

# MINUTES

## SOUTH DAKOTA INVESTMENT COUNCIL

Pierre, South Dakota

February 5, 2015

### 1) Roll Call

The Investment Council meeting was called to order at 10:30 a.m. on February 5, 2015 by Chair Jon Hunter. Council members in attendance were Lorin Brass, Ryan Brunner, David Hillard, Jon Hunter, Steve Kirby, Jim Means, Rich Sattgast and Rob Wylie.

Others attending all or part of the meeting included Matt Clark, Brett Fligge, Chris Nelson, Tammy Otten, and Laurie Riss from the Investment Office; Jane Roberts, Michelle Mikkelsen, Susan Jahraus, Jacque Storm, Doug Fiddler and Travis Almond from the South Dakota Retirement System; and Ashlee Keyes and Cindy Wellard from Legislative Audit.

(Note: For sake of continuity, the following minutes are not necessarily in chronological order. Documents referenced are on file in the Investment Office, and public access is subject to the provisions of SDCL 1-27.)

#### AGENDA ITEMS:

- 1) Roll Call
- 2) Minutes
- 3) Appropriations Hearing Review
- 4) Investment and Asset Allocation Update
- 5) Blackstone Real Estate Partners Fund VIII Investment
- 6) Trust Fund High Yield-Ext Management
- 7) Iran Divestiture & Shareholder Activism Reports
- 8) Legislation Update
- 9) Higher Education Savings Program
- 10) Audit Committee Update
- 11) Compensation Committee Update
- 12) New/Old Business
- 13) Future Meeting Dates
- 14) Adjournment

### 2) Minutes

JIM MEANS MOVED, SECONDED BY STEVE KIRBY, TO APPROVE THE MINUTES OF THE NOVEMBER 25, 2014 AND DECEMBER 9, 2014 INVESTMENT COUNCIL MEETINGS. MOTION PASSED UNANIMOUSLY.

### 3) Appropriations Hearing Review

The Council discussed the FY 2016 budget hearing that took place with the Appropriations Committee immediately preceding this meeting. The Council felt the presentation went well and that there was an appropriate amount of focus on future return expectations and the importance of their continued support. There were no follow-up issues with the budget expected at this time.

### 4) Investment and Asset Allocation Update

Tammy Otten reviewed the Motions and Actions Notes which included the staff actions taken on the Council motions made on the November 25, 2014 conference call and at the December 9, 2014 meeting.

Otten reviewed the estimated fiscal year to date total return for the various funds as of December 31, 2014 and January 31, 2015. Highlights of the attribution analysis for the first six months of the fiscal year were provided.

Brett Fligge discussed the current internal weighting of energy stocks compared to benchmark and described the scenarios that would affect valuations and future exposure to the energy sector. He summarized the views of the internal portfolio managers as well as our external managers in the energy area, including Bridgewater and Blackstone.

5) Blackstone Real Estate Partners Fund VIII Investment

Chris Nelson discussed the Blackstone Real Estate Partners presentation which was given by Jon Gray at the last Council meeting. He noted that BREP VIII was closing soon and Council action is being requested. He reviewed the staff's recommendation of \$300 million in BREP VIII for SDRS plus additional amounts for the trust funds.

Clark discussed the exposure to real estate compared to both the base case and worst case scenarios. He also discussed the maximum exposure to Blackstone. It was confirmed that including the recommended investment to BREP VIII, the Council's exposure falls within the limits for both real estate and Blackstone overall. The realized and expected return of capital from Blackstone was also discussed.

JIM MEANS MOVED, SECONDED BY ROB WYLIE, TO AUTHORIZE THE STATE INVESTMENT OFFICER TO INVEST UP TO \$300 MILLION FOR THE SOUTH DAKOTA RETIREMENT SYSTEM AND UP TO AN ADJUSTED PROPORTIONATE AMOUNT FOR THE SCHOOL AND PUBLIC LANDS FUND, THE DAKOTA CEMENT TRUST, THE EDUCATION ENHANCEMENT TRUST, AND THE HEALTH CARE TRUST IN BLACKSTONE REAL ESTATE PARTNERS FUND VIII. MOTION PASSED UNANIMOUSLY.

6) Trust Fund High Yield – External Management

Otten stated that the high yield investments for the four trust funds are currently managed by the internal high yield portfolio managers. Many high yield securities are issued in 144A form that can only be purchased by a Qualified Institutional Buyer (QIB). Due to information regarding the definition of a QIB, it has been determined that the State may not meet the QIB definition for purposes of the trust funds. This issue does not impact SDRS assets as state retirement systems are specified to meet the definition. Due to inefficiencies in managing the funds without using 144A securities, staff recommended that trust fund high yield assets be managed by an external firm. The Council had previously utilized Vanguard to manage trust fund high yield portfolios, and staff recommended Vanguard be used again.

STEVE KIRBY MOVED, SECONDED BY DAVID HILLARD, TO AUTHORIZE THE STATE INVESTMENT OFFICER TO UTILIZE THE VANGUARD HIGH-YIELD CORPORATE FUND ADMIRAL SHARES FOR THE MANAGEMENT OF HIGH YIELD INVESTMENTS FOR THE SCHOOL AND PUBLIC LANDS FUND, THE DAKOTA CEMENT TRUST, THE EDUCATION ENHANCEMENT TRUST, AND THE HEALTHCARE TRUST. MOTION PASSED UNANIMOUSLY.

7) Iran Divestiture & Shareholder Activism Reports

Otten stated that the Iran divestiture annual report was provided to the Executive Board of the Legislature on January 13, 2015 as required by law. Requirements of the state and federal law had been completed to date. The Council was provided the January 26, 2015 memo that included the recent scrutinized lists from Colorado and Florida compared to the South Dakota list. Staff recommended no changes to the South Dakota list.

Otten also reviewed the required reporting on the SDIC Shareholder Activism Policy related to Federal Divestiture Enactments (Sudan) that was provided to the Executive Board of the Legislature on January 13, 2015. Staff recommended the continued use of the Colorado scrutinized company list and that no changes were needed at this time.

8) Legislative Update

Otten updated the Council on various legislative bills that were of interest to the Council. The three Council sponsored bills (SB 8, 9, & 10) have cleared the Senate and await committee hearing in the House. SB 52 on the general fund proration process will be heard in Senate Appropriations Committee on Friday, February 6. HB 1092 would establish another scholarship in the Education Enhancement Trust Fund for rural school teacher recruitment assistance. HB 1208 is the general appropriations bill for fiscal year 2016. Rob Wylie provided an update on the retirement bills.

Otten stated that a weekly update on the status of bills of interest to the Council will continue to be provided by email throughout the legislative session.

9) Higher Education Savings Program - Update

Otten reviewed the Higher Education Savings Plan summary of accounts/assets and the quarterly compliance schedule. All changes approved by the Council at the December 9, 2014 meeting had been communicated to Allianz.

10) Audit Committee Update

David Hillard, Chair of the Audit Committee, stated that there was no official report at this time. He stated that he will be meeting with Legislative Audit in the Investment Office on February 25, 2015 and is also planning to review accounting procedures with the investment accountants at that time.

Rob Wylie stated that Buck Consultants is beginning work on the quadrennial investment performance review for the four years ended June 30, 2014. He stated the report should be completed in late spring and will be reported to the Council at the April or June Council meeting. He discussed the additional issues that will be included in this quadrennial report.

11) Compensation Committee Update

Jim Means, Chair of the Compensation Committee, stated there was no official report at this time.

12) New/Old Business

No new or old business was brought before the Council.

13) Future Meeting Dates

The next Investment Council meeting will be held in Madison on April 8, 2015.

14) Adjournment

Chair Hunter declared the meeting adjourned at 12:15 p.m.