

NEW MEXICO
PUBLIC EMPLOYEES RETIREMENT BOARD
INVESTMENTS COMMITTEE MEETING

April 30, 2015

This meeting of the Public Employees Retirement Board Investments Committee was called to order by Vice Chair Roman Jimenez, at approximately 9:00 a.m. on the above-cited date in the PERA Building, 33 Plaza La Prensa, Fabian Chavez Jr. Board Room, Santa Fe, New Mexico.

1. **ROLL CALL:** Executive Director Wayne Propst called roll and a quorum was established with the following members present:

Members Present:

Roman Jimenez, Vice Chair
Dan Esquibel
Patricia French
Stewart Logan
Louis Martinez [late arrival]

Member(s) Excused:

Dan Mayfield, Chair

Other Board Members Present:

Tim Eichenberg
Paula Fisher
Loretta Naranjo Lopez
John Reynolds

Staff Members Present:

Wayne Propst, Executive Director
Susan Pittard, Chief of Staff/General Counsel
Jonathan Gabel, Chief Investment Officer
Sylvia Barela, ASD Director
Greg Trujillo, Deputy Director
Julian Baca, Deputy CIO
Judy Olson, Executive Assistant
Karen Risku, Deputy General Counsel
Roderick Ventura, Assistant General Counsel
Claudia Armijo, Assistant General Counsel
Sam Ojinaga, Bureau Chief, Contributions Accounting
Natalie Cordova, Controller/CFO
LeAnne Larrañaga-Ruffy, Portfolio Manager
Joaquin Lujan, Portfolio Manager

Christina Keyes, Portfolio Manager
Jude Perez, Portfolio Manager
Mark Montoya, Financial Analyst
Kristen Varela, Financial Analyst
Karyn Lujan, Deferred Compensation Administrator

Others Present:

Stanley Bernstein, Bernstein Liebhard
Jamie Feidler, Cliffwater
Tom Toth, Wilshire
Paul Lium, Nationwide
Richard Ong, RRJ Capital
Charles Ong, RRJ Capital
Ronald Merriman, Retiree
Barbara Pardo, Retiree
Theo Livingston, Retiree
Patrick O'Brien, Retiree

2. APPROVAL OF AGENDA

Mr. Logan moved to approve the agenda as published. His motion was seconded by Ms. French and passed by unanimous [4-0] voice vote. [Mr. Martinez was not present for this action.]

3. APPROVAL OF CONSENT AGENDA

Ms. French moved to approve the consent agenda. Mr. Logan seconded and the consent agenda was unanimously [4-0] approved. [Mr. Martinez was not present for this action.]

4. CURRENT BUSINESS

Chief Investment Officer's Report

1. Investment Performance Summary – March 2015

Jonathan Grabel, Chief Investment Officer, offered that the plan finished March with a balance of \$14.6 billion, down \$114 million from February. The plan has recovered from the drawdown during March. The plan is up 2.15 percent fiscal year to date to the end of March. He reminded the Committee that the true focus needs to be on the long-term performance. As the fund transitions to the new custody bank there will be changes to the monthly reporting to highlight the importance of the long term. The actuarial assumptions of 7.75 percent will be included as a benchmark and the reports will include 10-year results.

Mr. Grabel highlighted longer-term results, noting the fund's 5-year numbers are up 9 percent. While the plan was down 49 basis points for March, April has been strong. Since inception of the records, June 1986, the plan is up net 9.36 percent, thus a dollar invested in 1986 is worth – with adjusting for inflation -- \$14.65 today. "It's not about weeks," stated Mr. Grabel, "it is about decades."

Over the five and seven-year period the strongest performer has been domestic equities. Over the five-year period, real estate had a very strong period, up close to 15 percent which he attributed to low interest rates. The weakest performer has been international equities. Mr. Grabel reminded the Committee of the importance of a widely diverse asset allocation. At this point the return reports tends to be one dimensional on its focus on returns. He expected more dynamic and multi-dimensional reporting with the new custody bank to see a better view of what impacts the returns of a portfolio. Wilshire has already begun including more dimensions in their quarterly reports.

The strong performers during March were absolute return, small-mid cap domestic equity, real estate and private equity. It was a weaker month for large cap domestic equity, international equity and real assets. Real asset results are attributed to the dramatic correction in the price of oil.

In response to Ms. French's question regarding the new custody bank reporting, Mr. Grabel said staff plans on providing an update/preview at the May meeting on some of the reporting changes.

Mr. Logan asked how the cash plan and transitioning to the new strategic asset allocations might impact the returns. Mr. Grabel said there is currently \$940 million in cash which is all invested through the cash overlay program. The cash is reduced with RFP awards and private asset recommendations. He noted that public stocks and fixed income can be transitioned quickly while private assets take years.

2. Cash Plan Update

Mr. Grabel reminded the Committee that the cash balance is higher as a result of the implementation of the new strategic asset allocation. PERA has transitioned billions of dollars this year. The more efficient asset categories can transition faster than private assets and given that private assets have grown in allocations there appears a mismatch in timing. The current environment in the private assets markets has exacerbated by private asset managers are calling down capital slower than returning capital. The private asset managers are doing the right thing by selling assets at great multiples yet being more cautious about making new investments – this has contributed to the cash balance being higher than anticipated.

Staff is working on a presentation to demonstrate how the cash balance will be reduced by the end of the fiscal year.

Mr. Grabel identified the last tranche from domestic equity which was the largest inflow in the amount of \$276 million. The use of cash during March included \$33 million in benefits, refunds, and manager fees; \$100 million was transitioned to the fixed income plus transition account with Blackrock which will be shifted to the Board approved managers, and \$27 million in capital calls. He noted the inflow was \$138 million with outflow of \$27 million. Also a transition for international equity began with \$100 million and \$70 million was an accounting reallocation between the STIF and overlay. The cash overlay was down \$8 million for March; however, for the quarter the cash overlay was up \$9 million and for April it is up \$30 million.

Ms. French thanked Mr. Grabel and his staff for the decisions they are making for the PERA fund.

Mr. Grabel confirmed Mr. Reynold's point that the cash is invested synthetically through various derivative instruments replicating the market.

3. Other Updates

Mr. Grabel noted that he preferred committing to new managers and opening new accounts prior or following the custody bank transition the provided the following updates:

- Emerging Market Equity – evaluation committee met and due diligence visits for finalists are being scheduled
- High Yield RFI – evaluation committee met and semi-finalists interviews occurred. An on-site visit is scheduled as well as Board recommendation in May
- Pending RFIs & RFPs include: Listed Infrastructure was posted April 1;
- The following MQs will be presented today: Multi-category credit, International Equity small-cap and 457B
- Securities lending unrealized losses for May decreased by \$1 million. The unrealized balance as of March 31st was \$4.2 million
- The implementation with BNY Mellon is very comprehensive and rigorous and an update is scheduled for May

Mr. Grabel mentioned he recently spoke at Asset International's CIO Conference in New York where he presented PERA's fee study. The study was well received and PERA is considered a national thought leader.

Contained in the Board packet are PERA's portfolio managers' views regarding different topics.

B. Action Item: Alternative Asset Recommendation for Approval, to be Funded According to the Cash Plan and Subject to Legal Review by General Counsel

1. Recommendation to Commit up to \$75 Million to RRJ Capital Master Fund III, LP, in the Private Equity Portfolio

[Exhibit 1: Staff recommendation re: RRJ Capital Master Fund III, 4/30/15; Exhibit 2: Cliffwater report, 4/30/15; Exhibit 3: RRJ Master Fund III, LP March 2015]

LeAnne Larrañaga-Ruffy, Portfolio Manager, said staff, in conjunction with Cliffwater, is recommending commitment up to \$75 million to RRJ Capital Master Fund III, an Asia buy-out fund for PERA's private equity portfolio. Currently PERA's portfolio has a 4 percent exposure to Asia and Southeast Asia. This fund will complement the current private equity portfolio by diversifying it geographically to less efficient markets and will be a good accompaniment to 57 Stars that was approved last month.

Ms. Larrañaga-Ruffy introduced RRJ's chairman and CEO Richard Ong and co-chair and co-CEO Charles Ong.

Mr. Richard Ong provided background of his professional investment history leading to RRJ Fund I. The first fund earned an internal rate of return (IRR) above 40 percent and the second fund is at about 19 percent IRR. He pointed out that Charles Ong had worked for the Sovereign World Fund of Singapore Government, a \$200 billion fund, and together they co-manage RRJ.

Mr. R. Ong said their main focus of investment is China and Southeast Asia, heavily populated areas with a growing middle class. Their investment thesis is simple: It is about population and about middle-class. While the middle class is still relatively small it is growing by the day. Focus investment opportunities include food, environmental services and educational services.

The portfolio of Fund III, is expected to be invested in areas of high growth despite the general GDP being 5 percent or 6 percent. They are looking for industries that will grow in the 15+ percent over the next few years including areas such as logistics.

In the food sector RRJ owns one of the largest dairy companies in China and has secured the Dunkin' Donuts franchise for China, Hong Kong and Macau. They expect to have 5,000 stores.

As far as financials, RRJ is invested in insurance and electronic payments as well as environmental services related to cleaning up China's air, water and waste.

Mr. R. Ong said investors in Fund II include the states of Oregon, New York, and cities include Sacramento, San Francisco, as well as corporate investors. He anticipated the Fund III portfolio would be similar to Fund II.

Mr. Esquibel asked about illiquidity risk in the fund investments. Mr. Grabel said the illiquidity risk is not unique to RRJ and is true of all private assets. Jamie Feidler, Cliffwater, agreed with Mr. Grabel's observations and added that the liquidity of the total PERA fund was considered when the new strategic asset allocation was developed. RRJ has a history of returning capital and generating liquidity much more quickly than the average private equity firm.

Mr. Charles Ong pointed out that vintage 2012 Fund I has returned cash back to investors at approximately 85 percent and by the end of 2015 although 100 percent of the investment will be returned and yet seven major assets have not been sold.

Mr. C. Ong pointed out that the Ong family is one of the biggest investors in the funds. The family and employees invest with the same terms as other investors. Nothing has been drawn from Fund III and the goal is to raise 10 percent more than Fund II which is \$4 billion. He noted there was 100 percent re-up from all Fund II investors.

Mr. Feidler reviewed the performance comparison which included the net IRRs against the most-like public index which is the MSCI Asia Ex-Japan.

Ms. French made a motion to recommend that PERA commit up to \$75 million to RRJ Capital Master Fund III LP, a private equity partnership focused on non-US investments, to be funded according to PERA's Cash Plan, subject to approval of legal documentation by General Counsel. Mr. Esquibel seconded. The motion passed by 4-0 voice vote with Mr. Martinez abstaining because he arrived during the presentation.

C. Information Item: Multi-Strategy Credit RFP MQs and Timeline

Joaquin Lujan, portfolio manager, pointed out that the multi-strategy credit portfolio will be about \$365 million. He highlighted that the mandate returns are in excess of 200 basis points over the Global High Yield Index, less volatile than that index, contain a higher Sharpe ratio than the index, have better downside protection and are less correlated to the ACWI IMI index and the US Barclay's Aggregate index.

Mr. Lujan reviewed the timeline with the RFP release date May 8, 2015. He anticipated that 20 to 30 firms would respond.

Mr. Grabel noted from a portfolio construction standpoint he would have preferred one firm to manage this mandate. There is a possibility for better pricing as well as a better view of the impact on the portfolio as a whole with one manager. The recommendation for this to be conducted as an RFP is that it is a less discrete category and involves review judgment.

D. Information Item: International Equity Small Cap RFI MQs and Timeline

Ms. Larrañaga-Ruffly said this RFI will be issued next week due to the September 30, 2015 contract expiration of the current manager, Principal Global Investors. The mandate is between \$150 million and \$175 million. No more than 10 managers will be invited to submit responses. She noted that the MQs are standard for PERA RFIs.

The deadline for submissions will be June 1, 2015 and a recommendation is anticipated for presentation the Board in July 2015.

Tom Toth, Wilshire, noted that there are discrete categories in this group and it is much easier to work through data.

E. Action Item: Deferred Compensation Plan Document Loan Amendment

Karyn Lujan, Deferred Compensation Plan Manager, said staff recommends the Committee approve the amendment to section 7.2.h. This amendment removes the limitation of

participants to have no more than two loans in any 12-month period. The deletion will allow participants to have one outstanding loan at any given time. The amendment provides consistency with industry standards and there are no IRS guidelines regarding loan frequency for 457B plans. She noted that according to Nationwide, New Mexico is the only state with this limitation.

Mr. Grabel said the number of loans outstanding can never be more than one. PERA had a second limitation that limited the participant to two loans a year even if they had been paid back. This provides increased flexibility to the members.

Mr. Esquibel moved to approve the plan document amendment. His motion was seconded by Mr. Martinez and passed by [4-0] voice vote. Mr. Logan was not present for this action.

F. Action Item: Recommendation of Auditor for FY 15 Deferred Compensation Plan Audit – Eide Bailly LLP

Ms. Lujan said staff requests that the Committee approve Eide Bailly to conduct the PERA Deferred Compensation Plan Audit for FY 15. Eide Bailly is currently on the NM State Auditor's list of approved firms and conducted PERA's FY 14 audit.

Mr. Esquibel moved to approve the recommendation for Eide Bailly for the FY 15 Deferred Compensation Plan audit. Ms. French seconded and the motion passed by unanimous [5-0] voice vote.

G. Informational Item: Deferred Compensation Investment Consultant RFP MQs and Timeline

Ms. Lujan said the current consultant contract with Mercer will expire September 30, 2015 and the RFP will be released May 1, 2015. Proposals will be due on June 19, 2015 and she anticipated awarding the contract on August 27, 2015. She reviewed the MQs.

Ms. Lujan noted that at the time of contract expiration, Mercer will have been with PERA for eight years.

Mr. Grabel pointed out PERA's recent contracts have been for eight years with a 30-day termination clause.

H. Informational Item: Deferred Compensation Buffer Account Surplus and Litigation Settlement

Ms. Lujan said that in January 2015 PERA's accounting department assessed the DC account's availability budget to actual expenditures ratio and discovered a running cash balance of approximately \$75,000. There has been a quarterly surplus of \$2,500 from the actual DC operating expenses and that has accumulated to \$75,000. The funds will be used for upcoming quarterly operating expenses.

Ms. Lujan said the DC plan will be awarded \$28,959 from a recent class action law suit involving 22 different mutual funds within the Massachusetts Financial Service Company. The settlement was based on market timing and late trading. Nationwide does not have the capability to reimburse specific participants; instead the award will be given to PERA and the funds will be used to offset operating expenses.

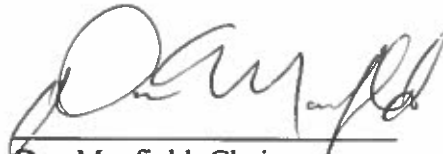
5. **OTHER BUSINESS**

Mr. Reynolds said he appreciated the scheduling of the Investments Committee occurring before the Board meeting. He said he hoped it could become practice. Vice Chair Jimenez agreed.

6. **ADJOURNMENT**

Having completed the agenda, and with no further business to come before this Committee, Ms. French moved to adjourn. Mr. Logan seconded and Board Vice Chair Jimenez declared this meeting adjourned at 10:45 a.m.

Approved by:



Dan Mayfield, Chair
Investments Committee

ATTEST:


Wayne Propst, Executive Director

Attached Exhibits:

Exhibit 1: Staff recommendation re: RRJ, 4/30/15

Exhibit 2: Cliffwater report; Re: RRJ, 4/30/15

Exhibit 3: RRJ Master Fund III Report, 3/2015