South Carolina Retirement System Investment Commission
Meeting Minutes

June 14 -15, 2018 9:30 a.m.
Capitol Center
1201 Main Street, 15th Floor
Columbia, South Carolina 29201
Meeting Location: Presentation Center

Commissioners Present:
Dr. Rebecca Gunnlaugsson, Chair
Dr. Ronald Wilder, Vice Chair
Ms. Peggy Boykin, PEBA Executive Director (Absent)
Mr. Allen Gillespie
Mr. Edward Giobbe
Mr. Reynolds Williams
Mr. William H. Hancock
Mr. William J. Condon, Jr.

I. CALL TO ORDER AND CONSENT AGENDA

Chair Rebecca Gunnlaugsson called the meeting of the South Carolina Retirement System Investment Commission ("Commission") to order at 9:31 a.m. Dr. Ronald Wilder made a motion to approve the proposed agenda as presented. Mr. Bill Condon seconded the motion, which was approved unanimously.

The Chair asked whether there was a motion to approve the draft minutes from the Commission's April 12, 2018 and May 17, 2018 meetings as presented. Mr. Condon made a motion to approve the minutes as presented. Dr. Wilder seconded the motion, which passed unanimously.

II. CHAIR'S REPORT

The Chair began by noting that the nomination period had expired for the Commission's Retiree Representative Member ("Retiree Representative") and that no additional nominations had been received since the Commission nominated Dr. Ronald Wilder for a second term as the Retiree Representative during the April Commission meeting. Dr. Wilder asked to be excused before the vote for any discussion by the Commission members of his nomination. The Chair asked if there was a pending motion to elect Dr. Wilder as the Retiree Representative. Mr. Condon made the motion after clarifying that there was a quorum present. The Chair noted that there was a quorum with four voting members present. The Commission unanimously approved Dr. Wilder as the Retiree Representative.

The next order of business was the election of the Chair and Vice Chair for the new term commencing July 1, 2018. The Chair explained that currently there was a pending motion to elect Dr. Wilder to serve as the Chair and herself to serve as the Vice Chair. She also clarified that the term is for two years, ending June 30, 2020. The Chair called for a vote on the motion for Dr. Ronald Wilder to serve as Chair and Dr. Rebecca Gunnlaugsson to serve as Vice Chair, which was unanimously passed. Dr. Wilder thanked the Chair for her leadership over the past two years and stated that he was looking forward to the Commissioners serving together to do the best for the beneficiaries of the fund.

Mr. Allen Gillespie and Mr. Edward Giobbe joined the meeting at 9:35 a.m.

III. AUDIT & ENTERPRISE RISK MANAGEMENT COMMITTEE REPORT

The Chair recognized Mr. Allen Gillespie for the Audit and Enterprise Risk Management Committee Report. Mr. Gillespie began by stating the Committee met on June 7, 2018. The Committee received an update on a variety of routine compliance matters. He noted that there were no exceptions to report.

Mr. Gillespie then discussed internal audit updates including the agreed upon procedures completed by the State Auditor's office. The report had been completed on the areas of cash receipts, disbursements on payroll and non-payroll and had no findings.

He announced that a GIPS compliance vendor was selected, which was ACA, and he added that ACA had already begun work on the GIPS compliance verification process.
Mr. Gillespie noted that that the Committee received an update on the fiduciary performance review which is required by law and is now underway with Funston Advisory Services ("Funston") performing the review. He stated that Funston will be performing in-person interviews during the month of June, beginning Monday.

Lastly, Mr. Gillespie stated that the Committee received an ERM update including an update on the ERM framework and developmental process.

Mr. Condon inquired as to when Funston would be interviewing the Commissioners. Mr. Brad Gainey, Director of Audit and Enterprise Risk Management, stated that Funston would be onsite in the coming week to interview RSIC Staff. He explained that Funston provided agendas and topics that they would like to cover for each individual person, in advance of the scheduled interviews. He stated that the Commissioner interviews are the next phase and he expects that Funston will also provide topics for those interviews.

IV. CEO's REPORT

The Chair recognized Mr. Hitchcock for the CEO's Report. Mr. Hitchcock, on behalf of the Staff, thanked the Chair for her service over the past two years, which had helped the organization progress substantially during that time. Mr. Hitchcock also expressed his gratitude on behalf of the organization to the Commission for their hard work over the last two years, especially Vice Chair Dr. Wilder.

Mr. Hitchcock then turned the discussion to an overview of both the Statement of Investment Objectives and Policies (“SIOP”) and the Annual Investment Plan (“AIP”). He explained that he and Staff had been exploring ways to re-structure both documents to make them more functional as well as to make them more strategic, both long-term as to the SIOP, and shorter-term at to the AIP, and that he wanted to get a consensus from the Commission if they agree with this direction.

The senior leadership on Staff plans to work with the Commissioners and Dr. Wilder to develop changes to the structure and content of the SIOP by the September Commission meeting. By way of background, Mr. Hitchcock reminded the Commission that state law requires that the Commission adopt both an SIOP and an AIP. State law also requires the Commission to provide the CIO and CEO with annual investment objectives. The AIP is required by state law to be adopted by May 1 of each year for the following fiscal year and the Commission is also required to reaffirm or adopt a new SIOP on at least an annual basis.

He suggested that the Commission shift to a more pro-active approach with these documents and have them reflect the strategic vision of the Commission, both on a long- and short-term basis. Mr. Hitchcock stated that the SIOP’s principal role should be to house the state-mandated content, as well as long-term strategic and policy matters relevant to the Commission’s long-term asset allocation. As for the AIP, Mr. Hitchcock noted that there is some state mandated content that is required to be included. He suggested that the AIP should also focus on the annual investment team initiatives, as well as a method of tracking their progress, as suggested previously by Mr. Condon.

Mr. Hitchcock suggested that going forward, the Commission would review and approve the SIOP each fall, as well as review organizational strategic planning. The Commission would then provide the CIO and CEO with guidance on investment objectives at the November/December meeting, which they would then use to guide the development of the key initiatives in the AIP, which would be discussed in draft form by the February meeting and adopted before the May 1 statutory deadline. The cycle would then start over in June when the Staff would begin reviewing the SIOP in preparation for the following September meeting. Mr. Condon made several suggestions, including a suggestion to lessen the technical jargon used in the documents to make them more readable.

Next, Mr. Hitchcock discussed the proposed Communication Plan. By way of background he reminded the Commission that Funston had recommended the adoption of a communications policy in their initial report.

The proposed Communication Plan is a proactive policy, which promote confidences that the RSIC is a world class investment organization which performs solely in the best interests of the beneficiaries' financial future. Mr. Hitchcock stated that he had discussed the Communication Plan with the Chair and Dr. Wilder and incorporated their suggestions in making it more general and placing the majority of the responsibility of carrying out the communication plan on the external relations team as well as himself. He then summarized the key points of the proposed Policy. Mr. Wilder stated that he was pleased to see a list of key initiatives in the Policy. Mr. Hitchcock responded by stating the he wants the RSIC to be prepared and to be a ready resource for the General Assembly as they look at pension reform. He also stated that it is important that the Commission educate the public on what we do, how we do it, and why we do it and to make it as jargon free as possible to make it more understandable to the general public.

The Chair requested a motion to approve the Communication Plan. Mr. William Hancock moved that the Commission approve the Communication Plan as presented and authorize Staff to finalize the Plan by making any technical revisions or formatting edits consistent with the action taken by the Commission. Dr. Wilder seconded the motion, which passed unanimously.

V. CIO'S REPORT

The Chair recognized Mr. Geoff Berg for the CIO's report. Mr. Berg began his presentation by thanking the Chair for her service, support, valuable perspective, and her generosity with her time over the past two years. He then introduced Mr. David King, Senior Reporting Officer, to present the Investment Performance Report for the fiscal year through April 30, 2018.

Mr. King started by stating that through April 30, 2018, the Plan returned 8.01 percent versus the policy benchmark of 7.29 percent. He noted that fiscal year to date ("FYTD"), the Plan paid out $933 million in net benefits and, through investment performance, increased the value of the Plan approximately $1.5 billion, to bring the Plan's value to $31.57 billion as of April 30, 2018.

Mr. King turned next to the Plan's portfolio exposures, noting that the Commission had adopted new ranges at its April meeting in order to transition into the previously adopted asset allocation. Mr. King indicated that all asset classes were within the required ranges. He reviewed the Plan's market value through time, noting that the Plan's April 30, 2018 ending market value of $31.57 billion was near its highest level since inception. Since inception, the Plan has paid out $12.2 billion in net benefit payments to retirees.

Mr. King then reviewed asset class performance, noting that most of the asset classes had positive FYTD returns, with the exception of core fixed income, REITs, and infrastructure. He noted that private equity was the highest performing asset class on an absolute basis, even though it is still significantly underperforming its benchmark, due in part to the lagged benchmark. Mr. King explained that most private equity managers value their assets on a quarterly basis. Because many of the valuations have not been received, it can inflate the underperformance in periods of strong public equity market performance. After additional discussion regarding lagging benchmarks and the performance of the private equity asset class compared to its benchmark, Mr. King noted that although private equity was the highest performing asset class on an absolute basis, the portable alpha hedge funds were the highest performing class on a relative basis. After some discussion regarding the anticipated payments to retirees as part of the wind down of the TERI program, Mr. King concluded his performance report.

VI. CONSULTANT REPORT

Mr. Berg introduced Mr. Frank Benham, Managing Principal and Director of Research for Meketa Investment Group ("Meketa") to provide a presentation on asset allocation and to provide follow up discussion on items from previous meetings. Mr. Benham handed the presentation over to Mr. Aaron Lally, Executive Vice President for Meketa. Mr. Lally first stated that there were two items from the Commission's April meeting for which additional clarification was needed. The first item relates to Treasury Inflation Protected Securities ("TIPS"), this asset class is new for the Commission, and a benchmark was not addressed at the time the allocation to TIPS had been approved. He recommended that the Commission adopt the Bloomberg Barclays US Treasury Inflation Notes Total Return Index Unhedged USD ("Barclays TIPS Index") as the benchmark for TIPS.

The second matter that required additional clarification relates to equity options and the new asset allocation of an increase in the target allocation from five to seven percent. Mr. Lally noted that the Commission had not formally addressed that the range should be increased accordingly. Therefore, he recommended that a range of five to nine percent be placed around the seven percent target.

Dr. Wilder asked about the background of the option-based equity strategies and whether the historical risk of those investments had been different from the risk in public equity. Mr. Lally replied that historically the risk was not much different, but perhaps slightly lower.

The Chair inquired if there were any additional questions. With no additional questions, she noted that there was a motion that needed to be addressed. Dr. Wilder moved that the Commission adopts the recommendation of Meketa to approve the asset allocation ranges and benchmarks revisions recommended by Meketa as set forth on red numbered page(s) 49 of the open session agenda materials as presented, with the ranges to be effective July 1, 2018; directs that the approved asset allocation and ranges be incorporated into, and made a part of, the SIOP; and authorizes Staff to finalize the benchmark and asset allocation ranges by making any technical revisions or formatting edits consistent with the action taken by the Commission. Mr. Giobbe seconded the motion, which was passed unanimously.

VII. INVESTMENT RECOMMENDATION

Mr. Berg offered introductory comments regarding Macquarie Super Core Infrastructure Fund ("Macquarie Super Core" or the "Fund"), the private infrastructure investment that was being presented to the Commission. He explained that the Macquarie Super Core investment is designed to provide predictable cash flow and went on to highlight some of the other reasons he believed Macquarie Super Core was an attractive investment. Mr. Berg noted that the Investment Team is attempting to identify investments that can achieve the assumed rate of return while simultaneously narrowing the range of outcomes for the Plan's rate of return. The Fund is expected to fit this profile, as its expected return was likely to meet or exceed the Plan's actuarial assumed rate of return. In addition, Mr. Berg noted to the Commission that the Fund has an anticipated life span of at least 20 years, which, while much longer than most other investments that the Commission considers, is appropriate given both the long-term nature of infrastructure assets as well as the long-term nature of the plan's liabilities. Mr. Berg then recognized Ms. Ashli Aslin, Investment Officer, for a presentation regarding the Macquarie Super Core fund.

Ms. Aslin began by explaining that Macquarie Super Core is the first private infrastructure investment that the Commission has considered. She then provided a summary of the infrastructure asset class, the role it plays in the Plan's portfolio, and the benefits of owning regulated assets. She explained that Macquarie Super Core will invest in regulated utilities, an area that includes water, sewage, electricity, heating, and gas distribution businesses. Mr. Condon asked about the geography of the investment, and Ms. Aslin replied that the Fund's initial set of investments would be in European regulated utilities.

Ms. Aslin then provided an overview of the investment strategy. She explained that the type of assets the Fund will hold have a high initial cost, and they operate in a monopolistic environment, affording them long-term, stable and predictable cash flows.

Ms. Aslin stated that Staff's recommendation to the Commission was to invest up to €125 million into the Fund. She explained that the Fund would make investments with a net-of-fee return expectation of 7-8%, with 5% of that return coming from distributed yield. She noted that the management fee was 50 basis points on uninvested capital and no greater than 65 basis points on the Fund's net asset value and explained that the Fund will also charge a performance fee of 20% on distributed yield over a 4% hurdle after all other fees and expenses. The term of the fund is 20 years with two two-year extensions, and investors may elect to extend the Fund's term beyond the 20-year term in five-year increments.

The Commissioners asked a variety of questions about the strategy. Mr. Condon asked if Staff is expecting 5% annual distributions from the Fund. Ms. Aslin replied in the affirmative. Mr. Giobbe inquired about the 20% performance fee over the hurdle and asked whether the performance fee is higher than most private equity investments. Ms. Aslin clarified that the performance fee is not 20% of all the performance; the performance fee will be 20% of the yield after the first 4%.

Mr. Reynolds Williams asked if and how the strategy is protected against inflation. Ms. Aslin explained that as inflation increases, there is a mechanism for these utilities to obtain rate increases, which acts as a hedge against inflation. Mr. Hancock asked if there was any research concerning the gap between what a European regulator deems an appropriate cost and what a utility manager deems an appropriate cost. Ms. Aslin replied that regulators understand the importance of allowing an appropriate rate of return, in order to ensure that essential services are adequately provided. Mr. Berg added that the manager has a long history of navigating regulatory processes to ensure that its investors earn an appropriate rate of return. Next, Mr. Condon asked what the Fund actually owns. Mr. Berg clarified that the Fund owns companies that operate and maintain the infrastructure assets. Additional discussion ensued regarding the proposed investment.

Mr. Williams then moved that the Commission: (a) adopt the recommendation of the CIO and the Internal Investment Committee as set forth in the Summary Terms Chart on pages 1 and 2 of the Due Diligence Report dated June 14, 2018; (b) authorize an investment of up to €125 million as of the date of closing; (c) authorize the CEO or his designee to negotiate and execute any necessary documents to implement the Investment as approved by the Commission (1) upon documented approval for legal sufficiency by RSIC Legal, and (2) upon expiration of the three business day review period as approved by the Commission on May 1, 2014 (or as the review period may be amended or superseded by the Commission); and (d) authorize the CEO and/or the CIO or their designee(s) to thereafter authorize the custodian of funds to transfer such funds as are necessary to meet the Retirement System trust funds' obligations with respect to the Investment. Dr. Wilder seconded the motion, which passed, with Mr. Hancock opposing the motion.

A brief break was taken from 10:57 a.m. to 11:14 a.m.

VIII. DELEGATED INVESTMENT REPORT

The Chair recognized Mr. Berg for the delegated investment report. Mr. Berg noted Staff closed two new private equity investments since the previous meeting. Mr. Berg then introduced Mr. Joshua Greene, Investment Officer, to give a brief summary of the Plan's investment in Industry Ventures Partnership Holdings V ("Industry Ventures"). Mr. Greene began by stating that the Plan made a $50 million commitment to Industry Ventures, a venture capital fund, and that the investment closed on June 1, 2018. He explained that Industry Ventures has an experienced team that focuses on broad venture networks. Industry Ventures accesses venture capital markets through three avenues. The first avenue is Industry Ventures' primary fund, which invests through a fundraising process. The second avenue is purchasing interests in other funds from exiting limited partners. Industry Ventures typically buys these interests at a discount and utilizes the information garnered from these funds to make more informed investment decisions. The final avenue is through direct and co-investments. Industry Ventures targets high conviction companies within the funds in which they have invested and directly invests or co-invests in order to get exposure. Mr. Greene reminded the Commission that the Plan's main access to venture capital is through Industry Ventures, and the Plan has made three investments with them since 2008. Mr. Greene then overviewed Industry Ventures' investment strategy. After answering several questions, Mr. Greene concluded his presentation.

Mr. Berg then introduced Mr. Derek Connor, Senior Investment Officer, to present another recent investment, Providence Strategic Growth Fund III ("PSG III"). Mr. Connor stated that the Plan recently closed a $75 million commitment to PSG III. PSG III's strategy is to invest in growth equity in lower middle markets companies in the software sector. PSG III tends to target smaller business that have an enterprise value between $10 million and $200 million. Mr. Connor explained that PSG III creates platform companies, which are grown until their size makes them attractive for acquisition by strategic buyers or private equity funds. Mr. Connor stated that PSG III focuses on four key areas: security and network technology, mobile payments, business applications, and artificial intelligence. Staff has strong conviction in the strategy, especially as a result of PSG III's focus on the rapidly growing cloud computing and mobile device sectors. Mr. Connor explained that PSG III is a new relationship for RSIC and will help fill the Plan's underweight to growth equity. Mr. Connor then answered several questions from the Commissioners regarding the investment strategy.

With there being no further questions, Mr. Connor concluded his report.

IX. EXECUTIVE SESSION

Mr. Gillespie made a motion that the Commission recede into Executive Session to discuss investment matters pursuant to S.C. Code Sections 9-16-80 and 9-16-320; to discuss personnel matters pursuant to S.C. Code Section 30-4-70(a)(1); and to receive advice from legal counsel pursuant to S.C. Code Section 30-4-70(a)(2). Mr. Giobbe seconded the motion, which passed unanimously.

X. POTENTIAL ACTION RESULTING FROM EXECUTIVE SESSION

Upon return to open session at 5:14 p.m., Mr. Hitchcock noted that the Commission did not take reportable action while in executive session. He noted that any action that did occur while in executive session, pursuant to S.C. Code Ann. § 9-16-80 and 9-16-320, would be publicized when doing so would not jeopardize the Commission's ability to achieve its investment objectives or implement a portion of the annual investment plan.

Mr. Giobbe then made a motion that the Commission approve the recommendation by the CIO to modify the investment guidelines of the existing MSCI World Index Fund mandate with Blackrock Institutional Trust Company to include the set of Accessible Strategies outlined in the confidential memo presented to the Commission in executive session on June 14, 2018, and authorize the CEO or his designee to negotiate and execute any necessary documents to implement the modifications as approved by the Commission. Mr. Hancock seconded the motion, which passed unanimously.

XI. RECESS

There being no further business, upon a motion made by Mr. Giobbe and seconded by Mr. Condon, the Commission voted unanimously to adjourn. The meeting recessed at 5:16 p.m.

MEETING TO RECONVENE FRIDAY, JUNE 15, 2018 AT 9:00 a.m.

I. CALL TO ORDER

Chair Rebecca Gunnlaugsson called the meeting of the South Carolina Retirement System Investment Commission ("Commission") day two to order at 9:01 a.m.

II. GLOBAL PUBLIC MARKETS DISCUSSION

Mr. Geoff Berg, Chief Investment Officer, announced that the next item on the agenda was a public markets update from three of our global asset allocation managers, which would be followed by a discussion of private markets by Brookfield Asset Management. He then turned discussion over to Mr. Steve Marino, Managing Director, who gave a brief overview of the global asset allocation within the Plan. In September of 2017 the Commission had approved three mandates to Aberdeen Standard Life, Morgan Stanley and PineBridge Investments. He explained the goal of the mandates was to add excess return to the portfolio through tactical asset allocation. This process is done by selecting markets instead of individual securities, and by increasing or decreasing risk, depending on the current economic conditions. He further explained that the second part of the mandate for each manager was to create more opportunities to increase communication between the parties, including the ability to leverage their teams, research, and opportunities like this to come and educate RSIC on where we are in the market cycle.

Mr. Marino introduced Mr. Guy Stern, from Aberdeen Standard Life, Global Head of Multi-Asset and Macro Investing. He noted that Mr. Stern is also responsible for the day-to-day management in the multi-asset investing team. Mr. Stern began by thanking the Communication for the invitation. He discussed how we deal with an end in the bull market in bonds. He then discussed in great detail the issues of inflation, interest rates, duration, credit and equity beta. The discussion then turned to topics including public equity allocation, real assets, and real estate, with a concentration on inflation. Lastly, he discussed global trade and trade barriers. He concluded his presentation by discussing Aberdeen's position that we are currently near the middle of the economic cycle.

Mr. Marino then introduced Mr. Michael Kelly, Chief Investment Officer and Head of Global Multi-Assets at PineBridge Investments. Mr. Kelly is responsible for overseeing the firm's global multi-asset business.

Mr. Kelly began his presentation by stating that where we are in the economic cycle matters a great deal, and it effects how and where we invest. PineBridge believes we are late in the cycle. He discussed the historical path of the economy and then discussed in detail the financial crisis, trade and how trade is globally viewed. Mr. Kelly then presented a five-year forward look on return prospects. The discussion turned to the impact of technology, including a brief history of the industrial revolutions and the economic effects of each.

He then provided the Commission with some 'musts' to think about in a disruptive world. First, you must be active in a disruptive period. Secondly, you must be very liquid. He stated that perhaps it would be important to slow down on private investments in this environment. Lastly, he stated that reflation is good at a macro-level, but at a micro-level it is very challenging.

Next Mr. Marino introduced Mr. Mark Bavoso, Senior Portfolio Manager, Global Multi-Assets from Morgan Stanley Investment Management. Mr. Bavoso began his presentation by thanking the Commission for the invitation to come and speak about his team's views on the market and the economy. He then stated that determining where we are in a cycle is difficult to do. He spoke briefly about global growth and the effect it has had on the economy this year.

Mr. Bavoso briefly discussed information technology ("IT") and IT spending. After some questions from the Commission regarding IT spending, he turned the to China and its impact on the global economy. After a thorough discussion of China, Mr. Bavoso turned to a discussion of topics including global inflation and the Euro Zone.

A lengthy question and answer session occurred with the participation of the Commissioners and all three representatives.

III. PRIVATE MARKET UPDATE

Mr. Berg introduced Mr. Barry Blattman, Vice Chairman of Brookfield Asset Management ("Brookfield"). He noted that Brookfield has nearly $300 billion of assets under management, largely private market assets. Mr. Berg outlined the Commission's relationship with Brookfield, noting that we have committed slightly more than $500 million to strategies managed by Brookfield. He then stated that Mr. Blattman was going to discuss private markets. Mr. Blattman first reviewed his background as well as Brookfield's background. He explained that his presentation would cover statistics, and how Brookfield sees the world, as well as private credit, real estate, and infrastructure.

Mr. Blattman then discussed the highlights of private markets, noting that private equity, private credit, and private real asset strategies have returned 12.6 percent annually over the last 15 years. He stated that Brookfield primarily focuses on value when it comes to strategies in private equity.

The first topic Mr. Blattman discussed was private credit, stating that the interest in floating rate debt is very high right now. He discussed the reasons for the growth in interest in floating rate debt, as well as other topics related to private credit.

Mr. Blattman then turned his discussion to the private real estate market. He stated that we are in a period of an over-supply of capital and discussed the impact of that on private real estate and fund closings. Mr. Blattman also discussed the difference between public and private real estate and how each affects the market.

Infrastructure was Mr. Blattman's final topic. He noted that in Brookfield's holdings, real estate was significantly higher than infrastructure, but they feel over time infrastructure will exceed real estate due to the scale of opportunities created around the world.

IV. ADJOURNMENT

There being no further business, the Commission voted unanimously to adjourn. The meeting adjourned at 12:00 p.m.

[Staff Note: In compliance with S.C. Code Section 30-4-0, public notice of and the agenda for this meeting was delivered to the press and to parties who requested notice and were posted at the entrance, in the lobbies and near the 15th Floor Presentation Center at 1201 Main Street, Columbia, S.C., at 5:05 p.m. on June 11, 2018]