



MINUTES

**Meeting of the Investment Committee
of the Board of Trustees of the
State Universities Retirement System
9:00 a.m., Thursday, June 12, 2014
The Northern Trust
50 South LaSalle Street, London Room B9
Chicago, Illinois 60603**

The following Trustees were present: Mr. Craig McCrohon, Chair; Ms. Lindsay Anderson, Ms. Jacqueline Berger, Dr. John Engstrom, Mr. Richard Figueroa, Mr. Paul R. T. Johnson Jr., Mr. Andrew Matthews, Ms. Dorinda Miller, Mr. Peter Newell and Mr. Antonio Vasquez.

Others present: Mr. William Mabe, Executive Director; Mr. Michael Weinstein, General Counsel; Mr. Daniel Allen, Chief Investment Officer; Mr. Douglas Wesley, Deputy Chief Investment Officer; Ms. Kimberly Pollitt and Mr. Joseph Duncan, Senior Investment Officers; Ms. Lou Ann Fillingham, Investment Officer; Ms. Marilyn Branson, Investment Governance and Compliance Officer; Ms. Phyllis Walker, Chief Financial Officer; Mr. Steve Hayward, Director of Internal Audit; Ms. Lori Kern and Ms. Karen Hipskind, Executive Assistants; Ms. Mary Pat Burns of Burke, Burns & Pinelli; Mr. Douglas Moseley, Ms. Kristin Finney-Cooke and Mr. Kevin Leonard of NEPC; Ms. Patti Somerville-Koulouris of the Northern Trust Company; Ms. Leslie Thompson and Ms. Amy Williams of Gabriel Roeder Smith & Company; Mr. Jason Parks of Loop Capital; Mr. Patrick McGarvey of Grosvenor Capital Management.

Investment Committee roll call attendance was taken. Trustee Engstrom, present; Trustee Figueroa, absent; Trustee Johnson, present; Trustee Matthews, present; Trustee McCrohon, present; Trustee Vasquez, absent; Trustee Vogel, absent.

APPROVAL OF MINUTES

Trustee Craig McCrohon presented the Minutes from the Investment Committee meeting of April 24, 2014. Trustee Paul R. T. Johnson Jr. made the following motion:

- That the Minutes from the April 24, 2014 Investment Committee Meeting be approved as presented.

Trustee Andrew Matthews seconded and the motion carried with all Trustees present voting in favor.

Trustee McCrohon also presented the closed session minutes that were scheduled for semi-annual review. Ms. Mary Pat Burns recommended that the closed session minutes be opened since the transaction they referenced has been finalized. Further discussion of the minutes was not requested and Trustee Matthews made the following motions:

- That the closed session minutes from the October 17, 2013, Investment Committee meeting be opened.
- That the closed session minutes from the November 22, 2013, Investment Committee meeting be opened.
- That the closed session minutes from the December 12, 2013, Investment Committee meeting be opened.
- That the closed session minutes from the February 6, 2014, Investment Committee meeting be opened.

Trustee John Engstrom seconded and the motions carried with all Trustees present voting in favor.

Copies of the staff memorandums, entitled “Report from the April 24, 2014 Investment Committee Meeting” and “Investment Contracts Approved,” are incorporated as a part of these Minutes as [Exhibit 1](#) and [Exhibit 2](#).

CHAIRPERSON’S REPORT

Trustee McCrohon provided a short presentation regarding the complexity of the naming conventions associated with private equity and other types of investments as well as the evolution of financial products and the asset allocation structure over time. Trustee McCrohon also discussed the importance of timeline considerations given the differing requirements for implementation of various asset classes.

Trustee Antonio Vasquez joined the meeting at the beginning of the presentation at 9:08 a.m.

CHIEF INVESTMENT OFFICER REPORT

Mr. Daniel Allen reported that an investment return of 14.0% was achieved for the fiscal year to date as of April 30, 2014, and 17.0% for the calendar year 2013. Mr. Allen also remarked that total assets have increased to \$17 billion currently, state funding has been more consistent the past few years and the plan funded ratio is estimated at approximately 47%.

DISCUSSION OF INVESTMENT PORTFOLIO TRANSITION, REBALANCING AND CASH OVERLAY STRATEGIES

Trustee Johnson remarked that the use of options for rebalancing was discussed at the February meeting and subsequent inquiry of the cash overlay manager candidates indicated

that the strategy would be a separate endeavor. Trustee Johnson observed the success that the North Carolina Retirement Systems has had with utilizing options and he remarked on the benefits that could be captured.

The following representatives of Gladius Capital Management (Gladius) were invited to the meeting to discuss their firm's strategy for plan rebalancing utilizing options:

- Mr. Pav Sethi
- Mr. Ragu Raghavan
- Mr. Eric Magac

During the discussion of the strategy that followed, Mr. Douglas Moseley reviewed the plan's current need to move money and the practices presently employed. Mr. Douglas Wesley noted that rebalancing due to market moves has been rare since the dynamic nature of the portfolio generates cash flows that offer opportunities to rebalance. Various aspects of the strategy presented by Gladius were discussed, including possible similarities with hedged equity strategies and potential crossover with the cash overlay strategy for which Parametric Clifton was recently hired. Mr. Moseley remarked that several projects are already on the work plan and he advised that further analysis by NEPC and SURS staff of the mechanics and intricacies of the options strategy is recommended. Mr. Allen concurred and suggested the cash overlay manager be put in position before making a decision on the options strategy.

Trustee Richard Figueroa joined the meeting at this juncture at 10:25 a.m.

Trustee Johnson recommended approval of issuing a request for proposal (RFP) for rebalancing services at some future point so that the topic could be added to the work plan. As discussion continued, varying degrees of favor were expressed and as a result, Trustee Johnson suggested postponing any action until the September meeting. Mr. Moseley remarked that NEPC does not oppose the strategy but further analysis regarding the mechanics, the proper way to issue the RFP and the work plan for the coming year is needed. After additional discussion concerning perceived risks, Trustee Lindsay Anderson made the observation that the consensus of the Board is to continue discussion of the issue at the September meeting in order to allow for a well informed decision.

Copies of the Gladius Capital Management presentations, "Mechanics of Plan Rebalancing Utilizing Options" and "Portfolio Rebalancing Utilizing Options," as well as the NEPC report that was distributed, "Overview of Transition Management," are incorporated as a part of these Minutes as [Exhibit 3](#), [Exhibit 4](#) and [Exhibit 5](#).

REVIEW AND CONSIDERATION OF ASSET/LIABILITY STUDY OUTPUTS

Mr. Allen remarked that the discussion at the April meeting regarding the Asset/Liability study indicated a consensus for further education on hedged equity strategies. Mr. Moseley discussed the nature and characteristics of hedged equity strategies, the potential to reduce the volatility risk of the portfolio and performance compared to other asset classes in detail. The session also examined the results of the liquidity study that tested how different asset

allocation mixes would impact plan liquidity given various scenarios for projected cash inflows. Mr. Moseley observed the equity risk present in the portfolio and advised that NEPC and staff recommend approval of the Mix B allocation targets, which would further reduce total equity to 50%, introduce 5% to hedged equity and maintain the 3% allocation to emerging markets debt and 2% to commodities approved at the April meeting. During the discussion, consideration was given to the risk profile of hedge funds in general, the best structure for a hedge fund portfolio and the opportunity for utilization of emerging managers. The subject of investment management fees and the actions of other public funds with respect to the hedged equity asset class were also discussed.

Trustee McCrohon made the following motion:

- That the strategic policy allocation targets set forth below as Mix B be approved as presented, giving staff the discretion to gradually implement those policy targets in coordination with the actual transition of assets.

Newly Approved				
Asset Class	Target	New Mix A	New Mix B	New Mix C
U.S. Equity	26%	25%	23%	22%
Non-U.S. Equity	21	19	19	18
Global Equities	8	8	8	8
Total Equity	55%	52%	50%	48%
Core Fixed Income	19	19	19	19
Emerging Markets Debt	3	3	3	5
TIPS	4	4	4	4
Total Fixed Income	26%	26%	26%	28%
Private Equity	6	6	6	6
Real Estate	6	6	6	6
REITS	4	4	4	4
Hedged Equity	0	3	5	5
Opportunity Fund	1	1	1	1
Total Alternatives	17%	20%	22%	22%
Commodities	2	2	2	2
Total Other	2%	2%	2%	2%
Grand Total	100%	100%	100%	100%

After further discussion of Mix B and Mix C, Trustee Matthews seconded the motion and the motion carried with all Trustees present voting in favor.

Copies of the staff memorandums, “Continuation of the Asset / Liability Study Discussion” and “Status Update of the Asset / Liability Study,” and the NEPC presentation, “Asset Liability & Liquidity Study,” are incorporated as a part of these Minutes as [Exhibit 6](#), [Exhibit 7](#) and [Exhibit 8](#).

REVIEW OF SURS INVESTMENT PERFORMANCE AND RISK MANAGEMENT REPORTS

Mr. Kevin Leonard discussed the portfolio's investment performance as of March 31, 2014. An investment return of 2.0% was achieved for the first quarter of calendar year 2014, total assets were approximately \$16.7 billion and the one-, three- and five-year annualized returns were 13.5%, 9.4% and 15.8% respectively. The returns that Mr. Leonard referenced were quoted on a gross of fees basis. As of the end of the quarter, equities were slightly over allocated due to strong market returns and fixed income was slightly under allocated. Mr. Leonard remarked on the portfolio's strong performance over the last ten years relative to the large public fund peer group, noting that NEPC is seeking to reduce the slightly higher volatility of the portfolio.

Mr. Joseph Duncan presented the key findings from the Executive Summary of the SURS Risk Report for the quarter ended March 31, 2014. Total plan risk declined to 11.2% from 11.59% for the previous quarter, indicating that over the next one-year period, the return of the portfolio is expected to be between +11.2% and -11.2% based on a normal distribution of outcomes and a one standard deviation confidence level (68% of the time). Mr. Duncan noted that equity exposure is responsible for the majority of total plan risk, which is expected to be moderated by the new asset allocation targets. Mr. Duncan also discussed fixed income contributors to total plan risk and the significance of key rate durations.

Copies of the staff memorandum, "Executive Summary Risk Report," and the Northern Trust Risk Services report, "SURS Executive Risk Review 1Q2014," are incorporated as a part of these Minutes as [Exhibit 9](#) and [Exhibit 10](#).

DEVELOPMENT OF THE FISCAL YEAR 2015 INVESTMENT PLAN

Mr. Allen discussed the preliminary outline for the 2015 Investment Plan that will be developed over the summer for presentation at the September meeting and encouraged the trustees to provide their input. Mr. Allen advised that the search process for emerging markets debt strategies has commenced and he remarked on other upcoming projects. Mr. Allen also noted the Fiscal Years 2014-15 Summary Work Plan document and the plan to routinely provide trustee education at future meetings.

Copies of the staff memorandum, "Introduction of the Fiscal Year 2015 Investment Plan," and the document entitled "Possible Board Annual Education Calendar / Self Development" are incorporated as a part of these Minutes as [Exhibit 11](#) and [Exhibit 12](#).

APPROVAL OF THE MULTI-YEAR PRIVATE EQUITY FUNDING PLAN

Mr. Wesley remarked on the private equity investment cycle, noting that capital is called over time, distributions flow back and investments wrap up, necessitating continual recommitment to the asset class.

Ms. Kristin Finney-Cooke provided a review of the private equity program and the funding plan, which provides a framework for continuing to invest in the asset class in a consistent and systematic manner. Ms. Finney-Cooke remarked that commitments must keep pace with the growth of the total plan in order to maintain the private equity target allocation and she noted that \$150 million remains from the 2012 funding plan that extends through 2014. The fund of funds structure, the various sub-strategies and the use of secondary private equity investments to add vintage year and sub-strategy diversification were also reviewed. After further discussion of the proposed pacing model, Ms. Finney-Cooke presented the new three year funding plan, which points to commitment of \$250 million in 2015, \$300 million in 2016 and \$300 million in 2017, and she noted that the plan will continue to be evaluated on an annual basis.

After the ensuing discussion, Mr. Wesley noted that the historical practice has been a three year private equity funding plan and he advised that staff and NEPC recommend approval of the \$850 million plan for the 2015 to 2017 period.

Trustee Johnson moved:

- That a multi-year Private Equity Funding Plan be approved for calendar years 2015, 2016 and 2017 at a level of \$250 million, \$300 million and \$300 million, respectively. In addition, any uncommitted amounts from a preceding calendar year may be included in the following years through 2017.

Trustee McCrohon seconded and the motion carried with all Trustees present voting in favor.

Copies of the NEPC report, "Private Equity Program Review & 2014 Strategic Investment Plan," and the staff memorandum, "Private Equity Funding Plan for Calendar Years 2015 – 2017," are incorporated as a part of these Minutes as [Exhibit 13](#) and [Exhibit 14](#).

PRIVATE EQUITY AND OPPORTUNITY FUND ASSET CLASSES **ANNUAL REVIEWS – CONSENT AGENDA**

Mr. Wesley reviewed the Private Equity asset class, remarking that distributions from private equity amounted to \$260 million while contributions amounted to \$91 million during calendar year 2013. Over the last four years, distributions of over \$100 million per year have been received due to continuous commitment and strong absolute returns. Since inception, approximately \$2.6 billion has been committed, slightly over \$2 billion contributed, \$2.4 billion distributed and the remaining market value of the private equity portfolio is over \$1 billion.

Mr. Wesley also reviewed the Opportunity Fund asset class, noting that the PPIP fund investments have been fully liquidated over the last year. With respect to infrastructure, Mr. Wesley advised that Macquarie Infrastructure Partners III, L.P. has just closed and he discussed the characteristic differences between core and value-added infrastructure investments.

Copies of the staff memorandums, “Executive Summary of the Private Equity Asset Class” and “Executive Summary of Opportunity Fund,” are incorporated as a part of these Minutes as [Exhibit 15](#) and [Exhibit 16](#).

APPROVAL OF THE SCRUTINIZED COMPANIES LIST
AS DEFINED BY IRAN LEGISLATION

Ms. Marilyn Branson provided a report on compliance with the requirements of Public Act 95-616, which prohibits investment in companies involved in Iran’s petroleum-energy sector. After reviewing changes to the Iran Scrutinized Companies list during fiscal year 2014 and noting the communications undertaken with companies and investment managers, Ms. Branson advised that divestment was not required this fiscal year since the amount invested in scrutinized companies amounted to less than 0.5% of the \$16.79 billion total fund as of April 30, 2014. Ms. Branson remarked that the legislation requires the list to be updated annually and therefore staff recommends the adoption of the Iran Scrutinized Companies list updated as of June 1, 2014.

Trustee Johnson moved:

- That the Board adopt the Iran Scrutinized Companies list updated as of June 1, 2014, as presented.

Trustee Vasquez seconded and the motion carried with all Trustees present voting in favor.

A copy of the staff memorandum, “Iran Legislation Compliance,” is incorporated as a part of these Minutes as [Exhibit 17](#).

REVIEW OF THE FISCAL YEAR 2015 INVESTMENT DEPARTMENT BUDGET

Ms. Lou Ann Fillingham presented the Investment Department Operations Budget for fiscal year 2015, noting that personnel costs have been transferred out of the investment department budget and included in the total personnel budget. The proposed administrative expenses budget for fiscal year 2015 is approximately \$2.3 million, which is an increase of 1.2% from the fiscal year 2014 budget when personnel costs are excluded. Investment management expenses are budgeted at \$53 million, which is 16% above the fiscal year 2014 budget due to increased investment in alternative asset classes. Ms. Fillingham noted that SURS continues to monitor and negotiate lower fee structures and investment fees calculated as a percentage of assets compare favorably to other Illinois public funds and the median public fund.

Trustee McCrohon moved:

- That the Investment Department Administrative Expense Budget for Fiscal Year 2015, excluding personnel costs, be approved as presented.

Trustee Figueroa seconded and the motion carried with all Trustees present voting in favor.

A copy of the staff memorandum, "Investment Operations Budget – Fiscal Year 2015," is incorporated as a part of these Minutes as [Exhibit 18](#).

ANNUAL CONSULTANT EVALUATION OF SURS MANAGER DIVERSITY PROGRAM

Ms. Finney-Cooke presented the annual review of the Manager Diversity Program (MDP), which is focused on investment opportunities with minority-, women- and persons with a disability-owned investment managers (MFDB). As of March 31, 2014, seventeen firms participate in the MDP via direct relationships that manage approximately \$1.7 billion in assets or 10.4% of SURS' total fund. One MDP manager was terminated during the year; however, the assets were distributed among the MDP fixed income managers and remain in the program. In addition, one new MDP manager was hired to manage a private equity emerging manager fund of funds structure. Ms. Finney-Cooke also discussed techniques utilized for MDP manager outreach and searches and she reviewed the manager oversight and evaluation processes.

Discussion of the MDP followed, which centered on approaches for maximum discovery of qualified MFDB investment managers as well as for potential ways to mentor and nurture rising talent. Ms. Burns noted that the Illinois legislature recently passed a new bill that may become law which will require disclosure of diversity statistics regarding the personnel and suppliers of majority-owned firms before the retirement system can enter into a contract with such firms. Issues concerning non-selection were also briefly discussed and Trustee Figueroa remarked the importance of understanding the reasons why managers are not selected by the MDP manager of managers program providers.

A copy of the NEPC memorandum, "Annual Manager Diversity Program Review," is incorporated as a part of these Minutes as [Exhibit 19](#).

PRESENTATION OF THE SURS INVESTMENT MANAGER WATCH LIST

Ms. Kimberly Pollitt presented the June 2014 Investment Manager Watch List which reflects investment performance for the period ending March 31, 2014. Three managers are currently on watch, Calamos Advisors due to performance and personnel issues, Herndon Capital Management due to performance and PIMCO due to senior management changes. Ms. Pollitt noted that watch status indicates a heightened level of monitoring and staff will keep the trustees informed of any changes.

A copy of the staff memorandum, "June 2014 Investment Manager Watch List," is incorporated as a part of these Minutes as [Exhibit 20](#).

INFORMATIONAL ITEMS NOT REQUIRING COMMITTEE ACTION

Mr. Allen noted that Internal Audit recently completed an Investment Compliance Review, which found Investment department procedures to be compliant with state statute.

The Resolution of the Investment Committee which pertains to the motions approved at this meeting is presented in Appendix A.

The following items were provided for reference and are incorporated as a part of these Minutes:

1. [Exhibit 21](#) - SURS Projected Funding Status through April 2014.
2. [Exhibit 22](#) - Staff memorandum entitled "Compliance Update."
3. [Exhibit 23](#) - Investment Compliance Activities 2014.
4. [Exhibit 24](#) - Fiscal Years 2014-15 Summary Work Plan Investment Committee Schedule.
5. [Exhibit 25](#) - Schedule of Formal Reviews for SURS Investment Managers: Defined Benefit Plan & SMP.
6. [Exhibit 26](#) - Staff memorandum "Schedule of Investment Committee Meetings."

PUBLIC COMMENT

There were no public comments presented to the Investment Committee.

Since there was no further business before the Committee, Trustee Vasquez moved that the meeting be adjourned. The motion was seconded by Trustee Figueroa and carried with all Trustees present voting in favor.

Respectfully submitted,



Mr. William E. Mabe
Secretary, Board of Trustees

WEM:mb

RESOLUTION OF THE INVESTMENT COMMITTEE
STATE UNIVERSITIES RETIREMENT SYSTEM OF ILLINOIS
Adopted June 12, 2014

RECITALS:

1. The SURS Investment Policy, dated September 13, 2013 (the “Investment Policy”), Section VIII(D) (Investment Manager and Fund Monitoring), permits the Staff or Consultant to present managers to the Board for termination by the Board. The Investment Policy provides that the Staff may recommend “changes in funding for an investment manager, outside the rebalancing process.”
2. Pursuant to its practices and procedures, Staff has reviewed the performance of each of its Private Equity Separate Account managers, as identified in Schedule 1 to this Resolution (the “Private Equity Separate Account Managers”), as of the end of the first quarter of 2014.
3. Staff has reviewed the performance of the equity mandates and risk measures relative to performance benchmarks as deemed appropriate by the Staff. The Staff has further reviewed the turnover of key management of each of the Private Equity Separate Account Managers, changes in the total assets under management, and other factors identified in Sections VIII(D) and X (Investment Manager Termination Guidelines) of the Investment Policy. Selected information regarding such review has been presented to the Board for review and discussion. It is Staff’s assessment that the Private Equity Separate Account Managers are in compliance with their respective contractual agreements with SURS.
4. Capitalized terms used, but not defined, in this Resolution shall have the meanings given in the Investment Policy.
5. Based on the recommendation of Staff and Investment Consultant, the Investment Committee of SURS recommends the strategic policy allocation targets be approved as presented by the Board, giving staff the discretion to gradually implement those policy targets in coordination with the actual transition of assets.
6. Based on the recommendation of Staff and Investment Consultant, the Investment Committee of SURS recommends that the Board approve the Private Equity Funding Plan for calendar years 2015, 2016 and 2017 at a level of \$250 million, \$300 million and \$300 million, respectively. In addition, any uncommitted amounts from a preceding calendar year may be included in the following years through 2017.
7. The Investment Committee of SURS recommends that the Board adopt the Iran Scrutinized list updated as of June 1, 2014, as presented.
8. The Investment Committee of SURS recommends that the Board approve the Investment Department Administrative Expense Budget Fiscal Year 2015, excluding personnel costs, as presented.
9. The Investment Committee of SURS recommends that the Board accept the Investment Department Investment Management Fees for the Fiscal Year 2015 as presented.

RESOLUTIONS:

Now, therefore, be it resolved as follows:

The Investment Committee of SURS recommends that the Board approve the strategic policy allocation targets be approved as presented, giving staff the discretion to gradually implement those policy targets in coordination with the actual transition of assets.

The Investment Committee of SURS recommends that the Board approve the Private Equity Funding Plan for calendar years 2015, 2016 and 2017 at a level of \$250 million, \$300 million and \$300 million, respectively, allowing any uncommitted amounts from a preceding calendar year to be included in the following years through 2017.

The Investment Committee of SURS recommends that the Board adopt the Iran Scrutinized list updated as of June 1, 2014, as presented.

The Investment Committee of SURS recommends that the Board approve the Investment Department Administrative Expense Budget Fiscal Year 2015, excluding personnel costs, as presented.

SCHEDULE 1:
PRIVATE EQUITY SEPARATE ACCOUNT MANAGERS

Pantheon Ventures

Adams Street Partners