New Mexico
Public Employees Retirement Association
Investment Committee
November 9, 2021

Call to Order

This meeting of the New Mexico Investment Committee meeting was held on the date cited above via Zoom tele/video conferencing. Chair Steve Neel called the meeting to order at approximately 11:00 a.m.

1. **Roll Call**

   The meeting attendance met quorum with the following members present;

Committee Members Present:
Steve Neel, Chair
Paula Fisher, Vice Chair
Lawrence Davis
Loretta Naranjo Lopez

Committee Member Absent
Diana Rosales Ortiz

Additional Board Members Present
Francis Page
Tim Eichenberg
Shirley Ragin

Staff
Greg Trujillo, Executive Director
Trish Winter, Executive Assistant
Anna Williams, CFO
Kristin Varela, Acting CIO
LeAnne Larranaga Ruffy, Acting Deputy CIO
Misty Schoeppner, Acting General Counsel
Geraldine Garduno, Asst. General Counsel
Jessica Trujillo, HR Manager
Karyn Lujan, SmartSave Plan Manager
Melinda Marquez, Member Services Bureau Chief
Angela Romero, Albuquerque Office Manger
Sara Hume, Director of Beta
Frank Mihail, Director
Jovanna Archuleta, Investments
Aaron Kayser, Investments

Other
Rose Dean, Wilshire Consulting
Tom Toth, Wilshire Consulting
Steve DiGirolamo, Wilshire Consulting
Mike Krems, Aksia
James Walsh, Albourne

Sarah Grist, Albourne
Jackie Bernsen, Albourne

2. Approval of the Agenda

Chair Neel proposed an amendment to the agenda by moving Items C and D to the top of the agenda, followed by Item B.

Paula Fisher moved to amend the agenda as proposed. Lawrence Davis seconded the motion. The motion passed by a unanimous roll call vote as follows;

Steve Neel	Yes
Paula Fisher	Yes
Lawrence Davis	Yes
Loretta Naranjo Lopez	Yes

Lawrence Davis moved to approve the amended Agenda. Paula Fisher seconded the motion. The motion passed by a unanimous roll call vote as follows;

Steve Neel	Yes
Paula Fisher	Yes
Lawrence Davis	Yes
Loretta Naranjo Lopez	Yes

3. Approval of the Consent Agenda

Lawrence Davis moved to approve the Consent Agenda. Paula Fisher seconded the motion. The motion passed by a roll call vote of 3 to 1 as follows;

Steve Neel	Yes	
Paula Fisher	Yes	
Lawrence Davis	Yes	
Loretta Naranjo Lopez		No

C. Annual Investment Policy Review

Chair Neel stated the Investment Policy statement should be reviewed annually.as well as the Committee Charter.

He further stated the common element in the proposed changes is transparency around investment reporting to memorialize performance reporting, specifically in the specialty asset classes, which are more opaque than most parts of the portfolio. The transparency will provide members and retirees greater visibility into what's going on in the portfolio. As part of the transparency, the specialty reports will be published on the PERA website.

Acting CIO, Kristin Varela, reiterated they have been working on transparency with the aim of memorializing expectations and policy and process. She stated very few red lines had been added to the

Investment Policy Statement, IPS. There was one specific section of the IPS was enhanced to add expectations for reporting going forward.

Ms. Varela stated they had done a clean edit to the Policy with a three-sentence addition as follows;

i. There will be a memorialization of the expectations on total fund performance reporting and a formalized presentation to the Investment Committee quarterly.

ii. Memorializing the new illiquid asset class performance reporting. The Investment Committee (IC) will receive the reporting quarterly and there will be a formal presentation every other quarter, covering fiscal year-end and calendar year-end.

iii. Memorializing expectation regarding dissemination to the public. After the quarterly reviews have been provided to the IC, there will be a requirement for all reporting to be posted to the PERA website for public resource and consumption.

Ms. Fisher thanked Chair Neel and Ms. Varela for the transparency.

Mr. Davis also appreciated the transparency. He moved to amend Section 6(b) to read as follows; Total fund performance reporting will be formally presented to the Investment Committee quarterly and shall include comparative peer performance data compiled by the Board's investment consultant.

Paula Fisher seconded the motion.

Mr. Davis explained the amendment will ensure members are provided with more information to have greater transparency regularly. Chair Neel opined that the comparisons will be edifying and will also be very positive since PERA's performance has been good.

Ms. Naranjo Lopez asked if the amendment was a necessity since staff was already required to provide the performance recording. Ms. Varela confirmed it was part of the standard reporting package and staff had no problem with the amendment. Staff, therefore, saw no reason to deviate from the standard reporting.

Mr. Davis pointed out the Board only started receiving peer review information recently. Therefore, his amendment was a memorialization to ensure the information is provided consistently to both the Board and the members. Mr. Davis confirmed the amendment would also ensure the peer rankings are included in the quarterly investment reports that are done in the specialty asset classes.

The motion to amend the IPS passed with a unanimous roll call vote as follows;

Steve Neel	Yes
Paula Fisher	Yes
Lawrence Davis	Yes
Loretta Naranjo Lopez	Yes

Paula Fisher moved to accept the amended IPS. Lawrence Davis seconded the motion. The motion passed with a unanimous roll call vote as follows;

Steve Neel	Yes

Paula Fisher	Yes
Lawrence Davis	Yes
Loretta Naranjo Lopez	Yes

D. Annual Investment Committee Charter Review.

Ms. Varela stated that refreshing and reviewing the Charter is a consistent theme across all committees. She further stated the Charter had not been reviewed for some time and thus looked like it had more changes than there were. The changes were consistent with how business is currently conducted, how they are formalized in policy through the Investment Policy Statement, and the new reporting and transparency initiatives.

Ms. Varela reported the first change was around polishing the 2010 language and the way certain parts of the portfolio were referenced. It also aimed at homing in on the key strategic initiatives the Board focuses on, the IC advises and recommends on, and the entire collective governing body adopts.

The first is the advisement of investment-related issues, including targeted total fund risk and assumed rate of return, strategic asset allocation limits and ranges, active risk and excess return targets, which in 2010, would've been more of the active versus passive determination, policy asset class benchmarks, and simple reference portfolio benchmarks for purposes of monitoring implementation effectiveness.

All the above are consistent with how strategic initiatives and governance are documented in the IPS. There was also a change to how Board Consultants were being referred to, they will now be referred to as Board Investment Strategic Consultants. Investment advisors will also be referred to as contracted investment managers.

Item E on the presentation provided recognition of the amount of work, understanding, and educational resources required for a committee member to be able to see and understand the complex investment portfolio. Items G, H, and I were consistent with the IPS.

Ms. Varela also reviewed the Charter requirements and stated the IC now meets four times a year. This had been edited but had not been limited. Ms. Varela also reported they had added a new section proposing a charter review annually as well as a running log of revisions and edits over time.

Lawrence Davis moved to amend Item G to include the statement 'and shall include comparative peer performance data compiled by the Board's investment strategic consultant. He also highlighted the addition of the word 'strategic' in the amendment. Paula Fisher seconded the motion.

The motion passed with a roll call vote of 3 to 1 as follows;

Steve Neel	Yes	
Paula Fisher	Yes	
Lawrence Davis	Yes	
Loretta Naranjo Lopez		No

Ms. Naranjo Lopez stated she voted 'no' because she felt there was a need to look at how it matched the Policy. She was also concerned the Board did not have total understanding when they could not do due diligence. She also felt the Board was not privy to a lot of information and wondered whether they were meeting their fiduciary responsibilities.

In response, Chair Neel stated all the amendments were on transparency and allowing members and retirees to have more information. Ms. Naranjo Lopez argued she was not denying transparency but was concerned because Legislators was implying the fiduciaries were not doing their job. Ms. Naranjo Lopez stated the Board was not making investment decisions because Policy did not allow them to. She, therefore, felt the amendments were also not allowing them to do their job.

Lawrence Davis moved to accept the Charter as amended. Paula Fisher seconded the motion. The motion passed with a roll call vote of 3 and 1 abstention as follows;

Steve Neel	Yes
Paula Fisher	Yes
Lawrence Davis	Yes
Loretta Naranjo Lopez	Abstain

Ms. Naranjo Lopez requested more information.

B. Planning for Inflation.

Chair Neel pointed out inflation had affected everyone. He stated the biggest threat to the fund is hyperinflation.

Ms. Varela pointed out they have been seeking to diversify risk across the PERA portfolio due to fears of rising inflation. She introduced Rose Dean and Stephen DiGirolamo from Wilshire Consulting, to discuss inflation. Wilshire and another firm, Bridgewater, had assisted PERA in the risk diversification investment strategy.

Ms. Varela also reported there will also be a study of liabilities. She informed the Committee the Cost-of-Living Adjustment, COLA, is not pegged to CPI at all. Therefore, on the liability side, risks occur with rising salaries, but those are offset by rising contributions. The second risk that will be discussed by Ms. Rose Dean is the diminishing returns which could be driven through inflation shocks.

Mr. Stephen DiGirolamo kicked off the presentation by stating inflation should be thought of as a risk. Mr. DiGirolamo presented some risks listed by Wilshire that relate to investment, with inflation being one of them. He defined inflation as the process of continuously rising prices or continuously falling value of money. When prices are rising, the value of money falls, because it takes more currency to purchase that same item.

Mr. DiGirolamo stated a lot of what drives inflation comes down to supply and demand curves. He further stated an increase in aggregate demand is a demand pool catalyst for inflation. A decrease in aggregate supply is a cost-push catalyst to inflation. Several different catalysts are usually in conflict with each other, thus making it hard to come up with short-term assumptions and projections for inflation. He discussed some of the ways in which inflation can be measured.

Mr. DiGirolamo discussed the need to care for inflation. Some of the reasons to care about inflation risk are as follows;

i. Inflation is generally the minimum hurdle rate for any investment strategy. If an investment does not allow the fund to maintain the real asset of the investment, then there's no point of that investment.

ii. Inflation erodes the purchasing power of any portfolio.

iii. The performance of traditional asset classes has historically suffered in rising inflation.

iv. Several secular trends could contribute to structurally higher inflation, including fiscal deficits and monetary policy, supply disruptions, peak globalization, corporate concentration.

Mr. DiGirolamo also discussed how traditional asset classes correlated to inflation over a long period.

Rose Dean discussed the PERA portfolio and the potential impact on inflation. She reported PERA has a decent amount of inflation mitigating assets in its policy allocation. Ms. Dean stated Wilshire looks at portfolio exposure in terms of factor risks. Two economic factors show potential vulnerabilities for different asset classes and the portfolio. These are growth and inflation. Ms. Dean presented a chart showing how different asset classes behave when the two factors surprise to the upside or downside.

Wilshire also did a one-time additional negative impact on the growth asset class returns, assuming inflation would be running much higher than expected. They then considered three scenarios as follows;

i. Assumed the inflation shock remains for one year, then the asset class returns go back to their base case scenario.
ii. Assumed the inflation shock remains for two years, then the return expectations revert to the base case.
iii. Assumed the inflation shock remains for four years.

Ms. Dean recognized the three scenarios were very broad-stroked and the PERA portfolio might be different. They however wanted to show the range of outcomes and what could happen to return and market value expectations.

Ms. Dean stated even though PERA is well positioned to mitigate risks, they will continually review the portfolio and the asset allocation to ensure the vulnerabilities are managed.

Ms. Dean further stated while the starting point is low, the impact is still unknown because of the current unprecedented environment. She added the biggest potential source of volatility for the equity markets is the support the capital markets returns get from the monetary and fiscal policies.

Ms. Varela stated they had spoken to each of the Board members about the mismatch between PERA's risk tolerance and the required rate of return. She added the mismatch will need to be focused strategically for the PERA Board going forward to determine what to balance. She pointed out everyone was anticipating elevated volatility going forward and they also understood the required rate of return would not match the targeted risk profile the fund currently deploys.

Chair Neel introduced the two people from Bridgewater Associates, Melody Rollins, and Jennifer Armstrong.

Ms. Armstrong kicked off her presentation by stating Bridgewater believed the coming years could be very different from the past decades in terms of inflation. She pointed out the current inflation in the U.S. is the highest seen in 30 years. The inflation of the last 30 years was very low and stable, which is something quite rare. She also stated Bridgewater felt the current inflation is more persistent than policymakers and markets are pricing.

Ms. Armstrong pointed out even though people are anticipating more inflation, markets do not. Markets are indicating the inflation seen today is going to be fleeting. It will quickly return down to the level of roughly 2.5% seen in the past. It was also the risk spectrum Bridgewater felt that investors should be thinking about as they think about how to navigate the environment ahead.

Since markets are not anticipating much inflation, it will be a risk for investors and retires if it materializes. Ms. Armstrong discounted the common notion that assets that did well recently would also do well in the future. She stated it is a dangerous notion, particularly as the world today is changing.

Mr. Davis asked how far into the future the huge demand outpacing supply will be sustainable. In response, Ms. Armstrong stated a lot of things about demand are self-reinforcing. For instance, one person's spending is another person's income. She felt the current times are in that self-reinforcing phase and thus the demand will be very sustainable. Ms. Armstrong however added the one thing that could end the sustainability is if policymakers start to worry about inflation and start to tighten. On the plus side, policymakers are avoiding tightening too soon because they do not want to slow down the economy. They would rather tolerate high inflation. Taking into account the current level of economic activity and spending, Ms. Armstrong stated the expectation is that sustainable demand will be strong going forward.

Chair Neel requested details on the discussion around the U.S. dollar being the reserve currency and how that will mitigate a significant amount of inflation. He also asked how slowing demographics could inhibit inflation. He further referenced the huge infrastructure bill in Washington D.C. and asked how that exacerbates inflation.

On the U.S. dollar and the reserve currency, Ms. Armstrong stated if the U.S. can maintain its reserve currency status, is a protection against inflation. It doesn't guarantee against inflation, but it helps prevent the worst outcomes because the worst inflations throughout history have occurred when a country lost control of its currency. However, that's unlikely for the U.S. because there is a natural amount of demand for the dollar. Even though the U.S. economy is doing better than all the other developed world economies, there is still a vulnerability that's unfolding.

Ms. Armstrong further explained policy is inflationary because keeping interest rates low as inflation is surging usually just fuels the fire. She added the current world is in a balance mode, where policymakers are looking at how to lean in the direction of inflation while keeping interest rates low.

Chair Neel and Mr. Davis thanked the teams from both Wilshire and Bridgewater for the presentation.

A. <u>Performance and Market Review.</u>

<u>Q3 2021 Investment Performance Review</u>

Tom Toth with Wilshire Consulting overviewed the scorecard and stated it is the regular template for reporting particular metrics to the Investment Committee and setting them against very defined targets.

Mr. Toth reported the portfolio lagged over the last 3, 5, and 7 years versus the reference portfolio. He stated the reference portfolio is a simple index made up of global equities and fixed income.

Mr. Toth stated in the scorecard, they consider risk-adjusted performance as they believe it is the most pertinent measure of the universe comparison. They also include the straight universe comparison which shows the returns irrespective of risk positioning for the portfolio across time. The longer periods, 3, 5, and 10-years were below median.

With regards to asset allocation comparison, Mr. Toth stated it is a work in progress as the main challenge here is planned sponsors have different ways of categorizing their assets. Therefore, capturing one view is difficult. He added it will be highlighted when it provides a reasonable comparison for the PERA portfolio versus peer groups.

Mr. Davis inquired about the amount of active management dollars sitting in the information ratio. Mr. Toth stated the portfolio has a reasonable amount of exposure to index and index-oriented strategies to get very efficient, extraordinarily low-cost exposure. But from an active management standpoint, it was just north of 50 or 55%. He added he would go back and verify this information.

Chair Neel requested more details on the fiscal year-to-date policy benchmark return. Mr. Toth explained it is a relatively simple calculation of the performance of the policy benchmark over a relatively short period. It represented one quarter's worth of performance.

Chair Neel requested the Wilshire team to review their minutes from the last Investment Committee as there had been some deliverables that had been asked from Wilshire that had not been addressed.

Q2 2021 Illiquid Asset Reporting

Chair Neel stated this item dovetailed into the Charter and Investment Policy changes discussed earlier. He added the discussion here would revolve around some examples of the enhanced reporting and transparency that the Committee could anticipate in the future from some of the illiquid asset classes.

Head of Alpha, Ms. LeAnne Larranaga-Ruffy, introduced PERA's investment associates and selection consultants. She stated the team was structured with an asset class focus and they look across the liquidity spectrum and review public and private assets simultaneously.

Kate Brassington is the investment associate covering global equity and would be responsible for public and private equity.

Clayton Cleek would be covering credit-oriented fixed income, and was responsible for liquid, alternative, and illiquid credit.

Michael Killfoil would be covering real assets and was responsible for liquid and illiquid real estate and real assets.

Selection Consultants were; Mike Krems, from Aksia, the one responsible for private equity; James Walsh, Sarah Grist, and Jackie Bernsen, from Albourne, are responsible for credit real estate and real assets.

Private Equity Portfolio- Aksia

Mike Krems highlighted five important areas within private equity as follows;

i. **Exposure** – as of June 30, 2021, the total exposure in the portfolio was $2.1 billion.
ii. **Performance** – the portfolio performed well. The inception to date net IRR was 16.8% as of June 30, 2021. The direct alpha has been 7.4%.
iii. **Cash Impact** - the cash impact for calendar 2021 is expected to be a positive inflow of about $11 million from the portfolio. Distributions have exceeded contributions this year. This was different than in prior years. There's been more capital being called for new deals over each of the past three years. As the seeds have been planted, returns have been generated and it was evident realizations exceed contributions.
iv. **Commitment Pace** - has been about $315 million per year on average over the past five years. Looking at a five-year rolling period, it totals $1.6 billion over the period.
v. **Overall impact** - Inception to date, the portfolio has generated $1.6 billion in profits for the benefit of beneficiaries and others related to PERA.

Mr. Krems stated the above takeaways will be available and accessible to a wider audience.

Chair Neel thanked Mr. Krems and Ms. Larranaga-Ruffy for the presentation.

Credit Portfolio - Albourne

Sarah Grist overviewed the performance for the illiquid credit portfolio as follows;

i. The IRR of the portfolio had tracked the liquid benchmark recently. The portfolio currently had an IRR of 9.3% and has kept pace with the public credit benchmark.
ii. The portfolio is currently well-funded. There hasn't been a lot of capital deployed in the last few years. Currently working with PERA staff on building out a pipeline to build up the private credit portfolio to its target weight.
iii. Overall performance was strong. The distressed asset class ad an IRR of 10% and real estate was lower at 5.8%. The overall portfolio total IRR was 9% with a small, positive alpha of 0.2%.
iv. Currently, the portfolio is more tilted towards the U.S. with also a reasonable amount of exposure to Europe. There are future opportunities in Asia and other regions would be incorporated into the build-out of the portfolio. There's also a large allocation to real estate debt. Real assets debt and some other strategies will be added going forward.

Real Estate Portfolio

Jackie Bernsen reported the overall performance of the portfolio was either in line or exceeded that of the public benchmark, which is generally favorable. The portfolio has also been a bit more active in deploying capital over the last couple of years.

From a total plan perspective, the plan has been active in new commitments, making a total of four closed-ended and one open-ended new commitment over the 12 months. The aim is to try and diversify the exposure and grow the overall cashflow nature of the portfolio through new commitments to core plus and value-added funds.

Real Assets Portfolio

James Walsh reported the IRR was 5.5%, which is ahead of the index. The alpha is 2.2%, indicating the portfolio has one ahead of what could have happened in the public markets. There have been cash outflows, meaning money has been going into the portfolio in contrast to what was seen in private equity. Capital calls have been greater than distributions as a result of restructuring going on in the portfolio.

Chair Neel reiterated these are the type of reports which will be published on the website. There will also be a more in-depth review of each of the asset classes twice a year.

E. CIO Search

Executive Director, Greg Trujillo reported an RFP had been issued for recruitment consulting services for a chief investment officer. The RFP was put out last Friday.

F. Investment Division Compliance Update

1. **Manager Selection Activity Report**

Ms. Larranaga-Ruffy reported there have been several approvals since August, including

i. A multi-proposal
ii. Global public stock restructure, which required a combination of physical rebalance across all managers.
iii. The discontinuation of the overlays, which should decrease the structural tilts and the active risk in the portfolio
iv. Illiquid commitments in private equity and real estate.

Ms. Larranaga-Ruffy also reported the Portfolio Fit and Review Team met on September 17, September 29, and October 27, to review the proposals. The team includes the Executive Director, the interim CIO, and the Deputy interim CIO. The IC Chair, Steve Neel, and IC member Lawrence Davis share the responsibility to attend the meetings as an observer.

All proposals were agreed to by the team and have been forwarded to legal review and diligence.

2. **Q3 2021 Cash Activity & Rebalance Update**

Ms. Varela reported they had gone through all compliance. In July, $60 million of benefit payments were paid out. That was funded from real assets, which was holding the largest overweight.

In September, the investment activities funded $43 million of benefit payments. That was funded by global equities liquidity account. There was also some replenishing of liquidity accounts, where there was asset purchase versus the liquid asset redemption.

$71 million was paid out in August for benefits from investment activity. That was funded from cash alone. In August, there was sufficient liquidity in the cash account from distributions and pooling or replenishing of cash balances was not required.

3. **Q3 2021 Securities Lending Update**

Frank Mihail reported there are 570 million securities on loan for the program, which is about 3% of the portfolio and generated 24 bips of performance for the quarter.

Adjournment

With no further business to discuss, Chair Neel adjourned the meeting at approximately 1:01pm.

Approved by:

Steve Neel, Investment Committee Chair

ATTEST:

Greg Trujillo, Executive Director

Exhibit(s)