South Carolina Retirement System Investment Commission
Meeting Minutes

April 21, 2016
9:30 a.m.
Capitol Center
1201 Main Street, 15th Floor
Columbia, South Carolina 29201
Meeting Location: Presentation Center

Commissioners Present:
Mr. Edward Giobbe, Chairman
Dr. Rebecca Gunnlaugsson, Vice Chair
Ms. Peggy Boykin
Mr. Allen Gillespie
Dr. Ronald Wilder
Mr. Reynolds Williams, (via telephone)
Mr. Curtis Loftis, State Treasurer

Others present for all or a portion of the meeting on April 21, 2016: Ashli Aslin, Geoff Berg, JP Boyd, Betsy Burn, Andrew Chernick, Lily Cogdill, Kim Cornell, Greg Cowell, John Farmer, Robert Feinstein, Scott Forrest, Mitchell Goldsmith, Joshua Greene, Michael Hitchcock, Lynn Lesueur, Kevin Matherly, Steve Marino, Tricia Miller, Bryan Moore, Kathleen Shealy, and Justin Young from the South Carolina Retirement System Investment Commission; Clarissa Adams, Bert Cassell, Edward Frazier, and Allen Townsend from the State Treasurer's Office; Suzanne Bernard and Tim McEnery from Aon Hewitt Investment Consulting; Tammy Nichols and Faith Wright from the South Carolina Public Employee Benefit Authority; Wayne Pruitt from the State Retirees Association of South Carolina; Madeleine Lee from Southern Strategy Group; Bruce Crouch, Jared Nobles, Tom Posey and Stephen G. Younts from SC ETV; and M. Sean Cary from Creel Court Reporting.

I. CALL TO ORDER AND CONSENT AGENDA

Chairman Edward Giobbe called the meeting of the South Carolina Retirement System Investment Commission ("Commission" or "RSIC") to order at 9:32 a.m. The Chairman referred to the proposed meeting agenda and asked for a motion to adopt the agenda. Mr. Allen Gillespie made a motion to adopt the agenda as presented, Dr. Ronald Wilder seconded the motion, which was unanimously approved, with Mr. Reynolds Williams being absent.

The Chairman asked for a motion to approve the Minutes of the Commission Meetings held on January 4, 2016 and February 4, 2016, as presented. Dr. Wilder made a motion to adopt the Minutes, and Dr. Rebecca Gunnlaugsson seconded the motion, which was unanimously approved, with Mr. Gillespie abstaining and Mr. Williams being absent.

II. CHAIRMAN'S REPORT

The Chairman recognized Mr. John Farmer, Human Resources Director, who stated that the Commissioners would receive the annual Commission Evaluation Discussion Guide via an email link. Mr. Farmer requested the Commissioners provide their feedback via the online survey as soon as possible in order for the results to be tabulated before the June 2016 Meeting.

Mr. Michael Hitchcock, Chief Executive Officer, reviewed the Commission's procedures for the nomination for Chair and Vice Chair, reminding the Commissioners that nominations would be made during this meeting, with the voting to take place at the June, 2016 Commission meeting. Dr. Wilder moved to nominate Dr. Gunnlaugsson to serve as Chairperson for the Commission term commencing on July 1, 2016 and ending June 30, 2018. Mr. Gillespie seconded the nomination. Dr. Gunnlaugsson moved to nominate Dr. Wilder to serve as Vice Chairperson for the Commission for the term commencing on July 1, 2016 and ending on June 30, 2018, Mr. Gillespie seconded the nomination.

III. CEO's REPORT

Mr. Hitchcock provided an overview of his recent meeting with the State Financial Affairs Authority and his appearance before the Senate Finance Committee. Mr. Hitchcock described both meetings as having robust discussions that allowed him the opportunity to explain the new direction of the RSIC and Commission with regards to the Portfolio.

Dr. Wilder inquired about the status of the CIO search. Mr. Hitchcock updated the Commissioners on the timing of the Charging Panel meeting, and the process for the Charging Panel to internally score the solicitations.

Mr. Curtis Loftis asked for more detail about Mr. Hitchcock's meeting before the Senate Finance Committee. Mr. Hitchcock stated that there was some discussion on implementing an increase to the employee contribution. There was also discussion of how and why the RSIC has been underperforming and how that has and will affect the budget writers and state employees this year as well as next year. Mr. Hitchcock explained that the RSIC has owned its partial responsibility for the unfunded liability deficit. Mr. Loftis noted that the debt must be looked into and funds are needed for this year. He further stated that if something is not done this year by the General Assembly it would lead to bigger problems in years to come. The Chairman announced that the Treasurer has performed a valuable service to the Commission by pointing out what should be done and what needs to be done and thanked him for his service.

At 9:46 a.m., Mr. Reynolds Williams joined the Meeting by teleconference.

Next, the Chairman requested a Motion on the Iran/Sudan Divestment Policies that were presented at the last Meeting. Mr. Loftis moved the Commission to (1) approve the recommendations of the CEO and the Acting CIO to adopt the Sudan and Iran Divestment Policies ("Policies") for inclusion in the SIOP; (2) Authorize the CEO and Acting CIO to take any and all action in accordance with and in furtherance of the objectives of the Policies; (3) Direct Staff to make any technical revisions or formatting edits to the Policies and other RSIC policy documents consistent with the Policies; and Reaffirm the SIOP, as amended, Mr. Gillespie seconded the motion, which passed unanimously (6-0).

IV. ACTING CIO's REPORT

Mr. Geoff Berg, Acting Chief Investment Officer, began his presentation by introducing Mr. Tim McEnery from Aon Hewitt, who presented a brief overview of the global economic environment.

A. RSIC Performance Summary

Mr. Berg began his performance update for the fiscal year through February, 2016 with a general overview of market performance, noting that real estate and investment grade fixed income were the only outperformers for the period. Turning to the Fund's performance for the period, Mr. Berg noted that the Fund is not outperforming its policy benchmark. Mr. Berg also pointed out that over the previous five years, only private equity and real estate benchmarks generated a return in excess of the assumed rate of return.

Mr. Berg noted that the mixed credit portfolio is not performing well. To this end, he stated that the restructuring of the asset class is now roughly two-thirds completed, and he expected that the performance will improve. Mr. Berg summarized by stating that he believed the restructuring will leave RSIC with a portfolio that will perform better and cost less than the portfolio did in 2014.

Next, Mr. Berg reviewed the GAA portfolio, noting that it had experienced a very disappointing three year period. He noted that a portion of the underperformance was due to the managers getting into emerging markets too early, while another cause of the underperformance had been certain managers' use of risk parity investing. Mr. Berg explained that risk parity tends not to do very well in periods where equities significantly outperform fixed income. Mr. Berg noted that Staff was currently conducting an internal evaluation of this entire asset class.

Lastly, Mr. Berg reviewed the private debt asset class, which had also underperformed fiscal year to date. He noted that Staff was shifting the private debt asset class into higher quality, more senior debt strategies, rather than the subordinated credit securities which the asset class had focused on previously.

Mr. Berg also reviewed the real estate portfolio and recognized Mr. Eric Rovelli, Senior Officer for Real Estate, for his work in this category. Mr. Berg stated that the real estate portfolio had performed particularly well since the prior recession. He noted that the RSIC had employed a more aggressive approach to seize the opportunity provided by the financial crisis.

Mr. Berg then discussed a project that Staff had undertaken related to private equity. He reminded the Commission that they had approved a floating target for the private equity class at a prior meeting. Mr. Berg indicated that Staff was working to enhance its quantitative underwriting of private equity strategies. The major goals of this project include (a) understanding the true value drivers responsible for prior performance, (b) supporting the previously-stated goal of requiring greater-conviction for private markets investments, and (c) enabling the program to pursue fewer, more concentrated relationships in order to achieve better economics.

Mr. Berg further stated that a great deal of money was flowing into this asset class, which may present challenges for both managers and investors. He indicated that Staff was evaluating different approaches toward co-investments and discussed the attractiveness of investing in private equity with no fee or carried interest.

B. EnTrust Consent

Mr. Berg explained that one of the Fund's strategic partners, EnTrust Capital, announced a plan to merge with the Permal Group ("Permal"). He noted that Permal had been acquired by Legg Mason in 2005. The new entity will be called EnTrust Permal and will increase EnTrust's assets under management from approximately $12 Billion to $30 Billion, making it one of the largest hedge funds investors in the world. Mr. Berg noted that SEC rules require that EnTrust seek RSIC's consent to assign the investment advisory function from EnTrust to EnTrust Permal. Mr. Gillespie made a motion to adopt the recommendation of the Acting CIO to (i) consent to the assignment of the investment advisory function with respect to EnTrust Palmetto LLC and EnTrust Palmetto Strategic Partnership LP from EnTrust to EnTrustPermal and (ii) authorize the Chairman or his designee to execute any necessary documents to implement the decision as approved by the Commission. Dr. Wilder seconded the motion, which was unanimously approved.

C. Approval of AIP for Fiscal Year 2016-2017

Mr. Berg thanked the Commission for their feedback and summarized the changes to the draft Annual Investment Plan ("AIP") which had been presented at the February 25, 2016 meeting. The first change reviewed was the addition of a paragraph providing context and background information for proposed strategic initiatives. Mr. Berg also noted that another paragraph had been added to the section of the AIP identifying two objectives for all asset classes. First, Mr. Berg noted that Staff will continue working to reduce the total number of relationships with investment managers, with the goals of consolidating assets with those managers in which the team has the highest conviction, and improving the cost of the investment program. In order to achieve this first objective, Mr. Berg noted that Staff will focus on developing a robust assessment of the key value drivers for these strategies. Mr. Berg reminded the Commission that this document needs to be approved by May 1, 2016 and will go into effect as of July 1, 2016 per the statutory requirement.

Mr. Gillespie moved to adopt the recommendation of the Acting CIO and Staff to approve the proposed AIP dated April 21, 2016 as presented, and authorize Staff to finalize the AIP by making any technical revisions or formatting edits consistent with the action taken by the Commission. Dr. Gunnlaugsson seconded the motion, with Mr. Loftis opposed (5-1).

Mr. Loftis discussed the actions of the Senate Finance Committee and stated that he felt that there needed to be a discussion about the SIOP and AIP line by line in order to highlight his historic objections to the asset allocation decisions made by the RSIC. Mr.

Hitchcock made some suggestions as to how to capture Mr. Loftis' request and noted that Staff would follow up with Mr. Loftis after the meeting. Mr. Hitchcock also reminded the Commission that they have the authority to revise the AIP whenever necessary throughout the year.

Mr. Berg introduced Ms. Bernard to present a preliminary discussion on benchmarks and noted that this item was being presented for discussion purposes only at this meeting. Ms. Bernard explained that any changes approved at a subsequent meeting would go into effect on July 1, 2016. Ms. Bernard discussed each of the recommended benchmarks, highlighting instances where changes were being proposed to existing benchmarks, as well as instances where benchmarks were being proposed for new asset classes and strategies (equity options strategies, portable alpha, other opportunistic, REITs and infrastructure). A discussion ensued regarding the recommended changes and related topics.

A brief recess was taken from 11:30 a.m. to 11:40 a.m.

V. INVESTMENT RECOMMENDATIONS

A. Equity Options Strategies

Mr. Berg provided a summary of the Portfolio's existing equity exposure and current market conditions. He noted that the Portfolio had been underweight to equity – specifically, U.S. equity – by roughly 15 percent relative to other pension funds, and reminded the commissioners that the asset allocation adopted in February 2016 included a five percent allocation to equity options strategies. Given its assessment of current conditions in the market, Mr. Berg noted that Staff had extensively researched and developed two initial proposals for implementing equity options strategies in the Plan.
Mr. Berg introduced Mr. Steve Marino, Senior Investment Officer, to present the two recommendations for the Commission's review. Mr. Marino noted that, as a result of its challenging beliefs review, Staff determined that the Plan would benefit from more equity-like returns, but recommended that this be accomplished without incurring full equity market downside exposure. Mr. Marino noted that Staff had identified strategies which should outperform the CBOE Buy-Write Index ("BMX Index") through a full market cycle, while minimizing equity drawdown risk. Mr. Marino recommended two managers to implement the Equity Options Strategy:

B. Russell Implementation Services, Inc.:

Russell Enhanced Put Write Strategy – Mr. Marino presented a detailed explanation of the elements of this systematic enhanced put writing strategy to the commissioners. He noted that the goal of this strategy was to minimize unintentional risks from strike date selection, and thereby generate 200 basis points of excess returns versus the BMX Index with improved downside characteristics. Mr. Marino explained that selling a more diversified set of options should help generate additional returns through diversification. Mr. Marino provided a ten (10) year total return historical performance for Russell, detailed Russell's extensive experience and resources in managing $72 billion in derivative overlay assets and $5 billion in options strategies, and noted that the proposed fee was approximately 15 basis points (on a blended fee basis) for a $600 million dollar allocation. Mr. Marino concluded by noting that Staff recommended investing of up to 3% of Plan assets in the Russell Enhanced Put Write Strategy in a separately managed account, with custody provided by The Bank of New York Mellon.

C. AQR AERO Composite Strategy:

Mr. Marino then presented the second recommended equity options strategy, AQR's AERO Composite Strategy. He provided background information regarding the firm, its resources and history, and noted that this strategy would consist of investments into two commingled vehicles managed by AQR. The first component of the strategy, Mr. Marino explained, was the AQR Style Premia U.S. Equity Beta 1, L.P. ("SP US"). Mr. Marino summarized the function that the SP US component would play in AQR's equity options strategy, and noted that AQR would aim to maintain a consistent 55 percent equity exposure in this component of the strategy. Mr. Marino then explained the second component of the strategy, the AQR Volatility Risk Premium Master Account, L.P. ("VRP"). He summarized the function that the VRP component would serve in the strategy, and noted that the manager would aim to invest approximately 45 percent of the strategy in VRP. Mr. Marino then summarized the rationale behind AQR's equity options strategy, noting that it should (i) provide returns superior to the BMX Index through structural enhancements, (ii) enhance premium collection through market diversification, and (iii) enhance returns through security selection.

Mr. Marino noted that Staff recommended investing up to three percent (3%) of Plan Assets into the AQR AERO Composite Strategy, consisting of the two underlying commingled vehicles (SP US and VRP), with a separately managed account governing the relationship and the rebalancing between the two commingled vehicles. Mr. Marino noted that the custodian for this mandate would be State Street, and stated that there would be a 45bps blended fee on a $600 Million allocation. Mr. Marino also noted that there would be a 10bps cap on operating expenses at the commingled fund level. Mr. Loftis stated his concerns about too much volatility and the RSIC's history with investing in this type of strategy. Mr. Marino responded by stating that the returns should be equity-like, noted that these strategies should perform well in sideways or down markets. Additional discussion ensued.

Regarding the Russell recommendation, Mr. Gillespie moved that the Commission:

(a) Adopt the recommendation of the Acting CIO and the Internal Investment Committee as set forth in the Summary Terms Chart on Page 1 of the Due Diligence Report dated April 21, 2016;
(b) Authorize an investment of up to 3% of Total Plan Assets into the Russell Enhanced Put Write Strategy through the use of a separately management account agreement (the "Investment");
(c) Authorize the Chairman or his designee to negotiate and execute any necessary documents to implement the Investment as approved by the Commission (1) upon documented approval for legal sufficiency by RSIC Legal, and (2) upon expiration of the three business day review period as approved by the Commission on May

1, 2014 (or as the review period may be amended or superseded by the Commission); and

(d) Authorize the Chairman and/or the Acting CIO or their designee(s) to thereafter authorize the custodian of funds to transfer such funds as are necessary to meet the Retirement System trust funds' obligation with respect to the Investment.

Dr. Wilder seconded the motion, which was unanimously approved (6-0).

Regarding AQR Capital Management, Mr. Gillespie moved that the Commission:

(a) Adopt the recommendation of the Acting CIO and the Internal Investment Committee as set forth in the Summary Terms Chart on Page 1 of the Due Diligence Report dated April 21, 2016;

(b) Authorize an investment of up to 3% of Total Plan Assets into the AQR AERO Composite Strategy governed by an investment management agreement. The Strategy will invest in, and rebalance between, two commingled funds: AQR Equity Style Premia U.S. Equity Beta Master Account, L.P. and the AQR Volatility Risk Premium Master Account, L.P. (name subject to change)(collectively, the "Investment");

(c) Authorize the Chairman or his designee to negotiate and execute any necessary documents to implement the Investment as approved by the Commission (1) upon documented approval for legal sufficiency by RSIC Legal, and (2) upon expiration of the three business day review period as approved by the Commission on May 1, 2014 (or as the review period may be amended or superseded by the Commission; and

(d) Authorize the Chairman and/or the Acting CIO or their designee(s) to thereafter authorize the custodian of funds to transfer such funds as are necessary to meet the Retirement System trust funds' obligations with respect to the Investment.

Dr. Rebecca Gunnlaugsson seconded the motion, which unanimously passed (6-0).

D. Deutsche Global Infrastructure Securities

The Chairman recognized Mr. Berg, who provided a brief overview of the asset allocation adopted by the Commission in February 2016, including an eventual 3% allocation to infrastructure phased in at 1% per year over the next three years. Mr. Berg noted that Staff had determined to first seek funding of a listed infrastructure mandate, which would provide flexibility, exposure and liquidity as the infrastructure portfolio was built out with other investments, including closed end and open end funds.

Mr. Berg then introduced Ms. Ashli Aslin, Investment Officer, who presented the Deutsche Global Infrastructure Securities recommendation. Ms. Aslin summarized the benefits and characteristics of listed infrastructure, noted the expected return range for listed infrastructure (in comparison to other types of infrastructure investments), and summarized the search process. Ms. Aslin concluded by noting that Staff was recommending an investment of up to 2.5 percent of Plan assets in the Deutsche Global Infrastructure Securities strategy (with an initial estimated funding of approximately $275 million or 1 percent of Plan assets), that will be executed through a separately managed account, with a negotiated blended fee of no greater than 55 bps. Ms. Aslin also noted that Aon Hewitt had given a qualified rating, and that The Bank of New York Mellon will be the custodian.

After a brief discussion, Mr. Gillespie moved the Commission to:

(a) Adopt the recommendation of the Acting CIO and the Internal Investment Committee as set forth in the Summary Terms Chart on Page 1 of the Due Diligence Report dated April 21, 2016;

(b) Authorize an investment of up to 2.5% of Total Plan Assets into the Deutsche Global Infrastructure Securities through the use of a separately managed account agreement, with an anticipated initial investment of $275 million (the "Investment");

(c) Authorize the Chairman or his designee to negotiate and execute any necessary documents to implement the Investment as approved by the Commission (1) upon documented approval for legal sufficiency by RSIC Legal, and (2) upon expiration of the three business day review period as approved by the Commission on May 1, 2014 (or as the review period may be amended or superseded by the Commission); and

(d) Authorize the Chairman and/or the Acting CIO or their designee(s) to thereafter authorize the custodian of funds to transfer such funds as are necessary to meet the Retirement System trust funds' obligations with respect to the Investment.

Dr. Wilder seconded the motion which was unanimously passed (6-0).

VI. EXECUTIVE SESSION

Mr. Gillespie moved to go into Executive Session and discuss investment matters pursuant to S.C. Code Sections 9-16-80 and 9-16-320 and to receive legal advice from legal counsel pursuant to S.C. Code Section 30-4-70(a)(2). Dr. Wilder seconded the motion, which passed unanimously. The Commission reconvened in open session. Mr. Hitchcock reported that no action was taken during Executive Session.

VII. ADJOURNMENT

There being no further business, Mr. Loftis moved to adjourn. Mr. Gillespie seconded the motion, which passed unanimously, and the meeting adjourned 2:31 p.m.

[Staff Note: In compliance with S.C. Code Ann. Section 30-4-80, public notice of and the agenda for this meeting were delivered to the press and to parties who requested notice and were posted at the entrance, in the lobbies, and near the 15th Floor Presentation Center at 1201 Main Street, Columbia, SC, at 8:32 a.m. on April 19, 2016.]

Approved by the Commission on June 16, 2016, subject to the addition of an addendum to be provided by the State Treasurer at a later date