be inadequate to return the economy to a sustained growth mode. In 2001-2002, 3.1 million private sector jobs were lost. From 2003-2007, a total of 7.0 million jobs were added. In 2008-2009, 8.8 million jobs disappeared. In 2010-2013, a total of 8.1 million jobs were added. While this is close to the 8.8 million jobs lost, many new entrants to the job market during those years also need jobs.



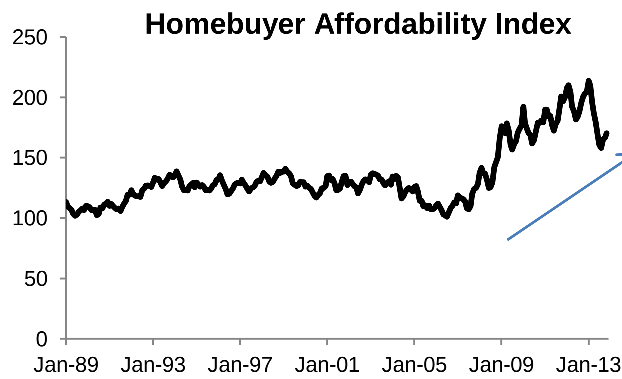
Source: Bureau of Labor Statistics. November and December 2012 subject to revision. Seasonally adjusted.

Optimism

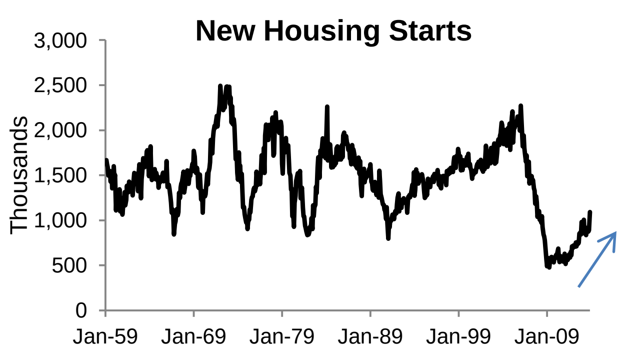
Optimism is again the word as we review the positive direction of four indicators of the health of the U.S. economy. As shown on the graphs that follow, U.S. auto sales, new housing starts, and new orders for core capital goods have all rebounded from 2008-2009 lows. While the homebuyer affordability level slipped in 2013 as interest rates increased, housing generally remains much more affordable than it was five years ago.



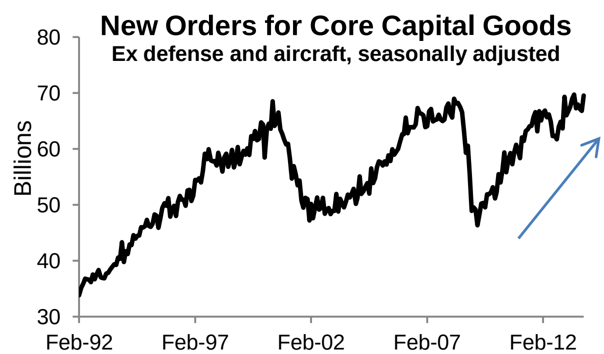
Source: Bloomberg



Source: National Association of Realtors



Source: National Association of Realtors

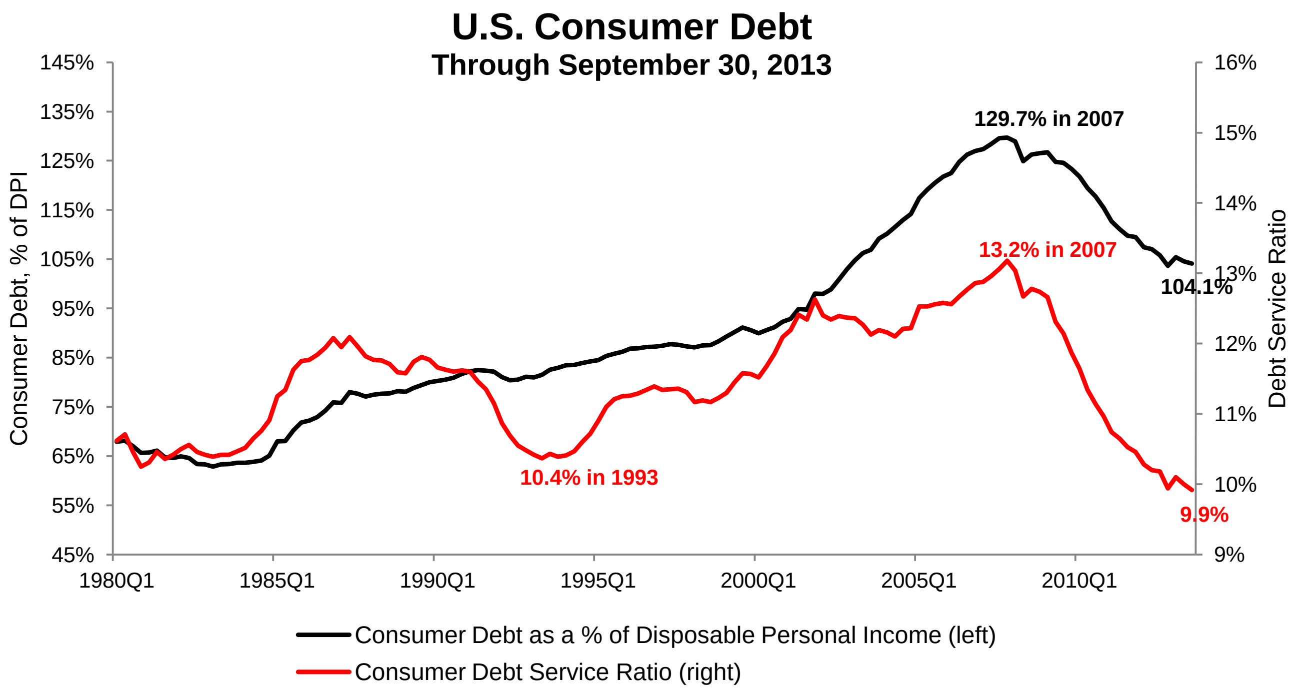


Source: Census Bureau

In Charge/Optimism for Consumers/Pessimism for Spending

The changes in levels of U.S. consumer debt are highlighted on the graph that follows. The black line is consumer debt as a percentage of Disposable Personal Income (DPI). It was 68% in 1980, declined to 63% in 1983, then began a steady increase until reaching a staggering 129.7% of disposable personal income in the third quarter of 2007. Current consumer debt is 104.1% of DPI, and given an uncertain economic backdrop, consumers are showing little appetite for meaningfully increasing their debt levels.

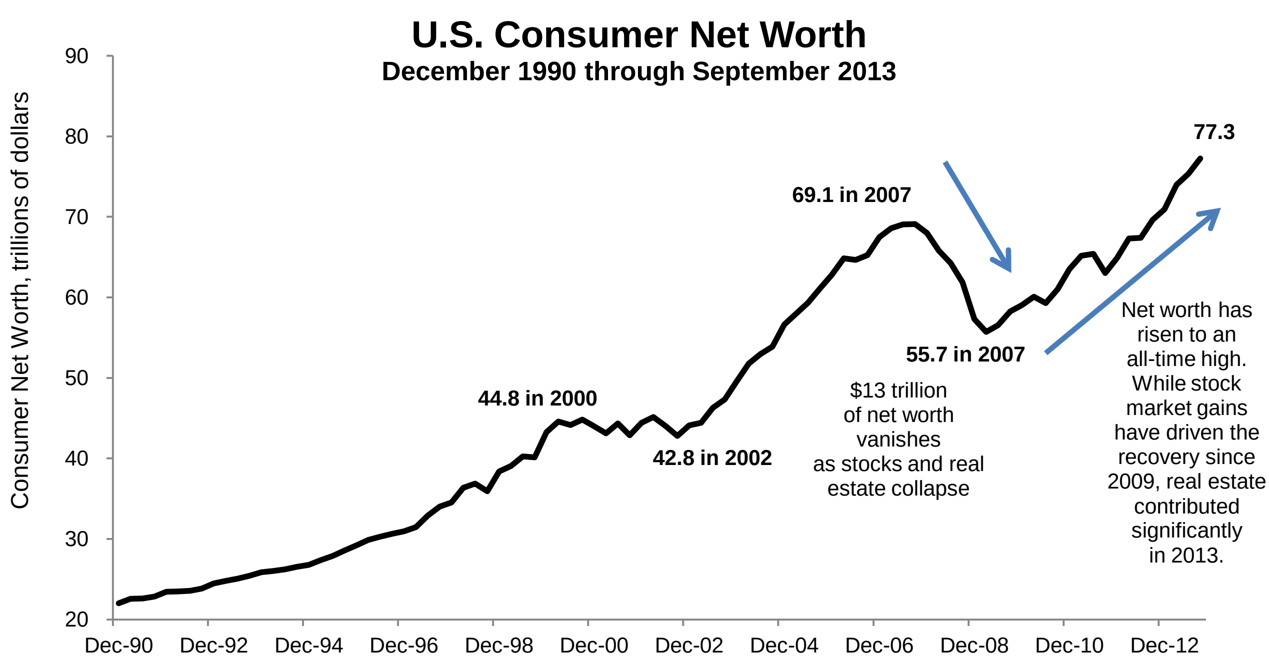
The more volatile red line is the consumer debt service ratio, or the percent of income used for debt payments. In 1980, it was 11.2%, dropping to 10.4% at the end of 1993. As consumers took on more debt and paid off less, the ratio increased to 13.2% in 2007. The current debt service ratio of 9.9% in 2013 is the lowest since 1980.



Sources: Federal Reserve, Bureau of Economic Analysis

Not in Charge/Optimism

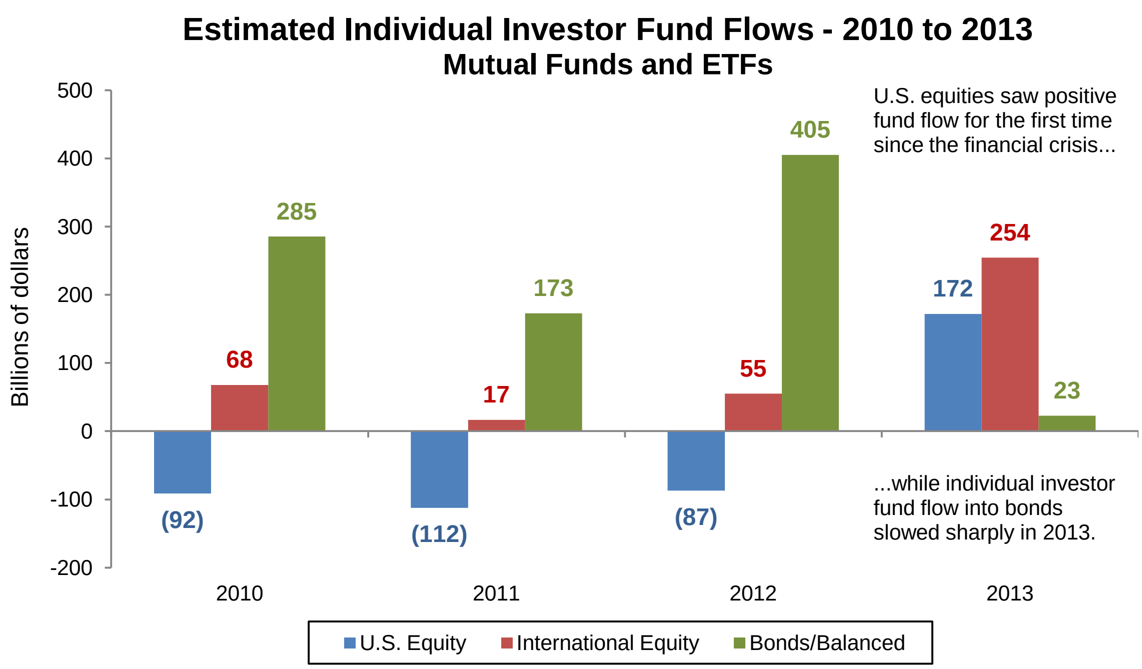
Consumer net worth peaked at $44.8 trillion dollars in the third quarter of 2000, just before the technology bubble popped. Collective consumer net worth declined by 4.5%, bottoming at $42.8 trillion dollars in the third quarter of 2002. A little less than five years later, consumers had added $26 trillion to their net worth which peaked at $69.1 trillion dollars in the second quarter of 2007. Consumers lost a staggering $13 trillion in net worth between the second quarter of 2007 and the first quarter of 2009, as the value of homes and investment portfolios collapsed. Current consumer net worth of $77.3 trillion, up 39% from the bottom in 2009, is significantly above the tech bubble peak in 2000 and the 2007 peak, driven by stock market gains and a broad recovery in real estate values.



Source: Federal Reserve

Investors In Charge/Optimistic

Following the financial crisis in 2008, investors shunned stocks and relied on bond and money market funds as safe havens for personal assets. This continued through 2012, despite record low interest rates. As the U.S. economy improved in 2013, people were more optimistic about their future employment propects, less risk averse, less willing to have a zero return from money market funds, and more concerned about the performance of bond funds in a period of rising interest rates. As shown on the graph that follows, based upon individual investor cash flows into and out of mutual funds and exchange traded funds (ETFs), an estimated $863 billion was invested in bond and balanced funds in 2010, 2011 and 2012, with net outflows of $291 billion from U.S. equity funds over the same three year period. In 2013, the flow into bond funds became a trickle, with many large bond funds experiencing net redemption as retail investors began to purchase U.S. stocks for the first time since the financial crisis in 2008.



Sources: ICI, ETFIA, IndexUniverse, BlackRock

Our identified themes and drivers for 2013 were **War and Politics**, **Pessimism/Optimism** and **In Charge.**

Despite significant uncertainty driven by regional wars and political conflict with no one in charge, there was minimal impact on U.S. markets. Sentiment shifts between pessimism and optimism were important in moving markets as were shifting perceptions of who was in charge. Markets sensed lack of control and responded accordingly.

Overview of Financial Markets

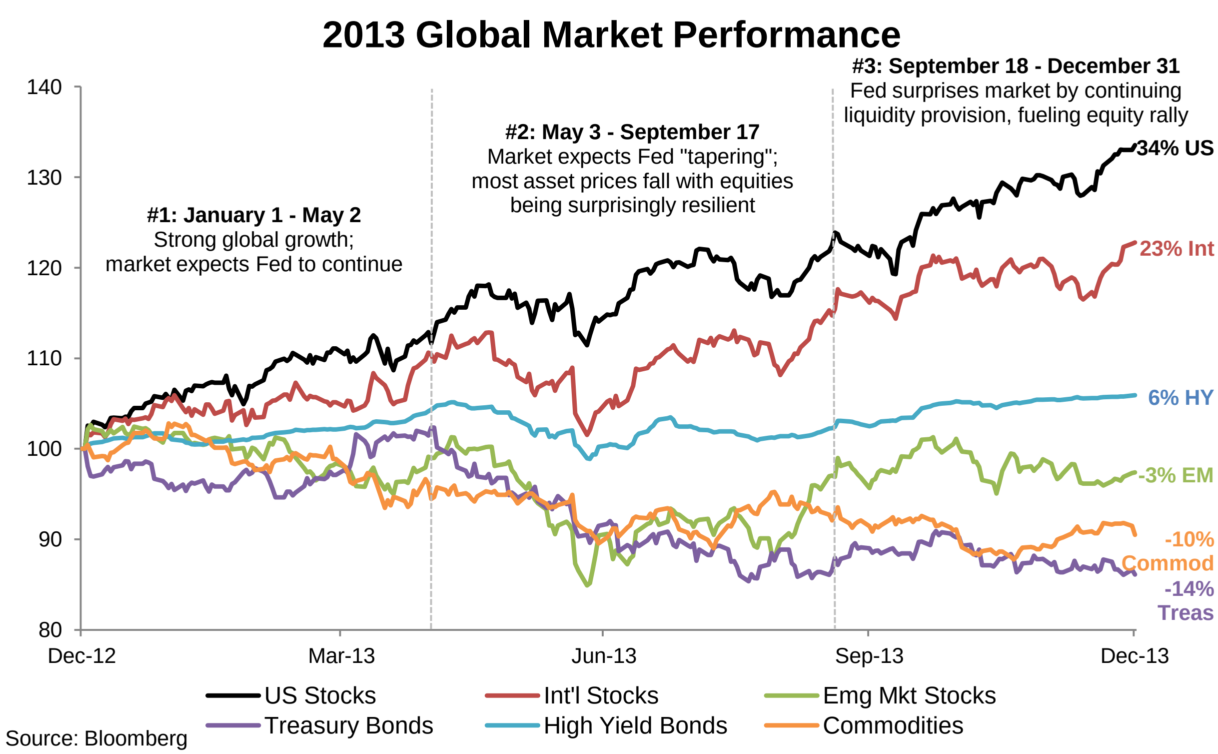
While U.S. and international stock markets had an exceptional year in 2013, global markets were volatile in 2013, with virtually all other asset classes providing negative returns at some point. We have divided the year into three phases to better illustrate the challenges faced by investors in 2013. In 2012 the key theme for each phase was "Risk On/Risk Off". In 2013, it was "Fed On/Fed Off".

Phase 1, "Fed On Hold". From January 1 through May 2, 2013, investors believed that chances of a global recession had diminished, there would be strong global growth in 2013 and the U.S. Federal Reserve would continue to provide liquidity and stability through Quantitative Easing. In this environment, U.S. stocks, international stocks, high yield bonds and long Treasury bonds performed well, while commodities and emerging market stocks provided negative returns.

Phase 2, "Fed Off/Tapering?". From May 3 through September 17, 2013, most markets expected the Fed to begin to reduce the purchases of bonds, or the tapering of Quantitative Easing. Unclear communications from the Federal Reserve introduced additional volatility to financial markets. Prices fell for most asset classes, with long Treasury bonds down 15.4% for the period. Only developed market stocks maintained a positive return as commodities and emerging market securities declined on the expectation of a global slowdown and high yield bonds declined due to increasing U.S. interest rates.

Phase 3, "Fed On Hold". From September 18 through December 31, 2013, all asset classes except commodities and long Treasuries rebounded, despite a U.S. government shutdown and lack of a budget resolution in 2013.

The year ended with the strongest performance from U.S. equities at 33.6%, followed by international equities at 22.8%, and high yield bonds at 5.9%. Emerging market stocks returned (2.6)%, commodities, (9.5)% and long U.S. Treasury bonds were the worst investment, with a return of (13.9)% for the year.



The market phases of 2013 can also be seen in the table that follows. Markets moved between "Fed On Hold" and "Fed Off/Tapering" phases throughout the three phases of 2013, with markets reacting primarily to Federal Reserve as well as global economic developments. The best performing asset class in each phase is shaded in yellow, with the worst shaded in gray.

	Phase 1 Fed On Hold 1/1 – 5/2	Phase 2 Tapering? 5/23 – 9/17	Phase 3 Fed On Hold 9/18 – 12/31	**Stocks Won Full Year 2013**
U.S. Stocks	**12.8%**	**8.6%**	**9.1%**	**33.6%**
International Stocks	9.6	4.6	7.0	22.8
Emerging Mkt Stocks	(1.0)	(1.9)	0.4	(2.6)
High Yield Bonds	4.5	(2.1)	3.6	5.9
Long Treasury Bonds	2.3	**(15.4)**	(0.5)	**(13.9)**
Commodities	**(5.3)**	(2.7)	**(1.8)**	(9.5)

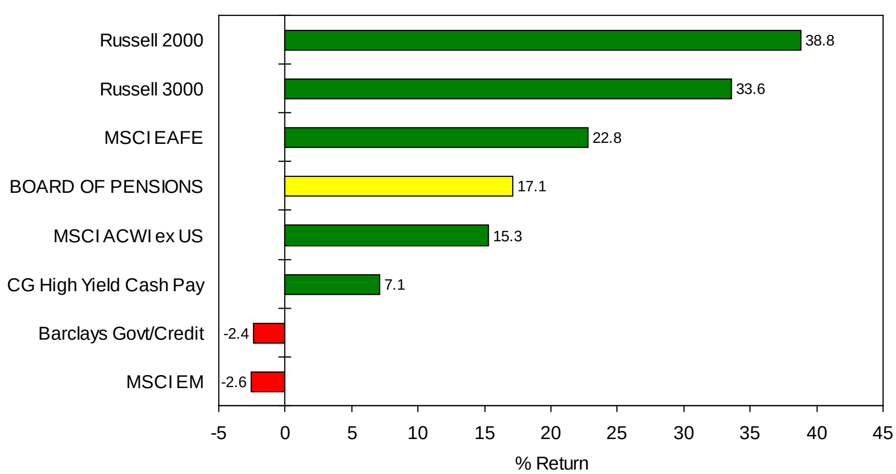
Review of the Board of Pensions Balanced Investment Portfolio

We begin the detailed review of the Board of Pensions Balanced Investment Portfolio with a comparison of its 2013 return of 17.1% to the returns available from market indices.

As shown on the graph that follows, 2013 was the year to have shunned diversification and been 100% invested in U.S. small and all capitalization stocks as represented by the Russell 2000 Index of small companies and the Russell 3000 Index of all U.S. companies. While investing in developed international markets was advantageous, emerging markets stock and U.S. bond index funds provided negative returns.

The Board of Pensions Balanced Investment Portfolio return of 17.1% reflects the exposure to multiple asset classes. The 2013 Investment Review provides a detailed commentary, analysis and performance review of components of the Balanced Investment Portfolio, to include U.S. equity, international equity, fixed income and alternative investments.

Returns of Market Indices and
Board of Pensions Balanced Investment Portfolio
December 31, 2013



Sources: BNY Mellon, MSCI (net)

What is the Structure of the Board of Pensions Balanced Investment Portfolio?

The Board of Pensions Balanced Investment Portfolio uses external investment management firms for the day-to-day investment of $8.5 billion in assets. The Portfolio is unitized on a monthly basis and is the investment portfolio for the Pension Plan as well as other plans and programs administered by the Board of Pensions. The U.S. equity component of the Portfolio has eleven investment managers and three index funds. The international equity component has eight managers, including two managers focused solely on emerging markets, and two index funds. The fixed income component has seven managers, including dedicated assignments to managers for high yield or below investment grade securities, global bonds, emerging markets debt and short duration securities. Alternative investments include commitments to 55 funds or limited partnerships investing in distressed debt, private equity, venture capital, real and absolute return, and inflation protection strategies.

Two managers were excused in 2013, with assets reallocated to index funds. Managers may be excused for changes in investment style and firm ownership as well as performance. In 2013, four new commitments were approved to limited partnerships in distressed debt, energy and emerging markets private equity. The allocation to liquid alternative investments was reduced with the elimination of a global real estate strategy. Portfolio diversification is a function of the long-term expected return for each asset class, but also must include risk assessments based on investment styles, liquidity and the potential firm risk for each investment manager retained by the Investment Committee.

Each year separate account managers for the Balanced Investment Portfolio are provided a list of those companies on the current Prohibited Securities lists. The lists include companies on the General Assembly Divestment List for involvement in military and tobacco, as well as those companies whose primary businesses are in the alcohol and gaming industries. The military list includes those corporations that manufacture hand guns and assault weapons. The Board of Pensions policy does not force the sale of companies newly added to the lists, which could reduce the investment return on the portfolio. Instead the policy prohibits the future purchase of the securities.

BOARD OF PENSIONS BALANCED INVESTMENT PORTFOLIO
PERIODS ENDED DECEMBER 31, 2013

	Annualized Rate of Return						
	1 Year	2 Years	3 Years	5 Years	10 Years	15 Years	20 Years
BOP U.S. EQUITY	36.4	26.2	16.6	20.3	8.7	6.5	9.9
Russell 3000 Index	33.6	24.7	16.2	18.7	7.9	5.3	9.3
BOP INTERNATIONAL EQUITY	18.7	18.6	7.9	13.6	8.7	7.4	7.3
MSCI All Country World Index ex US (gross)	15.8	16.6	5.6	13.3	8.0	5.8	6.3
BOP FIXED INCOME	0.0	4.5	5.3	8.6	5.4	5.7	6.2
Barclays Gov/Credit Index	-2.4	1.2	3.6	4.4	4.5	5.2	5.7
BOP PRIVATE PARTNERSHIPS	12.6	11.9	10.4	10.1	11.7	14.1	--
BOP LIQUID ALTERNATIVES	-0.6	4.5	4.6	12.2	--	--	--
Consumer Price Index + 500 basis points	6.5	6.6	7.1	7.1	7.4	7.4	7.4
BOP BALANCED PORTFOLIO	17.1	15.5	10.3	14.0	7.4	6.5	8.3
BOP RELATIVE BENCHMARK Asset Mix Policy Benchmark*	16.9	14.8	10.1	13.0	7.1	5.8	7.9
LONG-TERM INVESTMENT RETURN Pension Plan Actuarial Assumption	7.0	7.0	7.0	7.0	7.0	7.0	7.0

Notes:
Returns are net of management fees.

*Effective 1/1/2005, the Asset Mix Policy Benchmark is calculated using each asset class midpoint multiplied by its index.
The policy benchmark is:
U.S. Equity = 47.5% * Russell 3000 Index (Includes allocation of 7.5% to alternative investments)
International Equity = 17.5% * MSCI All Country World Index ex US (ACWI)
Fixed Income = 35% * Barclays Capital Gov/Credit Bond Index
Alternative Investments = 0

Review of the Board of Pensions Balanced Investment Portfolio Performance

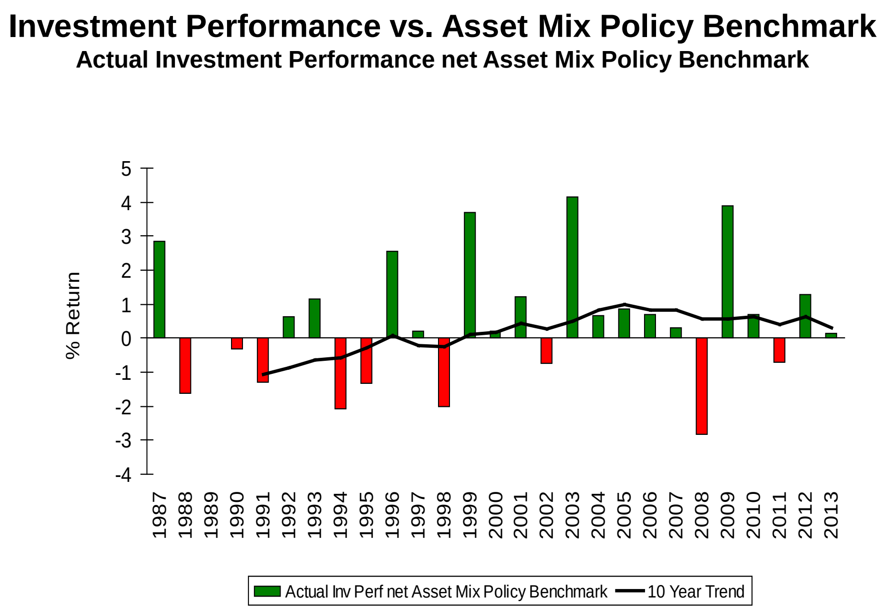
Performance of the Board of Pensions Balanced Investment Portfolio is measured against both a relative benchmark and the 7.0% long-term investment return assumption for the Pension Plan.

The Relative Benchmark: The Asset Mix Policy Benchmark of Investable Market Indices

The relative benchmark, or asset mix policy benchmark, is used to compare the performance of the Board of Pensions Balanced Investment Portfolio to that of investable market indices. The asset mix policy benchmark is the return the Portfolio would have achieved by investing in each asset class using a passively managed index fund at the mid-point of the long-term strategic allocation range for each asset class. Alternatives are not included in the benchmark since there are no investable market indices for alternative investments.

Years such as 2013 with above benchmark performance reflect the contribution, both positive and negative, of active investment management strategies and asset allocation decisions, including allocations to small capitalization stocks, high yield bonds, emerging markets stocks, distressed debt, private equity and other alternative investments.

The graph for the Balanced Investment Portfolio that follows shows returns compared to the asset mix policy benchmark. Columns above the line are those years when the difference between the actual return and the asset mix policy benchmark is positive. Columns below the line are years when the actual return was lower than the policy benchmark. The red bar for 2011 is the 0.6% actual return less the 1.3% asset mix policy benchmark return, or a shortfall of (0.7)%. The green bar for 2013 is the 17.1% actual return less the 16.9% return for the asset mix policy benchmark, or 0.2%. While it is difficult to consistently add value over a passively managed index portfolio, the Balanced Investment Portfolio has been able to do so in 18 out of the last 27 years, or 67% of the time, as well as over the three, five, ten, fifteen and twenty year periods ended December 31, 2013.



The Long-Term Investment Return: The 7.0% Pension Plan Actuarial Assumption

In calculating the health and solvency of the pension plan, the actuary uses certain assumptions about plan demographics and financial metrics. These assumptions are reevaluated regularly to ensure that they are reasonable and current. One of the critical assumptions is the investment return of pension plan assets.

To measure the health of the pension plan, the actuary assumes that the return on the Balanced Investment Portfolio will, over the long term, meet or exceed 7.0%. It is important to remember that this is a long term goal and will not be met in every calendar year. For the long-term health and stability of the pension plan, it is imperative that the actual return on assets meet or exceed the plan investment return assumption.

The 17.1% return in 2013 exceeded the 7.0% long-term assumption. The Balanced Investment Portfolio returns exceeded the 7.0% assumption for the one, two, three, ten and twenty years ended December 31, 2013. It did not meet the 7% expectation for the fifteen years ended December 31, 2013, which included negative returns in 2000, 2001, 2002 and 2008.

Performance Attribution

Performance attribution compares actual investment performance with Asset Mix Policy Benchmark performance. The Asset Mix Policy Benchmark does not include alternative investments since there are no investable index funds for alternative investments. The table that follows shows the average allocation in 2013 for each asset class compared to the allocation used in the Asset Mix Policy Benchmark.

2013 AVERAGE ASSET ALLOCATION vs. ASSET MIX POLICY BENCHMARK

	2013 Actual Average Asset Allocation	Asset Mix Policy Benchmark Asset Allocation	Over/ Underweight
U.S. Equity	39.0%	47.5%	(8.5%)
International Equity	19.0	17.5	+1.5
Fixed Income	30.0	35.0	(5.0)
Alternative Investments	12.0	0.0	+12.0
Total	**100.0%**	**100.0%**	

2013 PERFORMANCE ATTRIBUTION
BOARD OF PENSIONS BALANCED INVESTMENT PORTFOLIO
vs. ASSET MIX POLICY BENCHMARK

U.S. Equity	+0.86%
International Equity	+0.34
Fixed Income	+0.55
Private Partnership Alternative Investments	(0.17)
Liquid Alternative Investments	(0.81)
Asset Allocation/Cash Flow Timing	(0.57)
Net Impact on Portfolio Performance	**+0.20%**

The 0.2% outperformance of the Board of Pensions Balanced Investment Portfolio in 2013 compared to the return of the Asset Mix Policy Benchmark can be primarily attributed to outperformance in the U.S. equity, international equity and fixed income components of the Balanced Investment Portfolio. Alternative investments detracted from performance.

Overall performance in 2013 could have been further improved with better stock selection by U.S. large capitalization growth equity managers, better stock selection of U.S. small company growth stocks, a reduced allocation to emerging market stocks and bonds, an increased allocation to cash and short duration fixed income, and a decreased allocation to alternative investment strategies.

The U.S. equity component exceeded the benchmark of the Russell 3000. However, the lower allocation to U.S. equities versus the relative benchmark hurt relative performance because U.S. equity was the best performing asset class.

Performance of the international equity component exceeded its benchmark of the MSCI ACWI (All Country World Index) ex U.S. A small overweight to international equities, which performed well, modestly helped relative performance as well.

The fixed income component provided superior performance in 2013 and its 5.0% underweight to the Asset Mix Policy Benchmark weight of 35% helped improve relative performance compared to the Asset Mix Policy Benchmark because bonds were weak performers in general.

Alternative investments are a 12.0% overweight in actual asset allocation compared to the Asset Mix Policy Benchmark, which has no allocation to alternatives. Underperformance in this non-benchmark asset class detracted from performance in 2013.

Asset Allocation

The Balanced Investment Portfolio is invested for the long term, not a single one-year period. The strong performance in 2013 was based on asset allocation decisions and manager selections made since 2010. Asset allocation shifts between year end 2012 and 2013 reflect market movement but also rebalancing from asset classes and managers with the greatest outperformance in 2013 to those with the best expected returns in 2013 and 2014. The continued strong performance of U.S. stocks throughout the year enabled us to raise $265 million in cash for benefit payments and to increase the allocation to international equity in the second half of the year. The allocation to private partnerships decreased from 7.7% at the beginning of 2013 to 7.2% on December 31, 2013. This was due to the return of invested capital from some partnerships which realized gains.

COMPARATIVE ASSET ALLOCATION
BOARD OF PENSIONS BALANCED INVESTMENT PORTFOLIO

	December 31, 2013		December 31, 2012	
	$Millions	Percent	$Millions	Percent
Equity	4,971	58.6	4,170	55.8
U.S. Equity	3,163	37.3	2,759	36.9
International Equity	1,808	21.3	1,411	18.9
Fixed Income	2,499	29.5	2,276	30.4
Alternative Investments	1,008	11.9	1,030	13.8
Private Partnerships	614	7.2	575	7.7
Inflation/Real Return	91	1.1	170	2.3
Absolute Return	303	3.6	285	3.8
Total	**8,478**	**100.0%**	**7,476**	**100.0%**

U.S. Equity Component of the Balanced Investment Portfolio
37.3% of the Balanced Investment Portfolio on December 31, 2013

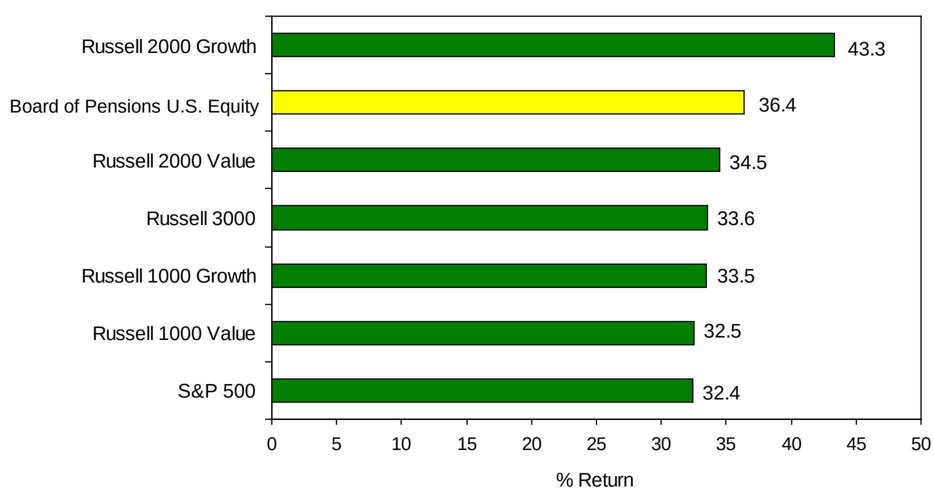
The U.S. equity component of the Board of Pensions Balanced Investment Portfolio had a return of 36.4% in 2013, exceeding the 33.6% return of the benchmark Russell 3000 Index. The U.S. equity component exceeded the return of the Russell 3000 Index for the one, two, three, five, ten, fifteen and twenty years ended December 31, 2013.

In 2013, the Russell 2000 Index of small company stocks returned 38.8%, exceeding the Russell 3000 Index of large company stocks return of 33.6%. Despite the above benchmark return, the U.S. equity component would have had stronger performance if several managers with large and small capitalization portfolio assignments had outperformed their respective benchmarks.

The large capitalization component of the portfolio returned 35.5% exceeding the 32.4% return of the S&P 500 and the 33.1% return of the Russell 1000 Index. Two of the three core managers outperformed the return of the benchmark S&P 500. All three value managers exceeded the 32.5% return of the Russell 1000 Value Index. One of the three growth stock managers exceeded the 33.5% return of the benchmark Russell 1000 Growth Index. While, in combination, the large capitalization managers beat their benchmark, stronger stock selection, especially by two of the growth managers, would have added to already strong performance in 2013.

The small and mid capitalization component of the Portfolio returned 40.3%, exceeding the Russell 2000 return of 38.8% for small company stocks. The small capitalization core manager returned 45.0%, significantly better than the 38.8% return of the Russell 2000 Index. The small capitalization growth manager had a return of 33.9%, lagging the 43.3% return of the benchmark Russell 2000 Growth Index. Stronger stock selection by the small capitalization growth stock manager would have added to the already strong performance in 2013.

U.S. Equity Index Returns
Year to Date December 31, 2013

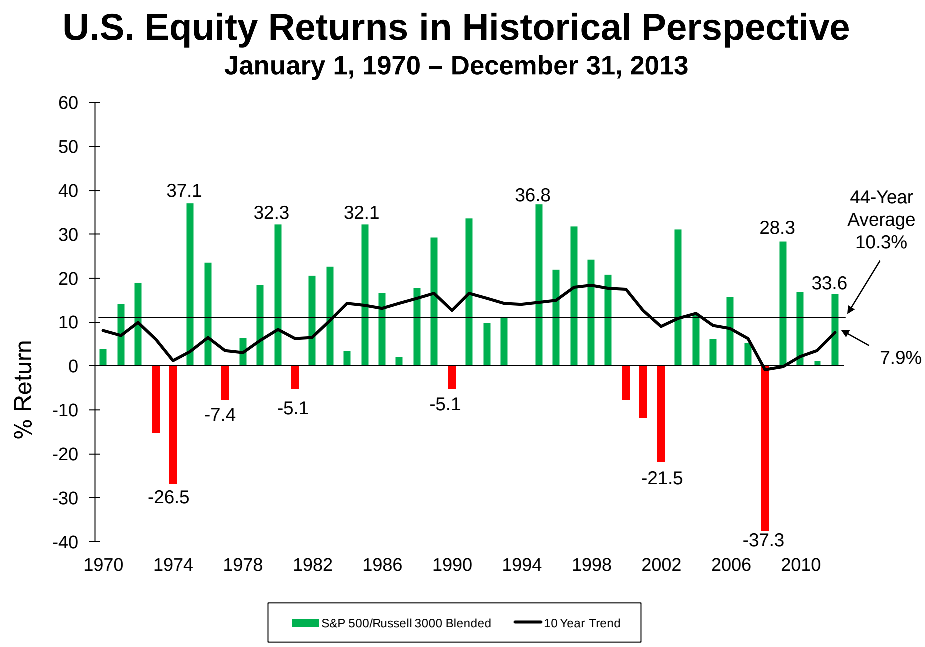


Source: BNY Mellon

U.S. Equity Market Historical Performance

The Russell 3000 Index includes stocks of large and small companies and is a broader measure of the U.S. equity market than the S&P 500. However, the Russell 3000 originated in 1979, so it does not have the extensive historic database that is valuable for long-term investment perspective. For purposes of the following graph, U.S. equity market returns are represented by the S&P 500 Index beginning in 1970 and the Russell 3000 Index in 1979.

The Russell 3000 Index had a 33.6% return in 2013. The 33.6% return is above both the 7.9% average return of the last ten years, as reflected in the 10-year trend line, and the long-term 44-year average return of 10.3% since 1970. The U.S. equity market had negative returns in 9 out of those 44 years and in 4 of the last 13 years.



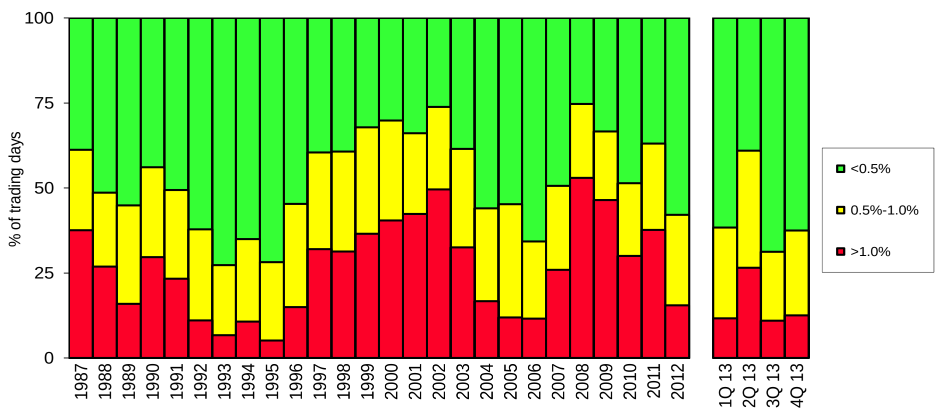
Note: S&P 500 through 1978; Russell 3000 effective 1979

Market Volatility

2013 follows 2012 as a second consecutive year with subdued market volatility in large capitalization U.S. equity markets. The chart that follows portrays the daily movement of the S&P 500, the index most commonly tracked by investors, based upon the change in daily closing price from one trading day to the next. The graph divides market movements into three categories. The red or bottom bars are periods of high volatility, with daily movement of the index greater than one percent. The green or top bars are periods with lower volatility, when the Index moved up or down less than one-half percent. As an example, in 1995, only 5% of all trading days had a daily price change of greater than one percent. This low volatility can be compared to the high volatility of 2008 when 53% of all trading days had a daily price change of greater than one percent. In October 2008, as frantic investors sought liquidity and sold stocks into ever declining markets, trading volumes escalated and 87% of trading days had a daily price change of greater than one percent. Market volatility in the first quarter of 2013 was low, with only 12% of trading days experiencing a daily price change greater than 1%. This increased to 27% in the second quarter, when Ben Bernanke announced the decision to reduce or taper the Federal Reserve bond purchase program, causing a market sell-off in late May and June. Market conditions stabilized and volatility dropped in the third and fourth quarters of 2013.

U.S. Equity Market Volatility

Daily Movement of S&P 500 Index



* Daily closing value of S&P 500 as compared to prior trading day's closing value. Does not differentiate between movements up or down. Does not reflect intraday movements.

Market Capitalization and Style

Investors know that the size of the companies they invest in, or company market capitalization, can significantly impact portfolio success. Small company stocks in the Russell 2000 Index returned 9.1% annually for the ten years ended December 31, 2013, exceeding the 7.4% return of large company stocks in the S&P 500. Investment styles also affect results as investors believe growth or value stocks will benefit more in the next period, though style impacts performance more in shorter than longer periods. Stocks in the Russell 1000 Growth Index returned 7.8% annually for the ten years ended December 31, 2013, slightly exceeding the 7.6% return of the Russell 1000 Value Index.

As shown in the table that follows, getting both style and market capitalization right was important in 2013. Stocks of large companies in the Russell 1000 Index returned 33.1%, lagging the 38.8% return of small companies in the Russell 2000 Index. Growth had the advantage over value for large, midcap and small companies, with stocks of companies in the Russell 2000 Growth Index providing the highest return of 43.3% in 2013.

2013 U.S. STOCK MARKET PERFORMANCE BY MARKET CAPITALIZATION AND STYLE

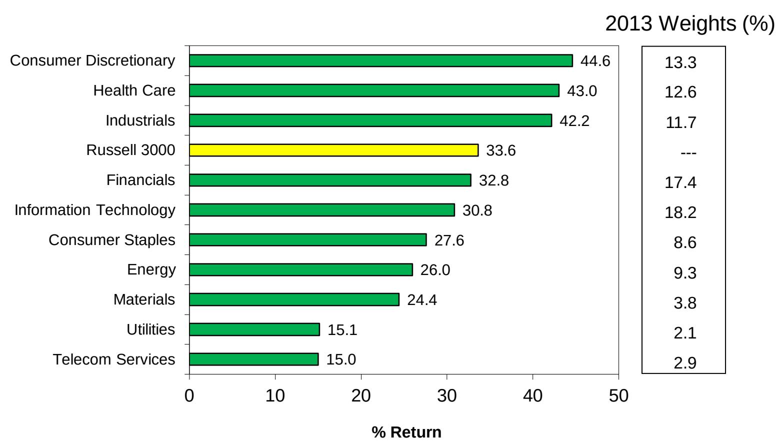
Russell 3000 – Total Market	33.6%	
S&P 500 Index (Large Capitalization)	32.4	
Russell 1000 Index (Large Capitalization)	**33.1**	
Russell Mid Cap Index (Mid Capitalization)	34.8	5.7% advantage to small
Russell 2000 Index (Small Capitalization)	**38.8**	
Russell 1000 Growth Index	33.5	1.0% advantage to growth
Russell 1000 Value Index	32.5	
Russell Midcap Growth Index	35.7	2.2% advantage to growth
Russell Midcap Value Index	33.5	
Russell 2000 Growth Index	43.3	8.8% advantage to growth
Russell 2000 Value Index	34.5	

Source: Russell Investments

Sector Performance

The broad U.S. stock market, as represented by the Russell 3000 Index, had a return of 33.6% in 2013 with all sectors providing positive returns. Performance ranged from 44.6% for stocks in the consumer discretionary sector, to 15.0% for companies in the telecommunication services sector, an advantage of 29.6% for investors in consumer discretionary stocks. The consumer discretionary sector includes companies in a wide range of businesses, including Best Buy, Amazon and Walt Disney. While a consumer might debate the way consumer-related companies are classified, the consumer staples sector includes those companies that provide basic goods and services, such as Campbell Soup and Wal-Mart, rather than goods and services that some might deem less essential. Superior stock selection and sector allocation is important in portfolio construction and performance. In 2013, information technology companies, with an 18.2% weight in the Russell 3000 Index, underperformed the return of the Russell 3000 Index for a third consecutive year. Financials are the second largest sector, representing 17.4% of the Index, followed by the consumer discretionary and health care sectors, at 13.3% and 12.6% of the Index, respectively.

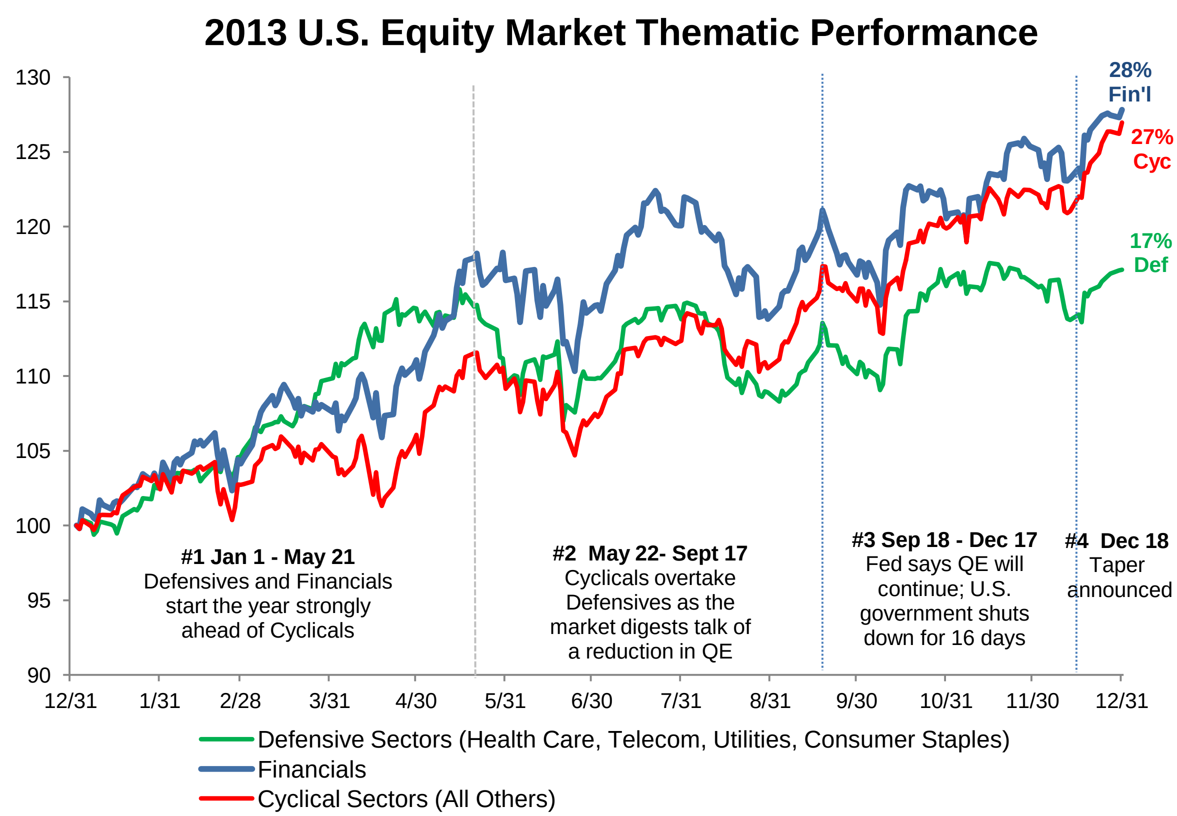
Russell 3000 Index Sector Returns and Weights 2013



Source: BNY Mellon

As shown on the graph that follows, the U.S. equity market had four distinct investment phases. In 2013, stock market performance was impacted more by monetary policy, Federal Reserve comments and actions, fiscal policy, and the shutdown of the U.S. government for 16 days. Exogenous shocks, such as wars in other countries, played a smaller role than in prior years. In Phase 1, from January 1 through May 21, stocks in the financial and defensive sectors had the strongest performance. On May 22, Ben Bernanke made comments which led investors to believe that quantitative easing would soon be reduced. As noted in the discussion of market volatility, market volatility increased on the rumor and stabilized with the actions taken by the Federal Reserve on September 18 to continue quantitative easing for the foreseeable future. In this period cyclical stocks such as those in the technology, materials and industrials sectors, gained ground and outpaced defensives.

Phase 3 began on September 18 when the Federal Reserve announced they would not begin to reduce bond purchases due to continued weakness in the U.S. economy. All sectors performed through the 16 day U.S. government shutdown, from October 1 through October 16. Phase 4 began on December 18 with the Federal Reserve announcing a modest January 2014 tapering, or a $10 million reduction in the amount of bonds purchased on a monthly basis, from $85 million to $75 million. While defensive stocks rallied in late December, closing the year with a 17% return, it was too late to close the performance gap between financials, with a 28% return, and cyclicals, with a 27% return.

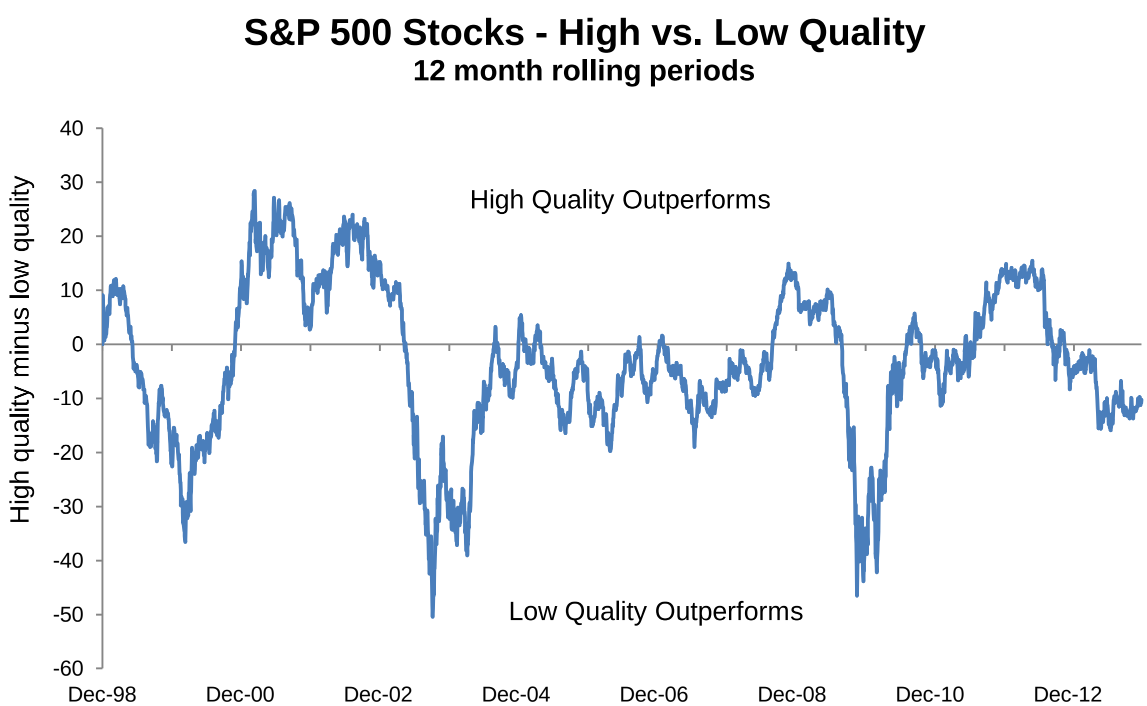


Source: Bloomberg. Assumes an equal weighted portfolio of MSCI US sector indices, rebalanced daily

The Balanced Investment Portfolio had broad sector diversification in 2013. The top ten stocks held on December 31, 2013 were Google, Microsoft, Johnson & Johnson, Charles Schwab, Biogen Idec, Texas Instruments, Qualcomm, Visa, FedEx, and Amgen. These stocks were not the top ten holdings of the Balanced Investment Portfolio for the entire year. Six of the companies were in the top ten holdings on December 31, 2012, with three companies moving up in portfolio weight and three down. These top ten U.S. stock holdings were a diverse representation from the financials, health care, industrials and information technology sectors.

2013 was expected to finally be the year that investors focused on quality companies. However, the stocks of the poorest quality companies in the S&P 500 significantly outperformed the stocks of the highest quality companies. Best Buy, a company with a low quality rating, returned 237% in 2013 while many high quality companies returned below the market average. IBM returned (2)% in 2013 while Coca Cola returned 14%.

While investors may strive to invest in high quality companies, as shown in the graph that follows, there are long periods of time when the stocks of low quality companies will outperform, whether through the "Dead Cat Bounce" from a market bottom or a turnaround by a new management team.



Source: Bloomberg

Structure of the U.S. Equity Component of the Balanced Investment Portfolio

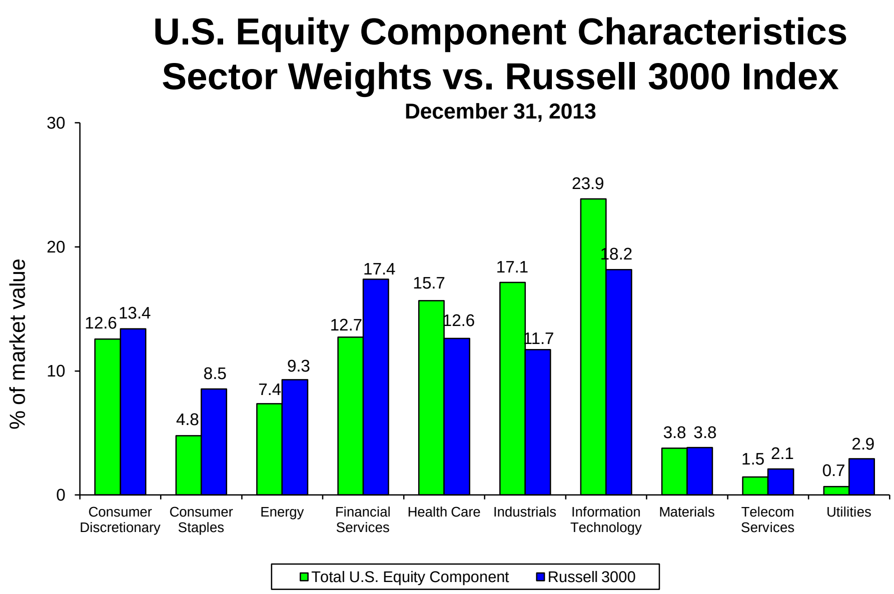
Stock Selection in the U.S. Equity Component

Active portfolio managers select individual stocks based upon valuations and expectations for future growth. Many of the best managers call themselves "benchmark agnostic", meaning they don't select stocks or sectors based upon the weighting in a benchmark. It is important to remember that the composition of most indices is backward looking, since it reflects the performance of prior periods. The weighting of an individual stock and its sector in most indices is based upon its market capitalization, so strong past performance leads to a higher weighting. When you buy an index fund, you are buying more of the recent winners, and less of the recent losers. Since active managers try to anticipate the next winners, the stocks and sectors in their portfolios can differ significantly from an index.

Sector Allocation in the U.S. Equity Component

When the stocks selected by our U.S. equity managers are aggregated by sector, the U.S. equity component will have over and underweights in certain sectors. If we explore the structure and composition of the U.S. equity component of the Board of Pensions Balanced Investment Portfolio compared to the sectors of the Russell 3000 Index, as shown in the graph that follows, we can see that the portfolio's U.S. equity component, based upon sector allocations, does not look like the Russell 3000 Index. Employing active portfolio managers who select companies with the greatest potential for stock price appreciation should result in a portfolio that does not look like an index fund. Since these are decisions made at the level of individual companies and not sectors, the resulting portfolio has over and underweights when compared to the sector weights of the Russell 3000 Index.

U.S. equity managers' favorable outlooks for health care and industrial stocks resulted in an overweight in these two sectors, two of the three best performing sectors in the Russell 3000 Index. While these sector overweights helped performance, a small underweight in consumer discretionary stocks, the best performing sector and 13.3% of the Index, slightly detracted from performance. These three best performing sectors made up 37.6% of the Russell 3000 Index. U.S. equity manager collective unfavorable outlook for telecom, utility and materials stocks resulted in under or equal weights in these sectors, the three worst performing sectors. The three worst performing sectors made up 8.8% of the index.

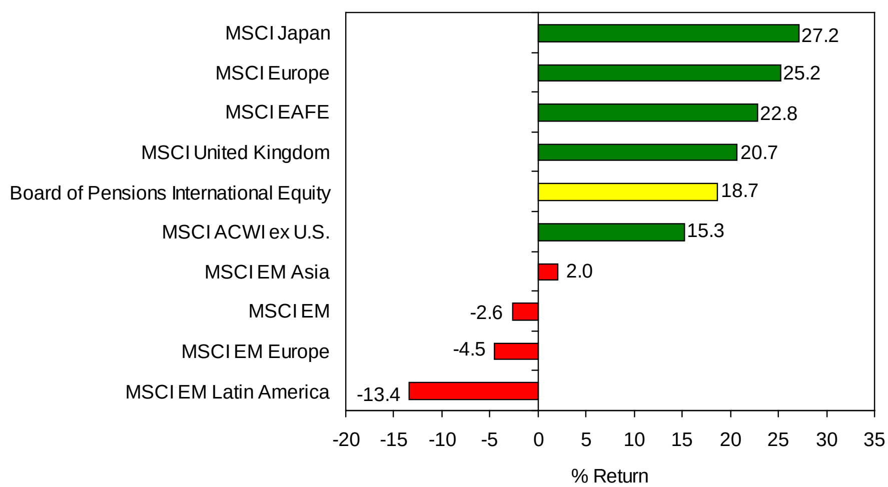


Source: BNY Mellon

International Equity Component of the Balanced Investment Portfolio
21.3% of the Balanced Investment Portfolio on December 31, 2013

The international equity component of the Board of Pensions Balanced Investment Portfolio had a return of 18.7% in 2013, exceeding the 15.8% return of the benchmark MSCI All Country World Index ex U.S., or ACWI ex U.S[1]. The index is designed to measure the equity market performance of both developed and emerging markets, including the country indices of 23 developed and 21 emerging market countries. The international equity component of the Balanced Investment Portfolio exceeded the return of the ACWI ex U.S. Index for the one, two, three, five, ten and twenty years ended December 31, 2013.

International Equity Index Returns
Year to Date December 31, 2013



Sources: BNY Mellon, MSCI (net)

Developed markets including Japan, Europe and the United Kingdom provided investors with strong, positive performance in 2013, while emerging markets in Europe and Latin American provided negative returns.

Since managers in the international equity component of the Balanced Investment Portfolio build portfolios on a stock by stock basis, superior stock selection was the primary reason for above benchmark performance. However, in 2013, sector, country allocation and currency were also important for performance. A strong U.S. dollar hurt returns for U.S. investors in Japan, Brazil, India and South Africa, while a stronger local currency improved returns for U.S. dollar investors in the U.K., European Monetary Union, Korea and China.

Four out of six developed market international equity managers outperformed their respective benchmarks in 2013. Two of the four managers that outperformed had allocations of 25-27% in Japan, significantly higher than the MSCI All Country World Index ex U.S. weight of 15.5% on

[1] The International Equity component of the Balanced Investment Portfolio is benchmarked against the ACWI ex U.S. benchmark **gross** of taxes on dividends, which returned 15.8% in 2013. Several charts in this review show the benchmark **net** of taxes on dividends, which returned 15.3% in 2013.

December 31, 2013. Japanese stocks returned 54.6% to local investors, and even after the 27.4% appreciation of the U.S. dollar to yen, U.S. dollar based investors in Japanese stocks had a return of 27.2% for 2013.

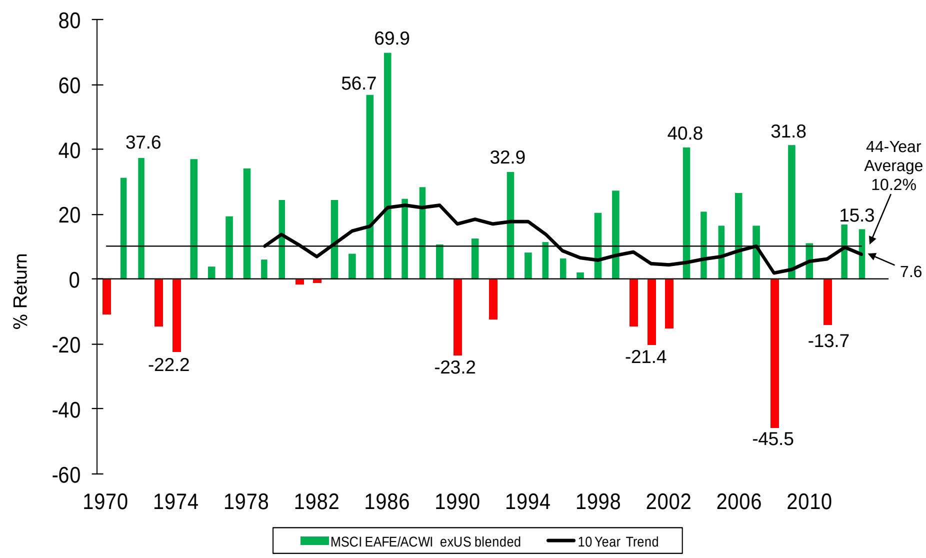
Five out of six developed market international equity managers had above benchmark allocations to Europe, with above benchmark allocations in France and Germany and a focus on countries not in the European Monetary Union, such as the U.K., Switzerland and Scandinavian countries.

Emerging market stocks are selected for the international equity component of the portfolio by the six core managers and one dedicated emerging markets manager. Five of the core international equity managers did not find many compelling investment opportunities in emerging markets, improving investment performance since emerging market equities underperformed. Performance of the dedicated emerging market manager exceeded the return of the MSCI Emerging Markets Index, but with a return slightly above zero, detracted from the return of the international equity component.

International Equity Market Historical Performance

We have created a graph of historical long-term international equity returns showing developed international equity markets, as represented by the MSCI Europe, Australasia and the Far East (EAFE) Index from 1970 through 2000 and developed and emerging markets represented by the MSCI All Country World Index ex U.S. beginning in 2001, the inception date of the ACWI ex U.S. Index. As shown in the graph that follows, the 2013 return of 15.3% is significantly above the 10-year trend line return of 7.6% and above the long-term 44-year average return of 10.2% for the blended indices since 1970. Following the pattern of the U.S. equity market, international equity had negative returns in 12 out of 44 years and in 5 of the last 14 years.

International Equity Returns in Historical Perspective
January 1, 1970 – December 31, 2013



Note: MSCI EAFE until 2000; MSCI ACWI ex US effective 2001

As shown in the graph that follows, we expected the U.S. market to outperform international markets in 2013, as it did. However, the pattern of U.S. versus international outperformance is not predictable, with long periods of over and underperformance for developed market international stocks versus U.S markets. Stocks in the S&P 500 Index had a ten year compound annual return of 7.4%, slightly outperforming the return of 6.9% from stocks in the developed market EAFE Index.

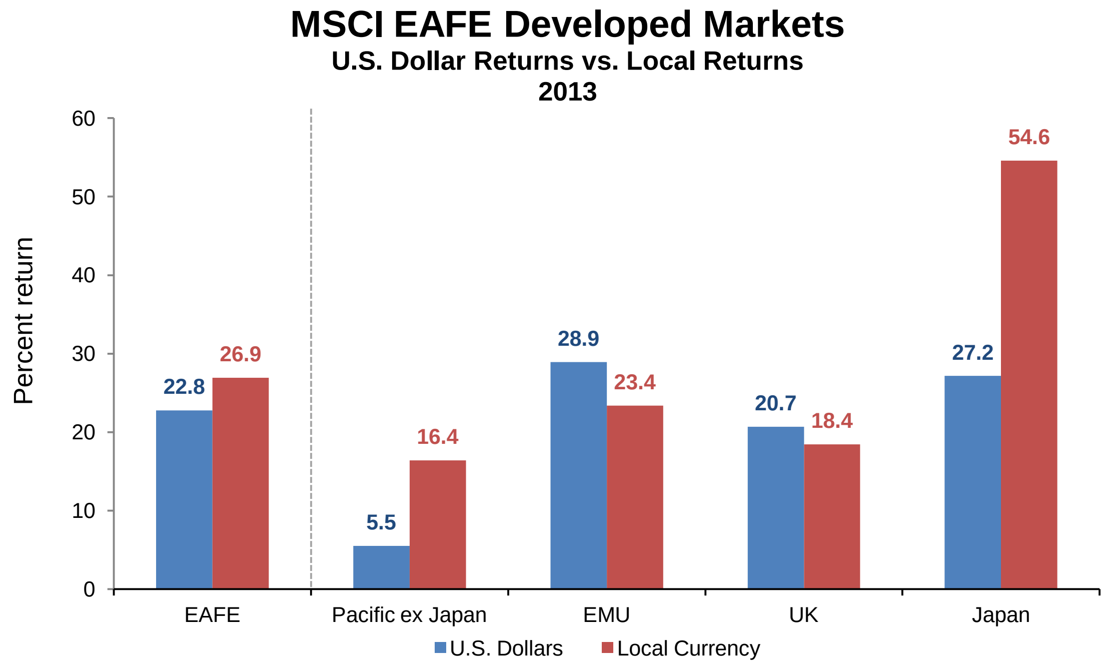
Source: Bloomberg

Developed Market Performance

International equity performance in 2013 depended on both stock and country selection while, as shown in the graph that follows, currency had a mixed impact. A strong dollar contributed to lackluster returns for U.S. dollar investors in Japan but a weak dollar helped returns in countries in the European Monetary Union (EMU) and the United Kingdom, as the value of the euro and pound strengthened against the U.S. dollar. A strong dollar makes imported goods and vacations abroad less expensive for Americans, but it hurts our export industries and reduces our returns since our Japanese stocks are worth less in strong U.S. dollars than in yen.

The U.S. dollar appreciated 27.4% against the Japanese yen in 2013, resulting in a 54.6% return to yen-based investors and a 27.2% return to U.S. dollar investors. When fears subsided over possible debt defaults, many European currencies strengthened against the U.S. dollar, including a 5.7% decline in the dollar against the euro and decline against the British pound.

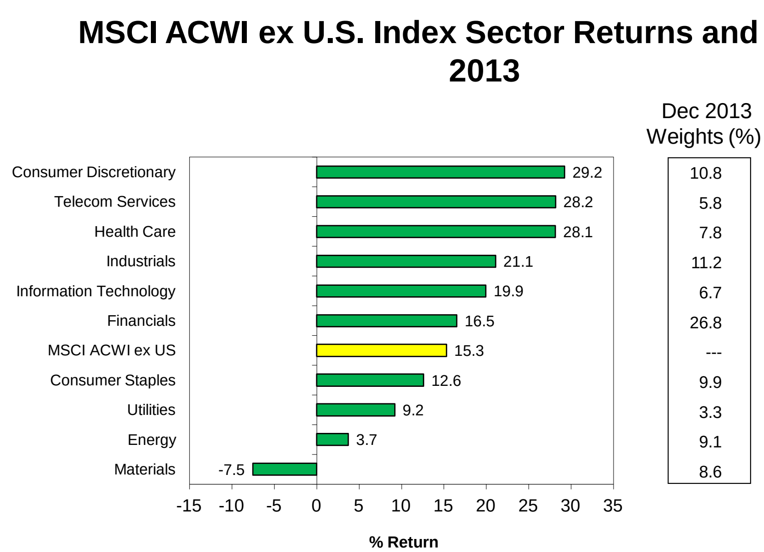
As shown on the graph that follows, investors in the twelve EMU countries that use the euro as their currency had a return of 23.4% compared to the 28.9% return to the U.S. investor. However, the 28.9% return from an index of stocks based in the twelve countries in U.S. dollars masks the variability of returns U.S. investors would have received from the indices of each country, from a 11.0% return in Portugal, to a 51.1% return in Greece, with a return of 31.4% from Germany. The 16.7% appreciation of the U.S. dollar to the Australian dollar reduced the return in dollar-based investors in the EAFE Index, which includes Australia.



Source: MSCI (net dividends)

International Sector Performance

As shown in the graph that follows, consumer discretionary companies returned 29.2%, making the sector, a 10.8% index weight, the best performer in the MSCI All Country World Index ex U.S. Telecommunications services returned 28.2% and health care returned 28.1%. The three best performing sectors, consumer discretionary, telecommunication services and health care, made up 24.4% of the index, while the three worst performing sectors, materials, energy and utilities, made up 21.0% of the index on December 31, 2013. Stock selection by managers in the international equity component resulted in an overweight in consumer discretionary and health care, which improved performance, and an underweight to materials, energy and utilities, which also improved performance.



Source: MSCI (net)

As investors review portfolio performance in 2013, it is important to appreciate the difference in composition between the Russell 3000 Index of U.S. companies and the ACWI ex U.S. of international companies. Active portfolio management results in different sector allocations than the index and provides portfolio diversification that is different from that of the Russell 3000 Index of U.S. companies. Financials are the largest sector in the ACWI ex U.S., with a 26.8% weighting yet financials had only a 17.4% weight in the Russell 3000 Index. Information technology, the largest sector in the Russell 3000 Index, had a weight of 18.2% on December 31, 2013. With fewer technology companies based in non-U.S. markets, information technology had only a 6.7% weighting in the ACWI ex U.S. Index.

Despite the linkages of a global economy, it cannot be assumed that the best performing sector in one region will also be the best sector in another. However, in 2013 consumer discretionary stocks and health care provided the best returns from both U.S. and international stocks, while energy and utility stocks were among the worst performers. Telecommunication services, the worst performing sector in the Russell 3000 with a 15.0% return, was the second best sector in ACWI ex U.S., with a return of 28.2%.

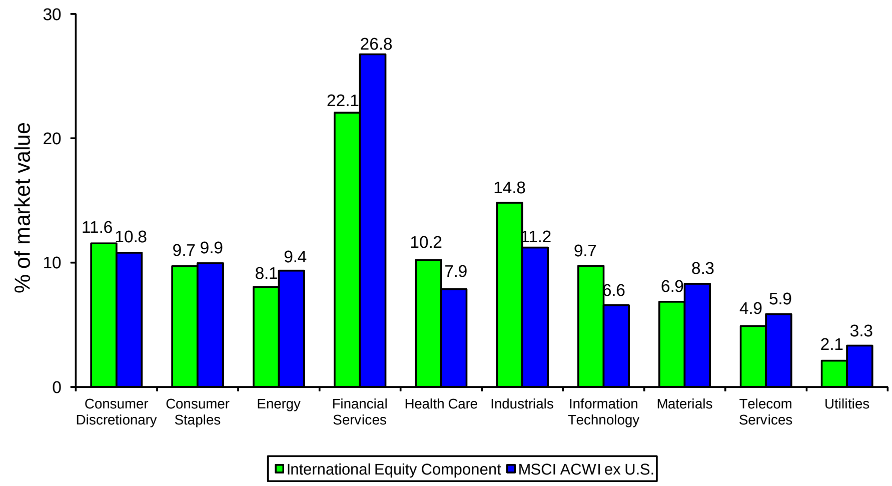
In 2013, performance of both the Russell 3000 and ACWI ex U.S. was concentrated in three sectors. In the Russell 3000, the three best sectors, consumer discretionary, health care and industrials were 37.6% of the index.   In the ACWI ex U.S., the three best sectors, consumer discretionary, telecommunication services and health care were 24.4% of the index. Superior stock selection in these important sectors resulted in outperformance compared to the benchmark index.

Sector Allocation in the International Equity Component

When the stocks selected by our international equity managers are aggregated by sector, the international equity component has over and underweights in certain sectors. If we explore the structure and composition of the international equity component of the Board of Pensions Balanced Investment Portfolio compared to the sectors of the ACWI ex U.S. Index, as shown in the graph that follows, we can see that the portfolio’s international equity component, based upon sector allocations, does not look like the ACWI ex U.S. Index. Employing active portfolio managers who select companies with the greatest potential for stock price appreciation should, and did, result in a portfolio that does not look like an index fund. Since these are decisions made at the level of individual companies and not sectors, the resulting portfolio has over and underweights when compared to the sector weights of the ACWI ex U.S. Index, with an underweight in financials and materials and overweights in health care, industrials and technology.

International Equity Component Sector Weights vs. MSCI ACWI ex U.S. Index

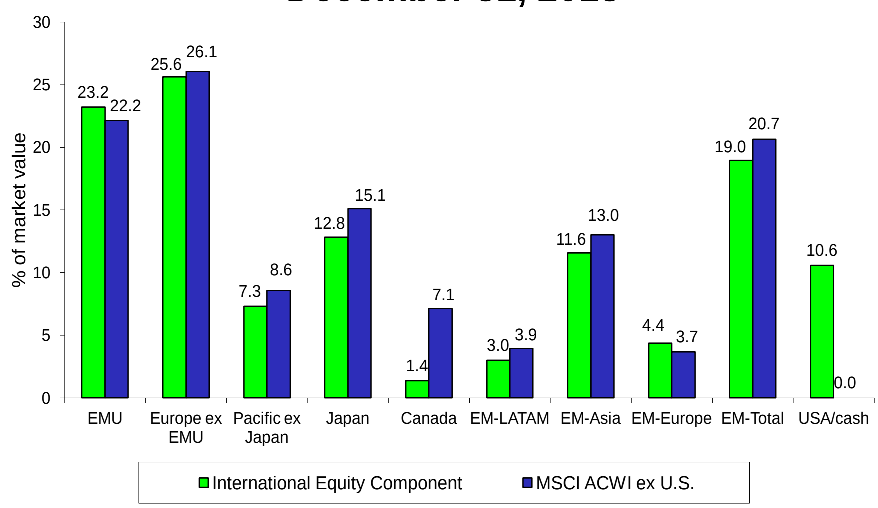
December 31, 2013



Source: BNY Mellon

Active stock selection also results in country allocations that differ from the ACWI ex U.S. Index. The international equity composite main overweight was to EMU countries, which helped performance. The underweight to Japan detracted from performance. An underweight to emerging markets improved performance in 2013.

International Equity Component Country Allocations vs. MSCI ACWI ex U.S. Index December 31, 2013

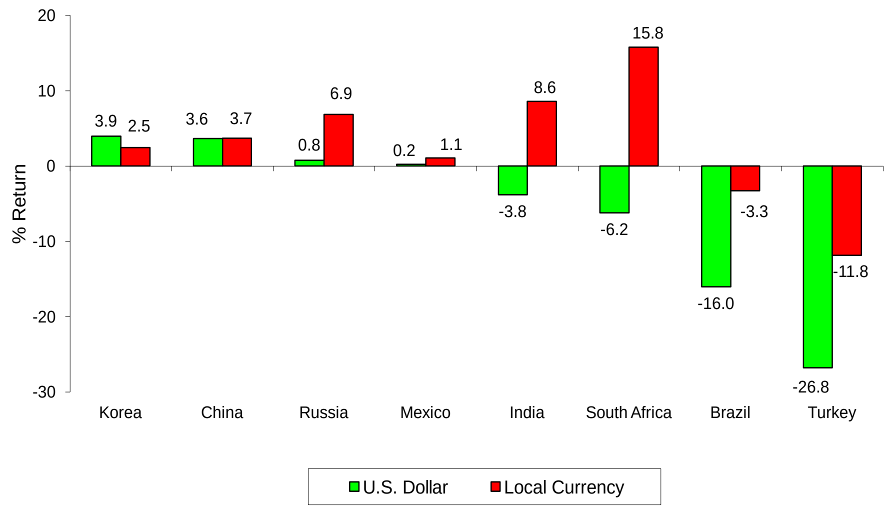


Source: BNY Mellon

Emerging Markets Performance

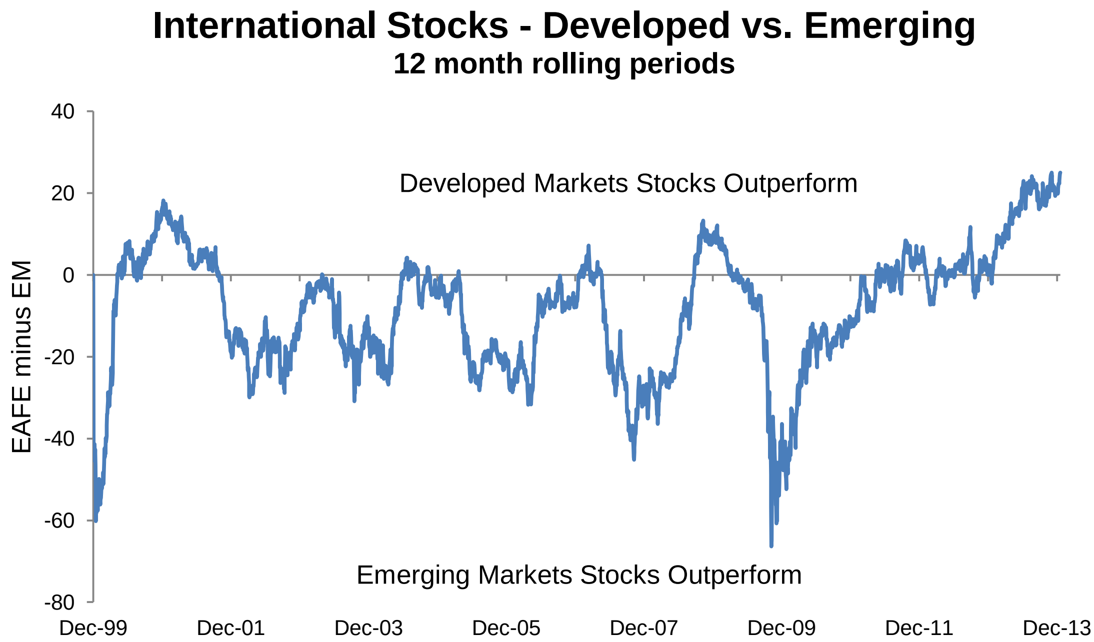
In 2013, the MSCI Emerging Markets Index returned (2.3)%. There was wide divergence in returns from emerging markets, from a 51.1% return to investors in Greece, to a (26.8)% return for investors in Turkey, one of the best emerging markets in 2012. Russia, China and India, three of the four BRIC countries (Brazil, Russia, India and China), which are the largest emerging market countries, had positive returns and exceeded the (2.3)% return of the index. In many years, currency in emerging markets has had limited impact on investment performance, but in periods of rising inflation and central bank management of reserves and interest rates, the relationship of a country's currency to the U.S. dollar can add to or detract from performance for U.S. dollar-based investors. Brazil's local return was a (3.3)%. However an economic slowdown and an increase in inflation contributed to the 12.8% appreciation of the U.S. dollar against the value of the Brazilian real, for a return of (16.0)% to dollar-based investors in Brazil. Political turmoil in Turkey contributed to the 20.1% appreciation of the U.S. dollar against the value of the Turkish lira, for a return of (26.8)% to dollar-based investors in Turkey.

Selected Country Performance – MSCI Emerging Markets
U.S. Dollar Returns vs. Local Returns
Year to Date December 31, 2013
Sorted by US$ returns



Source: MSCI (with dividends reinvested, net)

As shown on the graph that follows, emerging markets underperformed developed markets in 2013, with a return of (2.3)% compared to the 22.8% return from EAFE developed markets. Despite negative performance in 2013, emerging markets in the MSCI Emerging Markets Index had a ten year compound annual return of 11.2%, significantly outperforming the return of 6.9% from stocks in the developed market EAFE Index.

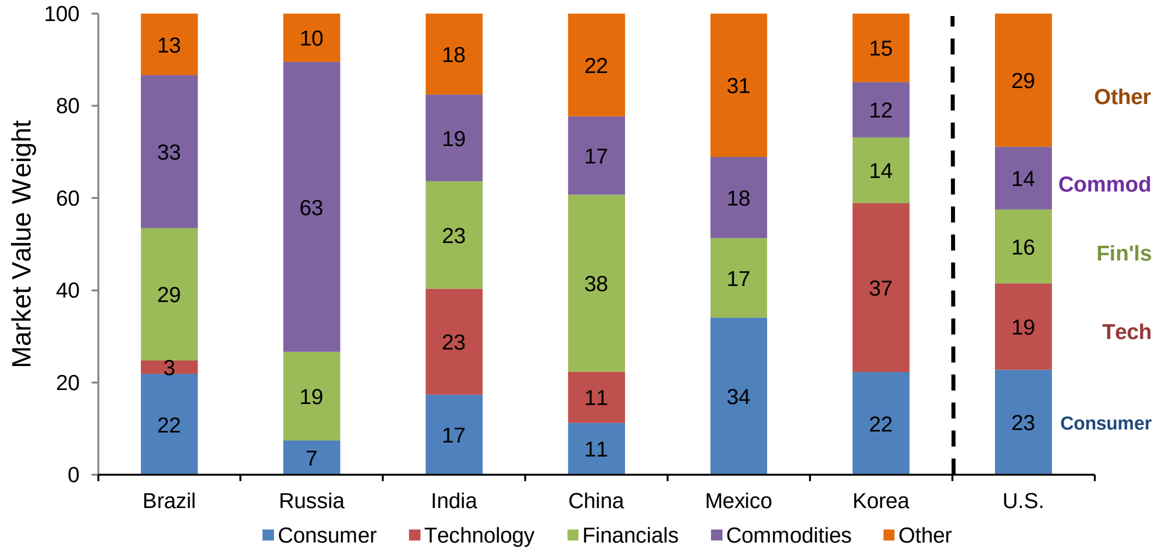


Source: Bloomberg

It is important to understand the difference in the composition of the economies and stock markets of emerging market countries. The increasing and decreasing role of key sectors in each country will determine long-term investment stability as well as national growth. On the graph that follows, we compare and contrast the composition of stock markets in several emerging market countries. Each country index is comprised of the stocks of companies domiciled in that country and listed on their local stock exchange.

If we begin with the U.S. on the far right, the U.S. stock market is well diversified, with 23% in consumer sectors, 19% in technology, 16% in financials, 14% in commodities and 29% in other sectors. However, the diversification observed in a mature economy like the U.S. is generally not seen in emerging markets. Brazil, the bar on the far left, is heavily concentrated, with 33% in commodities and 29% in financials. Russia has fully 63% in the commodity sector, 19% in financials, 7% in consumer and no technology. As a result, as a commodity driven economy, the Russian market performs well when oil prices are increasing and supplies are tight. India has a 23% financial allocation, with 23% in technology. The consumer sector is 17% and did not grow in the last year. China, with a 38% allocation to financials, needs to reduce savings and grow the 11% consumer sector. Mexico has 34% in the consumer sector, 18% in commodities, but no technology. It is not surprising that 37% of the Korean index is technology and consumer is 22%.

MSCI Country Indices
Individual Countries by Sector



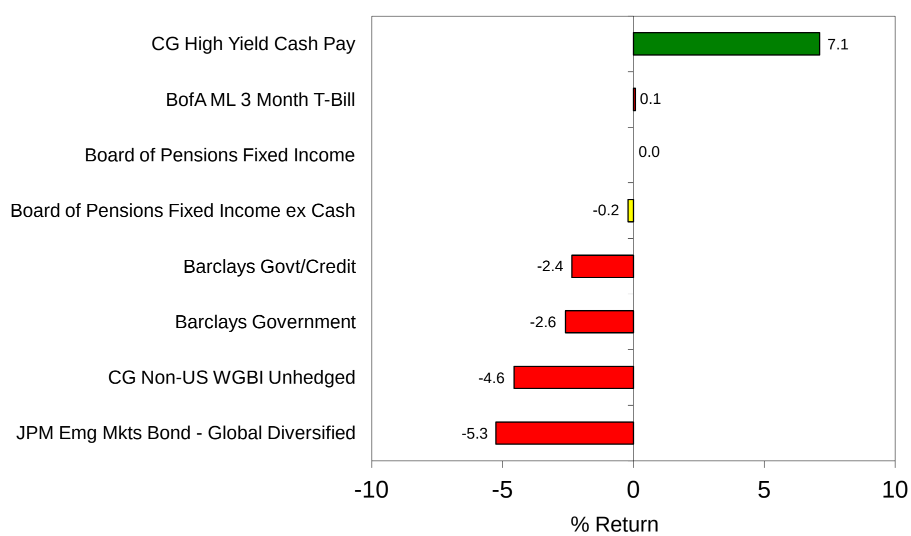
Sources: J.P. Morgan, MSCI

Fixed Income Component of the Balanced Investment Portfolio
29.5% of the Balanced Investment Portfolio on December 31, 2013

The fixed income component of the Portfolio had a return of 0.0% compared to the benchmark return of (2.4)% provided by the Barclays Government/Credit Index. The fixed income component exceeded the return of the Barclays Government/Credit Index for the one, two, three, five, ten, fifteen and twenty years ended December 31, 2013.

As shown on the graph that follows, 2013 fixed income index performance ranged from the 7.1% of the Citigroup High Yield Cash Pay Index to the (5.3)% return from JPM Emerging Markets Bond Index.

Fixed Income Index Returns
Year to Date December 31, 2013



Source: BNY Mellon

In this environment, all managers in the fixed income component of the Balanced Investment Portfolio, with the exception of one core manager, exceeded their passive benchmarks. Two of the three core fixed income managers exceeded the return of the Barclays Government/Credit Index, providing returns of 0.6% and (1.1)% compared to the Index return of (2.4)%. Core fixed income manager outperformance was primarily due to shorter than index duration, portfolio underweighting in U.S. Treasury bonds and the allocation to and superior selection of corporate bonds.

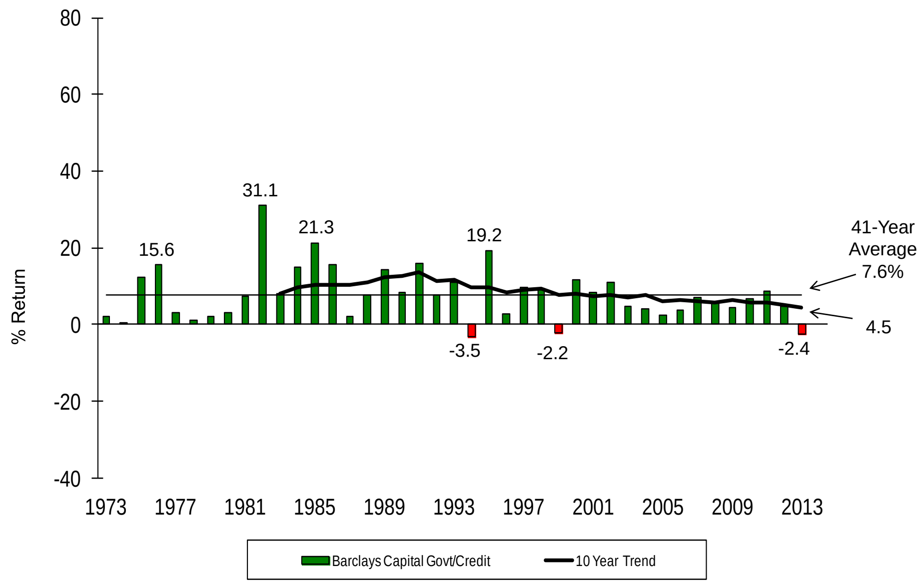
The 0.0% return of the fixed income component included the returns from core fixed income managers as well as a 6.7% return from our high yield portfolio and a 1.1% return on the short duration portfolio. The emerging market debt portfolio returned (0.5)% and the global sovereign bond portfolio returned (3.2)%. All four actively managed specialty portfolios outperformed their benchmarks. Cash and the short duration portfolio comprised 18.1% of the fixed income component on December 31, 2013. The strategic short duration fixed income allocation of 125% of annual benefits payments was approved by the Investment Committee in July 2008. The short duration strategy improved the performance of the fixed income component of the Balanced Investment Portfolio throughout 2013 as interest rates increased. Excluding cash and the short duration portfolio, the fixed income component had a return of (0.2)% for 2013.

Fixed Income Market Historical Performance

The chart that follows provides the historical performance of the U.S. fixed income market, as represented by the returns of the Barclays Government/Credit Index. Investors in fixed income can experience negative returns during periods of rising interest rates or when spreads widen on corporate bonds and other types of credit based instruments. However, if we compare annual performance in a graph similar to those of long-term performance for U.S. and international stocks, fixed income has had far fewer and less severe years of negative performance. Over the last 10 years, as shown on the 10-year trend line in the graph, the Barclays Government/Credit Index had a return of 4.5%, below the 41-year average return of 7.6%. Fixed income markets had negative returns in 1994, 1999, and 2013 or only 3 out of 41 years.

Fixed Income Returns in Historical Perspective

January 1, 1973 – December 31, 2013



Investment Performance

Bond performance depends on multiple factors but usually the most important ones are the level and direction of interest rates, portfolio duration, credit quality and investor appetite for risk, as reflected in the spread over U.S. Treasuries for corporate bonds. In 2013, the big bond market events were related to Federal Reserve comments, decisions and actions. In 2012, the Fed announced the expiration of Operation Twist, a strategy to use short term debt to buy long term debt on the open market. However, they planned to continue to purchase up to $85 billion in long-term Treasury and Agency securities per month. It was anticipated that Fed purchases and the zero interest rate environment would be maintained until unemployment dropped below 6.5% or inflation projections topped 2.5%. These actions indicated to markets that the Fed would be aggressive in attempts to not only bring unemployment down, but also potentially offset any fiscal consolidation, tax increases and/or spending cuts approved by Congress in 2013.

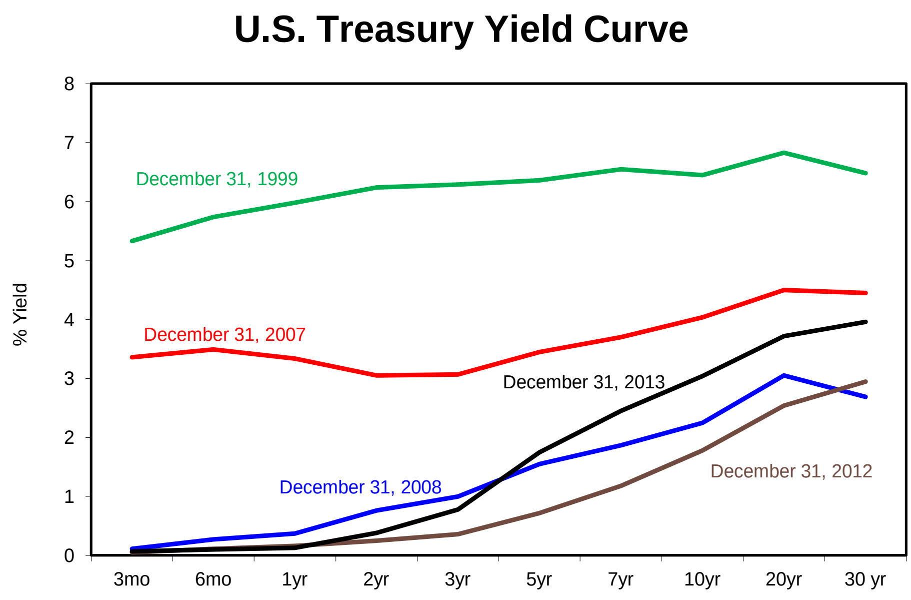
Global markets had an immediate and negative reaction to the May 22, 2013 speech by Fed chairman Bernanke in which he commented that he believed the Fed would start to “taper” or reduce the purchase of Treasury and Agency securities in 2013 and eliminate the bond buying program completely in 2014, when unemployment fell to around 7%. Yields on emerging markets debt sharply increased and global stock markets declined. When the Fed took no taper actions in late summer 2013, markets began to stabilize. The Fed announced on December 18, 2013 that the improvement in the outlook for the labor market warranted a reduction in the bond purchases to $75 billion a month but low short term rates would not be increased in the near term.

Interest Rates

The Federal Reserve’s target for the federal funds rate was 4.25% at the start of 2008. This is the interest rate at which private depository institutions, primarily banks, lend balances at the Federal Reserve on an overnight basis to other depository institutions. On December 16, 2008, after six reductions in the first ten months of 2008, the Federal Open Market Committee made the unprecedented move of setting the funds target rate in the range of zero to 0.25%. No change in the fed funds target rate has been made since 2008.

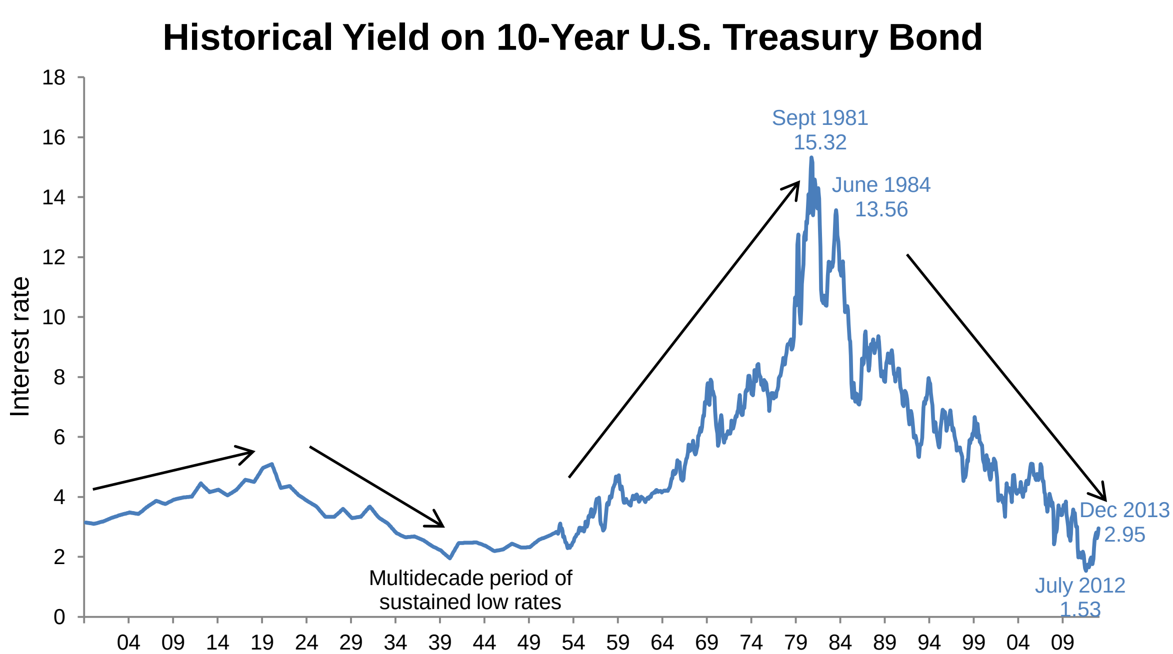
Interest rates on the shortest U.S. Treasury maturities increased very slightly in 2013, with a more significant increase in rates on longer maturities. The yield on the 3-month Treasury bill was 0.04% on December 31, 2012 and increased by 3 basis points to 0.07% on December 31, 2013. The yield on the 2-year note increased from 0.25% to 0.38% over the same period, while the 10-year Treasury yield increased by 126 basis points, from 1.78% on December 31, 2012 to 3.04% on December 31, 2013.

While the absolute level of interest rates is important, the shape of the yield curve and the relationship between short and long rates is equally important. Curve watchers in 2010 focused on the near-record steepness of the Treasury yield curve, as reflected in the 270 basis point difference in rates between the 2-year and 10-year Treasury. On December 31, 2011, there was a 164 basis point spread between the 2-year and 10-year Treasury, an important decrease of more than 100 basis points. On December 31, 2012, there was a 151 basis point spread between the 2-year and 10-year Treasury, reflecting historically low rates that even the Fed could not push lower. On December 31, 2013, there was a 265 basis point spread between the 2-year and 10-year Treasury, an increase of 114 basis points.



Source: Federal Reserve, statistical release

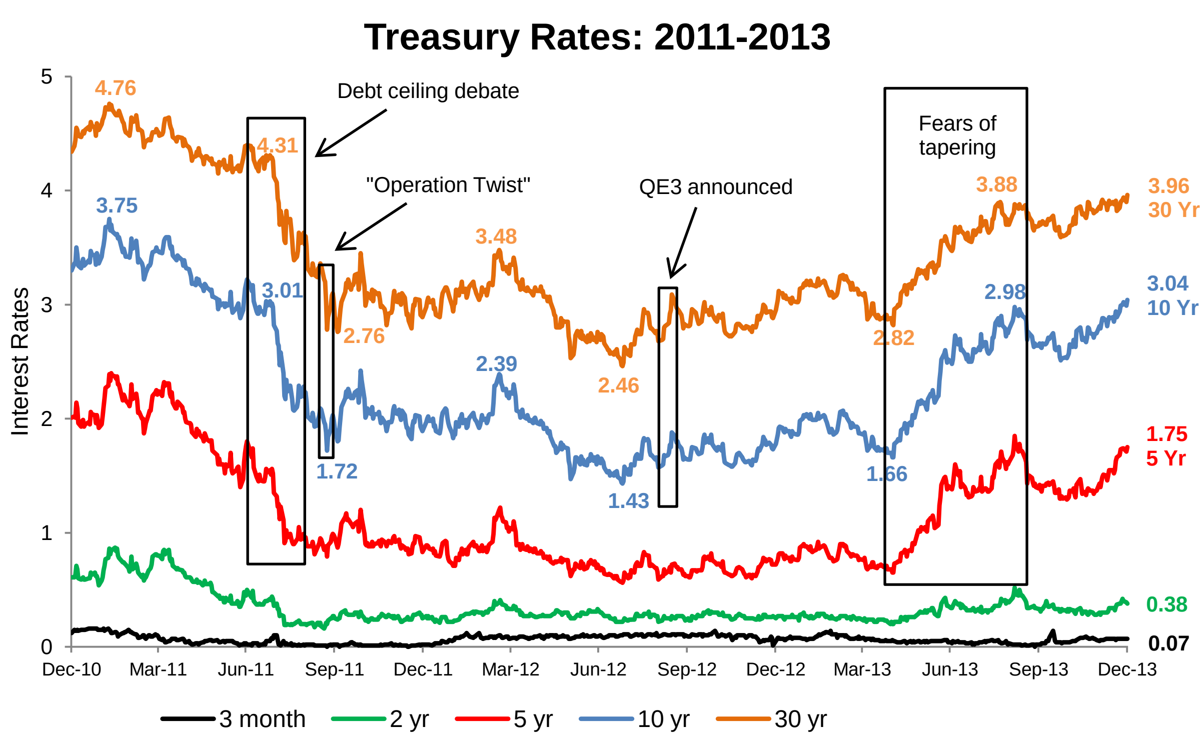
We have experienced historically low interest rates since the global financial crisis of 2008, so it is important to step back and review where yields have been over the longer time periods. In July 1954 the yield on a 10-year U.S. Treasury bond was 2.30%. Yields had an uneven but steady progression to higher levels, culminating in the 15.32% yield on a 10-year Treasury in September 1981. While yields experienced modest increases and decreases on an annual basis, over the next 30+ years interest rates declined providing investors in long bonds more than 30 years of superior returns. The 10-year Treasury was 1.53% in July 2012, increasing 151 basis points to 3.04% on December 31, 2013 as the Federal Reserve announced the slowdown in Quantitative Easing and the reduction or tapering of the bond buying program. As shown on the graph that follows, the U.S. experienced interest rates persistently below 4% on the 10-year Treasury from the late 1920s through the 1950s.



Source: Federal Reserve from 1953 to 2013; Robert Shiller from 1900 to 1953. Reflects monthly averages which differ from daily data shown elsewhere.

The graph that follows illustrates why the Federal Reserve quietly ended Operation Twist and introduced QE 3 in September 2012, followed by an increase in the bond buying program. If we first review interest rates in 2011 in greater detail, we can see the downturn in long rates that helped spark the rebound of the U.S. stock market in the third quarter of 2011. As shown in the top line on the graph that follows, the 30-year Treasury rate peaked at 4.76% in early 2011 and was 4.31% just prior to the debt ceiling debate, flight to Treasuries and Operation Twist. By late September the interest rate on a 30-year Treasury was 2.76%. The interest rate on the benchmark 10-year Treasury mirrored the pattern of the 30-year bond. The 10-year Treasury rate peaked at 3.75% in early 2011 and was 3.01% just prior to that debt ceiling debate, flight to Treasuries and Operation Twist. By late September 2011 the interest rate on a 10-year Treasury was 1.72%. However, rates rose in early 2012 as investors anticipated better economic growth. The 30-year Treasury increased from 2.89% on December 31, 2011 to 3.48% on March 19, 2012.

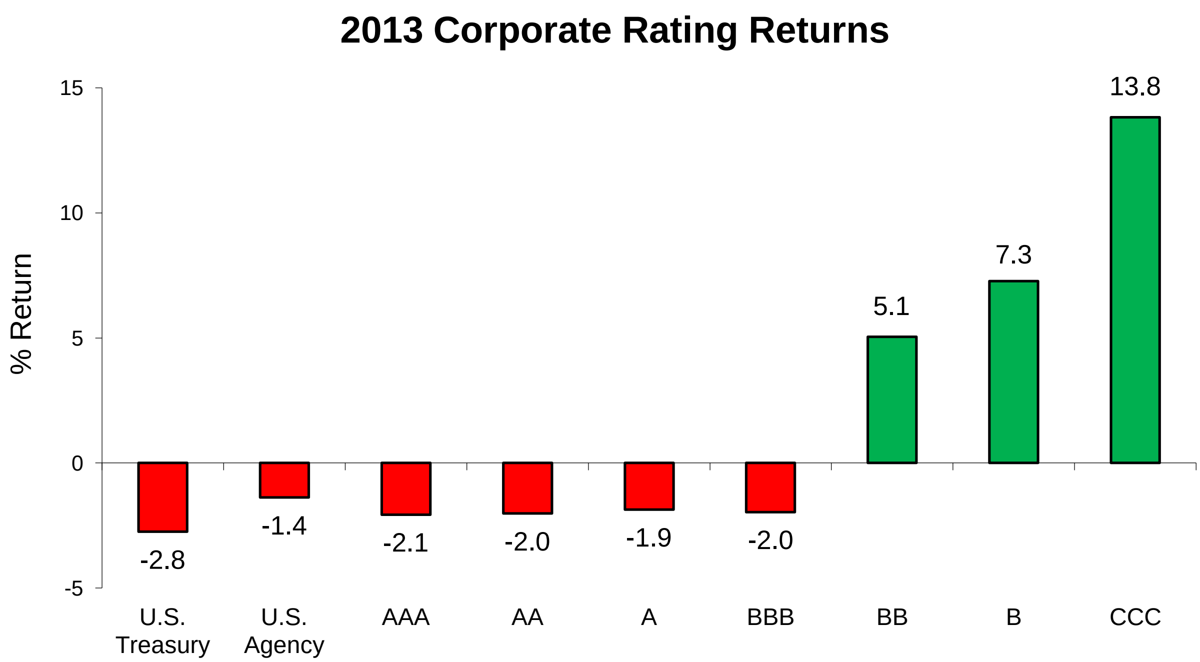
With Operation Twist running out of steam, in September 2012 the Federal Reserve announced the start of a new program of quantitative easing, or QE 3, buying $40 billion in mortgage-backed securities each month. The goal was to put downward pressure on long-term interest rates and support mortgage markets. QE 3 had minimal impact in 2012, with the 30-year Treasury closing the year on December 31, 2012 at the same 2.95% interest rate as on the day the program was announced. In late 2012 it was announced the Fed would now buy $85 billion a month of Treasury and mortgage-related securities. The 30-year Treasury was at 2.82% in May 2013, just prior to Fed chairman Bernanke's announcement that the Fed might soon begin to taper bond purchase. Market fears of tapering led to a 3.88% interest rate on the 30-year Treasury in August 2013, which closed the year at 3.96% or an increase of 114 basis points. The increase on the 10-year Treasury was similar, with an interest rate of 1.66% pre-taper comments, rising to 2.98% in August and closing the year on December 31, 2013, at 3.04% or an increase of 138 basis points.



Source: Federal Reserve

Credit Quality and Spreads

Credit ratings are given to bonds based on Standard & Poor's and Moody's analyses of the ability of the corporation to pay interest and repay principal on schedule to bondholders. As reflected in the graph below, U.S. Treasury bonds provided investors with safety and liquidity but a (2.8)% return in 2013. Investors in BBB bonds, the lowest rating for investment grade bonds, had the same (2.0)% return as an investor in AA corporate bonds, but with arguably less liquidity and security of principal repayment. Investors had to increase their risk tolerance to get a positive return from lower quality high yield bonds. Those with the greatest appetite for risk achieved a return of 7.3% from B bonds and 13.8% for CCC bonds.



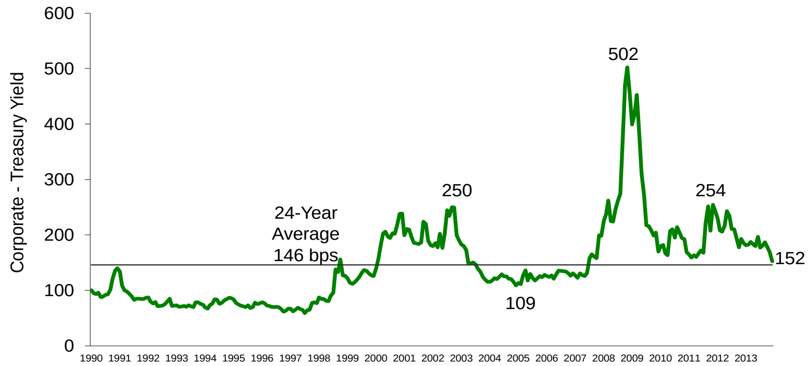
Sources: Barclays Capital, Dodge & Cox

The U.S. Treasury bond is typically considered the highest quality long-term fixed income investment with the greatest liquidity and no default risk. As such, it is the benchmark security used by investors to price all other long term bonds. The spread for investment grade corporate bonds is a risk premium, or additional yield that investors require for any bond that is not a U.S. Treasury bond.

As shown in the graph that follows, from 1990 through 2013 the average spread, or risk premium required by investors to purchase an investment grade corporate bond instead of the higher quality, more liquid 10-year U.S. Treasury bond was 146 basis points. In 2008, rating downgrades, lack of confidence in the rating agencies, weak corporate earnings, accounting and pricing concerns all impacted corporate bond spreads. Market liquidity evaporated and investors demanded higher yields for anything with even the most remote potential for default. The yield spread for investment grade bonds compared to a 10-year U.S. Treasury peaked at 502 basis points in 2009. In 2013, spreads narrowed then widened, then narrowed, closing the year at a spread of 152 basis points, lower than the 185 basis point spread on December 31, 2012. The 152 basis point spread on December 31, 2013 is slightly above the 24 year average of 146 basis points. In 2014 investment grade corporate bonds may earn their coupons under stable interest rates but will likely not experience much capital appreciation from spread compression.

Investment Grade Corporate Bonds vs. Ten-Year Treasury Bonds

Yield Spread in Basis Points



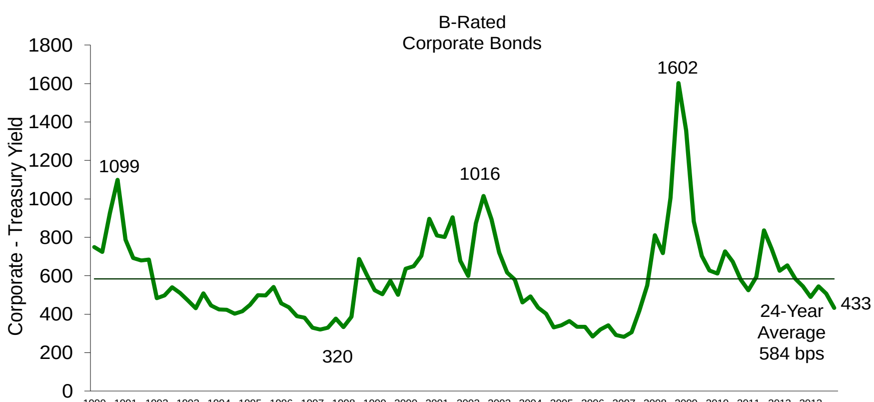
Sources: Dodge & Cox, Citigroup

Based on investment grade bonds with maturities greater than ten years

The graph that follows provides an historical overview of the relationship of the yield on high yield bonds and U.S. Treasuries. The yield spread, or risk premium is the additional cushion of safety required by investors to purchase high yield bonds instead of 10-year U.S. Treasury bonds. High yield spreads mirrored the relationship pattern of investment grade corporate bonds to Treasuries in 2008, with spreads tripling in the second half of 2008, to close the year at a historic high of 1602. By the start of 2012, investors willing to accept less liquidity and assume additional risk demanded a 740 basis point premium over the interest rate on a 10-year U.S. Treasury before they would purchase high yield bonds, above the 24 year average of 584 basis points. As high yield interest rates continued to decline in 2012, investors seeking higher income and capital appreciation in a world of low interest rates began to invest in high yield bonds and the required premium narrowed from 740 at the beginning of 2012 to 545 basis points on December 31, 2012, below the 23-year average. Spreads narrowed further in 2013, closing to 433 basis points on December 31, 2013. The current spread of 433 basis points is below the long term average spread of 584 basis points. In 2014 high yield corporate bonds may earn their coupons under stable interest rates or declining rates but will likely not experience much capital appreciation from spread compression.

High Yield Corporate Bonds vs. Ten-Year Treasury Bonds

Yield Spread in Basis Points



Sources: Oaktree Capital, Citigroup

Default Rates

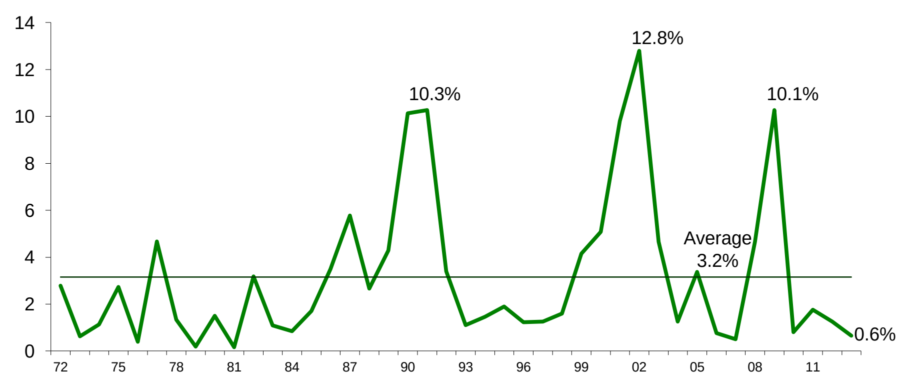
In 2013, some investors were concerned that the Greek, Italian and Portugese governments would default on their bonds, but that was not the case in the U.S. where the default rate on U.S. corporate bonds declined from 1.1% at the end of 2012 to an estimated 0.6% on December 31, 2013. This is the lowest default rate since 1972 and well below the 42-year average default rate of 3.2%.

As shown in the graph that follows, default rates for corporate bonds peaked at 12.8% in 2002, when the investment grade corporate bonds of WorldCom and other highly leveraged companies fell to below investment grade and defaulted in a matter of days. The default rate for U.S. dollar-denominated bonds is the par value of defaulted securities as a percentage of the par value of outstanding issues.

A record number of mergers and acquisitions in 2006 and 2007 required high levels of debt financing. Some acquisition debt was provided at extremely favorable rates and terms to companies potentially at risk for future financial distress. Many distressed debt investors believed that based on the level of debt outstanding and expected levels of bankruptcies, default rates in 2009 and 2010 would exceed the 12.8% experienced in 2002. While the 2009 rate was 10.1%, default rates since then have remained at historically low levels as banks and other lenders have provided corporations with extra time to work through potential breaches in loan covenants, extended maturities and refinanced interest rates to avoid foreclosures and bankruptcies. Investors have remained anxious to buy high yield debt refinancings in this ultra-low rate environment.

U.S. Historical Default Rates

1972 through 2013*



Sources: Oaktree Capital, Citigroup, and JP Morgan
* The 12/31/13 default rate provided is an Oaktree estimate.

Alternative Investment Component of the Balanced Investment Portfolio
11.9% of the Balanced Investment Portfolio on December 31, 2013

Review of Alternative Investments and 2011 Liquidity Study

The Board of Pensions initiated the alternative investment component of the Balanced Investment Portfolio in 1997 with a commitment of $30 million to an emerging markets private equity limited partnership. In 2007, a decade later and following a year-long liquidity study, the Investment Committee approved an allocation of up to 10% in illiquid limited partnerships, including U.S., international developed and emerging markets private equity, venture capital and distressed debt. The 10% allocation included investments plus any committed capital not yet invested. Liquid, marketable alternatives, including real estate investment trusts (REITs) and real return strategies, could be a maximum of 5% of the portfolio.

The 2007 liquidity study was updated in 2011 to incorporate more powerful modeling tools and provide scenario analyses utilizing global market conditions since the 2007 study, including the 2008 collapse of global financial markets. The study affirmed an allocation of 10% to illiquid limited partnerships but demonstrated the benefit of a more flexible allocation of up to 20% in alternative investments, to include illiquid limited partnerships as well as liquid strategies. In October 2011, the Investment Committee recommended and the Board of Directors approved a change in the range for alternative investments from 15% to up to 20% of the assets of the Board of Pensions Balanced Investment Portfolio, to include committed but uncalled capital commitments.

2013 Retrospective Study of Limited Partnership Investments

Limited partnership investments are inherently illiquid investments. Partnership investments increased from six on December 31, 2002 to fifty one on December 31, 2013. The alternatives component began with limited partnership investments in emerging markets equity, with subsequent commitments made to distressed debt; U.S., international and natural resources private equity; and venture capital. As the number of partnerships has increased, so has the complexity of selecting, reviewing and monitoring these investments, in part due to increasing regulatory, accounting and reporting requirements.

The purpose of the retrospective study was to review the value of investing in limited partnership investments compared to public market investments. The study included all limited partnership investments from program inception through December 31, 2012. The study showed that the Balanced Investment Portfolio was approximately $357 million larger on December 31, 2012, than it would have been had the Board of Pensions invested the dollars in publicly traded securities instead of investing them in illiquid limited partnerships.

2013 Study of Limited Partnership Benchmarks

From the time of the Board of Pensions first limited partnership commitment in 1997, the single performance benchmark has been the Russell 3000 Index plus an additional 500 basis points to compensate for additional risk and illiquidity in limited partnership investments. Returns from these investments had a low correlation to public market returns prior to 2008 but correlations experienced a significant increase after accounting changes instituted in 2008 required that limited partnership assets be marked to market each quarter. In 2013, the Investment Team initiated a study of the relationship between the returns of different types of limited partnership investments and related public market equity and fixed income indices over periods before and after the accounting change. The Investment Team completed a research paper using extensive statistical correlation analyses to evaluate whether the existing benchmark for limited partnerships of the Russell 3000 plus 500 basis points was still appropriate or whether more appropriate benchmarks existed for each type of partnership investment. The Investment Team recommended and the

Investment Committee approved using more closely correlated public market indices for each sub-set of limited partnership investments. As shown in the table on the following page, these public market indices, plus a liquidity and risk premium of 300 basis points, provide more appropriate performance benchmarks for different types of limited partnerships.

Performance of Limited Partnership Investments
7.3% of the Balanced Investment Portfolio on December 31, 2013

In 2013, four new commitments were approved for limited partnerships in distressed debt, energy, and international emerging private equity. Three of the commitments were to firms with which the Board of Pensions had successful prior investments, with one commitment to a new firm.

Equity and venture capital limited partnerships underperformed their benchmarks in 2013. Some of the performance difference was due to a one quarter lag in performance reporting but it is important to remember that limited partnerships are long-term investments with a minimum of a ten year horizon. For the ten years ended December 31, 2013, the return of U.S. private equity and natural resource partnerships exceeded their public market benchmark of the Russell 3000 plus 300 basis points. Distressed debt partnerships exceeded the public market benchmark of the Citigroup High Yield Cash Pay Index plus 300 basis points in 2013 but lagged in longer time periods. Venture capital partnerships underperformed the Russell 2000 plus 300 basis points in all time periods.

Performance of Liquid Alternative Investments
4.6% of the Balanced Investment Portfolio on December 31, 2013

The investments in real return strategies were initiated in 2005 to provide protection during periods of increasing U.S. inflation. Inflation has not been a problem and those strategies reduced the return of the Balanced Investment Portfolio in 2013. Inflation and real return strategies provided a return of (0.3)% in 2013, lagging the 6.5% return of the benchmark of the CPI + 5%. Inflation and real return strategies outperformed for the five years ended December 31, 2013. The allocation to real estate through an investment in real estate investment trusts (REITs) was eliminated in July 2013.

The Balanced Investment Portfolio is invested in three absolute return strategies. One is a global macro strategy that returned 3.5% in 2013. Two risk parity strategies underperformed expectations. One returned (2.5)%, the other (3.9)%. Both managers had a significant allocation to fixed income, primarily using TIPS or Treasury Inflation Protection Securities. In May 2013 when Fed chairman Bernanke announced possible tapering and fixed income markets reacted negatively to the news, the market value of TIPS collapsed as hedge fund and mutual fund investors sold off TIPS, driving down prices in a relatively illiquid Treasury security. In 2013, the three absolute return strategies returned (0.7)%, underperforming the 6.5% return of the benchmark of CPI + 5%.

ALTERNATIVE INVESTMENT PERFORMANCE HIGHLIGHTS

PERIODS ENDED DECEMBER 31, 2013

	Annualized Rate of Return				
	1 Year	2 Years	3 Years	5 Years	10 Years
BOP LIMITED PARTNERSHIPS					
US PRIVATE EQUITY-NATURAL RESOURCES	14.4	15.1	14.8	9.9	13.2
Russell 3000 +300 bps *	37.2	28.1	19.4	22.0	10.9
INTERNATIONAL PRIVATE EQUITY	2.5	0.1	0.5	7.6	16.6
MSCI ACWI ex US +300 bps *	19.0	19.8	8.5	16.4	11.0
DISTRESSED DEBT	15.0	13.6	8.6	10.8	7.3
CG High Yield Cash Pay +300 bps*	10.1	14.1	12.2	21.1	11.2
VENTURE CAPITAL	8.1	6.8	12.5	8.7	4.5
Russell 2000 +300 bps *	42.6	30.6	18.9	23.4	12.1
BOP LIQUID ALTERNATIVES	(0.6)	4.5	4.6	12.2	--
Consumer Price Index +5% Annually	6.5	6.6	7.1	7.1	7.4

* The Index +300 basis points is calculated monthly and linked to provide an annualized number that will be different than the sum of the annual return of the Index +300 basis points.

Portfolio Accounting

The total return on the Balanced Investment Portfolio is measured using the actual market value of assets held on January 1, 2013, and the actual market value of assets held on December 31, 2013. The beginning asset value is increased by interest income and dividends and decreased by fees and benefits paid during the year. In 2013, the portfolio paid out $265 million in benefits in excess of dues received. The portfolio had net realized gains of $380 million on securities sold in 2013 and unrealized gains of $750 million due to appreciation in the market value of securities still held in the portfolio on December 31, 2013.

MARKET VALUE RECONCILIATION
BOARD OF PENSIONS
BALANCED INVESTMENT PORTFOLIO

	$Millions
Market Value on January 1, 2013	$7,476
Net Income	151
Net Realized Gain	380
Net Unrealized Gain	750
Cash Flows into Portfolio	9
Benefits Payments in Excess of Dues	(265)
Investment and Custody Fees	(23)
Market Value on December 31, 2013	$8,478

Plan and Program Participation

The assets of the Board of Pensions Balanced Investment Portfolio are unitized so that each participating plan and program owns units in the portfolio rather than individual securities. This reduces the investment and custodial fees for all plans and programs. The valuation of units is done monthly by BNY Mellon, custodian for all assets, using an accounting process similar to that used to develop the net asset value of a mutual fund. Plans, with the exception of the Benefit Supplement Fund, Medical Plan Long-Term Reserve and Medical Plan Contingency Reserve, own only units of the portfolio and have the same asset allocation and investment performance as the Balanced Investment Portfolio, dependent upon the time the plan or program adopted a 100% allocation to the portfolio.

The Assistance Funds and both Medical Reserve accounts own units of both the Board of Pensions Balanced Investment Portfolio and the Board of Pensions Fixed Income Portfolio. The Fixed Income Portfolio, valued at $57 million on December 31, 2013, can be used by plans and programs with differing investment horizons, enabling us to customize their long-term asset allocation.

The table that follows shows the market values of plans and programs participating in the Board of Pensions Balanced Investment Portfolio and the Board of Pensions Fixed Income Portfolio at BNY Mellon.

PLAN AND PROGRAM PARTICIPATION
December 31, 2013

	$Millions	% of BOP Balanced Investment Portfolio
Pension Plan	$7,594	89.58%
Death and Disability Plan	718	8.47
Supplemental Death Benefits Plan	31	0.37
Medical Plan Long-Term Reserve	27	0.32
Medical Plan Contingency Reserve	11	0.13
Endowment Fund	20	0.23
Benefit Supplement Fund	24	0.28
Retirement Housing Fund	8	0.10
General Assistance Fund	30	0.35
Chaplains Deposit Fund	4	0.04
Restricted Gifts Fund	8	0.10
Other	3	0.03
Board of Pensions Balanced Investment Portfolio	**$8,478**	**100.00%**
Board of Pensions Fixed Income Portfolio	57	
Total Investments at BNY Mellon	**$8,535**	

The Assistance Fund, Medical Plan Long-Term Reserve and Medical Plan Contingency Reserve own units of the Board of Pensions Balanced Investment Portfolio and the Board of Pensions Fixed Income Portfolio. “Other” includes the GAC Special Cuban Fund and the SR Plan, which each have total assets of less than $3 million.

Note: Due to rounding, percentages may not total 100%.

Partnerships We Can Be Proud Of

The Board uses multiple investment managers for each asset class in the Board of Pensions Balanced Investment Portfolio. Staff and the Investment Committee evaluate, retain and monitor managers for specific assignments within the total portfolio. The managers are responsible for the selection of individual securities or companies for their portfolios.

Custodian: The Bank of New York Mellon Corporation, Pittsburgh, PA

U.S. Equity
Adage Capital Management, Boston, MA
BlackRock Institutional Trust Company, San Francisco, CA
Barrow, Hanley, Mewhinney and Strauss, Inc., Dallas, TX
John W. Bristol & Co., Inc., New York, NY
Brown Investment Advisory, Baltimore, MD
Dodge & Cox, San Francisco, CA
PRIMECAP Management Company, Pasadena, CA
Sit Investment Associates, Minneapolis, MN
T. Rowe Price Associates, Inc., Baltimore, MD
Royce & Associates LLC, New York, NY
Wasatch Advisors, Salt Lake City, UT

International Equity
Baillie Gifford, Edinburgh, UK
Capital International, Los Angeles, CA
Franklin Templeton Institutional, Fort Lauderdale, FL
Genesis Investment Management, London, UK
Marathon Asset Management LLP, London, UK
Walter Scott & Partners Limited, Edinburgh, UK
Silchester International Investors Limited, London, UK
Tweedy, Browne Company LLC, New York, NY

Fixed Income
Colchester Global Investors, New York, NY
Dodge & Cox, San Francisco, CA
GMO, Boston, MA
Oaktree Capital Management LP, Los Angeles, CA
Pacific Investment Management Company, Newport Beach, CA
Reams Asset Management Company, Inc., Columbus, IN
Standish, Pittsburgh, PA

Alternative Investments in Private Equity, Distressed Debt, Venture Capital, Natural Resources/Energy, Absolute Return, Real Return and Total Return Strategies
Actis Capital Management, London, UK
AQR Capital Management, LLC, Greenwich, CT
Bridgewater Associates, Inc., Westport, CT
Capital International, Los Angeles, CA
The Carlyle Group, Washington, DC
Cerberus Capital Management LP, New York, NY
Commonfund Capital, Inc., Wilton, CT
Kolberg Kravis Roberts & Company, New York, NY
Lime Rock Resources, Houston, TX
Madison Dearborn Partners LLC, Chicago, IL
Merit Energy Partners, Dallas, TX
Oaktree Capital Management, Los Angeles, CA
Riverstone Holdings LLC, New York, NY
Silver Lake Partners, Menlo Park, CA
Templeton Asset Management Ltd., Fort Lauderdale, FL
Värde Partners, Inc., Minneapolis, MN
Warburg Pincus LLC, New York, NY
Wellington Management Company LLC, Boston, MA
Whippoorwill Associates, Incorporated, White Plains, NY
Wind Point Partners, Chicago, IL
Yorktown Partners LLC, New York, NY

Conclusion

Our identified themes and drivers for 2013 were **War and Politics**, **Pessimism/Optimism** and **In Charge.** Despite significant activities on regional war and political fronts with no one in charge, there was minimal impact on U.S. markets. Sentiment, both pessimism and optimism was important in moving markets as was who was in charge. Markets sensed lack of control and responded accordingly. We look forward to identifying themes for 2014.

Commentary and Outlook for 2014

Wags called the decade that ended December 31, 2009 the “decade of the naughts” due to the decade long negative return from U.S. stocks, with predictions for low single digit returns from U.S. stocks for decades to come. We have been supporters of the U.S. economy and stock market since our 2011 Midyear Investment Review, “We Ain’t Down Yet”, channeling the spirit of the Unsinkable Molly Brown as cheerleaders for the U.S. economy. While emerging market stocks remain the best performing asset class for the last decade, U.S. stocks roared back in 2013, with a ten year compound annual return of 9.7% for small company stocks and 7.7% for the entire U.S. market.

JANUARY 1, 2004 – DECEMBER 31, 2013
Ten Year Compound Annual Investment Returns

Index	Description	Return
MSCI Emerging Markets	Emerging Markets Stocks	11.2%
Russell 2000	U.S. Stocks (Small Companies)	9.1
S&P REIT	Real Estate Stocks	8.4
JPM Emerging Markets Bond	Emerging Markets Debt	8.2
Russell 3000	U.S. Stocks (Large and Small Companies)	7.9
MSCI ACWI ex U.S.	The World Stock Market Index of Developed and Emerging Market Stocks, excluding the U.S.	7.6
MSCI EAFE	Developed Market Stocks in Europe, Australasia and the Far East	6.9
Barclays Government/Credit Bond	U.S. Bonds	4.5
3 Month U.S. Treasury Bill	U.S. Money Market Fund	1.7

We are proud that the Balanced Investment Portfolio had a return of 7.4% for the decade ended December 31, 2013, above the asset mix policy benchmark of 7.1% and above the 7.0% long-term Pension Plan actuarial assumption, and the twenty year return of 8.3%, which exceeds the benchmark return of 7.9% and actuarial assumption of 7.0%.

While investment performance is important, we have several missions, and risk management is an integral part of our stewardship, if not our primary responsibility. It is difficult, if not impossible, to protect the Balanced Investment Portfolio from unexpected global risks that might have a probability of 0.3% or less, but such risks, known as tail risks by statisticians, are very real. Investors should recognize that in an interconnected global economy, we should expect systemic global shocks. We need to be mindful of what could be unusual, high risk events and their potentially devastating impact on investment portfolios. The possible, improbable and “impossible” are with us every day as part of a normal distribution of events. As always, the hard part is to know where we are on the risk curve today and where we could be tomorrow.

While it is true that we are not in charge of much about life, we must think about where we expect markets to be in 2014 and beyond so as to best position the Balanced Investment Portfolio for the benefit of our Plan members.

- Global investors in equity and debt markets will face challenges in 2014. There are few clearly undervalued asset classes as we enter 2014, so once again it should be a year for managers gifted in security selection. We believe we have retained those managers in our relationships we can be proud of.

- We believe international equity will outperform U.S. stocks in 2014. The U.S. economy remains fragile and there has been no resolution or agreement on the direction of the U.S. budget. We have no idea how the January 1, 2014 changes to the health care system will impact public and private employers, whether large or small businesses.

- International developed markets will also face challenges in 2014. The potentially negative impact of new regulations on European banks in 2014 has been deferred, but there will be increased regulatory and market issues in the telecommunications and technology sectors and many governments will continue to grapple with large debt levels. We believe our managers will select the best companies, and we have slightly increased the allocation to developed markets.

- We expect longer duration fixed income assets will continue to be less attractive in 2014 as U.S. short term interest rates remain low but volatile and long term interest rates continue to increase for the next few years. The impact of the end of the Federal Reserve Quantitative Easing is unknown. Spreads on high yield and investment grade corporate bonds have narrowed, reducing opportunities in 2014. Selective investment in distressed debt will continue to provide attractive opportunities.

- Emerging market stocks and bonds should provide superior long-term investment performance. We increased our allocation to emerging market stocks in late 2013 and plan another increase in 2014. We are exploring opportunities in emerging markets debt. Overweighting these opportunities in global growth must be a long-term commitment. We believe investments in emerging markets private equity provide diversification to managers in public market securities.

- While we don't expect inflation will be a problem in 2014, the Investment Committee and staff will continue to evaluate inflation and real return strategies that could help to maintain the purchasing power of the portfolio in periods of inflation.

- We will continue to use short-term market outperformance or volatility in individual asset classes to raise cash to pay benefits. Benefits payments will require cash in excess of dues of more than $280 million in 2014.

- We are long-term investors. We have a long-term strategic asset allocation based on our liabilities, or the future benefits to our Plan members. We will not increase portfolio risk by using short-term trading strategies to improve investment performance.

- We are socially responsible investors and partner with the denomination's Committee on Mission Responsibility Through Investment (MRTI) to assist in the mission of the denomination on issues of corporate governance and social responsibility.

- Our Prohibited Securities Lists includes those companies whose primary businesses are in the military, alcohol, tobacco, and gaming industries. In 1995 the General Assembly approved an expansion of the military divestment list to include those corporations that produce weapons whose use can lead to mass or indiscriminate injury and/or death to civilians. In 1998, the General Assembly refined the guidelines to include chemical and biological weapons and anti-personnel weapons such as landmines, assault-type weapons, rifles, shotguns, handguns and ammunition sold to the civilian market for non-peaceful purposes.

- We will faithfully pursue the goals of our assigned mission, recognizing the needs of those we serve in the Presbyterian Church (U.S.A.).

January 30, 2013

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The **2013 Investment Review** was prepared by the Investment Team of the Board of Pensions of the Presbyterian Church (U.S.A.)

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Notes on 2013 Themes:

War and Politics
William Shakespeare's play **Julius Caesar** was first produced in 1599.
The full quote by Mark Antony in Act 3, Scene 1:
And Caesar's spirit, raging for revenge,
With Ate by his side come hot from hell,
Shall in these confines with a monarch's voice
Cry "Havoc!" and let slip the dogs of war,
That this foul deed shall smell above the earth
With carrion men, groaning for burial.

Pessimism/Optimism
Dietrich Bonhoeffer was a German theologian arrested by the Nazis in 1943 and executed in 1945. His letters and papers were smuggled out of prison before his death.

In Charge
Dr. James Phillips Noble was president of the Board of Annuities and Relief in Atlanta prior to becoming the Co-President of the Board of Pensions of the Presbyterian Church (U.S.A.). Dr. Noble is one of a small number of key people responsible for hiring me in September 1988. I have used his poem to reflect my own feeling of loss of control over stock markets and investments. The poem had a higher purpose. Dr. Noble wrote the poem on July 10, 1968 after the loss of his son to leukemia. Dr. Noble was fully in charge in his participation in the civil rights movement as pastor of Anniston First Presbyterian Church. He has described this era in his book, "Beyond the Burning Bus: The Civil Rights Revolution in a Southern Town". (2011).