

**DRAFT**

**INVESTMENT SUBCOMMITTEE OF THE NORTH CAROLINA SUPPLEMENTAL  
RETIREMENT BOARD OF TRUSTEES**

**MINUTES OF MEETING**

**May 17, 2017**

**Time and Location:** Investment Subcommittee (the “Subcommittee”) of the North Carolina Supplemental Retirement Board of Trustees (the “Board”) met at 9:00 a.m. on Wednesday, May 17, 2017, in the Dogwood Conference Room of the Longleaf Building, 3200 Atlantic Avenue, Raleigh, North Carolina.

**Members Present:** The following members were present: Melinda Baran (Chair), Karin Cochran. Hal McKinney attended via phone.

**Staff and Guests present:** The following staff and guests attended the meeting. From the Department of State Treasurer (the Department): Dale R. Folwell, CPA, Steve Toole, Reid Chisholm, Mary Buonfiglio, Kevin SigRist, Mary Laurie Cece, Casey High, Loren de Mey, Rekha Krishnan, Catherine Jarboe, Maja Moseley, Patti Hall, Sam Hayes, and Fran Lawrence. From Mercer: Liana Magner and William Dillard. From Prudential: Michael McCann; Ann Cashman and Jessica Quimby via phone. From Galliard: William Weber.

**AGENDA ITEM – WELCOME AND INTRODUCTIONS**

Meeting convened at 9:00 a.m.

Ms. Baran, the Chair, welcomed the Treasurer, staff and guests.

**AGENDA ITEM – ETHICS AWARENESS AND IDENTIFICATION OF CONFLICTS  
OR POTENTIAL CONFLICTS OF INTEREST**

The Chair asked Subcommittee members to review the meeting agenda and identify any actual, implied or potential conflicts of interest. There were no conflicts identified.

**AGENDA ITEM – MINUTES FROM FEBRUARY 15, 2017 INVESTMENT  
SUBCOMMITTEE MEETING**

The Chair stated that the minutes already have been approved and are included for reference only. No action is needed.

## **AGENDA ITEM – POLICY AND PROCEDURES FOR INVESTMENT TRANSACTION AND INVESTMENT MANAGER SELECTION**

The Chair recognized Mr. Chisholm who directed the Subcommittee members' attention to the policy draft (included in the meeting materials). He noted that the policy describes the selection of investment managers, and the Board's procedure to delegate this duty to the Department's Investment Management Division and the Supplemental Retirement Plan's (SRP) Investment Consultant.

The Chair entertained a motion to approve the policy and Ms. Cochran so moved. Mr. McKinney seconded, and the motion passed unanimously.

## **AGENDA ITEM – PLAN DESIGN RECOMMENDATION**

The Chair recognized Mr. SigRist and Ms. de Mey. Ms. de Mey summarized the recommendation for Large Cap Core and SMID Cap Core Funds, noting that a formal recommendation regarding specific investment managers will follow during the SRP Board meeting scheduled for June 22nd. She added that, while SRP's Investment Consultant, Mercer, will present the details of the recommendation, the staff did work closely with the Investment Consultant on this recommendation. In addition, she noted that manager fee negotiations have been captured in the recommendation memorandum. Details regarding estimated fees will be provided by the staff, as amendments to investment management agreements currently are being finalized.

Next, Ms. Magner presented the current investment lineup, the recommendation and background information for the Large Cap Core Fund analysis and the Small/Mid Cap Core Fund analysis. She also described Mercer's research methodology and shared various GoalMaker allocation scenarios, by way of example. The recommendations were as follows:

- Consolidate the NC Large Cap Value Fund and NC Large Cap Growth Fund into a single NC Large Cap Equity Fund;
- Consolidate the NC Small/Mid Cap Value Fund and the NC Small/Mid Cap Growth Fund into a single Small/Mid Cap Equity Fund; and
- Add a liquidity sleeve within both funds – 25% of the NC Large Cap Equity Fund and 5% of the Small/Mid Cap Core Fund.

Ms. Magner emphasized the fee reduction in the Large Cap Core Fund will be approximately 29 basis points, caused by the addition of the Russell 1000 index fund and negotiated fee reductions with current investment managers. A discussion followed, regarding potential risks in the portfolio. Mr. SigRist noted that in the long term, it is difficult to beat the benchmark in the large cap space, and noted that large cap investment managers do not have the same forward-looking potential to outperform their respective benchmarks compared to small/mid cap managers. Ms. Magner added that the addition of index options will also mitigate volatility. Subcommittee

members requested that Mercer prepare and present an analysis of the proposed large-cap product performance versus a market benchmark to show how there can be long periods of underperformance versus the benchmark given the highly efficient characteristics of U.S. large cap stock markets. Mr. SigRist confirmed that the staff would collaborate with Mercer to prepare such analysis.

Ms. Magner continued to the recommended NC Small/Mid Cap Fund and described the investment styles of current managers. She explained that Mercer recommends retaining all existing managers and adding a five percent liquidity sleeve. Ms. Magner added that recent fee negotiations conducted by staff resulted in an estimated fee of 53 basis points for the proposed NC Small/Mid Cap Fund which represents a reduction of 10 basis points.

The Treasurer inquired about the effective date of these proposed changes, if approved by the Board. Ms. de Mey and Ms. Cece responded that work on amendments to agreements will start immediately and could be expected to be finalized within two weeks. Mr. SigRist added that the required motions regarding plan design will be presented to the full Board of Trustees during its June Board meeting. Ms. Buonfiglio noted that appropriate communication will be sent to participants prior to the transition scheduled for the end of September. The Treasurer stressed his commitment to ensuring that our plans continue to provide high quality investment options and valuable benefits and features, at low costs to our participants. He recognized that we have a history of transparency, education and communication that helps ensure members are aware of the value of the plans, and stressed his desire that this continues to be a priority.

The Chair entertained a motion to approve the recommendations for both funds as presented, and Ms. Cochran so moved. Mr. McKinney seconded and the motion passed unanimously.

Next, the Chair entertained a motion to approve the recommended GoalMaker glidepath changes, and Mr. McKinney so moved. Ms. Cochran seconded and the motion passed unanimously.

### **AGENDA – STABLE VALUE PORTFOLIO REVIEW**

The Chair recognized Mr. Weber. Mr. Weber provided a brief update regarding a lawsuit against Galliard, noting that a filing on May 5 affirmed two previous rulings and that Galliard is optimistic this matter will be finalized soon.

Mr. Weber stated that there were no notable changes in Galliard's staff, its growth was observed in assets under management and in the number of clients, and the Fund's performance remains competitive and stable. He added that cash flows were flat for the quarter and there were no changes in portfolio allocation strategies, with managers remaining relatively neutral with respect to the benchmark. He shared that Galliard has also softened their stance on asset-backed securities and is cautiously adding short-term, high-quality corporate securities.

A break took place from 10:06 a.m. until 10:15 a.m.

**AGENDA ITEM – ECONOMIC OVERVIEW AND 1<sup>st</sup> QUARTER INVESTMENT PERFORMANCE REPORT**

The Chair recognized Mr. Dillard and Ms. Magner who presented the highlights of the capital markets commentary and performance summary. Mr. Dillard noted the favorable environment for active managers and very strong performance of international equities and emerging markets. He also noted a change in the Plans’ investment structure: TCW took over J.P. Morgan’s portfolio in the NC Fixed Income Fund. Lastly, Mr. Dillard provided manager updates and discussed the performance scorecard and managers on Watch List. Ms. Magner noted two manager name changes: “Robeco” is now “Boston Partners,” and “Delaware Investments” became “Macquarie Investment Management.”

**AGENDA ITEM – INVESTMENT UPDATE**

Ms. de Mey referenced the memorandum included in the meeting materials and provided a summary of investment compliance monitoring for the quarter. She noted that all managers are compliant with their respective guidelines.

**AGENDA ITEM – NC 403(b) PROGRAM INVESTMENT POLICY STATEMENT AMENDMENT**

Ms. de Mey highlighted the proposed revisions to the policy, including: clarification of the roles and responsibilities of the Board, Investment Subcommittee, staff, and the Plans’ recordkeeper and custodian; inclusion of an updated, current investment lineup; enhancements to the Watch List and manager termination process; and the addition of the GoalMaker product.

The Chair entertained a motion to approve the Investment Policy Statement as amended and Ms. Cochran so moved. Mr. McKinney seconded and the motion passed unanimously.

**AGENDA ITEM – NC 403(b) PROGRAM 1<sup>st</sup> QUARTER INVESTMENT PERFORMANCE REVIEW**

Ms. de Mey shared the summary of the Program performance. She noted funds added during the Program transition in February and reviewed the passive options, as well as active managers’ performance. She noted a favorable quarter for the latter, with the exception of DFA U.S. Small Cap.

The Chair inquired about the Program enrollments and Ms. Buonfiglio noted a small increase and said that detailed data will be shared during the June Board meeting. Mr. McCann added that post-transition, both the NC 401(k) and NC 457 Plans and the NC 403(b) Program share one, consistent communication and education strategy.

**AGENDA ITEM - SUBCOMMITTEE MEMBERS QUESTIONS/COMMENTS**

There were no additional comments.

**AGENDA ITEM – PUBLIC COMMENT**

No public comments were offered.

Ms. Cochran moved to adjourn the meeting and Mr. McKinney seconded. The meeting adjourned at 10:42 a.m.

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Secretary