



## Teachers' Retirement System of the State of Illinois

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### MINUTES

#### Meeting of the Investment Committee February 19-20, 2014

A meeting of the Investment Committee of the Illinois Teachers' Retirement System was held on February 19-20, 2014 at the Springfield office of the Illinois Teachers' Retirement System 2815 West Washington Street. Cynthia O'Neill, Chair, called the meeting to order at 1:55 p.m. A quorum was present.

Roll Call attendance was taken with the following trustees present: Cynthia O'Neill (Chair), Mike Busby (Vice Chair), Mark Bailey, Marcia Campbell (arrived 3:00 p.m.), Rainy Kaplin, Cinda Klickna, Bob Lyons, Sonia Walwyn, Sharon Leggett, Chris Koch (2/20 9:00-12:30). Absent: Enrique Vasquez and Chris Koch (2/19)

Others present: Dick Ingram, Executive Director; Stan Rupnik, Chief Investment Officer; Greg Turk, Director of Investments; Deron Bertolo, Director of Investment Operations; Scottie Bevill, Sr. Investment Officer; Ken Musick, Investment Officer; Kenyatta Matheny, Sr. Investment Officer; Jerry Quandt, Investment Officer; Bob Jiroutek, Sr. Investment Analyst; Kirk Sims, Investment Analyst; Brennan Basnicki, Investment Analyst; Brian Nobis, Investment Analyst; Tim Hays, Sr. Investment Officer; Dakin Sanert, Sr. Investment Analyst; Bill Thomas, Investment Officer; Chuck Handy, Investment Officer; Tom Gray, General Counsel; Stacy Smith, Director of Internal Audit; Tassi Maton, Sr. Internal Auditor, Christina Baker, Internal Auditor; Dave Urbanek, Director of Communications; Tammy Green, Asst. to Executive Director; Sue Billington, Executive Assistant; Pat O'Hara, Cavanagh & O'Hara (Fiduciary Counsel); Avery Robinson, Callan Associates (Real Estate Consultant); Becky Gratsinger and Greg Kantor, RV Kuhns (Investment Consultant).

Visitors present: Shirley Dodds, IRTA; Dennis Murfin, IRTA; Gayla Dial, IEA-R/IRTA; Bob Kaplan, IEA-R/IRTA; Angela Myers, Loop Capital; and Jim Baker, UNITE HERE (2/20).

## **APPROVAL OF MINUTES**

A draft of the December 5, 2013 minutes of the Investment Committee meeting was sent to the committee for review. On a motion by Sharon Leggett, seconded by Rainy Kaplan, the minutes were approved as printed.

## **OLD BUSINESS**

### Investment Manager Chart

Stan Rupnik, Chief Investment Officer, provided an organizational chart of TRS's investment managers as of December 31, 2013. Documentation is on file. Allocations are shown for the main TRS trust fund, the POB account and on a total TRS basis. In addition, the committee received a chart detailing the System's top manager relationships.

### Cash Withdrawal

Mr. Rupnik discussed the recent cash withdrawals necessary to fund the System's cash requirements. Documentation is on file.

## **STAFF/CONSULTANT PRESENTATIONS**

### Investment Performance Review

RV Kuhns provided an update of the investment performance for the quarter ending December 31, 2013. Total assets: \$42.75 billion. Documentation is on file.

The total fund return, gross of fees:

- 1 year: 15.93%
- 3 years: 10.64%
- 5 years: 12.31%
- 10 years: 7.48%

The total fund return, net of fees:

- 1 year: 15.26%
- 3 years: 10.00%
- 5 years: 11.67%
- 10 years: 6.99%

### Watch List

Staff provided an update of the investment managers currently on the watch list for the quarter ended December 31, 2013. Levin Capital Management (domestic equity) remains on watch due to performance concerns. Staff recommended that the PIMCO Global Multi-Asset strategy be added to the watchlist due to performance. A motion was made by Cinda Klickna, seconded by Bob Lyons, that the committee recommend to the Board to accept the watch list as presented. The motion passed by a unanimous voice vote.

### W/MBE Utilization Report

Kenyatta Matheny provided preliminary data on the participation of minority and female-owned brokers/dealers and investment managers within the TRS investment portfolio through December 31, 2013. Assets under management for WMBE-owned investments were \$5.62 billion, representing 13.78% of the total TRS portfolio. Documentation is on file.

Director Ingram reported on the hearings by the Senate Committee on Pensions and Investments concerning the use of minority- and woman-owned asset management and brokerage firms by Illinois public pension systems. The hearings were conducted on December 11, 2013 in Chicago. The goal of the Senate Committee is to increase WMBE and Illinois-based business participation in the IL public pension funds. Over the past 10 years, the Senate Committee has expressed concern that the IL pension funds have taken minimal steps to increase MBE/WBE participation. Staff recognizes opportunity for continued improvement of the program. Senator Martinez submitted follow-up questions for staff to respond by the end of February. The trustees received a memorandum from Director Ingram on the focus of improving diversity initiatives of the investment program. Documentation is on file. Additional discussion will be held at the April Board retreat on how to further evolve the program.

The System's 10<sup>th</sup> annual Opportunity Forum is March 13, 2014 at the Crowne Plaza hotel in Springfield.

### Vista Equity Partners – Private Equity

Representatives of Vista Equity Partners presented an investment opportunity in the firm's fund, Vista Equity Partners Fund V, Limited

Partnership and Vista Co-Investment Fund, L.P. Their presentation booklet is on file. Staff provided an overview of the due diligence that was conducted. A motion was made by Mike Busby, seconded by Mark Bailey, that the committee recommend to the Board to commit \$200 million to Vista Equity Partners Fund V and \$100 million to Vista Co-Investment Fund. The motion passed by a unanimous voice vote.

## **RECESS**

The meeting recessed at 4:04 p.m. and reconvened at 4:15 p.m.

### Quarterly Compliance Summary

Deron Bertolo, Director of Investment Operations, provided a summary of the quarterly compliance for the quarter ended December 31, 2013. TRS is in compliance with Public Acts 95-0616 (Iran) and 95-0521 (Sudan).

### Global Equity Asset Class

Bill Thomas, Investment Officer, reported on the recent activity within the global equity asset class. Staff recommended revising the OakBrook domestic equity mandate from the current 1.00% to the 1.75% tracking error product, relative to the S&P 500. A motion was made by Bob Lyons, seconded by Sharon Leggett, that the committee recommend to the Board to approve staff's recommendation of shifting to 1.75% tracking error product. The motion passed by a unanimous voice vote.

TRS last conducted a search for a commission recapture broker in 2006. Following a review of the TRS program and industry landscape, staff recommended a request for proposal (RFP) to identify broker(s) for the commission recapture program. Following the RFP process, a final recommendation will be presented to the Board in May or June. A motion was made by Cinda Klickna, seconded by Marcia Campbell, that the committee recommend to the Board to submit a request for proposal to identify broker(s) for the commission recapture program. The motion passed by a unanimous voice vote.

### Real Estate

Staff recommended additional allocations to Capri Capital Partners, Invesco Real Estate, and Heitman to increase the System's long-term real estate

allocation from 11.7 percent to 14 percent of the investment portfolio. This is consistent with the System's real estate tactical plan and pacing study. Staff recommended that Capri Capital and Invesco receive an additional \$125 million each and allocate an additional \$100 million to Heitman, for a total allocation of \$350 million. A motion was made by Rainy Kaplan, seconded by Marcia Campbell, that the committee recommend to the Board to approve the total allocation of \$250 million to Capri Capital, Invesco, and Heitman, as presented. The motion passed by a unanimous voice vote.

### Private Equity

Staff requested ratification of a follow-on investment in an existing co-investment with Energy Capital Partners that has been approved by the Investment Committee Chair. The follow-on opportunity is a complementary fit with the goals and objectives of the private equity co-investment program. A motion was made by Bob Lyons, seconded by Sonia Walwyn, that the committee recommend to the Board to ratify the Investment Committee Chair approval of an increase in TRS's commitment to Energy Capital Partners II Annex A, L.P. The motion passed by a unanimous voice vote.

Staff requested ratification of the Investment Committee Chair's approval to sale 17 funds within the private equity program. Staff sold the portfolio with the assistance of Park Hill as an advisor. A motion was made by Mark Bailey, seconded by Sharon Leggett, that the committee recommend to the Board to ratify the Chair's approval for the secondary portfolio sale within the private equity program. The motion passed by a unanimous voice vote.

### Investment Education

R V Kuhns provided an educational session relating to the firm's investment manager search and due diligence process. Documentation is on file.

### **RECESS**

The meeting recessed at 5:10 p.m. and reconvened at 8:05 a.m. the following day.

### Union Grove Venture Partners – Private Equity

Representatives of Union Grove Venture Partners presented an investment opportunity in Union Grove Venture Partners Fund I, L.P. to fund investments in venture capital funds and direct co-investments in venture capital companies. Their presentation booklet is on file. Staff provided an overview of the firm and due diligence that was conducted. A motion was made by Mike Busby, seconded by Sharon Leggett, that the committee recommend to the Board to commit \$100 million to Union Grove Venture Partners Fund I, L.P. The motion passed by a unanimous voice vote.

### Lightspeed Venture Partners – Private Equity

Representatives of Lightspeed Venture Partners presented an investment opportunity in Lightspeed Venture Partners X, L.P. and Lightspeed Venture Partners Select, L.P. to fund investments in technology companies. Their presentation booklet is on file. Staff provided an overview of the firm and due diligence that was conducted. A motion was made by Cinda Klickna, seconded by Mark Bailey, that the committee recommend to the Board to commit up to \$30 million between Lightspeed Venture Partners X, L.P. and Lightspeed Venture Partners Select, L.P. The motion passed by a unanimous voice vote.

### **RECESS**

The meeting recessed at 9:18 a.m. and reconvened at 9:37 a.m.

### Black Diamond Thematic – Absolute Return

Representatives of Carlson Capital presented an additional investment opportunity in Black Diamond Thematic. Their presentation booklet is on file. Staff provided an overview of the due diligence that was conducted. Staff recommended an additional \$100 million investment to Thematic in addition to the \$50 million that was invested in June 2013. This increase in allocation is in line with staff's effort to concentrate the portfolio into high conviction managers and away from funds of funds allocations. A motion was made by Cinda Klickna, seconded by Sonia Walwyn, that the committee recommend to the Board to approve and increase the allowable allocation to Carlson Black Diamond Thematic from \$50 million up to \$150 million. The motion passed by a unanimous voice vote.

### STARS Composite Exemption – Fixed Income

Staff noted that the cash component of fixed income recently exceeded the 10% maximum the Board approved in February 2013. Staff requested a temporary exemption to the 10% maximum for a period not to exceed six months. A motion was made by Bob Lyons, seconded by Mike Busby, that the committee recommend to the Board to ratify the temporary exemption to the 10% cash reserve maximum pending rebalance/funding of new mandates and/or other portfolio cash needs. The motion passed by a unanimous voice vote.

### Revised Investment Management Agreement – Fixed Income

TRS staff, external investment managers, and internal/external counsel reviewed and recommended revisions to the TRS Investment Management Agreement (IMA). The purpose is to ensure the IMA is in line with current legal and regulatory requirements, ensuring the System is following best practices and to address manager comments or concerns. Staff provided a summary of the primary changes to the IMA. A motion was made by Bob Lyons, seconded by Sharon Leggett, that the committee recommend to the Board to approve revisions to the IMA, as presented. The motion passed by a unanimous voice vote.

Prior to 2000, changes to the IMA were handled internally by TRS staff, with the Board approving only changes to the Investment Policy. From 2000 to present, the Board is required to approve the IMA in its final format. Going forward, staff and legal counsel believe formal Board approval of the IMA should no longer be a requirement, but staff would disclose IMA changes to the Board instead of a formal approval process. Following discussion, the Investment Committee chose to continue the current process related to Board approval of IMA changes.

### Barclays – Benchmark Change – Fixed Income

Staff reported that Barclays officially switched the index name from the Barclays Global Inflation-linked index to the Barclays World Inflation-linked index. This change will be reflected in the contracts of existing mandates PIMCO and New Century Advisors. Going forward (retroactive to January 1, 2014) the benchmark will be a hybrid of the former Global Index and the World Index. A motion was made by Cinda Klickna, seconded by Marcia Campbell, that the committee recommend to the Board to approve

the index name change as noted. The motion passed by a unanimous voice vote.

### Oaktree Capital Management – Fixed Income

Representatives of Oaktree Capital Management presented an investment opportunity in Oaktree Enhanced Income Fund II, L.P. to fund investments in senior loans. Their presentation booklet is on file. Staff provided an overview of the firm and due diligence that was conducted. A motion was made by Mark Bailey, seconded by Mike Busby, that the committee recommend to the Board to commit \$100 million to the Oaktree Enhanced Income Fund II, L.P. The motion passed by a unanimous voice vote.

### **RECESS**

The meeting recessed at 10:40 a.m. and reconvened at 1:05 p.m.

### Apollo Global Management – Fixed Income

Representatives of Apollo Global Management proposed a customized separate account portfolio within the global fixed income asset class. Their presentation booklet is on file. Staff provided an overview of the firm and due diligence that was conducted. A motion was made by Mike Busby, seconded by Bob Lyons, that the committee recommend to the Board to select Apollo to manage a \$250 million customized separate account within the global fixed income asset class. In addition, commit \$250 million to a separate account to target credit investments with high-teens net returns. The motion passed by a unanimous voice vote.

### State Street Global Advisors (SSgA) – Cash Management

TRS staff attempted to negotiate a different mechanism within cash management to allow more flexibility within the TRS cash management program. Staff was unable to come to contract terms with SSgA and recommended tabling the recommendation to select SSgA for an enhanced cash mandate. A brief discussion was held regarding staff's frustration with the contract review and negotiation process with State Street.

Staff and State Street custody also recommended the removal of the Liquidity Management Control System (LMCS), an off-shore vehicle on State Street's balance sheet that pays a lower rate than the Short-term



Investment Fund (STIF) fund. Staff proposed the Interest Bearing Demand Deposit Account (IBDDA) as a replacement for LMCS and noted the benefits. A motion was made by Marcia Campbell, seconded by Mark Bailey, that the committee recommend to the Board to approve the removal of the State Street LMCS and to alter from LMCS into the IBDDA platform effective upon completion of all necessary documentation. The motion passed by a unanimous voice vote.

### Fixed Income Targets


Due to the additions of Apollo and Oaktree within the global fixed income asset class, staff recommended minor internal target changes.

- Decrease Dolan McEniry from 5.0% to 4.0%
- Decrease MacKay Shields from 12.5% to 12.0%
- Decrease PIMCO Core Plus from 17.5% to 17.0%
- Decrease Loomis Sayles from 10.5% to 10.0%
- Decrease Franklin Advisors EMD from 7.5% to 7.0%
- Increase allocation to Special Situations from 9.0% to 12.0%

A motion was made by Marcia Campbell, seconded by Rainy Kaplan, that the committee recommend to the Board to approve the revisions to the global fixed income targets, as presented. The motion passed by a unanimous voice vote.

### **ADJOURNMENT**

There being no further business to come before the Investment Committee, a motion was made by Mike Busby, seconded by Marcia Campbell, to adjourn the meeting at 2:35 p.m.



Richard W. Ingram, Executive Director

Approved 5/28/14