

STATE BOARD OF INVESTMENT

Minutes Investment Advisory Council May 18, 2020

Call to Order

The Investment Advisory Council (IAC) met at 12:00 P.M. on Monday, May 18, 2020. The Chair of the Minnesota State Board of Investment's Investment Advisory Council determined that an in-person meeting was not practical or prudent because of the current COVID-19 pandemic and ongoing peacetime emergency declared under Chapter 12 of Minnesota Statutes. As is permitted under the Open Meeting Law in these conditions, this meeting of the Investment Advisory Council was conducted via WebEx video conferencing software and over the phone. Attendance and all votes were conducted by roll call.

MEMBERS PRESENT: Denise Anderson, Dennis Duerst, Kim Faust, Susanna Gibbons, Morris Goodwin Jr., Jennifer Hassemer (for Myron Frans), Peggy Ingison, Erin Leonard, Gary Martin, Dan McConnell, Malcolm McDonald, Nancy Orr, Carol Peterfeso, Jay Stoffel and Shawn Wischmeier.

MEMBERS ABSENT: Doug Anderson.

SBI STAFF: Mansco Perry, Patricia Ammann, Paul Anderson, Shirley Baribeau, Nate Blumenshine, Cassie Boll, Tammy Brusehaver, Andy Christensen, Stephanie Gleeson, Aaron Griga, Andrew Krech, Steve Kuettel, John Mulé, Erol Sonderegger, Jonathan Stacy, Charlene Olson and Melissa Mader.

OTHERS ATTENDING: Kristen Doyle and Katie Comstock, AON Hewitt Investment Consulting, Inc.; Neil Rue and Gordon Latter, Meketa Investment Group; Christie Eller, Attorney General's Office; Karl Procaccini, Governor's Office; Bibi Black, Secretary of State's Office; Ramona Advani, State Auditor's Office.

Members of the public attended the meeting, however due to a virtual teleconference the SBI was unable to track the information.

Approval of Minutes

The minutes of the February 18, 2020 IAC meeting were approved unanimously by roll call vote.

Executive Director's Report

Mr. Perry, Executive Director, referred members to Tab A of the meeting materials and stated that as of March 31, 2020, the SBI was responsible for managing approximately \$91.4 billion of assets. Mr. Perry reported that the Combined Funds had outperformed its Composite Index over the ten-year period ending March 31, 2020 (Combined Funds 8.0% vs. Combined Funds-Composite Index 7.8%) and had provided a real rate of return of 3.6% above inflation over the latest 20 year period (Combined Funds 5.6% vs. CPI-U 2.1%).

Mr. Perry stated that the Combined Funds assets decreased over the quarter (Combined Funds ending value of \$64.6 billion versus a beginning value of \$74.2 billion) primarily from net investment results. The Combined Funds underperformed the benchmark for the quarter (Combined Funds -12.2% vs. Combined Funds-Composite Index -12.1%) and underperformed for the year (Combined Funds -2.8% vs. Combined Funds-Composite Index -2.6%). The Combined Funds slightly underperformed the five-year period and outperformed the benchmark in all other time-periods reported.

Mr. Perry referred members to the Combined Funds asset allocation mix and asset class performance summary. The public equity performance matched for the quarter (Public Equity -22.0% vs Public Equity Benchmark -22.0%) and for the year (Public Equity -11.7% vs Public Equity Benchmark -11.7%). The total fixed income segment underperformed for the quarter (Total Fixed Income 7.2% vs. Total Fixed Income Benchmark 8.5%) and for the year (Total Fixed Income 14.0% vs. Total Fixed Income Benchmark 15.3%). Mr. Perry noted that the fixed income segment underperformance was primarily from the core bond allocation and that the Treasury portfolio, on an absolute basis, was the highest performing asset group for the quarter and the year with a 13.8% return and 21.6% return, respectively.

Mr. Perry referred members to the SBI Combined Funds Strategic Allocation Category Framework and noted that the portfolio's allocation is within the respective category ranges. Mr. Perry continued to the Volatility Equivalent Benchmark Comparison, which showed the Combined Funds return exceeding the benchmark return for all time-periods listed. The members also reviewed the Trust Universe Comparison Service (TUCS) summary, which provides a comparison of the SBI's asset allocation and returns to public and corporate plans over \$1 billion in assets. Mr. Perry stated that for the quarter and the year, the Combined Funds return ranked below the median funds in the universe somewhat reflecting the riskiness of the SBI's portfolio given the higher equity allocation.

Executive Director Administrative Report

Mr. Perry referred members to Tab B of the meeting materials for the Administrative Report, which shows that the SBI is within their administrative budget for fiscal year to date along with the travel summary for the quarter. Mr. Perry asked Mr. Mulé to provide a brief update on the legislative update. Mr. Mulé informed the members that the 2020 Pension Bill, which included the State Board of Investment's proposed legislation relating to co-investments and separate accounts, bank loans and removing liquid alternatives from the 35% statutory restriction, passed both the House and the Senate unanimously. The bill will go to the Governor for signature and, if signed, would take effect immediately. Additional legislation in the Pension Bill was the removal of duplicative annual reporting requirements for the SBI to the State Auditor's Office. Lastly, Mr. Perry referenced the update on restrictions for Sudan and Iran and stated that the SBI was not involved in any litigation.

Private Markets Program Report and Commitment for Consideration

Mr. Perry referred members to Tab C, the Private Markets Program Report and Commitment for Consideration, of the meeting materials and asked Mr. Krech to review the two recommended private markets investments listed in the report with existing managers: Oaktree Opportunities Fund XI and the TCW TALF Opportunities Fund. Mr. Krech and Ms. Boll responded to questions from the members. After discussion a motion was made that the IAC endorse the two recommended private markets investments which was seconded and approved by roll call vote. The motion passed.

Report from the SBI Administrative Committee

Mr. Perry referred members to the Administrative Committee Report in Tab D of the meeting materials. After Mr. Perry's review of the items listed in the Executive Director's annual work plan and budget, Mr. Perry asked for the IAC's endorsement. A motion was made that the IAC endorse the FY21 Executive Director's Work Plan, the FY21 and FY22 Administrative Budget Plan, and adopt the Continuing Fiduciary Education Plan as presented. The motion was seconded and approved by roll call vote. The motion passed.

Executive Director Comments and Discussion

Mr. Perry referred members to Tab E of the meeting materials for the SBI Executive Director Comments and Discussion Report. The first item of discussion was the SBI Board Resolution concerning Environmental Social and Governance initiatives adopted at the February 26, 2020 Board meeting. The IAC discussed the long-term objective of reducing carbon risk exposure and was supportive of the staff's efforts to address the risk of exposure to companies in the thermal coal business and in Canadian oil sands. Next, Mr. Perry asked for member comments on potential portfolio modifications within the fixed income segment to include the deployment of a short duration treasury ladder plus cash. The cash allocation would be measured against the three-month T-Bill and the short-term bond ladder portfolio would have a custom benchmark representative of the term structure risk. The members were supportive of the additional liquidity this approach would provide. Lastly, Mr. Perry identified four groups within the Combined Funds: public equities, fixed income, private markets, and unallocated. The unallocated is the non-invested portion of the private markets targeted allocation. Mr. Perry is recommending that the unallocated assets be invested as a separate asset group for operational reasons and would consist of cash, securities and currency overlay strategies along with other risk management vehicles. Staff continues to work on the structure of the unallocated asset group and plans to bring a recommendation to the members in the near future. After discussion, a motion was made that the IAC endorse the general concepts laid out above; to increase the fixed income allocation (which includes cash) from 22% to 25%; to adopt the private market plus unfunded allocation approach; and to increase the market value plus unfunded commitment cap from the current 35% to 45%. The motion was seconded and approved by roll call vote. The motion passed.

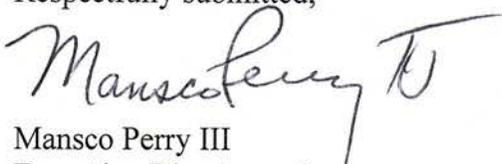
Reports

The remainder of the reports included the Public Markets, Non-Retirement and Participant Directed Investment Programs Report in Tab F; Tab G contained the Market Environment Report prepared by AON; Tab H contained the Capital Markets Outlook & Risk Metrics Report prepared by Meketa; and Tab I included the SBI's Comprehensive Performance Report.

Adjournment of Meeting

The meeting adjourned at 2:13 p.m.

Respectfully submitted,



Mansco Perry III
Executive Director and
Chief Investment Officer

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