

ACTION SUMMARY

INVESTMENT COMMITTEE

November 9, 2017

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MINUTES OF THE
NEW MEXICO EDUCATIONAL RETIREMENT BOARD
INVESTMENT COMMITTEE

November 9, 2017

1. a. CALL TO ORDER

A meeting of the New Mexico Educational Retirement Board Investment Committee was called to order on this date at 1:30 p.m. in the Educational Retirement Board Conference Room, 6201 Uptown Boulevard, N.E., Ste. 203, Albuquerque, New Mexico.

Members Present:

Mr. H. Russell Chairman Goff, Chair
Ms. Mary Lou Cameron
Mr. Larry Magid

Members Excused:

None.

Staff Present:

Ms. Jan Goodwin, Executive Director
Mr. Bob Jacksha, CIO
Ms. Kay Chippeaux, Deputy CIO, Public Markets and Credit
Mr. Mark Canavan, Real Assets Portfolio Manager

Others Present:

Mr. Allan Martin, NEPC
Mr. Sam Austin, NEPC
Mr. Asif Hussain, Caledon
Ms. Noi Spyrtatos, Caledon
Ms. Judith S. Beatty, Recorder

b. Approval of Agenda

Ms. Cameron moved approval of the agenda, as published. Mr. Magid seconded the motion, which passed unanimously by voice vote.

c. Approval of Minutes of 10/19/17

Mr. Magid moved approval of the October 19 minutes, as submitted. Ms. Cameron seconded the motion, which passed unanimously by voice vote.

d. Introduction of Guests

Chairman Goff welcomed staff and guests.

2. NMERB INVESTMENT POLICY REVISIONS

[Presenter: Kay Chippeaux]

Ms. Chippeaux said staff would like to change the benchmark for the new S&P 400 equity being managed internally.

Ms. Chippeaux stated that, while the board is charged with approving changes to the Investment Policy, staff feels it is important for the Investment Committee to review any changes first to be sure there are no questions or objections. Secondly, this affords the committee an opportunity to include its annual review of the Investment Policy while reviewing the requested changes.

Ms. Chippeaux said the major change was changing the benchmark from the Russell 2000 Index, which was the index used by the external manager, to the Russell 2500 Index for small/mid cap. She said the Russell 2500 would better match what internal management is trying to accomplish with the portfolio.

Ms. Chippeaux said NEPC ran some correlations for the NMERB and found that the Russell 2500 was very closely correlated to the S&P 400.

Ms. Chippeaux said the NMERB is trying to capture a little “quality bias” in the S&P 400 versus the Russell 2500. The S&P looks at the past four quarters of performance of each company, while the Russell looks at market capitalization regardless of individual company performance. She commented that there are companies with very high market caps but without positive earnings.

Mr. Martin said NEPC is very comfortable with this recommendation. He said there is a best practices document for investment policies, and the NMERB would check off well against that list in terms of completeness, simplicity, understanding and operability.

Mr. Jacksha added that, when the NMERB did the internal audit, the auditors reviewed the investment policies against best practices and said the NMERB's was fine.

Ms. Cameron moved that the Investment Committee recommend the board approve the changes to the Investment Policy Statement. Mr. Magid seconded the motion, which passed unanimously by voice vote.

Ms. Chippeaux congratulated Alan Myers and Marla Vigil for doing an excellent job in managing the transition and settling all of the trades on the NMERB's side. The trade went very well, and was completed by the end of the month.

3. Q2 INFRASTRUCTURE REPORT

[Presenters: Mark Canavan and Caledon advisors Asif Hussain and Noi Spyratos.]

Mr. Hussain stated that the portfolio is doing well overall; performance is improving, and the earlier vintage funds are starting to divest. Net IRR since inception (2008) is 5.9 percent and continues to rise each quarter.

Ms. Spyratos and Mr. Hussain reviewed the fund commitments that the program has made since 2008.

4. Q2 REAL ESTATE AND NATURAL RESOURCES REPORT

[Presenter: Mark Canavan.]

Mr. Canavan presented highlights:

- As of June 30, 2017, total portfolio value was \$12,333,534,379.
- As of June 30, 2017, NAV of the real estate portfolio was \$925.9 million and NAV for the natural resources portfolio was \$463.5 million.
- Public Real Estate net IRR since inception: 12.58% (time weighted 9.36%).
- Private Real Estate net IRR since inception: 10.75% (time weighted 8.47%).
- Natural Resources net IRR since inception: 6.77% (time weighted 4.55%).

5. ANNUAL MANAGEMENT FEE SUMMARY

Mr. Jacksha reviewed the annual management fee summary.

6. OTHER REPORTS AND DISCUSSION

CEM Benchmarking Report

Mr. Jacksha stated that the CEM Benchmarking Report is for CY 2016, while the annual management fee summary is compiled on a fiscal year basis. This creates a bit of a mismatch.

Ms. Goodwin commented that some items in the CEM report are inaccurate.

Mr. Jacksha reviewed some of the inaccuracies.

-- Mr. Jacksha said he disagreed with CEM's ranking of the NMERB as well above average on asset risk. In the public fund space, the NMERB is probably below average on volatility. CEM only looks at the NMERB's asset allocation and generates the asset risk calculation from that.

-- Mr. Jacksha said the chart showing the NMERB's total investment costs compared to a peer group reflects that the NMERB is one of the highest. There are some reporting issues that are the NMERB's, however, and now that he understands more about the survey, he can correct that for next year.

-- Mr. Jacksha said that, with respect to the benchmark cost analysis, one factor that would need to be adjusted was reporting carry in the wrong column. He did not know what the right number for 2016 would be without redoing all of the numbers, but based on a loose calculation that it is 20 basis points, that would say the NMERB would be over by 19 basis points. The other issue, however, is in how the NMERB categorizes its assets. On page 22 of CEM's report (2016 asset management cost in basis points), there is no category for opportunistic credit, so Mr. Jacksha included it in CEM's private debt category. Mr. Jacksha said he thought it made more sense to have it in the hedge fund category, though, because of a lot of hedge fund structures. Using CEM's formula (page 20) under "using your fund's data," if he moves the opportunistic credit into the hedge fund category and recalculates the formula, it knocks the NMERB's cost down another 39 basis points, putting it below the median for that asset allocation. Mr. Jacksha commented that this is where he feels the NMERB sits given all of the co-investment that it is doing with reduced fees, internal management, etc.

Mr. Martin said he shared Mr. Jacksha's concerns. He commented that he did not know how CEM was able to determine standard deviation given the data they have. NEPC has

observed the NMERB's actual standard deviation through time, and runs the numbers against a universe of other funds, and it comes out to be quite low, so he questions their methodology.

Mr. Martin commented that the fee data is just "bad data." Some funds report carried interest, and some don't, so the data is flawed.

Mr. Jacksha said CEM lists 17 public peers, which includes cities and counties, and they say the median size is \$11.36 million versus the NMERB's \$11.36 million, which is obviously an error.

Quarterly and monthly performance

Mr. Jacksha said the fund was up about .6 percent for the month of September. Returns were 3 percent for the quarter and 11.1 percent for the one-year. These numbers are below the median, as expected in a double-digit year. For the quarter, the fund underperformed the index somewhat.

Mr. Martin commented that the NMERB has a less risky portfolio, so these numbers are not a surprise. The fund continues to do well at a steady pace.

7. NEXT MEETING: THURSDAY, DECEMBER 7, 2017

The next meeting was tentatively scheduled for 12:00 p.m.

ADJOURN

Its business completed, the Investment Committee adjourned the meeting at 2:25 p.m.

Accepted by:



H. Russell Goff, Chairman

