

**South Carolina Retirement System Investment Commission
Meeting Minutes**

**December 12, 2019 9:30 a.m.
Capitol Center
1201 Main Street, 15th Floor
Columbia, South Carolina 29201
Meeting Location: Presentation Center**

Commissioners Present:

Dr. Ronald Wilder, Chair
Dr. Rebecca Gunnlaugsson, Vice Chair
Ms. Peggy Boykin, PEBA Executive Director
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 Dr. Ronald Wilder called the meeting of the South Carolina Retirement System Investment Commission (“Commission”) to order at 9:30 a.m. Mr. Allen Gillespie made a motion to approve the proposed agenda as presented. Mr. Edward Giobbe seconded the motion, which was approved unanimously.

Mr. Hancock made a motion to approve the minutes from the September 12, 2019 Commission meeting. Mr. William J. Condon, Jr. seconded the motion, which passed unanimously.

II. CHAIR’S REPORT

The Chair noted that he had nothing to report to the Commission.

III. COMMITTEE REPORTS

Mr. Hancock presented the report of the Audit & Enterprise Risk Management Committee as written and noted that it had been made available to the Commissioners for review prior to the meeting.

Dr. Rebecca M. Gunnlaugsson reported that the Human Resources & Compensation Committee met on October 24, 2019. The Committee received a human resources update from Mr. Hitchcock with staff changes since February 2019 and an update on the learning management system. The Committee also discussed the compensation consultant Request for Procurement (“RFP”) and decided to use the current plan and policy in place.

The Committee will not issue an RFP at this time but will update the compensation data through other current sources.

IV. CEO'S REPORT

Mr. Michael Hitchcock, Chief Executive Officer, began his presentation of the Agency Business Plan (the "Plan") by explaining the Plan started being developed by the executive leadership team since its' retreat in August. The Plan is a Funston recommendation, it focuses on the middle and back office functions and how we see those developing to support the overall goals of the Agency. Mr. Hitchcock stated that there are four strategic goals which the executive leadership team will be tracking the process towards meeting the goals, the initiatives, and the underlying objectives.

V. CIO'S REPORT

The Chair recognized Mr. Geoff Berg, Chief Investment Officer, for his report. Mr. Berg gave an update on fiscal year-to-date performance and prefaced his report by noting that while the update had been prepared using the new performance reporting framework, the report reflected the 17 asset classes in the current portfolio.

Mr. Berg stated that the performance for the quarter ended September 30, 2019 was 0.61 percent versus the policy benchmark of 1.15 percent, noted that the Plan increased in value by \$210 million during the quarter to nearly \$32.2 billion, and indicated that approximately \$1 billion in gross benefits were paid during the quarter. The Commissioners and Mr. Berg discussed various topics, including Plan and policy benchmark returns during various time periods, and a review of performance during the quarter. Mr. Berg noted that private equity and private credit underperformed during the quarter due to return drag from older investments. Returns for GTAA, mixed credit, and emerging market debt lagged the returns of their benchmarks during the period, while equity options, other opportunistic, and public real estate exceeded their respective benchmarks' returns. Mr. Berg also noted that REITs and public infrastructure were top performers for the one-year period.

Mr. Berg turned to a discussion of the new reporting framework. Mr. Berg reminded the Commissioners that the goal of the framework was to answer three main questions: (1) did the diversification in our Policy Benchmark beyond the Reference Portfolio add value; (2) if our portfolio deviated from the Policy Benchmark in a structural, top-down way, did these deviations add value, and (3) how well did managers perform relative to their benchmarks? Mr. Berg indicated that over most time periods, the value of diversification had been positive, while overall portfolio structure and management selection decisions had not improved returns during most of these time periods. A discussion ensued, during which Mr. Berg, Mr. Hitchcock and the Commission addressed an array of topics relating to the new reporting framework, including observations regarding the quality of portfolio structure versus the simplified policy, and the quality of manager selection.

Mr. Berg then reviewed asset allocation. He discussed over-weights and under-weights against the current policy targets, reviewed changes in Plan exposure during the quarter, and reviewed the public equity and bond portfolios in detail with the Commissioners. Lastly, Mr. Berg gave a high-level report on risk for the total portfolio.

Mr. Berg then turned the discussion to the quarterly AIP progress update. He stated that the implementation of the portfolio reporting framework was a major priority for Staff. Mr. Berg indicated that another priority was to continue to drive improvements to private markets returns. He stated that there are four main areas that the Investment Team is focusing on to support this ongoing initiative: (i) phasing in the co-investment platform; (ii) evaluating how to better use the secondary market; (iii) continuing to improve sourcing of investment opportunities, and (iv) adapting the Investment Team's process to make better use of the specialty consultant. The final priority mentioned by Mr. Berg related to continued enhancements to risk reporting.

VI. CONSULTANT REPORT

The Chair recognized Meketa Investment Group, Inc. ("Meketa") for their report. Mr. Benham stated that the themes of the report were whether investment managers add value and whether past performance indicates future returns. Mr. Benham introduced Mr. Roberto Obregon, Research Consultant, to provide the Active Management Presentation. Mr. Obregon provided an overview of the three main topics related to manager selection – searching for manager alpha; persistence in manager return; and active risk budgeting.

The first was searching for manager alpha. He stated that there was no clear answer as to whether managers add value and it may depend on the asset class. Fees are a necessary part of evaluating the value of investing in an active manager. He stated that the data showed that, net-of-fees, median managers do not add value.

Turning to the second topic, persistence in manager return, he stated that past performance is not a good predictor of future manager returns. Mr. Obregon showed that there has been no predictive relationship between how managers have performed historically and how they subsequently performed. He re-iterated the point that past performance does not guarantee future results.

Closing with the third topic, Mr. Obregon explained risk budgeting, which is monitoring and calculating how the risk is distributed in a portfolio. He noted that risk budgeting approaches often use standard deviation as the measure of absolute risk, and tracking error, or active risk, as the measure of relative risk. He stated that it is common for investors to measure the amount of active risk that individual managers take relative to their benchmarks. Mr. Obregon explained that active risk can also be calculated for an asset class or at the total system level and it is important to have appropriate benchmarks in place for this to be of value. He stressed that it is important to be able to measure the risk to manage it. Mr. Obregon stated that of the top 30 US public plans, seven currently have explicit active risk budgets at various levels of their portfolio.

A lengthy discussion ensued regarding active risk budgeting among Meketa, the CIO, and Commissioners. This concluded Meketa's presentation.

A break was taken from 11:20 a.m. to 11:35 a.m.

VII. SIOP AND AIP PRESENTATION

The Chair recognized Mr. Hitchcock for his presentation on the proposed Statement of Investment Objectives and Policies (“SIOP”) and the Annual Investment Plan (“AIP”). Mr. Hitchcock stated that the SIOP and AIP are the Commission’s foundational documents that explain what the Commission does and what it is trying to achieve. He noted that both documents are required by State law. Traditionally, RSIC had maintained them as two separate documents, but there was no requirement that the documents be separate. Mr. Hitchcock noted that the requirements for the two documents overlap and RSIC had decided to consolidate the documents. The consolidation will instill a sense of permanence into longer term strategic decisions like asset association.

Mr. Hitchcock reviewed the proposed SIOP and the overall changes. The first section amended in the SIOP is Purpose, Investment Objective and Belief. He noted that the job of RSIC is to invest and manage the Plan to produce revenue that, when combined with contributions, would equal benefit payments. He went on to explain that the Roles and Responsibilities section was changed to align with existing lines of authority and accountability as well as to emphasize the importance of risk management with a more detailed description of the Internal Audit and ERM/Compliance functions. The amended section also adds a description of the Executive Team and IIC to highlight their increased management role.

Mr. Hitchcock continued by reviewing the changes in the Asset Allocation section of the SIOP. The amended section directly links the purpose of Strategic Asset Allocation to meeting RSIC’s primary investment objective of making the Plan work. He stated that it also emphasizes the risk management benefits of employing a long-term perspective to asset allocation and provides perspective on the need to simplify the Policy Portfolio.

The Portfolio Benchmarks section was amended to trace the Commission’s process and deliberation on the Reference Portfolio Benchmark, Policy Portfolio Benchmark, and Implementation Portfolio Benchmark. Mr. Hitchcock described this section as providing the role of each benchmark in the assessment of the value of additional risk and complexity in the portfolio. He stated that this section grounds the selection of the Reference and Policy Portfolios in the needs and risk of the Plan. It also set the asset class return benchmarks for the Policy Portfolio Benchmark and how the Implementation Portfolio Benchmark would be determined. And finally, the section established ranges for asset and sub-asset classes.

Under the Portfolio Performance Framework Section, the changes would require the creation of a Portfolio Performance Framework that compares the relative performance and risk of the portfolio benchmarks and the actual portfolio. In this section Mr. Hitchcock noted that RSIC was trying to measure three decisions: diversification, which is the comparison between the Policy Portfolio and the Reference Portfolio; portfolio structure, which is the Implementation versus the Policy Portfolio, and the actual implementation of the Portfolio, which is the actual Portfolio versus the Implementation Portfolio. He explained that the Commission would have greater insight into the decisions, the decision-making process, as well as creating a sense of accountability of those decisions.

Mr. Hitchcock described the changes to the next section, Strategic Initiatives, as major ongoing Staff projects that would have a more significant impact to the portfolio, asset class, or investment strategy than typical decisions. The changes to these initiatives would be included in the AIP and progress would be reviewed at Commission meetings. Investment Policies was the next section of the SIOP to be amended. Those changes were organizing existing policies into more cohesive categories. Mr. Hitchcock noted the updates to certain policies to correspond with and implement new SIOP/AIP strategic direction. He also stated that this section would introduce the concept of baselines for each asset class and would be reviewed by Commission. It would also clearly define items that must be reviewed at each Commission meeting to comply with South Carolina Code Section 9-16-320.

The next section discussed was the Securities Litigation Policy, Mr. Hitchcock explained that this section had major changes. He explained that the primary focus of changes to the Securities Litigation Policy involved when and how RSIC would take an active role in securities litigation. He stated that the Policy now sets a \$5 million loss threshold for U.S. actions before considering taking a lead plaintiff role. The CEO would approve outside counsel. It also sets a \$1 million threshold for foreign claims that require actively opting-into litigation in a foreign jurisdiction. Other changes to this section included the delegation of lead plaintiff decision to the Executive Team and would require a unanimous vote to become lead plaintiff and delegated opt-in decisions on foreign claims to the CEO based on the Chief Legal Officer's recommendation. Lastly, the CEO has authority to direct litigation and settlement.

Mr. Hitchcock concluded his presentation by outlining the next steps and suggested that in the interim before the next Commission meeting, the Commissioners would provide input as to the changes outlined. The Chair stated that the Commission had reached a consensus on the main elements that relate to what Commissioners are responsible for regarding the Reference Portfolio and Policy Portfolio and sought additional input or feedback from the Commissioners on the proposed revisions.

VIII. DELEGATED INVESTMENT REPORTS

Mr. Berg noted that there were six delegated investment that had closed since the last Commission meeting. The six investments are as follows:

<u>Asset Class Investment</u>	<u>Investment Amount</u>	<u>Closing Date</u>
1. Private EquityHorsley Bridge XIII Venture, L.P	\$50 million	September 17, 2019
2. Private CreditKKR BDC JV(Strategic Credit Opportunities Partners, LLC – Phase 2)	\$75 million	September 30, 2019
3. Private EquityKPS Special Situations Fund V	up to \$75 million	October 9, 2019
4. Private EquityKPS Special Situations Mid-Cap Fund	up to \$20 million	October 9, 2019
5. Private CreditGoldenTree Loan Management II	\$75 million	October 18, 2019
6. Private EquityBrighton Park Capital Fund I	up to \$75 million	December 11, 2019

IX. EXECUTIVE SESSION

Mr. Giobbe moved 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 related to CEO performance and compensation pursuant to S.C. Code Section 30-4-70(a)(1); and receive legal advice from legal counsel pursuant to S.C. Code Section 30-4-70(a)(2). Dr. Gunnlaugsson seconded the motion, which passed unanimously.

X. POTENTIAL ACTION RESULTING FROM EXECUTIVE SESSION

Upon completion of executive session, the Commission moved to adopt the recommendation of the CIO and the Internal Investment Committee as discussed in executive session regarding BlackRock SLS; (ii) authorize an investment of up to \$200 million in the Fund; and \$200 million in the secondary co-investment side-car; (iii) approve a waiver of the three-business day review period;(iv) authorize the CEO or his designee to negotiate and executed any necessary documents to implement the investment as approved by the Commission upon documented approval for legal sufficiency by RSIC Legal; and (v) authorize the CEO and/or CIO or their designees 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. Gunnlaugsson seconded the motion, which passed unanimously.

XI. ADJOURNMENT

There being no further business, Dr. Gunnlaugsson moved to adjourn the meeting. Mr. Giobbe seconded the motion, which passed unanimously, and the meeting adjourned at 4:27 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., 4:58 p.m. on December 9, 2019]