

MINUTES OF THE

NEW MEXICO EDUCATIONAL RETIREMENT BOARD

INVESTMENT COMMITTEE

December 8, 2016

1. a. CALL TO ORDER

A meeting of the New Mexico Educational Retirement Board Investment Committee was called to order on this date at 2:00 p.m. in the Educational Retirement Board Conference Room, 6201 Uptown Boulevard, N.E., Ste. 203, Albuquerque, New Mexico.

Members Present:

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

Members Excused:

None

Staff Present:

Ms. Jan Goodwin, Executive Director
Mr. Bob Jacksha, CIO
Mr. Steve Neel, Deputy CIO, Alternative Investments
Mr. Aaron Armstrong, Portfolio Manager

Others Present:

Mr. Kevin Tatlow, Top Tier
Mr. Allan Martin, NEPC
Mr. Reino Ecklord, NEPC [by telephone]
Ms. Judith 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 11/17/16

The following correction was made to the second paragraph on page 5:

~~“Ms. Cameron~~ Ms. Cameron moved that the Investment Committee approve...”

Mr. Magid moved approval of the November 17 minutes, as amended. Ms. Cameron seconded the motion, which passed unanimously by voice vote.

d. Introduction of Guests

Chairman Goff welcomed staff and consultants.

2. ORCHARD TAIGA FUND – OPPORTUNISTIC CREDIT

[Presenters: Bob Jacksha and NEPC consultant Allan Martin, with NEPC analyst Reino Ecklord on the telephone.]

Mr. Jacksha stated that the NMERB has been a long-term investor with Orchard Global Asset Management, having committed to both its EleganTree and Black Forest funds.

Mr. Jacksha said the NMERB committed \$200 million to EleganTree in 2012, and about \$90 million remains from that commitment. There is a 10.8 percent return on that investment (as of October 16) based on NEPC’s performance report. He said the strategy of that fund was essentially to sell insurance to banks on a slice of their portfolio, and the credits in there have obviously done well.

Mr. Jacksha said the NMERB invested \$150 million in Black Forest in 2014. Currently outstanding is \$108 million in market value, and the NMERB still has remaining monies to commit of \$44 million. Per NEPC’s performance report, the return is 7.6 percent; and on an IRR basis, it is in the low double digits.

Mr. Ecklord provided highlights from NEPC’s report.

-- Taiga Special Situations Fund is a newly designed product offering from Orchard that combines the strategic focus of EleganTree and Black Forest. The fund aims to capitalize on the shift in the global banking environment following the 2008 global

financial crisis and the subsequent regulatory changes that make it more capital intensive for banks to lend and hold loans on their balance sheets.

-- Orchard created EganTree and Black Forest to capitalize on the regulatory pressures newly imposed on banks. The EganTree funds are focused on regulatory capital relief transactions, which were designed to help alleviate current bank balance sheet exposures through risk transfer. Black Forest is focused on new loan origination, partnering with banks to provide companies with access to capital. With Taiga, Orchard will focus on both styles of investments, continuing to aim to be a bank capital solutions provider to banks, but with more flexibility to invest capital where they see the best opportunities.

-- A team of senior investment professionals leads Orchard with extensive experience in the global credit markets, including leading the development of regulatory capital relief transactions. The team's experience and relationships have fostered a network of contacts at banks and financial intermediaries that derives idiosyncratic deal flow in a market that is growing in homogeneity.

-- Orchard has demonstrated a strong track record across its investment strategies. The average deal level IRR is 15 percent for EganTree and 13 percent for Black Forest.

-- As part of its new-issue credit origination strategy, Black Forest, Orchard has primarily partnered with one major European bank as a deal flow resource. With the new fund, however, there is no contractual relationship with this bank.

In reviewing the origin of the loans with Black Forest and any potential currency risk, assuming the dollar continues to strengthen, Mr. Ecklord said the underlying loan pool is rather diverse. What Orchard brings to the table with this type of deal is the ability of their European partner to pass non-domestic deals that would normally be treated more capital intensively if they were to originate these types of deals on their own balance sheet.

Mr. Jacksha clarified that there are 13 loans in the Black Forest portfolio. Eight are in North America, two in Europe, one in South America, and two in Asia. Mr. Martin noted that Black Forest and EganTree are 50-60 percent North America.

Mr. Jacksha stated that staff was originally recommending a \$100 million investment; however, after he and Mr. Martin had a conversation, they decided to

increase it to \$150 million, as it appears that opportunities in other areas of the credit space have recently become more limited.

Mr. Ecklord commented that this is a solid decision given the NMERB's current prior committed level of exposure, which is winding down over time.

Mr. Jacksha said Orchard has engaged a placement agent; however, their contract does not include the investment under discussion because NMERB has an established relationship with Orchard.

Mr. Magid asked Mr. Ecklord to comment on recent stress testing of European banks and how that might affect this investment. Mr. Ecklord responded that this creates more opportunities for these types of deals. The banks are still fairly under their capital requirements, as seen from the stress tests, so they need to do more work to shore up their balance sheets. These types of deals avoid some of the adverse problems that happen when someone is underwater with a deal they did and have to sell at a loss. As an alternative, Orchard can create an insurance package that offsets the exposure and helps manage the credit risk more effectively.

Mr. Martin added that the regulators welcome this opportunity because it allows them more flexibility in being tough on the regulation. Mr. Ecklord concurred.

Ms. Cameron moved that the Investment Committee approve a commitment of \$150 million to Orchard Global Asset Management Taiga Fund for the opportunistic credit portfolio. The commitment is subject to New Mexico State Law, Educational Retirement Board policies, Educational Retirement Board approval for placement agents and negotiation of final terms and conditions, and completion of appropriate paperwork. Mr. Magid seconded the motion, which passed unanimously by voice vote.

3. OTHER REPORTS AND DISCUSSION

Q2 Private Equity Portfolio Report

Mr. Neel and Mr. Tatlow reviewed the June Private Equity Performance Report for Q2 2016 (ending 6/30/16).

-- The NMERB Private Equity Portfolio experienced a Q2 return of 3.7 percent and a one-year return of 7.9 percent. Distributions were at \$109.2 million for the quarter.

- The portfolio has achieved a since-inception return of 12.5 percent and a multiple on invested capital of 1.35x.
- Since inception distributions from the portfolio reached an amount in excess of \$1 billion.
- As of year-end, the portfolio has \$2.57 billion in net commitments to 66 private equity funds managed by 42 different managers.
- The Q2 return was 3.66 percent, with \$69.4 million in distributions.
- The NMERB Private Equity Portfolio is a first or second quartile program, depending on the vintage. It has a 20 percent IRR for the 2015 vintage year and almost 33 percent for 2016.

Recent Buys and Sells

Mr. Jacksha distributed an information sheet on recent buys and sells.

4. NEXT MEETING: THURSDAY, JANUARY 19, 2017

The meeting was scheduled at 1:00 p.m.

ADJOURN

Its business completed, the Investment Committee adjourned the meeting at 2:45 p.m.

Accepted by:



H. Russell Goff, Chairman