

MINUTES OF THE
NEW MEXICO EDUCATIONAL RETIREMENT BOARD
INVESTMENT COMMITTEE

September 21, 2018

1. a. CALL TO ORDER

A meeting of the New Mexico Educational Retirement Board Investment Committee was called to order on this date at 9:30 p.m. in the Educational Retirement Board Conference Room, 6201 Uptown Boulevard, N.E., Ste. 203, Albuquerque, New Mexico.

Members Present:

Mr. H. Russell Goff, Chair
Ms. Mary Lou Cameron
Mr. Larry Magid

Members Excused:

None.

Staff Present:

Ms. Jan Goodwin, Executive Director
Mr. Rick Scroggins, Deputy Director
Mr. Mark Canavan, Real Estate Portfolio Manager
Mr. Steve Neel, Deputy CIO, Alternative Assets
Mr. Rod Ventura, General Counsel
Mr. G. Alan Myers, Public Securities & Debt Portfolio Manager

Others Present:

Mr. Steve Gruber, Hamilton Lane
Mr. Sam Austin, NEPC
Ms. Charmaine Clair for Judith S. Beatty, Recorder

b. Approval of Agenda

Ms. Cameron moved approval of the agenda, as published. Mr. Magid seconded the motion, which passed unanimously.

c. Approval of Minutes: August 23, 2018

Mr. Magid moved approval of the August 23, 2018, minutes, as submitted. Ms. Cameron seconded the motion, which passed unanimously.

d. Introduction of Guests

Chairman Goff welcomed staff.

2. LONE STAR FUND XI, REAL ESTATE

[Presenters: Mark Canavan; Steve Gruber, Hamilton Lane]

Mr. Canavan presented staff's recommendation for a \$50 million commitment to Lone Star Fund XI.

-- Lone Star is seeking to raise Lone Star Fund XI, a distressed debt platform, which Lone Star has been investing in for the last 25 years.

-- The ERB is currently invested in the credit opportunity side in Lone Star Funds VIII, IX and X.

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-- ERB returns from the Lone Star funds to date range from 14.84 percent net to 46.57 percent net (70 percent gross).

-- On the commercial real estate side, the ERB is invested in Lone Star Funds II and V, which were related to commercial mortgage-backed securities in the United States. Lone Star is scaling down the size of these funds because of the size of the opportunity.

-- Fund XI represents a compelling opportunity to capitalize on dislocation and distress globally, particularly within Europe. The region is expected to comprise a majority of the Fund's activity. Targeted investments within the region include corporate and residential non-performing loans, equity investments in financial institutions, and corporate debt and equity investments.

Mr. Gruber noted that this is approximately the 14th time he has been involved in underwriting a Lone Star Fund since 1998, and he supported the recommendation. He commented that what was different about Lone Star is that, as the opportunity set moves around the world, Lone Star right-sizes and reorganizes its organization. Currently, there are about 100 people at Lone Star and about 800 at Hudson, its affiliate, which is also owned by Lone Star founder John Grayken. Since the ERB made its first commitment to Lone Star in 2010, only two people are the same at the senior level (President Andre Collin and Grayken) and this is largely due to the changing opportunity set.

Ms. Cameron noted language on the Important Disclosures page in the Hamilton Lane report stipulating that the information in the report would not be disclosed to a third party by the recipient of the report, meaning the ERB, and that Hamilton Lane would seek a protective order or other appropriate remedy if such disclosure were required by law. She asked if this is typical for the ERB.

Mr. Canavan responded that this is usually the case. The ERB does receive FOIA requests for proprietary information that, if disclosed, would be potentially harmful to the ERB's beneficiaries, and this language is in writing because Hamilton Lane is publicly traded.

Mr. Gruber stressed that Hamilton Lane tends to be very open and transparent, so FOIA requests are always an issue. He said they walk a fine line in disclosing everything they can in their reports while working with internal counsel and with Mr. Canavan to protect those reports.

Mr. Magid moved that the Investment Committee approve a commitment of \$50 million to Lone Star Fund XI for the Real Estate portfolio. The commitment is subject to New Mexico State Law, Educational Retirement Board policies, Educational Retirement Board approval for placement agents and negotiation of final terms and conditions, and completion of appropriate paperwork. In addition, the Investment Committee grants staff discretion to invest an additional amount, not to exceed \$10 million, in secondary partnership interests offered by other limited partners in the fund, should they become available from time to time. Ms. Cameron seconded the motion, which passed unanimously.

3. SUDAN INVESTMENT POLICY

[Presenter: G. Alan Myers]

Mr. Myers asked the Investment Committee to recommend to the board the suspension of the Sudan Divestment policy and direct staff to amend the NMERB investment policy to reflect that. He provided background regarding U.S. sanctions in response to terrorist organizations.

-- ERB joined the movement to divest in December 2007 and subsequently the policy was amended to include the restriction. In support of the restriction, staff submitted the EIRIS tier one list to all externally managed accounts and core fixed income accounts. Managers were required to certify they met the mandate.

-- When the third quarter 2018 list was published ERB core fixed income found GE had been added to the list. They have a controlling interest in Baker Hughes, an oil and gas services company with operations in Sudan. The fixed income portfolio currently has five Baker Hughes bonds included in the tier one list. Market value is \$1.5 million. GE is included in the EIRIS report but is not on the tier 1 list. The value of the GE holdings is \$9.8 million.

-- The environment in Sudan has improved over the last 10 years and President Obama lifted most sanctions on Sudan in January 2017. The target date was extended to October 2017; the Trade Department revoked the core U.S. sanctions on Sudan.

Mr. Myers commented that, considering there has been improvement in the humanitarian conditions in Sudan to the point that two different administrations have determined sanctions should be lifted, staff believes it would be appropriate for ERB to suspend the Sudan Divestment Policy and amend the Investment Policy to reflect this change at the next review.

Ms. Goodwin noted that Colorado PERA has done the same.

Responding to Chairman Goff, Mr. Myers said he did not know what other pension funds have followed suit, but he thought it instructive that two different government administrations, one Democratic and one Republican, had decided to lift the sanctions.

Mr. Austin stated that NEPC supports staff's recommendation. In general, NEPC believes that restricting investment managers from the full array of securities that they choose to invest in isn't optimal, according to portfolio investment theory. He said NEPC hasn't done a broad survey, but he could add Georgia's teacher retirement system and Georgia's employee retirement system to the list of funds that have revoked these restrictions.

Mr. Myers added that, while the ERB could easily divest from the fixed income bonds it owns at Baker Hughes, but it also owns Baker Hughes in the S&P 500, and it would have to sell those shares.

Ms. Goodwin commented that this goes back to the divestment discussion at the last board meeting. Selling those shares would mean the index fund, with 499 securities instead of 500, would always have tracking issues.

Ms. Cameron said she thought the suggested motion should be amended to state that the Investment Committee was not recommending approval, but was submitting this to the full board for consideration. She stated that the suggested motion implies that this is an Investment Committee decision and not a board decision.

Following discussion, Mr. Myers consulted the 2007 Board of Trustees minutes and noted a statement by Mr. Martin that "the Investment Committee met yesterday and recommended this divestment."

Mr. Magid moved that the Investment Committee recommend the Educational Retirement Board suspend the NMERB's Sudan Divestment Policy and direct staff to amend the NMERB Investment Policy to reflect this change.

The motion failed for lack of a second.

Ms. Cameron moved that the Investment Committee submit the suspension of NMERB's Sudan Divestment Policy to the board for consideration. Mr. Magid seconded the motion and the motion was passed unanimously.

4. OTHER REPORTS AND DISCUSSION

Mr. Neel reported that August preliminary numbers are up about 75 basis points.

Mr. Neel also noted that, with respect to the hurricane in the Carolinas, the committee may recall approving a reinsurance commitment fund last year, and it does not appear that the fund has been impacted. Most of the policies were wind related and not water related.

5. NEXT MEETING: THURSDAY, OCTOBER 18, 2018

[Time to be determined.]

ADJOURN

Its business completed, the Investment Committee adjourned the meeting at 10:35 a.m.

Accepted by:

H. Russell Goff, Chairman