State Investment Commission

Monthly Meeting Minutes
Wednesday, March 25, 2015
9:00 a.m.
Room 205, State House

The Monthly Meeting of the State Investment Commission (SIC) was called to order at 9:03 a.m., Wednesday, March 25, 2015 in Room 205, State House.

I. Roll Call of Members

The following members were present: Mr. J. Michael Costello, Ms. Faith LaSalle, Mr. Thomas Mullaney, Mr. Thomas Fay, Ms. Paula McNamara, Mr. Frank Karpinski and Treasurer Seth Magaziner.
Also in attendance:
Mr. Alan Emkin, Mr. David Glickman and Ms. Christy Fields of Pension Consulting Alliance (PCA), general consultant; Mr. Nick Beevers of Lone Star Funds; Mr. Thomas Lynch of Cliffwater, alternative investment consultant; Mr. Joe Tansey and Mr. Evan DiPaolo of Garrison Investment Group; Mr. Steve Johnson, Ms. Joyce Marsilia and Ms. Margie Vose of Fidelity, custodian for the Ocean State Investment Pool; Mr. Greg Balewicz, Mr. Scott Conlon, Ms. Tia Wang and Ms. Jennifer Bender of State Street Global Advisors; Ms. Sally Dowling of Adler Pollock Sheehan; Mr. Jeffrey Padwa, General Counsel to Treasurer Magaziner; Ms. Anne-Marie Fink, chief investment officer, and members of the Treasurer's staff. Ms. Tiffany Spudich of Capital Cities, 529 plan consultant, joined via conference call.
Treasurer Magaziner called the meeting to order at 9:03 a.m.

II. Approval of Minutes

On a motion by Mr. Mullaney and seconded by Mr. Fay, it was unanimously
VOTED: to approve the draft of the minutes of the February 25, 2015 meeting of the State Investment Commission.

III. Real Estate Recommendation – Lone Star Real Estate Fund IV

Ms. Fields introduced Lone Star. She said PCA recommends a $30 million commitment. Fund IV is an opportunistic closed-end real estate vehicle that will target investments primarily in distressed commercial real estate and related debt opportunities in U.S, Europe and Japan. She noted that the firm has a very strong track record.
She added that this would be the first vehicle that has off-shore U.S exposure in ERSRI in recent years so it is subject to currency and regulatory risks.
Mr. Beevers gave an overview of the firm and its strategy. He expressed the firm's focus on returning capital to investors quickly and efficiently as they are investing in distressed assets. They employ a number of strategies in order to minimize risk in the markets in which they invest. They acquire large portfolios and liquidate them very quickly. They pay down debt in the fund extremely quickly which reduces the leverage in the portfolio and reduces absolute dollar commitment in that market.
He said they are disciplined in their purchases with a focus on large scale transactions where there is limited competition. Lone Star has been active in US Europe and Asia over the past 15 years. They have multi-jurisdictional European operation and Europe is where they anticipate deploying around 80% of the fund. He said the European market has been very transactional in the last 8-12 months. They have benefited from those transactions.

He went on to review the terms of the fund. The fund has a $5 billion target with a final close in April ,2015. They expect the fund to be largely committed to by existing investors. He reviewed the fee structure. The fund charges management fees of 1.1% during the investment period, reducing to 0.6% thereafter. Until the preferred return is achieved in the fund, there is no incentive fee to the General Partner; all equity return goes to investors. The General Partner, the asset management operations and their chairman are committing $375 million on top of the fund target, which means great alignment of interests and they are highly incentivized to perform.
The board asked questions.
Lone Star left the room.
Ms. Fink said the recommendation is a $30 million allocation to the fund. She believes it gives the portfolio some diversification in real estate.
Ms. Fields said it fits well within the portfolio and it highlights a very clear market opportunity.
The board discussed.

On a motion by Mr. Mullaney and seconded by Ms. LaSalle, it was unanimously
VOTED: to approve a $30m allocation to the Lone Star Real Estate Fund IV.

IV. Private Equity Recommendation – Garrison Opportunity Fund IV

Mr. Lynch introduced Garrison Investment group indicating how the fund fits into the allocation strategy. They are a private debt, special opportunity credit fund.
Mr. Tansey gave an overview of the firm. They focus on smaller, lower-middle market companies and specialty finance opportunities, finding opportunities where the banks have retreated. He reviewed the performance of previous funds and gave an overview of their team. He said they have a very diversified investment pool and presented an example of an investment.
The board asked questions.
Treasurer Magaziner asked how they are positioned to handling regulatory risk in areas of their business that could become more heavily regulated over time.
Mr. Tansey said the segment they focus on that has regulatory pressure is consumer lending. They are not a sub-prime consumer lender. They do credit card consolidation debt for the most part. All the regulatory pressure is really in the deep sub-prime interest rates and lack of disclosure. A big part of their due-diligence is to determine if the disclosures to consumers are appropriate.
The board asked questions.
Garrison left the room.
The board discussed.
Treasurer Magaziner said he feels comfortable that they are well-diversified and they would be able to adjust their strategy accordingly.
Ms. Fink said the fund is positioned very well regardless of whether or not there is a distressed cycle in the U.S.
Mr. Lynch added that from a portfolio position perspective, it is a shorter term at 6 years and a 3 year investment period. They would be putting money to work at a reasonable rate and with the expectation of getting capital back rather quickly.

On a motion by Mr. Fay and seconded by Mr. Costello, it was unanimously
VOTED: to approve a $30m allocation to the Garrison Opportunity Fund IV.

Ms. Fink asked Mr. Lynch if Luxor Capital was on Cliffwater's watch list.
Mr. Lynch said no funds are currently on watch list and they are seeing a good rebound in the portfolio performance.

V. Ocean State Investment Pool Extension & Fee Reduction

Ms. Fink gave a brief overview of the Ocean State Investment Pool. She said it has been a good vehicle in a challenging time for banks. She added that given the environment it does not seem like an appropriate time to adjust it so she would recommend a contract extension.

Ms. Marsilia gave an overview of the group that manages OSIP and the overall presence of Fidelity in Rhode Island.

Mr. Johnson gave a review of asset management. He said institutional money market is key to Fidelity from fixed income stand point. He noted that Fidelity is the largest money manager in the country. They have a team- oriented approach among, research analysts, traders and portfolio managers. They continue to bring that approach to bring safety to the OSIP. The advantage of OSIP is the great level of expertise of the team.

Ms. Vose talked about the marketing approach of the pool and the local events they attend for outreach. She reviewed some of the interactions they have had with agency heads across the state. She highlighted the benefits of the pool are safe and liquid investments with a market-rate of return and the diversification of the pool. It also keeps other banks competitive with interest rates they provide.

Ms. Marsilia reviewed the proposed terms for a contract extension. The new fee schedule for the next three years would be 0.01% reduction in pricing. As we move into an environment where interest rates are expected to rise, they would expect money market funds to deliver higher performance.

Fidelity left the room.

Ms. McNamara noted that she had previously worked with Fidelity so she would recuse herself from voting.

On a motion by Mr. Costello and seconded by Mr. Mullaney, it was

VOTED: to approve a three year contract extension with Fidelity for the Ocean State Investment Pool.

VI. Approval of 529 Plan Investment Policy

Ms. Fink reminded the board that at the previous meeting Capital Cities distributed a draft of an investment policy statement for the 529 plan. She said minor changes were made and a final draft had been distributed to the board prior to the meeting. She asked the board for approval of the draft.

The board discussed the changes.

Mr. Costello asked if AB (AllianceBernstein) would have to sign off on the document.

Ms. Spudich said that although AB had reviewed it they do not need to sign off on it. She added that they are already operating within the parameters of the policy

On a motion by Mr. Costello and seconded by Ms. LaSalle, it was unanimously

VOTED: to approve the draft 529 Plan Investment Policy Statement.

VII. Briefing on Equity Factor Tilts

Mr. Conlon said the passive investment landscape is evolving and this is creating exciting opportunities for investors. In recent years a number of beta strategies have emerged. These involve building passive portfolios using different weighting methodologies in order to identify or favor certain factors or themes. These strategies bring elements of passive and active investments. They have a high level of transparency, are very consistent and the cost is very similar to a traditional passive cap-weighted strategies. The performance expectations are more in line with active investments.

He said these strategies offer opportunity to enhance return over traditional cap-weighted indices and reduces volatility over those strategies. There is a lot of compelling interests in the marketplace in elements of quality and low volatility. These investment factors tend to do very well in a rapidly falling market environment.

He added that the decision comes down to investors and which factors make the most sense for them. Some of their clients are considering looking to combine factors together that offer good diversification.
He concluded by saying that this is very interesting area that provides potentially strong return benefits for investors without straying from the traditional characteristics of the indexing strategies. They continue to see investors consider these types of portfolios and allocate to them in their investment portfolios.
Ms. Bender added that institutional investors with long horizons are uniquely positioned to harvest these long-term premiums because they already have the governing structures in place to withstand the shorter term periods of volatility.
Mr. Emkin added that a lot of institutional investors are looking at these strategies because of their dissatisfaction with traditional active management.
Treasurer Magaziner noted that this is something worth looking further into. In the coming months, staff along with SSGA will look to see if there are compelling factors worth discussing. He expressed the benefits of staying passive but also understanding that the decision is an active decision on the board’s part.
The board discussed and asked questions.

VIII. Treasurer’s General Comments

Treasurer Magaziner thanked the board for their work and reminded everyone that the focus is on the long-term and that should guide decisions.

IX. Legal Counsel Report

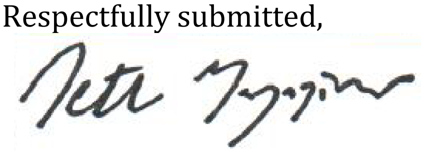
There was no legal counsel report.

X. Chief Investment Officer Report

Ms. Fink reviewed the performance of the portfolio and the market environment for the month of February. The fund was up 3% edging out the benchmark and the 60/40 plan. Fiscal-year-to-date the fund was up 2.3% and a tad behind both the benchmark and the 60/40 plan. The 3 year performance is ahead of both the benchmark and the 60/40 with considerably less risk. The strategy and diversification is really working in the long term.
She followed up on discussion from the previous meeting with Capital Cities and AB. As they went back to implement changes to the share class, they realized that the plan is not eligible for the share class. They agreed to change to the lower fee share class but they are not giving a rebate for retro compensation.

There being no other business to come before the Board, on a motion by Mr. Fay and seconded by Mr. Mullaney the meeting adjourned at 10:51 a.m.

Respectfully submitted,



Seth Magaziner,
General Treasurer