NEW MEXICO EDUCATIONAL RETIREMENT BOARD

INVESTMENT COMMITTEE

TELEPHONIC/VIRTUAL MEETING

May 21, 2020

1. a. CALL TO ORDER

A meeting of the New Mexico Educational Retirement Board Investment Committee was called to order on this date at 1:10 p.m. via teleconference.

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. Rod Ventura, Deputy Director
Mr. Bob Jacksha, Chief Investment Officer
Mr. Steve Neel, Deputy CIO, Alternative Assets
Ms. Susanne Roubidoux, General Counsel
Mr. Aaron Armstrong, Portfolio Manager
Mr. Casey Poe, Compliance and Portfolio Manager

Others Present:
Mr. Allan Martin, NEPC
Mr. Sean Gill, NEPC
Mr. Steve Gruber, Hamilton Lane
Ms. Noi Spyratos, Caledon
Mr. Asif Hussain, Caledon
Mr. Teddy Haimes, Reporter, Financial Investment News
Mr. Max Rodriguez, Barings
Ms. Judith 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: April 16, 2020**

Mr. Magid moved approval of the April 16 minutes, as submitted. Ms. Cameron seconded the motion, which passed unanimously.

d. **Introduction of Guests**

Chairman Goff welcomed staff and guests.

2. RAITH NMERB CORE-PLUS SMA – REAL ESTATE

[Presenter: Steve Gruber, Hamilton Lane.]

Mr. Neel reviewed staff's recommendation of a $50 million commitment to Raith NMERB Core-Plus Separately Managed Account, to acquire and originate commercial real estate debt.

Through this customized account with ERB, Raith would originate and acquire first mortgage whole loans, subordinate loans, B-notes, mezzanine debt, rescue financing, investment grade and non-investment grade commercial mortgage backed securities, and other debt-related investments. ERB staff and Raith believe that the current market environment has created a significant investment opportunity for lenders with the ability to appropriately value and underwrite loans and securities on a one-off basis.

Raith Capital Partners co-founder and managing partner Bill Landis introduced himself and made a presentation. He said Raith has its own asset management team which looks after each individual investment in its portfolios, and constantly tracks markets in which it has exposure, and looks broadly for any changes in general market conditions. He said many members of the team go back to well before Raith was started, which provides a lot of stability. He noted that the transition to working from home during the COVID crisis was relatively seamless, and they were able to move everyone out of their New York City offices before March 10, when things became very bad in the city.

Mr. Landis said they anticipate a 10-12 percent gross return and do not anticipate the need for leverage. This will be an opportunity to team up with a lot of first mortgage lenders, namely on the banking side of the business, that may not want to lend beyond a 50 percent LTV of the asset, and Raith will be able to fill in that space of 50-65 percent.

Mr. Jacksha asked Mr. Landis to comment on how the strategy in this fund differs from the first two funds the ERB has committed to. Mr. Landis responded that the first fund, which was raised in 2013, focused on purely nonperforming debt, so they were cleaning up a lot of the bad debt that sat on the balance sheets of banks and insurance companies. Raith actually bought the debt with the intention of moving through the debt, foreclosing on it, and taking the real estate and repositioning it. He said this new fund is not a loan-to-own strategy, but a strategy to make a very solid investment with a good return on a very well structured piece of real estate.

Mr. Jacksha commented that the ERB has been invested with the Raith team for a number of years, and is taking advantage of their existing experience and tailoring this allocation to the current environment. This is a little different from the environment the ERB faced before, but this is a good strategy.

Mr. Gruber said this is an opportunity to generate equity-like returns from quality properties and quality sponsors on what people in the profession are calling "post COVID pricing" that allow Raith to structure these in a way that preserves capital and drives return. In these one-off transactions, recourse is not off the table, so there are additional ways beyond just having the real estate collateral to protect the capital invested. He said they feel they are exploiting inefficiencies in the market that have been driven by this crisis to generate attractive core-plus returns.

Ms. Cameron moved that the Investment Committee approve a commitment of $50 million to Raith Capital Credit Partners Separate Account 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, negotiation of final terms and conditions, and completion of appropriate paperwork. Mr. Magid seconded the motion, which passed unanimously.

3. **<u>INDUSTRY VENTURES SECONDARY FUND IV, LP – PRIVATE EQUITY</u>**

[Presenter: Steve Neel, Aaron Armstrong, and NEPC consultant Sean Gill.]

Mr. Neel stated that this would be the eighth commitment the ERB has made to Industry Ventures, with a total of about $250 million committed in different vehicles. Mr. Neel commented that this is a timely commitment for a number of reasons, including the fact that it has a distressed flavor, and deal flow tends to ramp up in secondary activity in times of distress, as occurred in 2008. He said the ERB appreciates secondaries across the private markets platform, particularly when there is inefficiency, which is definitely the case here.

Mr. Armstrong presented staff's recommendation of a $50 million commitment to Industry Ventures Secondary Fund IX for the Private Equity portfolio. He said the fund has a $750 million target and will make secondary investments in venture capital related assets, following a similar strategy to the predecessor funds.

Mr. Armstrong said the ERB has been active in the secondary markets since 2007 and continues to believe niche secondary market strategies present interesting opportunities for solid risk-adjusted returns, and with a reduced J-curve due to the timing of purchases. An efficient method to exit a private equity position early is for the seller to make buyers of these types of positions aware of its intentions and let them bid on the assets. Over the past ten years, many large firms have entered the market for this type of transaction as buyers; as a result, there has been a decline in information advantage coupled with an aggressive pricing structure, which the ERB believes has led to more efficient markets and thus reduced the opportunity for better returns. Industry Ventures targets smaller transactions that don't make sense to a mega-billion dollar fund, which allows the team to identify unique deal flow. The firm also targets the venture community, which historically has been difficult to access due to its closed-circle nature, and the team can go directly to the individual equity holder to negotiate a price, which would be more challenging to a larger firm. The fund has a net targeted IRR of 20 percent and a 2.0x net multiple on invested capital.

Mr. Armstrong stated that Industry Ventures has disclosed that no placement agent has been engaged with respect to the ERB, no campaign contributions were disclosed, and no investments in private prisons has been made and there is no intention of doing so in the future.

Mr. Gill said this is an attractive way to access venture-backed companies, and it mitigates some of the tail risk, or number of companies that face unprofitability. Over 75 percent of the deals in which Industry Ventures have done investments have been profitable, which is very different from a typical venture capital portfolio. In addition, the previous Industry Ventures funds have committed to more than 250 venture capital limited partnerships, cultivating relationships with the managers of these funds and others over the past 20 years. Economic uncertainties and declines in financial markets over the past couple of months have created liquidity challenges for many private equity investors, and secondary buyers in this environment are likely to find opportunities to purchase investments at attractive prices.

In discussing negatives, Mr. Gills said the firm's long-time managing director of secondaries, Victor Wang, is transitioning to another role and will not be involved in the investment of Fund IX. NEPC believes senior leadership is strong enough to make up for the departure. In addition, Fund IX's $750 million target is approximately 50 percent higher than the $513 million raised for Fund VIII, and no hard cap has yet been established; however, NEPC feels there will be a lot more opportunities in the current investment environment than there were in previous funds.

Mr. Neel said this is a longstanding and consistent performer for the ERB, and recommended approval.

Mr. Magid moved that the Investment Committee approve a commitment of $50 million to Industry Ventures Secondary Fund IX for the Private Equity portfolio. The commitment is subject to New Mexico State Law, Educational Retirement Board policies, Educational Retirement Board approval for placement agents, 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 Industry Ventures Secondary

Fund IX should they become available from time to time. Ms. Cameron seconded the motion, which passed unanimously.

4. Q1 PROXY VOTING REPORT

Mr. Jacksha stated that he saw nothing out of the ordinary in the report needing the committee's attention.

Ms. Cameron moved to accept the proxy voting report. Mr. Magid seconded the motion, which passed unanimously.

5. REAL ESTATE AND NATURAL RESOURCES COMPLIANCE REVIEW

[Presenter: Steve Gruber, Hamilton Lane]

Mr. Gruber stated that, Hamilton Lane normally would do the year-end report using the Q3 performance reports as a basis for comparison. Given the changes in the market, this review has been updated incorporating some of the more recent information. Hamilton Lane therefore used the year-end data from the managers, updating it for capital calls and distributions in the time period since, and also included 3/31 valuations provided by the public market investment managers, Brookfield Investment Management and Harvest Fund Advisors.

Mr. Gruber stated that all of the positions are within the policy framework established by ERB, requiring no corrective action. There were no issues to report. He added that, while exposure does occasionally bump up against the limitation at times, Mr. Jacksha and Mr. Canavan are well aware of this and keep an eye on it.

6. Q4 2019 INFRASTRUCTURE REPORT

[Presenters: Bob Jacksha and Caledon consultants Noi Spyratos and Asif Hussain.]

Executive Summary items:

- Portfolio Fair Value: $455,571,036
- Unfunded Commitments: $175,183,204
- Total Number of Fund Investments: 12, across 7 GP relationships
- Total Number of Direct Investments: 18
- Net IRR since inception: 7.2 percent with over $700 million committed

Mr. Jacksha said the program is doing well, despite a slow start in 2008, the year of inception. Since then, most returns are in the double digits and high single digits. Co-investments have done quite well overall.

Ms. Spyratos shared insight on how some of the funds are expected to perform in the current market environment due to the COVID-19 crisis along with the recent drop in oil prices. Caledon has had discussions with each of its general partner relationships to understand what the potential impact is expected to be on their portfolios, and has done the same with all of the co-investments in the Andromeda Co-Investment Fund, and will continue to receive updates from them as the situation evolves. She commented that Caledon expects the portfolio to do quite well overall. In particular, the Stonepeak fund has meaningful exposure to digital infrastructure, and there are also a couple of strong digital infrastructure investments within the Andromeda Fund. This sector is expected to perform better coming out of this crisis given that more and more businesses have greater needs for data as people work from home. In addition, some exposures are in the midstream energy sector, and one good thing is that the majority of the energy exposure is through preferred instruments, so there is no direct exposure to commodities. Areas of potential weakness, with possible write-downs in 2021-22, are almost exclusively in the earlier fund commitments to the Alinda Infrastructure Fund II and Alterna Core Capital Assets Fund I and II. With respect to Alterna, much of their portfolio is invested in the aircraft leasing space, a sector that is experiencing some pressure, and Alinda is also expected to experience pressure due to the drop in oil prices, as much of the portfolio is exposed to midstream assets. These three funds represent about 10 percent exposure of the total infrastructure program, a relatively small portion of the portfolio.

Mr. Hussain gave an overview of performance. While there is a heavy weighting toward energy in the portfolio, Caledon expects that to decrease over time as the portfolio becomes more diversified.

7. Q1 COMMISSION REPORTS

[In packet as informational item.]

8. OTHER REPORTS AND DISCUSSION

The committee agreed that, since it has been two years since the last discussion about the delegation of investment responsibilities and authority to staff, this would be revisited in July by the Investment Committee and in August by the Board of Trustees.

9. NEXT MEETING: THURSDAY, JUNE 18, 2020

The meeting was scheduled on 1:00 p.m.

ADJOURN

The meeting adjourned at 2:10 p.m.

H. Russell Goff, Chairman