State Investment Commission
Monthly Meeting Minutes
Wednesday, July 24, 2013
9:00 a.m.
Room 135, State House

The Monthly Meeting of the State Investment Commission (SIC) was called to order at 9:03 a.m., Wednesday, July 24, 2013 in Room 135, State House.

I. Roll Call of Members

The following members were present: Mr. J. Michael Costello, Mr. Robert Giudici, Ms. Paula McNamara, Ms. Marcia Reback, Mr. Andrew Reilly and General Treasurer Gina Raimondo. Also in attendance: Mr. Timothy Walsh of TIAA-CREF; Mr. Christopher Flick of Vanguard Institutional Investor Group; Mr. Thomas Lynch and Mr. Mark Johnson, of Cliffwater, alternative investment consultant to the Commission; Ms. Esther Rombault and Mr. Kamil Salame of CVC Capital Partners; Mr. John Burns, Mr. Alan Emkin, Mr. David Glickman, Mr. Jeremy Thiessen, of Pension Consulting Alliance (PCA), General Consultant, Real Estate Consultant and 529 Consultant to the Commission; Mr. Greg Balewicz and Mr. Andrew Letts of State Street Global Advisors (SSGA); Ms. Sally Dowling, of Adler Pollock, legal counsel; Mr. Norm Geller and Ms. Denise Olsen of GEM Realty Capital, Inc.; Mr. Mark Sullivan of Bank New York Mellon, custodian bank to the Commission; Mr. Charlie Kelley and Ms. Gail Mance-Rios of Rhode Island Higher Education Assistance Authority (RIHEAA); Ms. Anne-Marie Fink, chief investment officer and members of the Treasurer's staff; Members of the House and Senate fiscal staff and various local reporters. Mr. Thomas Fay, Mr. Thomas Mullaney and Mr. Frank Karpinski were absent.
Treasurer Raimondo called the meeting to order at 9:03 a.m.

II. Approval of Minutes

On a motion by Mr. Costello and seconded by Ms. McNamara, it was unanimously
VOTED: To approve the draft of the minutes of the June 26, 2013 meeting of the State Investment Commission.

II. Defined Contribution Plan –Vanguard Vehicle Change

Ms. Fink said since the target date funds with TIAA-CREF have reached $100,000,000, the plan is eligible to go into a different vehicle. Currently the plan is in mutual funds vehicle. The plan can be changed to a Collective Investment Trust (CIT). She said a main advantage is that the cost would be lowered from approximately .18% to .11%. She said the CIT has the same investment approach as the target date mutual funds, however is a different structure.
Mr. Walsh added that the CIT is basically a clone product of the current vehicle and the benefit is cost. He said that there is a communication program to help participants understand the changes.
Ms. Fink explained that due to CIT being a trust, there are no prospectuses and the reporting is slightly different than a mutual fund and explained the governing entities of each. She reminded the

board of the state administrative fee participants will see in their September statements which were previously paid by the state during the transition year.

On a motion by Ms. Reback and seconded by Ms. McNamara, it was unanimously
VOTED: to approve the change for the Defined Contribution target date funds from Mutual Funds into a Collective Investment Trust.

III. Private Equity Recommendation

Mr. Lynch introduced CVC Capital Partners.
Mr. Salame introduced CVC Capital Partner's Fund VI. He reviewed the firm's business model, management structure.
Ms. Fink asked where they see opportunities in Fund VI and Mr. Salame answered disproportionally in Europe. He explained there was paralysis for a couple years and there is a bit more stability now.
Ms. Rombault added they also see opportunity in partnering with governments to help them improve business.
Ms. Rombault discussed performance and expected marks for the investment in the fund.
Mr. Salame added that CVC has built a franchise for long-term value creation all around.
CVC left the room.
Mr. Lynch said that this is one of the most experienced and one of the largest private equity firms in Europe. He added that all their prior funds are top quartile performers.
Mr. Lynch said PCA recommends a commitment of up to $25,000,000.

On a motion by Mr. Reilly and seconded by Mr. Costello, it was unanimously
VOTED: to invest in CVC Capital Partner's Fund VI for up to $25,000,000.

IV. CollegeBound Fund Review

Mr. Thiessen said, at the request of the Treasurer's Office and RIHEAA, he reviewed the current structure of the program and what is offered. He said the plan currently offers a full suite of age-based options and a suite of individual funds. He noted that in the current structure there are no individual fund options geared toward a rising inflation environment. He recommended offering short-date Treasury Inflation-Protected Securities.
Mr. Thiessen also said he looked at target-date allocations and concluded it is well positioned going forward in relation to others in the industry. He said a key point is that the target-date funds, compared to others in the industry, have gradual step down of equities into more conservative asset classes, making them less subject to timing risk.
Mr. Thiessen said PCA's monitoring models found persistent underperformance issues in many underlying funds, with the exception of fixed income. He added that the whole international equity lineup has consistently underperformed. He recommended identifying the key funds in the portfolio which have performed below benchmark significantly and recommends that AllianceBernstein suggest alternatives.
Mr. Thiessen also recommended including conservative, moderate and aggressive glide paths built with passively managed index funds.
Ms. Fink gave an update on ongoing discussions with AllianceBernstein and said Treasury staff, RIHEAA and PCA will work with AllianceBernstein in the coming months to continue work on improving the CollegeBound Fund.

V. 2013 Proxy Season Review- Issues and Outcomes

Ms. Fink introduced Mr. Balewicz from SSgA as part of an informational series to support the corporate governance policy. She reminded the board of Ann Yerger's presentation about the Council of Institutional Investors (CII).

Ms. Fink said SSgA manages the vast majority of ERSRI's equities, about $3.5B. Therefore, she pointed out, that is where the vast majority of our vote assets are.

Mr. Balewicz, senior relationship manager, introduced Mr. Letts, head of corporate governance at SSgA and chair of the proxy advisory committee and co-chair of their ESG Committee. Mr. Letts also serves on the advisory council of CII. Mr. Letts leads a team which votes on over 14,000 meetings a year over 63 markets globally and leads the engagement efforts with senior management and boards of companies.

Mr. Letts provided an overview of ESG investments using section two of the presentation.

He then took the board through SSgA's governance structure outlined in section three and explained his staff's background in the field. He explained their relationship with Institutional Shareholder Services (ISS) and the services they provide for SSgA.

Treasurer Raimondo asked how we can influence SSgA's policy and Mr. Letts explained the process and ways ERSRI could leverage their influence.

Mr. Costello asked if they could split votes and Mr. Letts said no, not in a pooled product.

Mr. Letts then reviewed their voting record and said they vote against management about 8% of the time over the past three years. He explained most of their activity is in antitakeover related issues and protecting shareholder rights. He touched on other issues they monitor including, director elections, say-on-pay and emerging markets accounting standards. He then gave a case study regarding Hess.

Mr. Emkin asked what percentage of the market SSgA is and Mr. Letts said they hold about 3% of the Russell 3000, the 4th largest shareholder. He explained further that they are the 2nd largest shareholder in the S&P 500 and the largest or 2nd largest in the Dow. He said this usually provides them with a lot of influence.

Mr. Emkin pointed out years ago big funds used to vote more in line with management where the trend is moving away from that because of pressure from funds like ERSRI.

VI. Legal Counsel Report

There was no legal counsel report.

VII. CIO Report

Ms. Fink updated the board on the discussion with Brown Brothers Harriman on the recent challenges of Global Inflation-Linked Bonds (GILBs) as an asset class. She said an option was to add a hedge, but that it looked expensive. She said another option is to change the benchmark from the Barclays Global Inflation-Linked Bond Index to the Barclays Intermediate Inflation-Linked Bond Index. She said such change would encourage Brown Brothers Harriman to lower the duration and the interest rate sensitivity in the portfolio. She said she believes this is a good idea to lower overall inflation sensitivity while preserving inflation protection.

Ms. Fink reviewed the portfolio's performance for the last month and reviewed each asset class. She said the portfolio is up 11.1% fiscal year to date compared to 11.3% for the total plan benchmark and compared to the 9.6% return for a 60% equity/40% bonds portfolio. She said the outperformance vs. 60/40 means asset allocation has paid off and risk is also lower.

She noted that since the hedge funds were added 20 months ago, return is higher and risk is lower compared to the 60/40 plan. She said ERSRI's risk is 6% versus 7.2% of the 60/40 approach.

VIII. Treasurer Report

Treasurer Raimondo commended the efforts of the board for their continued work.

On a motion by Ms. Reback and seconded by Mr. Reilly, it was unanimously
VOTED: to cancel the meeting scheduled for August 28, 2013.

IX. Real Estate Updates

Ms. Fink introduced GEM Realty Capital, Inc. She said GEM is the first value-add real estate asset allocation since before the global financial crisis.
Mr. Glickman said the fund is in line with the implementation of a change in real estate strategy. He said PCA recommends GEM's Fund V for the non-core portion of the real estate portfolio.
Ms. Olsen gave a brief introduction to the fund.
Mr. Geller further described the firm and the investment strategy. He said they focus on risk and trying to produce superior risk-adjusted returns. He believes GEM's platform to invest in private real estate and publicly traded real estate is what gives them an edge.
Mr. Geller gave an overview of Fund V. He said the fund's target is to produce an 18% net return for investors with moderate leverage and a focus on principal preservation.
Mr. Geller reviewed the primary strategies. He said he believes the greatest opportunities are in value-add investing. He said the fund will be opportunistic within real estate, even buying lower-risk debt instruments when they can generate equity-like returns.
Ms. Olsen went over their investment track record and portfolio construction over the prior four funds. She reviewed returns to date for the past four funds of realized and unrealized investments. She added that the fund has a very active pipeline for acquisition opportunities.
Ms. Olsen talked about the alignment of interests between GEM and its investors. She said GEM invests its own money alongside its LP's and went on to explain the fee structure. She pointed out the investor receives all the invested capital back plus an annualized 9% cumulative preferred return before GEM participates in any profit. She explained there is a management fee of 1.50% on 90% of committed capital during the investment period and 1.50% on invested capital throughout the life of the fund. She said for investors with a $50M or greater investment there is 0.25% fee break during both periods.
Mr. Giudici asked questions regarding valuations, the fund structure and the duration of holdings.
Treasurer Raimondo asked about the 9% hurdle rate in previous funds.
Gem answered board members questions and left the room.
Mr. Glickman said the size of the firm and the size of the fund suggest that they are focused on incentive fees rather than management fees. He also said because GEM will make its profits from selling properties after adding value, it means they will not sit on the assets longer than necessary.
Mr. Glickman also reviewed the risks of the fund. He said because GEM relies on their network of relationships to find deals, many of the deals are joint ventures with others. He said this potentially adds a level of complexity and difficulty. He added that GEM has the ability to have high leverage,

although historically they have not maxed out on it. He said that non-core funds, like GEM, don't use third party appraisers; however, the important mark is the ultimate sales proceeds.
Mr. Glickman said PCA recommends a $50,000,000 commitment. He pointed out this will provide ERSRI with the 0.25% fee break. He also mentioned that PCA is in discussion with GEM to give ERSRI the opportunity to observe or possibly gain a seat on the advisory board. He suggested the board not base their decision too much on this term, as the firm is very accessible.

On a motion by Mr. Reilly and seconded by Ms. Reback, it was unanimously
VOTED: to approve an investment of $50,000,000 in GEM Realty Capital, Inc. Fund VI as advised by PCA at stated terms.

For the next item, Ms. Fink stated since the next recommendation pertains to a former employer of hers, even though it was a separate division, she is recusing herself from the process to avoid even the appearance of any conflict of interest.

Ms. Renee Astphan, Treasury analyst introduced the next item saying the intent is to transition from an overweight in non-core real estate to core real estate. She said JP Morgan Strategic Property Fund is the largest of the core funds. She said that ERSRI currently has an investment which was committed to in 2006.
Mr. Glickman said PCA recommends considering committing up to an additional $25,000,000 to the JP Morgan Strategic Property Fund. He said PCA considers this fund one of the two best performing, large, open-end core real estate funds. He noted they have withdrawal procedures in place and said they reinvest the income generated from the fund.
Mr. Glickman said the fund invests in large, fully leased properties with no development or speculative risk. He said the fund has a moderate amount of leverage at around 25%.
Mr. Glickman added this additional investment is consistent with the strategy implemented last year to try to, whenever possible, reduce the number of relationships and to gradually expand core holdings so that they are the significant driver of real estate returns.

On a motion by Mr. Reilly and seconded by Mr. Costello, it was unanimously
VOTED: to approve the recommendation by PCA to make an additional investment of $25,000,000 in JP Morgan Strategic Property Fund.

A motion was then made by Mr. Costello and seconded by Mr. Guidici to convene into executive session pursuant to Rhode Island General Law §42-46-5 (a) (7) as the discussion may relate to the investment of public funds, the premature disclosure of which may adversely affect the public interest. A roll call vote was taken to enter executive session and the following members were present and voted Yea: Mr. J. Michael Costello, Mr. Robert Guidici, Ms. Paula McNamara, Ms. Marcia Reback, Mr. Andrew Riley, and General Treasurer Gina Raimondo.
It was then unanimously
VOTED: To convene into executive session pursuant to Rhode Island General Law §42-46-5 (a) (7) as the discussion may relate to the investment of public funds, the premature disclosure of which may adversely affect the public interest.

A motion was then made by Mr. Costello and seconded by Ms. Reback to seal the minutes of the executive session of July 24, 2013, pursuant to Rhode Island General Laws §42-46-5 (a) (7) as the discussion may relate to the investment of public funds, the premature disclosure of which may

adversely affect the public interest. A roll call vote was taken, and the following members were present and voted Yea: Mr. J. Michael Costello, Mr. Robert Guidici, Ms. Paula McNamara, Ms. Marcia Reback, Mr. Andrew Riley, and General Treasurer Gina Raimondo.
It was then unanimously
VOTED: To seal the minutes of the executive session of July 24, 2013, pursuant to Rhode Island General Law §42-46-5 (a) (7) as the discussion may relate to the investment of public funds, the premature disclosure of which may adversely affect the public interest.

On a motion made by Mr. Costello and seconded by Ms. Reback, to exit executive session pursuant to Rhode Island General Law §42-46-5 (a) (7). A roll call vote was taken and it was unanimously
VOTED: To exit executive session and return to open session.

It was reported to the public the only vote taken during executive session was an unanimous roll call vote to seal the minutes pursuant to Rhode Island General Law §42-46-5 (a) (7).

There being no other business to come before the Board, on a motion by Ms. McNamara and seconded by Mr. Reilly, the meeting adjourned at 11:54 a.m.

Respectfully submitted,

Gina M. Raimondo
General Treasurer